



REVIEW OF FINANCIAL MANAGEMENT OF CUSTOMARY AND OTHER LAND IN THE PACIFIC

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Review of Financial Management of Customary and other Land in the Pacific

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Disclaimer

This is one of ten reports commissioned by the Pacific Islands Forum Secretariat that comprise of a review of national, regional and international literature, and country case studies including the review of national policies and systems on key thematic areas:

- a. Subproject 1: Role of land in conflict escalation in recent conflict situations
- b. Subproject 2: A review of sources and causes of land related conflict
- c. Subproject 3: Current land management and conflict minimisation
- d. Subproject 4: Conflict management process

accessUTS Consultants prepared two components, subproject 2.3 (Review of Customary Property Rights and Formal and Informal Institutions for Economic Development and Conflict Minimisation) and subproject 3.1 (Review of Financial Management of Customary and other Land in the Pacific), which were carried out in conjunction with each other.

This paper is based on a review of the relevant literature and in-country discussions with regional practitioners and experts. The views expressed by the lead consultants and regional contributors are their own, and are not necessarily the views of any particular organisation or the organisations that they represent.

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3.1 REVIEW OF FINANCIAL MANAGEMENT OF CUSTOMARY AND OTHER LAND IN THE PACIFIC

SUMMARY

This document comprises a regional review report providing:

- > An overview of financial management of customary and other land management;
- > Lessons learnt from recent experiences in the region;
- > Guiding principles stakeholder based institutional design to encourage market based rental determination / negotiation, equitable intra and inter-generational distribution of returns that can also assist in conflict prevention and / or conflict minimisation; and
- > Recommended elements on financial management of customary land for inclusion in the proposed overarching Regional Land Management and Conflict Minimisation Framework for Action.

This report builds on recent regional initiatives and plans that engage with the financial management of customary land. These include the USP Solutions (2001) Land Tenure and Land Conflict in the Pacific, the FAO/USP/RICS Foundation South Pacific Land Tenure Conflict Symposium (2002), and the subsequent National Land Workshops / Summits (Fiji 2002, Solomon Islands / Melanesia 2005, PNG 2005 & 2006, Vanuatu 2006), and ADB Swimming Against the Tide (2004), Forum Secretariat Pacific Plan (2005), AusAID Pacific 2020 (2006).

The report provides a detailed review of published and unpublished literature, drawing on experiences from within and beyond the region. There are references to the evolution of landownership structures in Europe and, in particular, leasehold examples from Australia and the UK. This is intentional, as the Pacific can learn from both the strengths and limitations relating to the financial management of land in countries that have seen the full cycle of 99-year leasehold arrangements.

The report contextualises the effectiveness of the different financial management systems / arrangements using four detailed country case studies: Fiji, Samoa, Papua New Guinea, and New Zealand, which are included as appendices.

The recommended elements for inclusion in the overarching framework for action are solutions-based, comprising guiding principles for the Financial Management of Customary and other Land in the Pacific: Transparent Land Information Systems; Trusts and Incorporated Land Groups; Pacific Valuation Methodology and Valuation Application; Land Use Planning; Land Courts or Tribunals; Eliminating Premiums on Lease Transfer; Restitution; Leasehold Solutions; Debt and Equity Funding; Increasing Financial Management Capacity; and the One-Stop-Shop.

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INTRODUCTION

The Pacific provides a distinctive situation for the effective financial management of land. Institutional arrangements have been influenced in various ways by western countries. Generally, Pacific Island Countries (PICs) retain the core traditional belief that the superior interest in land should not be sold. The financial importance of land is its use for most economically productive activities. As more productive land uses become available, they have prompted changes to the traditional ways of dealing with land. These changes have also encouraged reconsideration of the economic balance within customary communities.

The income disparity that is available from new commercial land uses compared to traditional uses has distorted some aspects of customary life. Customary landowners have had the tendency to under optimise the financial return on their land when leased. In circumstances where they have subsequently become aware of the true value of their land, conflicts have arisen.

This has challenged their willingness to uphold contracts regarding their land. Western people place contractual obligation paramount, regardless of the equity in the arrangement. The principle of *caveat emptor* (let the buyer beware) is an accepted foundation of western commerce. By contrast, customary peoples place more importance on equity and respect for cultural traditions. This makes contractual obligations of only secondary importance.

Key to integrating the interests of customary owners into the recognised need to make customary owned land economically efficient is the actual financial management of customary owned land. Contrary to view of some popularised authors (e.g., Gosarevski *et al.*, 2004b; Gosarevski *et al.*, 2004a; de Soto, 2000), it is recognised that effective economic outcomes can be achieved within a leasehold property environment. This study will draw from the experience of the Pacific, as well as western examples of financially efficient land use. It will identify several major impediments to this objective that currently exist in the Pacific, and it will recommend strategies to overcome them.

FINANCIAL MANAGEMENT OBJECTIVES FOR LAND IN THE PACIFIC

FINANCIAL MANAGEMENT CRITERIA FOR CUSTOMARY AND OTHER LAND

The scope of what constitutes financial management of customary and other land in the Pacific focuses on practical issues in the utilisation of land that sit between the economic level of industry and national utilisation objectives, and the legal / cultural / institutional level of land or property rights. It forms a bridge between these two areas of interest that is important, spoken about, but appears largely neglected.

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The economic objectives for the Pacific include consideration of which industries should be encouraged, and how they should be fostered. Some economists have argued that customary ownership is linked to poor economic performance with claims such as, “communal ownership has not permitted any country to develop” (Gosarevski *et al.*, 2004b, p.134). This claim deserves some attention because it implicitly leads to the elimination of customary ownership as was made more explicit by the same authors when they identified private title with freehold (Gosarevski *et al.*, 2004a). In doing so, they aligned themselves with mainstream neoclassical economics in general, and the current missionary of that position into the developing world, Hernando de Soto (2000). Fingleton *et al.* (2005) have represented the alternative position, agreeing that “the absence of secure, individual and transferable property rights limits the type of development that can be undertaken, which in turn limits the level of development of an economy” (Lightfoot, 2005, p.23), but denying that this means freehold.

Leasehold is a system of property title that can provide secure, individual, and transferable property rights. It is the purpose of this study to examine practical aspects of realising leasehold solutions to create dynamic and workable systems for the effective financial utilisation of customary and other land in the Pacific. However, before this is attempted it is necessary to clarify why this modest aim of Pacific people has aroused such scholarly objection from professed modern western economists. It is also necessary to set out the parameters for evaluating financial success within the Pacific cultural context.

The objections raised by authors such as Hughes and de Soto use as premises several valid observations of the economic under-performance of customary owned land and move to the strong conclusion that customary owned land cannot deliver effective economic outcomes. Fingleton and others do not reject the premises, but merely recognise that there are more possibilities available than the insistence on land reform leading to freehold title. Western property markets over the last half century, especially commercial (office) markets, provide ample evidence of this. For example in 1960 owner-occupiers, at least in terms of the larger space users, occupied the majority of the Sydney CBD. This included the offices of most major companies and the major retailers.

Today, very few space users in the Sydney CBD own a freehold interest in the space they occupy; in many cases, they have strategically divested themselves of their real estate holdings (i.e., their operational property asset) in order to improve their financial performance. Instead, they lease their office and retailing space. Other major cities in the developed world have followed a similar trend. Likewise, in Australia, about a third of residential dwellings are leased, and the proportion is greater in many other countries. The World Bank acknowledges, for example, that land renting is fully consistent with modern agricultural practices and is widespread in developed market economies (such as the OECD countries of Western Europe) but varies strongly among countries (Swinnen *et al.*, 2006). In some countries of the

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OECD around 70% of farmland is rented (e.g., Germany 68% and Belgium 75%), whilst the figure is less than 25% in others (e.g., Denmark 24% and Ireland 17%)¹. The aspirations of Pacific peoples appear to follow these trends, which makes the ferocity of the objections from some quarters peculiar. If the objections were valid, exploring possible methods for effective financial use of customary land would be futile, so understanding the mechanics of this school of thought is extremely important at the outset.

Francis Fukuyama (1992) revived the generally discredited sociological notion of *progress* when he argued that democratic capitalism, of the sort found in the USA, represented the cultural/economic system at the end of history. In terms of property, this translates into the popular claim that no system of property can deliver the same benefits as freehold title in land property. He built on a succession of thought that was earlier expressed by Richard Weaver (1948), who claimed that private property of the US freehold type represented the “last metaphysical right” of humanity, and was an absolute necessity for a free and prosperous society. This claim is implicitly embedded within neo-classical market economics and can be found within any defence of that system. It means three things. Firstly, that development necessarily requires land reform leading to freehold title. Secondly, it means that general economic thought is written in a way that makes freehold private property the only effective system of land title. Thirdly, and most uncomfortably, it means that if another system of land property were to succeed economically and socially, then fundamental economic foundations of the west would be challenged.

In the past, socialism arose as a challenge to freehold market capitalism, and history has proven its inadequacies. Currently there is a similar religious-economic challenge coming from Islam with Islamic economic thought taking hold in practice in some Islamic countries (Cooper, 1981; Behdad, 1989). Islamic economic thought shares similarities with the principles of customary ownership of land though most contemporary attention is focused primarily on banking and finance. Without intending it, customary people are advocating another alternative, one that is definitely not socialist, but revolves about a system of landownership and community relationships that is alien to modern western thinking. The possibility of its success is beyond the scope of modern economics and the realisation of that success would force a major rethink of some of the cultural fundamental of that system, even though customary peoples contemplated nothing of that sort. It is therefore important that criticisms of customary land based economic systems are understood in terms of this wider understanding of the modern western theory and culture from which they originate.

This undercurrent within western thought deserves attention for another more positive reason as well. Its history contains a number of valuable insights for contemporary customary landowners and the countries to which they belong.

¹ Source: Eurostat.

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Western history provides a rich source of evidence on the effective financial management of alternatives to private freehold and the lessons learned could be extremely beneficial for the Pacific.

Karl Zimmerman's (1947) study of the rise and fall of great civilizations clearly shows that systems of landownership more akin to those found amongst contemporary customary people is correlated with cultural growth and economic success. This is found in the early histories of the ancient Greeks (to 450BC), the Romans (to 150AD), and Western Europe itself (to 1500AD). All of these cultures had free market places, strong family and cultural bonds and a general rejection of commerce in land. By contrast, freehold land title is linked to cultural demise, along with the move to individualism and away from family and tradition. Zimmerman's recommendation was widely distributed private property, reflecting a conclusion that was more akin to his cultural circumstances and definitely locating him away from anything remotely socialist. This he linked with the importance of strong family or clan bonds and social identity, values that are strong in the Pacific.

Thorold Rogers (1884, reprint 2001) earlier completed an equally thorough study of England's economy between 1300 and 1900. Rogers showed that freehold property title was strongly associated with the impoverishment of working people. This historical correlation is an economic fact was also evident in the late Roman era though ignored by modern western economics. Helen Hughes hinted at this possibility when she opined optimistically that freehold title would mean that customary people may lose their land but they would have access to jobs in a way that is not currently possible in the Pacific (Gosarevski *et al.*, 2004a). What is not specified in this scenario is the level of wages these landless indigenous people might expect, as history suggests it would not be equivalent to an ongoing meaningful participation in the future economic prosperity of the economy as a whole. The Hawaiians are an example of what this means. Within a generation of establishing freehold title over 75% of their land was owned by foreigners and despite finding employment, the indigenous people have only occupied the lowest strata of the island's economic and social hierarchy every since (McGreggor, 1989).

The importance of continuous family or clan ownership for a people's economic stability has been recognised in western thought since the earliest times as evidenced by Walter Kaiser's (1983) analysis of the property system advocated by the Christian Old Testament. Kaiser concluded that the ancient Hebrew custom of permitting what were effectively 50 year leaseholds with rent paid up front, had the practical effect of "*maintaining long-term extended family economic independence with equity*" (Kaiser, 1983, p.34). The tendency of economists to point to GDP per capita improvements, while avoiding the fact that most of the capita miss most of the GDP improvements is a common theme in this literature.

In addition, there is ample evidence that customary peoples can achieve impressive economic outcomes using their land productively. The early colonial era Māori enterprises in coastal shipping, milling and other businesses (Kingi, 2002) and the

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achievements of the people of the PNG Burum Valley (Mandan and Holzknicht, 2005) are documented instances of outstanding entrepreneurial performance. The *Abi* people of Lae (see PNG Case study) appear to be currently reproducing similar outcomes. They demonstrate that effective economic outcomes are possible. The current question is to find how to increase the prevalence of successes, specifically utilising customary owned land, while remaining within authentic cultural boundaries.

This current study has this objective, economic independence for Pacific people with equity. It will accept that some form of private tenure for use, within an overarching regime of financially authentic continuing customary ownership, is culturally acceptable has the capacity to return economically acceptable outcomes. It will focus on the mechanics of leasehold tenures as these are already in operation within the Pacific and examine the conditions whereby they might provide the cultural and economic objectives of Pacific peoples. Leasehold tenure is a system of property rights that has considerable history and application in the west. Historically it correlates with some of the most the most successful periods of western history in terms of the double bottom lone of economic growth and equity (Rogers, 1884, reprint 2001; Burnette and Mokyr, 1995; Grantham, 1995).

In recent times, leasehold has been aggressively pursued as a strategy for financial success by businesses such as Woolworths, the Commonwealth Bank of Australia and even the commercial property usage of the Australian Commonwealth Government. These entities have divested themselves of their property assets in order to free capital for their core business, in many cases leasing back the property assets they previously owned. Their success illustrates that not only is leasehold tenure capable of producing financial and economic success for tenants, but in western countries it is often the preferred tenure system for property users. Likewise, Archer (1974) has documented the many international examples where leasehold development has been successful.

This is not to claim that leasehold is the most attractive tenure system for attracting foreign investment, or that it is without considerable challenges in getting the design right. Part of achieving the optimum design is objectively setting performance criteria. For this study, the criteria include cultural and economic objectives as well as financial ones. The question of equity is an important practical issue within the cultural dimension of the effective use of customary owned land. It is closely linked to the practical genesis of land related conflict, which is a major issue in the Pacific. The notion of equity is problematic within economic thought. This is partly because the market and utilitarianism are implicitly relied upon as the ultimate moral reference point (Small, 2000). It is also partly because economic thought is normally considered to be an entirely separate discipline to ethics (Boettke, 1998), and therefore questions of equity are beyond its scope. The major financial objectives used in this study will therefore include the following:

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Equitable, or just distribution of incomes between tenants and other parties

Rents should reflect a reasonable return for the involvement of land in the productive use of customary land. Rentals should be neither excessive, thereby exploiting tenants, nor too low, allowing land income to leak into the hands of non-owners. This raises the question of what a just distribution of returns between landowners and tenants means (Sheehan and Small, 2006). At first sight, it could be taken to mean that all persons have equal reward for the contribution that they make to the productive effort. However, the relativity between land and labour has never been adequately resolved in terms of justice, only in terms of relative market prices. If relative market prices are adopted, then there will be no wrong answer, so long as there are the usual conditions for reasonable market efficiency, and these are usually taken in practice to be a plurality of participants on each side of the transaction with reasonable knowledge and freedom. These conditions already exist in many parts of the Pacific, such as Fiji, where there are many Indo-Fijian tenants and many Fijian parcels of customary land priced, at least notionally, with respect to the market. The question infers that these cases are not equitable, and the case studies support this contention.

Market pricing alone is therefore inadequate in solving the equity between land and labour in the Pacific, and there is debate over whether it can anywhere else. In the end, if one family supplies labour to the productive enterprise, and another supplies land, then the latter will always have an income without effort, and therefore live relatively more comfortably. On the other hand, if landownership is considered to be a family treasure handed down from generation to generation to help support the current generation, then to surrender that treasure up to others and be left to toil like a tenant is to desert one's cultural inheritance. This is especially the case where surrendering the benefits of the land does not result in equity in practice. Instead, it promotes the potential for foreign parties to take control of the land, which in turn forces the former landowners to take the role of employee. The case of Hawaii illustrates the second possibility. At some point, the people of the Pacific will need to explore these questions if the issue of equity with respect to the use of customary owned land is to be resolved. The question is soluble, but only when located within cultural beliefs regarding justice and fairness.

Related to the question of leased land, notions of fairness and equity ultimately focus on the fact that rent competes directly with the tenant's ultimate net income. This means that once the tenant earns an income deemed reasonable by the community, then the remaining income from the productive use of the land may be taken as land rent without injustice.

Rental collection efficiency

Part of the rent collected must be devoted to property management services, or land administration costs. While these services might be supplied through a variety of arrangements, including government departments, trusts, independent private

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property professionals, or directly by customary owners, the portion of rent devoted to them must be optimised. They can be considered as costs, or equally as the incomes to the persons who perform them.

The property management costs associated with rent valuation and collection should be minimised, though sufficient to provide reliable, sustainable, and professional results. They should be sufficient to provide reasonable remuneration to an appropriate number of adequately skilled property management officers. Implicit in this cost is the training and education of an adequate body of property specialists. This means that they should be neither too low, in which case rental collection will be compromised, nor too high, in which case they will create a burden for those actively involved in the use and ownership of customary land.

Of note, is that the real costs of managing a property generating an annual income of, for example, \$24,000 are the same as for one generating \$5,000. If one month's rental per annum is accepted as a reasonable annual management fee for the \$24,000 p.a. property ($\$24,000 / 12 = \$2,000$ p.a.) this would equate to a reasonable rate of 8.33%. In contrast the same amount of management work would be required for a property with a rental of \$5,000 p.a., but a \$2,000 management fee would equate to an unrealistically high rate of 40%.

Just distribution within the customary owner community

In various parts of the Pacific, rental distribution structures are in place that allocate portions of the rent to different strata of the customary owner community. The balance within these distributive structures should provide adequate recognition of the varied roles and responsibilities within customary owner communities, without undue bias of returns. To answer this question the social, cultural, and historical dimensions of these roles and responsibilities must be considered and rendered into financial terms.²

Adequate inter-generational equity

Three distinct problems exist regarding intergenerational equity. The first is the problem of falling real financial returns to customary owners over time. The second is the problem of dislocated indigenous peoples. There is considerable evidence that current leasing arrangements are implicitly setting intergenerational financial inequities in place across the Pacific. The third problem relates to intergenerational inequities for tenant communities. Despite appearing to gain over time, through the fall in real ground rents to the customary owners, each time a long lease is transferred to a new tenant, the outgoing tenant is able to charge a premium (sometimes referred to as a profit rent) that can be shown to absorb the anticipated benefit. Conversely, tenants buying leases near the end of their term will experience a loss of the premium

² For a more detailed discussion of this issue, refer to Subproject 2.3

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investment associated with possible liabilities related to the obligations of their lease covenants. This will be modelled in the analysis of case studies.

Land use and rental is dynamic. Arrangements that may appear adequate at one point in time may create inequities at some point in the future. Once distribution between tenants, property management, and the various parts of the customary owner community has been agreed, its consistency through time must be ensured.

Conflict minimisation

Land related conflict can originate from many sources, but amongst these the most pressing sources of conflict relate to perceived financial injustice. Some of these sources can be from issues discussed above and include the following:

- > Tenants' concerns over excessive rents;
- > Inflexibility generated through inappropriate property management structures;
- > Inadequate remuneration to sectors of the customary owner community;
- > Title or ownership conflicts; and
- > Victims of perceived inter-generational inequity.

FINANCIAL MANAGEMENT ARRANGEMENTS FOR LAND IN THE PACIFIC

TYPES OF FINANCIAL MANAGEMENT ARRANGEMENTS

Customary owners have been willing to make their land available through leases to foreign people since the earliest periods of colonial history, though they have never fully embraced the notion of alienation through sale (Crocombe, 1961). Despite sharing some fundamental commonalities customary owned land is leased and administered in many different ways across the Pacific. However, it is incorrect to take either the extreme view that customary land is either so varied that no common principles for its effective financial administration can be distilled, or that it is so homogenous that a single system could be devised that would adequately meet all needs.

The following significant commonalities exist with respect to all or most customary owned land currently being used commercially:

- > Customary landowners do not want to sell their land (and are often precluded by Constitution from doing so) and have difficulty accepting the financial reality of land sale;
- > There is a general openness to the effective commercial use of at least part of traditional owner groups' land;

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- > Rental determination is difficult and valuation methods suited to economies where land is bought and sold are of diminished usefulness; and
- > There is broad evidence that the effective financial interests of customary owners will be compromised over time.

Several differences exist. These may be grouped according to several aspects including the direct or indirect management of land, the use of trusts, formal and informal leases, and systems of access to non-customary owners. Trusts and leases are explored in more detail below.

Trust funds

A common difficulty across the Pacific is the lack of financial management capacity amongst landowners, especially in the face of potentially high value uses for their lands. This has been a recipe for exploitation and conflict in the past and it will take time to mitigate. There are several common issues that are evident, including:

- > Inexperience in dealing with money and investment;
- > Inexperience in working within a contractual environment and acceptance of the rights and obligations involved in contracts for lease and sale;
- > Inexperience with western commercial economic mechanisms, income expectations, and costs;
- > Inexperience in operating within an environment where land becomes the primary vehicle for effective income, necessitating precise boundary definition and ownership recognition;
- > The financial implications of cultural tensions involved in relating to dealing with the western commercial world; and
- > Inexperience in adapting traditional authority structures in the face of inordinate comparative wealth relative to traditional subsistence lifestyles.

Generally, it is the case that customary people are willing to lease parts of their lands to tenants, so long as the land ownership (superior property rights) does not pass out of the control of customary landowning group. The problem arises when lease contracts are required to formalise the relationship. Leases involve relatively long-term *partial* alienation (of occupation and use rights) and this is foreign to the experience of customary people. As a result, customary owners have not been particularly effective, in general, in negotiating leases for appropriate values. When they sense that they have undersold themselves, there has been a tendency to violate the contractual lease terms. This risk of violation of formal / contractual lease terms has acquired the name *sovereignty risk*, on the basis that violation of contractual obligations by persons in authority locally is similar to default by government at higher levels.

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Trusts have been used to overcome many of these problems, especially the general sovereignty risk problem. Three types of trusts are found in the Pacific. The most local are legal corporations representing landowners, such as the Incorporated Land Groups (ILGs) in PNG. These entities can be considered as trusts to the extent that they are bodies who represent the landowners in legal dealings with others, without actually being the landowners. They negotiate and operate in the same way that an individual or small business does and their activities are only generally regulated. They have the major advantage of overcoming ownership uncertainty by permitting the creation of leases even when a complete and precise understanding of customary ownership is unavailable. As a trust, they can stand for the customary owners productive use of the land even while ownership disputes are being resolved.

In many PICs, the government (or a Minister thereof) serves as a trustee for customary landowners. This has two levels of expression. In countries such as Samoa, leases are made through the government, who acts as a guarantor that the lease terms will be honoured. In many countries, this notionally provides a degree of rental determination consistency. This strategy is even used in situations where landownership groups are the expression of the customary owner group, such as PNG. Despite mitigating sovereignty risk and providing nominal rental consistency, these arrangements do not appear to effectively ensure rental equity due to the valuation methods employed and the practice of selling leases with premiums. However, there is a risk that the government could be seen as not being impartial in the arrangements, with ensuing potential for being sued by the customary landowners.

The most developed private trusts are found in New Zealand representing Māori interests. The Māori trusts in New Zealand are self-governing corporations representing the interests of Māori customary landowners. Some of them are quite sizeable; e.g., the *Atibau-Whanganui* Incorporation employs about 40 people. As private entities, they are entirely self-funded and are responsible for providing adequate human and organisational resources to carry out their mission of managing Māori land on behalf of the customary owners. Much of the land administered by the trusts are occupied by non-Māori tenants, though it is the long term goal to return the land to Māori occupants as leases expire. The financial performance of the Māori trusts is lower than for comparable non-Māori ventures (Wedderburn *et al.*, 2004), though this is in part due to the social objectives of the Māori trusts that place an emphasis on both and financial goals.

The Māori trusts are owned and managed by the customary owners. As such, they have a level of autonomy and responsiveness that is higher than statute backed trust system found in Fiji, the Native Land Trust Board (NLTB). This is a government instrumentality that has the most independent and formal trust character. Its officers do not necessarily have any connection with the customary owners whose land they administer. It was originally created to provide a convenient point of contact with

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customary owners for the colonial powers (Fingleton, 2002). It will be described in detail below.

The Native Land Trust Board (NLTB) was established under the *Native Land Trust Act* (NLTA), 1940. It was created to:

- > Administer and control all customary land for the benefit of the native landowners;
- > Set aside some land within each landowning unit's total acreage as its reserve and such land shall be for use, maintenance, and support of its members;
- > Make unreserved land available for leasing to anyone;
- > Support government development programme through leases or outright purchase under the state Acquisition of Lands Act for public purposes;
- > Ensure, at all time, that each landowning unit has sufficient land to support and maintain it; and
- > Provide sound financial management in all facets of its operation so that the landowners wealth continues to grow and be guaranteed.

The Board of the Native Land Trust comprises, H.E. President of the Republic of Fiji as its President; The Minister for Fijian Affairs as its Chairman; 1 or 2 members appointed by H.E. President of the Republic of Fiji; 5 members appointed by the Great Council of Chiefs; and 3 members appointed by the Fijian Affairs Board.

The NLTB administers some 32,000 leases of different kinds. Amongst them are some 13,800 agricultural leases of which some 11,000 are leases granted under the provisions of ALTA and the others are leases on native reserved land that are outside the jurisdiction of ALTA. Other lease types are Residential; Industrial; Commercial; Hotel and resort developments; Reforestation (pine and mahogany plantations leases); Educational; Religious; and Civic purposes.

The NLTB distributes rental income to customary owners on the basis of the traditional social hierarchy of Fiji. Under this distribution, the NLTB takes an initial 15% of rents to cover administrative expenses, sets aside a 5% part for a collective trust fund, and distributes the remainder to customary owners. The customary owners are separated into various chiefly groups to whom 30% of the net rent is paid. This leaves ordinary villagers to share in the remaining 56% of the rent paid by tenants. The relatively large gap between rents paid by tenants and rents received by villagers is a growing source of tension and an inclination to avoid formal leases through the NLTB trust structure.

The NLTB sets rents using a set rental yield worked from a notional unimproved land value. The land value is notional because there is negligible sales evidence and the value is only derived through the application of a fixed capitalisation rate of 6%

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to rentals. However, the amount collected varies and in line with government rentals is often nearer 3%.

Despite the size and importance of the NLTB, it has encountered significant property management problems. Arrears in rents have been with NLTB from its very beginning and the Board has been criticised for them from all quarters. On the first quarter of each year over the last 10 years, the Board carried rental arrears totalling some \$12 million. This is about a third of the total rent roll of around \$33 million. The difficulties in arrears collection seem to be:

- > Serving notice and collecting rents is costly and time consuming and tenants are not penalised for the extra costs through interest payments or other penalties; and
- > Large scale default requires prohibitive resources to control, beyond the reasonable capacity of the Board.

More common in the Pacific are smaller scale trusts of the sort found in PNG as Incorporated Land Groups (ILGs). The family trusts in Samoa and Solomon Islands have similar characteristics. The primary purpose of ILGs is to produce a robust landowning entity capable of acting as customary legal entity for leasing land to individuals. They have the primary objective of overcoming ownership conflicts by creating a corporate owner group comprising the customary community who own the land. The construction of the group is a matter for resolution by the customary people themselves, who stand behind the ILG in its activities with the land. As trustee, the ILG has the right to lease the land, and the obligation to respect lease contracts once made. ILGs also have the authority to alienate land to the government when infrastructure needs necessitate sale (although leasehold arrangements are considered preferable).

The advantages of ILGs over a national level trust arrangement such as the NLTB, are that they are at a smaller and more local scale, they do not carry substantial administrative overheads, and the distribution of income to various members of the customary owner community is more dynamic and responsive to contemporary circumstances. This is illustrated by contrasting the NLTB in Fiji and the land management through the *Abi* Corporation in Lae, PNG. The *Abi* Corporation is a company owned by the *Abi* people to manage their interests, especially over land. One of its current projects is the development and eventual management of an urban precinct on the edge of Lae City. The corporation is largely headed by the community leaders of the *Abi* people, whose incomes are not based on an arbitrary rental, but rather a management salary. The financial structuring of the venture has few leakages out of the customary community and the eventual rental income will be efficiently utilised for community maintenance and the support of the *Abi* community.

