

IN THE HIGH COURT OF THE COOK ISLANDS  
HELD AT RAROTONGA  
(LAND DIVISION)

Application No. 62/99

IN THE MATTER of Section 409B of the  
Cook Islands Act 1915  
(as inserted by Section  
2 of the Cook Islands  
Amendment Act 1978-  
79).

AND

IN THE MATTER of PUATIKI SECTION  
84B ARORANGI

AND

IN THE MATTER of a Deed of Lease dated  
01 May 1974 to ISLAND  
HOTELS LIMITED

Parties: Island Hotels Ltd, Applicant

Mrs T Browne

Owners, Respondent

Mrs J Poa

Court: This matter first came before the Court for hearing on 20<sup>th</sup> October 1999 when Mrs J Poa on behalf of the landowners produced Mr J McElhinney a registered valuer to give evidence as to the capital value of the land.

The hearing was adjourned to enable Mrs Browne to bring rebuttal evidence because she had not been advised of the nature of the evidence brought.

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The application was further adjourned on 14<sup>th</sup> March 2000 and 24<sup>th</sup> August 2000 to enable the parties to discuss the possibility of a new lease.

On the 12<sup>th</sup> March 2001 the application was called again. Although Mrs J Poa through her counsel sought a further adjournment for negotiations concerning the lease, Mrs Browne as counsel for the lessees stated that the lessees wished the matter concluded so that the owners could receive their land money. She quite rightly pointed out that the determination of the market rental would not preclude the parties continuing negotiations concerning the lease, but the lessees prime concern was payment of rent for the owners.

Since Mrs Poa had presented evidence for the owners and sought an adjournment only to progress negotiations the application for adjournment was dismissed and the Court reserved its decision.

### **DECISION**

Section 409B of the Cook Islands Act 1915 grants the Court jurisdiction to determine the market rental payable under a lease irrespective of any conditions contained in the lease for such determination.

The lessee is an interested party for the purposes of Section 409B of the Act and at the request of the lessee the Court proposes to determine the market rental payable as from the 1<sup>st</sup> March 1999.

The land concerned is part of Puatiki Section 84B Tapere of Tokerau, Arorangi District comprising 16,187 square metres together with a right of access over a further portion of the land running from the main road to the mean high water mark and contiguous to the northern boundary of the leased land.

The land has been developed with extensive buildings by the lessee Island Hotels Limited and the lessee carries on the business of Hotel, Restaurant and accommodation under the name of Edgewater Resort.

The buildings have a value in excess of \$8m.

The lease is for a term of 60 years from the 1<sup>st</sup> March 1974 at a rental of 5% of the capital value of the land "after deducting therefrom the value of all improvements effected by the lessee following valuations to be made as at the 1<sup>st</sup> March in the year immediately following the expiration of each period of 5 years hereby granted."

There is no compensation payable to the lessee for improvements effected and existing at the termination of the lease.

As at the 28<sup>th</sup> February 1999 the rental payable was \$5624 pa. By letter dated 19<sup>th</sup> March 1999 counsel for the lessee offered an increase of \$1875.00 to a total of \$7500 pa.. This represents an increase in excess of 30%.

That offer was rejected by the owners and the matter came before the Court for determination.

In the absence of registered valuers on the islands it has become the custom for the Court to determine the value of leased land through comparison of values attributed to and rental payable in respect of comparable sections in the island. This was the way in which counsel for the lessees approached the matter, but the landowners managed to acquire the service of the only registered valuer resident in the Cook Islands to carry out a valuation on their behalf. His written valuation is attached to the file.

In the course of his evidence, the valuer referred to the following:

- (i) The rental payable upon review would affect the amount paid by a prudent purchaser of the un-expired term of the lease at that time, 35 years, since there is no right of renewal nor any provision for payment of compensation for the lessee's improvements.

- (ii) A prudent purchaser would need to consider the possible commercial gain he can expect from the business if he is required to pay 5% of the value of the land as a rental.
- (iii) There is no clause in the lease "as is found in some more recent leases involving commercial use whereby the lessee pays 1½% of gross turnover in addition to ground rent ..."

