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NEW ZEALAND INSTITUTE OF VALUERS

Incorporated by Act of Parliament

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The New Zealand
Valuer

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CONTENTS:

50 Publications and Services.

COMMENT

51 Editorial
52 Council Photograph.
53 Presidential Profile.
55 President's Message.
55 The Direct Media Advertising Campaign.
57 Citation Life Membership.
58 Citations Fellowship.
61 46th Council Meeting and Annual General Meeting Report.
65 Letters to the Editor.

NEWS

66 Membership.
76 Book Review "Property Valuation in South Africa."
98 Idea 85. Investment and Design.
99 IAAO Bibliographic Series.

ARTICLES

68 Computer-Wise - Viewdata.
71 Application of the Opportunity Cost Doctrine to Right-of-Way Valuation.
78 Equated Yields - Jargon or Genuine.
87 The Discounted Cash Flow Concept.

LEGAL

99 Valuers Registration Board Decisions.
104 Professional Directory.

This Issue

THOU SHALT NOT ADVERTISE 51

All public valuers advertise to survive. More open advertising will be acceptable in the future.

WIDER RANGE OF WORK 55

Your President outlines the need to adapt to changes in the market place.

DIRECT MEDIA ADVERTISING 55

N.Z.I.V. promotes "The Valuers" in advertising campaign.

VIEWDATA 68

Use of telephone system to transfer data. Simple and cheap technology. The blueprint for the future?

RIGHT-OF-WAY"EASEMENTS", 71

Land a critical factor of production. Cost of alternate route is true cost.

EQUATED YIELDS - INTERNAL RATE OF RETURN 78

The development of this tool and the need in future for greater sophistication by valuers.

DISCOUNTED CASH FLOW 87

Paper delivered by Lincoln W. North as part of the Seminar "A Critical Analysis of The Income Approach to Valuing Revenue Producing Real Estate."

Editor:
M. E. Gamby, Dip. Urb. Val., ANZIV, MPMI
P.O. Box 27146, Wellington.

Asst. Editor: J. Dunckley, B.Ag., Comm. V.P.U., A.N.Z.I.V.

General Secretary:
K. M. Allan, A.N.Z.I.V.

Statistical Officer:
L. E. M. Grace, M. Com. ACA.

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P.O. BOX 27-146, WELLINGTON)

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Editorial Comment

THOU SHALT NOT ADVERTISE

The Eleventh Commandment of Professional Organisations

The Institute ethics clearly state at Clause 23:

> *"The solicitation of professional work by such means as personal canvass, circular, advertising in directories, year books, or the public press (except by means of a professional card) or by use of radio or television or the exhibition of unduly large name-plates or painted or illuminated signs, is forbidden".*

Government action in the recent past has forced all professional groups to examine their restrictive trade practice in this regard. All have opted for Society or Institute advertising if for no other reason than; "if we don't do it then our members will demand the right to do it themselves."

The Publicity and Public Relations Committee (see open letter in this issue) has your Institute's approval to spend $50,000 between June and December this year on what can best be described as "identity advertising". This action will have its critics, but in truth the amount is very *small in advertising terms, possibly insignificant as a promotional exercise, is long overdue, and does no more than scratch the surface of this important issue.*

Many of our members provide the minimum of professional service in the belief that they have found their professional niche, protected by legislation and Institute restrictive practices. It is these *very members who cry wolf when any attack on their territory is mounted by another professional or non-professional organisation. Although the parallel may be unpalatable; war is not willingly waged against a strong adversary.*

Your Institute and its members do not require and should no longer court the protection offered by legislation. Our educational qualifications are very high by world standards, and your Institute is sufficiently strong to satisfy the most searching enquiry as to professional ability both internally and internationally. We must learn to go it alone; face competition and as our appointed advertising agent recommends, convince the public that we are "The Valuers".

Some members would like to advertise on their own behalf now. Should they not be entitled to promote their abilities? The relative ease with which the hallowed fee scale was demolished should at least in part convince us *all that many of our entrenched attitudes are just that, "entrenched attitudes".*

Advertising! Who among us does not advertise? All public valuers advertise. Some by the quality of their report, others by client contact, some by reputation, others by speed of service. Valuers now appreciate that advertising is necessary for their continued survival, not only in competition with one another but against others who would break into what to outsiders is now seen as a lucrative field. Valuers must have the right to compete against these outsiders. Some members will form organisations permitting them to compete on an equal footing. These will be the firms who have grasped the nettle and will move forward to meet the demands of a changing society.

Thou shalt advertise - to survive - but in accordance with the tests of good taste, dignity, and restraint.

New Zealand Institute President 1935

G. J. HORSLEY

At the 1985 Council Meeting of the New Zealand Institute of Valuers held in Palmerston North in April, Mr G. J. Horsley was elected to the highest active office in the professional body - President of the Institute.

Graeme Horsley, who is a partner in the firm of Darroch Simpson & Co., Registered Valuers and Property Consultants of Wellington, was born in 1943 and educated at Scots College, Wellington, completing the N.Z. Institute of Valuers urban professional qualifications in 1967. He was admitted to Intermediate membership that year, and became an Associate and Registered as a Valuer in December 1968.

Mr Horsley entered the valuing profession as an employee of the Northern Building Society in 1962, initially in Auckland, and was appointed Senior Valuer in the-Society's Wellington Office in 1965.

Upon leaving the Northern Building Society Graeme Horsley worked in the Valuing Division of Harcourt & Co., until 1973 when he formed the Wellington based partnership of Simpson Horsley Nyberg and Associates. This practice was subsequently expanded and with national associations, became known as Darroch Simpson and Company.

After initially serving on the Wellington Branch Committee Mr Horsley was elected as Branch Chairman, and was later appointed to the Institute's Publicity and Public Relations Committee serving as its Chairman until 1983. A Fellow of the Institute, he is currently a member of the Executive Committee and serves on a number of its sub-committees with tasks involving professional practice, and particularly Assets Valuation Standards. In this latter capacity he currently represents New Zealand on an international committee which is investigating and preparing world wide standards for asset valuations.

Graeme has regularly contributed to the education of the profession in New Zealand with the presentation of seminar papers, some of which have been regarded as innovative and thought provoking. He has also addressed an inaugural international valuation congress in London, and attended three of the Pan Pacific congress conferences in the Pacific region.

Graeme's elevation to President of the Institute, by election, is recognition of his outstanding contribution to the valuing profession.

His other interests include involvement in the liquor industry and in garment manufacturing. He is married with four children and lives in Seatoun, Wellington.

STOP PRESS

NEW MEMBERS TO HIGH COURT BENCH

It has just been announced that two new appointments have been made to the Administrative Division of the High Court to sit on valuation matters. Both appointees are members of the Institute and practising valuers; the congratulations of the Institute are extended to these individuals whose appointments were gazetted in late June.

The members involved are Mr J. N. B. Wall of Wellington who is a practising valuer with the from of Geilatly, Robertson and Co., and Mr I. W. Lyall practising in the Blenheim partnership of Hadley and Lyall.

The above appointments have been made in substitution of the former members Mr R. J. MacLachlan and Mr R. Frizzell.

Further details of the new appointees will be contained in the next issue of "New Zealand Valuer".

ELECTED SENIOR VICE-PRESIDENT 1985

R. E. HALLINAN

Mr R. E. Hallinan was elected Senior Vice-President by the Council Meeting of the Institute in Palmerston North in 1985, having served the preceding two years as Junior Vice-President. Roger is a senior partner in the Christchurch firm of Telfer, Hallinan, Johnston and Co., and was born in Christchurch in August 1945. He was educated at Shirley Boys High School, and after appointment to the Valuation Department as an urban field cadet in 1963, proceeded to Auckland University where he completed a Diploma in Urban Valuation in 1966.

He was posted to the Invercargill Branch of the Valuation Department in 1967, and during the year completed the Real Estate Institute examinations, and became an Associate Member of that Institute.

Roger was transferred to the Christchurch Branch of the Valuation Department in 1968, and became registered as a valuer in September 1970, being advanced to Associate status in December of the same year.

He was appointed Senior Valuer to the Department in Hokitika in 1971 but resigned shortly afterwards to take up an appointment in the valuation practice of Moyle Fright & Telfer.

Roger's involvement in Institute affairs has included Secretaryship of the Canterbury/Westland Branch from April 1970, service on the Branch Committee in 1975, and election as Branch Councillor in 1979, a post he continues to hold.

He is held in very high esteem by his colleagues in the local branch and has gained reputation amongst business and professional people for his competent and thorough approach to valuation assessments. He has a particular interest in the insurance valuation area and has delivered papers on this and other subjects within New Zealand and overseas.

Mr Hallinan is married with three daughters, and lives in Christchurch.

ELECTED JUNIOR VICE-PRESIDENT 1985

R. L. JEFFERIES

Mr Jefferies who was born in 1942, is the Auckland Branch Councillor, and is a Senior Partner in the Valuation Practice Barratt-Boyes Jefferies Laing & Partners. He qualified with a Diploma of Urban Valuation from the University of Auckland in 1964, and completed a Bachelor of Commerce & Administration Degree at Victoria University in 1967. He became registered in 1967, an Associate of the Institute of Valuers in 1968, and was advanced to Fellow of the Institute in 1979. He is also a member of the Property Management Institute.

Rodney Jefferies has made a considerable contribution to the valuing profession in New Zealand, having filled lecturing positions at Auckland University in valuation from 1973 to 1982, written the textbook "Urban Valuation in New Zealand - Volume 1" published in 1978, and was the Hon. Editor of the Journal, the New Zealand Valuer, published by the N.Z.I.V. between 1968 and 1974. He was awarded the John Harcourt Memorial Award by the Institute for recognition of his outstanding services, and has been in private practice in Auckland since 1970.

He is currently Chairman of the Committee of Inspection into the liquidation and collapse of the Securiti-Bank & Merbank Group of Companies and has served as a consultant to the Directorate General of Taxation in Indonesia for three and five month periods in 1980 and 1983 respectively.

Rodney Jefferies has addressed numerous seminars, conferences and workshops on valuation and property investment topics throughout New Zealand during the past twenty years, and continues to make a major contribution to the profession.

Rodney remarried in November 1984 and has a son and two daughters by a previous marriage. He resides in Auckland.

President's Message

Developments which are taking place both from within and outside of the profession will have increasing importance on the livelihood of our members over the next few years. The way in which individual members adapt to changes within the market place will become all important if we are to prosper and move into the 1990's as the principal land based profession in New Zealand. I firmly believe that the sights of individual members must be lifted above a horizon that concerns itself with petty differences between members and squabbles over the make-up of administrative committees of the Institute.

Ours is a profession where the skills of our members are in ever increasing demand from a widening spectrum of clients. We must remove our blindfolds and move outside of the straight jacket of Registered Valuers' work, which if you stand back and look at your own workload forms a very small part of our daily responsibilities as a valuer.It is the wider range of other valuation, appraisal and property consultancy work that is a direct derivative of a valuer's training and experience to which we must address ourselves. The marketing of our services in these fields is an absolute necessity. It starts from our report standards and moves out to making our clients aware of the whole parameter of services which we as valuers are able to offer and to offer with more expertise than any of the other land based professions.

I recently travelled overseas on behalf of the Institute to attend the International Assets Valuation Standards Committee Meetings in London and Hong Kong. On both of these trips I was interested to note that valuation practices around the world have moved ahead of many of our practices in New Zealand and have broadened their scope of expertise and involvement in property matters to a stage where many of the large practices of valuers in the world today define their business activities on their letterhead, not as being valuers and property consultants, but rather as "John Smith & Co. Professional Services", a definition that is extremely wide and one which requires promotion of the specific professional services offered by the particular valuer or valuation practice. The marketing of our services is being supported by the Institute, who at the end of May gave approval to a nationwide publicity campaign to promote the services of valuers who are members of this Institute. It is my opinion that the full weight of our advertising endeavours must be placed behind the letters "N.Z.I.V.".

If the Institute and the profession as a whole is to continue to be a leading force in land related matters in New Zealand then the Institute must move towards assisting in the marketing of the benefits to be gained in utilising the services of members of the New Zealand Institute of Valuers. This is the challenge that lies ahead of the Institute, this is where the future of the membership at large lies.

G. J. Horsley.

The Direct Media Advertising Campaign-

AN OPEN LETTER FROM THE CHAIRMAN, PUBLICITY AND PUBLIC RELATIONS

COMMITTEE NEW ZEALAND INSTITUTE OF VALUERS

Ladies & Gentlemen,

You will be able to see from the President's commentary contained in this issue that the Council of the NZIV at its meeting in Palmerston North in late April 1985, appointed a Wellington based advertising agency - Charles Haines Ltd. - to promote the valuing profession throughout New Zealand by direct media advertising.

During 1984 a number of members of the Institute approached Mr Morley Donaldson, the then President, and expressed concern that there was no visible form of media advertising on behalf of the profession. Some of these individuals appear to have been practitioners in the smaller centres, who felt that a number of competitive activities were affecting their livelihoods, and yet on account of the Rules of the Institute they were unable to advertise personally, either their skills or identity (except under special circumstances such as an expansion or alteration to a partnership, change of premises or address which would enable a public notice to be inserted in the daily newspapers).

As a practising valuer and particularly as Chairman of the Publicity and Public Relations Committee of the Institute, I found I could accept these concerns in the knowledge that a number of events had occurred in the relatively recent past which might diminish the normal workloads of

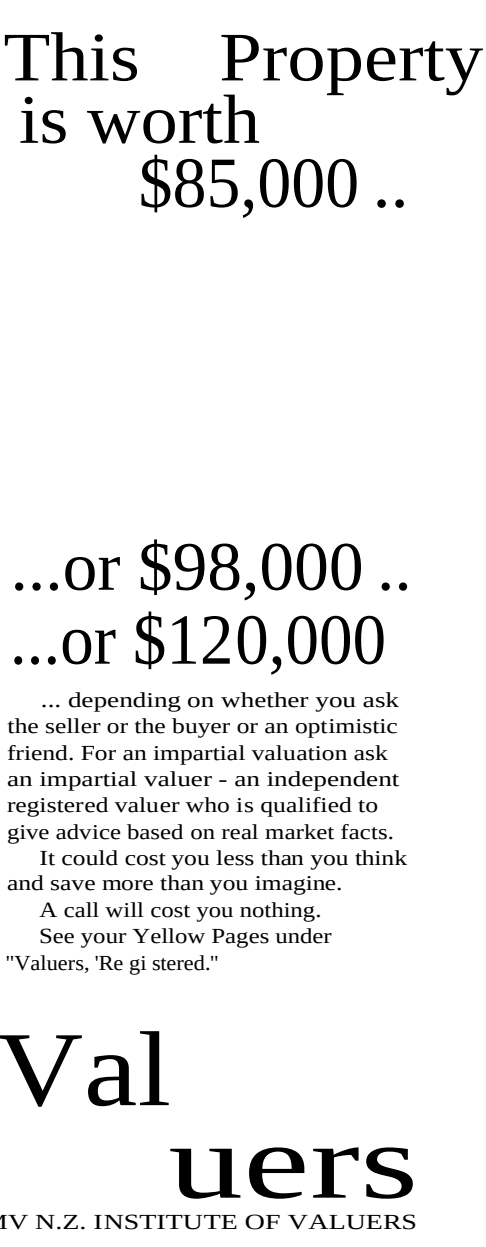
practising valuers. In particular our specified identity had been removed from the Building Society's legislation, there had been a widening of the definition of persons authorised to make valuations under the provisions of the Earthquake and War Damages Act, an appraisal service had been introduced by the Real Estate Institute, and a property inspection service introduced by the N.Z. Institute of Architects. Concurrently, successive central government administrations had demonstrated, particularly during 1984, the volatility of the mortgage market, when subjected to political control. Under such circumstances it is reasonable for a practising professional to look to his parent professional body for support, and it was in response to this notion that I delivered a report to the mid year meeting of the Council of the Institute (in October 1984) containing a recommendation for direct media advertising, and demonstrating that the normal budgetary allowance granted to this Committee was quite insufficient to mount and maintain any sort of worthwhile promotion.

The approval in principle by Council gave this Committee a mandate to prepare a brief for presentation to advertising agencies and public relations consultants, in order to determine the services available, their likely benefits, and whether or not the indicative budget of $50,000 could be workable. The brief to the agencies expressed concern that the basic services of the Registered Valuer as well as his counterparts in government departments, local authorities and other areas of employment were not widely known by the general public or business community in either the rural or urban spheres. The brief also stated that the Institute acknowledged that it had a relatively low public profile and had struggled on occasion to have its publicity releases accepted by the written and visual press. The consultants were advised of the Institute's motto "Integrity and Fidelity".

Three national advertising agencies were approached as well as two national public relations consultancies. However in the final analysis only one of the advertising agencies replied, as well as both of the public relations consultancies. Largely on account of the more visible and immediate impact that a direct media advertising compaign can bring, the Charles Haines Ltd. proposal was accepted by the Council of the Institute as providing the most appropriate solution to our perceived problems.

The agency recommended the adoption of the distinctive logo "The Valuers" and designed both a press advertisement (which has flexibility for use in residential, commercial and rural capacities by the simple interchange of graphics and texts) as well as a suggested professional body listing in the Yellow Pages of the telephone directories throughout New Zealand, for valuers as a group. The agency recommended a sequence of advertisements in the main metropolitan dailies; however Council decided that to be truly representative of the membership, the campaign should be visible in all of the thirteen regions represented by its branch councillors. Accordingly the campaign has been redesigned to allow for eighteen sequential insertions in seven metropolitan dailies, with eight insertions in two of the other metropolitan dailies, and eight insertions in the fourteen provincial dailies. The total estimated cost of the campaign including an allowance for increases in the advertising rates, over a period June to December 1985, is in the order of $45,000, with the balance of the budget to meet the agency's design and establishment costs.

It is considered that a Yellow Page listing should follow in subsequent years, but it may well be appropriate to arrange such listings regionally.



The initial advertisement exposures will take the form illustrated, but as mentioned, there will be a revision of the format periodically during the

campaign, with substitution of property types and price ranges. The advertisement is to be inserted amongst real estate advertisement columns on selected days, and it is expected that the format will focus attention on the pricing dilemma faced by buyers and sellers, and alert them to the availability of an Independent Valuation Service. This campaign, a first of its type for the N.Z.I.V. is the product of many hours honorary work involving research, discussion and debate. However it is appreciated that it will have its critics for a variety of reasons. While the Committee acknowledges that the direction of the campaign will favour practising valuers, it is hoped that at the same time there will be an improvement in the public's awareness of the services available from all valuers including those employed in institutions, central and local authorities.

In years to come, I hope that all facets of valuation and the services provided by valuers can be demonstrated to the public, by campaigns of this nature, or by the employment of public relations consultants who have a variety of techniques available for assimilating information. Some of you may wonder why we are not embarking upon a televised promotional campaign. There are several reasons, the most fundamental being the cost of such promotion for which an annual budget of approximately $200,000 would be required. Other professional groups have utilised a television format for promotion, but from this Committee's enquiry and research, it appears that the direct benefits have been difficult to recognise, and the campaigns have on occasion generated unexpected criticism.

I hope that you will all benefit from this campaign and invite any member with constructive criticism to write to me Cl- The Institute's Wellington box number.

GRAEME KIRKCALDIE

Citation
Life Membership Murray Raymond Mander

After attending New Plymouth Boys' High School, Mr Mander joined the Public Service in 1942 as a rural field cadet. He served in the Royal New Zealand Navy in the United Kingdom during World War II and in 1948 gained his Diploma in Valuation and Farm Management from Lincoln College obtaining the highest aggregate mark and gold medal for the course. He transferred to the Valuation Department in 1949 after service in the State Advances Corporation and Maori Affairs Department. He was appointed District Valuer Rotorua in 1956 and in 1964 was further promoted to the position of Supervising Valuer, Palmerston North. He has been located in Head Office of the Department since 1969 being initially appointed there as Chief Valuer. He was subsequently promoted to Deputy Valuer-General in 1973 and was Valuer-General and Chairman of the Valuers' Registration Board from 1975 until his retirement from the Public Service in 1984.
He is now employed in private practice with Jones, Tierney and Green, Public Valuers and Property Consultants, Tauranga.

Mr Mander has throughout his career always striven for the highest standards of professionalism, both within the Valuation Department itself and the profession generally. In his early career he became well known as a capable expert witness on valuation matters. His expertise and knowledge of valuation has attracted interest overseas and he has presented papers and participated in a number of international conferences as well as hosting numerous overseas valuers here in New Zealand.

Mr Mander is held in very high regard by the valuing profession both here in New Zealand and overseas. Prior to his appointment as Valuer-General in 1975 he held various positions with the N.Z. Institute of Valuers at branch and national level and was made a Fellow of the Institute in 1973. He has in the past acted as an examiner in rural valuation for the practical and oral examinations, he served for a period as Chairman of the Board of Examiners, the Valuer-General's representative to Council and as a member of the Executive Committee.

As Valuer-General for nearly 10 years Mr Mander initiated a number of changes which have greatly enhanced the Valuation Department's effectiveness. Perhaps the most significant was the general upgrading of the department's computer systems and the introduction of an on-line enquiry computer terminal network which links each district office in the country. The establishment of a computerised property sales recording and retrieval system within the department has been of major benefit and with Government approval this sales data is released for dissemination to the profession at large.

Citation for Fellowship
Neil Kelvin Darroch

Neil Darroch is a senior partner and currently Chairman of the national valuation practice of Darroch Simpson & Co., and is well known as a leading valuer both locally, nationally and has undertaken work in the Pacific Islands.

Neil was born in 1935, educated at Auckland Grammar, obtained his U.E. in 1953 and joined the Lands and Survey Department on leaving school as a Rural Field Cadet. He attended Lincoln College and graduated with a Dip.V.F.M. in 1958, commenced full time valuing with the Department in Wellington as a Field Officer in 1959. He was transferred to Palmerston North in 1961 becoming an Intermediate Member of NZIV. He obtained registration as a Rural Valuer in 1963 and became an Associate Member in 1964, being transferred to Auckland in 1965.

In 1967 he commenced the NZIV professional urban examinations completing these in 1971.

Neil joined the Auckland Harbour Board as a Property Officer in 1969, later working for a property development company before setting up as a private valuer on his own account in 1971 in Takapuna on the North Shore - where his practice has grown and is still based. He became an Associate Member of the Institute of Arbitrators in 1980 and became a Member of The Property Management Institute in 1978.

Neil has been an active member of the Institute of Valuers, particularly at local level. He has participated in lecturing students and been actively involved in the practical training of young valuers both in his own practice and also valuers preparing for The Institute's practical and oral examinations.

He has also participated as a speaker at 'Seminars and Conventions, and earned a reputation as an innovator and leader both in business and Institute life.

Neil joined the Branch Committee in 1975, serving on practically all the sub-committees over a four year period and was Branch Chairman 1977/78, leaving the Committee after his following ex-officio year.