Identification of customary ownership rights is one of the objectives of the trust structure, but it is not always realised. The *Abi* community is an example of where there has been clear identification and acceptance of the customary owner group. The Māori trust model has modest difficulties identifying the membership rights of

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various customary owner groups, but many countries, such as PNG and the Solomon Islands, experience substantial difficulty identifying customary owners adequately. In PNG, the ILGs are left largely to themselves to include owners precisely, and there is suggestion that many have been formed hurriedly under the incentive of development incomes, where the members are unlikely to correctly represent people with ownership rights. In Fiji, the disbursement to various chiefly levels encourages dispute over chiefly domains.

Lease arrangements

Lease arrangements can be separated into formal and informal arrangements. Formal leases are registered by the state and they are often made through a state intermediary. In Fiji, the majority of formal leases over customary land are made through the NLTB (it is a statutory requirement), whereas in PNG formal leases are created through a lease and leaseback arrangement with the government. When customary owners want to lease land to individuals, they must first lease the land to the government, who in turn leases the land back to the customary owners. The customary owners then on sell the lease to tenants. Through this arrangement, customary owners are legally only leasing to the state and tenants are leasing from the state. The arrangement means that leases are legally secure, being controlled by the state. This avoids possible failure by either party to violate the terms of the lease. Where customary owners are unfamiliar with the contractual obligations of leasing land, this strategy is especially appropriate. It notionally affords a level of consistency to the leasing landscape. The emergent family trust system in Samoa has a similar underlying effectiveness.

There are examples where leases are sold to tenants with a premium, or key money. The fact that tenants are prepared to pay an initial sum in excess of the agreed rent indicates that rents are too low, as the premium represents the present value of the worth of the property above its rent. Although the premium goes to the customary owners in the first instance, where long-term leases are subsequently transferred through a secondary market, the premium becomes a quasi capital interest that behaves in the same way as a partial ownership. This apparently innocent practice is responsible for many of the subsequent problems in the effective use of customary land through time.

There are varieties of informal lease arrangements. The financial inefficiency of the NLTB has encouraged informal (*vakavanna*) lease arrangements between Fijian owners and tenants. Through direct leases, Fijian villagers are able to sidestep administrative fees and payments to remote chiefs. Informal leases are common throughout the Pacific for various other purposes as well. The most widespread informal leases occur in peri-urban (*quasi squatter*) settlements. In all cases, informal leasing provides financial incentives to local customary owners and tenants, but adds considerable risks to tenants and sometimes creates problems for customary owners.

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QUALITY OF TITLE

“Insecure land tenure is linked to poor land use” (FAO/USP/RICS Foundation, 2002). There is evidence that despite a generally clear understanding across the Pacific of the customary origin of landownership, the various tenures that have been developed upon it are perceived as risky. Sovereignty risk is a major issue across the Pacific and it has significant financial implications. The call for *ex-gratia* payments over land that was sold to the state to become freehold is a good example of this problem. The following are instances of apparently risky land title found in the Pacific:

- > Jackson’s airport in PNG where current descendants of the customary owners who sold it to the government have recently militated for *ex-gratia* payments to compensate them for what they consider to be the shortfall in the price paid to their ancestors who sold the land outright;
- > Freehold title, for example in Vanuatu, Solomon Islands, Samoa, and Niue where it was extinguished at by the respective Constitutions at Independence;
- > Peri-urban leases on the fringes of many Pacific towns and cities. This is especially important when attempts are made to regularise these settlements, such as what has been attempted in Fiji;
- > *Vakavanua* leases outside formal institutional arrangements in Fiji. These notionally illegal leases bypass the institutionalised leasing systems, which village level customary landowners and tenants see as financially inefficient;
- > The pervasive but generally extra-legal practice of selling leases using a premium payment; and
- > The transitional situation of tenants in NZ on lands that were previously state leasehold and have now been returned to Māori customary owners. These tenants previously enjoyed very low rents and an informal private interest that capitalised into premiums paid on lease transfer, but will be amortised as leases roll over into Māori hands with the likely prospect of genuine market rents.

No formal title, such as the examples found in peri-urban settlers, does inhibit efficient financial utilisation of the land. It compromises the provision of necessary services and infrastructure, and creates the perception that development on customary owned land is high risk. From a financial point of view, this elevated risk translates into higher profit thresholds for tenant developers, which in turn depresses the rental return to customary owners. Sovereignty risk therefore, in all its guises, is a financial burden and impediment on effective utilisation of customary land.

LEASE STRUCTURES

Rent determination

Rental determination is perhaps the single most important issue in the effective financial management of customary owned land in the Pacific. However Setefano

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(2000) outlined the way that even recently the Pacific was at a loss to set a reasonable method for valuation and rental determination. Of more concern was Tim Anderson's (2006) conclusion that his calculations suggested that rents to customary owned land were inappropriately low. Compared to western freehold countries, there is no significant market for sale and the rentals use either inconsistent or inappropriate methods of valuation.

Land price and land rent are intimately connected through the yield rate in western freehold land markets. This means that market evidence can be used to ascertain the appropriate yield rate, and if either the sale price or rent is known for the subject property, the application of the yield rate will solve for the missing element.

In the Pacific, rents are usually set as statutory yield rates to Unimproved Capital Value (UCV). The problem is that UCV is only a notional quantity as there is no positive market evidence of value (sale price) as little land is sold in the Pacific. UCV is derived by capitalisation, dividing rents by the yield, or capitalisation, rate. Usually opinions of experts are used to estimate UCV. This practice appears to have its origin somewhere in the colonial history that saw land valuation methods imported from the first world into environments that had no land market whatsoever.

Similarly, the percentages adopted to compute rents from UCV are the result of established rather than market forces. They tend to be set using a very simple set of land categories (rural or urban) and there is evidence that their simplicity leads to inconsistent valuation. For example, rural land leased from customary owners in Samoa or Fiji is valued using the same formula regardless of whether it is to be used for plantation crops or tourism, despite a massive difference in the value of these land uses (this is expanded on in the next section).

The capitalisation and yield approaches to solving value and rental problems are useful in practice given their relative simplicity, but they obscure the fact that in sum they do not answer the question of which factors are primary in establishing value. Garrick Small (1999; Small, 2002) used experimental methods to conclude that rent is prior to sale price. This is consistent with classical economic theory, though it is a fact that is often ignored in recent economic thought. Likewise, at least in theory, the yield or capitalisation rate is grounded in the finance markets, where property investment competes with other investments to attract funds. The yield is based on risk in comparison with other possible investment options. In its most developed form, this risk and return relationship is valued within the capital asset pricing model. Combined, these two economic facts suggest that rents are the primary component of land value and the habit in the Pacific to rely on standard yields ignores financial realities.

There is another stream of evidence from the Pacific regarding the quality of rental determinations for customary land. There is a well developed secondary market for property, especially in urban areas. Table 1 (below) is an analysis of a vacant commercial site in Port Moresby. The lease for the land is currently valued at about

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K4,000,000 yet the rent to the customary owners is only K2 p.a. Using the capitalisation rate that is used in PNG (5%), the current rent being paid to customary owners is only 0.001% of the true market rental. Not only are customary owners being disadvantaged through the use of UCV, Abdul Hassan (2005) has argued that UCV is not effective in providing vertical equity when used for land taxation, despite its wide application across the Pacific.

TABLE 1: 'STEAM SHIPS' COMMERCIAL SITE IN BOROKO, PORT MORESBY, PNG (CURRENTLY VACANT LAND)

Current price to buy lease	K	4,000,000	
Current rent to customary owners:	K	2	per year
Capitalised rent to customary owners:	K	40	
PNG Capitalisation rate		5%	
Ratio		0.001%	

An analysis of residential property in Fiji demonstrates a similar situation (see Table 2). Most leased land is developed in the urban areas of the capital, and in Suva there is a well developed market for rental housing. Investors acquire leases for urban land, erect houses, and rent the developed property to tenants. It is possible to strip back the value of the house improvements to estimate the underlying component of the market rent that relates to the land.

TABLE 2: FIJI - HOUSES IN SUVA

	Medium value	High value
House Prices range:	\$ 300,000	\$ 500,000
Improvements Value:	\$ 150,000	\$ 150,000
Land value (deduction)	\$ 150,000	\$ 350,000
Land rental per annum by deduction	\$ 9,000	\$ 21,000
Typical land rent to customary owners	\$ 800	\$ 800
Capitalised land rent	\$ 13,333	\$ 13,333
Capitalisation rate	6%	
Ratio	9%	4%

This suggests that even though the market has been able to set rents in the secondary market, the land rents flowing to customary owners is perhaps as low as 5-10% of the true market level.

Informal rents are more difficult to analyse. It appears that rents for peri-urban lands on the fringes of towns are set directly between the parties, and often follow patterns conforming to traditional life more than mechanical western pricing. In Lae, rents in peri-urban settlements are often in terms of erratic contributions to the tribal obligations of the customary owners, such as feasts for weddings. As such, they are almost certainly not set at economic optimum levels and are likely partially the cause of the flourishing of squatter peri-urban settlements. In particular, they are not organised in a way that provides potential for the funding of basic urban

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infrastructure. Informal rural leases appear to be common in some area. In Fiji they are a practical, though risky, alternative to the official structures via the Native Land Trust Act (NLT) or Agricultural Landlord and Tenant Act (ALTA) and Lal *et al.* (2001) tabulate their apparent frequency and attractiveness.

From the secondary and informal rental markets, it is apparent that the community is capable of setting rental values on land, and these are probably more reasonable than those proceeding from formal rental determination methods. This suggests that there is scope for a revision of rental determination methods. Rental determination for the Pacific, however, should not attempt to mimic methods better attuned to markets that are fundamentally dissimilar.

In addition to appropriate valuation methodology, rental determination also requires an adequate body of skilled valuers. There is a lack of experienced valuers in the Pacific. In PNG, Solomon Islands, and Samoa for example, the Lands Department has insufficient valuers on staff and in PNG an almost insignificant number who are prepared to do rural work compared to the scale of need. Private practice in PNG, Solomon Islands, and Samoa is similarly under-resourced in terms of appropriately educated and trained professional staff. Discussions with various graduates of the USP degree course in land management suggest that despite the quality of that programme, in many Pacific countries there are very few educated property valuers and few of those have the experience or have been appropriately mentored to meet the scope of the work required (Boydell, 2007a).

In addition to the formal leases, there are many instances of informal direct leases. These are often the result of frustration by customary owners and tenants with formal institutional arrangements, which introduce considerable transaction costs and rigidities. As stated, informal leases are also found in peri-urban settlements on the fringes of towns. In many PICs, town land is limited through for various historical reasons and squatters often use adjacent customary land. The term *squatter* is not strictly appropriate since these settlements usually have some degree of acceptance by the customary landowners and the landowners do collect some rents. The relationships are informal and the rentals are in no way secure for either party. The rental levels are the result of a local practical market of sorts, but they are frowned on by authorities since they avoid rates, taxes, formal distributions to chiefly groups and result in infrastructure problems.

The absence of formal records and registers impedes transparency. This raises questions about the effectiveness of the market in peri-urban rental to deliver appropriate pricing.

Rent collection

Rent collection across the Pacific is varied. The level of rents collected by customary owners is in general low in most cases, except in New Zealand. Despite this, there is strong evidence from formal sources that rent collection is problematic. Kiribati has

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69% of its rents in arrears (Brotoisworo, 2003). Rent collection by the NLTB and related arrears issues are a major and well-recognised problem (see country case study). Apart from the very high level of arrears mentioned above, there is also evidence that systemic problems with rent collection have had the practical effect of prompting rental levels to be lowered in practice.

A discount rate is applied to the UCV of the land to determine the annual ground rent applied to a particular parcel. The statutory ground rental rates vary between 5% (e.g., PNG) to 6% (e.g., Fiji, Solomon Islands³), and apply to both government and customary land. However, it is common to find that far lower percentages are applied than those permitted under various country legislation. For example, in Fiji the maximum rent under both the Agricultural Landlord and Tenant Act (ALTA) and the Native Land Trust Act (NLTA) is 6% of the UCV. In practice, the Native Land Trust Board (NLTB) as Trustee of the customary owners only collects 2½-3% of UCV, because the State as a matter of informal policy collects this much, or less, under their ALTA leases. The situation is similar in the recent UCV model developed in Honiara, Solomon Islands, where the Valuer General's office has charged as low as ½-3% of UCV on urban government land, based on reasonableness and affordability.

The widespread difficulties in rent collection provide further evidence the UCV model is unrealistic. In a western market, an investment property with a reputation for uncertain rent collection would attract a very high capitalisation rate, to reflect uncertainty and risk. This has the effect of lowering the sale price. This mechanism is impossible in the Pacific with its practice of fixed capitalisation rates.

These variations in regulated rentals raise several issues:

- > A belief by some in government that 6% of UCV is not affordable;
- > Does this mean 6% is too high or the UCV is too high, and who could tell in a market skewed by limited access to freehold or perpetual estate title?
- > Opens potential for corruption if deals are negotiated at less than 6%, albeit that the benevolent actions of the government in charging less than the prescribed maximum serve to liberate access to land at a level that provides some social support. Complications, and resultant conflicts, will inevitably arise in the future (taking a 50-75 year time horizon) when available urban land is in even shorter supply and the land value is at a premium;
- > Problems for trustees (e.g., NLTB) of customary land in attracting tenants if they are charging the statutory rate (6%) and the government is charging half of this (3%); and

³ Although the Solomon Islands legislation specifies 8% for restored freehold land, where the freehold title has been extinguished by the Constitution.

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- > Risk of the government or trustee being sued for charging less than statutory maximum rental.

UCV is also adopted as the basis for municipal rates for services in certain urbanised areas in the Pacific, again with a notional 5-6% being applied as the basis for the rateable component. This double application of the hypothetical UCV in the determination of both regulated ground rent and municipal rates adds to the confusion.

A criticism of the UCV approach from a landowner or landlords perspective is that the resultant regulated rentals do not keep pace with the increasing value of land over time, despite inbuilt periodic review clauses.

Planning and land value

In western countries, land value is significantly influenced by land use planning controls. This is due to the fact that different land uses have different values and different yield rates. In Australia for example, commercial land is usually considerably more valuable than residential land. In addition, Sydney commercial yields are between 8-11%, while residential yields are 3-4%. This means that the UCV depends on the possible land use and in some cases, the rent is even more varied. UCV determination in the Pacific generally is based on value as undeveloped rural use. This means that it does not respond to the potential increase in value due to land use type. The adoption of a single national yield rate further constrains rentals to unrealistic levels.

Ground rents should be sensitive to permitted or probable land use in order to be realistic. This is linked theoretically to the fact that land rent is a residue computed through the highest and best use of the land. Obviously, specification of the highest and best use is a necessary precondition for accurate rental valuation. The absence of a land use planning system with rents linked to optimum land use is an important shortcoming in the Pacific.

Access to debt

Customary land has been said to result in difficulties, limiting access to debt capital. de Soto (2000) is representative of authors who have claimed that development would accelerate if customary owned land was privatised into freehold, since freehold title is seen by lenders as the optimum security for debt. Customary people the world over have been reluctant to follow this path to development, since it jeopardises what is seen as their obligation to future generations (Ezigbalike, 1994). Discussions with senior staff in major banks servicing the Pacific indicate that customary ownership is not in itself an impediment to debt finance.

Discussions with senior Westpac staff, for example, revealed a consistent policy of lending to ventures being developed on customary land in the Pacific. This was evident both in Australian administration, and in local country head offices. Several

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important factors emerged from the bank's position. It was collaborated by similar approaches from other banks (notably, ANZ the other leading regional bank).

From the bank's perspective, it is the business venture rather than the land that has financial value. The business venture has the capacity to generate debt-servicing cash flows. Customary land in itself is not the primary security in its undeveloped state. Generally, there is an abundance of alternative land potentially competing for any given land use, which makes holding title to the land not especially valuable. However, there are many potentially profitable ventures on land in the Pacific and these are realised through the reality of the physical development.

Likewise, from a bank's perspective, lending into a development venture is a reasonable position so long as the venture can demonstrate a credible profitability. The security in this case is control over the cash flows generated by the development. While controlling the land is one way to gain control over this security, it is not necessary for the land title to be freehold, it only needs to be secure leasehold over the economic life of the development, or a sufficient portion of it to cover the bank's financial exposure (risk).

Banks express a willingness to lend to leasehold titles, and cite examples in other countries, such as the leasehold regime in the Australian Capital Territory (ACT) where they routinely provide loans against leasehold interests as security. An important difference between these cases and leaseholds over customary owned land in the Pacific is the perceived unreliability of institutional arrangements in the latter. If banks cannot be confident of being able to use or liquidate leasehold interests, then their security value in the land and possible improvements becomes negligible. The use of trusts goes a long way to mitigating this risk and the varying risk quality of institutional trust arrangements goes a long way to explaining different attitudes to lending in different parts of the Pacific.

This would suggest that any difficulty regarding access to debt is not related to land tenure, but rather to the lack of evident capacity to manage development and commercial enterprises. The ANZ bank has developed an education programme and mobile banking facilities to raise financial literacy amongst villagers in Fiji, PNG, and the Solomon Islands in an attempt to increase financial capacity.

The above examples suggest that debt-financing effectiveness on developed land uses on leased customary owned land should not be a problem. It further suggests that the blockage in the effective financial use of customary owned land largely lies with increasing financial management capacity of the indigenous community. However, to ensure success there is a need for an increased level of flexibility on the part of the lenders head offices to support localised arrangements.

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COMPENSATION ON LEASE EXPIRATION AND/OR RENEWAL

Compensation for tenants improvements

Strategies for clarifying property rights and related compensation for the undepreciated value of improvements made by tenants is an important component of customary land management. If compensation is not made, tenants are discouraged from investing in useful improvements towards the end of leases, leading to sub-optimal land utilisation. Fijian leases under NLTA (see Fiji case study) include provision for tenants to either remove or be compensated for improvements at lease expiry. Similar provisions exist in other PICs, such as Samoa, but in countries where leases are less standardised, such as New Zealand, provision for compensation is less consistent.

There are difficulties with compensation from the perspective of landowners as well. Landowners often will not be in a position to purchase improvements, so the expectation of compensation to outgoing tenants may unduly burden them, or have the effect of forcing them to roll over the leases. This would be more likely where improvements are substantial and the landowners do not have the capacity to operate them effectively, such as the case with tourist facilities. While there is evidence that banks are willing to lend against project cash flows resulting from the developed use of customary land, they need to be confident that the borrower has the ability to manage the project effectively (this is known as *client risk*).

Clear pathways are needed for the treatment of compensation for improvements that give all parties flexibility and incentives for efficient economic utilisation of resources. At the end of leases where landowners are faced with the prospect of inheriting improvements that are beyond their means to purchase, methods of being able to sell the outgoing tenants property rights in improvements to and incoming tenant need to be fostered. This would mean the changeover of the lease would include a rental component negotiated between the incoming tenant and the landowner, as well as a sale component that would relate to the transfer of property rights in the improvements. Perhaps, in time, there may be scope for even the latter to be rented, though this level of complexity does not appear easy to engage with in the near future under existing institutional arrangements.

Compensation for land/property deterioration

Closely related to compensation for improvements is compensation for property deterioration. Notionally the land should be returned in the same condition as it was given. This view has been used as the basis for clearing improvements off the land at lease expiration. Such a policy limits the value and use of the tenants' improvements for all parties. As a result, the improvements under a leasehold arrangement are seen as a wasting asset to the tenant, commonly resulting in an increasing lack of maintenance in the latter years of the lease. Prior practice in the case of residential leases in Fiji administered by the NLTB has been to grant a lease renewal or

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extension without capturing what could be referred to as the *marriage value* between the respective landowner and tenants property rights in such an renewal / extension.

In respect of property rights in the land component, the development of environmental science has demonstrated that land can be easily degraded through apparently ordinary use. Currently degradation is most apparent in mining projects with spectacular examples of land degradation, such as those in PNG, or through deforestation initiatives in several PICs. This is a source of conflict that will become increasingly prevalent in the future.

BENEFIT AND COST SHARING

There is a wide variety of benefit and cost sharing across the Pacific. The common underlying themes are the sharing between landowner and tenant, the allocation of resources for land management and the changes in these allocations through time.

Landowners are in a natural position of economic power in most economies due to the scarcity of land. This is not always evident in the Pacific, where the value of land needs to be unlocked using development or land uses that are often materially of financially beyond the entrepreneurial capacity of customary landowners. The sharing of costs and benefits is an essentially financial matter. It can be analysed in terms of the costs of developing commercial land uses, the costs of land administration, including rental determination and lease management, and the provision of public goods that are necessary for realising the best level of productivity from the land. All of these can be considered as being drawn from what would otherwise be available as land rent.

DISPUTE RESOLUTION MECHANISMS

Two major sources of dispute exist relating to customary owned land, *viz.* disputes over landownership and disputes over rentals. The majority of attention appears to be given to ownership disputes. Rental disputes relate mainly to rental levels and payment default. The former is a valuation problem, while the latter is contractual. This section briefly considers the land dispute mechanisms available but with emphasis on the financial aspect of dispute, which relates to rentals.

FORMAL MECHANISMS

Recourse to formal legal institutional processes is available for land related disputes, but there is an abundance of evidence that it is increasingly seen as the remedy of last resort. Specialist land courts, such as the Māori Court in New Zealand, the Land and Titles Court in Samoa, or mediation bodies such as the Land and Property Directorate in East Timor have the advantage of bringing more specialist knowledge, less expense, and (potential to reduce) delay. The absence of a specialist land court in Fiji has been identified as a weakness in that country's ability to efficiently resolve land conflict (see Fiji case study).

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There is a general preference for more local and informal mechanisms that respect and engage with customary protocols.

INFORMAL MECHANISMS

The Judicial Training Programme operated Pacific-wide by the Institute of Justice and Applied Legal Studies (IJALS) at the University of the South Pacific has taken the lead in supporting Alternate Dispute Resolution (ADR). They have developed this through training programmes in adjudication and mediation techniques for the judiciary and court structures. The Commonwealth Association of Surveying and Land Economy (CASLE) support this approach, recommending that adjudication and mediation be added to the 'toolkit' of surveying and land economy professions in developing countries (Dann, 2007). There is a view (e.g., Williams, 2002) that trained non-partisan mediation professionals are the most appropriate facilitators to undertake the mediation role. Traditionally, chiefs or 'big-men' have taken the adjudication role within clan / familial structures in the region.

Village courts in PNG represent the nexus of the formal and informal dispute resolution system. Circuit magistrates visit villages regularly to resolve local disputes, in a manner that owes its origin to the tradition of patrol officers who represented the colonial government at the local level. Some village court magistrates invite disputants to talk over their grievances before the flag is raised by the court, signalling that the village court is in formal session. Before raising the flag, the magistrate is merely a third party who might listen and give informal advice. After it is raised, he exercises the authority of the state to decree a resolution and expect a level of formality from disputants.

Truly informal dispute resolution is merely the meeting of disputing parties, perhaps in the presence of community representatives. This has the advantage of using local knowledge and common sense, is inexpensive, and usually faster than formal mechanisms. Developments in formal mechanisms, such as the Land and Property Directorate, aim to capture some of the advantages of the informal mechanisms while still bringing a higher level of closure than is sometimes possible through the latter. However, these mechanisms work well in resolving social matters, but are commonly less well accepted when the problem is economic, having at its core an element of financial dispute.

ABSENTEE LANDOWNERS

Internal migration away from one's customary lands in search of better work, housing, health care and education opportunities, is becoming common in the Pacific as more people leave their home in search of employment and better futures for their children. This creates a raft of problems that will potentially catalyse conflict situations in the future.

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Trends of globalisation, urbanisation and concentration in commercial centres affects property rights, both of absentee 'customary' landowners, as well as of frustrating those who are left behind in semi-subsistence lifestyles on Pacific islands, reliant on remittance income from their urbanised overseas kin. As Crocombe (2001) identifies, there exists current legislation to cancel the rights of absentee land owners in some Pacific islands.

In Samoa, the accepted authority of the *matāi* is not limited by location, so for any decision over the commercial development of familial land the support of all *matāi* in the family must be obtained. Given that Samoa has a resident population of 180,000 (approx.) and there are 120,000 (approx.) Samoans resident in New Zealand alone, plus a significant population of kin resident in (but not limited to) Australia and the US, proctoring full *matāi* support can be a time-consuming if not impossible task. The *matāi* chiefly title brings a range of rights and obligations, and whilst the issue of leaving the management of land 'back-home' in Samoa to the resident family residents, this solution to facilitate the development decision-making process was not warmly received. There remains a politically strong view that once a *matāi* always a *matāi*, irrespective of global location.

The challenge of absenteeism in the decision making process is not limited to Samoa. For example, Fiji law allows the clan to delete from joint ownership any person who has been absent for two or more years, yet this has never been invoked... indeed many men will have been absent for at least that long. A similar law in Kiribati, albeit no longer applied, assumes that any man who has been absent for seven years is assumed to have been 'lost at sea', and his lands reallocated. Whilst some 91% of Cook Islanders do not live in the Cook Islands, nowhere is the issue of absentee landowners so clearly demonstrated than in the Polynesian raised atoll of Niue, with 93% of Niueans residing overseas (Levi and Boydell, 2003).

Restrictive attitudes of absentee owners (irrespective of their length of absence) are an impediment to land development projects. Absent Niueans often refuse, or are reluctant, to enter into negotiations, collectively or individually and attempting to negotiate with them is a consuming and frustrating process (Tongatule, 1981). Kalauni (1977) describes land negotiations on Niue as 'fiddling with feelings rather than reality'. As customary land titles represent 95% of land area, it is difficult to precisely define the rights of a descent group in any land. The claim of equal land rights for absentee Niueans to those who remain resident on the land is grounded in the 'descent group concept', ignoring criteria for use and residence.

The above examples highlight that the management and enjoyment of the benefits of customary landownership become problematic for people who leave their traditional lands. In some PICs, people lose their land rights when they leave their traditional locations but in others, they do not. Absentee owners have different priorities to local owners and have the potential to be disruptive as they romanticise the 'old' village or country way from afar. It is debatable whether they retain a right to enjoy rents earned from customary land.

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Conversely, internal migrants commonly find themselves landless at their destination and subject to the need for employment for income and usually the obligation to pay rents. In many cases, they find themselves in peri-urban settlements on very low wages. In this situation, they miss access to being able to derive a livelihood directly from the land or the rents that are increasingly available from leasing it to foreign (or non-local) tenants. They often aspire to returning to their ancestral lands, or at least ensuring that it remains available for their children.

A second class of internal migrants are also important. These are people who obtain an education and move to the cities to take up positions of importance and semi-western lifestyles. These people are often in positions of influence and have the capacity to influence policy. They are landless, though they often have aspirations to secure land for themselves or their children. Their influence on policy needs careful consideration, especially if they have received a western style education that can serve to challenge cultural values grounded in very different customary traditions.

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LESSONS LEARNT AND KEY GUIDING PRINCIPLES

PREMIUMS AND RENT PAYMENTS

When leases are transferred, the property rights are often ‘sold’ as packages where the return to the property right holders can consist of two components: an annual rent and an initial premium. The *premium* in this situation equates to the present value of the tenants interest derived from a *profit rent*. A profit rent occurs where the open market or ‘full’ rental value is higher than the passing (total or ground) rental paid by the tenant. An issue arises over who the beneficiary of the premium should be – the landowner or the tenant. All parties must recognise, or understand, that the premium is a component of the total return for the land.

Finance theory defines the financial value of an asset as *the present value of its future returns* (Wilson and Keers, 1990). This means that the sale price or transfer value of a piece of land is actually the total of all its future rents, discounted by the time value of money (also known as the time *preference* of money). Conversely, in the case of premiums, these can be considered as a one-off rent payment equivalent to a string of periodic (e.g., monthly or annual) rent payments over time. The relationship between the premium and the equivalent annual rent is a function of the length of the lease and the adopted discount rate.⁴

The primary lesson here is dependant on who ‘owns’ the property rights in the leasehold profit rental component. The total return to the customary owners is made up of the immediate premium plus the annual rent and each can be calculated in the terms of the other. For example, a premium can equate to the annual equivalent at today’s worth of series of future rental payments, discounted at an appropriate interest rate sourced, ideally, from transactional evidence. The perception that premiums are independent *ex gratia* payments is common and this misunderstanding often reaches the highest levels.

A typical example of this confusion was demonstrated in PNG, where a senior government official involved in the National Land Development Taskforce outlined what he saw to be the desirability of customary owners being able to earn twice from the lease of customary land, as though these two components were independent receipts. It was suggested that for the sale of piece of customary land, the owners would be able to earn a \$200,000 premium, as well as an annual net rent of \$5,000 per year. This case will be analysed below as an example of the underlying embeddedness and the resultant problems.

