Rodney L Jefferies
12 Henley Way
Tauranga 3112
New Zealand
+64 27 2489950

e jefferie@maxnet.co.nz

To: commentletters@ivsc.org 12 February 2014

Comments on IVSC Exposure Draft

Development Property Exposure Draft

The Commentator:

The commentator has recently retired from Lincoln University's property research and teaching staff. He is currently completing his PhD research into investment valuation methods.

He is the author of the New Zealand chapter in the Appraisal Institute's global valuation text in H. C. Gelbtuch & E. H. Park (Eds.) 2011 Real Estate Valuation in Global Markets (2nd ed., pp. 310-336) Chicago, IL: Appraisal Institute).

Comment on Questions:

Question 1: Yes.

Question2: Yes.

Re **Introduction and Scope**

Question 3: No.

The following bullet point should be added at the beginning of the list under para 1.:

- the development of previously undeveloped land by subdivision into serviced sites for separate building development,

The following bullet point should be added at the beginning of the list under para 2.:

- sale and purchase negotiations,

Comment: The above bullet point is all encompassing and all that is required. Retaining the existing bullet point (• acquisitions, mergers or sale of a business or parts of businesses) is superfluous. In practice the valuation of development property is normally not part of a business. If it were, then the normal basis of value and methodologies establishing its market value would apply, unless there was some special value attached to the purchase, such as being an adjoining property.

The following bullet point should be added at the end of the list under para 2.:

- Property taxation and/or rating.

Re **Definitions**

The following definitions in the table under para (5) require amendment:

Development property: the words "of improvements" should be added in the second line, immediately before the words "is contemplated,"

Residual Method: the following words "and profit expected to be made and compensation for development risk to be undertaken" should be added immediately before the words "in order to achieve that value."

Re **The Existing Asset**

Question 4: In the first bullet point under para (7) the following words "environmental consents," should be added in the last line immediately before the words "or constraints on permitted development;".

The following should be added as an additional bullet points:

- any constraints due to historic places designations,
- the risks associated with the proposed development and marketing required for which compensation as an allowance for profit and risk is required. (i.e., as in para (19).

Re **Valuation Basis**

Re para (11): the word ", infrastructure" should be added immediately after the word "building" in the second line.

Re para (14) the words ", and/or required rates of return" should be added to the last line immediately before the words "may be appropriate."

Re **Market Approach**

Question 5: Yes, however an additional paragraph following para (17) under the Market Approach is suggested as follows:
"The market approach may be appropriate in establishing completed realisation values, in a residual approach, e.g. estimated sale prices of individual units, sites, building(s) or real property interests to be marketed on completion."

Question 6: Yes, para (21) and (22) are sufficient as stated.

Re **Income Approach**

Question 7: The following inputs should be included under para (24):

Lease agreements — Add “where lease agreements are yet to be negotiated, suitable allowance for leasing costs, incentives, and anticipated vacancies that may extend beyond the estimated completion date need to be allowed for”.

Add “Realisation sales forecasts and costs — where a development property’s value is dependent on sales of building sites, completed building units, or separate buildings following the completion of the development, the forecast timing of sales and associated holding costs and selling costs need to be allowed for as well as unrecoverable operating and service costs.”

Add “Long-term liabilities — long-term liabilities retained by the developer, such as long-term covenants, bonds, maintenance costs, environmental and/or contamination liabilities, etc., that cannot be transferred to another party requires quantification and allowed for as from completion of the development.”

Re clause (e) Finance costs: the following sentence should be added: "Such finance costs should be forecast until all development costs have been recovered, either by full occupancy of the completed the buildings, or all development units and/or sites sold."

Re clause (f) Consultants' fees: the following should be added. "Separate selling and marketing costs should be allowed where post-completion sales are forecast."

Re clause (g) Buyers profit and risk: an additional paragraph is required under this heading as follows: "Where an income approach under paras (20 to 23) above uses a DCF method, care should be made to distinguish between the profit and risk elements, especially where a percentage profit on the cost method is applied. See also discussion under para (25) below."

Re **Residual Method – Discount Rate**

Question 8: Additional matters are required to be discussed:

Following para (25) the suggested wording should be added. "Where a lump sum is allowed separately for the profit, the discount rate applied will allow for the required return on the equity (where interest on construction loans are separately deducted), or on the purchase and development costs, to take account of the risk of the development."

Para (26) requires amendments as follows:

The word "real" needs to be inserted in the <u>third</u> line <u>before</u> the word "discount rate".

The word "nominal" needs to be inserted in the <u>last</u> line <u>before</u> the word "discount rate".

Reference should be made to TIP1 for discounting in real or nominal cash flow terms.

Re **Reporting**

Question 9: Yes, except under the fourth bullet point the words ", and marketing" should be inserted in the <u>last</u> line immediately <u>before</u> the words "of the completed project",

Question 10: Yes.