Neil Darroch has served the profession both in his vocation and Institute service with enthusiasm and has earned a reputation as a leading valuer of good repute and integrity.

The Branch Committee unanimously supports Mr Neil Darroch's elevation to a Fellow of our Institute.

Citation for Fellowship
Bruce Gregg Grinlinton

Bruce Grinlinton joined the Rural Bank as a Cadet in 1956 and was located in Invercargill, Rotorua, Whangarei before moving to Manawatu as a District Appraiser in 1968. Subsequently he moved to Te Kuiti in 1970 before transferring to Hamilton in 1971 where he is currently located. Bruce was Registered in October 1963 and became an Associate of the Institute in 1965. Bruce has served on the Waikato Branch Committee since 1972, becoming Vice Chairman in 1976 and 1977 and Chairman in 1978 and 1979. He has been a member of the Rural examination panel since 1974. Bruce has been a conscientious member of the Branch Committee and has actively encouraged his staff to participate in Institute affairs with the result that the Rural Bank is very well represented in all Branch activities.

Bruce's opinion on all matters affecting Valuation and the Institute is sought after and he is held in high esteem as a man of integrity by his associates, professional colleagues, staff and the general public.

The Branch Committee has no hesitation in recommending his advancement to Fellowship status.

Citation for Fellowship Terrence Rawclif f e

Terry Rawcliffe is a partner in the Napier ifrm of Rawcliffe and Plested. He was born in Masterton in 1944 and was educated at Wairarapa College.

Terry qualified as a joiner and worked in the trade in Masterton before joining the Valuation Department, Lower Hutt in 1964 as an urban valuer. He completed the Urban Professional Examinations in 1968 and was registered as a valuer on 1 October 1969 and in 1970 was granted Associate status.

Following his resignation from the Valuation Department in 1969 Terry worked as a valuer for the Northern Building Society (now United) in Wellington. In 1971 he moved to Napier and commenced private practice on his own account, forming the firm Rawcliffe and Plested in 1973. This firm has now grown into one of the largest valuation practices in Hawke's Bay.

He has been very active in Institute affairs and was secretary of the Hawke's Bay Branch in 1972-73. In 1974 he was elected Branch Councillor attending his first meeting in New Plymouth. Terry remained Councillor for 10 years until his resignation in 1984. Over this period he gave his undivided attention to the interests of the Branch and gained the reputation of being a quiet effective worker. Terry is still an active and valued member of the Branch Committee.

As Chairman of the organising committee, Terry was instrumental in arranging the successful 1982 Annual General Meeting and Seminar of the N.Z. Institute of Valuers held in Hastings.

He has also been involved with education matters acting on several occasions as local examiner for the Institute's Practical and Oral Examinations and has also assisted and advised students on valuation matters.

His outside interests have included Jaycees, involvement with the Sea Scout organisation and he has coached schoolboy soccer and cricket teams.

Terry Rawcliffe's professional standing and his competence in the valuing field are highly regarded in the Hawke's Bay area. He can number among his clients several leading financial institutions, national companies as well as leading legal and accountancy practices.

Terry sets and maintains the very highest of professional standards and his honesty and integrity are without question. By example he has always endeavoured to promote the image of the Institute.

The Hawke's Bay Branch unanimously support the recommendation for Terrence Rawcliffe's advancement to the status of Fellow of the. Institute.

Citation for Fellowship Timothy John Bernau

Tim Bernau was born in 1941 and for the last 16 years has been a partner in the valuation firm of Sporle Bernau & Associates.

Tim completed the Diploma in Sheep Farming at Massey in 1961 and in 1967 completed the Diploma in Valuation and Farm Management at Lincoln. He became registered as a valuer in 1969 and became an Associate of the Institute in 1970. Prior to commencing in valuation Tim was involved in farming in the Waikato and King, Country area.

Tim has been a Committee member of the Waikato Branch of the Institute of Valuers since 1970, being the secretary and a member of the education sub committee until 1977, vice chairman from 1978 to 1979, chairman from 1980 and 1981 and continues to be a valuable member of the committee up until the present time. Tim has also been a rural examiner for the last four years.

Tim as a private valuer, has a high professional standing, and over recent years has built up a well deserved reputation as a specialist in the new farming ventures of horticulture and deer and goat farming. Tim is a credit to the Institute and his recommendation for advancement to fellowship status is unanimously supported by the Waikato Branch Committee.

Citation for Fellowship
Graham Allan Halstead

Graham Halstead is in public practice under the style of Graham Halstead and Associates.

In 1961 he was selected as a Rural Field Cadet and graduated from Lincoln College in 1966 with Diplomas in Agriculture and in Valuation and Farm Management. He commenced work as a valuer with the Valuation Department's Rotorua Office in 1967 and subsequently served in the department's Auckland Office and spent two years with the research group in Head Office.

Mr Halstead resigned from the department in 1972 to establish his own practice in Wellington. He became registered as a valuer in 1969 and completed the N.Z.I.V.'s urban professional examination in 1971. He was born in 1944 and has been an Associate member of the Institute since 1970.

Mr Halstead was appointed a member of the Education Committee and Board of Examiners in 1974 and has served continuously in this capacity since then. His contribution in this area has been significant and is ongoing as he is currently convenor of a project arranging for the writing and publication of a second volume of Urban Valuation in New Zealand. He has also had technical articles published in the "Valuer". Graham has also served as a practical and oral examiner for the Wellington Branch candidates.

His professional standing and his work in the valuation field are highly regarded amongst his peers in the Wellington region.

Citation for Fellowship
Ian Robert Telfer

Ian Telfer is a principal of the firm Telfer, Hallinan, Johnston and Co., Registered Valuers and Property Consultants of Christchurch.

Ian was born in Dunedin in January 1938 and educated at King's High School, Dunedin.

On leaving school he joined the Lands and Survey Department working in Dunedin and Invercargill until May 1964 when he transferred to the Land Purchase Section of the Ministry of Works in Christchurch. He was engaged as a Land Purchase Officer for a period of four years.

After leaving the Public Service in March 1968 Ian was privately employed as a Valuer in Christchurch for a period of 18 months or so before joining the Christchurch valuation practice which subsequently became known as Moyle, Fright and Telfer but nowdays known as Telfer, Hallinan, Johnston & Co.

Ian completed the Institute examinations in 1967 and was registered as a Valuer on 3rd October 1967. He was admitted as an Associate Member of the N.Z. Institute of Valuers in March 1970.

During the 1967-70 period Ian completed the Real Estate Institute examinations and was admitted as an Associate of that Institute. Apart from a brief period in 1968 he has not acted as a real estate salesman.

For the last 15 years Ian has' been solely engaged in public valuation and consultancy work which has gained him wide respect from the business community and clients generally, together with his fellow members of the Institute. Ian's sound professional approach to his work is accompanied by a likeable extroverted manner.

Throughout his Institute membership Ian has, and continues to be, a particularly supportive and keen participant in all Institute affairs. He stood and gained election as a Committee member of the Canterbury-Westland Branch in February 1973 and remained on the Committee until 1982.

He was Branch Chairman for the 1979 and 1980 years.

Ian Telfer's ongoing contribution to the Institute and the profession is based on a sound professional attitude which is a credit to the Institute.

The Canterbury-Westland Branch unanimously supports Ian Telfer's elevation to that of a Fellow within the Institute.

EDITORIAL BOARD - NEW ZEALAND VALUER:

At the 1985 meeting, Council approved the appointment of an Editorial Board with initial appointments to be for a two-year term. The following members were appointed to the Editorial Board:

Mr R. Frizzell.
Mr R. L. Jefferies.
Mr A. P. Laing.
Mr J. A. B. O'Keefe.
Mr S. L. Speedy.
Mr R. J. Chappell (Chairman Education Committee)
Mr M. E. Gamby (Editor)

Report on the 46th Council Meeting and Annual General Meeting of The New Zealand Institute of Valuers

by the Editor

The venue of this year's Council Meeting, Annual General Meeting and Valuation Seminar was the Centennial Convention Centre, Palmerston North, April 20th - 23rd, 1985.

Mr R. J. MacLachlan tendered his apologies. All other Councillors and Executive Members were present.

The President, Mr R. M. Donaldson, welcomed back as re-elected Councillors Mr G. T. Foster of Gisborne, and Mr A. G. Johnson, Taranaki. Mr A. P. Laing was introduced as the new Councillor for Otago, succeeding Mr R. Lord.

THE ELECTION OF PRESIDENT AND VICE-PRESIDENTS:

Mr G. J. Horsley was elected President of the Institute for 1985 and 1986. Mr R. E. Hallinan (Canterbury/Westland) was elected Senior Vice-President and Mr R. L. Jefferies was elected the Junior Vice-President.

In his acceptance speech, Mr Horsley stressed the spirit of co-operation which exists in Council and the Institute generally and his pleasure in looking forward to his two-year term as President.

LIFE MEMBERSHIPS:

Mr M. R. Mander was elected a Life Member of the Institute and this was approved by acclamation at the Annual General Meeting.

HONORARY MEMBERSHIPS:

No Honorary Memberships were conferred.

JOHN HARCOURT MEMORIAL AWARD:

No Award has been made for the current year.

ADVANCEMENTS TO FELLOWSHIP:

The following members were elevated to the status Fellow of The New Zealand Institute of Valuers:

Timothy John BERNAU - Waikato.
Neil Kelvin DARROCH Auckland.
Bruce Gregg GRINLINTON - Waikato.
Graham Allan HALSTEAD - Wellington.
Terrence RAWCLIFFE - Hawke's Bay.
Ian Robert TELFER - Canterbury/Westland..

MATTERS ARISING:

Council received a report on "Valuation and Reporting Standards", and recommended that:

- The report be released as an exposure draft to members at large.
- That members be invited to comment on the report.
- That a time limit be set for comment by members.
- That the matter be reported back to Council at the mid-year meeting for a final decision..

Council approved the setting up of an Editorial Board as follows:

1. The Board will comprise five members approved by Council together with the Editor and the Chairman of the Education Committee.
2. The appointment of members be reviewed. after two years.
3. The duties of the Board are as follows:
   (i) To decide editorial policy and matters of importance to be recommended to Council for the next twelve month period.
   (ii) The format and general content of the journal be agreed for the next twelve-month period.
   (iii) The Board consider extensions to the existing functions of the journal and modifications thereto.

The five members appointed to the first. Editorial Board are:

R. Frizzell.
R. L. Jefferies.
A. P. Laing.
J. A. B. O'Keefe.
S. L. Speedy.

The Lincoln North Lecture Tour, March 1985 was recognised as being a success. Although there was a small financial loss, there was support for more seminars of this type should the opportunity arise. Council approved a letter to Lincoln North expressing Councillor's thanks on behalf of the Institute.

REPORTS:

Reports were received from Committees of the Institute and circulated to Councillors prior to the meeting. Brief details from the reports are outlined below:

(a) Statistical Bureau:

Mr J. N. B. Wall, the Chairman of the Statistical Bureau Committee, indicated in his report that the numbers of bureau members have continued to increase steadily with now 580 bulletin subscribers, 590 micro fiche subscribers, 18 electronic data subscribers and 540 bureau members.

During the year, the new Valuers' Handbook has been published and the intention is to continually update and add to the publication through the additional pages in the monthly bulletins. The Handbook will remain the permanent record with the bulletins providing for changing information.

There is a tentative date to implement the change in the micro fiche information by the end of the 1985 year. Residential categories RB to R8 will be one grouping with other categories such as VR, FO, VI, IN, VC, CC, etc., in individual groupings within territorial Local Authorities.

New charges for the period commencing 1st January 1986 were approved as follows:

(a) One set of micro fiche to each subscriber: a standard charge of $250.00 per annum per subscriber, or the level of cost paid during the 1982/83 year, whichever is the greater.

(b) Additional sets to a subscriber:

(i) Where more than one set of fiche is supplied in a single envelope to a subscriber the charge is $250.00 per annum for the first set and $100.00 per annum for each additional set.

(ii) Where the subscriber orders more than one set but requires them sent separately by the Bureau to several different places the charge is:-

(a) For the first 4 sets at $250 each set per annum.

(b) The next 4 sets at $200 each set per annum.

(c) Each additional set after the first 8 at $100 per annum.

(iii) Charges for Government Departments to be increased by *15%*.

(iv) All other charges to be increased by 15%, rounded to the nearest $10.

(v) One set of micro fiche to electronic data subscribers - $100.00.

(NOTE): If the Goods and Services Tax is applicable to the supply of micro fiche this would be added to the account.

(b) New Technology Committee:

The New Technology Committee comprises Messrs Hargreaves, Marks, Stewart and Allan. It appears that Videotext is a technology possibly suited to the distribution of sales data. There is also a proposal to re-write the Valpac programme into different modes suitable for 16 bit and/or other hardware systems. Three valuation firms have negotiated the purchase of sales data in tape form and have put in place their own retrieval mechanisms for extracting sales and building their own data bases. This is in addition to the 17 subscribers using data in a diskette format and a further two users taking printed sales information from an electronic system.

Mr Allan, the Chairman of the New Technology Committee, recommended the use of Mailmerge as a new membership distribution system and this was approved by Council.

(c) New Zealand Valuer:

There has been a marked decline in the material coming to hand for printing in "The Valuer", and to your Editor, a disappointing standard in some contributions received. The Editor reported that this has in part caused delays in producing "The Valuer". Also the content of the December and March issues was approximately 20% below comparable issues for the previous two years.

The Professional Directory has continued to grow, increasing from 53 listings in March 1984 to 67 by December 1984. Subscribers have reported back their satisfaction with the current system of listing.

Council discussed binding of "The Valuer" by volume and moved that this matter be incorporated in a newsletter for members' interest and action.

(d) Education Committee:

Mr Ralston presented his final report as Chairman of this Committee. He reported that the Post-Graduate Scholarship has this year been awarded to Mr L. Comely who is completing a post-graduate diploma in Horticultural Science at Massey University. The subject of his thesis and research work relates to the varying methods currently used for the valuation of horticultural land. It is anticipated that a report in booklet form will be published in due course, and this should benefit valuers in this area.

The Education Committee has proceeded to arrange for the publication of Squire Speedy's contribution to "Urban Valuation in New Zealand - Volume 2" as a separate book under the heading "Land Compensation". Squire Speedy has waived his writing fee for the publication, and the Education Committee with Executive approval, has arranged for payment of a $2,500 capital sum for the setting up by the Auckland University Council of a suitable prize to be known as the Squire Speedy Award.

Council has approved a special final examination for the five remaining candidates who have not yet passed the practical and oral examinations of the Institute. Council reconfirmed the appointment of The Board of Examiners and this appointment will cease at the end of this year.

Council recorded the grateful thanks of the Institute to the members of the Examination Board over many years.

In completing his report, Mr Ralston indicated that as a profession we need to focus on continuing education and make this our priority in the education field in the future.

(e) Publicity and Public Relations:

Council approved the appointment of an advertising agent and endorsed the direction taken to date by the Publicity and Public Relations Committee. In doing so, a national advertising campaign was authorised to be implemented forthwith.

In making his report to Council, the Chairman, Mr Kirkcaldie, stressed that the Property Market Report has again been a major exercise. It was released to the media during the first week of February 1985, and was widely distributed to the Press, N.Z. Radio, and Television.

After lengthy discussion on the issue of publicity and public relations, Council approved the setting up of a task force to prepare an exposure draft on the whole area of public relations and advertising, to report back to the October Council Meeting. It is clear that all professional groups are aware of the need to meet a change in this area and our Institute must move in the same direction.

(f) Assets Valuation Standards Committee:

Standards have been formulated since the meeting with T.I.A.V.S.C. An exposure draft will now have been received by all members of the Institute with comments and submissions to reach the General Secretary's office by 31st August 1985. Subject to changes, the standards will be formally ratified and adopted in October 1985 in accordance with the Code of Ethics as amended by Clause 16A at the 1985 Annual General Meeting.

There are now 27 countries represented in T.I.A.V.S.C., the most recent addition being Ghana. Applications are being considered from Switzerland, Nigeria and South Africa.

(g) Executive Committee:

A lesser number of complaints has been received for the current year. Also Mr A. J. Chappel replaced Mr A. Fear on Executive during the current term. Mr Chappell is the General Manager of the Rural Bank.

(h) N.Z.I.V. Services Limited:

N.Z.I.V. Services Limited was incorporated as a Company on the 4th May 1984 and presented its first Accounts to the 31st December 1984. During the year it has been involved in the sale of hardware and software to valuation practices. No dividend or Directors' fees were approved for the current year.

(i) Land Professionals Mutual Society (Inc.), (L.P.M.S.I.):

The majority of public valuers in New Zealand are now insured through the L.P.M.S.I. Mr A. L. McAlister in providing his brief report indicated that our interest in the Society was proceeding on a satisfactory basis.

(j) Council of Land Related Professions:

All five Presidents met in Wellington on the 7th February 1985. At the 21st March 1985 meeting,. Mr F. Easdale was reappointed Chairperson, and Mr M. Hartshorne was appointed Vice-Chairperson. Mr E. S. M. Keys was appointed Secretary/Treasurer. Messrs Horsley and Jefferies were appointed our delegates to the Council for the forthcoming year.

(k) G.S.T.:

A sub-committee comprising Mr J. N. B. Wall,. Mr R. E. Hallinan, Mr A. P. Laing and Mr R. L. Jefferies was formed to consider the White Paper on Goods and Services Tax which is *now* available.

REMITS:

Council approved the following:

"That for graduates who join the New Zealand Institute of Valuers within the calendar year of graduation the annual subscription for that year be waived and only the joining fee be charged."

"That the Education Committee be requested to look at the whole question of New Zealand Institute of Valuer Awards and report to the. October Council Meeting."

PAN PACIFIC CONGRESS - HAWAII:

Council received the report advising that arrangements were well in hand to enable our members to attend the 13th Pan Pacific Congres& of Real Estate Appraisers, Valuers and Councillors in Hawaii in February 1986. The Institute has been allocated a plenary paper and a choice of workshop papers. The conference venue and accommodation is at the 1900 room Sheraton Waikiki Hotel on Waikiki Beach, at a special group rate.

Council approved the expenditure of a sum associated with promotion at Hawaii of the 14th Pan Pacific Congress scheduled for Christchurch in March 1988.

PAN PACIFIC CONGRESS - CHRISTCHURCH:

Preliminary planning and discussions are well in hand for the 1988 Pan Pacific Congress at Christchurch. Council approved the engagement of Convention Consultants and the payment of a "fixed administration charge".

APPOINTMENT OF OFFICERS AND COMMITTEES:

(i) Executive:

McAlister - A. L. (Chairman).
Cooper - K. J.
Chappel - R. J.
Wall - J. N. B.
McDonald - H.

(ii) Publciity and Public Relations:

Kirkcaldie - G. (Chairman).

(iii) Professional Practices;

McAlister - A. L.
Horsley - G. J.
Hallinan - R. E.
Jefferies - R. L.

MEETING WITH REGISTRATION BOARD REPRESENTATIVES:

Mr M. R. Hanna, Mr P. Tierney and Mr S. W. Ralston were welcomed to the Council Meeting by the President of the Institute.

Mr Hanna outlined the Board's work during the year. This was obviously very substantial, and included the processing of 99 applications for registration, of which 83 were registered, 11 were deferred, 4 declined and 1 awaits the Board's decision.

Five complaints were received against valuers of which three were investigated by the Valuer General, one is currently under investigation and one has lapsed. Of the three investigated, two resulted in an inquiry, and in the third no inquiry was deemed necessary.

The number of complaints is of concern to the Board and it intends to continue publishing decisions in `The Valuer'. The editing of decisions will not necessarily be the case henceforth and the Board will exercise its discretion on the publication of names.

ANNUAL GENERAL MEETING

22nd APRIL, 1985

The President Mr R. M. (Morley) Donaldson introduced the President-Elect of the Institute Mr G. J. Horsley and his Vice-Presidents Mr R. E. Hallinan and Mr R. L. Jefferies.

The Minutes of the 45th Annual General Meeting were summarised briefly by the General Secretary and passed as a true and correct record.

The Annual Report and Accounts were taken as read and the President highlighted certain activities in the report including the widening affairs of the Institute, a greater use of the depth and talent within the Institute outside the Wellington area, a 7% growth in the number of Public Valuers with the potential for a larger growth in the forthcoming year, and a movement towards a publicity programme in response to the wishes of members.

Mr M. R. Mander was elected a Life Member of the Institute and this was approved by acclamation of the meeting.

Mr N. H. Chapman was reappointed the Auditor of the Institute's Accounts for the forthcoming year.

The six Fellows of the Institute were named and received a vote of acclamation from the meeting.

There were three Notices of Motion. All Notices of Motion were carried by the meeting and are recorded below:

1. Rules - Section 14 (1).

Rule 14 (1) was amended to read as follows: "Any member who has attained the age of 60 years and who has retired from professional work, business or employment as a valuer, on supplying to the Council proof of his age and retirement, and so long as that retirement continues shall be entitled to retain his membership of the Institute and his classification as a member on payment of an annual subscription prescribed by the Council from time to time and subject to Rule 8 (2) hereof shall be entitled to all the privileges as a member of the institute.

2. Rules - Section 69 (F).

Rule 69 (F) was amended to read as follows: "It may as necessary from time to time appoint a sub committee consisting of three public valuers who are members of the Branch, of whom any two shall constitute a quorum, with power to examine any matter relating to professional charges referred to it by a member of the Institute or by a member of the public and, following any enquiries made by it, the Committee may render an opinion as to the appropriateness of the particular charges in question."

3. Code of Ethics - Clause 16:

Clause 16 of the Code of Ethics was amended by the addition of the following new clause:

16A. Council may from time to time after due consultation with members adopt and publish guidance notes, standards or practice notes for observance by members. Such guidance notes, standards or practice notes will be complied with and be binding on members as if they formed part of the Code itself".

The incoming President thanked Mr Donaldson for his dedication to the Institute affairs over the past years and particularly during his term as President. Morley Donaldson prior to closing the meeting expressed his grateful thanks to the Central Districts Branch for conducting an excellent Seminar.

Letters to the Editor

Professionalism and the Philosophy of Valuation.

Sir,

The topic I wish to canvass is broad but hopefully capable of defined comment - it relates to our existence as a legitimate group professing to have special skills. In raising these matters my main purpose is to elicit other opinions.

Since becoming involved in valuation I have had misgivings about the manner in which valuers apply the "willing buyer, willing seller" concept. In New Zealand this has a legal basis in several statutes and I have no argument with this.

My concern relates to the practical application whereby sales evidence is slavishly adopted as a sole method of valuation. An example may be found in Wellington where two government revaluations have occurred during real estate `booms' in 1974 and 1984. Almost before the valuations were notified these had evaporated (predictably!) leaving instances of sales below government valuation.

Is it good enough, as professionals, to shrug and say "so what? . . . we only reflected the market at the time". Are we locked into a transitory concept of value that may prove invalid only weeks later? What of a mortgagee whose time horizons are, necessarily, somewhat longer?

