ANZVGN 6 VALUATIONS OF ACCOMMODATION HOTELS

1.0 Introduction

1.1 Purpose

The purpose of this Guidance Note is to set out matters to be addressed in addition to those required by IVA 2 Valuation for Secured Lending Purposes and ANZVGN 2 Mortgage Security Reports on Real Property.

1.2 Status of Guidance Notes

Guidance Notes are intended to embody recognised 'good practice' and therefore may (although this should not be assumed) provide some professional support if properly applied. While they are not mandatory, it is likely that they will serve as a comparative measure of the level of performance of a Member. They are an integral part of the Valuation and Property Standards Manual.

1.3 Scope of this Guidance Note

This Guidance Note should be applied to properties that are valued with regard to their trading potential, including Accommodation Hotels, Motels and Serviced Apartment complexes of 3 star standard and higher. This Guidance Note is not specifically intended to cover licensed hotels (pubs), whether free standing or part of, Accommodation Hotels.

1.4 International Valuation Standards

This Guidance Note recognises the International Valuation Standards 1 and 2, and International Valuation Application 2 by the International Valuation Standards Committee and it is intended to be consistent with the concepts and definitions contained in those standards, however, there may be departures from IVSC Standards to reflect Australian & New Zealand law and practice.

1.5 Role of the Valuer

The valuer needs to demonstrate in a report an understanding of the operation of the subject property, the operator and/or lessee, the Hotel's market place, competition and any unique features it possesses.

1.6 Basis of Valuation

The valuation should clearly state whether it reflects the terms of an Operating or Management Agreement, or an occupational lease or whether the valuation is on a vacant possession basis. It should also state whether it has been undertaken as a 'going concern' on a 'Walk In Walk Out' basis inclusive of all plant, equipment, furniture and fittings but excluding stock.

1.7 Interests

The valuer should be aware of the different interests in a property, and should apply the same valuation principles to all interests based on the term of the management agreement or lease.

2.0 Compliance

2.1 Statement

A valuation of a property defined in 1.3: Scope of this Guidance Note should state that it complies with this Guidance Note.

2.2 Accepting an Instruction

Prior to accepting an instruction, a valuer must be confident of having the necessary expertise and sufficient information to undertake the valuation. For example, if the valuer does not have complete or appropriate access to comparable sales and trading data, then the valuation instruction should be declined, or undertaken in conjunction with a valuer who has the expertise and access to such information.

3.0 Review of Improvements

3.1 Key Factors

The improvements need to be considered in the context of their specialist use, with the following being examples of relevant factors:

- summary of room numbers by size/type/aspect
- location and adequacy of kitchen(s)
- appropriateness of food and beverage outlets
- size, location and appearance of entrance lobby and front desk
- layout and capacity of meeting rooms
- back of house facilities
- other facilities (eg Health Club, pool, etc)
- on-site car parking (numbers/adequacy)
- technological facilities (e.g. visual display units, communication/media access facilities)

3.2 Specialised Features

The valuer should consider the design characteristics and appeal of the property, including unique or specialised features that may impact upon the viability of operation, value and marketability. Factors to be considered include the efficiency of the layout in relation to guest servicing and labour costs, back of house servicing and adequacy of storage space (wet/dry/cold rooms).

4.0 Repair and Condition

4.1 State of Repair

Comment on the state of repair of the improvements of the property, including any outstanding works to be completed, and any modification or maintenance work required. Make comment upon the condition of Fixtures Fittings & Equipment, back of house equipment (e.g. kitchens), in the context of the Fixtures Fittings & Equipment Reserve.

4.2 Refurbishment

Comment on the feasibility and extent of possible refurbishment likely to be necessary over a normal investment period. Comment upon economic and functional obsolescence and the need or capability to upgrade improvements.

4.3 Capital Expenditure

The valuer should provide an estimate of likely required Capital expenditure, in respect to building works/services, refurbishment and Fixtures Fittings & Equipment Replacements.

4.4 Balance in FF&E Reserve

The valuer should establish whether there is an existing balance in the FF&E Reserve, and comment on its adequacy and appropriateness in relation to current and future Capital Expenditure requirements. Whether such balance has been reflected in the valuation figure should be clearly stated.