Firstly, the term of the lease will be assumed to be for 50 years, and the discount rate (acceptable rate of return) will be assumed at 10%. Under these conditions, the \$200,000 premium is equivalent to an annual rent of \$20,171 per annum over the life

⁴ It is important to highlight that the term *premium* is also commonly used for other single or periodic payments under a lease. In the later example of rent up-front, the single up-front payment is also known by some as a premium. This variable meaning and application of the word in the region has been a cause of confusion for several of the valuers interviewed during the fieldwork for this report.

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of the lease. This is about four times the actual passing value of the annual rental. If, for example, the lease term extended to 99 years, the annual rental equivalent of the premium would only fall to \$20,001. This small difference is typical and demonstrates how distant cash flows have little impact on present values. In contrast, if the lease term is reduced to twenty years, the annual equivalent rental of the \$200,000 premium would equate to \$23,491 p.a. These figures are summarised in Table 3.

TABLE 3: ANALYSIS OF PREMIUMS AS EQUIVALENT ANNUAL RENTAL

Lease Term (in years)	20	50	100
Discount Rate	10%	10%	10%
Premium payment	\$200,000	\$200,000	\$200,000
Annual Equivalent ⁵ of \$1 for selected lease term at selected discount rate	8.5136	9.9148	9.9992
Equivalent Annual Rental	\$23,491	\$20,172	\$20,001

Conversely, the annual rental of \$5,000 for a 50-year lease term, discounted at 10%, is equivalent to a single upfront payment of \$49,574. Table 4 summarises the financial mathematics and includes computations for lease terms of 20 and 99 years as well.

TABLE 4: ANALYSIS OF PRESENT VALUE OF LEASEHOLD INTERESTS

Lease Term (in years)	20	50	100
Discount Rate	10%	10%	10%
Annual net rental received	\$5,000	\$5,000	\$5,000
Present Value of \$1 for selected lease term at selected discount rate (i.e., YP)	8.5136	9.9148	9.9992
Capital Value of Lease at today' worth (i.e., the amount that the time constrained property rights in the lease could potentially be sold for on the open market)	\$42,568	\$49,574	\$49,996

⁵ AE\$1 p.a. is the inverse of the Years Purchase (YP – also commonly known as the Present Value of \$1 p.a.)

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For this example, the complaint that the rent that the customary owners are receiving is below market is explained by the fact that premium represents about 80% of the effective market rental. In this way, at least initially, the customary owners are earning a package for their land leases that is a reasonable market return, even if rents are well below market levels. The fact that premiums are usually negotiated within a free and often informed market environment goes further towards substantiating the claim that overall returns to customary owners are not unreasonably low. This was supported empirically by Lal *et al.* (2001), who found that for the sugar industry in Fiji, total returns to customary owners were comparable to global land values for similarly productive sugar land.

Several problems complicate this apparently equitable outcome. The premium is paid as a single payment at the beginning of the lease to the representatives of the customary owners at that time. Since it has the effect of reducing the rent over the full life of the lease, it essentially draws income away from future generations of customary owners. To the extent that customary owned land should provide for the material needs of the customary owners at any particular time, the drawing forward, sometimes by many generations, of future land related income is an important instance of intergenerational inequity. In this case, the customary owners who take the \$200,000 today take 80% of the rent that is due to their children and their children's children. Discussions with indigenous owners and administrators indicates that is not due to any conscious malice against future generations but rather it is due to an ignorance of the underlying financial mechanisms, compounded by inappropriate initial rental valuations.

The payment of premiums creates a second and more complicated problem. In growing economies, the value land tends to appreciate faster than other prices, including the replacement value of improvements. Moreover, improvements tend to depreciate over time, in contrast to land component that appreciates. The tenant has title to the use of the land as personal property for the duration of the lease, with the future capital appreciation of the land being the reversionary interest of the landowner. However, the capital sums paid as premiums as long-term leases change hands tend to appreciate (particularly if the tenant is only paying a ground rent based on 6%, or less, of the hypothetical UCV). This is arguably reasonable, since the premium payment represents a financial quasi-equity interest in the land. That is, the premium can be viewed as financially equivalent to a partial sale of property rights in the land for a fixed period (i.e., the duration of the lease). This is a widespread phenomenon across the Pacific and causes several problems.

To understand this problem, it is necessary to review exactly what the premium represents in financial terms. As the above example demonstrates, the premium is a component of the total lease value of the land to the customary landowners, where they have permitted a partial alienation of their property rights for a fixed term of years whilst retaining the reversionary interest in the land. The premium can be expressed in terms of its equivalent annual rental. The Annual Equivalent (AE)

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formula is the inverse of Years Purchase (YP), i.e. the inverse of the Present Value of \$1 p.a. In the example in Tables 3 & 4 above, the market value of the property under a fifty-year lease was probably in the order of \$49, 574. However, in Table 3 the anticipated annual rental for the 50-year lease term was paid by way of a single rent up-front premium of \$200,000. This premium represents the annual equivalent rental of \$20,172 p.a., in contrast to the actual annual rental payment of \$5,000 p.a. paid to the customary owners. If the premium is defined as the capitalised value of *profit rent* over the life of the lease, it would indicate that the current market rent of the land is actually \$25,172 p.a. (i.e., \$5,000 ground rent plus \$20,172 profit rent).

As a tenant transfers (sells on the property rights in) their leasehold interests through the term of the lease, the value of the premium should reflect the same balance. However, the premium actually reflects the gaps between the remaining market rents and actual rents (the difference being the profit rent). Since, in general, the rents grow faster than prices; the premium will reflect this growth, even though the remaining term of the lease is diminishing. This is set out in Table 5, which considers the critical values at ten-year intervals assuming a property growth rate of 5% and a general inflation rate of 3%.

TABLE 5: REAL VALUE MODEL OF FUTURE RENTS AND PREMIUMS (50-YEAR LEASEHOLD MODEL)

Years into lease	Rental (with 5% p.a. growth)	Annual Equivalent Rental of Premium (with 5% p.a. growth)	Notional Premium (with 5% p.a. growth based on 10% discount (Cap) rate)	Real current value Rental (with 5% p.a. growth and 3% inflation)	Annual Equivalent Rental of Premium (with 5% p.a. growth and 3% inflation)	Notional Premium (with 5% p.a. growth based on 10% discount (Cap) rate and 3% inflation)
	Market prices			Real current values deflated by inflation		
0	\$5,000	\$20,172	\$200,000	\$5,000	\$20,172	\$200,000
10	\$8,144	\$32,858	\$321,318	\$6,060	\$24,449	\$239,091
20	\$13,266	\$53,522	\$504,546	\$7,345	\$29,634	\$279,355
30	\$21,610	\$87,182	\$742,225	\$8,903	\$35,918	\$305,787
40	\$35,200	\$142,009	\$872,587	\$10,791	\$43,534	\$267,497
50	\$57,337	\$231,318	\$ -	\$13,079	\$52,765	\$ -

In this example, the rent paid to the customary landowners grows by over 11 times in face value, or about 160% in real terms. However, the rental loss to the customary landowners also grows considerably in last decade. It is also approximately 160% larger per year. Meanwhile, the loss of rental to the customary landowners over the last decade of the lease alone is considerably more than \$400,000 in today's values. Importantly, in the context of future potential conflict, this is twice the value of the entire rent up-front earned by their forebears who took the premium in the first place (\$200,000). It is easy to see why this mechanism gives rise to conflict, dispute, and the motivation for sovereignty risk in the latter parts of long leases.

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The motivation for dispute due to premiums is not limited to the customary landowners. Table 5 presents the notional (or, perhaps, rational) premium that should be paid for to compensate the property rights relating to transfers at ten year intervals. It can be seen that the premiums rise at a greater rate than inflation for the first thirty years of the lease, then their growth falls below inflation for the second last decade before the premium disappearing altogether in the last decade. It is this phenomenon that explains why the ownership of a tenants interest (property rights) in the lease is considered to be a time constrained wasting asset. The psychological impact of this odd trajectory has produced problems in every market where it has been allowed to happen. It is not well explained by either economic or financial theory, as it appears to follow a path that is not entirely rational, though it does have logic.

If one considers a tenant purchasing a lease, say in year 0 of the above model (Table 5) and holding it for a generation, say thirty years, the experience of that tenant is that the payment of the premium was a good investment as it enabled the resale of the lease with a real capital gain. Given that tenants are people with families, that tenant could be expected to counsel his children regarding the wisdom of buying leases and the way that the premium is really an investment that will increase the tenant's wealth. Such 'wisdom' is predicated by the timing of entry into and exit from the lease arrangement. However, if the original tenants children buy leases in the market at the 30-year point, they will be buying leases with only a decade or two prior to expiration. Through this latter period, they will experience loss of their capital investment in the premium in real value terms.

Markets appear to be irrational in the pricing of premiums on long-term leases where the rents are below market. The prospect of impending loss that tends to be ignored until about the last decade of the lease is usually translated into political agitation. Usually it is presented in the form of pressure for either conversion of the lease to a freehold title, or the compulsory renewal of the leases on similar (inequitable) rental terms, but without an additional premium that would redress the inequity. Such a solution is clearly beneficial to the tenant and thus lacks equity for the landowners. This has happened in various parts of Australia, such as urban leaseholds in the Australian Capital Territory (Brennan, 1971), and on rural 99-year state leaseholds in Queensland (Small, in print). In New South Wales, the NSW government is currently offering expiring leases to tenants at 3% of their market value, being the financial value of the current rent to the state. Brennan, in particular, clearly showed the connection between sale of leases with a premium and the failure of state leasehold property over a period of about half a century.

The growth and eventual loss involved in premiums through the life of leases is more acute with 99-year leases. Since there are examples of such leases in the Pacific, the data has been analysed for this case as well (see Table 6). Several importance lessons can be seen from the comparison of 50- and 99-year leases. Firstly, the real growth of premiums extends through the first seventy years of the lease in the 99-year case,

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making the psychological effect of the last two decades even more severe (see Graph 1). Similar circumstances were experienced in the UK towards what was known colloquially as the *fag end* of 99-year Victorian building leases. Secondly, the contribution of the rentals of the last five decades makes negligible difference to the initial premium, but the loss of rental to the descendants of the customary landowners who took the premiums is very substantial. It is therefore likely that these descendants, who could easily be grand children or great grandchildren of the persons who benefited from the premiums, could be most unhappy with the situation.

TABLE 6: REAL VALUE MODEL OF FUTURE RENTS AND PREMIUMS (99-YEAR LEASEHOLD MODEL)

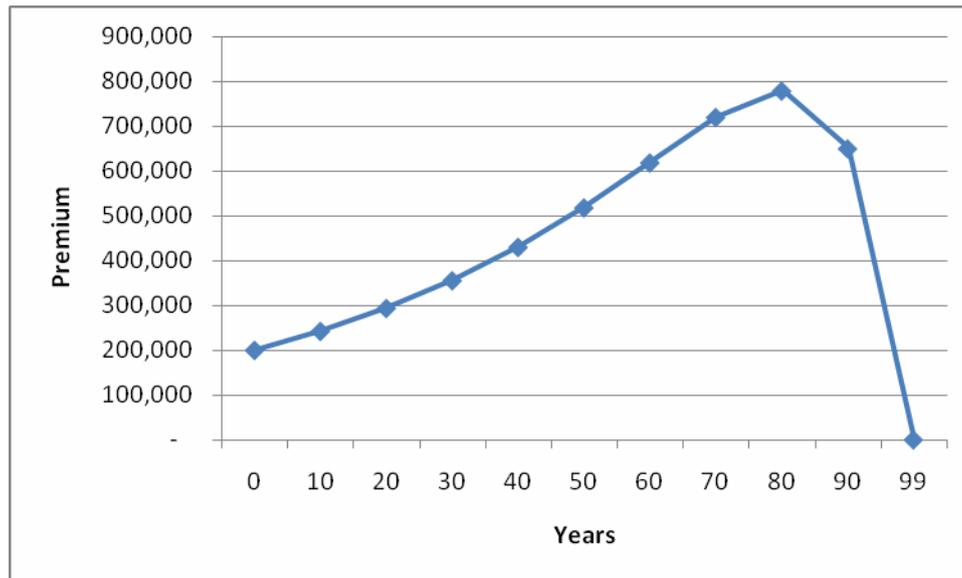
Years into lease	Rental (with 5% p.a. growth)	Annual Equivalent Rental of Premium (with 5% p.a. growth)	Notional Premium (with 5% p.a. growth based on 10% discount (Cap) rate)	Real current value Rental (with 5% p.a. growth and 3% inflation)	Annual Equivalent Rental of Premium (with 5% p.a. growth and 3% inflation)	Notional Premium (with 5% p.a. growth based on 10% discount (Cap) rate and 3% inflation)
	Market prices			Real current values deflated by inflation		
0	\$5,000	\$20,002	\$200,000	\$5,000	\$20,002	\$200,000
10	\$8,144	\$32,580	\$325,737	\$6,060	\$24,243	\$242,379
20	\$13,266	\$53,070	\$530,417	\$7,345	\$29,384	\$293,679
30	\$21,610	\$86,446	\$863,253	\$8,903	\$35,615	\$355,649
40	\$35,200	\$140,811	\$1,403,023	\$10,791	\$43,167	\$430,106
50	\$57,337	\$229,366	\$2,272,170	\$13,079	\$52,320	\$518,298
60	\$93,396	\$373,614	\$3,645,331	\$15,852	\$63,415	\$618,733
70	\$152,132	\$608,577	\$5,702,127	\$19,214	\$76,862	\$720,164
80	\$247,807	\$991,308	\$8,292,212	\$23,288	\$93,160	\$779,278
90	\$403,652	\$1,614,736	\$9,299,304	\$28,226	\$112,915	\$650,280
99	\$626,196	\$2,504,986	\$ -	\$33,560	\$134,252	\$ -

Likewise, tenants who hold the leases in the last two decades of a 99-year term could be expected to be strongly politically motivated to press for lease renewals without new premiums, as they would be the first generation of tenants for whom the premium was not a growth investment, but rather a major cost. Ironically, the loss these latter tenants would suffer if the leases were duly terminated upon expiry (according to their legal nature), would be largely the reversal of the profits that their forebears had made over the period of the foregoing decades. That is, the capital gains made by intermediate tenants would eventually be paid for out of the loss of the tenants holding the lease in the last decade or two. In circumstances where tenants come predominantly from one ethnic group and landowners another (such as the case in Fiji), this means that for both groups the costs incurred near the ends of

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the leases are the results of unwitting actions of their own ancestors. The financial reality of leases, with different benefits to different parties at different times during the currency of the lease, are not as a result of opposing ethnic groupings as is often popularised by the media and political agitators.

GRAPH 1: THE REAL VALUE OF PREMIUMS OVER TIME (99-YEAR LEASEHOLD MODEL)



In many parts of the Pacific, premiums are illegal under formal institutional arrangements, despite being common to the point of being almost universal. As informal payments, they are not systematically recorded and there does not appear to be adequate research into their magnitude or policy directions to mitigate their adverse affects.

In summary, the practice of charging premiums, whether formal or informal, does the following:

- > Creates intergenerational inequity if the lease duration extends beyond one generation;
- > Creates the financial equivalent of sale of part of the customary interest (a partial time constrained alienation of subsidiary property rights);
- > Inclines future political action by tenants for the perpetuation of the privilege; and
- > Produces intergenerational inequity within the tenant community, with evidence of financial gains in the early part of the lease and loss in the latter years.

The Changing Role of Land

Land has had many levels of significance in traditional life in the Pacific. Apart from its importance in the social, symbolic, and spiritual realms, it has always offered the practical aspect of providing the basis for material welfare. At the material level,

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traditional society operates on a complex system of exchanges that ultimately conform to a notion of distributive justice. This means that in traditional society goods and services exchange in such a way that individuals are materially supported in a way the community considers just. Usually, this includes actions that balance human input, tribal status, and life situation using principles that have origins in custom and customary law.

Within the broader social regime, property is a minor component and property rights do not provide the dominant organising principles in intra-clan relationships. Property in land is considered inalienable from the clan and allocations to individuals are only expressions of deeper customs expressed as temporary rights, matched with substantial complementary obligations.

The status of property as an organising principle for action is reversed in relation to other social principles within western economic relationships. Contemporary western property rights are only intelligible in terms of powers to demand a return from productive land use in opposition to other persons engaged in, or affected by, the productive activity. It does not include any sense of social obligation to those stakeholders as human persons. By contrast, notions of fair play and equity continue to be more dominant in the Pacific. The financial efficiency of customary land use is intimately linked to this fundamental social reality, as contemporary western property is only considered financially efficient when the needs of non-owner parties are ignored and sometimes exploited.

This is not to say that there is no merit in contemporary western property rights systems. They have been effective in promoting highest and best use of land over the half-millennia that it has dominated western culture. Along with highest and best use, it has fostered technological advances and the personal discipline of all participants towards maximum material efficiency. These have contributed in no small measure to the technological and economic leadership of the west at this time in history. Customary people now need similar benefits, and effective financial management will only be realised within these parameters. The unique contribution of indigenous cultures, however will be to circumscribe effective financial management within a wider framework of social principles that respect the dignity of human persons in a manner that is consistent with traditional beliefs regarding one's obligations towards others.

In order to understand the structure of western property rights better, they can be considered to be designed with the following goals in mind:

- > Private property affords the holder with a set of explicit rights that are ordered towards facilitating the use of the property in some way. In contemporary western economies, these uses are dominated by material outcomes that can be evaluated using financial/economic indicators;
- > The rights of private property must be explicit;

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- > The rights of private property must be fixed and certain over time with agreed procedures for change;
- > The term of the rights must be explicit, and where they terminate the method of reversion and the distribution of component values should be explicit;
- > Property should be capable of dissection through the transaction of component property rights, or purchase and consolidation;
- > Property rights should be secure and this usually means their protection and underwriting by the state in a modern economy; and
- > The economic benefits of private management should flow to the property holder in a fixed and certain way as a reward for effective management. However, this does not mean that a part of the economic benefit is not due to other parties engaged in the productive activity or the community in general.

This definition of property rights is consistent with that found in most contemporary western economies, especially those developed from English origins. Historically they were articulated in the eighteenth century through the legal, economic, and moral investigations of key English thinkers, especially Sir William Blackstone (1769 / 1966 reprint) and Adam Smith (1776 / 1976 reprint). The articulation of what property means is a key component in understanding the wide question of the appropriate distribution between the property owner (landowners) and other interested parties.

Distribution

In the Pacific, this role has been taken in the past through traditional laws and customs that have been adopted from antiquity. These laws and customs operate at the moral or ethical level, and underline the practical reality that economic or financial management of property rights are ethical issues. Many commentators have recognised that the practical outcome of the property rights regimes of many non-western cultures have been ordered through tradition towards equity across the community and between the present and the future.

This question of equity has two dimensions - equity across current persons (*intra*-generational equity), and over time (*inter*-generational equity). For customary land to be effectively managed in the Pacific, it must deliver reasonable equity in both of these.

Four broad groups have interests in the outcome of the productive use of property. These are the

- > Customary landowners;
- > Workers who apply labour to the property as tenants or employees;

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- > Purchasers / consumers of the products that are produced using the property; and
- > Community in general, including the state.

To these four can be added a fifth possible group, being the people of the future, and these in turn can be considered to be made up of future members of the four present groups, thereby doubling the possible interest groups to eight. The following discussion will focus primarily on the current interest holders, though some consideration of their fortunes into the future will also be necessary.

In traditional customary land uses, there were heavy overlaps between these stakeholders. In contrast, in contemporary western economies they are usually considered quite separate. Contemporary western economic theory assumes that these parties are separate and have equal economic power in the market. From this assumption, it is argued that the market has the capacity to provide the optimum distribution of benefits of productive use. The evidence of this outcome in the west is highly equivocal and many commentators relate this practical problem to the unreality of the assumptions. Within contemporary western economic theory, it is difficult to challenge the assumptions simply because they form the premises of the discipline itself. The resolution of the question necessarily comes from a perspective capable of operating beyond the confines of economics itself. Put simply, if one assumes no imbalances in economic negotiating power it becomes impossible to analyse the effects of imbalances in economic negotiating power.

In order to deal with the reality of negotiating power imbalances within economic systems, one must look to social and political systems, as well as the cultural understandings and customs that a community adopts to mitigate possible inequalities that follow from them.

Urban areas contain the oldest and most numerous instances of private occupation of land. In many Pacific countries, it is in the urban areas that the majority of freehold and leasehold land, if any, exists. Generally, freehold is exempt from consideration of effective financial management from a customary property point of view, though the case of Jackson's Airport in PNG and the dissolution of freehold title in other countries, show that customary interests can persist even through freehold alienation.

The urban land in PICs that is not state owned or freehold is predominantly held as customary leasehold, either directly or through trust systems. Leases of customary lands in urban centres is different in practice from rural leaseholds, as there is little likelihood that the customary people will ever regain practical occupation of the lands and improvements thereon, except through repurchase of the leasehold interest. This is despite the notional termination of the lease, as a time constrained interest. The proposed *Abi* development in Lae City is an exception to this tendency, where

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the customary owners intend maintaining a close landowner interest in their land through entrepreneurial development and leasing to others.

Maintaining the Real Value of the Customary Owned Interest in Land

In general, the major problem with urban leasing of customary land is the maintenance of the real value of the customary interest in the property rights. The practice of selling leasehold interests using a premium up-front price in addition to the annual rental creates an initial capital interest for the lessee. Over time, this capital interest tends to appreciate while the rents paid to customary landowners tends to grow at a lower rate. This means that the financial benefit returning to the customary landowners tends to depreciate over time in real terms.

This problem with leasehold title is also experienced in other countries where customary ownership is not present in significant amounts, but where there is significant state leasehold land available. State leasehold in countries like Australia has several similarities to customary leasehold. Both have landowners who are considered well separated from the actual use of the property; both are for long lease terms; and in both cases there is usually a dearth of comparable sales available to provide an adequate basis for comparative valuation at transaction or rent review. In NSW Australia, the government has realised that the rents collected on its state leasehold land only capture 3% of the true land rental. This means that the state has effectively lost 97% of the value of the interest (property rights) that legally belongs to it. Similar loss of effective financial interest appears to have occurred in many parts of the Pacific. In Australia, the loss has been accepted by the government and the political situation actually promotes it. By contrast, there does not appear to be any conscious intention on the part of customary people to surrender (or minimise) their financial interest in their land - there are many indications that similar losses are occurring.

The transfer of effective financial interest from customary landowners to tenants, especially when it is combined with political pressure to become a virtually perpetual interest, is the financial equivalent of a sale. Whilst customary owners are understandably highly resistant to selling the superior title in their land (and statutorily precluded from doing so by Constitution), the financial reality is sometimes equivalent to a sale. This does not enhance the effective financial or economic use of land, as can be seen where it simply fosters subsidiary leasing with head lessees taking profit rents at the expense of customary landowners. When these situations are transferred to new head lessees, the premium reflects the anticipated profit rents, which enables the outgoing head lessee to take a capital gain. This leaves the incoming head lessee financially committed to maintaining or extending the extent of the profit rents.

The efficient economic use of land is not enhanced by these aberrations in rental, as the final productive user of the land is usually subject to the full market value of the land. This is balanced between rental to customary landowners, purchase premium,

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or sub-rental from a superior leaseholder. Hence, the regularisation of rents to customary owners would not affect the physical use of land; rather, it would redistribute incomes from the use of land back to the legal landowners.

Urban lands, with the exception of those that remain customary, are generally taxed through local level government rates on unimproved value to provide for infrastructure and services. These rates can be thought of as a participation in the land rental. While it may be argued that the customary owners have the right to the entire rental value of their land, the logic behind local government rates argues that local level infrastructure and services actually contribute to land values. Hence, rates are in fact an appropriation by the local level government of what its action has produced.

The ownership of improvements is an important consideration for long leasehold interests in land. Effective financial management requires that appropriate improvements be made to the land to realise its highest and best use. This requires capital expenditure and tenants usually undertake the development. The investment of capital in spatially fixed locations requires that a developers property rights are adequate to realise an appropriate return with security for a period of time that is sufficient to make the venture adequately profitable. Improvements to real property tend to have working lives measured in decades, which makes it necessary for the lease term to match these. This is generally the case, with lease terms between twenty-five and ninety-nine years being common. However, as has been demonstrated, there are significant intergenerational benefits by keeping development lease terms to a maximum of 25-30 years, where possible.

ENSURING MARKET BASED RETURN ON LAND

The UCV method of rental determination does not ensure a market based return on land. Pacific countries do exhibit secondary rental markets of sufficient quality to enable direct market based valuation of ground rentals, if the data was made available and analysed appropriately. Such methods are less direct than the current UCV method, but they are more robust.

The faults in ground rent determination are currently creating unearned profits from tenant land use in several circumstances. These anomalies could be controlled by attention to the profitability through the productive supply chain, originating from the use of customary owned land. In this way, the return to land could be based on the adequate market performance of tenant businesses.

There is evidence that the government does take income from productive use of customary owned lands through various royalties, excises and export taxes. These should be considered when computing effective market performance of tenant businesses.

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INTER AND INTRA GENERATIONAL RETURNS

The matter of premiums have already been addressed in this report as a major source of intergenerational and intra-generational inequity. There are several other ways that current and recent practices regarding customary land are responsible for intergenerational and intra generational inequity. These include:

- > The UCV method of land valuation, which tends to reduce the effective financial interest of the customary owners;
- > Internal indigenous migrants are finding themselves landless tenants, often in peri-urban settlements. They also include educated people who take up urban jobs. As economic and other pressures increase over time, this group will increase and will become a substantial disenfranchised part of the community; and
- > Non-indigenous citizens, and their children, are placed in a difficult position due to being excluded from landownership.

Landownership has been recognised as a major method of ensuring intergenerational equity. For people who do not enjoy property rights, other mechanisms are necessary to ensure their equitable participation in the financial performance of the country.

EFFECTIVE DISPUTE MINIMISATION AND RESOLUTION

There are several measures and questions that PICs could consider in order to minimise the risk of land related disputes. These include:

- > Specialised land courts. These should be as informal as possible to provide fast and inexpensive access. They are discussed below. Their contribution to dispute resolution is through providing accessible independent review;
- > Transparent rental property registers that record all details of all lease transfers. This would include analysis of the secondary rental market, premiums paid and, ideally, professional estimates of the value of improvements;
- > More precise recording of customary ownership rights. Ideally, this would consist of a customary ownership cadastre with a precise spatial foundation. A GIS platform would be preferable;
- > A review of the financial distribution landowner related benefits within customary society may be appropriate. A revised understanding of the link between income and obligations for leaders of traditional communities appears timely.
- > Consideration of how to deal with internal migrants in terms of their relationship with land is needed. What rights do indigenous people have when they leave their villages? What support should the country afford these people, especially when they migrate for the benefit of their families? What is the meaning of tenancy when these people find themselves as landless inhabitants of peri-urban

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settlements? What of people who leave their villages to take up public offices in cities, or other roles that serve the broader community?

- > At what point does rent constitute exploitation of tenants, and to what extent should productive tenants be rewarded for their effort in strengthening the country's economy?

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KEY STRATEGIES

This section provides potential strategies that could be used or adapted to enhance the financial management of customary and other land in the region.

TRANSPARENT LAND INFORMATION SYSTEMS

Brotoisworo's (2003) recommendation for a system of land dealing registers for Kiribati is a strategy that could be generalised for most PICs. Currently, land dealings are in general poorly managed, and some critical data is simply not collected. Computer based transaction data bases should be considered as a high priority. Considering the many similarities across the Pacific regarding the need for a register of land rentals, there is potential to develop a common basic land management software for the administration of customary and other land. This could then be adjusted, as appropriate, for specific countries. Such an approach could be cheaper and provide maintenance efficiencies. The disadvantage of this approach is that local differences and practices may negate any savings potential and make it more cumbersome to attempt a common solution.

The type of data to be collected needs review. In particular, because rents are payable for time constrained property rights as the critical valuation foundation for the Pacific, all leases should be registered and their on transfer should be centrally recorded. If transparency is to be achieved, critical lease terms should be on the public record. These would include rents, rent review provisions, and rental changes over time. The details of compensation provisions for undepreciated improvements should be recorded, and if possible reduced to a minimal number of standard options and associated lease covenants. Finally, the payments of premiums (both key money and profit rent) should be recognised as part of the near universal practice in the Pacific, and these payments should be recorded at each successive transfer.

Cadastral registers already exist across the Pacific, but are often incomplete, poorly integrated, or inadequately maintained. Land Information Systems require adequate resources to maintain data precision and frequent update to be effective, or they rapidly lose credibility. On the other hand, well maintained systems return considerable economic benefits. The benefit/cost ratio is strongly positive, but has not been adequately realised in the Pacific.