The question really is whether to treat the market as God or whether to be dispassionate and look to timeless measures of value. What happens in practice is that sales reported during a property boom or crash are rapidly translated by valuers into firm predictions for other properties. The tendency is for an exercise in extrapolation to take place which results in an aberrant market being used to fix authentic values.

Yet most valuers have been around long enough to know that overbought or oversold markets are, by definition, short-lived. Are they doing clients, whether public or private, a disservice by perpetuating emotive trends in the market? And what is the alternative?

I think the first point to examine is our claim to be professionals. If this is so, then we must offer more than a competent clerk, or computer, can. By this I mean that if current comparable sales evidence is to be the sole criterion of value then we should use machines rather than people to do valuations. The beauty of using a trained person should be that they have a sense of perspective and judgement unavailable to computers ... this is presumably what valuers are paid for.

We are trained, in effect, to be urban or rural land economists - not clerical processors of sales data. This is ultimately what sets valuers apart from real estate agents . . . the latter will have a good idea how much he can sell a property for, but a valuer should know what it's really worth. In a normal and stable market there will be no difference between them - but in unstable markets there will be. Under such circumstances it is incumbent on a valuer to have regard to earning potential, replacement cost, depreciation, opportunity cost etc. Of course it will cause passing embarrassment but valuations must pass the test of time.

It is quite commonplace for an economic value, based on assets and earnings etc., to be placed on a company's shares which may be selling for much more or less. A prudent accountant would have more regard to these factors than to transactions which may be distorted for any number of reasons. As a perfect parallel, this is the difference between a `valuer of shares' (maybe a corporate entity) and a sharebroker.

Brierley Investments, for example, doesn't 'phone a broker to find out the value of a share ... only the current price. The question of real worth is one to be determined by experts not traders. Surely this clear division must apply in our profession?

I hope these comments will serve to promote some discussion of what seems to be a vital topic.

Yours faithfully,
J. B. C. Lenart, A.N.Z.I.V.

Internal rate of return

Sir,

I write to congratulate Mr John B. Wall for his excellent article on Internal Rate of Return (IRR) published in your December 1984 edition of the New Zealand Valuer.

The concept of IRR is not always easy to convey to the uninitiated, and I think the first example using an outlay of $100,000, an annual cash flow of $10,000, and a redemption value of $100,000 (giving a year 5 cash flow of $110,000), illustrates the concept of an IRR of 10% when Nett Present Value = 0; very clearly. Especially so as when followed by the second example which showed an IRR of 14.76%.

N.Z.I.V. members may be interested to read my article, published in the January 1984 edition of "The Valuer", entitled "Equated Yield, Jargon or Genuine." A copy of the article is enclosed.

While the calculation of IRR or NPV is not a primary valuation process, it can with practice, become a most useful tool in testing "best" and "worst" and "most probable" future cash flow predictions. These may give a range of possible values which have been accurately quantified; far better than the results of capitalisation of year one income, using selected capitalisation rates, drawn from a wide margin by the valuer's intuition. The final result and valuation will be by capitalisation, but from a capitalisation rate selected from a narrowed field, assisted by the IRR /NPV process.

Yours sincerely,
DUNCAN ROSE, F.A.I.V.

(Australian Taxation Office, Adelaide).

EDITOR'S NOTE:
The author's article is printed in this issue of "The Valuer".

Membership

ADMITTED TO INTERMEDIATE:

Archer (Ms) K. E.	Wellington.
Bennett, R. S.	Auckland.
Bevin, M. J.	Auckland.
Franklyn, M. C.	Canterbury/Westland.
Glew, D. J.	Auckland.
Irving, M. P.	Canterbury/Westland.
Jarman, C. R.	Auckland.
Khan, Y.	Auckland.
Kwang Heng Lee (Miss)	Overseas.
Leijh (Miss)	Auckland.
Lemoto, S. N.	Overseas.
Lindsay, J.	Northland.
Lucas, T. W.	Canterbury/ Westland.
Mitchell, I. E.	Northland.
McBride, I. R.	South Canterbury.
McCarroll, S. L.	Wellington.
McGowan, I. R.	Auckland.
McKeown, K. G.	Auckland.
McQueen, A. T.	Nelson.
Peters, R. O.	Wellington.
Pittar, A. V.	Rotorua/BOP.
Scott, M. J.	Auckland.
Sellar, A. K.	Hawke's Bay.
Sherlock, M. T.	Central Districts.
Smith, G. M.	Gisborne.
Smith, S. S.	Auckland.
Stewart, K. R.	Rotorua/BOP.
Woolerton, D. R.	Rotorua/BOP.

ADVANCED TO ASSOCIATE:

Allock, C. D.	Auckland (as at 2/5/85).
Aston, P. D.	Rotorua/Bay of Plenty.
Bellingham, J. W.	Waikato.
Blincoe, S. J.	Auckland.
Buchanan, D. R.	Hawke's Bay.
Carmichael, A. L.	Wellington.
Carruthers (Ms) E. A.	Auckland.
Crookes, G. M.	Waikato.
Dryden, (Ms) S. E.	Canterbury/Westland.
Fong (Ms) E.	Auckland.
Gavey, N.	Canterbury/ Westland.
Gunton, M. K.	Canterbury/Westland.
Heron (Ms) C. J.	Auckland.
Hill, G. W.	Rotorua/Bay of Plenty.
Hudson, P. D.	Rotorua/BOP.
Lee, S. T.	Overseas.
McIntosh, S. R.	Auckland (as at 28/2/85).
Morrin, B. P.	Auckland.
Paul, B. E.	Otago.
Plume, A.	Auckland.
Rhodes, J. B.	Auckland (as at 5/3/85).
Rope, R. W	Auckland.
Russell, T. L.	South Canterbury.
Senior, P. W.	Wellington.
Spencer, P. R.	Northland.
Spiers, G. D.	Hawke's Bay.
Stanley, C. N.	Canterbury/Westland.
Wall, D. S.	Wellington.
Wright, D.	Waikato.

RE-ADMISSION:

Bristow, M. J.	Wellington.
Plume, A. J.	Auckland.

REVERTED TO NON-PRACTISING:

Ellett, J. R.	Overseas:
Gibbons, R. W.	Canterbury/Westland.
Glossop, P .	Auckland.
Jackson, E. D.	Wellington.
McBain, J. E.	Auckland.
Marsden, R. J.	Overseas.
Matthews, M. C.	Northland.
Sadler, R. G.	Auckland.
Smith, D. M	Auckland.
Twaddle, A. G.	Wellington.

RETIRED:

Boswell, W. G.	Auckland (Rule 14(2)).
Brown, H. L.	Otago (14(1)).
Bryant, A.	Rotorua (Rule 14(1)).
Foster, R. D.	Wellington Rule 14(1)).
Gilliand, D. W.	Auckland (Rule 14(2)).
Hem, A. M. (14.2)	Auckland.
Miller, N. M.	Waikato (Rule 14(2)).
Munro, J. L	Waikato (14(2)).
Mygind, B. A.	Wellington (14(1)).
Sale, V. S.	Auckland Rule 14(1)).
Thomas, R. J.	Wellington (14(1)).
Vaile, G.	Auckland (Rule 14(2)).
Wade, M. A.	Auckland (Rule 14(1)).
Warner, H. V.	Auckland 14(1)).

RESIGNED:

Aston, P. D.	Rotorua/BOP.
Bird, R. J.	Rotorua/BOP.
Blucher, K. J.	Waikato.
Bristow, M. J.	Auckland (Reg.).
Butcher, W. H.	Waikato.
Chambers, S.	Waikato.
Cockburn, C. H.	South Canterbury.
Cotter, P. N.	Canterbury/Westland.
Cottrell, M. B.	Canterbury/Westland.
Croucher, B. J.	South Canterbury.
Eastgate, A. G.	Gisborne.
Ellis, R. B .	Southland.
Evans, P. K. M.	Gisborne.
Glover, P. E.	Wellington.
Gunning, M. F.	Central Districts.
Halstead, L. R. W.	Wellington.
Hood, T. B.	Canterbury.
Kerr, A. J.	Wellington.
Keyte, P. L.	Waikato.
Lemon, M. H.	South Canterbury.
Lander, R. B.	Taranaki.
Loveridge, P. J.	Central Districts.
McKeafe, I. D.	Wellington.
Shalders, G. R.	Central Districts.
Stansell, J.	Auckland (Reg.).
White, S. A.	Auckland.
Wild, J. P.	Auckland.

DECEASED:

Dodd, A. L. F.	Nelson.
Mason, N. J.	Northland.
Sutton, H. E. T.	Southland.

REMOVED FROM ROLL OF MEMBERSHIP:

Muir, W. A.	Auckland.

Computer Wise

VIEWDATA.

by R. *V. Hargreaves*

Bob Hargreaves is a Senior Lecturer in Valuation at Massey University, Palmerston North. He is also the Councillor for Central Districts and is a member of the New Technology Committee.

Viewdata is the generic name for one of several systems that uses telecommunications to send information between computers and remote terminals. Viewdata (also known as Videotex) was first developed by British Telecom in the United Kingdom during the early 1970's.

Viewdata was originally aimed at the mass residential market in the U.K. and was designed to be as easy to use as the telephone. Although Viewdata in New Zealand is aimed more at the business market, there is no doubt that the system is user friendly and that the "KIS" (keep it simple), principle has been adhered to. People selling Viewdata systems find that there is no need to run training courses for users.

Experience in the United Kingdom indicates that viewdata has particular applications for volatile information such as sharemarket prices, interest rates, real estate listings, real estate sales, livestock prices, and farm input costs.

How does it work?

Viewdata combines two of the elements that are already present in almost all houses in New Zealand. These are a telephone and television set. The telephone is linked to the television set through a viewdata terminal that incorporates a microprocessor and built in modem. The user controls the system through a small key pad which is not unlike a remote control for a television set or a hand held calculator. The viewdata system is programmed using an indexing system with pages being identified by numbers. Most of the pages of information that appear on the TV screen are printed, but viewdata also has some graphics capability. With the addition of a modem and communications software, most common brands of micro-computers can be used as viewdata terminals. Figure 1 illustrates how the telephone system is used to connect the user to computers both in the home, country and other computers around the world. Whereas purpose built viewdata terminals can generally only access information stored in viewdata format, micro-computers can also access a wide variety of other data bases.

Viewdata information can be made available on a restricted or unrestricted basis. Most professional organisations want to limit access by other groups and form a closed user group (CUG). For example, an information provider (IP) such as the New Zealand Institute of Valuers could supply real estate sales and statistical information only to those valuers that subscribed to the system and had a valid password.

See Fig. 1: A Viewdata System for Valuers.

The veterinarians are the first professional group in New Zealand to use viewdata. Features of "Vetlink" are information on animal remedies, diagnostic assistance, a mailbox and bulletin board, classified advertisements, and company price lists. A number of companies in New Zealand are planning to use viewdata for communication between branches and Federated Farmers have recently chosen viewdata for communication linkage with farmers.

Public information available through viewdata is presently confined mainly to airline timetables and financial data. Doubtless this data base will expand rapidly as the number of users increases.

The New Zealand Post Office is supporting viewdata by making their packet switching network available to users. Packet switching utilises computer technology to rapidly move large volumes of data around the country at a current cost of 8 cents per minute irrespective of distance.

FIGURE I: A Viewdata System for Valuers

Applications for Valuers

The N.Z.I.V. Technology Committee are currently exploring the feasibility of mounting the property sales data presently contained on microifche on a viewdata computer. This information could potentially be updated daily and manipulated using a "Valpak" type sales retrieval programme.

Several real estate firms in New Zealand are following the example of their United Kingdom counterparts and using viewdata as a means of storing, manipulating and retrieving current properties for sale. This information is likely to be of considerable interest to a number of valuers who may wish to subscribe to a multiple listing type real estate user group. Other applications that would probably follow a sales system are the electronic distribution of information in the N.Z.I.V. statistical bulletin, a rental data base, a bulletin board for valuers, and access to specialised computer programmes such as replacement cost estimation.

With the increasing emphasis by lenders on the borrower's debt servicing ability valuers are also likely to make use of viewdata as a source of up to date budgetary information. Electronic title searches have been introduced in Australia and viewdata could be used for this in New Zealand.

Cost Considerations

Provided that a valuer already has access to a telephone and a television set then the only piece of equipment required is a viewdata terminal. The capital cost of the terminal is approximately $1200 or the terminal can be rented for around $30 a month. If the valuer already has access to a microcomputer then a viewdata terminal would not be required. The communication equipment and software to connect a microcomputer to viewdata would be slightly less than the cost of a purpose built viewdata terminal.

Printers and tape or disc storage can be added to the system as finance permits.

The costs of belonging to a valuation closed user group have not yet been calculated since the computer programming requirements have not been specified. Cost will also depend on the number of users, but is likely to be somewhere between the cost of the microfiche service and the present system of mailing out floppy discs.

There are significant capital cost savings to be made if valuers work together and share a sales data base rather than all attempting to set up their own sales data bases. The reason for this is that users will be able to get by with smaller computers and less disc storage capacity.

Additional cost savings can be achieved by eliminating the duplication of effort required for individual firms to continually keep in house data bases updated.

Disadvantages of viewdata and potential pitfalls

In the United Kingdom viewdata is very much controlled by British Telecom who provide the telephone system and computers. The New Zealand Post Office is playing a much more passive role and at this stage only provides access to the telephone system. Viewdata here may develop into a private enterprise system dominated by various computer companies. The danger of an ad hoc approach is that the direction viewdata takes may be dictated by computer companies rather than the needs of the users. Any viewdata system must, as its prime consideration, find out what the potential users are interested in and provide them with that information. For example, the National Farmers' Union in the United Kingdom spent about five years doing research into viewdata and the needs of farmers in the United Kingdom before they actually mounted the system. Viewdata is programmed to show the volume of use for each page of information and this provides rapid feedback on what the users are interested in. Planning is also required to make sure that volatile information is regularly updated. People simply won't use the system unless they can be sure that they are dealing with the most current information. A considerable amount of man power is required to keep a system updated but there is significant cost saving if this is done on a centralised basis. Because viewdata systems rely on using the phone lines to move information around the information can be corrupted if there is interference on the telephone lines. Interference should be insignificant except in a few country areas where people are still using party lines.

Summary and Conclusions

The computer revolution has led to an information revolution. Part of the information revolution is using the telephone system to transfer data between computers. Viewdata is one of a number of overlapping technologies that allows this type of information transfer to occur. Viewdata has the attraction of being so simple to use that many people who would not normally use a computer terminal become information users.

The precedent provided by our valuer counterparts in the United Kingdom, U.S.A., Australia and Canada makes it inevitable that centralised data bases with user access from remote terminals is the blueprint for the future.

INTERNAL RATE OF RETURN.

The calculation of the Internal Rate of Return in Volume 25, No. 12, Page 679 at 14.82% is incorrect. The correct I.R.R. is 16.13%. The redemption value of $6,157,000 was treated as an end of year 9 income, It should have been added to the Year 8 income of $584,915, to give a total Year-8 income of $6,741,915. The present value of the cash-flows then equates the outlay of $3,645,000 at 16.13%. Editor.

Application of the Opportunity Cost Doctrine to Right-of-Way Valuation

By Theodore Reynolds Smith and Ahmed Kooros

Theodore Reynolds Smith, Executive Vice President of The Keystone Centre, previously served as chief operations officer for the Council of Energy Resource Tribes and as chief economist for the Department of Savings and Loan, State of California. Dr. Smith has been an economist for the Harvard Law School and the Harvard University Institute for International Development.

Ahmed Kooros is the Chief Economist for the Council of Energy Resource Tribes. Dr. Kooros was formerly the Deputy Minister for Oil and Economics, Ministry of Economics and Finance, Government of Iran. He has been on the staffs of Stanford University, University of Santa Clara, and Rutgers University.

Introduction

There has been an historic attempt to build an economic foundation to support what have come to be known as the "three approaches" to value in real estate appraisal. The "real cost" principle of the English classical economists has served as the basis for the accepted approaches to value. Appraisers are taught that the summation of cost components should represent a valid indication of real property value. Moreover, if properly applied, this replacement cost indication of value should correlate with what the market (sales) and income approaches suggest. Due to insufficient information this process of applying the three approaches to value frequently requires the manipulation and re-use of much of the same data. Arch Woodruff has aptly suggested that this process of recirculation of data when applying the three approaches to value represents an application of the theory of "redundant logic." The implication is that possibly more attention should be devoted to developing better appraisal tools, as in the advancements made through mortgage equity appraisal techniques.

This discussion is designed to explore some directions appraisal practice might take in situations where accepted techniques are deficient. Consequently this article will stress the insights gained from the opportunity cost doctrine' and how, under certain circumstances, its expanded application might serve to correct some of the methodological deficiencies found in the standard three approaches to value.

Economic Rent

Appraisers make a distinction between contract rent and economic rent. Contract rent represents the actual amount a tenant is paying for use of the premises; economic rent is the amount the tenant would be willing to pay? By not charging the tenant a rental equal to the amount suggested by the prevailing market, the property owner is experiencing an opportunity cost.

The magnitude of this variance is depicted in Figure 1 as the difference between (p2-pt), where the owner's current contract rent schedule suggests a demand curve of dl, while the prevailing market demand comes closer to approximating d2. Marshall has identified this condition as consumer's surplus.' The excess of the price which a consumer would be willing to pay rather than go without the property, over that which is actually paid, is the economic measure of this surplus satisfaction.4 What is represented as a surplus to the consumer can be considered as an opportunity cost to the property owner. In economic theory, opportunity cost is the cost of any particular course of action reflected by the amount of gain which could have been obtained by pursuing the next most desirable alternative.5 The concept was developed between 1871 and 1914 and was principally expressed by the Austrian economists.' A key ingredient of the opportunity cost doctrine is the necessity for choice. The "choices which are compared must be real and not illusory if the doctrine is to have meaning.[m] Although not explicitly recognized as such in appraisal literature, elements of the opportunity cost doctrine are already present in existing appraisal practices which contrast contract and economic rent. Kinnard has also introduced the concept of opportunity cost in his discussion of substitution as it applies to replacement cost. According to Kinnard, "the informed and rational purchaser-investor will pay no more for an existing improved income property than the cost to him of producing a substitute property with the same utility."8

Non-Market Conditions

It is accepted appraisal practice for the appraiser to look to the market for answers to unknown situations. In most instances, the appraiser should verify the economic viability of contract rents by searching the market for comparable rental data or economic rents? Economic rent still means the prevailing market rent. Unfortunately, there will arise those conditions where there are no comparable properties and, as a consequence, no available economic rents. In these cases the appraiser is asked to stretch the imagination to the point where, in some instances, hypothetical examples are used to simulate free market conditions. The use of hypothetical examples is particularly prevalent in the application of the highest and best use principle in condemnation cases. The highest and best use concept is used to value land based upon a utilization plan which will "produce the greatest

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FIGURE 1
MARSHALLIAN CONSUMER SURPLUS: OPPORTUNITY COST

future benefit to the owner."10 Determination of highest and best use requires a keen imagination on behalf of the appraiser. According to the American Institute of Real Estate Appraisers, "it may be necessary to produce a series of gross and net income yields from hypothetical buildings of various types and sizes, to derive a use and programme of future utilization producing the highest present land value."11

Further consideration needs to be given to those circumstances where market conditions, real or imagined, do not exist. It is all too often that the appraiser is dealing with situations where market information is not available. The United States has gone through periods where entire blocks of land in depressed urban centres were turned over to the tax collector because there was no purchaser willing to assume ownership. At the other extreme, there exist large tracts of land-either governmentally or privately owned-where there is no desire to place the property on the market. Yet these situations frequently require access in the form of rights-of-way for the construction of highways, dams, pipelines, or power transmission lines. In these cases there may not be any real or imagined sales of comparable property, for example, where a strip of land is being acquired for the purpose of a right-of-way. The owners may be indifferent at best to the awarding of a right-of-way; especially if the use is to generate profit for a company which will be transporting high value goods such as oil or gas.

Under these conditions it may prove productive to consider a thought suggested by Caves in another context, wherein he stated: "if factors of production are indifferent among various employments, then opportunity costs furnish a sufficient measure of the cost of securing.any particular output."12

Caves goes on to suggest that "the opportunity cost approach emphasizes the valuation of alternative choices of goods . . . "13 There exists an underlying issue which must be resolved when valuing property for right-of-way and that is whether it is necessary to have comparable sales. What is the best means of valuing what is essentially a non-marketable commodity?

Market Value

The Constitution of the United States of America provides that "No person shall . . . be deprived of life, liberty, or property, without due process of law; nor shall private property be taken for public use, without just compensation. 1114 This constitutional principle is deeply embedded in case law and judicial decisions. During the past two centuries lawyers and judges have fought to bring a practical meaning to the concept of "just compensation" and how to determine its value.

Central to the estimation of value is what has grown to be the concept of "market value." "The market value estimate has been defined as an interpretation of the reactions of typical users and investors in the market."15 Those ingredients thought to be most significant when defining market value are summarized as follows:

1..... the most probable price in terms of money which a property should bring in competitive and open market under all conditions requisite to a fair sale;

2. . . buyer and seller, each acting prudently, knowledgeably and assuming the price is not affected by undue stimulus;

3..... . a reasonable time is allowed for exposure in the open market.16

A reading of these ingredients which comprise market value does not yield a significant degree of commonality between the concept of market value in the awarding of just compensation and the condemnation of property for rights-of-way. Any specific transaction in real estate is so strongly influenced by personal considerations of both the buyer and seller, that it is seldom a pure expression of the meeting of the minds as to the real estate alone. Fair market value, as determined by one or more of the three conventional valuation methods, is based on certain assumptions, and central to these assumptions is the marketability of the land. These assumptions create and define a domain of obscurities surrounding the concept of fair market value, when, as in the case of federal lands, corporate- or family-held estates, and American Indian reservations, the land is not marketable.

There would appear to be very clearly defined circumstances where the traditional theory of market value is not appropriate. Why should the owners of land, which has not been-and will not be-placed upon the open market, be limited in the value received for their property due to an interpretation of market value which is biased in favour of an agency or company exercising the power of eminent domain? Transmission pipelines being constructed across the United States require the acquisition of thousands of miles of right-of-way; frequently across uninvited land. For much of the land involved, there will be no clear-cut market value-only the simulated efforts at arriving at an appraised value through the frequently unfounded application of the three approaches to valuation. What is needed is a means whereby the property owner which contrasts contract and economic rent. can better realize a fair price for land being condemned. It is not truly just compensation when an owner is required to sell land which is not for sale, to a purchaser who will in turn realize a significant gain from the acquired land. There are other means of arriving at a value which are better founded in economic principle and theory, and provide a more equitable basis of determining and measuring just compensation.

The Opportunity Cost Doctrine and Value

The opportunity cost doctrine would appear to suggest an alternative to the conventional means of appraising rights-of-way. Following up on Caves' suggestion, the value of a good can be suggested through consideration of alternative choices. One such consideration might be the choices available to the party attempting to secure the right-of-way.