5.0 Approvals and Authorities

5.1 Building and Planning

Where necessary, issues relating to building compliance, heritage, environmental and planning classification should be reviewed and any consequent impact on value fully explained.

5.2 Non-Compliance

Whilst it is acknowledged that the valuer may not be qualified in these areas, based upon the inspection (noting limitations of such), comment should be made on any possible occupational health and safety requirements or requisitions recommending further inspection by qualified experts where appropriate.

In addition, the valuer should seek from the instructing party details of any notices of non-compliance of which the instructing party is aware.

5.3 Licences

The valuer should sight and comment on all licences required for the property's operation and note that these are included in the valuation.

5.4 Legislation

Comments are required as to whether the building is compliant with any current and pending legislation. Whilst it is recognised that the valuer is not an expert in this area, the report should highlight any potential risks in this regard through inspection and inquiry.

6.0 Trading Performance

6.1 Accounts

Where possible, accounts should be presented and analysed in accordance with the Uniform System of Accounts for Hotels. State whether the figures that have been relied upon have been audited.

The valuer should make a specific notation where relying upon information provided without being able to verify it, and clearly state any consequent limitations to the advice as a result.

6.2 Summary of Detailed Figures

The valuer should provide a summary of detailed figures for the hotel, showing trading performance for the last 3 years on a departmentalised basis, together with year to date trading figures. Appropriate periodic occupancy and average room rate statistics should be considered and commented upon.

6.3 Expenses/Outgoings

The valuer should itemise all expenses/outgoings in schedule form including management, all fixed costs, capital expenditure, and FF&E allowances, where possible in accordance with the Uniform System of Accounts for Hotels. Compare and contrast the current trading with the previous year's actuals, YTD figures versus budget, and comment upon any major variances. These figures should also be compared with appropriate industry benchmarks.

6.4 Trading Levels

The valuer should comment in detail on the current level of trading being achieved, the stability of the income and the projected maintainable trading performance of the property compared to the operator's projections.

6.5 Business Mix

The valuer should comment upon the business mix, typically analysed where available by geographical source, market segment and by guest type.

6.6 Operational Review

The valuer is not expected to carry out a detailed Operational Review, but would be expected to make appropriate comment upon:

- the marketing plan
- budget vs actual performances
- effectiveness of referrals within the operating group
- a fair market share analysis
- profile of operator

7.0 Trading Environment

7.1 Benchmarking

Benchmark the performance of the hotel in comparison to the Following:

- accepted market and industry indices,
- comparable and competing properties, to the extent that such data is available as well as identifying any items of revenue/ expense which are outside acceptable market parameters.

7.2 Competition

The valuer should provide full details of current and proposed competition within the catchment area, incorporating demand and supply criteria.

7.3 Current State of Industry

The valuer should analyse the current state of the hotel and tourism industry and in particular the subject property's target market, and detail any changes (current or anticipated) which may impact on the long term income sustainability and growth potential of the asset. Statistics and research data should be used to highlight trends and as a basis for projections.

8.0 Management Agreement / Tenancy Details

8.1 Commentary

The valuer should:

- Sight a copy of the Management Agreement / Operating Lease. A summary of the Agreement / Lease should be incorporated together with commentary on the general market acceptability of its terms and conditions. If these terms are outside typical market practice this should be stated and some commentary on what is considered acceptable should be provided.
- Read and understand all factors in the agreement or lease which could affect value, such as quality and certainty of income, income guarantees and associated clawbacks, break clauses, owners involvement. The valuer should also comment on remedies of default, assignability, termination clauses, non-disturbance clauses and the quality of the lease covenants.

- Provide a brief profile on the hotel operator including details of its brands, number of hotels/rooms and geographical spread.
- Investigate and comment upon the existence of any agreements between the owner and manager/operator which may affect value. Similarly, comment upon any agreements between the operator and other properties in the vicinity that may affect the operation of the property, for example, non-compete clauses, shared costs and expenses.
- Where the hotel forms part of a mixed-use project, all leases relating to the property should be reviewed by the valuer. Tenancy information should be summarised in schedule form. Comment upon the relationship of the hotel with the other components of the property.