TRUSTS AND INCORPORATED LAND GROUPS

The challenge in the Pacific is to provide channels for customary owned land to be made available for optimum financial benefit without compromising traditional values. To be financially effective, access to land must have certainty. Tenants must have an explicit and low risk access to productive land for the land in order to maximise the value of the underlying asset. This means that leases must be available that are perceived as reliable and free from the possibility of default through sovereignty risk. Currently this is achieved through state intermediaries. These

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provide consistency and certainty that is in no small way responsible for the level of rentals currently available. The challenge is to further refine the workings of these intermediaries.

The NLTB in Fiji provides good quality technical support and in this respect is a model that has considerable merit. Its relative inefficiency has been the focus of considerable criticism. In circumstances where only 15% of a modest residential or UCV based rural rental is collected, as a manager the costs to administer customary land potentially outweigh the management income. Likewise, payments to chiefly hierarchies make it understandable that the other parties to the matter, tenants and villagers, are both critical of the impacts of its operation.

The delegation principle of subsidiarity, that matters should be handled by the smallest competent authority, suggests that local land trust groups are preferable (Schumacher, 1973). Despite this, small and local groups often lack the practical ability and skill to manage land effectively. The Māori trusts appear to offer the best example of effective land administration in the Pacific. Their focus is on effective management by indigenous leaders for the indigenous community within an ethic of equity. Their critics appear to be largely comprised of tenants who have been in the habit of paying considerably below equitable rents. Their technical failings, such as poor investment choices, are instructive for future avoidance. However, they do not constitute adequate grounds for their rejection.

New and emerging initiatives, such as the PNG incorporated land groups have the advantage that they are more likely to be managed by traditional local authorities, in the Māori style. The *Abi* initiative in Lae City offers a positive example for replication. This approach encourages local clans to invest in educating their leaders. In many cases, it will be necessary for local leaders to rely on independent advisors, either from the government or private practice, and those costs should be factored into the costs of administration of customary owned land

PACIFIC VALUATION METHODOLOGY AND VALUATION APPLICATION

The UCV method of valuation for rental determination is widely accepted in the Pacific, but it is highly inappropriate. It is the cause of many of the practical problems in the effective financial management of both customary owned and other (especially state) land in the Pacific. Other methods exist, and they should be explored for effectiveness of application to replace the existing method. Two general methods merit further consideration by PICs, as follows:

- > *Market derived ground rents* - This method may be more applicable in urban areas where a secondary rental market exists. It consists of analysing the rentals of leases in the secondary markets and stripping back the contribution of improvements. This method has been adopted in this report to estimate the distribution of ground rents. If this method was further developed and applied widely, it could be used to evolve an understanding of general levels of ground

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rents across submarkets. This would provide consistency and equity for ground rents paid to customary landowners or the state.

- > *Residual method* - This method has strong theoretical and practical support. It is consistent with the economic nature of land rents. It recognises the fact that in an efficient market land rent is the residual that remains from the income from land use once the non-land costs of production are removed. Since the non-land costs of production tend to have quantifiable market derived values, they can be evaluated with reasonable precision. This method would suit more complex properties where a secondary market might be too thin to be useful. It would suit many non-urban land uses. Profit participation clauses in leases are a primitive form of financial recognition of the mechanics embodied in the residual method. Already there are instances of profit sharing arrangements with customary landowners in the Pacific, such as the Guadalcanal Plains palm oil initiative and the turnover based NLTB tourism leases. It is also a common feature of western rental environments, such as retail leases within shopping centres where tenants pay a percentage of turnover to the centre owners in addition to a base rent.

Equity will also be enhanced by frequent rental reviews. Parties to a lease must recognise that it is possible for land values and rents to move both up and down, depending of unfolding circumstances.

As mentioned above, rental valuation needs to recognise the contribution of premiums paid to acquire leases (either for the overbid known as key money, or compensation for the increasing value of the tenants interest known as profit rent).

Where leases include the expectation that property rights in improvements made by the tenant will become the landowner's property on lease expiry, these leases should be limited in term to no more than one generation, ideally 25-30 years maximum. This is necessary to avoid the roll up of the transfer premium that has created problems in all situations in which it has been tried.

LAND USE PLANNING

Efficient and equitable financial management of customary owned land requires rental valuation to be sensitive to both the permitted and probable land use. This implies that land use should be controlled or registered in some way. This does not necessarily require advance planning control of permitted land use. It might merely take the form of specifying the permitted land use at the time leases are created and including this land use in the lease register as one of the limitations of the lease. In this way, ground rents could be related to land use rather than the inaccurate assumption the land is undeveloped (i.e., unimproved) and its use will be similar to the existing.

At a future time, some PICs may want to move to pre-emptive land use planning, but this is not required for efficient financial management.

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LAND COURTS OR TRIBUNALS

The establishment of independent land courts to review rental determinations as well as other matters related to land is highly recommended. These may have property specialists, or traditional leaders, as commissioners rather than purely legal trained judges. Training programmes to educate trained independent mediators will support this approach by offering an initial Alternat Dispute Resolution avenue for disputants.

Valuation practice has always been tested in courts, and the introduction of novel methods of rental determination will require mechanisms for review to ensure equity. It might be found, for example, that tenant hardship provides a valid ground for a downward rental review. This is already done implicitly in Fiji where ALTA rents have been arbitrarily set below the statutory level due to the belief that the higher level would create undue hardship. This unofficial practice is consistent with the theory of land rent, but it is not a formally recognised practice. This potentially leaves trustees open to litigation by landowners. A transparent review process, such as land court or tribunal would recognise this need.

ELIMINATE PREMIUMS ON LEASE TRANSFER

The practice of selling leases at (or with) a premium is flawed and should be abolished where possible or controlled. It flows from a misunderstanding of the contribution of premiums as a component of rent. It potentially creates an extra-legal interest that behaves financially like freehold ownership. As such it is offensive to customary culture. It complicates effective rental determination. It complicates and probably is an underlying cause of land related disputes, especially towards the end of longer leases.

There are financially valid and equitable strategies for the amortisation of these premiums (Small, in print). It is recommended that the premiums be amortised over a reasonable period, ideally a generation, in line with the depreciation of comparable personal property (say buildings). Whilst legalising premiums might be a first step towards their control, removing them will rely on the development of effective direct methods of valuing ground rents.

RESTITUTION

There are ongoing and outstanding claims in many PICs over the return of land acquired by the state, or alienated to private individuals, under colonial administration. Society will not move past misdeeds until restitution of the superior has been resolved, and action is required to ensure security of subsequent land dealings. There is a role for post-independence land courts and land tribunals to formalise the property rights of the respective stakeholders.

The Johnson's Airport example in PNG is representative of the underlying rejection of land sale by customary owners. It has been shown that sale price, or

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compensation value, can be thought of as a single upfront payment that is the financial equivalent of all future rentals. It has also been shown that due to the effect of discounting on rentals in the distant future, the sale price of land does not adequately embody the real value of those future income streams.

This means that regardless of how much a present generation is paid for the alienation of land (statutory or otherwise), it will never adequately compensate for the losses of all future generations. The one possible exception to this financial reality is the case where current recipients of compensation for the sale of land are able to invest their compensation in an alternative investment that has the same profile of risk, growth and return and the original land. This is very difficult, despite the apparent Māori successes.

On the other hand, and also consistent with finance theory, if the sale value of land is equal to the present value of all future rents, then governments should be open to renting, rather than buying, customary land for public purposes. So long as the terms of the lease are respected, governments could lease land for roads, infrastructure, and other public needs, from customary owners. This would have several advantages, including the following:

- > Future generations of public users of the land would contribute to the compensation of the customary owners;
- > The present generation of government would not have to borrow or use other funds to acquire land for public purposes;
- > Government debt could be reduced;
- > Changes in needs could be more flexibly dealt with, such as the realignment of roads or the discontinuance of other infrastructure;
- > Future generations of customary owners would receive reasonable rents in perpetuity thereby eliminating future conflict; and
- > Traditional values would not be violated.

There is currently a trend in modern western countries for governments to lease private property for government, public, and infrastructure purposes. In Australia, government offices are increasingly located in leased commercial space. Likewise, private companies are now owning roads and infrastructure under public private partnership (PPP) arrangements, again relieving the government of the ownership. In this way, the tendency for PICs to still require government and public facilities to sit on government owned land is actually moving against trends in the west.

Such an approach will minimise subsequent demands for restitution, and moving to a lease model for public lands might be a more satisfactory strategy for the Pacific. It is consistent with the general removal of freehold in, amongst others, Vanuatu, Niue and the Solomon Islands. It also eliminates the possible present financial burden for

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governments who may recognise the validity of restitution claims over state land but do not have the financial capacity to satisfy them.

FINDING LEASEHOLD SOLUTIONS

This lengthy section provides additional context to leasehold based solutions. It demonstrates limitations of current lease structures in the Pacific (Boydell, 2007b) and draws on useful leasehold reform lessons from the UK, where 99-year development leases established in the Victorian era have experienced a full leasehold life-cycle.

The simple dictionary definition of a lease is a “contract by which one party conveys land, property, services etc. to another for a specified time, usually in return for a periodic payment” (Pearsall, 1998). A lease is a proprietary interest in land that provides property rights to temporarily pass on to another party for a term of years absolute (i.e., a fixed term estate) in the land/property in return for equitable rental payment. The purpose of leases is to create an opportunity for those who hold a ‘superior’ interest in land to provide access to land for those who have the capacity to make it economically productive. The equitable rent is, taking the Ricardian model, the surplus of productivity from the land having taken out the costs of production and labour on the part of the tenant.

The opportunity to liberate access to land for a term of years absolute to enable economic production through leasehold structures that retain the superior property rights in the custom ‘owners’ is the accepted solution in the Pacific. Leasehold structures are located between the extremes of the unacceptable ‘do nothing’ and ‘privatisation’ models. Leasehold models are, of course, already in place in the Pacific, ranging from 20+20 year residential leases, 30+30 tourism leases, and other variations for 50, 75 and 99-year terms.

In order to avoid, or significantly minimise the risk of, future conflict it is essential to manage the adoption and implementation of the fixed term leasehold estates very carefully. At the outset, it has to be stated that the term of year’s absolute approach is not without its limitations, problems and challenges. It is important to recognise and learn from the lessons experienced in managing leasehold interests in other countries where they have been applied in various ways for far longer.

In the UK, where 30% of household tenure is leasehold (and most commercial) there is increasing ‘disenchantment with fixed-term leasehold estate as a medium of residential ownership’ (Gray and Gray, 2005, p.458). It is argued that the leasehold system, having its roots in the feudal system has benefited the residential landlord, whilst leaving the tenant with a wasting asset. In response, the government has approved the Commonhold and Leasehold Reform Act (2002) to enable owners of flats/units in apartments to own a perpetual interest. This follows 35 years of ongoing residential leasehold reform legislation dealing with the expiry of 99-year

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Victorian leases (from 1967 Leasehold Reform Act). As mentioned above, relevant learning outcomes from these examples are incorporated in the strategies below.

In the Pacific, there remain differences of public perception between leaseholds offered on government or freehold land, compared to those offered on customary land. This is a curious anomaly, given that it is the role of the State to guarantee all formalised property rights over registered or recorded land. This anomaly is compounded, in part, by the adoption of a regulated rental basis that is grounded on the hypothetical construct of unimproved capital value (UCV). In contrast, Samoa has no statutory provisions governing how the rental for a lease of customary land is to be calculated (refer to Samoa country case study).

A criticism of the UCV approach from a landowner or landlords perspective is that the resultant regulated rentals do not keep pace with the increasing value of land over time, despite inbuilt review clauses. A solution to this is to move towards a valuation model that reflects an equitable share of the improved market value returns to the landowner, either at the end of the lease, or during the currency of the lease. However, we cannot integrate this solution without first providing background to a range of related leasehold issues.

It is one thing to generate leases to liberate access and related fixed term use rights to others, but it is critical to think ahead about future issues that will affect the lease, use and rights of the parties, such as:

- > *Default* – under what circumstances can the trustee or landowner reclaim the land and any improvements thereon in the event of non-payment of rent or other charge on the property? [Note: there are cultural and value issues surrounding the repossession of customary land. Certain of the banks have also identified these cultural issues as impediments to lending on any title over customary land. Lending institutions see the risk of negative media attention associated with dealing with repossession over customary land as outweighing their financial gains in providing lending for this class of ownership.]
- > *Death* – what provisions are in place for the passing of the tenant? Will the lease convey to their spouse (who is often not named as a joint-tenant or tenant-in-common) and / or their children? The circumstances surrounding the death of a landowner are not usually an issue, as long as the leasehold arrangement is formalised with a trustee, the land is registered or recorded in some way, and the arrangement is backed by the State. This highlights the potential risks experienced in informal lease or informal tenancy arrangements.
- > *Expiry* – this is a major issue and one that has already caused major conflict (e.g., the recent expiration of sugar cane leases in Fiji). However, the cane lease example is small scale compared to the impending expiration of residential leases in urbanised areas of Fiji. Whilst it has been accepted practice for the government or NLTB to negotiate an extension (arguably a surrender and renewal) of leases in

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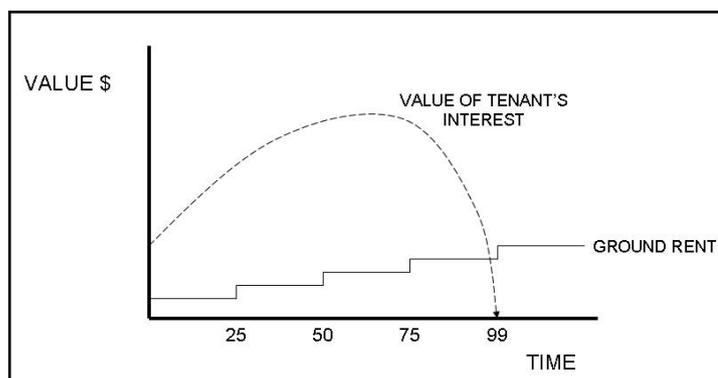
the latter part of their term, there is a major uncertainty about the ownership of tenants improvements on expiration (see 'Improvements' below). Hitherto, the only benefit in granting an extension of the lease term is to ensure a continuation of tenancy at a renewed ground rent (albeit at 3-6% of UCV). However, given the ownership of any improvements on the land being vested in the tenant, a legal challenge is impending over what rental should be charged on lease renewal [given that the landlord (e.g., NLTB as the trustee) could demand that the land be returned in the condition that it was in at lease commencement]. There is obviously a need to find an equitable legal compromise before expiration.

- > *Improvements* – the concept of improvements to land is a Western law concept and may not apply to customary land or may apply but not in the way in which it is applied to Western property. Given the extensive experience of lease expiration in England, the issue of improvements was specifically investigated in two of the country case studies (Samoa and Fiji). The issue surrounds a level of ambiguity evidenced in leases for land for both residential and tourism purposes, and how leases have arguably adopted more of an Australian rather than English approach in managing improvements.

By way of background, as English towns and cities grew during the 18th and 19th century, landowners optimised the financial gains from letting land to builders rather than less profitable farming tenants (George, 1992). These were 'building' leases, with premiums paid at lease commencement and thereafter a low or nominal ground rent (similar to the ½-6% of UCV variously applied in Pacific Island Countries).

Where they differed from the current Pacific examples is that builders developed the land, and then sold the land and buildings by way of a sublease (at a premium) for the unexpired term of the lease (commonly 97-95 years). However, the leases were clear that the approved improvements were to be returned to the landlord in good and tenanted repair at lease expiry. Details of the approved 'tenants improvements' undertaken by the builder, along with a comprehensive building plan, were included with the lease documentation.

FIGURE 1: LEASEHOLD INTERESTS AS A WASTING ASSET



Obviously, with the granting of a 99-year lease, there is little concern in the early years of tenancy regarding the 'wasting asset' nature of a term of years absolute (see Figure 1). As was demonstrated earlier in the report (see Table 6), given the time-

preference of money, in valuation terms there is not a significant difference in the

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right to receive rental for 99 years or for perpetuity. This is not the case as the lease progresses, and particularly in the last 25-30 years of the term, when it becomes difficult to secure mortgage funding [with no lender prepared to lend beyond the expiration of a terminating lease]. The large numbers of these building leases that were due expire in the 1970s-1990s was in no small part a factor in the degeneration of inner urban areas England at that time. Given the uncertainty of lease renewal and the declining value of the tenants interest in the wasting asset, there was no incentive to maintain or inject capital into the improvements.

Politically a range of issues emanate out of the UK example, with tenants seen as victims and local governments faced with urban decay attributable to the leasehold regime. The response, in a country where the dominant tenure is freehold, was to enact legislation to allow enfranchisement enabling tenants to acquire the freehold interest through a formula based payment that compensated the landlord for improvements with a discount based on length of occupancy (to avoid speculation), or obtain an extension of the lease on 'fair' market based terms. Obviously, unlike the Pacific, it was easier to determine market value in England in circumstances where 70% of the comparable evidence was freehold title. This example highlights an untenable outcome in the present political climate of the Pacific where the continuance of customary land as the superior interest is inviolable. The solutions detailed below recognise that circumstance.

The Pacific needs to learn from the lesson that it took the UK some 35 years to reconcile the challenge of leasehold ownership that commenced with the granting of 99-year leases a century ago, and the solution (enfranchisement of freehold interest) is inappropriate to the continued customary ownership of land.

Of major relevance to the Pacific is that the English building lease model was clear on the issue of improvements – they belonged to the landowner on lease expiry and were to be returned in good and tenantable repair as compensation for the land having been tied up at a low / nominal rent for 99 years. This ensured some intergenerational equity for the landowners (albeit that in many examples the landowner comprised the 'city fathers' and so there were political implications to reconcile at the level of local government).

For the purposes of this report, two types of lease in the Pacific are investigated: Residential and Tourism, as both of these are the inevitable causes of future conflict unless intervening action and education can be made in the short term. As the Fiji country case study highlights, the residential leases in Fiji fail to address the question of who owns the property rights in the improvements on lease expiry.

The commonly adopted wording in these leases is that any improvement erected by the lessee (tenant) on the land shall be removed within three months of the expiry of the lease. There is a provision for the lessee (landlord) to purchase the improvement (building) upon payment of fair value to the lessee. These clearly defined property rights (separating land as the landlords interest and the building as a tenants interest)

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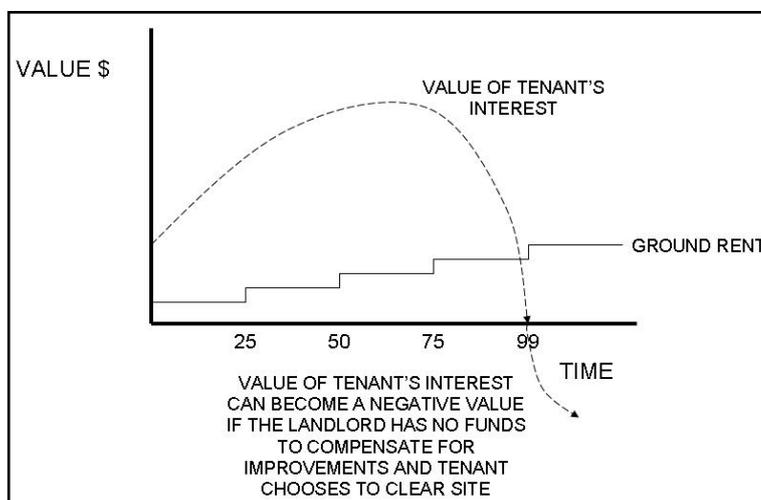
will lead to inevitable confusion and uncertainty as the term of years absolute expires. This is quite different to the English example, where the lease clearly places the onus on the tenant to return the property to the landlord at lease expiry.

What is the solution? Take the example of the 18,000 (approx.) residential leases granted by the Native Land Trust Board over customary land in predominantly urbanised areas of Fiji. The general perception of landowners (as opposed to their actual legal situation) is that they have received a very small rent whilst their land has been tied up for 60 plus years, and that the improvements will be their residual compensation. Their economic situation has not improved in line with the significant increase in value of the developed land in which they hold the superior interest. To date, as mentioned above, where a residential tenant has approached the NLTB for a lease extension, it has usually been granted without regard to any value in the improvements. This approach benefits tenants at the expense of the customary landowners.

However, as witnessed by the reaction to the expiry of cane leases, the landowners may assert their authority to take back possession of the land on expiration of residential leases. In Fiji, landowners are also aware that in 2000 the then Chaudhry Government took the unprecedented step of compensating agricultural tenants with the sum of \$28,000 on lease expiry to allow them to find alternative land and work. Following through the residential scenario, it is within the property rights of the landowners to retake ownership of their land on lease expiry. This results in one of two options:

- > The outgoing tenant has to clear all improvements off the land (and thus pay the expense of demolition and remediation) making the value of the improvements effectively a negative in the final days of the lease (see Figure 2);

FIGURE 2: TENANT'S INTEREST BECOMES NEGATIVE AT LEASE EXPIRY



- > The landowners have to compensate the tenant for the value of the improvements, and then they hypothetically have the opportunity to relet the land and improvements (as a single interest) at

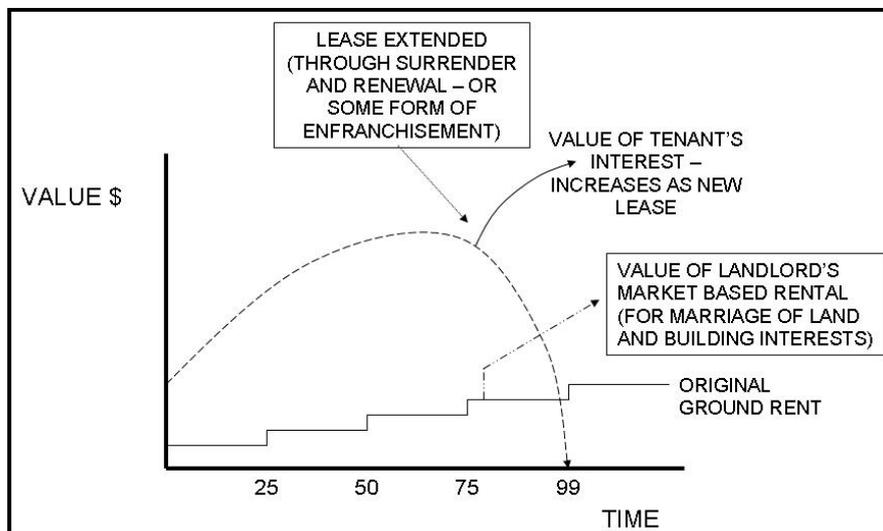
market rent. This assumes that the landlord (NLTB as trustee or the landowners

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themselves) has the money available to compensate the outgoing tenant for the improvements. Given there have been no ‘sinking fund’ provisions made to accumulate capital for this circumstance, which is understandable, as the ground rent model (up to 6% of UCV) bears no relationship to the market value of the land and improvements, no capital is in place to achieve this. If there is no capital available does this force the landlord (or trustee) to grant a lease renewal / extension? Not necessarily, as they can request that the site be cleared and remediated – a circumstance where all parties appear to lose. If the NLTB did have capital to compensate the existing tenant for improvements on expiry, there are further complications for what would follow. As far as granting a new lease is concerned, currently there is legislation in place for a short term tenancy arrangement, but not for a long lease with either a sale of lease (with improvements) with payment up-front, or a regularly reviewed residential tenancy to market rent.

The residential lease expiry solution is to ‘marry’ the interests of the landlord (land) and the tenant (improvements) to allow continued economic use of the land (Figure 3).

FIGURE 3: MARRIAGE VALUE OF LANDLORD AND TENANT'S INTEREST ON LEASE EXPIRY (ASSUMING CONTINUED TENANT OCCUPATION AND NO COMPENSATION)



This model reduces the risk of leasehold blight and resultant urban decay or shortage of homes. It will allow the tenant to reinvest in

the property once the lease is extended. The model will negatively affect the value of the tenants interest temporarily (to reflect the increased rental payable to the landlord through the marriage value generated by joining the interest in the land with the interest in the improvement). However, the value of the tenants interest will be enhanced at subsequent assignment through the ability to secure mortgage funding in the long term. Whilst there is potential to develop a model where a lease renewal is generated upon payment of a premium (rent up-front), the annual rental model ensures that the landlord receives an equitable return without prejudicing intergenerational returns.

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This model obviously creates an increased management role in administering the asset (now comprising land and building), something that in the case of customary land in Fiji the NLTB does not have the current capacity to manage. Obviously, the management fee for land plus improvements should be higher than mere land, and the model must incorporate a sinking fund for replacement of the improvements in due course. This is a hybrid model, and differs significantly from the UK example as it allows for the continued interest in the superior title to be vested in the customary landowners.

The model will require the development of a valuation methodology to manage the marriage value calculation. Provisionally this can be calculated on the capitalised income for an open market transaction for a residential investment (and there is adequate market evidence upon which to base this in all Pacific Island Countries), with a present value adjustment to reflect the number of years to lease expiry. The value can be moderated through a calculation of the value of tenants improvements (depreciated replacement cost) less cost of demolition and remediation. Valuation and legal costs related to undertaking the valuation and lease renewal should be levied on the tenants, given that if left to lease expiry the value of their interest will fall to zero.

Critical to the execution of this solution is the need to minimise future conflict. Assuming a long lease is granted, given that both the land and improvements will now be vested in the customary landowners, there will be intergenerational equity ensured from the market mediated rental payment. Dependent on the length of the remaining lease at 'marriage', the tenant will retain a level of profit rent for their interest, which can be transacted on the open market upon assignment of tenants interest to another party.

The model effectively moves, over time, an increasing share of the interest in the improvements to the landlord (i.e., the trustee on behalf of the custom owners). This brings a new set of rights, obligations and restrictions onto the landowners to ensure that the property is well maintained and regularly renovated to capture the maximum return on the investment. There are also associated insurance and maintenance covenants to address.

Such a model will inevitably provoke a range of reactions. Firstly, the tenants will feel aggrieved that they have a lesser interest under the new model. The response to this claim is straightforward as, in reality, tenants currently have no property rights at all beyond the expiry of their current lease other than having a negative financial obligation to clear and remediate the site within three months. Under this proposal, they will have continued opportunities for living in the same property, albeit with adjusted property rights and as true tenants rather than the rather confused and misplaced perception of owners with rightful renewal that exists at present. Critically in Fiji, the 18,000 families affected are an important voting block in urban areas, so the information and education programme to inform each party of their rights will require careful political management. The alternative, of course, is the unacceptable

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move to permanent alienation by way of individualised freehold interests, breaking fee simple ownership away from the customary stewards. The political management to achieve that would be insurmountable at the current time.

As stated, there are major limitations in valuation capacity to manage this model at present. Leasehold valuation models have been an ongoing source of contention (see, for example, Gane, 1995; Mackmin, 1995; Trott, 1980; Trott, 1986; Baum and Crosby, 1988). This is because of:

- > the adoption of low accumulative rates in the dual rate approach;
- > remunerative rates that relate to the differing implied growth in freeholds;
- > confusion of taxation adjustments;
- > difficulties in adjusting for variable profit rents;
- > the complexity of gearing; and
- > the major challenges in comparative analysis of leasehold sales.

Moreover, managing the interest during a lease renewal will require a good understanding of leasehold valuation, particularly as the level of ownership in the landlords interest moves firmly towards the full ownership of land and improvements. Caution will be required to prevent the limitations of valuation theory in the Pacific repeating the challenges experienced in the UK in the 1980s and 1990s.

Critical to minimising future conflict of the type detailed above, it is optimal to ensure that all new leases are drafted to vest improvements in the landowner on lease expiry. This leads into the challenge of tourism leases in Fiji and Samoa. A poignant example is provided by a recently negotiated lease for a new tourism development to take place on customary familial with multiple ownership on the southern coast of Upolu in Samoa.

The proposal relates to a prime tourism development site of some 7 hectares. The chiefs of the familial owners appear to have been attracted by a modest *ex gratia* payment (that could be equated to 'key money' or an initial premium) and, after a development grace period, a rental that equates to some 5% of a hypothetical UCV that was calculated at a nominal rural land use basis. Whilst the lease provides for first preference to be given for the future employment of 'suitably qualified' applicants from the families whose land is used, this relates to low-end service sector employment in construction, maintenance, supply of goods, and handicrafts, as well as cultural demonstrations and car hire.

The lease, which is for 30 + 30 years, contains similar provisions relating to the tenants ownership of improvements (and right to clear or be compensated on lease expiry) to those described in the Fiji residential example described above. This

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means that the land is tied up for 30 + 30 years at a nominal ground rent which if cautiously invested at an accumulative rate could never generate a sinking fund sufficient to compensate the tenants for their tourism infrastructure improvements on lease expiry.