It is pertinent to note at this stage that the "prudent purchaser" referred to in (ii) above would also be concerned in determining the purchase price as to the fact that he would receive no return on the purchase price paid in respect to the improvements on the expiry of the lease.

The comment made in (iii) above may also be misleading but was no doubt included in the report by way of reference to the Property Law Amendment Act 1995-96 which by section 2 inserted the following section in the Property Law Act 1952.

"106A. Further covenants included or implied in leases – (1) In every lease of Native freehold land for the permitted use of a commercial or industrial business or enterprise there shall be included, and if not included, implied, the following covenants by the lessee, for himself, his executors, administrators and assigns –

- (a) that where commercially appropriate the lessee will pay to the lessor a goodwill payment at the commencement of the term of the lease;
- (b) that the lessee will pay to the lessor the greater of:
  - (i) a fair and reasonable ground rent; and
  - (ii) a percentage of the annual gross turnover of all or part of the activities of the business or enterprise for which the land is being utilised, such percentage to be negotiated between the parties;
- (c) that the ground rent payable by the lessee pursuant to the lease shall be reviewed at intervals of not more than five years, with

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the ground rent following review to be as agreed between the parties or failing agreement as determined by an independent arbitrator or by the High Court.

- (d) that the lessee will give to the lessor reasonable opportunity to participate as shareholder on usual commercial terms in the business or enterprise for which the land is being utilised;
  - (e) that in the event of the sale or proposed sale of the business or enterprise for which the land is being utilised (including any sale or disposition of any business or enterprise which would alter the effective control of that company) –
    - (i) the lessee will give to the lessor the right of first refusal to take the assignment of the lessee's interest pursuant to the lease, or the transfer of the shares, on the terms of the proposed sale, and any such sale shall be deemed to be conditional on the non-exercise of the right of first refusal;
    - (ii) following settlement of the sale the lessee will pay to the lessor a percentage of the net sale proceeds of that enterprise or business and the lessor's entitlement pursuant to this subclause shall rank subsequent to any secured creditors and in priority to any unsecured creditors of the lessee.
- (2) This section applies:
- (a) to leases for a term commencing on or after the 1<sup>st</sup> day of January 1997; and
  - (b) to leases renewed or extended, pursuant to subsections 469(3) and 469(4) of the Cook Islands Act 1915 and its amendments, for a term commencing on or after the 1<sup>st</sup> day of January 1997; and
  - (c) with effect from 1 January 2007, to leases for a term commencing prior to 1 January 1997, which leases shall

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be varied to incorporate the covenants listed in subsection (1) of this section.”

It will be seen that since this present lease was entered into on the 1<sup>st</sup> May 1974 the above provisions have no application although in terms of the above section 106A (2)(c) the current lease will be caught by these provisions after 1<sup>st</sup> January 2007.

Therefore, in determining the rental review, this Court is bound by the terms and conditions of the lease varied only by the provisions of Sec 409B of the Cook Islands Act 1915.

Counsel for Island Hotels Limited in her submissions states that the valuer who concluded his valuation with a rental of \$40,600 pa which he said “could be compared to a 1% of turnover on total \$4.0m gross turnover which is only \$100/room/night turnover at 61% occupancy in 180 rooms (\$4.0077m)” has made calculations in reverse from a premise of 1% of the room revenue from the Hotel. Similar to the rental provisions in the lease of the Rarotongan Hotel. But that this ignores a comparison between the respective leases of the Hotels.” Although not stated by counsel it is understood that the lease of the Rarotongan Hotel contains a provisions for compensation for the lessees improvements on the expiry of the lease.

This Court notes also, that the valuer in his comparison of sales of the properties listed, notably the Crown Beach Resort has settled upon a per square metre value based upon the full purchase price which would include improvement, plant, and goodwill. Hardly a sensible basis upon which to assess the value of unimproved land.

The formula contained in this subject lease for the determination of the rental is 5% of the value of the unimproved land and as stated by counsel for the lessee this is best determined by an evaluation of rentals paid for comparable land capitalised at 5% to give the value of the land. This is the manner in which the Courts in Rarotonga have customarily determined rentals on review and this Court sees no reason to depart from that system. Any departure in the manner put forward by the registered valuer could

jeopardise future development of land in the Cook Islands to the detriment of the overall fragile economy.

