

## THE ESSENTIALS OF A JUST LEASE

Ladies and Gentlemen:

I want to say something to you today about leases because this is a generic term and the species are numerous. Some are genuine leases, based on the realities of life, property rights, and market values. Some are mock-leases with only the shadowy outline of the form of a lease but containing the substance and nature of freehold tenure.

If we are ever to enjoy the advantages of a Crown leasehold system of land tenure, leases must be based on sound principles of administration and above all they must pursue justice between the lessee and the leasing authority acting in the name of the people.

Leasehold land tenure can be very fragile and easily destroyed by legal cunning and human greed. In this lecture I will relate to you three instances where this has occurred and the system of leasehold tenure has consequently been reduced to a mere shadow of what such a system should be.

There are many different uses for land and the terms of a lease must necessarily vary in details but there are some leasing provisions which are determined by principles which are absolutely essential in all leases if they are to merit the accolade of justice.

I propose to tell you something about three leasehold experiences to illustrate just how leasehold land tenure can be corrupted and to emphasise what are the essentials of a just lease. Only one is from New Zealand. The other two are from Hong Kong and Australia.

### 1. Maori Reserved Land

There are many other New Zealand examples I could have chosen to illustrate the serious inadequacies of the kind of lease I am about to describe. Such are the reclamation leases in Wellington City or the endowment land of Te Aute College, but I have chosen the leases prescribed by the Maori Reserved Land Act 1953 because it is part of the Maori land question which at present is hotly debated and little understood. I must say that Maori Reserved Land is only a part — and not a major part — of the larger issue.

All Maori reserved lands have a special history and all have

from their beginning been administered on behalf of their Maori owners by trustees. Since 1921 this has been the Maori Trustee who took over from the Public Trustee in that year. More recently some have come under the co-operative control of the owners. I propose to tell you something about three of these reserves and how they are occupied and used today.

### **New Zealand Company reserves**

From the very beginning the New Zealand Company, which founded all our Wakefield settlements, had a native policy. Maoris and European settlers were not to live in segregated areas but were to be intermingled in one settlement in order that the native peoples should learn civilised ways and civilised skills. This was to be achieved by a plan for providing estates or endowments for native chiefs and their followers and so prevent the natives becoming landless and being destroyed by the fatal impact of European culture.

When Colonel Wm Wakefield and the local chiefs stood on the deck of the "Tory" in Wellington harbour and negotiated the purchase of the lands from the Tararuas to the sea and between the hill tops east and west, a payment was made in trade goods. The Company was well aware of the inadequacy of such payment. The real payment was to be made in land set aside for the Maoris which would increase in value as the colony grew and prospered. The Maori was to be given an interest in this prosperity and so he would be encouraged to advance it in every way.

In England the Company sold land orders and received in payment over £100,000 to be used for expenses of emigration. These orders were to be honoured after the land had been purchased and surveyed. Every tenth land order was set aside for the Maori people. There were 110 of these in all in the town of Wellington, which at this time existed only on paper. These company tenths were what are called the 'New Zealand Company reserves'. They make up a considerable part of the borough of Motueka. There are a few in Nelson and Palmerston North (by an exchange of land) as well as those in Wellington. The site of Calvary Hospital, the Wellington South School and Athletic Park are the principal ones in Wellington.

### **Greymouth**

In 1860 James Mackay purchased the land on the West Coast

of the South Island from Karamea to Milford Sound and from the sea in the west to the eastern mountain tops for 3000 gold sovereigns. There were some pieces of land the Maoris would not sell and which were accordingly excluded from the sale. The principal area excluded was that of Mawhera pa and this is today the site of the borough of Greymouth. Recently the Maori Trustee handed over the administration of this reserve to the Mawhera Incorporation of beneficial Maori owners.

#### West Coast Settlement reserves

This reserve is an area of rural land of about 70,000 acres lying between Wanganui and Hawera. It was confiscated from the Maoris after the land wars and after much delay was subsequently returned to the eight tribes involved. It is almost all farm land and is leased to European farmers.