The customary familial interests are represented in trust, which the Minister of Natural Resources and the Environment administers as trustee. The lease is therefore drafted between the Honourable Minister of Natural Resources as lessor and the tourism developer / operator as lessee. Valuation advice was provided by the office of the Chief Valuer, in advising the Minister, as trustee.

In entering into such an agreement, at today's worth, the customary owners are tying up their land for at least the next sixty years for a very modest capital value plus potential employment opportunities. This may seem significant to a poor subsistence community, but will inevitably be a source of intergenerational discord.

In real terms, if they had the modest capital available the customary owners would generate a far higher income and maintain full control over their land if they were to build and operate a small-scale *fale* development.

There is no equity share provision in the lease, of the type that is now commonly adopted through experience in the Fiji tourism leases over customary land administered by NLTB, or through the conflict avoidance equity-sharing example in the palm oil venture discussed in Guadalcanal Plains, Solomon Islands. The Fiji model allows for the payment of a ground rent plus an equity turnover share of (variously) 1½ -3% of the tourism venture takings (albeit that this is difficult to verify, particularly in terms of offshore bookings and payments). The tourism turnover model, does however, provide a participatory arrangement whereby the custom owners have a stake in the success of the venture and a remuneration increase that is better than inflation.

On several levels, the Samoan example is likely to lead to infighting, political challenges (if the actions of the Trustee are challenged, which whilst not likely in the short term, given the chiefly nature of the Trustee, could inevitably be the cause of *matai* distrust and infighting in future years), particularly as the expiration of the second lease term approaches.

The example, of course, provides a lease that appears to be too good to be true on the part of the tourism developers, given that they will realistically clear their development costs and be operating on pure profit by year 15. The reality is that deals that appear to be too good to be true usually are, and achieving a deal that does not provide a fully equitable return to customary owners in the long term will inevitably be a cause of future conflict and disruption to the business venture.

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ALTERNATIVE LEASEHOLD SOLUTIONS

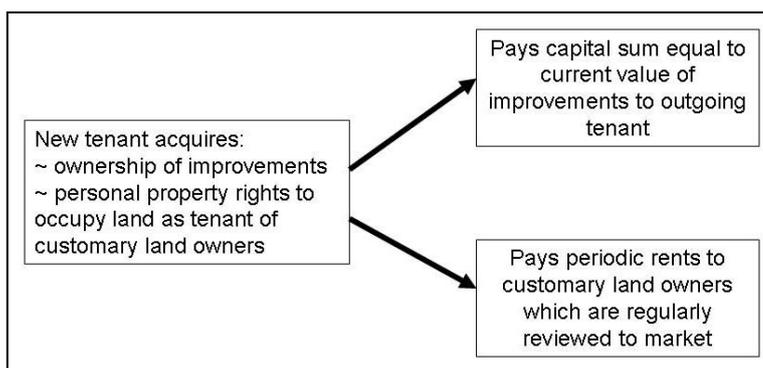
An alternative leasehold approach system is to consider a lease arrangement where the improvements are recognised as the property rights of the tenants, and they are valued separately at the termination of the lease. This strategy has the advantage that land rentals do not need to include a notional discount due to the anticipated eventual benefit of improvements to the landlord. It also has the capacity to encourage tenants to invest in appropriate improvements to maintain financially efficient use of the land right up to lease expiry. It could be expected within this situation that the risk of default, environmental degradation and risk of loss to the national economy would all be controlled.

The challenge within this approach is how to fund the compensation to tenants for the value of property rights in the improvements at lease expiry. There are several practical possibilities regarding how to manage the termination of the. These include:

- > Giving existing tenants the first option to renew leases on new terms. This is sometimes combined with a policy of insisting on automatic renewal of leases. The problem with these possibilities is that they diminish the ownership rights of customary owners by effectively taking from them the right not to renew the lease with the existing tenant. They have also been mooted in circumstances where political or other pressures have eroded rents over time creating informal capital interests for the tenants. This approach is not recommended as it empties the effective financial return to and control of property rights by customary owners, even while appearing to maintain their formal ultimate / superior ‘ownership’;
- > Including outgoing tenants as partial beneficiaries in the transfer of land into new leases to new tenants. It is possible to value the depreciated value or market value of improvements with reasonable precision. If the land were to be re-leased to new tenants, it would be possible to create a strategy for a tripartite transfer where the outgoing tenant is a financial beneficiary of the transfer. The new tenant would be required to pay the outgoing tenant a capital amount equal to the

assessed value of the improvements as well as contract to pay the landowners a periodic rent that is regularly reviewed to market. The value of improvements could be

FIGURE 4: INCLUDING OUTGOING TENANTS AS PARTIAL BENEFICIARIES OF NEW LEASES



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adjusted for all common valuation factors involved in specialised property valuation, such as functional obsolescence (see Figure 4).

Assuming the improvements represent commercial capacity, it may be possible for customary landowners to borrow against the expected business cash flows from running the improvements and buy out the tenant's interest in improvements. Banks have expressed willingness to fund commercial ventures based on expected cash flows. The risk with such a strategy is that customary landowners may not have the skills required to take over specialised businesses and it appears that there is sufficient evidence of failure of this type of strategy to make it unattractive.

There are several flaws in creating dual (or tripartite) interests by separating property rights in the underlying land asset from those in the improvements. It is far more efficient in a market economy to deal with land and improvements as a single title (as proposed in the previous section).

An alternative strategy for this circumstance would be for customary landowners to seek a new operator to take over from the previous tenant. They would still take over the improvements and be able to borrow against the rental cash flow that would include the combined ground rent and a rental component for the improvements. Borrowings would be made against the rental due to the improvements and would have to be matched against their financial performance. That is, the loan to cover the cost of improvements that would be paid to outgoing tenants would be structured to amortise over the likely economic life of the improvements as a minimum. This would be matched by a rental schedule to incoming tenants that would anticipate the depreciation of the improvements. While this option has the capacity to satisfy the needs of the various parties, it requires modelling that is beyond the scope of this report.

The interest of customary landowners in not renewing leases for developed land comes largely from the experience of many customary people whose rent has been insufficient to make re-leasing their land attractive. If rents were maintained at realistic market levels, rolling over leases equates to a renewed relationship between landowners and tenants to continue the productive use of the land as a form of implicit partnership.

DEBT AND EQUITY FUNDING

The view that investment in land is a more speculative form of venture than other forms of investment (e.g., Stock Exchange [SX] listed equities) was put forward by a number of commentators such as Whipple (1969) in the 1960s. This section summarises the complexities of debt and equity funding, identifying the importance of innovative funding arrangements to optimise the financial capacity of customary land in the Pacific. Highlighting the security of 'bricks and mortar' investments, it provides a leasehold equity funding model whilst highlighting the risk averse nature of major financial institutions over repossessing property rights over customary land.

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The speculative nature of any form of entrepreneurial investment was arguably not fully appreciated four decades ago, and today entrepreneurial endeavours which are grounded in buildings and land are clearly regarded as often less speculative than other investment vehicles. Indeed, investors seeking a greater level of security identify with ‘bricks and mortar’. Contrary to early views, the demand for land and buildings in locations that are not marginal remains constant. Although the use of a building or land may change during the life of the investment, it is unlikely that the building or land will remain unutilised or underutilised for very long.

Redevelopment of buildings and/or land is now regarded as a routine part of the investment cycle in ‘bricks and mortar’ investment vehicles. This merely mirrors the nature of buildings and land as a renewable albeit constant investment tool for investment funds globally. Investment in property related ventures generally requires the support of banks and financial institutions. The financiers weight the relative attractiveness of a land/building investment against other financial opportunities seeking funding. Investment in land and buildings is weighted against foreign exchange speculation, secure sovereign bonds, SX listed shares, and cash rates. In developed economies, investment in ‘bricks and mortar’ is viewed as a relatively constant, but beneficial hedge against inflation. Conversely, secure sovereign bonds are at fixed interest rates and arguably experience a value loss with rising inflation over time.

Aberrations in share price growth have occurred in some markets such as the ASX in recent years, which has been driven by the mining equities boom. However, this can be regarded as atypical of medium to long-term patterns in SX share values, which usually fail to catch up with the inflation rate. On the other hand, investment in ‘bricks and mortar’ has over similar medium to long terms risen at a rate greater than inflation, and hence the attractiveness of funding for entrepreneurial endeavours in buildings and land. Banks and financial institutions also see an underlying trend in land as a fixed commodity, which in locations that are not marginal, will increasingly become more scarce. This scarcity factor has meant that banks and financial institutions have recognised the intrinsic benefit in investing funds in such land and building-based endeavours, rather than in other investment opportunities that do not appear to have the underlying benefit of increasing scarcity.

Traditionally, the funding of entrepreneurial endeavours rooted in buildings and land has been based on debt funding. Simply, funds are provided to the entrepreneur to support a particular endeavour. The collateral base is land and buildings, which is given solidity through the registration of a mortgage over the land title. A charge in the form of a lien may also be taken over the entrepreneurial endeavour, which would be almost certainly conducted through a company structure. The mortgage will most likely have a term that corresponds to the anticipated life cycle of the entrepreneurial endeavour, say five/ten years with an ability to renew the mortgage for a further period. Such mortgages are ordinarily ‘interest only’ borrowings, with the original capital provided by the bank to be repaid at the end of the mortgage (or

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prior) by way of the sale of the complete entrepreneurial endeavour including land and buildings. The balance between the original capital borrowed and the value of the entrepreneurial endeavour when sold, can be described as the entrepreneur's capital gain.

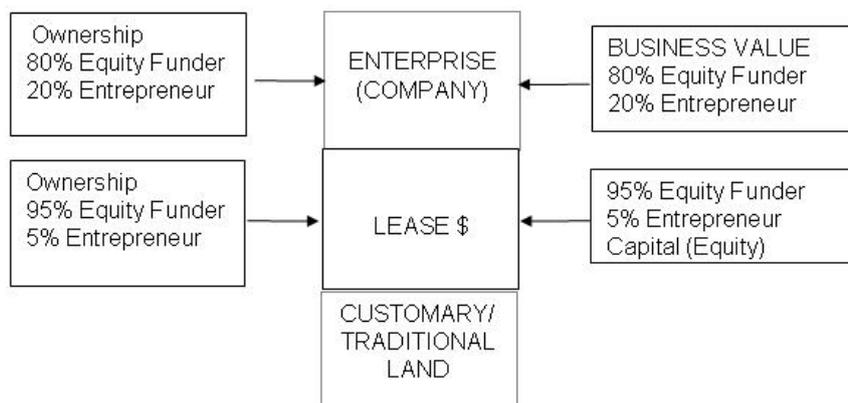
These funding arrangements are usually executed based on monthly or quarterly fixed interest payments for the term of the mortgage, with variable rate interest payments uncommon. The reason for this is that the success of the entrepreneur's business plan relies upon the crystallisation of as many outgoings as possible so that the entrepreneur may similarly crystallise the likely net profit of the enterprise.

In such cases, by way of example, the entrepreneur may borrow say \$10 million for ten years at 7% fixed, which would provide the bank or financial institution with a fixed annual interest payment stream of \$700,000. The entrepreneur utilising these funds may be able to increase the worth of the endeavour ten fold over ten years, giving a gross value of \$100 million, less of course the cost of conducting the endeavour over the ten years. If the cost of the endeavour amounted to say \$50 million over this period, the entrepreneur will net \$50 million, less the historic \$10 million to be repaid to the bank or financial institution.

It will be seen from the above example that the bank will receive after ten years the historic figure of \$10 million, but the entrepreneur will receive \$40 million. The 7% fixed return that the bank or financial institution received over the ten years amounted to \$7 million which can be added to the original \$10 million, but well short of the net worth accruing to the entrepreneur of \$40 million.

The banks and financial institutions have noted such imbalances in returns. It has become increasingly obvious that funding of entrepreneurial endeavours on land and buildings is based on equity funding, rather than simple debt funding such as described above. The reason for this change in attitude by the funding bodies is that the returns from debt funding do not provide an adequate return for the funder(s) relative to the net entrepreneurial profit.

FIGURE 5: EQUITY FUNDING (LEASEHOLD) MODEL



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Indeed, some funding arrangements involve a mixture of debt and equity funding (see Figure 5). Increasingly, banks and financial institutions, notably in larger developed economies such as New Zealand and especially Australia, have sought out involvement as solely equity funders. The financial institutions have realised that there is a larger amount of profit to be made if a greater level of risk is accepted. However, in the case of entrepreneurial endeavours involving land and buildings, equity funding has the benefit of the underlying strength of the land title as a collateral base. The move to equity funding of entrepreneurial endeavours raises both opportunities and problems where the enterprise is going to be undertaken on customary land.

Already, the example in New Zealand of the foreclosure of the Northland Māori land known as *Matauri X*, and the Karamu Reserve near Hastings revealed the distress that traditional owners encounter when their land is lost. In the case of *Matauri X*, the Māori land in question had to be sold to repay debt for a failed entrepreneurial endeavour. The reverberations throughout Māoridom of the potential for loss of land have clearly resulted in an attitudinal change regarding debt funding. Similarly, the banks and financial institutions in New Zealand and respective head offices in Australia, view the foreclosure of mortgages and the subsequent sale of Māori land as commercially undesirable given the sensitivities now apparent in the Māori to such actions.

Equity funding presents a particular challenge to customary landowners throughout the Pacific. If, as stated earlier, banks and financial institutions are moving inevitably away from debt funding towards equity funding for entrepreneurial endeavours, then financial structures will need to be conceived that respect the cultural sensitivities of traditional owners, whilst enabling equity funding to occur. Individuals and organisations seeking funding for entrepreneurial endeavours will not be able to access funds from banks or financial institutions unless they are able to accommodate the new funding criteria.

The nature of equity funding involves the funder becoming part owner of property rights in the land and buildings, as well as part owner of the enterprise to be conducted on the land or in the buildings. In a manner similar to farm-in arrangements in mining investment, funders assume an equity position that may amount to a percentage ownership overall approaching 90% or more. However in return for allowing the funder to take such large equity in the endeavour, the entrepreneur may only be required to contribute little more than nominal capital investment, but of course they will be tied to the project as manager for its duration. In return, the entrepreneur will gain a very substantial profit with little personal contribution of capital.

Where investment is proposed on customary land in the Pacific, or in New Zealand on Māori freehold land, it is obvious that a leasehold interest has to be created over the subject land. The lease and the buildings (or other associated investment such as trees) will be jointly held by the funder and the entrepreneur most likely as tenants in

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common, reflecting their respective percentages in the overall equity (i.e., funder 95%; entrepreneur 5%). Similarly, with a company structure being established to operate the enterprise, the share ownership would also reflect the respective equity position of the funder

INCREASING THE FINANCIAL MANAGEMENT CAPACITY OF CUSTOMARY LANDOWNERS

It has been observed that customary landowners retain strong notions of equity, family and tradition. These ethical fundamentals arguably put them well in advance of many people with whom they must interact in commerce. It suggests that they are not generally motivated to want to use the economic power of their land to exploit others, though they are extremely apprehensive that others may want to take advantage of them and their land. There is ample evidence to support their concerns. As generally ethical people, they can be relied upon in a way that modern western economics is unfamiliar with.

On the other hand, customary landowners often do not have sufficient understanding of the mechanics of financial management to manage their land resources effectively. Traditionally the responsibility for prudent stewardship lies with the community leaders, the chiefly classes and heads of families. This section of the indigenous community has the authority and income to be able to take this role. Since first contact with western people, members of this class have tended to seek western education. It is important that those who are in a position of leadership or influence decision-making have appropriate technical skills in the area of finance, property, and law. Disciplinary areas that will enable increased financial capacity for the effective management of customary owned land include the following:

- > Property valuation;
- > Understanding the new role of customary land in contemporary society;
- > Use of banks and money for financial management; and
- > Contributing to the development of knowledge concerning the responsible use of land for all cultures.

These objectives could be achieved through a range of measures, including some or all of the following:

- > Educating community leaders, or the emerging generation of indigenous leaders, and the media on land related issues;
- > Community groups engaging independent professional advice on land related matters;
- > Devoting sufficient resources to independent specialists to provide a platform for the formation and growth of a high quality indigenous professional body (see Boydell, 2007a);

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- > Providing educational opportunities to resource quality and culturally sensitive education at a state level;
- > The provision of adequately educated government field officers;
- > The support of trusts and government offices focused on the effective and culturally sensitive financial administration of customary land;
- > Exploring ways of directing a portion of the revenue stream from customary land rental into the above;
- > Reflection and new policy on the rights and responsibilities of those enjoying income from customary land to ensure the principles of fairness and equity that are implicit in traditional culture are carried through into the emerging regime of land management; and
- > The fostering of scholarship that explores and disseminates the meaning of the human relationship and social use of land and its culturally sensitive rendering into the emerging form of Pacific Island Countries.

THE ONE-STOP SHOP

The One-Stop Shop solution proposes the establishment of a suitably funded (via government or donor support) Land Resource Development ‘quango’⁶ of a small team of local and international planning, development appraisal, legal, anthropological, tourism, finance, management, marketing and agency specialists with the remit to:

- > Identify and investigate potential development sites;
- > Engage and gain support of land owning groups, families, clans in the potential development partnership;
- > Fast-track and resolve land ownership and title disputes;
- > Record and register land ownership;
- > Overcome any impediments to the provision of clear unfettered leasehold title and provision of finance;
- > Model development feasibility analysis to ensure that the highest and best use of the land is realised;
- > Market the available land internationally, through property and investment media, direct mailings, and the Internet;

⁶ A *quasi* non-government organization

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- > Facilitate planning, building, environmental and other statutory obligations pertaining to the site and the proposed development (both pre- and post-tender / negotiation);
- > Seek tenders or negotiate on behalf of custom owners, or their trustees, with prospective developers to ensure that a realistic and equitable residual land value is realised by way of premiums, rentals with appropriate review pattern and equity participation arrangements;
- > Draft leases to ensure intergenerational equity, precluding the risk of inadvertently creating perpetual leasehold interests (through clear covenants pertaining to tenants improvements) and ensure property rights and their respective rights, obligations and restrictions are clearly explained in both plain English and the relevant vernacular language;
- > Encourage, facilitate, and mentor complementary small-scale tourism ventures;
- > Act as Trustee on behalf of the customary landowners, as appropriate. This role is grounded on the preference expressed by financiers for a third party to act as intermediary, and the perceived conflict of interest that arises when the Minister of Lands or Natural Resources serves in this capacity. Obviously, the Trustee will have to charge an appropriate management that fully recompenses the services provided to the custom owners; and
- > Ensure the successful developer fulfils all their obligations under the lease, protecting the landowners' interests if there are any delays in the subsequent development process.

Obviously, in the first instance, such an initiative will favour landowners with high amenity customary land. The nature of development will ensure that secondary land will also realise economic benefit that follows on from the well-executed initial developments.

Where the economic potential of customary land is yet to be realised, there is a role for the government to assist with the 'One-Stop Shop' initiative.⁷ Uncertainty over secure access to land (through clearly articulated leases over customary land guaranteed by the State) creates investor uncertainty and limits the ability to secure finance. The situation is compounded where the potential to realise economic gain from land results in infighting both within and between landowning families holding land with resource potential (be it tourism, timber, copra, sugar cane, or palm oil). Such infighting can take years to resolve through formal court structures.

The One-Stop Shop solution takes a very proactive focus, facilitating development in its many forms⁸. Obviously, the activities will require funding, and it is realistic to

⁷ This important strategy is critical to both the financial management of customary land and institutional arrangements for economic development. It is therefore also identified as a key strategy in subproject 2.3

⁸ In this context, it has a very different remit to the Pacific Land Reform Unit advocated under a current AusAID initiative

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recoup the cost of the professional services of the specialist One-Stop Shop team from the proceeds of the sale of the development lease, thus ensuring ongoing funding for subsequent initiatives. While such a project at national level lends itself to be a candidate for donor support in the first instance, there is also scope to operate at the provincial level.

The role of Trustee and land management are ongoing responsibilities. It is envisaged that this type of national development catalyst would have a limited externally funded duration of ten years, with appropriate review and reporting mechanisms to consider the need for continuance. During this time, the quango will provide capacity and skill exchange with both government officers and private property development practitioners, providing support for complex land and development activities.

The One-Stop Shop initiative will ensure the principles of sustainable development are adhered, so that landowners are fully aware of the social, environmental, and economic trade-offs over the new financial management provisions of their customary land. The professional management of formal and informal institutional arrangements surrounding the economic development of customary land will enable a viable development partnership. It will achieve this with reduced risk of intergenerational dispute, whilst realising the most equitable return over customary land.

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APPENDICES

The appendices comprise four detailed country case studies that provide a rich context to the financial management of customary and other land in Fiji, Samoa, Papua New Guinea, and New Zealand.

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COUNTRY CASE STUDY: FIJI ISLANDS

Caveat: the current political situation in Fiji impacted on respondents ability to speak openly about land related issues.

TABLE 7: LAND ALLOCATION IN FIJI

Land Classification	Proportion by Area	Details
Native Land	87.9%	Formal leases administered through Native Land Trust Board (under Native Land Trust Act legislation), some through the Agricultural Landlord and Tenant Act, and others through informal <i>vakavanua</i> lease arrangements.
Freehold Land	7.94%	Over 20,000 titles under Torrens system
Crown (i.e. State) Land	3.91%	Approx. 7,500 state leases for varied specific land uses
Rotuma Lands	0.25%	

Native land

Native land cannot be sold outright and only licenses and leases are granted to individuals requiring land. Rental on native lease is regulated at 6% of the unimproved capital value of the land. Native land is classed as Native Reserve and Non- Reserve. The basic differences between these two types of land are:

- > that Native reserve can only be used by Fijians;
- > that the majority of land owning unit must approve to the granting of a license / lease on Native Reserve; and
- > that Native Reserves must not be subject to the Agricultural Landlord and Tenants Act.

Freehold land

Land held fee simple absolute in possession by an individual or corporations, subject to statutory law. It constitutes almost 8% of the total land area of Fiji. It is (mostly) referred to as Native Grant, Crown Grant, and Certificate of Title on the Standard Sheets.

Crown (or State) land

Land that is administered by Government Lands Department and is governed by *Crowns Lands Act*, Chap. 113 and 132, and *Crowns Lands (leases and licenses) Regulation* 1980. This is described under Chap. 113, Laws of Fiji as:

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“ .. all lands in Fiji including foreshore and the soils under the water of Fiji and all lands which have been / may be thereafter acquired on behalf of the Government for any public purpose”.

There are different types of State land:

- > State Freehold – is land bought over the years either from holders of Crown Grants issued in consequences of the findings at Lands Claim Commission or directly from the Fijians during the period 1905-1908.
- > Crown land without title;
- > Crown *Tiri*;⁹
- > Crown foreshore; and
- > Native land acquired by Crown.

Rental Issues

Equity

There are ongoing questions over equity pertaining to land allocation by tenure type. The argument is that the 49% non-indigenous population (and in particular the 44% Indo-Fijian population) has less equity in respect of land ownership. As discussed in sub-project 2.3, the communal nature of ‘ownership’ of indigenous land in Fiji does not equate to ownership from a western perspective (notwithstanding recent case law that supports acceptance of more individualised property rights). Equity is about equitable access rather than equitable ‘ownership’ or equivalency of property rights.

Market based Rent Determination

As expanded on below, the Native Land Trust Act allows for a market value basis for rental, albeit that the Interim Government have suggested that they are making changes to allow such a basis. There is mixed evidence regarding the closeness of rents paid to customary owners through the NLTB and true market values. Padma Lal and Mahendra Reddy (2002) found that international comparisons in the sugar industry suggested that current rents on sugar land are within international ranges. Despite this there has been criticism that agricultural rents are not sufficiently related to agricultural profitability and are too low. Freehold landlords can charge open market rental at first letting, but are restricted by the provisions of the Counter-Inflation Act [Cap 73] s12 from freely reviewing rental to market, having instead to make a case to the Prices and Incomes Board for any subsequent increase.

Urban rents suggest that ground rents to customary owners are extremely low. This is in part due to the practice of selling leases with an upfront premium. There is no

⁹ Both Crown *Tiri* and Foreshore are described as land permanently under water and rivers and streams, Rivers & Streams Act, Cap 136(2).

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public record of lease transactions/sales and secondary sales so the financial effectiveness of the total payment to customary owners is difficult to judge. However, the capitalisation of the premium into a major value component of urban lands is problematic.

Regulated rents

The Agricultural Landlord and Tenant Act [Cap 270] and the Crown Lands Act [Cap 132] provide for annual rents to be assessed at up to 6% of unimproved capital value (UCV). The Counter Inflation Act [Cap 73] provides for a regulatory environment that limits the level of rental increase upon lease renewal or review during the currency of the lease.

Rent collection

Depending on the land type and prevailing legislation, this is administered by the government or by the NLTB on behalf of the beneficiaries of the trust.

Rent monitoring (review procedures)

This is prescribed by the respective legislation. Under the Crown Lands Act 11.-(1) 'Not later than 12 months before the due date for re-assessment of the rent under regulation 10 the Director shall have the land valued by a competent valuer appointed by him for the purpose of assessing the yearly rental payable until the next due date for re-assessment or until the expiry of the lease, as the case may be. In such calculation the valuer shall have regard to what would be at the time of the valuation a fair market rent of the land under a lease granted for the same term and on the same conditions but not taking into consideration the improvements which are then in existence and unexhausted, and which have either been put on the land during the continuance of the lease or have been purchased by the lessee or his predecessors in title as existing at the commencement of the lease. The fair market rent under this paragraph shall in no case exceed 6 per cent of the value of the fee simple estate of the land not taking into account any improvements.'

The Agricultural Landlord and Tenant Act is clear on rental being set against unimproved capital value per 22(2) 'Save where the landlord is the owner of the improvements, or where the agricultural holding is to be let by tender, the tribunal, in assessing, fixing and certifying the maximum rent for an agricultural holding, shall allow the landlord a return of not more than six per cent per annum on the unimproved capital value of the land the subject of the holding: Providing that any premium paid by the tenant to the landlord (other than a premium paid under the proviso to subsection (1) of section 13) shall be taken into consideration when assessing, fixing and certifying such maximum rent.'

The Native Land Trust Act is silent on unimproved capital value, despite it being adopted in practice. This makes recent statements (03/07/07) by the Interim

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Governments Minister for Fijian Affairs, Heritage and Provincial Development and Multi Ethnic Affairs that the NLTB will now use market value rather than unimproved capital value (UCV) open to misinterpretation. The Native Land Trust Act clearly articulates that re-assessment of rent should be based on a market value approach under s.13 (5) 'For the purposes of this regulation, the rent properly payable under a lease of native land shall be the annual rent at which that land might reasonably be expected to be let in the open market by a willing lessor to a willing lessee if the full term of the lease had yet to run, having regard to the terms, conditions and covenants contained in the lease (other than those relating to rent) and assuming that the environment of the demised land is in all respects as it is or may reasonably be expected to be, at the appointed date, but disregarding-

- (a) any effect on rent of the fact that the lessee is in occupation of the land; and,
- (b) the current value of any unexhausted improvements on the land, other than those which have a value in relation to the purpose for which the land is demised and which-
 - i. were executed during the term of a previous lease of the land at the expense of the lessee where the lessee, or the lessee under any subsequent lease, was not granted a new lease upon the expiration of that term; or
 - ii. were executed by the Board; or
 - iii. were in existence at the time the land was first leased.'

However, adopting the market value approach specified in the legislation does represent a change in custom and practice on the part of the NLTB. There is a perception amongst both NLTB staff and Board members that the Native Land Trust Act adopts a UCV approach. This is, in part, grounded on the fact that there is no 'market' for inalienable customary land by virtue of it being inalienable. Given the lack of a commercial market in customary land, the NLTB deferred to adopting the UCV approach that is applied in both Agricultural Landlord and Tenant Act leases and Crown Lands Act leases. The situation is further compounded by the Government rentals. Whilst NLTB strive to collect at 6% of the hypothetical construct that is UCV, this is undermined by the Government only collecting a lower 3% (as opposed to the prescribed 'not more than' 6%) under their ALTA and Crown Lands Act leases. In practice, NLTB collects only between 2½- 3 % of UCV because the State as a matter of policy collects this much or less under their ALTA and Crown Lands Act leases.