In the event the party exercising the power of eminent domain could not acquire the right-of-way, it would necessitate alteration of the pipeline route. Such a detour would probably increase production costs, and the tariff charged the customers would increase accordingly. Hence, in the condemning of a right-of-way over land, the land must be viewed as a critical factor of production, the use of which is embodied with so-called opportunity cost. These opportunity costs are defined as the cost of the next-best, or most likely alternate pipeline route which detours around the parcel being condemned. It is this opportunity cost saving, realized by the use of the desired land for a right-of-way, which represents the true value-added associated with the awarding of the right-of-way. Therefore, one must look at this land as a factor that is directly responsible for the generation of value-added; a condition which will exist as long as the right-of-way is used for its intended purpose.

The magnitude of the value-added in the case of a pipeline right-of-way is the amount of tariff that the pipeline owner charges his customers for its use. Typically, tariffs are levied on a per-barrel-transported basis, and they must include both the cost of the pipeline and a reasonable per-barrel; profit for the owner. The tariff fee will therefore vary with the production cost of the pipeline which consists of land costs, the cost of the pipeline itself, its pumping stations, and operational maintenance. The tariff rate will therefore greatly depend on the route and length of the pipeline.

An example of this application of the opportunity cost doctrine can be seen by referring to Figure 2 which depicts a map showing the desired right-of-way for a pipeline and the alternate opportunity which exists for the pipeline company. By following the desired route, four property owners must be contacted as compared to 19 owners who must be dealt with if the alternate route is used. Most of the alternate route involves the acquisition of irrigated farmland, as compared with dry rangeland for the desired route. It is estimated that the land acquisition costs for the desired route would be $150,000, while the alternate route would require $957,000 for land acquisition (this amount includes increased administrative costs). Construction costs amount to $6,229,080 for the alternate route, as

FIGURE 2
OPPORTUNITY COST DOCTRINE
RIGHT-OF-WAY OPTIONS

		ALTERNATE RIGHT-OF-WAY
	DESIRED RIGHT-OF-WAY	ALTERNATE RIGHT-OF-WAY
LAND ACQUISITION	$150,000	$957,000
CONSTRUCTION COST	4,356,000	6,229,080
TOTAL	$4,506,000	$7,156,000

OPPORTUNITY COST: $7,186,080 - $4,506,000 = $2,680,080

compared to $4,356,000 for the desired pipeline route. If required to use the alternate route, the company would have to pay an additional $2,680,080. This $2,680,080 represents the opportunity cost confronting the land owner if only the $150,000 land costs are paid for the right-of-way. The value of the opportunity cost represents the upper boundary which the landowner would therefore aspire to receive as compensation for granting the right-of-way; while, as can be expected, the condemning party would like to limit the payment to $150,000.

The morality of the situation becomes even more obscure if the party condemning the property is going to utilize the right-of-way for the transport of gas, oil, coal in a slurry form, or some other high value substance. A percentage profit will be made with the passage of each barrel, mcf, or ton.

As time passes and the value of these items increases, as it is surely expected to do, the owner of the right-of-way will be confronted with increasing revenues as the result of having possession of the right-of-way. Should the operator of the pipeline keep all of these "price escalation returns" or can a case be made for the original landowner to share in future benefits? There are cases where the landowner has received payment reflecting a major portion of the opportunity costs as well as a share in the future benefits over time.

An Application of the Opportunity Cost Doctrine

The opportunity cost doctrine has been applied by the authors in the valuation and negotiation of several right-of-way agreements between American Indian tribes and energy transmission companies. The financial gains of applying the opportunity cost doctrine have been striking. As an example, the Four-Corners Pipeline Company, which had originally proposed to pay as compensation for the 20-year right-of-way renewal a lump-sum of over $300,000 to the Navajo Nation, agreed finally to pay in excess of $92 million during a 20-year period. Specifically, the agreement provided for the following financial provisions:

1. Payment to the Navajo Tribe of three cents per barrel of crude throughput; which amounted to close to a $500,000 payment for the first year of the new right-of-way grant.
2. Compensation for the first year will be adjusted upward according to the Consumer Price Index to determine compensation for subsequent years. This provision will guarantee the purchasing power of the Navajo Tribe against inflation of later years.
3. A $40,000 per annum scholarship fund to educate Navajos in the fields of engineering and business.

These are the most visible financial features of the Navajo Four Corners agreement and they have yielded immense financial consequences for the Navajo Tribe. This agreement, though it was a pioneering effort, is not the only one negotiated for Indian tribes by the authors using the opportunity cost doctrine; there are three other cases which have now become a reality. A summary of the three most recent examples is as follows:

1. A 6.9 mile, eight-inch pipeline right-of-way with a carrying capacity of 7,500-8,000 barrels per day of refined petroleum products. After an initial right-of-way valuation of $2,000, the Three Affiliated tribes of the Ft. Berthold reservation signed an agreement with CENEX for $286,000.
2. A sixty-four mile, twelve-inch pipeline right-of-way with a carrying capacity of 21,000-22,000 barrels per day of crude oil. The initial right-of-way valuation was $60,000, however, after applying the opportunity cost technique the Navajo Tribe signed an agreement with the Texas-New Mexico Pipeline Company for $1,760,000.
3. A thirty-four mile, thirty-inch natural gas pipeline with a capacity of 7,500,000 MCF per day. The owner received an initial offer of $191,000 based upon a traditional appraisal; however, after application of the opportunity cost, technique a right-of-way settlement of $1,500,000 was agreed to with the pipeline company.

These examples represent real world situations where there was need for a more fair representation of the landowner's interest; moreover,. they call into question the underlying foundation of the concept of just compensation. The large range of difference between the initial valuation and the agreed upon payment would suggest a significant economic rent accruing to the party acquiring the right-of-way, while the party granting the right-of-way is in a position of having to provide something that they do not wish to grant. There is indeed a serious question of "just compensation" in many aspects of accepted valuation methodology. Merely because the courts have used the best tools available to them at the time, in order to define the means of arriving at "just compensation," it does not mean that new techniques cannot improve upon the equity of the valuation criteria used by the American judicial system.

Conclusions

Acceptance of the opportunity cost doctrine clearly exists in existing appraisal principles-most notably in the use of economic rent and the principle of substitution. Under certain conditions there appears to be a serious deficiency in the application of the three approaches to value in the determination of just compensation for right-of-way acquisitions. An analysis of the opportunity cost doctrine has disclosed that it possesses the essential theoretical foundations to serve as an aid in determining right-of-way values. The authors have converted this theory into practice in several instances with results which have proven to be very beneficial to the landowners. The use of the opportunity cost doctrine is recommended for those instances where the more traditional approach seems to be biased against the landowners.

1. This concept draws upon and expands a note by the authors published in *The Appraisal Journal,* Vol. LI, No. 2, 1983, pp. 294-298, "The Opportunity Cost Doctrine: An Application to the Valuation of Tribal Land."

2. *The Appraisal of* Real *Estate,* 6th Ed. (Chicago, Illinois: American Institute of Real Estate Appraisers. 1973), p. 310.

3. Alfred Marshall, *Principles of Economics,* 8th Ed. (New York, New York: The MacMillan Company, 1948), p. 124.

4. Ibid. p. 124; also see: George J. Stigler, *The Theory of Price,* 3rd Ed. (New York, New York: The MacMillan Company), pp. 78-9.

5. H. H. Liebhafsky, *The Nature of Price Theory* (Homewood, Illinois.: The Dorsey Press, Inc., 1963), p. 152.

6. Joseph A. Schumpeter, *History of Economic Analysis* (New York, New York: Oxford University Press, 1959), p. 917.

7. Liebhafsky, p. 152.

8. William N. Kinnard, Jr., *Income Property Valuation* (Lexington, Massachusetts: Heath Lexington Books, 1971), p. 348.

9. William M. Shenkel, *Modern Real Estate Appraisal* (New York, New York: McGraw-Hill Book Company, 1978), pp. 207-10.

10. American Institute of Real Estate Appraisers, pp. 131-2.

11. American Institute of Real Estate Appraisers, p. 144.

12. Richard E. Caves, *Trade and Economic Structure* (Cambridge, Massachusetts: Harvard University Press, 1963), p. 221.

13. Caves, p. 221.

14. U.S. Constitution article V.

15. American Institute of Real Estate Appraisers, p. 273.

16. American Institute of Real Estate Appraisers /Society of Real Estate Appraisers, Byrl N. Boyce, Ed., *Real Estate Appraisal Terminology,* Rev. Ed. (Cambridge, Massachusetts: Ballinger Publishing Company, 1981) pp. 160-161.

Book Review

PROPERTY VALUATION IN SOUTH AFRICA AUTHOR A. J. JONKER BA (LAW),

MDP, PREP, MA (ECON) PUBLISHED BY JUTA & COMPANY LIMITED

When asked to review this book I expected from the Title, a conventional textbook on both the Principles and Practice of Valuation in South Africa. In other words, a "how" and "why" book. On an initial flick through, it was obvious that the reader is not to be told how to assess value but rather the much broader topic of matters affecting -value.

Having commenced to read you become somewhat disorientated. Is Jonker a valuer, lawyer or economist. Return to the preface together with the author's qualifications and you quickly realise that you are listening to a person who has a very sound knowledge of valuation, the law and economics. From then on, the book becomes absorbing reading despite the quite distracting overuse of footnotes at the bottom of each page, many of which would have had far greater impact to this reviewer if incorporated into the main body of the text.

New Zealanders will be interested to know that The Valuers Act 23 of 1982, came into operation in South Africa on 13 January 1983 and that the Valuers Council are in the process of registering property valuers. Like our own 1942 Valuers Act, the emphasis is on education but it was interesting to know that even old and experienced valuers who do not have the relevant qualifications, will have to receive same within five years.

The author's own preface states that the book has a particularly strong legal content which makes it suitable for use as a reference book by attorneys and advocates. On reading it, one could not agree more and Mr Jonker is obviously not afraid to question many past Court judgements and precedents. At the same time, the writer is also properly critical of methods of valuation which are so sophisticated as to be misunderstood by jurists and other valuers alike.

An intriguing aspect of this work is the obvious depth of research into writings beyond the shores of South Africa and in this respect New Zealand can be both flattered and proud of the repeated references to Jefferies, O'Keefe, K. J. Cooper and New Zealand Court decisions. Wisely though, Jonker has preferred not to be led astray by overseas case law and writings but prefers reliance on his own experiences in his own country.

The opening and longest chapter in this book is entitled "The Concept of Value". While one can suspect that extracts from legal decisions suit the author's own personal views, the following excerpt from a decision by Watermeyer J. in Durban Corporation & Another v. Lincoln relating to Ordinances that require land and buildings to be valued separately, struck an harmonious chord with this reviewer.

"A building standing upon a piece of land is like a picture painted upon a piece of canvas:

and just as it is impossible to sell the picture apart from the canvas on which it is painted, so it is equally impossible to sell a building apart from the land. It is possible to scrape the paint from the canvas and it is possible to pull the building down, but then the work has been destroyed and what is sold is not the building, but building material. In law, a building accedes to the land, it is not a separate property and cannot be owned as a thing separated from the land on which it stands. It is therefore idle to attempt to ifnd the market value of a building separately from the land on which it stands, and any valuator attempting to do this is pursuing the will o' the wisp."

The author emphasizes certain phrases from that decision and then goes on to develop a most interesting discussion on the willing buyer - willing seller concept pointing out that it is necessary to discern the difference between the approaches implied in the usage of the following key words:

(a) What price could have been attained.
(b) What price would have been attained.
(c) What price should have been attained.

That opening chapter is to say the least thought-provoking and one cannot help but be impressed by an author who is well prepared to question and debate the practicality of many Court decisions. One must however always be wary of the fact that any Court decision is made after having taken into account the totality of the particular circumstances and the quality of evidence given in that one instance.

One also gains the impression that the author tends to dwell a little too long on the oddities encountered by every valuer rather than the norm. Most valuers will be well aware that no Court decision, textbook or article can ever hope to lay down principles for those seldom found, special and unique problems.

In dealing with the various methods of valuation, Jonker quite rightly emphasizes the comparative sales method but in discussing income capitalization, the land residual method, discounted cash flows, summation approach and partial valuations, sums up beautifully in the following passage:

"In conclusion, it should be pointed out that the appropriate method of valuation in quantifying the value of a property must be ascertained in accordance with the nature of the property that is being valued. No one method should be given a general or blanket preference over another. The comparable sales method generally affords the best guide to actual market behaviour in valuing vacant land. The income approach generally affords the best guide to the valuation of income producing properties, while the discounted cash flow method serves as the best guide to the valuation of self-liquidating properties. The comparable sales method reveals actual market behaviour (even if unsophisticated or uninformed). Direct capitalization reveals an informed buyer situation, while the `discounted cash flow method' should be used virtually exclusively for the text of `a well-informed purchaser'."

What did this reviewer gain from the book? Apart from the shock of a very short reference to Court decisions relating to the Group Areas Act of 1971 and its reference to zonings for Blacks, Indians, Coloured. and Whites together with the effect of those zonings on value, that the valuation process the world over is very much the same.

It is a book that does not cover the practice of valuation but rather the principles and because of that, it is without doubt a book which despite its overseas origin is one that is the most perfect foil for the "how" or practice text. For New Zealand valuers it is well worthy of a place on your bookshelf if for no other reason than it makes you ponder far beyond the acceptance of sales without question, the nitty gritty of foot frontage and per square metre rates, the acceptance of extracts from a particular Court decision as being all-embracing and so on.

It is therefore thoroughly recommended but not really appreciated unless read twice and for both students and practitioners alike, well worthy of a place in your library.

R. M. McGough.

N.Z. INSTITUTE OF VALUERS

Tauranga Sub-Branch

Notice of Seminar on Leasing and Alternative Forms of Land Tenure

BAYCOURT THEATRE, TAURANGA
FRIDAY, 11th OCTOBER, 1985

9.00 9.30	Registration and Morning Tea.
9.30 10.00	Opening Address Mr W. Peters, M.P. for Tauranga.
Urban Session	
10.00 - 11.00	Speaker - Mr O. M. Newland, Property Developer, Auckland who will provide a market assessment on the leasing situation and current developments in Auckland.
11.00 - 12.00	Speaker - Mr McLennan, President of the Auckland Branch of the Building Owners and Managers Association who will provide a review on the recent amendments to the standard forms of measurement for different forms of tenancy, comment on how the market place influences net leasing versus the earlier traditional form of lease, etc.
12.00 - 1.00	Luncheon.
1.00 - 2.00	Speaker - Mr A. Robertson. Government Life Corporation who will present a paper on the development and marketing of the new Bayfair Shopping Centre at Mount Maunganui.
2.00 - 3.00	Speaker - Mr G. Wood, a Councillor of the Motel Association of New Zealand who will speak on Motel Leasing.
3.00 - 3.30	Afternoon Tea.
3.30 - 4.00	Commentary on Urban Session by Mr K. M. Allan, General Secretary.

Rural Session

10.00 - 11.00	Speaker - Mr D. Wright, Director of The Department of Maori Affairs, Hamilton.
11.00 - 12.00	Speaker Mr T. Te Kani, Maori elder. The above two speakers will both present papers on different aspects of Maori land leases.
12.00 - 1.00	Luncheon.
1.00 - 2.00	Speaker - Mr D. Horner, a partner in the firm of Horner & Greenlees who will speak on Horticultural Syndication.
2. OO - 3.00	Speaker - Mr R. Calver, Orchardist of Katikati who will speak on Share Farming.
3.00 - 3.30	Afternoon Tea.
3.30 - 4.00	Commentary on Rural Session by Mr W. A. Cleghorn, Rotorua-Bay of Plenty Branch Councillor.
4.00 - 5.00	Refreshments.

Seminar Registration Fee - $30.00 N.Z. Institute of Valuers members.
- $50.00 Non Institute participants.

The Registration Fee includes copies of papers. luncheon, morning and afternoon teas.

TEAR OFF HERE

SURNAME: CHRISTIAN NAME ....._ .

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Enclosed is my cheque for $_._._.... _._.. in payment of the Seminar Registration Fee.

Send To:

The Secretary,
Tauranga Sub-Branch,
N.Z Institute of Valuers.
P.O. Box 455,
TAURANGA.

Equated Yields Jargon or Genuine

by Duncan Rose, F.A.I.V.

The author is the City Valuer, Australian Taxation Office, Adelaide.

This paper is the development of an address given by Duncan Rose to members of the South Australia Division at the seventeenth annual Seminar, Adelaide, on 5th November 1982.

The term "Equated Yield" is appearing more and more often in real estate journals, "The Valuer" and in the "Australian Property News' and is becoming a recognised term in real estate jargon. It appears that the traditional Capitalisation Rate (1) used to value income earning properties, is under threat, and is being replaced by mysterious and more sophisticated techniques involving programmable calculators or computers. These techniques are collectively being called "Equated Yields".

This paper examines the function of the Capitalisation Rate and discusses its limitations in the valuation of complex urban income earning properties. The paper then goes on to fully describe the Equated Yield, and examines its possibilities and limitations.

It is hoped that this paper will help to clear up some of the confusion and misinterpretations surrounding the new techniques. It is also the aim of the paper to encourage valuers to master the use of more advanced calculators, so that they can learn and experiment with the new techniques, and make them work in practice.

The Capitalisation Rate

For years there have been only three basic methods used for the valuation of real estate. These are by direct comparison, by summation (the added values of land and buildings, stock and plant etc.), and by capitalisation of net annual income.

Using the capitalisation method, the valuer divides the annual net income of an income earning property by an appropriate Capitalisation Rate (expressed as a decimal) and thereby produces a figure which represents capital value. Alternatively he multiplies that net income by the Years Purchase (which is reciprocal of the Capitalisation Rate expressed as a decimal) and achieves the same result. When analysing a sale he goes through the same motions in reverse, and from the known data of sale price and net annual income, calculates a Capitalisation Rate or Years Purchase.

The method is simple and convenient, and enables properties, sale and subject to be ranked in terms of their capital values and Capitalisation Rates. Valuation follows by the selection of an appropriate Capitalisation Rate, and its appliation to the estimated achievable or actual net annual income of the property to be valued. The selection of the Capitalisation Rate from the data range available, and the final valuation figure, are both intuitive decisions made by the valuer.

Using the capitalisation method the valuer hypothsises a constant value annual net income for an infinite period. The philosophy behind that is the assumption that the present value of next year's income is the same as the full value of this year's income, and similarly for the third and fourth years, to an indefinite period: so we may just as well use the first year's full income and relate it to a known capital value. The other assumption is that if there is income growth, the capital value of the property will appreciate in proportion to the growth rate. The Capitalisation Rate thereby "reflects" the income growth and capital appreciation potential of the property. If the income actually is constant for an extended period then for that period the Capitalisation Rate could be said to represent the actual net yield on the capital cost or value of the property.

Historically the Capitalisation Rate was intended to be the true yield on capital cost (2). It is still regarded by valuers as a unit of measure, although its use is relative rather than objective. However, for the simpler property with say a single or dual tenancy, the application of a Capitalisation Rate as an indicator of the return on invested capital that the property should earn, is not so unrealistic, especially if the "net income" has been adjusted in some way to compensate for predicted income growth.

The Capitalisation Rate is useful to valuers mainly as a conversion factor. It converts earning potential into Capital Value. It can be said that its value when compared with the capitalisation rates analysed from sales of other properties, "reflects" the future earnings of the subject property. It reflects also the capital appreciation (or depreciation) potential of the property, and the relative security or risk of the investment. A skilled valuer can identify some or all of these qualities within the Capitalisation Rate, but would rarely find it necessary to quantify any of them. He would rather from his experience examine the sales data available and then select and apply an appropriate Capitalisation Rate in perpetuity to a single year net income achievable from the property to be valued. It is an intuitive selection, and the capital value so calculated may still be adjusted and rounded to reach the "Fair Market Value" of the property.

Although valuers are aware that the Capitalisation Rate generally does not measure the true desired investment return from the property, it may reflect the investment potential of the property, and with appropriate adjustments continues to be used as a capital value conversion factor.

It has become a cause of concern however to valuers when the Capitalisation Rate differs sub-

stantially from well known alternative investment rates.

When the first year income after sale demonstrates a Capitalisation Rate of 8% and we know that the purchaser could earn 12% in Aussie Bonds, the difference is 4%, half of the Capitalisation Rate. The difference is called the Reverse Yield Gap (the difference between the present earning rate, and what could be earned by realising the asset and reinvesting the money). What is happening of course is that the property is expected to earn a great deal more than 8% per annum on the capital cost, when anticipated future incomes including the eventual sale of the property are taken into consideration. In recent years major city properties have been selling for very high prices wherein the first year incomes have been less than 5% of capital cost, and the apparent Reverse Yield Gap has been nearly 10%. To consider such a Capitalisation Rate as representing the desired or anticipated investment return is obviously ludicrous.

Furthermore the first year return of net income on capital cost which is properly called the "initial yield" has been shown to vary considerably amongst properties which in other respects are similar. Not only has the initial yield failed to represent the desired investment return, it has been unreliable as an investment potential relfector, and therefore as a Capitalisation Rate.

The Capitalisation Rate also becomes unreliable when the "intuitive margin" from which the valuer must make his selection becomes unreasonably wide. A simple example will illustrate the point.

Net income $200,000 capitalised @ 10% gives Capital Value of $2 Million. Net income $200,000 capitalised @ 11% Capital Value of $1.82 Million.

If the sales data indicates that the appropriate Capitalisation Rate is between 10% and 11% then the Capital Value is somewhere between $1.82 million and $2 million. The valuer could make a reasonable intuitive judgment, and value the property at say $1.9 million (10.53%).

However if the sales evidence available shows initial yields between 5% and 8%, the capital value achieved by capitalisation of a net annual income of $200,000 is somewhere between $2.5 million and $4 million, which is just too wide a value margin from which to make an "intuitive selection". (If the net annual income was $2 million, those initial yields would show a capital value "range" from $25 million to $40 million.)

It is just because major investment properties are showing unreliable initial yields that valuers are becoming increasingly uneasy about using them as Capitalisation Rates, and are seeking other methods which are more accurate and reliable. Modern calculators and computers make this possible.

Nevertheless, experienced practising valuers who are inured to the capitalisation method will continue to use it for all income earning property valuations. When the data appears unreliable, then the data is "adjusted". (3) This procedure is acceptable if the data parameters are reasonably confined. However if the data parameters are wide, then this practice is dangerous, and in some cases may almost be pretentious. Valuers will continue to use the Capitalisation Rate, because it is simple arithmetic. Even when more sophisticated techniques are developed, the results will be simplified into effective Capitalisation Rates, and effective net annual incomes. Valuers feel confident with Capitalisation Rates, because they are simple to calculate, easy to understand and perceive, and appear almost tangible. They are value indicators.