All these Maori Reserved lands have one thing in common and that is the lease under which they are held. The leases prescribed for both urban and rural land are in the schedule of the Maori Reserved Land Act 1953.

The prescribed leases provide as follows:

1. The term of the lease is twenty-one years.
2. At the end of each term lessees have the right to renew the leases again.
3. The rents are reviewed at the end of each twenty-one year term.
4. Rents are fixed as follows:

The Valuer General makes a special valuation of the Unimproved value of each parcel of land.

The annual rent is fixed in the case of rural land at five per cent of this value and of urban land at four per cent of same.

The consequence of this method of rent fixation is that the rents are miniscule because (a) Government valuations are always conservative; (b) over a twenty-one year period land values always rise due to economic causes; (c) inflation erodes the value of the rent; (d) the percentage is absurdly low.

Because the lessor's interest is so small and the lessee's interest is great the leases are bought and sold at near freehold prices.

These points, however, are concerned merely with money. The worst feature of the lease is the right of renewal the lessee has in perpetuity. This guarantees that the Maori owners can never use or occupy any of the lands unless they purchase the

lessee's interest. A just lease would guarantee the lessee only the value of his improvements and when the term expired the lessor could purchase them at market price and enter upon his property. The Maori can never do that. Indeed if he walked uninvited on these lands he "owns" he would be a trespasser and so it will be forever. The tenant can sell his interest to anyone for cash any time and reap any capital gain available. The owners can sell their interest only to the tenants.

Such a lease contains multiple injustices. It is for the tenant merely a disguised freehold. These leases have been prescribed by Parliament. They could be fairly described as a device for depriving the Maori of almost all the advantages of land ownership or in blunter terms for robbing the Maori of his land.

That such a situation should be allowed to continue from year to year is a sad commentary on New Zealand law, its practitioners, its guardians and its makers. It is an abuse and perversion of law into an instrument of injustice.

A lease of this kind — and there are many such in New Zealand apart from Maori Reserved land leases — are to anyone designing a just leasehold land system a warning and a guide.

In parentheses I will add that if we in New Zealand were ever to adopt a system of Crown leasehold tenure in the place of freehold tenure special provisions would have to be made in regard to Maori land.

But to return to the main point — these leases point to several dangers which must be avoided in designing a just lease. These are:

- (a) The term of a lease must never be inordinately long and never, never, never perpetual.
- (b) The rent must be a market rent.
- (c) The intervals between rent reviews must be short to keep them near market realities.
- (d) The term of the lease must be the time interval between the commencement and termination of the contract and not merely the period of time between rent reviews.

I am aware this last note merely says again that it must never be a perpetually renewable lease. This is deliberate. It cannot be said too often.

## 2. Hong Kong

Hong Kong became a colony of Great Britain in 1841 and from the beginning the land tenure of the colony has been a Crown

leasehold system. It is probable that this fact reflects the influence of Adam Smith, David Ricardo, John Stuart Mill and Alfred Russell Wallace — the pioneers of economic science — on British thought at that time.

Despatch No. 31/1844 required that:

"All lands are to be disposed of in the first instance by auction, not in perpetuity, nor for a sum paid down, but for an amount of annual rent, on leases for such terms as may be fixed by the Governor not exceeding seventy-five years in the case of lands sold for building purposes."

However, a leasehold system of land tenure cannot be administered by freehold minds and private greed will implacably pursue concessionary modification of leasehold conditions. So it was in Hong Kong.

From 1848 to 1898 nearly all leases became leases for nine hundred and ninety nine years. After that year the standard lease became again a "seventy-five year lease renewable for a further period of seventy-five years at a reassessed Crown rent." They are, however, renewable on "similar" terms which implies that they carry the right for a renewal for a further seventy-five years and so on ad infinitum. This makes them perpetually renewable like the Maori Reserved land leases. I am not aware of the provisions for rent reviews in the thousand year leases but I have said enough to show up the glaring deficiencies of the system.