9.0 Earnings Potential

9.1 Sustainable Net Return

Calculate the sustainable net return to the owner after reflecting appropriate outgoings. The treatment of Management Fees and FF&E Reserve varies, but as a general guide valuers should apply as they analyse and reflect the manner in which the market is capitalising. Although net return is typically expressed after Management Fees and FF&E Reserve, an owner operated property may be considered on a 'before fees' basis.

9.2 Existing Agreement

Fees and FF&E provision should reflect any existing Management Agreement, or prevailing market rates. The net return should also be expressed before depreciation, amortisation, interest, tax and Capital Expenditure.

9.3 Projections

Any projections should be in accordance with the 'Uniform System of accounts for Hotels', and preferably undertaken for a period of five years or beyond, reflecting the method adopted to analyse sales.

9.4 Upgrades/Capital Expenditure

Have regard to any upgrading or capital expenditure which would impact on the trading performance of the hotel or its marketability.

9.5 Cashflow

A detailed analysis of the cashflow is an essential requirement. The calculations should be completely self explanatory. Details of the discount rate, time period, etc, should be shown.

9.6 Changes

Comment upon the anticipated changes to outgoings, timing of capital expenditure, particularly significant items (eg major contract renewals, rating changes, etc.

9.7 Variation

Comment on variations between the operator's projections and those assumed by the valuer, with rationale supporting any variations.

9.8 Analysis

A sensitivity analysis for key variables may be appropriate.

10.0 Market Commentary

10.1 Purpose

This should address the following sectors, as relevant to the specific hotel – global, local (regional), comparison of design features with market demand and competitive supply.

10.2 Market Conditions

This requires both a current and forward looking view (typically 3-5 years) rather than an historic view of market conditions. Typically this commentary should include:

- Investment activity including depth of market and identification of key 'players';
- Building activity including competition and likely additions to supply;
- A discussion of the major drivers of supply/user demand over the period under review;
- A valuer should consider a model of future supply and demand to project average occupancies and room rates within the market and to form the basis of a fair market share assessment.

11.0 Sales Evidence

11.1 Sales Analysis

It is not always possible to obtain sufficient information to fully analyse every sale; however, the valuer still needs an appropriate level of sales that have been adequately analysed in order to arrive at an opinion of value. To simply quote a yield or a room rate from a sale, without first seeking the information to analyse the sale is unsatisfactory.

11.2 Trading Performance

The future trading performance of the adopted sale or sales being analysed should be explored for each sale, in combination with the sale's historic performance. This is required, in order to allow the formation of an acceptable level of consistency between the sale being analysed and the subject property, to allow informed comparison.

11.3 Relativity of Sale

The relativity of each sale should be commented on and explained.

11.4 Recent Sales History

The valuer should indicate recent sales history of the subject property. Where the property is being transacted, the contract for sale should be sighted and commented upon.

12.0 General Issues

12.1 Vacant Possession

Where owner occupied properties are valued on a vacant possession basis in existing condition, an indication of net income after management expenses and replacement reserve should also be provided for comparison purposes.

12.2 Leases, Plant and Equipment

The valuer should comment on leases of plant and equipment where the lease payments for plant and equipment are substantial so as to have a material effect on value if the costs are deducted from income. In such an instance the costs may be ignored if instead a payout figure can be ascertained and deducted from the value assessed.

12.3 Leasehold Title

In cases of hotels held upon leasehold title, the impact of the ground rent on returns/incomes should be fully considered and reflected in the valuation. As with any other leasehold the valuer may need to consider the value of the hypothetical unencumbered freehold and then consider the value of the Lessors Interest, the Lessee's Interest, and potential Marriage Value of the interests concerned. See separate guidance note on Partial Interests.

12.4 Impact of Valuation

The impact on valuation of the separation of the various title components, related options, obligations and impediments, potential loss of tenure, etc should be identified and fully explored in relation to both sales and the subject property.

12.5 GST Caution

The Valuer should consider the manner in which similar properties are bought and sold from a GST perspective and adopt the most appropriate treatment of GST accordingly.