The standard practice of applying a selected Capitalisation Rate to a single year as a perpetuity, to calculate capital value, is receiving well deserved criticism from sources outside the profession. It is considered to be a gross oversimplification of what should be a complex appraisal process. These criticisms are not without foundation. In the past, major investment decisions have been based upon what appears to have been simple arithmetic and sometimes flimsy criteria. The risk of serious error has been considerable.

Adelaide architect John Chappel made some pointed comments in an article published in "The Advertiser" on 29th September, 1982. He said inter alia "calculations involving simple arithmetic, and graced with the rather pretentious title of `feasibility studies' form the basis of decisions affecting the future of cities. If construction costs, finishes, fees and extras (such as art works) are minimised, and estimated rentals thereby show an acceptable immediate return on the investment, then the project is said to be `off the ground'."

"It is well known that financial institutions will "buy" projects that comply with these simple criteria during the first year of their life". "There is at least one major office building in Adelaide built to minimum standards and occupied at high rents for about five years, which is now empty and consequently showing no return at all". The developer who "put it together" and "got it off the ground" to use the colloquialisms of the industry, has long ago taken his profit and left the scene. However he would seem to have left behind a permanent problem for the new owners and a permanent blight for the city of Adelaide".

To my knowledge this article has never been actively disputed by valuers. Why should it be? For in essence it is true. Adelaide valuers will know to which building Mr Chappel referred, and know that since the article was published it has been resold. It is to be hoped that the last sentences quoted do not remain true for the present owners, or for the city of Adelaide.

A final reason for the rejection of the Capitalisation Rate as the primary conversion factor of property income into capital value, is the extent to which it has to be modified or adjusted before it can become meaningful as a unit of conversion.

Without qualification, a quoted Capitalisation Rate or initial yield, could be any one of the following:

1. Capitalisation Rate calculated on actual net income.

2. Capitalisation Rate calculated on full net income, including vacancies.

3. Capitalisation Rate calculated on full net income, with an allowance made for vacancies, including a let up period, and for the burden of existing leases at rentals below market value.

All of these may be before or after acquisition costs, and should be adjusted to one or the other, "before costs" being more common.

Option 3 above produces a Capitalisation Rate which is more reliable, but which is necessarily more complex and subjective. A detailed qualification of that Capitalisation Rate would be necessary before it could be safely applied.

There is also a risk that Capitalisation Rates based on one criterium may be confused with those of another. The Capitalisation Rate from example 1 above, applied to a situation as in 2 above, could result in a horrific over-valuation. It is almost as bad as the valuers' traditional nightmare of confusing the "Gross Return" with the "Net Return".

The most serious problem to valuers of complex urban income earning properties is that, even with adjustments, calculated Capitalisation Rates have become unreliable as value calculation factors. They do not measure the desired investment return on capital cost, and the range from which they may have to be intuitively selected, is sometimes too wide. They also may be affected by hidden adjustments or other distortions which may not be apparent to the valuer.

These statements do not mean that the use of the Capitalisation Rate as a value calculation factor is to be dismissed out of hand. As I said before, it will continue to be used. It will certainly continue to be used as a "check" on other methods.

Even though more sophisticated valuation methods are emerging and developing, valuers should not forget that the principal attraction of the Capitalisation Rate is its fundamental simplicity.

The Equated Yield

In Australia there appears to be developing a common misuse of the term "Equated Yield" which needs to be isolated and corrected before it becomes generally accepted. I refer to the practice of predicting future yields after a sale date, averaging them, and calling that average ifgure an "Equated Yield". In the "Australian Property News" the term is regularly misapplied to simple sales analyses where the initial net yield, and the calculated net yield after an imminent rent review, are added together and averaged.

In "The Valuer" April, 1983, page 505 an article by Michael Lynch F. A. I. V. of Brisbane says, "The term equated yield is one that should become more widely used as this refers to the average yield that the building will produce in the period that the valuer has taken into account rental reversions". He goes on to give an example of an initial yield of 4.4% and future yields of 5.6%, 7.2%, 8.4% and 9.5%, all over a two year period, and calling the average of those yields, being 7.02% an "Equated Yield".

What Mr Lynch is talking about is an average yield not an Equated Yield. The two functions are quite different. The use of average yields is a modification of the traditional Capitalisation Rate and is based on simple criteria. The difference is that within the also simple criteria of capital cost, anticipated net income, and the expected re-sale value of the property, the Equated Yield measures the true net return on the capital cost. The Capitalisation Rate, initial or average, does not.

It is because the Equated Yield is a true measure of the return on invested capital that it is comparable to the desired rate of return, and therefore to alternative investment possibilities. The valuer's inituitive selection margin has been narrowed.

Definition: An Equated Yield is that investment rate which when applied to a series of projected incomes over a time scale, produces a series of present values which added together equal the capital cost of the investment (4).

In fact the Equated Yield is merely a simplifcation of the Internal Rate of Return (IRR) obtained from a Discounted Cash Flow (DCF) analysis.

It is important to note here that included in the projected incomes is the anticipated sale price (Reversion Value) of the Property. This means that the total investment is considered, and the Equated Yield is the calculated actual return on that investment. It should also be emphasised that the Equated Yield is the investment return on the stated capital cost and not necessarily the total cost. The latter is the function of the IRR and may include internal management costs, costs of finance etc. The Equated Yield is therefore a rather clinical factor, but is useful because it is based on criteria which are easy to identfy, and which generally can be made available to the valuer.

The calculation of a capital value from a known series of projected incomes discounted at a known Equated Yield, is a straightforward process. The calculation of the Equated Yield from a known capital cost or value and a known series of projected incomes, requires a number of trial and error applications of trial yields until the equation is achieved. With a suitable iterative calculator, or a computer, the calculations can be done quickly.

With practice the Equated Yield can be calculated using a non-iterative pre-programmed ifnancial calculator; or even a basic hand held calculator, provided that it has an exponential (vx) function, and a memory. Usually at least three attempts are necessary, and the results are plotted on a graph, or are interpolated. The graph is particularly useful, because it visually indicates the capital costs or values obtainable from the application of other yields and vice versa.

Even with practice the calculation of the Equated Yield by hand can be a tedious and time consuming procedure. However, I consider that for beginners the exercise is worthwhile if a full understanding of the procedure is to be gained. I

also strongly advocate that valuers should learn and use the appropriate compound interest formulae, and make them work.

Once the procedure has been mastered and the workings understood, the use of an iterative ifnancially programmed calculator or computer with print-out facility is desirable if the method is to be frequently used.

It is possible to calculate an Equated Yield using normal compound interest or valuation tables (The Present Value of $1). But this is slow and cumbersome and lacks the accuracy obtained by using a calculator. However for beginners I suggest that the tables be used, at least as a check on the factors you have calculated. The other great advantage of using a calculator in preference to tables is that whole or fractional interest rates or time periods can be used. Also the trial yields calculations results can be aggregated in the memory of the calculator, and only the calculated capital value and the trial yield % figures for each calculation need to be recorded on paper. Once the equation has been made, the full details pertaining to the equated yield only may be recorded on paper for future reference.

In case readers are already becoming discouraged let me assure you, that even by hand a small calculation does not take very long. The example below from start to finish, including the graph, done first in pencil as a rough copy, took less than 15 minutes. The calculator used was an old T130 which has a memory, an exponential function (yx), and parentheses (brackets). It was designed for the junior grades of high schools, and is quite suitable for compound interest calculations, if you have the formulae (5) in front of you.

Calculation of Equated Yield

Outlay $200,000

Initial Yield 7.5%, Reversion Perpetuity Yield 7.5%.

Growth Rate 8.5% p.a., Annual Reviews. Term 5 years.

	1	2	3	4	5	6	7
	Year	Income	Yield on Outlay %	Present Values on Trial Yields 15% $	15.5% $	16.5% $	Equated Yield 16.0% $
a	1	15,000	7.50	13,043	12,987	12,876	12,931
b	2	16,275	8.14	12,306	12,200	11,991	12,095
c	3	17,658	8.83	11,610	11,460	11,168	11,313
d	4	19,159	9.58	10,954	10,766	10,401	10,581
e	5	20,788	10.39	10,335	10,114	9,687	9,897
f	6	22,555	11.28				
g	5	300,733		149,517	146,309	140,137	143,183
h	CALC CV = DCF		$	207,765	203,836	196,260	200,000
i		Outlay	$	(200,000)	(200,000)	(200,000)	(200,000)
		NPV	$	7,765	3,836	(3,740)	0

Results of Trials (Target is the Outlay, $200,000).

15%	$207,765	high.
15.5%	$203,836	still high.
16.5%	$196,260	low.

EY is between 15.5% and 16.5%; a difference of only 1% and for purposes of interpolation and a graph linearity can be assumed.

Interplotation:

Range 15.5%to 16.5% =$203,836 - 196,260 _ $7,576.

Range 15.5%to target =$203,836 - 200,000 = $3,836.

Interpolating: 15.5% + 3,836

7,576

= *15.5%* + 0.50633558.

Interpolation: = 16.006336%.

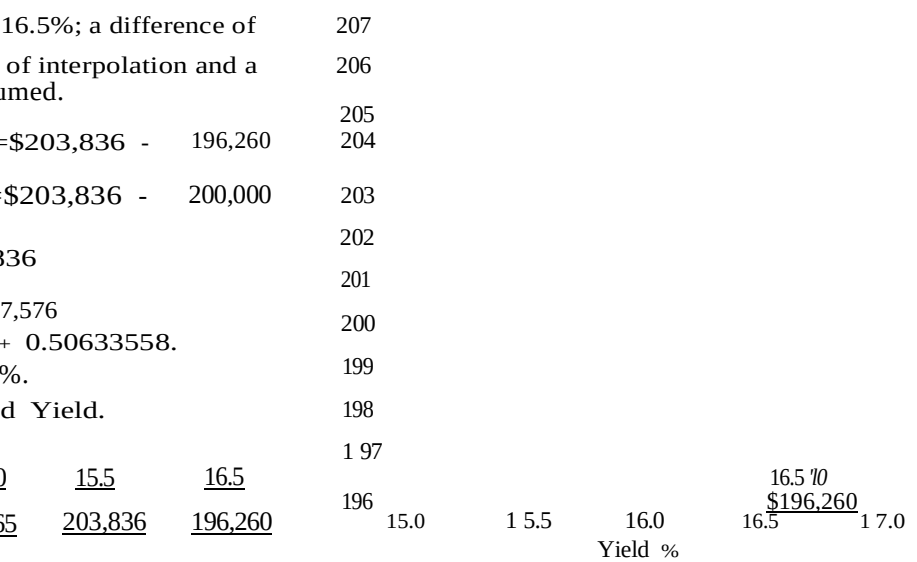
Say 16.0% = Equated Yield.

Graph of

	15.0	15.5	16.5
(x) Trial Yield %			
(y) Cale. CV $	207,765	203,836	196,260

Outlay

The graph shows that for a known Outlay or Capital Value of $200,000 the Equated Yield is 16.0%.



Explanation of EY Calculation

For ease of description the columns across have been numbered 1 to 7 and the lines down a to j.

Column 1 refers to the year in which the income was received. For ease of calculation the income is assumed to be received in arrears.

Column 2 shows the predicted net incomes. In this example the income growth rate is fixed at 8.5% per annum.

Column 3 shows the yield % on Outlay. 3 (a) is the initial yield of 7.5%. 3 (b) is the year 2 income divided by the Outlay, expressed as % and so on.

These yields of course are growing at the annual rate of 8.5%. It is interesting to note that the Average Yield over the 6 years (5-1) is 9.3% and bears little relation to the Equated Yield of 16.0%.

Columns 4-6 are the Present Values of the income projections at the trial yields of 15.5% and 16.5%.

Column 7 shows the Present Values of the income projections at 16% which is the Equated Yield.

Lines (a) to, (e) show the income projections in Column 1. Line (f) in Col. 2 is the estimated income for year 6. This is shown to assist in calculating the value of the Reversion at the end of year 5.

Line (g) Col. 2 shows the value of the Reversion, which has been calculated by capitalising the year 6 income of $22,555 in perpetuity at the initial yield rate of 7.5%. This is an arbitrary decision and is commented upon later.

Line (g) in Cols. 4 to 7 shows the value of the Reversion discounted at the trial yields to present values. The deferment period is 5 years (not 6).

Line (h) is the Calculated Capital Value, or the sum of the present values.

Line (i) shows the Outlay as a negative figure. This is standard practice in Discount Cash Flow Analysis.

Line (j) shows the Net Present Value (NPV) which is calculated by adding together all the cash flows, discounted to their present values. This includes the outlay, stated as a negative ifgure.

When the trial yield is such that the NPV = 0, the trial yield is called the Internal Rate of Return (IRR).

In Equated Yield analysis the only stated negative figure is usually the Outlay, and the aim of the exercise is to equate the outlay. So that ZPVs Outlay. This keeps the figure positive.

The graph shows clearly the equation of the Outlay of $200,000 with the yield at 16%. Other equations are also visible; 16.4% equates with an outlay of $197,000, and 15.2% equates with an outlay of $206,180 and so on.

Variables

The example given is merely a demonstration model. A number of arbitrary decisions have been made, and as seen, an Equated Yield analysis does contain several subjective variables. Once the method has been mastered, several calculations can be done to test the effects of changing the variables, and from these analyses a fuller picture of both sales and subject properties will emerge.

The most important variables are:

1. Projected incomes, including predetermined income growth rate if applicable.
2. The term of the DCF; how many years?
3. The value of the Reversion.

Growth Rate

In the model, a growth rate of 8.5% per annum was applied to the income. Normally an equated yield analysis would be based upon random incomes - that is actual estimates of the net incomes which could reasonably be achieved from the building over say a five year period. To extend the projections for a period greater than five years is probably unrealistic, so that at the end of the term some decisions or assumptions have to be made concerning the future of the property.

Reversion

The property in the example was given a Reversion Value in year 5 of $300,733. This was calculated by capitalising the estimated income for year 6, being $22,555 at the initial yield rate of 7.5%. By using the initial yield, it is implied that the income growth rate of 8.5% per annum is expected to continue for an indefinite period. This is an important decision, because at equation the property value at year 5, discounted to present value, is worth $143,183 or 71.6% of the total capital value of $200,000. The value given to the reversion has a significant bearing on the whole analysis. If it is decided that the trial yield rather than the initial yield will be applied in perpetuity to the year 6 income to calculate the reversionary value, the exercise re-calculates to an EY of 10.2973%, say 10.3%. This would imply that at reversion the rental growth is expected to be static. The reversion value becomes $219,038 and has a present value of $134,182, which is 67.09% of the outlay of $200,000.

The reversionary values so far calculated have been $300,733 by applying the initial yield of 7.5%, and $219,038 by applying an Equated Yield of 10.3%. It could be quite reasonable for a valuer to reject both these values and select an intermediate figure, say $250,000, which would represent a Capitalisation Rate of 9.022% on the year 6 estimated income of $22,555.

Sales could show that a Capitalisation Rate of about 9% would be appropriate for the perpetuity, whereas 7.5% might indicate a greater potential for increase in income than is reasonable to predict, and 10.3% could appear unreasonably conservative. If the reversion is valued at $250,000, the EY Calculates to 12.606%.

The exercise has demonstrated Equated Yields of 10.3%, 12.606% and 16.0% with the variation dependent entirely upon the value attributed to the reversion.

Term

The Equated Yield is sensitive also to the length of the term of the series. The model given has a term of 5 years, plus the reversion. If the model is extended 10 years, maintaining the same growth rate, the following results are obtained.

1. Perpetuity reversion yield of *7.5%* (initial yield) gives a reversion value at the end of year 10 of $452,200. The reversion has a present value of $102,506 and represents 51.3% of the outlay. The Equated Yield remains unchanged at 16.0%.

2. Perpetuity reversion at the Equated Yield, gives a reversion value of $274,171 and an Equated Yield of 12.37%. The present value of the reversion represents 42.7% outlay.

3. Perpetuity reversion at 9% (actually 9.02%) gives a reversion value of $376,000 and an Equated Yield of 14.587%. The Present Value of the reversion is 48.17% outlay.

In case 1 the Equated Yield is unchanged, but the value of the reversion as a proportion of the outlay has declined from 71.6% to 51.3c/&,.;JJhe longer the term, the less significant is, th"e value of the reversion. Both the growth rate and the reversion perpetuity yield have not been changed, and as expected, the Equated Yield is unchanged at 16%. This situation represents a stable investment, and if the evidence is available its value could be calculated simply by capitalising the ifrst year income at the initial yield. However 16'% is the true return on the investment, and is the discount rate which should be applied" to the projected cash flows of similar properties, provided that the sale and subject properties are based on cash flows of the same term. This is one of the most useful applications of the Equated Yield, particularly when applied to properties with an extended let up period. In which case 16% would represent the desired yield.

Cases 2 and 3 show the effect on the Equated Yield when the value of the reversion is changed.

Generally the model as shown in case 1 is useful with a maximum DCF Term of 5 years. There is no reason why the other models should not be used, provided sale analyses and subject valuations are based on similar models. The DCF term of say 5 years could be subdivided into 20 quarters, or 60 months, and the interest rate adjusted accordingly (6).

Random Incomes

The previous EY calculation was based on an initial income of $15,000 appreciating annually at 8.5%. Below is a second calculation where similar incomes are increasing irregularly. This is a more lifelike situation.

The structure and calculation is as shown in the previous example. No trial yields are shown.

The value of the reversion has been maintained at $300,733 as in the previous example. This means that any distortion will be generated only by the random incomes.

Column 3 shows yield on outlay, and column 4 shows the progressive average of the yield on outlay.

Column 5 shows how much the income has grown over the immediately previous year.

Column 6 shows the effective annual growth rate, relative to the initial income, of each subsequent income (7). At year 6 the income shows an overall annual growth rate of 8.5% which equals the applied annual growth rate in the ifrst model.

Column 7 shows the DCF calculated at the equated Yield of 16.0125%. The yield is only marginally different to the previous EY of 16(1/o_.

Column 8 shows the DCF calculated at the previous EY of 16%. The calculated Capital Value (CCV) is $200,095, and shows a NPV of $95. This means that if 16% is the desired investment return, the project is viable.

Column 9 shows that if 17.5% is the desired investment return, the project will not pay. The price of the property would have to be reduced by $10,862 to $189,138 before a return of 17.5% would be achieved.

Columns 8 and 9 also illustrate the application of desired yields to discount projected incomes and achieve calculated capital values.

1	2	3		5	6	7	8	9
Year	Income	Yield on Outlay %	Average Yiel0 o	Income Growth Over Previous Year	Income Growth Overall *p.a. °Ja*	DCF at E.Y. 16.0125%	DCF at 16%	DCF at 17.5%,
1	15,000	7.50	7.50	-	-	12,930	12,931	12,766
2	16,500	8.25	7.875	10.0	10.0	12,260	12,262	11,951
3	17,500	8.75	8.167	6.06	8.01	11,208	11,212	10,787
4	19,200	9.60	8.525	9.71	8.58	10,599	10,604	10,073
5	20,800	10.40	8.90	8.33	8.52	9,897	9,903	9,287
6	22,555	11.28	9.30	8.44	8.50			
5	300,733	-	-	-		143,106	143,183	134,274
	Equated Yield = 16.0125%			CCV		$ 200,000	200,095	189,138
				Outlay		$ (200,000)	(200,000)	(200,000)
				NPV		$ 0	95	(10,862)

Opportunity Rents and Cost

The model below is of a similar property where low net incomes are anticipated over the first few years. If these projections are correct what will be the Equated Yield on an outlay of $200,000? Alternatively if 16% or even 17.5% are the desired yields, what respective prices should be paid for the property?

Note that the initial yield is only 2.0% and shows a "reserve yield gap" of at least 14%.

Outlay $200,000 Initial Yield 2.0%

Random Incomes Term: 5 years

Reversion Perpetuity Yield 7.5%

Full initial income: $15,000

No trial yields are shown.

Reversion is maintained at $300,733.

Column 7 shows the annual income growth rate relative to the Full initial income of $15,000.

Column 8 shows DCF at EY of 13.8832%.

Column 9 shows DCF at deesired yield of 16%. At this rate the investment would not be viable unless the price was reduced to $183,544.

Column 10 shows DCF at 17.5%, and indicates that the price would have to drop to $172,899 before the project would pay if this return is desired.

What this means is that if 16% is accepted as a fair EY then this property has a capital value of $183,544, rather than $200,000. The difference results entirely from the low income in the early years, and is an exact quantification of this loss.

The figure would then be appropriately rounded.

1	2	3	4	5	6	7	8	9	10
Year	Income	Yield on Outlay %	Average Yield %	Income Growth over Previous Year %	Income Growth Over-all % p,a.	Income Growth Overall on Full Initial Income % pae	DCF at 13.8832%	DCF at 16%	DCF at 17.5%
1	4,000	2.00	2.00			-73.33	3,512	3,448	3,404
2	8,000	4.00	3.00	100.00	100.00	-46.67	6,169	5,945	5,795
3	16,500	8.25	4.75	106.25	103.10	4.88	11,171	10,571	10,171
4	19,000	9.50	5.94	15.15	68.10	8.20	11,296	10,494	9,968
5	20,800	10.40	6.83	9.47	51.01	8.52	10,858	9,903	9,287
6	22,555	11.28	7.57	8.44	41.33	8.50	-	-	-
5	300,733	-	-	-	-		156,994	143,183	134,274
	Equated Yield 13.8832%				CCV		$ 200,000	183,544	172,899
					Outlay		$ (200,000)	(200,000)	(200,000)
					NPV		$ 0	(16,456)	(27,101)

Development

The use of Equated Yields for the valuation of urban income earning properties is far from being a complete answer to a difficult problem. As has been shown the Equated Yield is highly subjective, and it is essential that the parameters of its analysis and application are in every case clearly defined. The Equated Yield assumes that income earned from the investment is automatically reinvested in the same investment, at the same rate. This may not be the case and in practice is unlikely to be.

The Witconsin Modified IRR (8) provides an answer to the internal investment problem but leaves the alternative investment rate to be decided by the valuer. This introduces yet another subjective element into a model which is in danger of already being too subjective.

In this paper I have not referred to Equated Yield Tables, because they are all based upon pre-determined growth rates, and are for a variety of periods. I think it is much more desirable that valuers take time and practise the calculations and application of EY, using appropriate models.

The models used in this paper have deliberately been made simple, and all incomes are shown as annually in arrears. In practice incomes are usually paid monthly in advance. By the time the income reaches the owner it is virtually in arrears, and so it has become the usual practice to base EY calculations with income paid monthly in arrears. The calculation of the monthly interest rate is shown in note (6).

Criticisms and Conclusion

The most common criticisms of Equated Yield analysis are that the projection of future incomes is unrealistically speculative; that the application of a "Capitalisation Rate" to calculate the value of the reversion is a contradiction of the method; and that the process is too difficult and takes too long.

Projection of future incomes is the basis of the whole exercise. All this is doing is quantifying what is implied by the selection and application of a Capitalisation Rate. Of course it is speculative, but it is not necessarily unrealistic. The very purpose of the method is to accurately predict future incomes, to vary those predictions, and to quantify those variations in terms of the present value or investment return. The importance of this exercise can best be demonstrated by reference to some examples.