In 1962 a great number of leases fell due for their seventy-five year rent review. In the interval the population had grown from thousands to millions and from being a minor coastal town Hong Kong had become one of the great ports of the world. The Crown "tenants" fought a splendid fight against any semblance of economic justice. They even threatened the Government of appealing to the Peoples Republic of China to intervene in support of their cause against their colonialist oppressors. The Government struck a bold posture but finally crumpled and rents were renewed for seventy-five years at a fraction of their true value.

In spite of the tremendous inadequacies of the land tenure system Crown leaseholds have made the phenomenon of Hong Kong possible. Rents and rates together provided about a third of public revenues in 1972. There are as a consequence minimal taxes on trade. The leases have been the principal instrument in town planning. They have in part removed the

land cost from public works. They have provided land for schools, hospitals and a great number of other community needs. They made all reclaimed land Crown land subject to lease.

In short they have made the human marvel which is Hong Kong possible.

Nevertheless the Crown leasehold system by its grossly inadequate rents has put many leaseholders of Hong Kong into the same economic class as the oil sheiks of the Persian Gulf.

For our immediate purpose Hong Kong leases have three lessons: (1) to preserve the rights of society land rents must be full market rents; (2) there must be no rights of renewal in perpetuity; (3) the intervals between rent review must be short not only to ensure that market rents are paid but to prevent massive and powerful popular resistance of a strength sufficient to destroy the whole leasehold system.

### 3. The Canberra Story

The Australian Capital Territory is a small enclave in New South Wales between Melbourne and Sydney. It covers an area of 940 square miles. The Seat of Government (Administration) Act 1910 which established the Federal Capital provided that "No Crown land in the territory shall be sold or disposed of for any estate of freehold". This was to be a completely Crown leasehold territory and theoretically it still is. But in 1970 the Government of John Grey Gorton, the nineteenth Australian Federal Prime Minister, abolished rents entirely within the Territory City Area, i.e. the urban part of the Territory.

Ordinance Number 45 dated 15th December 1970 read as follows: "The rent under a lease shall be five cents per annum to be paid if and when demanded by the Minister."

This one ordinance tore the heart out of the Canberra leasehold system leaving nothing but a few administrative advantages which could have been secured quite well in any freehold area by other means. In the words of Sir Ronald East: "It gave away the equity in \$100,000,000 worth of Crown lands in Canberra to wealthy banks, hotels, insurance companies and other commercial operators, as well as to thousands of public servants and a few pensioners."

What was the motive of this extraordinary move? The leases were all for a term of up to ninety-nine years. The rents were fixed at five per cent of the unimproved value of the land and the reappraisals of rents were to be made every twenty years.

When the reappraisals came for a considerable number of properties in 1965 the unimproved land values had increased by anything from 500 to 800 per cent. There was naturally a great deal of concern among the leaseholders. A by-election was due and the two Canberra seats were of the very greatest importance to the Government.

These facts illustrate the great fragility of a leasehold land system. This was the greatest experiment in land tenure which has ever been carried out in the modern world. It gave concrete expression to a profound social philosophy. It was the same philosophy which had inspired our Liberal Government in 1890. It was the most significant achievement of thoughtful and patriotic men striving for a better society in a better land. Political cowardice, political expediency and administrative incompetence combined to wreck the noble experiment.

Of course it was popular with the Canberra leaseholders. In the words of a distinguished economist, Mr Colin Clark, they "had been made a whole-sale gift of public money at the expense of every taxpayer in Australia".

This tragic event passed almost unnoticed by the majority of Australian citizens and I do not believe that a single newspaper in this country ever thought it was worthy of attention.

From this episode there is much to be learned because it is as near to us, our history and our experience as if it had happened in New Zealand.

First it repeats the lessons of Hong Kong viz. that rents must be market rents and that frequent rent reviews are essential to keep things so. There is, however, another and more important lesson. It is this. Land tenure is too fundamental a thing to be the toy of any Parliament and it is too fragile to withstand the combined assault of private greed, commercial intrigue, political manipulation, popular indifference and administrative incompetence. **When Crown leasehold land tenure is established and accepted it must be protected not by a simple Act of Parliament but by a Bill of Rights declaring the right of every New Zealand citizen to the occupancy of land without a purchase price and/or protection within the framework of a written constitution.**

#### Hallmarks of a just lease

By a just lease I mean a lease whose provisions give to the Crown its due as the landowner and to the tenant his due as the land occupant. If you give the tenant more than his labour

produces you will give him privileges his fellow citizens cannot have and which have a market value.