Market based

Unimproved Capital Value is defined by the Agricultural Landlord and Tenant Act 22(3) 'For the purposes of subsection (2), "unimproved capital value" means the capital sum which the land the subject of the agricultural holding, if it were held for an estate in fee simple unencumbered by any mortgage or charge thereon, might be

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expected to realise at the time the maximum rent was assessed, fixed and, certified if offered for sale with vacant possession on such reasonable terms and conditions as a bona fide seller might be expected to require and assuming that any improvements thereon or appertaining thereto made by the tenant or acquired by the tenant had not been made:

Provided that such capital sum shall only take into account the purpose for which the land is leased and not the actual use of the land or any purpose for which the land could be used.'

Section 21-Agricultural Land (Declaration of Unimproved Capital Values) Order provides a schedule of land uses, locations and categories (including contour and soil quality) for grazing land, dairy lands, rice land, arable land, and coconuts.

Regulated

Rent Control on Residential and Commercial property was initiated in Fiji when the Counter Inflation Act 1973 was enacted. Third party approval by the Prices and Incomes Board was required for rent increases from 1973 to 1989. From 1989 to 1996 no third party approval was required as rent control was removed from the Counter Inflation Act. However, rent control was reintroduced in 1996 and continues to the present. The Prices and Incomes Board plays a significant role in the rental market of the Central Business District in Suva City. They only allow for increases in rent if the landlord has made investment on his property. Normally 12% of the amount of investment was allowed until 1996 when this was reduced to 10%.

Indexation

Under the Agricultural Landlord and Tenant Act the responsibility for rental adjustment on agricultural land is determined by a Committee of Valuers, as prescribed under 21.-(1) 'There is hereby established the Committee of Valuers which shall consist of four persons to be appointed by the Minister responsible for land matters-

- a) one of whom shall be a person who in the opinion of the Minister has appropriate knowledge, experience or qualifications in agriculture matters, who shall be the chairman;
- b) one of whom shall be a valuer who is a public officer;
- c) one of whom shall be a valuer in the employ of the Native Land Trust Board; and
- d) one of whom shall be a valuer engaged in private practice,

who shall hold office for such term as he shall determine.

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(2) The function of the Committee shall be to determine and, by order published in the Gazette, declare the unimproved capital values of the different classes of agricultural land the subject of an agricultural holding, the first such order to be published within one month of the commencement of the Agricultural Landlord and Tenant (Amendment) Act, 1976 and subsequent orders to be published every five years thereafter:

Provided that the Committee may differentiate in any such order between different types or classes of land and in respect of land situated in different parts of Fiji.’

Enforcement Arrangements

Statutory provisions for action against tenants for non-payment of rental are included in the Agricultural Landlord and Tenant Act [Cap 270] s37, the Native Land Trust Act [Cap 134] s13, and the Crown Land Act [Cap 132] s15.

Compensation, if any, of tenants and / or landowners, at expiry of land leases for improvements and or deterioration of State or customary owned land

The issue of compensation under the Native Land Trust Act is addressed in s34.(b)(v) ‘at any time before the expiration of the notice of removal, the lessor, by notice in writing given by him to the lessee, may elect to purchase any building comprised in the notice of removal and any building thus elected to be purchased shall be left by the lessee and shall become the property of the lessor who shall pay to the lessee the fair value thereof to an incoming lessee of the land.’

A similar compensation clause pertaining to the improvement on lease expiration is used in many constituencies in the Pacific. However, NLTA differs on the determination of payment, which adopts the fair value of the improvements to an incoming tenant as the basis of compensation. This clause separates the property rights in the improvements from the property rights in the land. It will be for the courts to determine what compensation is payable to outgoing tenants in respect of their improvements in circumstances when the *mataqali* may request that the NLTB does not renew leases. This is likely the proprietary group can prove that it needs the land for its own occupation due to expansion of the group – a realistic eventuality in urbanised residential areas like Namadi Heights, Tamavua and Lami in the capital. If the courts determine that compensation is payable by the landlord to the outgoing tenant the nature of the ‘landlord’ will come into question, given that it is the NLTB who statutorily acts as the lessor as trustee of Native land. The NLTB does not have the financial reserves to account for compensation of large number improvements to prime residential properties in the capital.

Hitherto, there has been a perception on the part of tenants, and also within the NLTB, that there would effectively be an automatic renewal of residential leases. This has been the case at the time of sale of the leasehold interest (land and improvements for the expired term of the lease, plus anticipated extension) in a may

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properties on NLTB subdivisions in the last decade. However, members of the proprietary group are increasingly aware of the residual interest in the property rights held by the group, particularly in residential areas. The NLTB and government need to resolve this matter as a priority.

Under the Crown Lands Act improvements in the case of surrender are dealt with under s23. 'When any lease is surrendered as provided in regulation 22 any improvements on the land shall from the date when such surrender takes effect be deemed to be vested in the Crown provided that the Director may at his discretion allow the removal or sale of such improvements by the lessee within a specified period.' This provision assumes that it is unlikely that a lease would be surrendered as it would usually be assigned (sold) to a third in preference to surrender, given that surrender of lease also equates to the surrender of latent value of any improvements thereon.

The Agricultural Landlord and Tenant Act deals with compensation for improvements at 40.(1) 'Where the tenant of an agricultural holding has, after the commencement of this Act, made or caused or permitted to be made, thereon any of the improvements specified in the Schedule, he shall, subject as is in this Act mentioned, whether the improvement was or was not an improvement which he was required to make by the terms of his tenancy, be entitled, at the termination of the tenancy, to obtain from the landlord as compensation for the improvement such sum as fairly represents the value of the improvement to an incoming tenant: Provided that the tenant shall not be entitled to obtain compensation unless the consent or notice required to be obtained or given as specified in the Schedule has been so obtained or given and unless the tenant has, where requested by the landlord, served upon the landlord, within one month of the completion of the improvement, notice informing him of such completion.'

During the cycle of ALTA lease expiry that commenced in the late 1990s, the media has profiled imagery of tenants removing homes from cane farms to politicise expiration issues. The Act is quite clear on issues of compensation, which are payable in the event of landlords consent. In many examples, the tenants never obtained the appropriate consent from the landlord upon payment of a fee under the Second Schedule of the Act s8. For issue by nominee of Permanent Secretary for Agriculture of certificate of recommended improvements a fee dependent on estimated cost of improvements. In other instances, it has been suggested that tenants paid a fee but seemingly it was never processed. There are significant ramifications for a second or third language speaker in dealing with complex landlord and tenant legislation written in legal English.

There is an established appeals process to use a tribunal to fix compensation under s42: 'Where the parties are unable to agree as to whether compensation is payable under the provisions of sections 40 or 41 or as to the amount of such compensation, the landlord or the tenant may apply to the tribunal of the agricultural district in

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which the agricultural holding is situated to decide whether such compensation is payable and, if payable, the amount thereof?

Unimproved capital value of agricultural, particularly cane, land is a figure that is impossible to quantify in today's largely improved market. There are some 13,140 ALTA leases expiring from 1997-2028 with the most (3,549) expiring 1999-2000 (Government of Fiji, 1999). Under the 1999 coalition government headed by Mahendra Chaudhry, the first Indo-Fijian Prime Minister, some indigenous owners sought to regain and retain their land. Compensation for lease expiry (a controversial and unprecedented action) at \$28,000 per agricultural lease was proffered to tenants who did not want to be resettled (as the government had seen resettlement of these tenants as its responsibility). This windfall compensation offered by the government was controversial since it represented, in most cases, significantly more in dollar terms than the accumulated total received by the landholders over the last 30 or 50 years of the tenancy.

Distributive justice - Systems used for benefit and cost sharing within land owning groups, including trust funds

The management fee that the NLTB is entitled to charge is prescribed in the Native Lands Trust Act 14. -(1) 'Subject to the other provisions of this section, rents and premiums received in respect of leases or licences in respect of native land shall be subject to a deduction of such amount as the Board may from time to time determine not exceeding 25 per cent of such rent or premium, which shall be payable to the Board as and for the expenses of collection and administration, and the balance thereof shall be distributed in the manner prescribed.'

There has been ongoing reaction to this 25% management fee and the fact that it has been reduced to 15% over the last five years is commonly overlooked. In addition, the NLTB now retains 5% of the income in a collective Trust fund. Therefore 20% is deducted from income before the

balance of rents and purchase-monies is distributed in accordance with the Native Lands Trust Act 11.-(1) After deduction of any sums in accordance with section 14 of the Act, the balance of any monies received by the Board by way of rents and premiums in respect of native land shall be distributed by the Board as follows:-

- a) to the proprietary unit, seventy per cent;
- b) to the *turaga ni mataqali*, fifteen per cent;
- c) to the *turaga ni yavusa*, ten percent; and
- d) to the *turaga i taukei*, five per cent.'

By way of clarification, 'proprietary unit', in the case of native land, means the proprietary unit registered under the provisions of the Native Lands Act as being the owner of such land. This means that, for example, if the NLTB collects a rental of

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\$1,000 over a parcel of land, after they deduct their management fee of 15% (\$150) and trust fund component of 5% (\$50) the residue of \$800 will be available for distribution as follows:

- a) to the proprietary unit, 70% = \$560
- b) to the *turaga ni mataqali*, 15% = \$120
- c) to the *turaga ni yavusa*, 10% = \$80
- d) to the *turaga i taukei*, 5% = \$40

If, for example, there are 25 registered members of the proprietary unit over the age of 21, the \$600 will be divided between the 25 resulting in a payment of \$22.40 per person per annum. Obviously, the income per capita will be significantly less in larger proprietary units.

There has been increasing grass-roots reaction to the remuneration distribution under the aristocratic hierarchy formalised by the Native Land Trust Act in 1940. With an increase in education, members of certain proprietary units are questioning the 30% allocation distributed between their chiefs. Moreover, in some proprietary units the *turaga ni mataqali* controls the total income of the proprietary unit (15%+70% = 85%) and administers it for the good of the *mataqali*. From a communal perspective there is an argument that this is appropriate if it allows for enhanced community facilities. However, increasing economic demands for food, school fees and health care result in an increasingly individualistic approach to financial resources by beneficial members of the proprietary unit.

It also serves to explain why there was limited support for continuance of Agricultural Landlord and Tenant Act leases when they started to expire in the late 1990s. This lack of support is explained by the level of remuneration received when a 10-acre cane farm leased under ALTA may have only been producing \$700-1200 per annum in gross rent. Members of the *mataqali* identified that if they were to leave the land to go fallow and plant subsistence crops on part of the land to take to market they would potentially realise more than the \$24 per annum (using the above figures, or less for a larger proprietary unit) that they may receive for tying the land up under lease for another 20-30 years. This is acknowledged by the Interim Fijian Affairs Minister, Ratu Epeli Ganilau, 'We cannot bring back the formula we have been using for the last 50 years and expect the landowners to be happy about it because obviously they are much more educated now and aware of what they need to do to maximise their resource' (Fijilive, 2007).

Transparency

The formal leasing structures within Fiji are reasonably transparent, though the distributions within the customary community are not formally documented. This leaves the potential for some variation between clans and customary groupings.

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The premiums paid on lease transfer, especially in urban areas are not recorded on a public register. Since these constitute the apparent dominant portion of land rental value, this omission constitutes a major impediment in the effective financial management of customary owned land.

The level of transparency in dealing with the financial management of rental income differs from *mataqali* to *mataqali*.

Inter and intra-generational benefits

The Native Land Act provides that rights of ownership may be forfeited by over two years' absence under 20.-(1) 'Whenever any member of any land-owning communal division ceases to reside with such communal division for a period exceeding two years; it shall be lawful for the Minister, on the request of the other members of such communal division, to declare such Fijian to be no longer a member of such communal division and such Fijian shall thereupon become divested of all interest in the lands of such communal division'.

Cost sharing from the use of customary land

This is addressed in the management fee, currently 15%, charged by the NLTB.

The role of financial management arrangements / systems in recent land based conflicts and conflict management

Largely, a lack of understanding by the parties of their respective property rights, obligations, and restrictions as outlined in the relevant legislation is a core cause for inflammatory situations. In addition, there are many examples of grievances demanding restitution or compensation in respect of previous land dealings, particularly those that remain contentious since the early colonial era. Issues of restitution surrounding such conflicts have been developed in detail in sub-project 2.3. Additional examples are provided in respect of conflict arising from land acquisition by the government.

Leasing for Commercial Use

The Native Land Trust Act provides for this over customary land, with NLTB vested with the role of generating an economic return over Native land that is not needed for the operation of the proprietary unit.

There are a variety of ways that land is leased for commercial use. Urban commercial use is often via leases of state land as well as some customary owned land. There is also a developed secondary market consisting of head lessees who lease property to third party tenants. This market is reasonably developed, suggesting that a direct rental market exists with pricing that does not rely on UCV.

Rural leases for commercial agriculture are also major type of land use. These tend to be on customary owned land and usually operate through the NLTA and ALTA

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systems. There is a trend towards informal direct leases between customary landowners and tenants, through *vakavanua* leases. These avoid the administrative overheads of formal leases but are less secure as they are not supported by the state. Data on *vakavanua* leases is not systematically available.

An analysis of Covenants relating to tenant improvements (i.e., who owns the property rights in the improvements) for leases on customary land provides some useful insights. The pretext upon which the analysis was undertaken is the agreements that govern the residential and tourism leases. These agreements are the legal basis for the analysis. It has to be noted that the agreements have to be in conformity with the governing Acts and Regulations.

Generally, tourism lease agreements have no provision for renewal and the question of compensation of tenants improvements is not clearly addressed. What this means is that there is no contractual solution to this issue at the time of the execution of the lease. In terms of what rights are there with the tenant when it is not stated as to who owns what and whether compensation is payable one may have to refer to the purpose of the lease.

It is obvious that there is no payment to the tenant unless there is a trend of that type. The general rule of common law is that the tenant has to replace to the landlord the leased land back in its original form with husbandry land use practices. There is compensation payable by the landlord to the tenant if the lease is repossessed prior to expiry on the basis of market value (in an open market). This is provided for in the agreement.

On the issue of improvements...the tourism lease is silent.

As with the tourism lease, the commonly applied residential lease fails to address the question of who owns property rights in the improvements.

Common law indicates that fixtures and fittings that are 'fixed' belong to the owner, and those that are erected for tenants use belong to the tenant. However, it would be difficult to categorise at law what happens to fixtures and fittings like a residence, which is there as part of the land but built by the tenant and where the express reason for the lease is to build such a residential dwelling.

There is a prevailing naivety by stakeholders that indicates such a clause would be decided upon at the time of the actual happening, i.e., when the lease is nearing expiry. Such critical covenants should have been addressed in the lease agreements. However, this is not the case in the current residential lease agreement or in the tourism lease agreement.

If the question has not been addressed by the Agreements, the Act would apply. What does the Act state? Of particular importance is regulation 34 of the 4th schedule. The relevant section states as follows:

'General conditions

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34. All leases shall be subject to the following conditions in so far as they are applicable to the circumstances of any case:-

(a) that fruit trees growing on the demised land shall not be cut down without the consent in writing of the lessor:

Provided that this stipulation may be deleted at the discretion of the lessor in leases for a period longer than twenty-one years;

(b) that any building erected by the lessee on the demised land shall be removable by the lessee within three months after the expiration of the lease:

Provided that-

(i) before the removal of any building the lessee shall pay all rent owing by him, and shall perform or satisfy all his other obligations to the lessor in respect of the demised land;

(ii) in the removal of any building the lessee shall not do any avoidable damage to any other buildings or other part of the demised land;

(iii) immediately after the removal of any building the lessee shall make good all damage occasioned to any other building or other part of the demised land;

(iv) the lessee shall not remove any building without giving one month's previous notice in writing to the lessor of his intention to remove it;

(v) at any time before the expiration of the notice of removal, the lessor, by notice in writing given by him to the lessee, may elect to purchase any building comprised in the notice of removal and any building thus elected to be purchased shall be left by the lessee and shall become the property of the lessor who shall pay to the lessee the fair value thereof to an incoming lessee of the land;

(vi) If the lessee applies for a renewal of the lease the provisions of paragraph (c) shall be deemed to cease to apply as from the date of application of the lessee for a renewal of the lease;

(c) that the lessee shall bear, pay and discharge all existing and future rates, taxes, assessments, duties, impositions and outgoings whatsoever imposed or charged upon the demised land or upon the owner or occupier in respect thereof, landlord's property tax only excepted;

(d) that the whole of any portion of the demised land used for the grazing of stock shall be enclosed with good and substantial fencing so that all stock kept upon the land shall at all times be adequately fenced in;

(e) that the lessee shall not remove or dispose of by sale or otherwise any forest produce growing upon the demised land without the written consent of the lessor first had and obtained and subject to such conditions as to the payment of royalty or

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otherwise prescribed by the Native Land (Forest) Regulations as the lessor may direct;

(f) that the lessee shall not alienate or deal with the demised land or any part thereof, whether by sale, transfer or sub-lease or in any other manner whatsoever without the consent in writing of the lessor first had and obtained:

Provided that nothing in this paragraph shall be taken to purport to require consent by the lessor to the mortgages referred to in the proviso to subsection (1) of section 12 of the Act;

(g) that the lessee shall not subdivide the land without the written consent of the lessor first had and obtained and then only in accordance with a plan of subdivision approved by the lessor in writing;

(h) that the lessee shall keep open and maintain in good condition all drains, ditches and water-courses upon or intersecting the land the subject of the lease, to the satisfaction of the lessor or the Commissioner;

(i) that in the event of any breach by the lessee of any covenant or condition in the lease, the lessor may enter upon and take possession of the demised land or may at the discretion of the Board impose a penal rent in respect of such breach.

Section 34 (b) (iv) and (v) are the relevant sections for guiding us into what path lawyers may follow for improvements. Improvements are defined in the First Schedule of the Native Lands Trust Act and include dwellings. Applying section 34 where the landlord wishes to retain the building, then upon the issuing of a one month notice by the lessee the lessor has to express their intention of paying for the improvements. This suggests that if there are improvements which are not demolished by the lessee and which the lessor wishes to keep, then technically speaking the lessor may find themselves liable to the market value of the improvements.

Under common law, the tenant is entitled to the produce of the crops that he or she sowed after the expiry of the lease. In terms of improvements, the common law view tends to state that the improvements are generally governed by the terms for the tenancy.

In Fiji, the scene seems unique (albeit a familiar story in other PICs) as neither the Act nor the Agreements have stated as to what happens to the improvements that are on the land.

The Act does state that the land has to be returned to its original state, but not as to whether compensation is payable.

Section 34 sheds some light and allows some room for debate suggesting that the intention of Parliament may have been to ensure that worthwhile improvements are

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not lost. For example if someone erects a power generation scheme over leased land that may cost millions of dollars, there is prudence in retaining the infrastructure.

There is a view that maybe this failure to provide an exact policy on the matter of improvements is not a error or oversight. Arguably, it is a deliberate attempt to ensure that there is no pre-arranged means of ensuring the continuance of a lease, which might be likely where the lessor is unable to pay the costs of the improvements and becomes duty bound to renew the lease. Such circumstances ensure that the system goes back to the first steps (i.e., customary ownership of bare land) after each expiry.

Inter and Intra Generational Conflict over Commercial Land Use

The NLTB system of providing an intermediary between customary owners and tenants has proven to be a convenient and uniform channel for access to customary owned land. It does not necessarily serve the landowners' needs, which has led to considerable conflict. Three major areas of conflict can be identified:

- > Firstly, ownership rights internal amongst the customary community. This can be divided between rights disputes amongst members of the chiefly classes over land boundaries and tension between the chiefly hierarchy and the ordinary customary owners at the village level. The high value of rents flowing to various chiefly levels, from the *vanua* to the *mataqali* makes the precise allocation of land boundaries important in a way that was not previously necessary;
- > The fixed distribution to the hierarchy means that village people see only a small level of rent. This leads to conflict and an inclination to reject making land available for lease through formal institutional arrangements; and
- > The prevalence of informal premiums attached to the transfer of leases indicates that there exist considerable profit rents. These are very evident in urban areas, though their reality in rural leases appears debatable and possibly complicated by the perceptions created through administrative inefficiencies of the NLTB.

Dispute Resolution Mechanism

There is no specialist land court and there appears to be evidence that the NLTB rental determinations are constrained due to lack of resources and perhaps internal inefficiencies.

Encouraging common understanding

The rental determination for customary owned land does not appear contentious within the Fijian community, even though the UCV method is considered problematic. The fact that the actual rent charged is often different to the notional maximum based on UCV suggests that rents are being levied on an informal common understanding of what is reasonable.

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What is less clear is whether the balance between the value absorbed in the purchase premium and the rents to customary people is equitable. The development of a common understanding will require a better developed understanding of the cultural significance (as effective financial ownership) of the financial impact of lease transfer premiums.

Cost effectiveness

The NLTB takes a 15% administrative fee, which is perceived as excessive, though this might be due to the fact that it is combined to the disbursement to levels of the chiefly hierarchy before distributed rental income reaches the grass roots customary landowners.

An argument might be made of the cultural foundations of the chiefly role in the administration of land. Two facts should be considered. Firstly, the logic of traditional society suggests that it is the role of the chiefs to act as managers of the indigenous community. Part of that management involves management of the community's land. To discharge that role with respect to land, it could be expected that chiefs would have the skills to administer their clan's land effectively, or would use their resources appropriate the necessary skills. Secondly, many of the officers within the NLTB, along with other related institutions, are drawn from chiefly families. This is not surprising, as these families tend to have the resources to provide the education necessary to fulfil these public roles.

Viewed in this way, the NLTB could be criticised as providing a double return to this sector of the indigenous community. As such, it is not seen as being cost effective when viewed across the entire community.

There is a need for directing resources into improving capacity in the administration of land. This need is especially important for the strengthening of valuation capacity, both in terms of practical skills and in the development of an equitable valuation methodology.

Accountability

The NLTB being a state instrumentality embodies a high level of accountability within its own system of operation, although the credibility has again been undermined in the last year by the circumstances surrounding the departure of the General Manager, the Strategic Change Manager and three members of the Board. Generally, criticism of the NLTB tends to be more in terms of whether it does provide a fair and equitable administration of land for the various parties.

Certainty

There is a high level of certainty within the formal system through the NLTB. UCVs are set transparently and the terms of leases are honoured. Rental payments are less

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certain. The level of rents charged are often considerably less than the notional 6% of UCV.

Even with these lower rents, there is a high level of rental arrears that the NLTB does not appear to have the resources to rein in. This problem has been with NLTB from its very beginning and the Board has been criticised for it from all quarters almost at will. On the first quarter of each year over the last 10 years, the Board carries rental arrears totalling some \$12 million. This is a considerable portion of the total rent roll of around \$33 million per annum.

Acceptance

There is rising discontent with the NLTB system due to the gap in rental income between village level customary owners and rents paid by tenants. The rise of informal tenancies is indicative of a lack of acceptance of the formal mechanisms.

Peri-urban settlements constitute a second major instance of the rejection of formal options. Peri-urban settlements represent direct, though often poorly controlled leasing of customary owned land. They are a significant component of the urban landscape of Fiji and appear to defy formal attempts to dissolve them. They have a strong level of informal acceptance, but this creates problems for urban management. They do not permit the organised provision of services and infrastructure.

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COUNTRY CASE STUDY: SAMOA

Introduction

There is some contention over the land allocation data (see Table 8), which was the situation at Independence (1962) – different authors (e.g., Peteru, 2003; ADB, 2004) have suggested variations, but the above figures were confirmed by the Department of Minerals, Natural Resources and the Environment (MNRE). Since 1962, the Government has released several hundred acres for general public use.

TABLE 8: LAND ALLOCATION BY TENURE TYPE IN SAMOA (SOURCE: MNRE)

Customary Land	81%
Freehold Land	4%
Government Land	11%
WSTEC Land (public land now administered by Samoa Land Corporation [SLC])	4%
Leasehold land with secure tenure	<1%

There are only 197 active leases (2005 data) over Customary Land, with 80 relating to Government use, 85 for religious purposes and only 32 relating to commercial activity. The adoption of commercial development leases over customary land is in its infancy.

Different alienability laws apply to customary and freehold land. Customary land cannot be alienated by sale or mortgage but may be leased.¹⁰ The Alienation of Customary Land Act 1965 governs the leasing of customary land. Leases of customary land are entered into by the Minister of Lands as lessor and acting as trustee for the beneficial owners of the land.¹¹ The Ministry responsible for lands, presently the Ministry of Natural Resources and Environment, administers, oversees and manages the leases. The longest lease term available for customary land is a maximum lease term of 30 years with an option or options of renewal for an additional maximum 30 years in aggregate for hotel or industrial purposes.¹² Further terms and conditions of lease for customary land are to be determined by the Minister for Lands.¹³

Freehold land may be alienated by sale or lease. The creation of Freehold title is forbidden by the Constitution (s.102). However, freehold land may only be sold to resident Samoan citizens unless written consent of the Head of State is obtained.¹⁴

¹⁰ Above n1, art 102.

¹¹ Section 4, Alienation of Customary Land Act 1965.

¹² Above n4, s4(b).

¹³ Above n4, s4(e).

¹⁴ Sections 4 and 6, Alienation of Freehold Land Act 1972.

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The terms and conditions for a lease of freehold land are determined between the parties to the lease.

Public land may be sold or leased. There are two types of public land: land set aside for a public purpose and government land.¹⁵ Where it is found that land set aside for a public purpose is no longer required for the designated public purpose it may be sold or converted into government land.¹⁶ The Lands, Surveys and Environment Act 1989 governs the alienation of government land.¹⁷ The land is managed by the Land Board and may be leased or exchanged by way of grant in fee simple for freehold land.¹⁸ The Act provides the Land Board is the lessor, on behalf of the State.¹⁹ The Act contains provisions covering lease terms such as rental,²⁰ improvements owned by the Government²¹ and forfeiture of lease.²² Leases may contain any other terms and conditions so long as these are not inconsistent with the Act.²³ A lease over government land may only provide for a maximum lease term of 20 years with an option or options of renewal for an additional maximum 20 years in aggregate²⁴

The Taking of Lands Act 1964 provides for land acquired for a public purpose to be leased out by the Minister for Lands.²⁵ The provisions in the Lands, Surveys and Environment Act for the lease of government land shall apply to the lease of land acquired for a public purpose but substituting the Minister for Lands for the Land Board.²⁶

Property market conditions

The buying and selling of real estate in Samoa has captured the interest of Samoans in the past 15 years, during which there has been a 150% percent increase in property values in the capital.²⁷ This surge of urban property values has also highlighted the growing problems the property market faces and the need for regulation. Land use planning and related legislation is necessary to regulate residential and commercial development. Land use has always been an issue, especially in the Apia CBD.

Apia has seen rapid infrastructure development in the past few years and commercial developments in the Business District have been stunted by the many residential

¹⁵ See s2 and Part IV, Lands, Surveys and Environment Act 1989.

¹⁶ Section 22(1), Taking of Land Act 1964.

¹⁷ Above n8, Part IV.

¹⁸ Above n8, see s29, 36 and 49.

¹⁹ Above n8, s49.

²⁰ Above n8, s51 and 52.

²¹ Above n8, s53 and 65.

²² Above n8, s87.

²³ Above n8, s67.

²⁴ Above n8, s37.

²⁵ Above n9, s23A.

²⁶ Above n9, s23A(3).

²⁷ Pers.com. Lui Seru, Central Property Valuations.

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properties located close to the CBD. Without planning, many of these prime commercial sites continue to be used as residential sites, therefore limiting the expansion of the Business District. The small group of young property professionals who dominate the real estate market in Apia are calling for a proper land use zoning and town planning system, advocating that this will greatly benefit the growth of the commercial sector in Samoa.

The recent escalation of property values of the limited stock of both residential and commercial freehold properties has made it difficult for the local residents to purchase land. Land prices in some residential areas has jumped by 100% in the past two years. The increased demand and escalating price is fuelled by lifestyle changes for local Samoans and by land grabbing from overseas by non-resident Samoans. In the past Samoans were comfortable living in the extended family setting and most were living on customary land. However, with education and a move towards a market economy based lifestyle, many Samoans have moved away from their customary land, settling in the capital and living on their plot of freehold land.

Expatriate Samoans are also starting to return home, with many purchasing freehold land. Many of these Samoans bring with them cash to purchase property and are able to pay above market value in order to get the best properties. Given these factors property has become very expensive for the average islander.

The lack of infrastructure and amenities in areas such as Malololelei, Afiamalu and Tiavi needs to be addressed in order to liberate more customary land to meet the increasing demand for residential land. The development of these areas will also encourage economic growth in areas outside of the CBD.

The majority of land in Samoa is Customary Land. The legislation governing customary land precludes its use for commercial purposes, limiting the potential economic development of Samoa. The process involved when applying for a lease of customary land has not been reviewed since the Alienation of Customary Land Act 1965 was passed and is in need of adaptation.