• Valuation of a multi storey office building, in need of renovation, vacant estimated let up period after renovation is two years.

ie Valuation of offices, shops still to be built. Valuations required as on date of completion, in two years time, in five years time.

• Valuation of office tower in CBD due for renovation, fully let, asbestos problem in part of building.

In these examples there are no useful Capitalisation Rates, looming significant capital expenditure, and unknown vacancy periods. It is only by making a variety of reasonable projections in each case and applying an EY/DCF analysis that the valuer can calculate a range of subjective and qualified capital values. Then, by using his knowledge and intuition he can examine the evidence and form his opinion as to fair market value.

The application of a Capitalisation Rate to calculate the value of the reversion does seem to be a contradiction in terms. It is admittedly a tool of convenience. However the ability of the Capitalisation Rate to reflect the assumptions made about future income growth, is useful. On the normal EY analysis of a 5 year DCF plus reversion, the DCF is very often over a period of known anticipated expenditure or vacancy, while the deferred perpetuity is expected to be more stable. The (full net rent) initial yield is then applied to calculate the reversion. It is only when for some other reason that the reversion value is expected to be greater or less than what would normally be expected, that a different value would be given. The essential thing is that these details are recorded and included in the qualification of the EY analysed or applied, and in the capital values obtained. If the calculation of a fair reversion value is impossible, then the alternative is to extend the DCF period and to include the components which are causing the problem, and then add the reversion. The longer the DCF period, the less significant is the value of the reversion on the EY analysis or application.

The critics who complain that the EY/DCF methods are too complex and take too long are not really confronting the problems inherent in the valuation of complex urban real estate. There is no easy way out. Iterative programmable calculators and computer packages make the calculations simpler, and practice with them using EY/DCF analysis will vastly improve the valuer's understanding of the investment property market, and his competence in valuing it.

The hardest problem in valuation has always been that of obtaining and collating accurate, current and relevant sales data to support the valuations. The use of EY/DCF analysis makes the problem even harder, especially when details are needed about sales from interstate. Vendors, purchasers and real estate agents will generally disclose sales in minimal form and with the greatest reservation. This is one of the reasons why it has long been the practice to base valuations by reference to an array of initial yields; that is on minimum information and maximum intuition.

Resistance to disclosure about sales information is reasonable, and should be expected by valuers. Much of the information may be conifdential between agent and client, and valuers may have to be content with learning what little they can. Also many major transactions are still based more upon intuitive judgement, rather than by an assessment of accurately quantified financial alternatives; and there is no substantial data to disclose to valuers, although the parties involved are unlikely to inform valuers of that fact.

Just the same, if sophisticated valuation methods are to be accepted and used, they must be based upon adequate, comprehensive and up to date sales data. This would require the cooperation and good will of the people involved in the sales, and the respect of that goodwill by the people using the sales data. Can this be achieved?

The solution of the problem, if there is one, indicates two possibilities. One is that the professional institutes compile their own sales data banks. The Australian Institute of Valuers is well situated to perform this function and I would strongly support its implementation. Information could then be made available to members, on either an open or a restricted basis, dependent upon how the data was categorised, and an appropriate charge would be made for these services. The service would benefit in particular valuers needing information about transactions in other States, and is therefore relevant to valuers of large urban investment properties. Obviously the system would be computerised and all major valuation offices would have connecting terminals. The concept of an Australia wide real estate data bank to be conducted by the Australian Institute of Valuers was supported by Hon. Mr Justice R. Else-Mitchell in his address to the Rating Valuation Seminar in Canberra, April, 1982 published in "The Valuer" July 1982, pages 231 and 233. I personally consider that such a data bank conducted by a professional Institute would be more effective and more highly regarded than any similar bank run by a government department or a private firm.

I believe that all parties to a transaction would be reasonably willing to disclose information about sales to a highly regarded professional institute, and that if the information was disclosed to and used by members in a manner that met with the donor's approval, a mutual trust and respect would develop that would be beneficial both to the valuation profession and the real estate industry.

The second possibility is simply that of specialisation, wherein valuers using EY/DCF analyses become recognised as specialists in that area, and receive relevant detailed sales information because they are so known and recognised. This happens to any District Valuer in his own geographical area, but it is not so simple for the complex urban property valuer, especially when he wants detailed information on interstate sales. Few valuers could afford such specialisation, and I consider that the idea of forming some sort of professional elite does not somehow conform with the Institute's motto of broad vision and balanced judgment.

It is however quite clear that for the method to succeed there must be adequate sales information. Even old sales are worth analysis, when their future returns are known, so that historical analyses will form an important part of a new array of Equated Yields data. In time the EY/ DCF analyses will become part of standard valuation practice, and no doubt they will also be developed, modified, specialised and simplified. They are essential to our understanding and evaluation of real estate transactions. I think that it is only a matter of time before the Courts agree.

Nevertheless when all this has been said and done, the Capitalisation method, however obsolete, will still continue to be used. Once a valuation has been calculated, by whatever method, it will be checked in terms of full initial net income, and what initial yield results from its division by the calculated capital value. These initial yields will be compared with those obtained from sales and other valuations, and will themselves form a second line of reference data. This is fair, and is part of the valuation process.

The end result is a statement of what the valuer considers to be fair market value. It is an intuitive decision, based on analysed sales data, and the valuation figures calculated from that applied data.

To close I will quote from an article by Jim Cairns, who is Manager of Property Investments for the A.M.P. Society. The article was published in the April 1983 edition of "The Valuer".

> "It is the internal rate of return expected over the medium to long term rather than the immediate yield which is becoming most important to the long term investor.
>
> "Let me sound a note of caution. In making such a comparison between the internal rates of return available from different kinds of investments, it is the assumptions and not the mathematics which require the closest scrutiny. The successful property investor needs to have proven intuitive judgement to assess prospective investments - it's not all done by sums".

And the same is true for the valuer, but it is relative to the size and quality of that intuitive margin upon which he bases his judgment. The valuer must not only be professional, he must appear to be professional. Today that means the use of Equated Yields. Tomorrow more advanced computer methods will be used. This is inevitable, and the time to start learning and practising is now.

NOTES

(1) Capitalisation Rate $= \frac{\text{Net Annual Income}}{\text{Capital Value}} \times 100$

$$\text{Capital Value} = \frac{\text{Net Annual Income}}{\text{Capitalisation Rate\%}} \times 100$$

(2) Land Valuation and Compensation in Australia. R. 0. Rost and H. C. Collins page 97. "The year's Purchase is obtained by dividing 100 by the interest rate of return sought from the capital investment."

(3) The practice of averaging present and future yields is becoming common. Yields may also be adjusted for vacancies and burdensome leases, and for the relative estimated risk or security of the property as an investment.

(4) Equated Yield Tables. Phillip Marshall B.Sc. F.R.I.-C.S. September 1975, London. "An Equated Yield is the true yield on an investment, taking into account possible appreciation or depreciation of the income during the life of the investment and is found by discounting the projected future income at the appropriate rate to equate with the capital outlay, i.e. the summation of the discounted net rents equals the amount of capital committed to a particular investment. This corresponds to the internal rate of return in discounted cash flow analysis when the N.P.V. (Net Present Value) = Nil".

(5) The present Value of \$1 $= \frac{1}{}$

where i = interest rate expressed as a decimal, and n = the number of periods.

Hence the PV of \$1 due in 5 years time at 12.5% is

1 x -z = 0.554929

In equated yield analysis equation is reached when.

$$\frac{R1}{(1+i)} + \frac{R2}{(1+i)^2} + \cdots + \frac{Rn}{(1+i)^n}$$

Where R-Rn are the projected cash flows (including reversion); i is the trial yield, which at equation becomes the Equated Yield, n = number of periods. C = the Capital cost or outlay.

(6) If true annual interest rates are used, the monthly interest must *compound* to achieve the annual rate. This means that where i = the Annual interest rate, and i,,, = the monthly interest rate; 1 + i = (1 +i,,,)'2.

o, $1 + i_m = 12\ 1 + i, = (1 + w_{112;\ inn} = (1 + i)$

Similarly, where quarterly periods are used,

$$1 + i_q = (1 + i)^{1/4}$$

As the figure required is always one plus the interest rate, the problem is simply $1 + i_{,,} = (1 + i)^{1/12,}$ and can be calculated instantaneously using the exponential (y') function on a calculator.

If nominal annual interest rates are used, then monthly interest rates = 1/12 nominal annual interest. I suggest that nominal annual interest should never be used as a basis for calculating the monthly or quarterly interest rate. The method is mathematically incorrect.

(7) The periodic growth rate is calculated by formula

where R. = income at period n

R, = income at period I

n = number of growth periods

g = growth rate

(8) The Wisconsin Modified I.R.R. was developed by Professor J. A. Grasskamp. The method is outlined in a paper by Robert A. Milne and published in the April 1983 edition of "The Valuer" page 533.

$$g = 100\ [(\frac{Rn}{R,})^{i/n} - I]\ \%$$

The Discounted Cash Flow Concept

by Lincoln W. North, A.A.C.I.

This paper forms part of the seminar sponsored by the New Zealand Institute of Valuers and conducted by Lincoln W. North A.A.C.I.

The seminar topic was "A critical analysis of the income approach to valuing revenue producing real estate." Lincoln North has a valuation practice in Toronto, Canada and has an international reputation as an Appraiser, Real Estate consultant, author and speaker.

A. INTRODUCTION

Discounted Cash Flow is akin to a precision surgical instrument. It serves well if used properly. And proper use commands a practical understanding of its application.

The topics to be covered in this critical diagnosis are as follows:

1. The evolution of the concept.
2. The applicability of the concept.
3. The type of earnings processed into value.
4. The length of the forecast period.
5. The significance of market rents.
6. Forecasting earnings.
7. Establishing the reversion.
8. Developing the discount rate.
9. Methodolgy of application.

B. EVOLUTION OF THE DCF CONCEPT

1. The acquisition of investment real estate is motivated by the same basic logic and reasoning which governs the purchase of any investment: The production of future earnings and related benefits arising from ownership of the asset or commodity. The value of an investment represents the present worth of anticipated future benefits, with emphasis placed on the word "anticipated", for no future event has certainty of occurance.
2. Of all the methods commonly used in the valuation of investments, DCF is the only procedure which is available to find the present value of forecasted future receivables; forecasted as to a defined amount and a definitive date of receipt.
3. Functionally, the DCF method of valuation involves two key steps.
   a. Forecasting expected rents, or net incomes over a finite period of time, acording to the anticipated date of receipt (assuming such receivables are not prescribed by contract).
   b. Finding the present value of these predicted receivables through a "counting" process which is known as discounting.
4. When inflation was not a factor of concern, investors were content to appraise or evaluate an investment solely through consideration of a property's current earnings; leaving the influence of comparatively negligible inflation to produce the "icing on the cake": The value of the cake itself being adequately measurable through the capitalisation of current revenues.
5. When property values began to escalate rapidly, due to the influence of either actual inflation or perceptions of major inflationary growth, investors sought a means of evaluating this influence in a more definitive manner. Arithmetically, this was no problem; as DCF analysis had been used as a capital budgeting procedure in industry for over half a century. Further, valuers had been using the procedure for nearly the same length of time to find the present value of lease interests.
6. At the same time as inflation became a major area of concern to real estate investors, microcomputers came on the market, which resolved the problem of handling a multiplicity of tenants. Thus, the practical ability to use a DCF analysis in the evaluation of investment real estate was born in the mid-1970's.

C. APPLICABILITY OF THE CONCEPT

1. The valuation of lease interests (already discussed.)
2. The valuation of any revenue property.
3. Financial analysis (cost-benefit analysis) relating to new developments, modernization of existing projects, expansions, etc.
4. Buy-sell decisions related to portfolio administration.
5. Determining the impact which income participation will have on a lender's yield (on a participation mortgage).
6. Land subdivision analysis, to estimate the probable extent of profit to be realised over the development period.
7. Sensitivity analysis relating to any one of the foregoing objectives.
8. A practical means of valuing a property when:
   a. Operating expenses exceed the current rental income.
   b. A property is plagued by extraordinary vacancies,
   c. The date of valuation precedes the date of substantial completion and occupancy,
   d. Extraordinary changes are expecteed to occur in net earnings in the foreseeable future.
   e. A major change in use is expected to occur in the foreseeable future.
   f. Extraordinary capital expenditures must be accounted for in the valuation process.

D. THE TYPE OF EARNINGS TO BE PROCESSED INTO VALUE

1. Net Operating Income (or Net Rents).
   a. When value is to be found on the basis of an all-cash purchase (or sale):
   b. When the influence of any existing mortgage financing is to be disregarded in the valuation process.
   c. When refinancing of the property is contemplated following its sale or acquisition.
2. Pretax Cash Flow
   a. When a property will be sold subject to the conveyance and continuance of existing mortgage debt.
   b. When it is necessary to estimate the influence of mortgage leverage on value.
3. Post Tax Cash Flow (After-tax cash flow)
   a. When the influence of income tax and capital gains tax is to be incorporated into the valuation process.
   b. Seldom used to estimate the buying/selling price of a property.

E. LENGTH OF THE FORECAST PERIOD

The valuation of a leased fee or leasehold estate must be undertaken in consideration of a specific period of time, unless the lease is perpetually renewable under the same terms and conditions. This time frame is commonly known as the forecast period, regardless of whether the rent is prescribed by contract or is a variable rent to be estimated.

The length of the forecast period will normally be set by the lease expiry date. Under certain circumstances, however, the length of the forecast period may be shorter than the remaining term of the lease, due to specific covenants contained within the indenture or should the nature of the analysis command the establishment of an artificial reversionary date. At times, the length of the forecast period might extend beyond the remaining initial term of the lease; to reflect options-to-renew which may have to be taken into consideration pursuant to the instructions for analysis and valuation.

When evaluating a multiple-tenanted investment property by the Discounted Cash Flow Method (either to estimate its present value or to establish the most probable return on investment), a specific forecast period must be established to facilitate calculations. This time span is usually referred to as the investment horizon, although the terms income projection period or forecast period are used with equal frequency. The investment horizon is a period of time which is independent of lease expiry dates, for there would be no common date pertaining to all tenancies. Thus, the forecast period may be interpreted as an artificial horizon. Regardless, what is important to bear in mind is the fact that present values and returns on investment are directly related to the time-value of money and therefore it is essential to establish a specific length of time during which cash inflows will be received and to set the terminal date at which the reversionary value of the investment is to be calculated.

The length of the investment horizon, with reference to a multiple-tenanted property, will be established through consideration of many factors. To place the subject in a general focus, the majority of investors will utilise a forecast period of from five to ten years, for the purpose of present value and yield calculations and also when comparing and ranking alternative investment opportunities. A ten-year horizon is the most frequently used time span.

Circumstances which contribute to the selection and use of an investment horizon of the aforementioned durations are: 1. Revenue properties tend to trade quite freqently in North America and it is not uncommon for a transfer of title to occur every decade, give or take several years. Holding periods are relatively short due to expiration of tax benefits, the every-shifting composition of real estate portfolios, changes in investor preferences, changes in the relative desirability of product and simply the desire to move on or up to a different asset. 2. Investors desire to see the influence of the majority of new leases in a multiple-tenanted development roll-over at least once or to observe the impact of old leases having their rent reviewed to market at least once during a given time span. 3. Investor familiarity with the discounted cash flow procedure of analysis reveals that the extension of the investment horizon much beyond ten years will have very minor influence on changes in present values or calculated yields, unless significant rental reversions remain to be accounted for. For example, if twenty percent of all occupational rents were reviewable to market every year, extending the investment horizon even from five to ten years would make very little difference in the present market value of the asset; all else being the same of course.

These are but a few of the factors which contribute to the use of a short investment horizon. Occasionally, however, the forecast period will be set at an unusually long period of time say twenty or twenty-five years, particularly if a property is let to a single tenant at a fixed rent for an inordinate period of time. Mortgage lenders who have participation agreements written into the debt contracts will frequently require a long-term analysis to ascertain the full impact of the participatory arrangement on their yield.

When properties are analysed on an after-tax basis, the length of the forecast period will generally be set by the length of time over which earnings will be sheltered from taxation, as a starting point. The horizon will then be shortened or extended incremently to determine the influence which changes in the holding period will have on the investor's post-tax yield.

In summary, while the typical length of an investment horizon for revenue producing real estate may range from five to fifteen years, to set a broad band, each property must be evaluated in consideration of its particular operating characteristics, according to the nature of the micro-market in which it will most likely trade and in view of the purpose and function for which the exercise is undertaken.

DIFFERENCE IN PRESENT VALUE

Five-year Horizon vs. Ten-year Horizon.

Year of Receipt	Projected Receivables	Discount Factor at 187	Present Value
1	$100,000	0.8475	$84,750
2	108,000	0.7182	77,566
3	116,640	0.6086	70,987
4	125,971	0.5158	64,976
5 (Inc.)	136,049	0.4371	59,467
5 (Rev.)	1,335,755	0.4371	583,859
Total present value (5-yr. horizon)			$941,605
6	146,933	0.3704	54,424
7	158,688	0.3139	49,812
8	171,383	0.2660	45,588
9	185,094	0.2255	41,739
10 (Inc.)	199,902	0.1911	38,201
10 (Rev.)	1,962,673	0.1911	375,067
Total present value (10-yr. horizon)			$962,577

Reversion (E.O.Y. 5) $146,933 _ 1101o : $1,335,755

Reversion (E.O.Y. 10) $215,891 _ 11 % : $1,962,673

F. FORECASTING EARNINGS

1. Forecasting future revenues is one of the two basic steps in the DCF procedure of valuing a revenue producing property; the other being the actual discounting process.
2. If future revenues are prescribed by the terms and conditions of prevailing leases and if such revenues represent net-absolute rents, throughout the length of the investment horizon, no forecasting would be required other than possibly to establish the reversionary value of the asset.
3. Should leases expire during the income projection period, forecasts will be required to estimate the then market rental value of the space in question, for the remaining number of years contained in the investment horizon. The Zero-Growth assumption, prevalent in the U.K., avoids the necessity of forecasting future market rent; since it is presumed that all leased space will only revert to current market rent.
4. If the forecasting process relates to the estimation of future net operating income in a multiple-tenant property, the following considerations must be borne in mind.
   a. While individual leases may call for net-absolute payments of rent, the operation of such a property will seldom be net-absolute (due to non-rechargeable occupancy costs, vacancy allowances, bad debts, etc.).
   b. Will gross rent leases change to net, during the forecast period?
   c. Will leasing commissions and tenant allowances have to be considered at the date of rent review?
   d. Changes in expenses recovery procedures.
   e. Allowances for capital repairs and replacements.
   f. Vacancy and credit losses.
   g. All general considerations which influence the setting of market rents at any point in time.
5. When future market rents become a function of an inflation factor (a Rental Inflator) applied to current market rents, the investment community gives consideration to the following key indicators:
   a. The Consumer Price Index as it affects the entire economy.
   b. The estimated future trends in market rental rates for the type of property in question, in the local community.
   c. The projected future trends in market rental rates for the specific property under study, interpreting the characteristics of the rental space within the building in the light of:
      1. Competition.
      2. Supply and demand.
      3. Individual features of the property itself.
   d. The intrinsic trends within the building as they may affect the rental values of individual premises (particularly in a shopping centre).
6. Summary: Refer to the following table and narrative recap.

F. SYNOPSIS OF FORECASTING FUTURE MARKET RENTS

The valuation of revenue producing real estate through application of the Discounted Cash Flow Method, or even the valuation of a long-term variable rent lease, requires a projection of net earnings over a prescribed period of time; this time frame traditionally referred to as the length of the investment horizon, or income forecast period. Since net earnings are the result of reducing gross earnings by the quantity of operating costs and other deductible expenses which are required to sustain the production of gross receipts, the estimation of future net earnings must begin with a forecast of the rental income to be received during each year of the forecast period.

The point of commencement in the forecasting process is the estimation of the current market rental value of the space in question. Once established, the current market rent becomes the quantity of rent to be escalated (or deflated, if necessary) over the term of the forecast period, to produce an expression of the estimated future market rental value of the space in question at the date of rent review or lease renewal. This is usually accomplished by applying a Rental Inflator to the present market rental value; the inflator being a percentage rate or factor which will account for the forecasted annual change in the prevailing level of current market rent. Alternatively, the forecasting process may involve adjusting the present market rent in increments of absolute dollar amounts to account for the predicted extent of change in market conditions.

The actual rent to be received until the date of rent review, will be the prevailing contract rent. At the date of lease expiry or rent review, it is

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presumed that the actual rental value of the space in question will become the inflated current market rent; which, in turn, will become the contract rent for the ensuing rental period. In other words, once the rent "snaps to market" it is deemed to become the contract rent (and the actual rent) until the following date of lease renewal or rent review.

To illustrate the foregoing explanation, assume that the space in question was let three years ago at a fixed contract rent of $10,000 per annum, for a term of five years. Two years remain in the present lease and the current market rental value of the space is $12,000 per annum. Using a ten-year forecast period and a constant Rental Inflator of 5% per year, the actual rent to be received during this period of time is represented by the solid line on the following graph. (Assume each lease renewal to be for a further term of three years).

FORECASTING FUTURE MARKET RENT

TO ESTAI3LIS11 FUTURE RENTAL INCOME

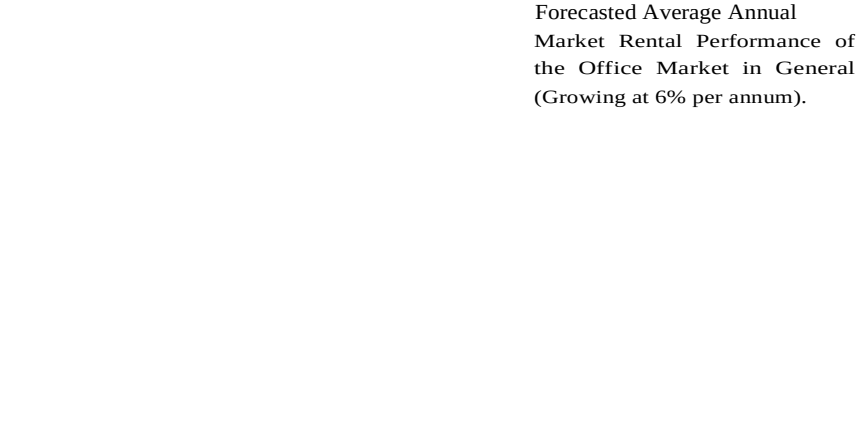
Several observations relating to the forecasting process may be made at this point: The estimation of future rental income is dependent upon establishment of the current market rent, the estimation of the annual rate (or annual dollar amount) of change during the forecast period and the prediction of the number of years to be contained in each rent renewal period. The actual rent predicted for each renewal period is generally referred to as the contract rent for that period of time. The contract rent is the quantity of rent which enures to the landlord (or lessor) and becomes the basis of establishing the value of the leased fee estate or the landlord's interest in the property. The rental margin (or difference between the market rent and the contract rent) enures. to the benefit of the tenant (or lessee) and will form the basis of establishing part of the value of the leasehold estate. (The full value of the leasehold estate may include tenant's improvements and other elements of contributory value).