The heart and essence of any just lease is rent. I must emphasise the word "just" because when rents were abolished in Canberra the Minister of the Interior in defending the abolition of rent in a document issued by his department boldly asserted a rent was "not an essential of leasehold tenure". This is certainly not true of a **just** lease.

After all what is freehold land tenure but a lease degraded by injustice. Legally it is a Crown lease in perpetuity and with no rent. Making any lease perpetual is half way to making it a freehold. Abolishing rent goes the other half of the way.

The rent of land is a fact, not a theory, just as much as wages are a fact and a return on investment is a fact. Only if one could say wages was not an essential fact in a contract to build a house could it be said that rent is not an essential fact in a contract to lease land. One party in the contract must receive the rent. Ethically it belongs totally to the owner-lessor and ethically the tenant-lessee must pay it in full. Rent is then the very essence of any leasehold system of land tenure.

I will try and drive home this vital point by saying a little more about economic rent. It arises primarily because land is fixed in quantity and varies widely in its usefulness. It is a payment made for the use of land and the selling price of land is the rent capitalised.

Economic rent of land depends on its native fertility, its location in regard to facilities and amenities provided by local and central government and by the size and nearness of adjacent communities.

When, because of better transport, greater natural fertility, better climate or better social services one farm will produce a thousand units of wealth with the same effort, time, and capital, that another farmer must use to produce five hundred units of wealth, the first farm will command a higher rent or market price than the other.

It should be noted that the factors making the difference in income are not the farmers' contribution. They are made by nature and the community. In both the two farms mentioned the farmers contribution in labour, time and capital is the same.

Economic rent is by its nature not produced by individual men and individual men have no title to it whereas the community has the best of titles — that of its causation.



The tenant must pay all the rent and the Crown must receive all the rent if justice is to rule the relationship.

The second essential of a just lease is that it must have a finite term and when this is reached the contract ends. It may provide for one or more renewals but all together the original lease and the renewals must have a time limit set on just principles and these are that the term must be related to the span of one human life. In the case of bodies corporate which never die the term should be related to the life expectancy of the improvements on the land. For example a commercial building or a factory will seldom endure as a useful and efficient entity beyond 100 years. Because the tenant makes the improvements they are his and a just lease must say so.

But I am getting off my main track. The details of leases may differ with different classes of property but I am mainly concerned with farm lands at this time and I suggest the maximal term of such a lease should be related to the span of human life.

I have already mentioned the perpetually renewable lease in connection with Maori Reserved land but I will reiterate it. Such a lease has only the form of a lease and nothing more. It is not a lease at all. It is a transference of nearly all of the rights of a property owner to another person for ever.

No doubt it is for this reason that leases in perpetuity were abolished in England by the Law of Property Act 1922 and since that date the only tenures permitted in England are freehold land tenure and leases for a stated term. When that Bill was introduced into the House of Commons Sir Leslie Scott, the Solicitor General, referred to a perpetually renewable lease "as a useless paradox" and this is a fair description. New Zealand should follow the example of England and make such leases illegal.

Now having discussed in a general way the principles which must find expression in any just lease of whatever class of property I propose to give my views on what should be the standard lease of a New Zealand farm, granted by the Crown.

#### **Farm leases**

Under a Crown leasehold system in effect every farm property will have two owners. The bare land will be owned by the Crown and the improvements (which will be carefully defined in the lease document) will be the absolute property of

the tenant. Nor will he have property in anything else and there will be no such thing as goodwill or any other incorporeal thing.

1. **Term:** The term I propose is a maximum of fifty years with no rights of renewal. The present average term of occupancy of a New Zealand farm is ten years and the effect of a fifty year occupancy should introduce a degree of stability and permanence which is so seriously lacking now.