Counsel for the lessee has submitted some helpful illustrations in properties which this Court accepts as comparable to the land in the present lease namely:

(a) Ngakuriao Section 88A, Arorangi.

Term: 60 years from 01 September 1987 (5 yearly reviews)

Area: Four acres two roods and twelve perches (4a:2r:12p) (1.85141ha)

Rental: \$7,750.00 as at 01 September 1997

(b) Ngakuriao Section 88B, Arorangi

Term: 60 years from 02 April 1989 (5 yearly reviews)

Area: One decimal zero one six nine hectares (1.0169ha)

Rental: \$4,500.00 as at 1 April 1999

(c) Vaitu & Puatiki Section 84A1, Arorangi

Term: 60 years from 1 November 1966 (15 yearly reviews)

Area: Three roods thirty seven perches (0a:3r:37p) (3,971m<sup>2</sup>)

Rental: \$1,521.00 as at 1 November 1996

(d) Vaitu & Puatiki Section 84A2, Arorangi

Term: 60 years from 1 September 1968 (15 yearly reviews)

Area: One acre twenty one perches (1a:04:21p) (45798m<sup>2</sup>)

Rental: \$2,100.00 as at 1 September 1999

(e) Manuia Beach Resort

Term: 60 years from 1 December 1987 (5 yearly reviews)

Area: Seven thousand three hundred and thirty one square metres (7,331m<sup>2</sup>)

Rental: \$2,750.00 as at 1 December 1992.

If these examples are reduced to cost per square metre then they would equate as follows:

- (a) 41c per square metre
- (b) 44c per square metre
- (c) 38c per square metre
- (d) 45c per square metre
- (e) 37c per square metre

The rental offered by Island Hotels Limited \$7,500 pa would amount to 46c per square metre which equates favourably with those listed above

The next review of rental will be as at 1<sup>st</sup> March 2004, but reviews thereafter will be caught by the provisions of Sec 106A (2)(c) of the Property law Act 1952 at which time, this system of comparative values will be of use only for the purposes of determining ground rental and the percentage of gross profits will need to be factored in. Until then this Court believes that the manner in which the registered valuer has approached the matter is quite inappropriate at this time and the customary method of review should be complied with.

During the course of conducting a review of the rental for properties leased by CITC the Court was advised that there has been a 2% increase in productivity in the Cook Islands for the 1999 year. There is no doubt that there has been an increase in the tourism industry which can only auger well for the economy of the country. But is there any certainty that such degree of support will continue? Already the economies of Japan, USA and Europe are showing signs of a depression which if it materialises must have an adverse effect on tourism and the general economy of this country.



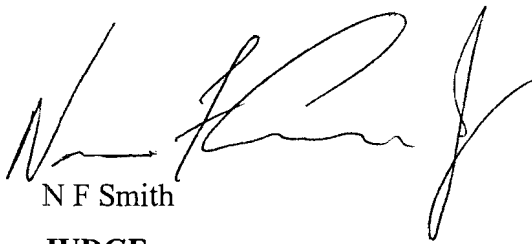
The offer of \$7500 pa an increase of some 30% in the existing rental does not appear unreasonable, as a fair rental for the land comprised in the lease. Because of the provision that the rental on review should not be less than that payable for the preceding 5 years, any substantial increase in the ground rental would have a detrimental effect when the provisions of Section 106A (2)(c) of the Property Law Act take effect in 2007 when the rental shall include a ground rental plus a proportion of profits.

The Court is satisfied that the figures as provided by the registered valuer are anomalous resulting in a rental of \$50 per square metre, because of the inclusion of improvements goodwill etc in the sale prices quoted by him.

The Court is equally of the opinion that the examples as given by counsel for the lessee produce a more equitable basis for review.

The rental for the lease as from the 1<sup>st</sup> March 1999 is set at \$8000 pa.

Dated at Rarotonga this 14<sup>th</sup> day of March 2001.



N F Smith  
**JUDGE**