It should be recognised at this point in the discussion that the forecasting process could be long and arduous if performed manually for a property containing numerous tenants. This is one instance where the use of a computer is of immeasurable assistance; particularly when the forecasting process commands use of a variable rental inflator and if a sensitivity analysis is subsequently called for. The problem would be further complicated if the future rental income was also a function of the tenant's retail sales performance.

Having examined the basis of the forecasting process, attention may now be turned to the theory and procedures related to the establishment of market rents for the term of the forecast period. It is an exercise requiring considerable judgment. Nevertheless, risk capital is being employed in anticipation of future returns and investors have developed certain benchmarks and other criteria to assist them in their projections. The relative accuracy of forecasts in the short-run is usually fairly reliable if proper respect is paid to market trends. If forecasts of long-run trends turn out to deviate materially from actual experience in the marketplace, the present value of such divergencies is cushioned significantly by the weight of the present value factors used in the discounting process.

Regardless of the type of property being evaluated, the primary benchmark or focal point of consideration in the forecasting process is the anticipated rate of inflation. More particularly, the real estate investment community tends to favour

FORECASTED FUTURE OFFICE RENTAL RATES
FOR THE ABC BUILDING LOCATED IN THE CBD



the use of the national or regional Consumer Price Index as the general reference point or at least as a target in the forecasting process; using the expected average annual rate of change over the next two to three years as the projected average annual rate of change for the total length of the forecast period. In lieu of using a constant average annual rate of change throughout the forecast period, the projected, trend curve may take on a wave-like shape (particularly during the initial years of the forecast period) to account for expected specific near-term shifts in the general economy. Beyond the fourth or fifth year of any forecast period, however, investors generally prefer to use a constant annual change; recognising the impracticality of forecasting specific business cycles that far into the future.

Having established the base line (or curve), as illustrated on the preceding chart, consideration can then be given to the real estate market in general and to the specific type of property under investigation, in particular. Over the long-run, real estate rentals will tend to "track" the CPI base line (or a base line formulated from consideration of a more applicable or preferable index in certain instances). However, market rental rates are significantly influenced by criteria other than the general performance of the economy, or even the specific performance of trend indicators that may be more reflective of the real estate industry. These criteria have the net impact of creating much wider fluctuations in rental performance trends than will occur in general economic trends; the net impact generally manifesting itself in terms of supply and demand. In matter of fact, trends in market rent could be directly opposite to trends in the general economy. For example, a forecasted increase of six percent in the general rate of inflation or even in a construction price index might be accompanied by a corresponding expected decline in rental rates as-the result of excess supply in the wake of diminishing demand.

The preceding chart illustrates how one particular sector of the real estate market was forecasted to perform vis-a-vis an expected rate of long-term inflation of six percent at the date of analysis. In this particular instance, the building in question was evaluated at a point in time when

a sharp upturn in the office market was expected to occur. Discussions with local brokers, leasing agents and other parties involved in the market led to the conclusion that net market rental rates would most likely achieve the specific levels noted on the chart for the next three years.

For the following two years, rental rates were projected to level off, as. the supply of office space in the CBD begins to exceed forecasted demand. Then, in the fifth year, as the market regains balance, rental rates should increase once again. However, rather than forecast a continuing wave pattern to reflect future cycles, the analyst elected to follow common perceptions of the investment community and thus linked the office rental curve to the CPI curve in the sixth year. As mentioned previously, if actual market performance diverges much from the forecast, the net difference in present value will be relatively nominal.

The foregoing example illustrates the need to forecast market rental rates (or to construct a market rental performance graph for a specific property) in a fashion to reflect expected trends in the specific market under investigation. Even though market rental rates will tend to follow inflation in the long run, astute projections must recognise the local supply and demand situation in the near-term. This may be done on a percentage basis, or in absolute dollars of expected change. Further, while a separate trend line (in contrast to a general economic index) may apply to the overall real estate industry in a particular community, individual (and separate) forecasts may vary widely for different types of property. At the date of analysis, office space vacancies might be excessively high. Yet, at the same time, apartment rental accommodations may be very limited in supply. There may be a shortage of retail space, whereas the industrial property market might be characterised by an oversupply. Consequently, general trends applicable to industry as a whole may be irrelevant in the forecasting process. Also, one geographic part of a community may be hot; while another part of the city might have a high vacancy status; all within the same category of property type and at the same point in time. The following chart illustrates a composite forecast of market conditions for several types of real estate within the same community.

To summarize the discussion at this point, each type of property and occasionally each property itself - must be evaluated in light of the current supply and demand situation, competition for space, and the relative tenant appeal which the asset in question has in the micro-market at the date of analysis. Armed with this information, and having adduced the current market rental rates applicable to the property under study, the analyst is then in a position to forecast the most probable changes in the years ahead with a fair degree of confidence and reliability.

When forecasts of future earnings are made pursuant to application of the Discounted Cash Flow Method of valuation, some analysts elect to omit consideration of inflation altogether. The nature of the exercise under such a postulation. may simply be to test the influence which no inflation (commonly called "zero growth") will have on present value. In conjunction with such an application, the analyst would assume that current market rental rates will remain constant; thereby acounting for uplifts in rental income solely to the extent that present below-market contract rentals will only rise to current levels upon lease expiry and subsequent renewal (or releasing) of the space.

Occasionally, sales will be analysed in this manner to extract internal rates of return. If such an analytical procedure is followed, the resultant rates of return could only be used in the appraisal process under the same forecasted rental performance postulation for the property being valued. Incidentally, if no inflation is infused into the projection of future earnings and if current contract rents are at full market levels, the internal rate of return abstracted from such a sale would be identical to the overall capitalisation rate produced by the sale. This subject is explored in greater length, in the discussion of formulating discount rates.

G. THE REVERSION

The return on an investment is measured by comparing the sum of the discounted net cash receivables to the original cost of the investment. These receivables, in turn, consist of periodic increments of income, either created by the rental provisions of a single lease or arising from the operation of a multiple-tenanted property; plus a final lump-sum amount at some future point in time. This final lump-sum receivable is commonly called the reversion, the capital value of the reversion or the future worth of the demised premises. When a lease expires or when an investment property is sold, the capital reversion will be an actual realization. If an artificial holding period and termination date is established, pursuant to setting a specified investment horizon for the purpose of calculating yields or estimating present value, the reversion would be referred to as a deemed realization.

The capital value of a reversion must be expressed in the same financial language as the periodic receipts of income, to produce a proper estimate of total present value. If a pretax approach is taken in the evaluation of the investment, both the income stream and the reversionary value of the premises must be expressed in pretax dollars. On the other hand, should the nature and purpose of the exercise be to establish the after-tax rate of return on an investment, all receivables (the periodic income and the reversion) will have to be reduced to post tax receivables prior to data processing.

Certain anxieties arise in the process of estimating capital reversions or the future worth of a property, usually amplified by the distance or length of time before reversion is to occur. Nevertheless, investors have discovered and do employ methods and procedures of estimating capital reversions which produce reasonably accurate and reliable results. Persons involved in the fore. casting process also realize that any differences which may evolve between the predicted value

FORECASTED FUTURE MARKET RENTAL PERFORMANCE
FOR SELECTED SECTORS OF THE PROPERTY MARKET

(expressed in terms of rate of change over previous year)

of the reversion and what, in fact, will actually occur; will be substantially reduced (in terms of present value) by the weight of the present value factor used in the discounting process.

On occasion, anxieties related to forecasting capital reversions lead to the posture that reversions might be better expressed in terms of constant dollars; ignoring the influence of inflation and other factors affecting future value and compensating for constant dollar forecasts by employing a comparatively "safe rate" of return to establish present value. The investment community (at least in North America), however, is not accustomed to forecasting future investment earnings in constant dollars; if for no other reason than the economy simply does not function in an inflation-free environment. Further the prediction of future incomes and values in current (inflated) dollars is necessitated for the purpose of making realistic comparisons between alternative investment opportunities.

In summary, practical ways and means exist for estimating capital reversions, developed by the investment community who are employing capital on the basis of expectations and anticipations of the future. Consequently, if the appraisal process is to reflect investor behaviour, forecasts of the future are not only warranted, but must be undertaken. Perhaps the following discussion on the subject of reversions will remove some of the anxieties associated with predicting the future value of a capital reversion.

Concept of the Reversion

Upon the granting of a lease, the owner of the demised premises transfers the exclusive right of use and possession (or occupancy) to another party for a specified period of time.; the owner of the premises becoming the landlord or lessor and the occupant being referred to as the tenant or lessee. At the date of lease termination, the rights of use and occupancy granted to the tenant revert to the landlord; hence, the origin of the term reversion.

Used without adjectives, the reversion generally refers to the leased physical premises which have been leased; time-framed to the date of lease expiry or, in the case of a multiple-occupant property, to the date of deemed disposition. If the capital value of the reversion is the point in question, the reversion is more appropriately designated as the capital reversion, meaning the capital value of the leased premises at the date of reversion. On the other hand, should the rental value of the demised premises be the object of the exercise, the reversion would then be referred to as the rental reversion.

Reversions, in the generality of the term, may be an actual or deemed occurence. In the normal course of events, the reversion of the demised premises to the landlord is an actual and specific realization, occurring at the date of lease expiry when the tenant ceases to possess any further rights of use or possession.

On occasion, reversion is an event which is deemed to occur at a specific moment in time other than at the date of lease expiry. In the valuation of a multiple-tenanted revenue property, through application of the Discounted Cash Flow Method, a specified holding period, income projection period or investment horizon is established for the purpose of calculating yield (or return on investment) or for the purpose of establishing a finite time frame for present value calculations. The investment community tends to refer to the termination date of this forecast period also as the date of reversion; although this date should (more appropriately) be referred to as the date of deemed disposition or deemed reversion. The expression deemed reversion appears to have become the more common term, on the basis that the date of such reversion is that point in time when the deemed proceeds of disposition revert to the owner of the investment.

The ensuing discussion will concentrate on the various considerations and methodology of establishing the capital value of the reversion, being the landlord's final receivable of earnings created through the granting of a lease or through the ownership and operation of a multiple-tenanted revenue producing property for a stated or prescribed period of time. The reversionary capital value or future worth of the demised premises, if income-producing in scope, will generally be a direct function of the estimated rental value of the premises or property at the date of reversion; albeit that many other factors will normally have to be considered or accounted for in the appraisal process. [The criteria related to estimating rental reversions (or the future rental value of leased premises) is set forth in the discussions pertaining to forecasting future market rent].

General Considerations in Valuing the Reversion

The amount of effort involved in estimating the reversionary value, or terminal value, of an asset will be governed to a considerable extent by consideration of the length of time before reversion occurs. If the term of a lease or the investment horizon of a property is fairly short (less than 10 years), the contributory present value if the reversion will be quite significant compared to the aggregate present value of the periodic earnings to be received up to the date of reversion. Consequently, a significant amount of weight will be placed on resolution of those factors and circumstances which bear on the estimation of the value of the reversion. In contrast, if reversion is postponed for an inordinate length of time, much less effort will be devoted to establishing value of the reversion, as its contributory present value will be diminished considerably by the magnitude of the corresponding discount factor.

The principal question to be resolved in the estimation of reversionary values, regardless of the significance of the reversion in terms of present value, is the predicted most probable use (or its highest and best use) of the property at the date of reversion.

If a revenue producing property is perceived to be suitable for continued use as it is presently developed, primary attention will be given to the estimation of the rental value of the premises at the date of reversion and to the corresponding establishment of the asset's then value based on its continued ability to produce income beyond

the date of reversion. In other words, the future worth of the property at the date of reversion (or simply its reversionary value) would be governed significantly by the then present worth of its future income producing capacity as measured from the date of reversion forward, generally found through the capitalization of net earnings at the date of reversion.

At the opposite end of the spectrum, the investment may have a limited remaining productive life as it is presently developed. Such a circumstance would command consideration of alternative uses of the asset and the corresponding means by which such values would have to be established. For example, the terminal value of the property might be adjudged to rest solely in the value of the underlying land for redevelopment with another use. Alternatively, the existing building might be better suited for extensive remodeling, refurbishing or even conversion to another use, in which instance a different set of parameters would be required to establish its future rental value (and to properly account for the corresponding capital costs of remodeling or conversion). In another instance, the existing building might be capable of a major expansion on the same site at the date of reversion, in which instance an entirely different set of criteria would have to be evaluated in the process of establishing the capital reversion of the property as a whole. In short, the most probable use of the investment at the date of reversion must be resolved before consideration can be given to specific valuation criteria.

Should definitive resolution of reversionary use be found difficult in light of the present age and condition of the asset and in consideration of anticipated changes in external market conditions, several alternative circumstances may have to be explored. Following the estimation of the residual or terminal capital value of the reversion under each scenario, a probability factor could be assigned to each and perhaps the discount rate adjusted accordingly. Too frequently, for example, one is inclined to estimate the reversionary value of an old property solely in consideration of the value of the land at the date of reversion. More frequently than not, old buildings are either restored, modernized or converted to another use, as long as the bone-structure of the building is structurally sound. The point of the argument is to explore all possible alternative uses of a property at the date of reversion, prior to estimating residual values.

Specific Factors Affecting Reversionary Values

Aside from general considerations which have to be taken into account as they bear on the methodology of establishing reversionary values and apart from the ways and means by which terminal values are set, certain specific factors may have to be accounted for in the process of arriving at a considered opinion of the net future worth of the investment. Some of the most critical considerations to be resolved deserve emphasis.

Physical Factors. The anticipated costs to correct deferred maintenance or to cure accrued deterioration must be properly accounted for.

Functional Factors. The expected capital outlays required to maintain the rental capacity of the property will also have to be considered in arriving at the net value of the reversion. If rental reversions are predicated on renovating and upgrading the space in question, the corresponding costs of attendant rehabilitation and modernization will normally constitute an offset to the capitalized value of the demised premises based on the new set of rental values.

Locational Factors. Appropriate consideration will also have to be given to predicted changes in the relative locational setting of the property between the date of analysis and the date of reversion, to the extent where such changes might affect either the rental value or the capital value of the asset.

Competitive Factors. Particular emphasis must be placed on evaluating possible changes in the competitive ranking of the property under study, in terms of consumer/user preferences, supply and demand factors and other related criteria to which the rental value or capital value of property is particularly sensitive.

Financial Factors. Anticipated changes in the structure of debt capital, if it affects the value of the asset under consideration, will have to be properly accounted for; both in terms of projected changes in the cost of debt or the need and availability of supplementary or extended financing at the date of reversion. For example, the present value of an asset may be amplified or suppressed by the presence of existing financing. Should the probability exist for material changes in the nature and extent of the debt structure with the passage of time, the influence of such changes must be quantified as best possible.

Trends in Earnings. Should the expected trends in rental income beyond the date of reversion have characteristics materially different from those forecasted until the date of reversion, appropriate adjustments would be required in the selection of the reversionary capitalization rate.

Re-leasing Costs. Leasing commissions and the costs of tenant allowances will usually be accounted for as a separate adjustment in setting reversionary values, particularly if such costs are not indirectly accounted for in the process of converting rental reversions to capital value.

Closing Costs. Terminal values of a multiple-tenanted property normally presume a deemed disposition of the asset at the date of reversion. If such is the case, proper credit would have to be given to brokerage fees and other related closing costs in order to ascertain the appropriate net reversionary value of the property.

Societal, Regulatory and Statutory Factors. Certain supplementary capital expenditures may have to be provided for at the date of reversion, for upgrading deemed necessary to maintain the operational status of the property, which may or may not necessarily increase the rental value of the property. For example, impending

changes in fire and safety codes, as well as functional modifications to a building to accommodate the handicapped, may require the infusion of capital from time to time. When a property is susceptible to such alterations at the date of reversion, the estimated gross value of the reversion will be subject to adjustment to reflect the anticipated extraordinary costs of effecting these changes. Impending governmental and societal regulations and controls could even be significant enough to seriously alter investor preferences, in which case an entirely different perspective might be placed on the task of estimating the value of the reversion.

Titular Factors. A property may have a "cloud on title" or one or more leases might contain unusual provisions which may influence the future marketability or value of the property. Options to purchase, participation in equity growth through refinancing, controls over expansion, etc. Any number of circumstances may arise from titular restrictions or contractual obligations which might have to be accounted for in the final determination of the net capital reversion.

Managerial Factors. Occasionally, the existing administration and management of an asset will result in the presence of encumbrances having an on-going and/or terminal impact on either the marketability or value of the asset, or both. Particular attention must be given to unusual and extraordinary circumstances and the duration of their impact on the value of the property. For example, a management contract may exist which calls for part of the renumeration for services rendered to be a percentage of growth in the value of the property; payable upon disposition.

The foregoing isolated circumstances are the more common specific factors which have to be considered in modifying gross reversionary values found through application of relevant appraisal methodology. While certain criteria affecting capital reversions cannot be figured with mathematical preciseness and while the length of time before reversion occurs may be so long as to call into question the reasonableness of certain calculations, any factor which has the probability of occurence should at least be judgment. ally accounted for in the generality of the matter when valuing the asset and brought to the attention of the recipient of the report. Generally accepted appraisal practice at least calls for full disclosure of all circumstances which affect value, even if quantification of such factors is difficult at the best of times.

Valuing the Reversion

The most common method of valuing a revenue producing asset at the date of reversion is through direct capitalization of the estimated net earnings of the property predicted to prevail on that date. This procedure, of course, presumes that the property will continue to have the capability of generating revenues of a prescribed nature and extent for a further period of time, generally of an indefinite duration.

In selecting the capitalization rate to be applied to the then net operating income, the investment community first selects the prevailing "going rate" for the type and location of the property in question, as if the asset was leased to its full operating potential at current market rent. Having established this base rate, and if no material changes are anticipated in market conditions which would affect the potential operating capacity of the property between the present time and the date of reversion, the base rate will generally be held constant or increased to a minor extent (by up to five percent of the base rate); such an adjustment being made to account for normal market changes and the general aging of the asset during the remainder of the forecast period.

Factors which foster an increase of more than ifve percent in the going capitalization rate are usually associated with one or more of the following circumstances. (1) The date of reversion will be at a point in time when the asset is beyond mid-life and some allowance may have to be made for extraordinary accrued depreciation. (2) The location of the property is expected to be significantly less desirable at the date of reversion, relatively speaking. (3) The property will become particularly sensitive to the competitive influences of the marketplace. (4) The property is being evaluated at a peak in a business cycle, when demand far exceeds supply and when prices are comparatively over-stated. (5) When supplementary capital expenditures of an extraordinary nature are anticipated in a general sense at the date of reversion, but are not specifically quantifable and (6) In general, when market conditions and/or the value of the property is expected to deteriorate moderately with the passage of time. In aggregate, the bonus for perceptions of the foregoing circumstances seldom exceeds twenty percent of the base rate, more or less. If anticipations of the future are particularly negative or if the property is expected to be near the end of its useful life expectancy at the date of reversion, alternative procedures will be used to set the capital reversion.

The reversionary capitalization rate will tend to be lower than the prevailing current rate if the date of reversion occurs at a point in time when: (1) A new unseasoned property will finally have achieved a proven track record of operating performance as it reaches maturity. (2) The property has entered a period of expanding market penetration. (3) When expansion is expected to be relatively imminent. (4) When preceding operational problems are expected to be fully resolved. (5) When the market is expected to be far more buoyant than at the date of valuation and (6) In general, when market conditions and/or the value of the property is anticipated to be in the up-swing of a business cycle. The sum of these circumstances seldom results in a blended decrease of more than twenty percent of the basic "going in" capitalization rate.

While the foregoing market practice of setting the reversionary capitalization rate might appear rather imprecise, it is simply the way in which the market functions. Investors realize that the contributory value of the reversion is quite sig-

nificant when matched against the present value of the periodic cash flow earnings. But investors are also aware of the fact that changes in the value of the reversion will only impact present value to the extent of the magnitude of the discount factor; the further removed is the reversion, the lighter will be the influence of any change in the value of the reversion, on present value. Finally, the investment community will seldom arrive at the decision-making stage without investigating the results of employing alternative value-measuring criteria as well.

Among the alternative means of valuing the reversion, the majority involve considerations of physical units of measurement. Should the asset be deemed to be at or near the end of its useful or productive life at the date of reversion, its terminal value could reside totally in the then highest and best use value of the land as if vacant; with due regard required of the costs of raising the existing structure and other incidental expenditures. Perhaps a major injection of capital could revitalize an existing development at that point in time, in which instance the appraisal process would be directed toward a cost-benefit analysis as part of the exercise of setting the reversion.

In summary, there is always a practical way in which to value the reversion and at times, it may be preferred to employ several methods and then select the alternative which best fits the probabilities of the future. Sensitivity analysis also allows one to determine the front-end margins of difference associated with several alternatives.

EDITOR'S NOTE: An article by Lincoln North on "Developing The Discount Rate" was included with his seminar material. This article will be printed in the December issue of "The Valuer."

IDEA 85

INVESTMENT AND DESIGN, THEIR EFFECTS ON YOUR ASSETS

Under the auspices of National Committee for Rationalised Building School of Architecture

Victoria University of Wellington Ministry of Works and Development

Concern over the shortening economic lifespan of many modern buildings has prompted the building industry, together with the Ministry of Works and Development, to call a major conference to discuss the topic.

A New Zealand and world first, the conference has been called IDEA 85 (Investment and Design, their Effects on your Assets), and will be held in Wellington in mid-October.

According to its chief organiser, Ministry of Works and Development chief architect (research), Mr H. P. (Henry) James, IDEA 85 is a response to recent data which shows that the lives of many modern buildings are not matching expectations.

He claims that as the traditional client/ contractor relationship has been largely replaced by that of entrepreneur/developer, investment considerations now often place undue constraints on building designers.

"A common scenario nowadays is that of the entrepreneur who sees a potential plot of land, gets some money together and approaches a design-build contractor, who undertakes to put up a building of the maximum size for the minimum price in the shortest possible time."

A related area of concern which will also be addressed by the conference is the growing cost and complexity of building maintenance and operation caused by the initial use of cheaper materials, finishes and construction methods.

"Factors such as component replacement and inefficient energy use can turn an initially attractive looking investment into a financial and technical millstone," Mr James said.

What is now starting to emerge, he claims, is that due to short term investment decisions, a massive replacement programme of relatively new buildings may have to be implemented sooner than need be.

Comprising representatives of all sectors of the building industry, the IDEA 85 organising committee has developed three major themes for the conference covering:

(1) Materials, environment and design.

(2) Procurement options and design determinants.

(3) Options/alternatives for the future.

"From the initial response to news of the conference from investors, builders, managers, researchers and users it is evident that there is widespread concern for the future," said Mr James.