Customary land surrounds majority of the freehold properties in Samoa, acting as a buffer to development and expansion of the capital. There is a need to devise a workable leasehold system to make it possible for customary land to be used for commercial purposes, with appropriate trust structures to enable it to be transacted freely and be of equal value / economic amenity with freehold land.

Trusts

The Minister acts as Trustee over leases under the Alienation of Customary Land Act 1965. This provides a buffer between tenants and landowners. A number of concerns were raised regarding the Minister signing the leasing agreement on behalf of the landowners and an option to be considered to address this concern is to allow the matai as the representative of the beneficiaries to co-sign the agreement. The

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role of the MNRE should eventually move to being that of a regulatory role and allowing landowners to enter the agreement as the lessor themselves.

The term “beneficiary owners” needs clarifying, as the current legislation has no mention of the *matai*. The role of the Village Council also needs reviewing and if need be should be incorporated into the legislation particularly in the sense of providing security to both the lessor and lessee.

Within the landowner group there is also a call to form family trusts to act as land owning trusts. The purpose of the family trusts would be to control the current arbitrary behaviour of *matai* who have the authority currently to retain what is considered an inappropriate share of rents. There is a need to clarify and educate land owners of authoritative issues pertaining to the *matai* title and not to the individuals themselves. The increasing number of multiple titles can cause friction in some instances as all these *matais* have the same level of authority over customary land pertaining to their title. Appropriate education and awareness programmes should be established and implemented so as to encourage the practice of good governance and transparency within communities and extended families.

Banks remain disinterested in using customary land as a security given that they cannot take a mortgage over it, and likewise the market for leases over customary land is untested so they are seen as unacceptably high risk. There have been discussions in extending the role of the Housing Authority, which currently caters for people who cannot obtain funding from conventional banks by accepting guarantees from family and friends, to leases over customary land. This could be achieved through a sublease to the Housing Authority (or a lease and leaseback arrangement).

Attractive sites away from the village have the most economic potential, as they can be leased most easily. There is scope to find suitably profiled sites and market them [ties in with One-stop-shop solution], resulting in a number of spin-off developments related to hotels, e.g. hydroponics, small scale fale developments, and related tourism activities (buses, car rental, dive operations, handicraft shops).

The opportunity can be extended beyond the Housing Authority to the National Provident Fund and the Development Bank – if these organisations start to accept leases over customary land as collateral and are serious about the investment potential, the conventional banks will have to join in to capture their share in the limited high potential sites within the 81% of customary land.

Rent determination

The fact that the country has not yet developed a market in the commercial use of customary land leases, there is little perception of their worth. Given that the alternative use of possible tourism land is to grow a few subsistence bananas or coconuts, any level of financial return is seen as beneficial by government.

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Market based

There is no established market for leasing customary land, so no market rental evidence is available. Customary land is beginning to be seen as the only direction for the expansion of towns but there is no perception of relativity between freehold and leasehold as yet. A market for urban leasehold land is yet to mature, requiring careful introduction to solicit general engagement and acceptance by the wider community. Government, in collaboration with the Asian Development Bank, has implemented an initiative that focuses on streamlining current practices and procedures relating to the lease of customary land. A number of significant issues have been identified and the project is currently working on strategies so that these issues may be best addressed not only to improve the framework whereby customary land may be leased but to preserve and maintain traditional aspects of the Samoan culture.

Regulated rents

Rentals are not regulated and there is no proposal to move to a regulated basis.

Rent collection

In a recent tourism lease where the Minister is acting as Trustee and the Director of MNRE is administering rental payment, Schedule 1.4 of The Alienation of Customary Land Act (1965) details the commission on rent at 5% by way of management fee. The former Minister was in agreement with the Prime Minister that Government should not receive any money (i.e., the 5% commission fee), suggesting that the cost of the work should come out of normal government expenditure of the Ministry to enable all the rental income to pass to the beneficiaries. They argued that the 5% commission was not just a clumsy arrangement, but that it is a service that the government should be providing [note: this is a confusing point – if the government is providing a commercial service on behalf of certain landowners, why should all of Samoan society share the cost? This is in contrast to the approach of the NLTB in Fiji, who take both a management fee for their services and slice five percentile of the rental into a collective trust fund]. The real issue may be that the government does not have the expertise or spare capacity within the Ministry to negotiate fairly for the landowners as beneficiaries [this ties in with the One-Stop Shop solution].

Indexation

This has not been identified as an issue or the process of indexation engaged with.

Enforcement of land rent payment

This responsibility is placed on the Director of MNRE under the legislation.

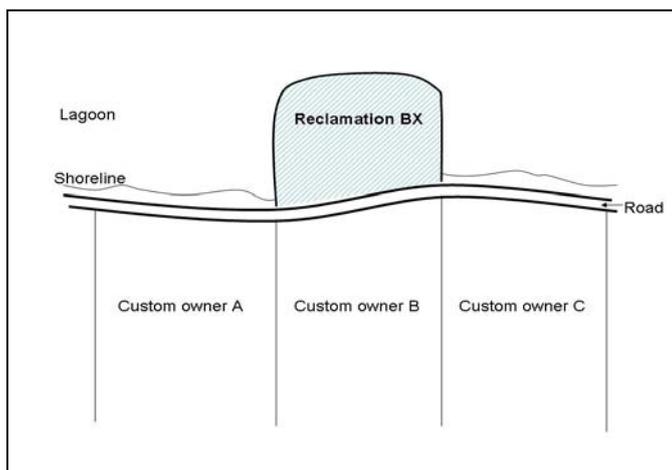
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Compensation, if any, of tenants and / or landowners, at expiry of land leases for improvements and or deterioration of State or customary owned land

Two pertinent examples assist – the example of the Vauvau tourism lease and the situation relating to licenses for land reclamation.

Land reclamation: the government is prepared to grant licences for ST\$500 plus costs of preparing an Environmental Impact Assessment (EIA) to customary landowners for land reclamation of waterfront land in front of their customary land. These sites are then managed through a 20+20 year lease from government. The lease of the reclaimed land can be used as collateral for loan security up to the value of the land (and improvements). However, the long-term ramifications of these reclamation sites do not appear to have been thought through.

FIGURE 6: LAND RECLAMATION



Take the example where custom owner B has been granted approval to reclaim land “BX” (see Figure 6), across the road from their main land holding. The government will grant a 20+20 year lease, which being a lease over government land can be used for loan security purposes. This raises the question as to what action the bank (as lender) can take in the eventuality of a

default on the loan. Can the financier enter into possession and market the remaining lease term? It is understood that this eventually has yet to occur, but it inevitably will. It also raises issues as to what happens on the death of the current named tenant (it is understood that the leases are usually granted in the name of a single *matai* rather than to tenants-in-common or as a joint-tenancy) – will the lease automatically transfer to the remaining members of the *aiga* or the new *matai*?

What happens at lease expiry and to whom do the improvements belong? One view is that they belong to the government in lieu of the tenants use for the preceding forty years, and a new lease at improved value could be granted. However, the more common perception is that while people enter into an agreement with the government, they still have the idea that it is their (the custom reclaimers) reclamation and land – so this is an issue (and potential conflict) that will arise in the future. Given that this is government land, it has the potential to be transacted (through assignment), possibly out of the tenancy of the immediate family. Obviously, over time, this alienable waterfront land will be at an economic premium. If these issues are not resolved, and leases are automatically renewed, the government

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will (assuming land values rise for alienable government land) run the risk of creating a perpetual leasehold interest.

Tourism leases: The example of leasing customary land is more complex. As detailed above, there are only 197 active leases (2005 data) over Customary Land, with 80 relating to Government use, 85 for religious purposes and only 32 relating to commercial activity. The adoption of commercial development leases over customary land is in its infancy. The proposal to use land for tourism purposes, e.g., the Warwick proposal at Vauvau (17 acres) and the ongoing saga over the APT ‘Return to Paradise Beach’ (750 acres) provide useful illustrations.

Given the restrictions on alienability by way of sale, access to land in Samoa for economic development purposes is primarily by way of lease. An issue that has the potential to cause land conflict is what happens to improvements to the land when the lease expires or is otherwise determined. The bulk of land available for development in Samoa is customary land. Leases of customary land have a limited lifespan and therefore the parties are likely to discuss the ownership and disposal of improvements at some stage.

Provisions addressing improvements are being included in lease agreements for customary land. Standard provisions of lease allow the lessee to remove its improvements at the end of the lease and/or for the lessor to purchase the improvements. It does not appear that the lease agreements are defining improvements. In relation to leases of government land the Lands, Surveys and Environment Act defines improvements as “...substantial improvements of a permanent character, and includes reclamation from swamps; clearing of bush, or scrub; cultivation; planting with trees or live hedges, the laying-out and cultivating of gardens; fencing; draining; roading; bridging; sinking wells or bores, or constructing water tanks, water supplies, and irrigation works, making embankments or protective works of any kind; in any way improving the character or fertility of the soil; the erection of any building; and the installation of any telephone or of any electric-lighting or electric-power plant”.²⁸

The concept of improvements to land is a Western law concept and may not apply to customary land or may apply but not in the way in which it is applied to Western property. In Western law improvements are generally understood to include buildings, fencing and also more permanent developments such as roading, sewerage and utilities (Blackstone, 1769 / 1966 reprint). The Supreme Court has determined that the law of fixtures applicable to Western property does not apply to customary land and therefore any property affixed to the land is to be considered personal chattels.²⁹ Issues over ownership of improvements may arise where the lessee effects more permanent developments to the land, such as streets and sidewalks, sewers and utilities, for example, as part of a hotel development project. There appears to be a

²⁸ Above n8, s2.

²⁹ See *Dive and Fly Samoa Ltd v Schmidt* [2005] WSSC 40 (22 December 2005).

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presumption in the way lease agreements for customary land are drafted that improvements are the property of the lessee. This may pose a problem because of uncertainties regarding the applicability of the concept of improvements to customary land. Lease agreements for customary land may therefore need to more specifically provide for improvements, beginning with some way of identifying what comprises improvements and who is the owner of the improvements.

There may be additional issues with the ownership of improvements where the lessee has relied upon investment to fund the improvements. For instance, where an investor has paid for an improvement and owns the improvement in its own right. If there has been intermingling of the investor's property with the lessee's property resulting in improvements that cannot be said to be fully owned by the lessee. Lease provisions should require that the Minister of Lands be kept informed as to improvements being made to the land. For instance, provisions obliging the lessee to regularly disclose its financial affairs and provide audits of the improvements to the land.

Issues may also arise as to how the improvements will be valued and how improvements may affect the value of the land. Consideration may need to be given to specifying the valuation principles or formula that will apply. The Alienation of Customary Land Act provides the Minister of Lands with the power to charge rent or collect other consideration from the lessee.³⁰ There are no statutory provisions governing how the rental for a lease of customary land is to be calculated. A recent Court of Appeal decision confirms that in the context of compulsory acquisition of customary land, fair market value principles apply when determining how much the State should pay for taking the land.³¹ Compensation is calculated based on what a willing buyer would pay for the land as if it was available on the open market.³² Any increase in the value of the land attributable solely to its acquisition is not to be taken into account.³³ The courts may apply similar valuation principles to the calculation of rental value of customary land, particularly if the lease agreement does not specify how rental value is to be calculated. Any increase in the value of the land attributable to improvements should be taken into account.

Where customary land is being leased for forestry purposes by the Minister for Agriculture the provisions of the Forests Act 1967 apply. The Act provides that no compensation shall be payable for improvements unless otherwise agreed to between the parties to the lease.³⁴ The lessee may remove the improvements conditional upon restoring the land to its original condition or may dispose of the improvements to an

³⁰ Above n4, s4(d).

³¹ See *Elisara v Attorney General* [2004] WSCA 4 (17 December 2004).

³² See also above n9, s37.

³³ Above n25, In *Elisara*, the Court of Appeal applied the 'Point Gourde' principle from *Pointe Gourde Quarrying and Transport Co. Ltd v Sub-Intendent of Crown Lands* [1947] AC 465.

³⁴Section 23.

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incoming lessee.³⁵ It may not be practical or desirable for the lessee to have a right to remove some or all of the improvements and consideration should be given to tailoring the lease provisions depending on the nature of the intended improvements.

If the lease agreement provides the lessor with a right to purchase the improvements, is it the Minister of Lands' obligation to pay for the improvements or the beneficial owners? What will happen if the lessor cannot exercise its right to purchase the improvements because there are no available funds to do so? Under these circumstances should the lessee be able to dispose of the improvements to a third party? These types of questions necessitate that more detailed considerations be given to using standard lease provisions providing a right to purchase improvements.

Generally, lease agreements for customary land should provide more specific and encompassing provisions for improvements identifying what comprises improvements, whom the improvements belong to, how the value of the improvements will be calculated and how improvements will affect the value of the land. The agreements should also provide for the effective and speedy resolution of disputes between the parties, such as through the provision of arbitration. Particular care should be taken to ensuring that not only are the interests of the beneficial owners protected but that the Minister of Land fully discharges his statutory obligations as trustee by way of adequate lease provisions to govern how improvements are to be dealt with.

Distributive justice - Systems used for benefit and cost sharing within land owning groups, including trust funds

Currently any payments go to the chief. There is one chief and they decide what to do with the money. He could distribute 10% to the family and retain 90% for himself, such actions are not unheard of. Without a complete change in the Samoan way, the situation will not change.

Many people are not happy with the way that *matiai's* have total control as there is a lack of equity. The *matiai* is supposed to be a governance role, a custodial role, rather than a take-take function. In reaction to examples of inequity, more families are proposing a family trust, where money is paid in and the trust will decide on family projects to best use the money. This has been cited as the type of evolution that people want.

Transparency

There is no standard reporting system for premiums, secondary lease assignments or the distribution made by chiefs. Without this information the situation cannot be transparent. There is a need for a major educational campaign in respect of how land income can best be managed and how best to establish trust funds.

³⁵ Above n28.

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Inter and intra-generational benefits

Inter-generational equity for future customary owners will depend upon how effectively rents to customary owners keep pace with effective market rents, especially given that capital growth in real estate resides in the land. The fact that freehold prices in Samoa have recently escalated suggests that Samoans are placing a higher value on privately owned land. This will lead to private rents over freehold property rising with the implication that comparable customary leasehold rents should follow. If the customary leases are initially sold with a premium, it is unlikely that the full value of capital gain will accrue to the customary owners.

Cost sharing from the use of customary land

Of the 81% of customary land in the country, little is currently seen as having significant commercial development potential (other than several key tourism sites and customary land in the peri-urban proximity to Apia and Salelologa). There is a view that families who currently have their homes / village on prime potential tourism sites would not be willing to forsake it for development. Conversely, it would appear that they have not yet been offered an equitable value for their land and thus are disinterested in giving up their home. As successful tourism ventures develop, there will inevitably be change in attitude

Leasing land for commercial use

As detailed above, there is currently limited adoption of leasing over customary land. In respect of tourism leases, the alternative use of coastal land has been cited as subsistence used for bananas and coconuts.

Regulating surveys of all customary land may not only have resource implications but may encounter objection from customary landowners. Government is therefore exploring the option of firstly identifying customary land with investment potential and stepping in to negotiate and facilitate the lease process.

The role of financial management arrangements / systems in recent land based conflicts and conflict management

The commercial banks (ANZ and Westpac) are not interested in lending on customary land. There is still doubt over whether the current legislation allows the mortgaging of a lease over customary land. A declaratory order from the Supreme Court needs to be sought to clarify the legality of mortgaging such leases. Once established that the current legislation does allow for mortgaging of leases over customary land further dialogue with the financial institutions need to be undertaken to ensure sound and effective requirements are established.

Banks are prepared to lend against reclaimed land as this offers security by virtue of a government lease. However, they are in reality lending against the risk profile of the *matai* rather than the lease itself. Given the limited availability of leasehold title over

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customary land, the banks are yet to engage actively in the leasehold market. However, they are open to engagement in this sector as it develops, assuming registered leases are guaranteed by the state. Critically, the commercial banks are a key-player in any One-Stop Shop type initiative.

Effective awareness programmes on the processes involved with the leasing of customary land need to be established and implemented so that more land owners are aware of not only the legal requirements associated with the lease but also their legal obligations and rights. In streamlining the processes involved with the leases of customary land, Government maintains its belief that any amendment to the existing legislation will not and should not allow for the alienation of customary land.

Land rent / benefit dispute resolution

Senior government officials identified limitations of capacity in their staff, and saw this as a reason why government should not be involved in a wider duty of care as Trustee. Government does not have the capacity to look after the interests of customary landowners and they would benefit from an alternative intermediary. The government is challenged in managing government land without extending its duty of care to customary land. The potential for a land development corporation / agency is required to manage the current very basic lease arrangements. Customary owners, whilst keen to protect their rights, do not really want to know about their obligations. Overall, there is a lack of adequate capacity to value and manage rents and insufficient formal or informal mechanisms to arbitrate over disputes.

In order to allow viable developments to proceed while disputes are being processed there is potential to legislate the option for beneficiaries to establish a Trust account in which lease payments may be paid into and only paid out upon settlement of the dispute.

The capacity of both MNRE and the Lands and Titles Court needs strengthening so that the MNRE are able to offer sound advice to landowners during initial negotiations while the Lands and Titles Courts are able to speed up the pace of disputes. An option to address the backlog of disputes currently encountered by the Lands and Titles Court is to explore the possibility of establishing a dispute resolution mechanism which may be used after all avenues of dialogue between the beneficiaries have been exhausted.

Arriving at acceptable decisions

Banks are not comfortable with the Government (Minister) acting as Trustee, whilst obviously they want to see the State guaranteeing the lease. The banks, and some sectors of government would prefer an alternative intermediary to act as Trustee – potentially with a body like a customary land development corporation. A similar initiative was proposed in the Government's 2002 *Strategy for Samoa* to establish an agency to lease customary land on behalf of investors. The government has also

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continued to investigate ways for commercial banks to use customary land as collateral.

There is a risk that future generations of disgruntled customary landowners in Vauvau could be inclined to bring an action against the Minister (and thus the Government) as Trustee for tying up the land for a 30+30 year tourism lease at what equates to a modest *ex gratia* payment and a very low annual rent. However, it has been argued that to landowners living on a wage of ST\$20 per day, the potential of a ST\$250,000 *ex gratia* payment to the village is more money than they could ever imagine. In the Vauvau case, the landowners came up with a lease proposal (albeit prompted any the prospective tenants solicitors), so in the view of Government they only acted as a facilitator and statutorily required intermediary. To this end, the role of government was merely to verify that the agreement was in accordance with the provisions of The Alienation of Customary Land Act, and they had little say over how much remuneration was involved – the families set up the organisation and came to the government to ratify the agreement as Trustee. However, this raises issues about the duties of a Trustee to ensure that the customary landowners are achieving the optimal return on their land.

The risk of future conflict due to inappropriate rent levels highlights the need for rents to be flexible through time. This is especially important when the current economic environment is immature. Adjustment to market at regular intervals, say three to five years, introduces a risk for tenants who may be less likely to invest in necessary in-situ capital improvements in case future customary owners attempt to claw out excessive rents using the land as a lever to access incomes reasonably originating from tenant improvements. This suggests the importance of rental methods that are transparent and recognise factor costs justly.

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COUNTRY CASE STUDY: PAPUA NEW GUINEA

Customary owned land

In PNG, customary landowners hold around 98% of the land, though there is some controversy about the current precision of that estimate. There is a near universal belief that land should not be sold or alienated in perpetuity. Generally, PNG land administration operates within this cultural principle, and its unique requirements have given rise to considerable attention from researchers, donors, NGOs and activists in the thirty years since independence.

As Prime Minister Somare (2006) expressed at the launching of the National Land Development Taskforce, “Despite this obvious interest, land problems in PNG remain poorly understood, even though the need for solutions has always been expressed”. He went on to highlight the need for drastic changes, identifying that previous attempts to progress land issues have mainly failed because external consultant led land reform did not pay full regards of cultural sensitivities.

The small proportion of alienated land (approx. 2%) accounts for about 90% of the most productive land in the country, including most of the land used for towns and cities. Alienated land is in one of three forms: very limited amounts of freehold purchased from customary landowners, State land used for infrastructure, and public works leased from customary landowners and land directly or indirectly leased to non-customary owners. Details of these are as follows:

Freehold land: This was largely alienated during the colonial era. Most is used for public purposes. It has been the subject of ongoing dispute, as the original customary landowners have tended to return to the government to complain that through the passage of time the prices paid for the land was insufficient or unjust. This has led to additional *ex gratia* payments being made to the customary landowners in recent years to placate the customary landowners. The payments are considered by the government to be the final payment that will be considered and that they represent a complete extinguishment of the customary claim. Considering the original acquisitions could be as recent as three decades ago and were considered completely settled at the time, the precedent of political willingness to make *ex gratia* payments makes the possibility of future customary landowners mounting similar claims a reality.

State land leased for public purposes: A more acceptable method of acquisition of customary land is leases from the customary landowners. The state leases land for various purposes from customary landowners. This has the advantage that it is in harmony with customary traditions as it leaves formal ownership with the customary owners while delivering practical use and control to the state representing the wider community. Two major challenges are associated with this form of ownership, the

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loss of control by customary landowners and the maintenance of a fair market rental return to them.

Lease and leasebacks: These are mostly arranged through the lease of customary land to the state, and then lease back to the customary landowners for subsequent sale to private tenant. This is known as the *lease and lease back* system. It has the advantage of placing the state between the customary landowners and the leaseholders thus providing a level of reliability, homogeneity, and consistency to formal leases. Rents are usually set through state valuation. The leases tend to be sold for a premium (key money) to the final leaseholders. The significance of the premium is that it attaches a value to the leasehold that tends to attract capital growth on resale. The relative magnitude of the premiums tends to give the leaseholds something of the character of ownership rather than tenancy. This is further emphasised through the relative diminution over time of the real financial significance of the rental payments.

Informal tenancies direct between customary landowners and tenants are especially evident in peri-urban squatter settlements. These quasi 'squatters'³⁶ are often present under the explicit approval of the customary landowners and often pay a rent directly to them. The lack of consistency, security, and market regularity make these arrangements dubious, but they have tended to flourish.

The *Abi* residential project adjacent Lae City is an excellent example of a strategy for moving out of the informal mode of settlement. By providing formal leases over recognised parcels of land, occupants can enjoy a level of social, spatial, and financial security that is not available in prevailing informal settlement arrangements. Social control will be more likely because there will be a clear line of relationship with the customary landowners who will take the role of superior landlord in a traditional sense: applying a level of customary authority over the settlement that is better aligned with traditions and likely to encourage better behaviour amongst tenants.

The prospect of regularising rents raises the possibility that additional expense may have repercussions on tenants, who have been in the habit of living on a lower budget. This would suggest that at least initially, the level of services and rents would need to be modest and aligned to the resources and needs of the tenants.

The National Land Development Taskforce

PNG has recently undertaken a major initiative known as the National Land Development Taskforce aimed at addressing the need for an efficient and effective public land administration system. Building on National Land Summits in 2005 and 2006 (Webster *et al.*, 2006), the goal of the initiative is to encourage common

³⁶ The term 'squatter' has been commonly misappropriated in the context of informal settlements. The occupiers are not legally 'squatters' in that their occupation is usually condoned by the customary landowning group and there is usually some form of informal rental arrangement.

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understanding, cost effectiveness, transparency, accountability, certainty, and acceptance of land reform in the country.

The National Land Development Taskforce comprises key leaders and experts in land administration in PNG, under the leadership Dr Thomas Webster the Director of the National Research Institute. It carried out an extensive investigation into land tenure and administration leading up to the publication of the National Land Development Taskforce Report (Webster *et al.*, 2007). Its work was divided between committees focusing on Land Administration, Land Dispute Settlement, and Customary Land Development. It developed a comprehensive summary of land administration and development in PNG along with recommendations on improvement. Many of its recommendations relate to administrative matters; however, several deal with fundamental issues pertaining to the effective financial utilisation of customary land. Its principle recommendations with respect to land administration included:

- > Customer relations and data storage/access need improvement;
- > Accountability: staff need to be more responsive and accountable for performance;
- > Information systems: integrated, accessible and reliable data systems need to be developed;
- > Rent collection is faulty due to reappraisal backlog, poor recording systems and inadequate regulation regarding rent default;
- > Valuation: Valuer General's department needs to be strengthened to meet commitments and the land tax system needs re-examination;
- > Physical planning: capacity needs to be increased through additional staff and relationship with land administrators needs improving;
- > Surveys & mapping: Modern equipment is required including digitising capacity;
- > Land Administration: procedures need refinement and codification with an emphasis on better relationships with stakeholders; degree course for land administrators needs revision and a professional body needs to be established;
- > Title Registry: title data systems need improvement;
- > National Land Board (NLB) An open auction system of land allocation is recommended to replace LNB;
- > Special Projects Unit: responsibilities to expand; and
- > Staff Training: need to educate.

The National Land Development Taskforce reflects a broad based intention to improve land administration and its recommendations are solid. They do not necessarily directly target the effective financial utilisation of customary land, though many of their recommendations will be genuine improvements.

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Rental Issues

Rent Determination

Rents for customary lands are initially set as part of the lease and lease back origination of leases over customary land. Customary land is leased to the government for a set rent and then leased back to the customary owners at the same rate. The customary landowners may then assign (sell) the lease to tenants. The rent and terms of leases are therefore set by the government, but the leases are usually sold on from the customary landowners to tenants with a premium payment. This is not set using any transparent formula and the capital appreciation of the premium is not tracked in accessible public records. This means that while rents are determined through a standardised valuation process, the real income to landowners is invisible to the community. It is likely that the total payments to landowners is effectively a practical market rent in its own right, though it does create some contingent problems.

The setting of rents on lands leased from customary landowners is one of the duties of the Lands Department. PNG has a State Valuation Office operating within the National Lands Department, as well as a small private sector valuation profession. An estimate of the number of valuers is quite small, variously suggested to comprise some 60-100 urban valuers but only about 10 rural specialists. Since much of the customary owned land is rural, it is evident that PNG is seriously undersupplied with rural valuers.

Whilst valuation approaches generally conform to standard internationally recognised methods, this is not adequate for the needs of the country where land is predominantly in customary ownership. In particular, the estimation of lease rentals appears less than convincing due to reliance on the UCV method that was developed in a predominantly freehold environment. The estimation of UCV appears to be almost totally notional due to the absence of sales and the selection of 5% as the universal yield rate for the country is problematic. UCV does not appear to be computed with adequate attention to permitted land use. In markets where rents can be computed from yields applied to UCVs it is recognised that planning permission and geographical factors substantially effect both the UCV and the appropriate yield rate. As a result, rentals to customary landowners appear well out of line with evidence available within the local property market itself. The following evidence illustrates some of these problems:

- > In one case in Boroko, Port Moresby, a leasehold commercial site, currently vacant, apparently has a lease sale (key money) value in the vicinity of K4,000,000 (about AUD2,000,000) yet only K2 p.a. is paid to the customary landowners;
- > The methods used to value rural land for rental determination use a notional unimproved capital value, effectively an unimproved land value, yet there is no market for the sale of this type of land; and

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- > A capitalisation rate of 5% has been adopted for land valuation across PNG, even though there is no factual market basis for its adoption.

Very little research is available on valuation methods appropriate to the PNG context, or indeed the Pacific in general. The Department of Lands and Surveying at the PNG University of Technology offers the only education route in the country for entry into the property valuation profession. The local valuation profession is of the opinion that university courses are not preparing valuation students adequately for the challenges of the prevailing local property right conditions. Discussions with the local valuation profession reveal several problems with the local property industry, including:

- > Lack of experienced valuers;
- > Low standard of valuation reporting;
- > Lack of knowledge of different types of valuations (e.g., Hotels, high rise buildings or investments properties, specialty use properties);
- > The PNG Institute of Valuers & Land Administrators are not working affectively to support the professions. Changes are required to the Land Act to allow the PNGIVLA to have some legislative powers and responsibility for the professions;
- > PNG valuers would benefit from practical training done in Australia with private valuation firms or Australian Valuation Office in order to upgrade their knowledge on all different types of valuations;
- > Only 3 valuers are known to have professional indemnity (PI) insurance;
- > Some valuers are under quoting on fees;
- > Some companies in PNG are still engaging valuers from Australia;
- > Some valuers are not submitting tax returns;
- > Valuers are not investing in continuing professional development such as participating in valuation conferences; and
- > There is only one plant/equipment valuer in PNG, as the result of me attending the practice certificate course arranged by API in Sydney. There is inadequate capacity in PNG in this area.

There is a need to strengthen the local profession in order to raise the quality of rental determination. This can only be done if resources are directed into the valuation profession to enhance capacity in education, professionalism, and continuing professional development.