2. **Family preference:** Although there can be no rights of renewal, when the lease is due for renewal, there should be given some preference for a member of the family of the outgoing tenant in order to secure an even greater identification between the farmer's family and the land he tills. This is proposed in pursuit of the national ideal of the family farm.

3. **Transference:** Leases may be transferred only to the Leasing Authority acting for the Crown. There should be no lateral transfer. The purpose of this condition is to provide an additional safeguard against trading in leases. The tenant's property rights are only in the improvements and when the lease ends these must be sold to the Crown at a negotiated price who must sell them to the new tenant at the same price. What are improvements should be defined in the lease itself and there should be every safeguard which can be devised to protect the interest both of the outgoing and ingoing tenant.

4. **Lease rents set by the market:** As frequently as possible leases should be auctioned to set the level of market values. It should not be required in every instance but at least one in five in any one land district should go under the hammer.

5. **Mobile rents:** In my view rents should be formally reviewed at five yearly intervals even though annual adjustments in fact make changes unnecessary. These annually adjustable rents are what I mean by a mobile rent. The annual adjustments are designed to adapt to inflation and changes in export prices. The rents should be indexed against inflation to keep a steady value. Rent must not be eroded by the value of the dollar falling. The rents should also be indexed against the level of export prices. They should fall when prices fall and rise when they rise. I will not discuss the details of how export price index values might be given effect to. I merely state the principle and the purpose of the indexation.

At present any downward slide in overseas prices create grave hardship and a demand for farm subsidies. There should

be a built in buffer operating automatically to enable the farming industry to respond to periods of falling prices which are absolutely certain to occur from time to time. This provision will further increase stability and strength in the economics of farming.

6. **Rates:** The idea that rates should be paid by the Leasing Authority and collected from the lessee with the rent is worth consideration and study.

There is little doubt that such a change would have important long-term consequences. In a rural area in time the Leasing Authority would come to be the sole direct ratepayer. Such a radical change would probably bring changes in the structure of local government. It would probably in time cause the rating base to change from the market value of land to the annual rental value of the land.

I merely mention these possibilities which could evolve in time. The idea of one charge, compounded of rates and rent on one corpus of value is theoretically desirable.

Of course export price indexation would apply only to the rent component of such a single payment.

It may be objected to any system of farm leasehold that the equity of the farmer in his farm would be so much reduced that he could not borrow readily for his seasonal needs or for farm development. This was a problem met by the Liberal Government of last century when they put thousands of leaseholders on to farms. It was met by setting up the "Advances to settlers" fund whose successor today, the Rural Banking and Finance Corporation, is still with us. This is an area where long experience should be our guide.

Finally I can see no reason why the rent a farmer pays should not substitute for his income tax — or rather that part of it which is a tax and not a welfare contribution. This would remove the final factor inhibiting production from the farmlands of the nations.

### **Radical changes**

Such a system of land tenure for farm lands will produce a radical restructuring of New Zealand's greatest industry. I have mentioned the factor of permanence and stability a fifty-year tenure would bring but there will be other changes equally large. When the farmer's equity is in improvement values only he will strive to maximise them so he will have as large a sum as

possible to supplement his life savings and his Universal Superannuation when he retires. Today he retires on a maximal capital gain from the increase in the land values of his farm during his term of occupancy. The more land he farms the greater will be his rent payments. He will therefore have as small a farm as possible consistent with producing his necessary income. He will have no motive for adding field to field or farm to farm to maximise his capital gain. Finally very little capital will be required for a young farmer to get established because he will not have to buy his way in. The lock-out will be broken. The average age of working farmers will be much lower. Energy and enterprise will increase. Health will be restored to a sick industry and the very basis of the national economy enlarged and strengthened.

If these things are accomplished New Zealand alone will in our troubled world have solved the universal problem of the proper relationship of man to the land. I have no doubt that her example would have a permanent and beneficent impact on the whole family of nations for centuries to come. To paraphrase a famous dictum — she will save herself by her own exertions and mankind by her example.