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Rent Collection and Distribution

Distribution of rents amongst the customary landowner community is a matter for the customary landowners themselves. It is not overseen by the state. The major difficulty with leases over customary owned land is identifying the customary landowners. The development of the Incorporated Land Groups sought to regularise this by creating an entity that represented customary landowners for particular parcels of land. The construction of ILGs is left largely up to the customary landowners themselves, however once an ILG is registered for a particular parcel, the ILG can lease the land and act as a landowner, even if dispute exists over the validity of the ILG membership.

Rent Monitoring

Optimally, rents should be reviewed at intervals between three and seven years, depending on the type of land use. In practice, review intervals have been longer due to human resource shortages. This creates a problem when rents do change as the jump in rental is often considered too great and is resisted by tenants.

Compensation Arrangements

Compensation for the value of undepreciated improvements at the termination of leases is not explicit.

Transparency

There are no registers of secondary lease assignments, so the value of the premiums that attach to lease transfers is not publicly available. The publicly available rental and lease data is incomplete being only part of the payment structure. In addition, the absence of records on the growth of premiums obscures the relationship between rents to customary landowners and market values.

Inter and Intra Generational Issues

Persons landless through intermarriage

Like other parts of Melanesia, PNG is notable through the mixture of patrilineal and matrilineal traditions of customary landownership transmission. Each system has its own particular advantages and shortcomings and it is not the purpose of this report to comment on their relative merit. The significant aspect of them from a financial management perspective is their capacity to either double or negate family rights to customary landownership depending on the combination of transmission traditions with the spouses to a marriage (Table 9). The main issue is that permanent customary rights are not necessarily passed on through a 'mixed blood' marriage.

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TABLE 9: PROPERTY RIGHTS AND LINEAL ARRANGEMENTS

		Husband	
		Patrilineal	Matrilineal
Wife	Patrilineal	Property from husband's clan	No customary rights
	Matrilineal	Property from both	Property from wife's clan

The problematic situation is that which leaves the family with no customary property rights over land. This makes it very difficult for these families to remain within their traditional clan system and discourages people caught in this situation from identifying with their traditional culture and customary systems of landownership. Currently this problem appears to be only beginning on any substantial scale, but the children or subsequent generations of disenfranchised people will possibly form a group within the society with very different views regarding the merits of customary landownership. This may have future political implications for the long-term sustainability of effective financial management of customary owned land.

Leasing for Commercial Use

Customary land is available for leasing for commercial purposes, both in rural and urban situations. There is debate over the distribution of incomes between customary landowners and the government (Curtin, 2004).

Inter and Intra Generational Conflict over Commercial Land Use

Several instances of inter-generational conflict exist, and there is evidence that the current structure of leases and values will be the cause of conflict into the future.

In every town in PNG, there are claims for *ex gratia* payments from alienated customary landowners. These are grounded on historical perception that the payments of the alienation of the land to the state to become freehold was too low and that current descendants of the customary landowners should be retrospectively compensated. The Port Moresby Jackson's airport claim is one illustration of this type of claim. While the government is currently countenancing these claims, it is taking the view that these *ex gratia* payments will completely extinguish the customary interest. However, the logic of the situation suggests that this will be unlikely as the original payments were intended to achieve this. The matter has more to do with the cultural misapprehension of absolute sale.

Conversely, analysis of urban property values suggests that the effective financial interest of the customary landowners has diminished considerably compared to the market rent of the underlying land (see Table 10). Whilst the private rental market in the towns and cities appears to be reasonably developed, it is not well connected to the rentals paid ultimately to customary landowners, as indicated by the data from

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Tougaguba Hill and Gerehu/Hohola. This suggests that the head lessees hold about 80% or more of the ground rental that is due to the customary landowners. Over time, the growth in this profit rent (the gap between the rental charged and the rental paid by a superior tenant) appears to grow relative to the rents to the customary landowners, giving rise to conflict.

TABLE 10: COMPUTATION OF RELATIVE INTEREST IN LAND BETWEEN CUSTOMARY LANDOWNER AND HEAD LESSEE IN SELECTED PORT MORESBY SUBURBS

		Tougaguba Hill	Gerehu /Hohola
		Upper class area	low cost area
Rental range of rentals on leases to state	K p.a.	3,000	100
	K p.a.	4,000	500
Mean adopted	K p.a.	3,500	300
Deduced UCV interest to customary owners (@ 5%)	K	70,000	6,000
Private rental furnished	K p.w.	1,800	500
Private rental annually	K p.a.	93,600	26,000
Deduced rent for improvements	K p.a.	76,988	21,484
Deduced private land rental	K p.a.	16,612	4,516
Deduced private land interest	K	332,248	90,315
Ratio of customary interest to private interest		21%	7%

Dispute Resolution Mechanism

The courts system provides the basic channel for formal disputes over land, but it is expensive and slow. Village courts are available at the local level and have the advantage of being less formal and expensive and income cases they promote informal dispute resolution. The primary source of conflict is uncertainty over customary landownership. As land becomes ripe for commercial use its value increases immensely and vagaries of ownership that were tolerable within traditional society erupt into disputes over the allocation of rental income. The ILGs were intended to resolve this, though in practice they only quarantine disputes away from tenants. The aspiration of the National Land Development Taskforce in respect of land dispute settlements is to establish a separate single land court system – amalgamating the functions of the Land Titles Commission, the National Lands Commission and the National Land Court system currently under the magisterial services (The National, 2007, citing Dr Thomas Webster from NRI).

The development of a register of customary interests has been suggested, but there are also considerable practical problems. A considerable amount of work was done in the late colonial era that involved physical survey, the placement of survey monuments (“cements”) and the development of registers of customary landowners.

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These records have not been formally gazetted, though in many areas they are relied on in practice as the most reliable historical records of the understanding of ownership a generation (c.1960) ago.

A second source of conflict concerns peri-urban informal settlements. These are informal occupancies on the fringes of towns over customary land. Usually there are informal rental payments, but the uncertainty of tenure and informality of the occupations create a number of financial, infrastructure and social problems. It is generally held that the consistency of rents and the real willingness of customary landowners to host these settlements are doubtful, though they tend to persist through recent local custom more than any substantial tradition or public policy. The nature of the conflict in this arena is very informal and deserves specific attention.

Lending to Property Development

Westpac and ANZ have a major presence in PNG. ANZ is committed to developing its impact at lower levels in the community and has developed a series of educational publications to help indigenous people understand saving and borrowing using the bank for personal and commercial purposes. Westpac is likewise aware of the importance of educating the wider PNG community towards understanding to mechanics of saving as a precursor to more complex business arrangements.

A major problem in PNG is the limited level of financial education amongst the population. This is largely the result of traditional life not requiring the use of money and the low level of reliance on money in contemporary village life. This unfamiliarity often leads to a lack of understanding regarding the importance of saving and the consequent inability to manage debt and operate the financial side of commercial operations. The practical result is inability to attract debt funding for productive enterprises.

Some commentators have suggested that the problem with accessing debt relates to ineffective title to customary lands as collateral. This claim ignores the reality that customary people, largely, lack financial management skills that are at least as critical in assessing credit worthiness for a prudent financier. The banks approached were equally dismissive of the proposition that quality of title was the primary reason inhibiting lending to customary people.

Both banks share a common approach to lending to land related projects. They do not lend against the security of land in the way that lending is done in countries like Australia. Instead, they lend against the anticipated cash flow that will be generated through developed use of the land, emphasising the importance of the business acumen of the borrower. This is an important distinction as it recognises that although the land is pivotal in forming the basis for productive businesses, it does not have a useful rental or sale value in the absence of the businesses carried out upon it.

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This means that the primary requirement for accessing debt capital is a convincing presentation of the borrower's ability to use the funds with commercial effectiveness. This leads to confidence that a satisfactory pattern of cash flows will be generated sufficient to adequately cover debt service obligations and entrepreneurial objectives. This is consistent with the fact that the land, absent of the business, has low intrinsic worth. This does not mean that the land is irrelevant, but rather that it represents merely the spatial location of the productive business for which funds are sought.

Through this approach, the banks are merely reflecting themes in commercial lending practice elsewhere, such as Australia, where loan approval a risk minimisation exercise dependent on confidence in future cash flows rather than in hard assets. A related important aspect of their position regarding land is their insistence on sound leasehold titles available as security. While the value of land might be low, title to it does secure rights to the business that it developed upon it, especially when it involves agriculture. Both banks expressed willingness to lend against state recognised leasehold titles. They did not indicate any necessity for freehold title for landing purposes. Equally, they did not admit leases or other proposals for land rights as loan security, that were not in a form that would be supported by the state. In PNG, this predominantly means land leases that have been formalised through the lease - leaseback system.

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COUNTRY CASE STUDY: NEW ZEALAND

Rental Issues

Typologies of financial management arrangements / systems

The holding of land in New Zealand whether customary or other land is subject to the provisions of Te Ture Whenua Act 1993 (TTWA). This legislation has its roots in the Treaty of Waitangi which established the broad relationship between the British Crown and the colonised inhabitants the Māori. The abrogation by the Crown of its beneficial title only relates to that class of land holdings which is either Crown land or General land which has been alienated from the Crown's beneficial title.

Apart from the above two tenures, four other tenurial classifications are established by s.129(1) of TTWA, namely Māori customary land, Māori Freehold, general land owned by Māori (other than Māori Freehold land), and Crown land reserved for Māori. The typologies of management regimes which have been established to deal with the above six classifications of land essentially reflect the dyschronous (separate in time) nature of the dual ethnic tenures which have been created under TTWA.

Very little of the surface area of New Zealand remains Māori customary land, and it is argued by Phillip Green, Barrister at Law acting for the Wellington Tenth that this land classification probably amounts to between 2-3% of the North and South Islands.

Over 95% of Māori rights and interests in land under TTWA are held as Māori Freehold. The Māori Land Court determines under the TTWA those lands which are to have the status of Māori Freehold land.

Since so little land is held as Māori customary land, most Māori landholdings are obviously Māori Freehold land, and hence this is where the focus of financial management arrangements/systems are focussed.

Rent Determination

The former Deputy Māori Trustee Richard Wickens of the Māori Trust Office, Wellington, advises that the trustee role of his Office has significantly declined with the compensation settlements that have emerged from the settlement of Māori claims in recent years. There is obviously a continuing need to manage lands by the Māori Trust Office, and these are generally undertaken on the basis of a typical ground rent arrangement.

However Mr Wickens, who is now a Project Officer with the Māori Trust Office, (having retired as Deputy Māori Trustee) strongly suggests that the overarching focus of financial management of Māori interests is on investment directly by Māori corporations on either Māori Freehold land, or importantly, on general Freehold

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land. This may have been alienated from the Crown for many years and may have been held by non-Māori owners.

Equity issues

The settlement of substantial Māori claims over recent years notably the widely publicised Waitangi Tribunal 1992 Fisheries Settlement Report (Boast *et al.*, 2004, s.2.2.6) and the subsequent National Fisheries Settlement Deed (Sealord Deed) has resulted in funds which arguably amount to in excess of \$NZ2 billion flowing to the Māori population according to Phillip Green.

Green further points out that the Māori population currently sits at somewhere between 16 – 18% of the overall New Zealand population of 4 million, and the compensation income stream has substantially changed the dynamics between Māori and non Māori in New Zealand.

Both Green and Wickens note that the Māori population now includes individuals with significant skill sets in disciplines such as law, accountancy, agriculture management, and particularly high level financial risk assessment. As a result investment of these huge compensation funds have been increasingly directed towards enterprises which are not necessarily associated with Māori Freehold land, and almost none are involved with Māori customary land holdings.

Increasingly the decision by Māori interests to invest their funds in profitable enterprises are resulting in endeavours which are located on general freehold land, with entrepreneurial and debt funding partners who may or may not be Māori or non Māori New Zealanders. Indeed, there is increasing anecdotal evidence that the decisions by Māori investors may well involve partnerships with foreign intermediaries who may be entrepreneurs or debt funders.

The experiences of Māori with foreclosures of Māori Freehold, notably the well publicised foreclosure of land block *Matauri X* in Northland, has resulted in a reassessment of investment decisions by Māori. The *Matauri X* debacle and other collapses (Durie, 2005, p.64) resulted in Māori landholdings being alienated from the traditional owners' control, and confronted Māori with the unpalatable prospect that investment decisions have a concomitant risk of unwitting potential dispossession.

All of the above has clearly been traumatic for Māori people according to Phillip Green, and it is instructive to note that current moves by banks and financial institutions away from debt funding to equity funding is in direct contrast to current Māori thinking.

Whilst Māori do not have difficulty with sharing the equity in a business venture or even sharing the property rights in a leasehold interest with an equity partner, the alienation even partially of the underlying landholding appears to now be problematic. Dr Tanira Kingi states that such funding approaches by the NZ banks and financial institutions would be looked at askance by Māori.

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Using Māori land as legal security

This section analyses cultural considerations on the capacity to raise debt and / or equity funding using Māori land as legal security. Restricted access to finance (debt or equity) is a major constraint for the owners and administrators of Māori land (Kingi and Maughan, 1998; Drummond, 1999; Kingi, 2000; Durie, 2005). A number of reasons exist for this problem including an increasing number of owners to fixed parcels of land (multiple-ownership) and the absence of an open land market owing to the alienation clauses of the current legislation that restricts alienation to landowners or those affiliated to landowners through marriage. Additional factors include the large number of blocks without a management structure, or where there is a management structure, the lack of committee members or trustees with commercial expertise and the knowledge of the requirements regarding access to finance (New Zealand Institute of Economic Research, 2003; Māori Land Tenure Review Group, 2006).

The situation is exacerbated by the low number of financial institutions with experience and information about the opportunities existing with Māori land organisations and within the current Māori land tenure administration system. Government initiatives have attempted to address these problems by offering pre-commercial facilitation services that assist landowners (or trustees/committees of small land blocks) to prepare business cases to strengthen loan applications and programmes to build governance capability within the organisations (Office of the Minister of Māori Affairs, 2006). Capacity issues are less of a constraint with large incorporations and trusts that have a commercial track record, sound relationships with financial institutions and alternative collateral i.e., assets other than Māori land.

A more pervasive issue with raising capital against Māori land that is common to both small and large Māori land organisations are the multiple viewpoints of the landowners. While a single 'Māori world view' does not necessarily exist in contemporary Māori society, there are several commonly-held values that influence decisions (Marsden, 1975; Marsden, 1992). A common theme that emerges in relation to the attitudes and values of Māori landowners is a consistent conservatism when it comes to using the land as collateral and therefore placing the land at risk. There are a number of aspects to this conservatism:

- > Where the trustees or committee members lack commercial expertise, the Māori landowners may perceive the likelihood of loan default as unacceptably high, even though the finance institution is satisfied that all requirements are met;
- > The lack of business experience among Māori landowners may view the carrying of debt or equity liability, no matter how small, as unacceptable even though the organisation has more than adequate capacity for the debt to be serviced;
- > Land that is the remaining area of land lost through Crown confiscation or illicit land sales creates a particularly sensitive issue for the landowners. For many

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Māori land retention is the paramount concern (and one of the key platforms of the TTWMA) and any activity that degrades the land or places it at risk is unlikely to be supported; and

- > Land has a particular place in the mythology and cosmogony of Māori that influences the values placed on its use and in particular its use as an economic instrument.

Both Wickens and Kingi confirmed that the move by banks and financial institutions away from debt funding to equity funding would present major problems culturally for Māori people.

Guardians and Administrators

Māori creation stories are widely known and have been popularised in New Zealand mainstream society (e.g., *Rangi* – sky father and *Papa* – earth mother). Strong attachments to land is common across many cultures, such as the affiliation felt by the fourth and fifth generation descendents of the early Scottish settlers toward their South Island high country stations. Māori on the other hand have a distinct attachment to the land that is based on a genealogical (*whakapapa*) connection to *Tanenuiarangi* – one of the *atua* or children of *Rangi* and *Papa*. This particular *atua* holds a special place in Māori cosmogony as the creator of humankind along with forests and birds. Therefore, according to Māori mythology humans have a genealogical connection to trees and birds (the only fauna in pre-European times).

Although the ability to recite the genealogical lines of individuals to show the family and tribal linkages is relatively common among certain Māori community leaders, tracing the genealogical linkage beyond human ancestors to mythological forefathers is known only to a very small number. The lack of specific knowledge however, does not stop this genealogical connection being commonly referred to in everyday Māori phraseology. This connection underpins the traditional *kaitiakitanga* (guardianship) role that Māori have in relation to the land and natural environment, being entrenched in the Resource Management Act 1993. The dual roles of guardian and commercial administrator of land can be the cause of conflict for Māori landowners. Juggling multiple objectives – commercial and cultural – often leads to conservative decision-making including the reluctance to place the land at risk – whether for debt or equity financing.

Market based

The ground rents that are calculated by the Māori Trust Office are obviously based on the value of the land presumably as general freehold equivalent, given that the land is to be utilised for some income earning purpose. There is substantial case law which supports this approach in particular *Geita Sebea v Territory of Papua* (1941) 67 CLR 544 which indicates that the value of land by the party utilising it can be distinguished from the value of the land in the hands of the traditional owners.

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Whilst this case pertains to compensation, it is a recurrent theme when addressing the value of land in circumstances such as those encountered by the Māori Trust Office. The value of the land in the hands of the customary landowner arguably becomes irrelevant to the calculation of a ground rent when the land is to be used by a party who is not associated with the subject land, such as an intending commercial occupant.

Regulated rents

This appears to be an aspect of rental calculation that is broadly irrelevant to the New Zealand experience.

Rent collection

In those cases where the Māori Trust Office is administering Māori landholdings, rent from tenants is collected by the Office or by agencies employed by the Office for this purpose.

Rent monitoring (review procedures)

Most rents gained by Māori are on commercial terms. Depending on the nature of the enterprise being conducted on land controlled by Māori, will be structured in accordance with the industry expectations. For example, if Māori land is being occupied for the purposes of long term retail development, such ground rent provisions would be firstly subject to confidentiality provisions, and secondly it can be anticipated that they would include a turnover impost (overage) calculated on retail turnover.

Enforcement of land rent payment

Normal commercial terms for re-entry apply.

Compensation, if any, of tenants and / or landowners, at expiry of land leases for improvements and or deterioration of State or customary owned land

Generally, the issue of compensation is not relevant at the expiration of leases because tenants are required to leave improvements unless the lease stipulates under normal commercial terms that certain fixtures and fittings are the lessees possessions. In the event of dispute between the parties regarding the definition of improvements *vis à vis* the personal property of the tenant, adjudication clauses in the lease will be activated.

However, the issue of compensation can be clouded by the uncertainty that still surrounds how Māori freehold land is to be valued, especially where the valuation forms part of termination arrangements between the tenant and the landowners. For example, it is known that improvements to land by a tenant can upon the cessation of the lease, involve a payment in part to the departing tenant for the increase in

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value of the land. Whilst not common, such provisions in leases raise the issue of just how Māori freehold land is valued.

The literature suggests that the traditional heads of compensation of special value to the owner and *solatium* are capable of being interrogated and expanded to assist the valuation of Māori customary and freehold lands. Such an approach could, for convenience be described in a manner analogous to the methodology suggested by Boyd (1995; Boyd, 2000). Where customary or reserved Māori land is considered to be incapable of alienation, Boyd ascribes it with a value type known as Non-Market Valuation (VNM). The second classification of native land, namely Māori freehold land is only transferable within the cultural group and is ascribed a value type known as Restricted Market Valuation (VRM).

However, Boyd does not provide practical guidance as to how the value types VNM and VRM are to be deduced. This view is also reflected in other rare commentary on the search for a native title valuation methodology, such as for compensation for the expropriated communal tribal lands in South Africa, Terblanche noting that, “[e]stablished and accepted valuation approaches do not offer a tailor-made method to deal with this property. It could be reasoned that, because the expropriated party received market value for the property, there exists no need for further compensation. This, however, cannot be accepted because the expropriated party was limited in respect of what it could do with the money received for the expropriated property.”

Importantly, Terblanche notes that, “...the foundation for compensation was the loss of growth that any person experienced; where the sum of the loss of the growth is the difference between the present value of the expropriated property and the present value of the compensation that the expropriated party received.”

It can be seen that Terblanche is proposing that an additional amount of compensation above market value should be paid to tribes who have been dispossessed of their traditional communal lands and land control system. In a subsequent personal communication with John Sheehan on 27 January 2004, Professor Terblanche confirmed that his views expressed in the 1996 article remain unchanged. Indeed, he strongly suggested that the recognition of spiritual and cultural values must occur in the valuation of indigenous lands for the resultant compensation to be truly representative of the bundle of indigenous rights and interests residing in land.

In sum, the views of Boyd and Terblanche support the view that Māori customary and freehold lands ought to be valued in a manner reflecting their spiritual and cultural worth as well as utility.

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Distributive justice - Systems used for benefit and cost sharing within land owning groups, including trust funds

The corporate structures which have been constructed by Māori people in recent years are effectively indistinguishable from companies established under New Zealand corporate law. Indeed, the corporate governance requirements are such that Māori investment endeavours are subject to the same prudential requirements as non Māori investment endeavours.

Phillip Green observes that trusts are created for the ongoing investment of profits from Māori enterprises, but these appear to be structured in a manner indistinguishable from usual trustee arrangements.

Transparency

Given that the increasing focus of Māori investment is on general freehold land and now less on Māori Freehold, the demands of corporate governance are such that leasehold arrangements with commercial partners, fund raising agreements, and of course profit sharing arrangements must be fully transparent. As Wickens points out, leasehold arrangements between Māori controlled corporations and entrepreneurs are now increasingly commonplace.

The due diligence requirements of such leasehold arrangements especially when an integral part of a profit focussed enterprise, are such that transparency is a given.

Inter and Intra Generational Issues

The investment by Māori is undertaken increasingly by corporations, and the relevant Māori community is, from the beginning, the beneficiary of the profits and other benefits generated by the corporation in the same manner as share holders of public companies. Indeed it is arguable that such Māori enterprises in 2007 are effectively indistinguishable in operation to similar non-Māori enterprises.

Cost sharing from the use of customary land

The sharing of costs arising from the use of customary land is always an issue of shared responsibility. In New Zealand the debacle in Northland where Land block Matauri X was foreclosed by the debt funder, presumably all of the Māori landowners were caught by the short fall in the sale of the land according to the description by Durie (2005, p.64).

Whether all of the Māori might have been holders of common rights and interests in this land is unknown. However, this subtlety in the dispersal within Māori groups of rights and interests has only recently been highlighted by an Australian decision in the Federal Court. Lindgren J. found on 5 February 2007 in *Harrington-Smith on behalf of the Wongatha People v Western Australia (No.9) 2007 FCA 31*, that the customary rights and interests in land held by the Western Desert Cultural Bloc Society (BDCB) could be recognised at an individual level. He took the view that the

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Native Title Act 1993 (Cth.) (NTA) at s.223(1) allowed him to form this view because it revealed, “a taxonomy of the kinds of native title recognised by the NTA: communal, group and individual. The community, the largest possible native title owning entity, is in fact the society whose laws and customs are in question. The group is smaller, and will ordinarily have a fluctuating membership (so, of course, will the community). The individual is the smallest possible native title owning entity.”³⁷

This view of customary rights and interests in land is also supported in an earlier case *De Rose v South Australia* (2003) 133 FCR 325 at [25] - [50], and also in the view of Sundberg J. in *Neowarra v Western Australia* [2003] FCA 1402 at [391], also the views of Beaumont and von Doussa JJ in *Western Australian v Ward* (2000) 99 FCR 316 at [160]-[161] and [239].

Given that the Canadian Supreme Court, and the Australian High Court and Federal Court inform each other on matters relating to indigenous rights and interests, the importance of the decision of Lindgren J. cannot be overstated. It has an impact far wider than the Australian legal milieu and given that many Pacific nations share a common law heritage with Canada and Australia, the decision by Lindgren J. has considerable weight.

Broadly speaking where rights and interests in customary are asserted by a group, that group must possess those rights and interests on a collective basis according to a recognised body of traditional laws and customs. Such a body constitutes a normative system, however individuals clearly can assert specific rights and interests in relation to some lands, notwithstanding that the actual customary title to the land is in the possession of and control by the group.

Lindgren J. was at pains to consider whether the individual specific rights could form an identifiable separate cohort of rights and interests, which in themselves could be ascertained, and presumably assessed for their worth (compensation?). The decision in *Wongatha* raises the distinction necessary between the content of an individual’s customary rights and interests in contrast to other individual’s rights and interests in a communal customary title. Indeed, the question was posed as to whether such individual rights and interests can be held independent of a concomitant collective holding of rights and interests at the group or even communal level.

Finally, the issue arises of whether specific individual customary rights and interests can survive when customary rights and interests of a larger social grouping have not survived. On this latter point, it is interesting that in *Wongatha*, Lindgren J. found that larger local groupings did not exist beyond a compendium of individual, presumably related generic assertions which together formed a collective entity.

³⁷ Lindgren J. in *Harrington-Smith on behalf of the Wongatha People v Western Australia* (No.9) 2007 FCA 31 at [1129] - [1165], and generally at [495] - [1042]

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The decision in Wongatha reveals that native title rights and interests in Australia and by analogy customary rights and interests in land elsewhere in the Pacific in common law countries have a level of complexity which was hitherto unknown to outside observers. Until Wongatha, the legal notion was that all customary rights and interests in land were held for the purpose of *commune bonum* (a common good), and hence as a proprietary interest in land having an overarching quality of communality rather than individuality. It was very comfortable for common law property theory to only consider customary land as something akin to the common property in a strata title. Wongatha suggests that this is an incorrect assumption, and that customary rights and interests must be considered at the communal, group, and individual levels.

This is fairly disturbing as the financial implications of Wongatha quickly reveal that any equity or debt raising over customary lands, must recognise that not all members of the 'ABC clan or tribe' will necessarily have equal legal interests in the particular customary land. Whether the clan or tribe is Australian indigenous, Māori, Fijian, Samoan, or in PNG does not really matter. What is of concern is that an individual or cohort of individuals may have discreet rights and interests in land which are not held by other members of their group or even community.

Clearly given the decision in Wongatha, not all of the Māori in the *Matauri X* foreclosure would have necessarily been holders of rights and interests in common in the land. As stated earlier this complexity was not fully understood until the Wongatha decision, and the sharing of costs and obligations from the use of customary land whether is be Māori customary, or Māori Freehold demands a more circumspect consideration.

Leasing for Commercial Use

The leasing of Māori landholdings, primarily Māori Freehold is undertaken on commercial terms for commercial use. The leasehold arrangements covering conditions, rental, lessee and lessors obligations, options for renewal and arrangements for determination of release are drafted in normal commercial phraseology.

This is particularly true of those leaseholds that are on general Freehold, which is owned by Māori.

The role of financial management arrangements / systems in recent land based conflicts and conflict management

The Northland foreclosure and others have resulted in an approach by Māori which is based on a more robust risk analysis of investment proposals. Coupled with this risk adverse approach, Māori investment is focussed on leasehold of their lands jointly with other investment partners.

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The conflict and division arising from the foreclosures have been directly responsible for a more circumspect view being taken by Māori of future investment decisions. Arguably, the flow of substantial compensation funds has permitted Māori to move beyond investment on Māori Freehold and onto general Freehold, which is in any event the largest single land tenure in the country.

The professionalism of Māori investment in the broader sense has acted to resolve the earlier land based conflicts.

Dispute Resolution Mechanism

Arriving at acceptable decisions

As stated earlier the increasingly preferred mode of financial management of customary lands and other lands under the control of Māori is by way of firstly direct investment by Māori corporations, or secondly through joint ventures with entrepreneurs and debt funders.

A recent example is the joint venture between Taranaki hapu Ngati Te Whiti and Greymouth Petroleum to develop oil and gas reserves off Port Taranaki near New Plymouth. The oil reserves within the tribal area have been estimated to provide 200 barrels of oil per day amounting to approximately \$NZ100 million for a 20 year production cycle at current prices. The joint venture is based upon the non Māori partner Greymouth Petroleum holding 98% of the mining licence with Ngati Te Whiti holding the remaining 2%.

Developmental funding for the joint venture is currently undertaken by the majority licence partner, however Nga Te Whiti will be required to contribute funds if mining and production subsequently occurs (Ray, 2007). The Port Taranaki oil field development reveals how Māori are undertaking joint ventures which will provide and income stream over many years, but not threaten their traditional land holding. In this example, the tribal lands of Ngati Te Whiti are only subject to a mining licence, which is the collateral base for current and future funding. Such investment decisions are acceptable because the Māori landowners obviously do not feel that their land based culture can be threatened through a foreclosure. This important development has significant ramifications for PICs.

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