I.A.A.O. BIBLIOGRAPHIC SERIES

THE VALUATION OF COMMERCIAL SERVICES PROPERTY

THE VALUATION OF COMMERCIAL SALES PROPERTY

The works are designed as a useful reference work, and bring together a considerable number of publications and articles which have appeared in the major authoritative property journals in recent years.

Prominent within the bibliographic series is mention of such publications as "The Real Estate Appraiser", "The Appraisal Journal", "The Valuer" (Australia), "The New Zealand Valuer". and "Real Estate Review".

Most of the references to the New Zealand situation are recent in origin, suggesting that the I.A.A.O. Research Department may not have had access to earlier New Zealand published works. The bibliography provides access to, and control of, the scattered books and articles on valuing commercial property. Many of the publications referred to will be available through the New Zealand Institute of Valuers library.

The bibliographies are available from:
International Association of Assessing Officers,
P.O. Box 94573, Chicago, 11. 60690-4573,
United States of America.

Please note that the monetary sums referred to are in United States Dollars terms.

- Editor.

IAAO NEWS

Appraising and assessing commercial property by the Research and Technical Services Department of the International Association of Assessing Officers (IAAO).

This is a two-volume set composed of The Valuation of Commercial Services Property (Bibliography No. 9) and The Valuation of Commercial Sales Property (Bibliography No. 10).

The Valuation of Commercial Services Property, the ifrst volume, opens with a section listing general works on the valuation of all commercial property. Titled "Commercial Districts and Commercial Property," it brings together references to commercial districts, appraisal of commercial property (including works in general, on depreciation, on distressed, damaged, and lfawed property, on commercial leaseholds, and on real and personal property as part of a commercial venture), assessment and mass appraisal of commercial property, and valuation of commercial land. The following nine sections contain references to specific types of commercial services property: airports, banks, commercial condominiums, commercial recreation property (including bowling centres, theatres, sports arenas, convention halls, race tracks, and clubs), grain elevators, office buildings (subdivided for general office buildings, medical office buildings, and forecasting demands for offices) outdoor advertising structures, parking lots and garages, and warehouses and waterfront property.

The Valuation of Commercial Sales Property, the second volume, continues the lists of references to specific types of commercial property with its sections on stores and shops, shopping centres and pedestrian malls, motor vehicle sales and service properties, and the property of food and beverage servers and franchised businesses.

Both volumes contain careful annotations that state the author's purpose, list the major points made in the work, and note special contents such as sample appraisals, forms, tables, and bibliographies.

The Valuation of Commercial Services Property, a 100-page bibliography with more than 400 main references, is priced at $18.00 ($15.00 for IAAO members). The Valuation of Commercial Sales Property, a 57-page bibliography with nearly 300 main references, is priced at $14.00 ($11.00 for members). The two volumes are sold as a set for $26.00, a saving of eighteen per cent.

REGISTRATION BOARD DECISIONS

VALUERS' REGISTRATION BOARD.

The following is an edited version of a recent decision of the Valuers' Registration Board concerning an inquiry into a complaint against a Public Valuer. Heard before Mr M. R. Hanna (Inquiry Chairman), Messrs D. J. Armstrong and P. E. Tierney. Date of Hearing 28 August 1984.

This inquiry arose from a complaint received on 21 September 1983. The complaint alleged, in effect, that the valuation and subsequent mortgage recommendation were grossly overstated and that this constituted evidence of negligence or incompetence.

The complaint was referred to the Valuer-General for investigation and his report was put before the Board at a Meeting held on 27 January 1984. It was determined that there appeared to be reasonable grounds for the complaint and that an inquiry should be held.

The charges framed in terms of Section 31 (1) (c) of the Valuers' Act cited grossly excessive valuation and mortgage recommendation.

The hearing was originally set down for 6 June 1984, but later by consent was postponed until 28 August 1984 at which time the defendant made no appearance nor was he represented by legal counsel. Since the defendant had been given every opportunity to appear at the inquiry and offered no explanation for his absence, the Board decided to proceed in the normal way.

Briefly stated, the circumstances which led to the complaint were that the defendant was instructed by the complainant to complete a valuation of the subject property. This was described to the Board as comprising a parcel of some 6,055 sq. metres upon which stood a substantial two storey dwelling, a bungalow, a cottage and a number of other improvements. The land was in five separate Titles and occupied a commanding position in a highly sought after locality. The land was the subject of a Planning Consent for a relatively intensive development comprising a mix of commercial and residential houses.

In order to not the facts of the matter in sequence, the Board recorded that on 23 September 1981, the subject land was purchased for the sum of $1,600,000 subject to the payment of an initial deposit of $30,000 by 16 December 1981 and the balance of $130,000 deposit within six months of the date of agreement. The vendor agreed to a first mortgage back to himself of $1,440,000 with no repayments or interest until 23 March 1983. By 16 March 1982 planning consent had been granted for a residential/commercial development project and in his valuation dated 18 March 1982 the defendant valued the property at $3,127,000 recommending its suitability as a security for mortgage advance under the terms of the Trustee Act up to $2,084,000.

Based upon that recommendation the complainant, through his firm's nominee company, agreed to advance a second mortgage securing a principal sum of $552,000. The property was subsequently sold in July 1983 to the first mortgagee pursuant to the Powers of Sale contained in his mortgage at the mortgagee's reserve

price of $1,500,000 and then resold to another party in August 1983 for the sum of $1,290,000. In July 1983, the solicitors for the second mortgagee instructed a Public Valuer to value the property as at 18 March 1982 and his assessment of its market value then was $1,250,000 with mortgage recommendation of $750,000. Furthermore, as a part of his inquiry the Valuer-General had later obtained a valuation from a Valuation Department District Valuer, and his independent assessment as at the same date was $1,230,000 with a mortgage recommendation of $738,000.

To a substantial degree the defendant's valuation had relied upon a highly confident view of the prospects of the land for successful development in terms of the proposed scheme.

Essentially, it is with the validity of his judgement as to the development potential of the land at the time of valuation and the soundness of the techniques he used in its estimation that this inquiry is concerned.

The case for the Valuer-General was opened by Crown Counsel with a general description of the above matters noting that both the first and second mortgages made against the security of the property in 1982 were within the first mortgage limit recommended by the defendant and it appeared that the second mortgagee's funds had not been recovered.

Counsel claimed that the relevant factors in the valuation were firstly the effect, if any, of the Town Planning Consent by the City Council dated two days prior to the defendant's valuation and secondly, the value of the land by sales comparisons including the sale to which we have previously referred in September 1981 for $1,600,000. It was Counsel's case that the valuation made by the defendant was grossly high and its methodology grossly incompetent and that regardless of its accuracy or otherwise that it was incompetent to recommend a mortgage advance as high as two thirds of the valuation on a property of this type.

As the first witness, Counsel called the Valuer-General who gave formal evidence submitting documents relating to the complaint and to his investigations of it.

Counsel then called the District Valuer. The District Valuer presented a lengthy and detailed report dated 21 December 1983, but effective as to value from 18 March 1982. This wide ranging report included a detailed physical description of the locality, land and improvements and a consideration of various market factors at the time. Town planning aspects were dealt with in detail, including the consent granted in March 1982, and the actual potential which the District Valuer considered to exist for a project of that type at the time. In short, it may be said that the District Valuer had little confidence in the economic viability of the planned development and was of the opinion that the highest and best use of the land was for a predominately residential development possibly with some very limited commercial function. He provided a large range of comparative sales and set out alternative approaches to the valuation exercise by a hypothetical development of either a whole site for residential use with some commercial content or by the retention of the existing dwelling and the redevelopment of the balance of the land. He also analysed sales of properties of similar zoning with adjustment for time and location and from this evidence valued the property on an area basis. The value bracket which resulted ranged from $1,205,000 to $1,241,000 and he set the value of the subject property as at 18 March 1982 at the amount of $1,230,000. After presenting his report, the District Valuer was examined in some detail by Counsel and also questioned at length by members of the Board who formed the opinion that the evidence he had offered was thoroughly researched, professionally and impartially considered and carefully presented.

Counsel then called the Public Valuer who had prepared the valuation for the second mortgagee. This valuation was also with effect from March 1982 but had not initially been made as any part of the inquiry for the Valuer-General. Although differing somewhat in content and approach, his report was also detailed, thorough and comprehensive. He too quoted a number of comparable sales and expressed reservations concerning the basic concept of the development upon which the defendant had placed so much reliance. The range of values indicated by his analysis was $1,084,000 to $1,340,000 and he finally concluded that the value as at March 1982 should be stated at $1,250,000. The Public Valuer answered to further examination by Counsel and to questioning by the Board. His answers were both authorative and persuasive.

Both valuers were questioned by Counsel on aspects of the valuation prepared by the defendant, and both submitted that not only was there no market evidence to support the level of value which the defendant had postulated but that his calculations of residual land value from the basis of analysis of a hypothetical development were defective in a number of technical aspects. The Board was very considerably assisted by the appearance of these two witnesses and thought the evidence of each to be of commendable quality.

In considering the case before it, the Board has been aware of an additional responsibility it carries in the absence of the defendant or his legal representatives. In his defence is only the report he addressed to the complainant on 18 March 1982, while against are the independent but mutually supportive opinions of two well qualified and highly regarded valuers. Accordingly the Board examined the defendant's report in detail, both as an entity and in the light of the evidence given by the witnesses for the Valuer-General. After the careful and critical examination of the evidence before it, the Board are entirely satisfied that the professional conclusions of the witnesses do fairly reflect the values of the subject property in March 1982. The Board believes that the defendant's report seriously, indeed grossly, overestimated the development potential for the land and gave quite superficial attention to the true prospects of the development project. Based on the evidence before the Board, it is clear the defendant failed to make a balanced and realistic analysis of the concept, the economics, or the market prospect of the scheme and that several aspects of his application of established valuation techniaues were deficient and misleading. Furthermore, his recommendation as to the security offered by the property for market purposes was both improper and shown to be irresponsible.

In all the Board was in no doubt that the charges of incompetence laid against the defendant. which have been the subject of this inquiry, are wholly proven.

In weighing the penalty which must be imposed, the Board felt obliged to consider not only the very serious and disturbing aspects of the defendant's valuation of the subject property, but also the record of his previous appearances before the Board. It was the Board's view that the present circumstances in themselves justified the most severe action and that in the context of his past record, there could be no room for leniency.

It is the decision of the Board, acting under the powers vested in it by Section 31 (1) (c) of the Valuers' Act 1948, that the name of the defendant be removed from the Register of Valuers.

VALUERS' REGISTRATION BOARD.

The following is an edited version of a recent decision of the Valuers' Registration Board concerning an inquiry into a complaint against a Public Valuer.

Heard before

Mr M. R. Hanna (Inquiry Chairman).

Mr R. P. Young.

Mr P. E. Tierney.

Date of Hearing: 20 November 1984.

This inquiry arose from a complaint received 24 November 1983. The Complainant alleged, in effect, that the valuation and subsequent mortgage recommendation were excessive and so unrelated to the true market value of the property as to indicate negligence or incompetence on the part of the Valuer.

In terms of Section 32 (1) of the Valuers' Act 1948, this complaint was investigated by the Valuer-General and his report dated 30 January 1984 came before the Board. After considering this report, the Board decided that in terms of Section 32 (2) of that Act an Inquiry should be held.

The circumstances which led to the complaint were that the complainants had recently sold the subject property for $107,000 including chattels of $7,000.

A term of the contract was that the Vendors "leave in" a second mortgage of $22,000 which was to rank behind the first mortgage and be limited to a Trustee recommendation of a registered valuer.

A valuation and Trustee recommendation obtained from the defendant who valued the property at $140,000 excluding chattels and recommended a loan on first mortgage not exceeding $93,000.

The Valuer-General was the first witness and he gave formal evidence submitting documents relating to the complaint and the investigation of it, including two valuations of the subject property, one completed by a Public Valuer, the other by a District Valuer.

A comparison of the three valuations is as follows. All valuations excluded chattels.

	Defendant	Public Valuer	District Valuer
Improvements	75,000	56,000	54,500
Land Value	65,000	50,000	48,000
Market Value	$140,000	$106,000	$102,000

While it can be seen that the Public Valuer's and the District Valuer's valuations bear a close relationship, the Board accepts that each made his valuation independently and based it only on sales information that would be available at the relevant date, 11 July 1983. In reply to questions from the Board, the Public Valuer thought that with hindsight his figure could be increased by a maximum of +5 to +10% and the District Valuer under similar conditions up to $110,000.

The Board then has to consider whether a valuation of $140,000 is "grossly overvalued" when other expert witnesses produce estimates in the range of $110,000 - $116,000 and having regard to other evidence presented to it.

The subject property is a villa erected around 1906 with a floor area of approximately 114 m2 plus a verandah and porch and with a timber deck at the rear, a glasshouse on one wall and carport on another. Other buildings comprise a laundry/toilet and store shed.

The house is in reasonably good order and has had a degree of modernisation.

It has a level, unsubdivisible section of 1051 m2 which under its Residential 'D' zoning could accommodate two further two storied flats on a "cross lease" title.

This is possible because the house is located close to the true right hand boundary. There is an asphalt tennis court which would need to be sacrificed to achieve a second unit.

Opinion was sharply divided as to the practicality of such a sub-division as there is a 300 mm diameter stormwater drain running diagonally under the tennis court which probably necessitates special foundation or a rather distorted placing of the units to avoid that problem.

It seems to the Board that neither the Defendant nor the Public Valuer were aware of the drain's existence at the time they made their valuations for if they were aware, they should have mentioned it in their reports. The Defendant indeed states in his report

> . it would be practical to build a home unit on the land now occupied by the tennis court and to divide this off by way of a cross lease .....

In the event the Defendant purported to have valued the land in two ways:

(a) As a two unit cross lease site at $32,000 per unit, or

(b) As a three unit cross lease site at $22,000 per unit.

The District Valuer and the Public Valuer treated it as a single site for different reasons. The District Valuer considered that a purchaser would discount the added site value because of the costs associated with the additional foundations and the extra delay and risk in gaining Council approval. Under cross-examination as to its additional value as a three unit site, the District Valuer pointed out that the tennis court and rear deck would have to be demolished and that there could be a loss in value of the villa of 5-10% but that with hindsight he thought the value of the whole property could be increased up to $10,000 i.e. an increase of $7,500.

The Public Valuer produced sales of bare land in late 1982 and early 1983 where areas to 1029 m2 with a three unit potential and 1258 m2 with a four unit potential sold at figures between $70,000 and $79,500. His evidence was that some of these lots were used for single unit houses and some for cross leases. He based his land value on these sales with an appropriate reduction for the lessened saleability of the lower end of the area.

The Public Valuer accepted that in hindsight he would have increased his land and capital value by 5-10,% or on his valuation of $106,000 by a maximum of $10,600 which on his original assessment of the land of $50,000 increases this figure to a maximum of $60,600.

Making the appropriate increase of $7,500 in the District Valuer's land figure of $48,000 to $55,500, we have a range of land values of

The Defendant	$65,000
Public Valuer	$60,600 Maximum.
District Valuer	$55,500 Maximum.

While the Board considers the correct figure to be nearer the District Valuer's $55,500, it does not consider the Defendant's land value to be "grossly over valued" by comparison with the Public Valuer's figure.

Turning to the next step in the valuation, that of the improvements, there was a wide divergence. All valuers purported to have obtained a "net per square metre value" for villas by analysing sales. This method broadly speaking consists of taking sale prices and deducting from them a land value and other improvements' value and arriving at a nett per metre figure from the residual value. Using this method, which has the advantage of adjusting depreciation by sales rather than by a mathematical calculation the Public Valuer and District Valuer arrived at a nett figure of around $300 per square metre, a gross replacement cost of around $600 per square metre and hence a depreciation figure of 50%.

The Defendant on the other hand used a nett rate of $545 p.s.m. which he said was based partly on the sale of a unit in July 1982. His experience was that using only 20% depreciation after allowing a replacement cost of +50% over the modal rate produced a suitable answer.

When asked to demonstrate the accuracy of his figures by reference to four of the sales he considered most relevant the Defendant was only able to demonstrate that the $545 per square metre figure produced a ridiculously low land figure in most of the examples or conversely if a suitable land figure was adopted, which is the accepted method used by the other experts, then a nett value figure of around $330 was indicated.

In only one case, with a sale price of $140,000, did the figure approach $545 per square metre. The land area of this property is 1095 m2; on it is a villa of 186 m2 which had been converted to flats. Allowing a land value of $65,000 as had the Defendant on the subject property, the nett residual value is $75,000 or $403 per square metre.. This sale was discarded by the two other valuers as in their opinion, flat conversions are a market of their own and quite unsuitable for comparisons with single family houses.

In respect of the second step of the valuation exercise the Board is satisfied that the Defendant's $545 nett per square metre is quite unsupported by sales and adopts the $300 per square metre nett used by the other valuers. In the Board's view, the Defendant has grossly overvalued this item.

The individual items that make up the valuation could be compensating if for example, the land com-

portent had been understated and the improvements overstated, but clearly given firstly that the Defendant's land value is $4,500 more than the highest estimate of the other two valuers and secondly the Board's opinion as to the house component, this coincidence appears unlikely.

Nevertheless it is, in the Board's view, necessary to examine the Defendant's total valuation in the light of the sales evidence available.

Twelve sales were considered. These ranged in price from $78,000 to $140,000.

The Defendant appeared to place considerable reliance on the sale of one particular property (X) as it was the one sale available at that date that approximated his valuation of the subject *property*. The Board does not accept that this sale is ideal for comparisons. The evidence before the Board from the Crown Witnesses was to the effect that there was a downward gradient in sales in the area and that the subject property was in the less saleable area than the comparison property. The Board accepts this evidence.

One other sale approached the level the Defendant fixed on the subject property. This property is a 1935 bungalow of 132 m2 and is again in a more saleable locality.

The most pertinent sale amongst the remainder is that of the subject property. Affidavit evidence from a Real Estate Salesman, stated that the property had been listed with the Multiple Listing Bureau with an asking price of $140,000 and that ultimately a sale was effected to the present owner for $100,000 plus $7,000 chattels.

Subsequently, on 1 October 1983 another contract which involved a partial swap with a small farm was negotiated. The price quoted for the subject property being $165,000.

Sale prices where swaps or partial swaps are involved are notorious within the valuation profession and are seldom, if ever, accepted as evidence or market value. The Board is being asked in this case to accept on face value a swap transaction that did not proceed, involving a farm property whose value was expressed as $205,000 but without any evidence being presented as to the real value of the property or the measure of the equity of exchange. The Board cannot and does not accept that this evidence has any probative weight.

Disregarding the sale at (X) and the swap deal on the subject property, the range of comparable sale prices lies between $78,000 and $120,000. The sale price of $100,000 is consistent with the other sales and supports, in the Board's opinion, the market level adopted by the Crown Witnesses.

The Board accepts the opinions of the District Valuer whose conclusions the Board found compelling, that the market value of the property lies in the range of $102,500-$110,000 but is conscious that the Public Valuer fixed the maximum at $116,600. In the Board's opinion, these conclusions are a careful consideration of the evidence available.

Returning then to the Defendant's valuation, the Board finds:

(a) The land value section of the valuation was high, but not grossly excessive.

(b) The value of the improvements section was grossly excessive.

(c) The capital value or market value at $140,000 is unsupported by the sales evidence, and was grossly excessive.

The Board finds the Defendant guilty of incompetent conduct in terms of Charge No. 1.

Charge No. 2 which relates to a mortgage recommendation is a direct consequence of a Trustee recommendation which limits the recommendation to two-thirds of the market value. In the circumstances of the finding on Charge No. 1 that the value of the property is correctly expressed at the District Valuer's figure of $110,000 then the maximum loan recommendation is $73,326.

The Board finds the Defendant guilty of incompetent conduct in terms of Charge No. 2.

The Board treats both of these breaches as serious and accordingly has given lengthy consideration to the suspension or removal of the Defendant's name from the Register of Valuers. However, as these are first offences under the Valuers' Act the Board has opted for the lesser penalties as set out in Section 33 of the Act and accordingly by the powers thereby vested in it, reprimands the Defendant as to Charge No. I and ifnes him the sum of TWO HUNDRED AND FIFTY DOLLARS ($250.00) and reprimands him as to Charge No. 2.

VALUERS' REGISTRATION BOARD.

The following is an edited version of a recent decision of the Valuers' Registration Board concerning an inquiry into a complaint against a Public Valuer. Heard before Mr D. J. Armstrong (Inquiry Chairman), Messrs M. R. Hanna and P. E. Tierney. Date of Hearing, 14 August 1984.

This inquiry arose from a complaint received on 6 December 1983. The complaint alleged, in effect, that the Valuer had acted in an unprofessional manner and acted improperly and unethically.

The complaint was referred to the Valuer-General for investigation and his report was put before the Board at a meeting held on 15 April 1984. It was determined that there appeared reasonable grounds for the complaint and that an inquiry should be held.

The charges framed in terms of Section 31 (1) (c) cited gross over-valuation of the property in question; and mortgage recommendation made under Section 10 of the Trustee Act 1956 was not in compliance with that Act.

The Defendant pleaded Not Guilty to Charge I and Guilty as to Charge 2.

Briefly stated, the circumstances which led to the complaint were that the Defendant was instructed by the Complainant to complete a valuation of the subject property. This property had been purchased by the Complainant and other investors for $145,000. The Defendant submitted a valuation of $200,000.

With consent of Counsel the Valuer-General's report to the Board was admitted as evidence and the Valuer-General was not called. His report contained the letter of complaint, correspondence with the Defendant, a covering letter to the Board from the Valuer-General, copy of the Defendant's report and a copy of a report from the District Valuer, Valuation Department.

The District Valuer formally presented his report. This report was compiled on 14 December 1983 and valued the property as at 24 November 1982. A summary of the District Valuer's valuation compared with the Defendant's is:

	Date	Total Lessee's Interest	Lessee's Int. in Land Value	Improvements
Defendant	24/11/82	$200,000	$3,000	$197,000
District Valuer	24/11/82	$140,000	$5,000	$135,000

The District Valuer's report described the land as comprising 1201 m2 being a Ground Lease of 21 years from 1 June 1980, subject to 5 yearly rent reviews. On this land was built in 1960 and 1963 a warehouse of quality construction comprising 891.2 m2 The report recorded that the property was sold for $110,000 in 1980. It also described the zoning and noted in terms of the Local Council's Operative District Scheme that the site was deficient as to front yard requirements and off street parking; thus restricting the property to a conditional use status which could affect future development and higher utilisation. The report also noted that any deviation from the current usage, or structural alteration had to be approved by the Lessor. Furthermore, the District Valuer noted that the type of lease being 21 years with 5 year reviews of rental was the standard commercial lease issued by the lessor.

The District Valuer presented schedules of sales and commented on them, expressing the view that sales of similar properties generally were hard to find, but

that the upper limits were set by properties closer in to the central city area. He also presented schedules of rentals of commercial and industrial properties to substantiate his rental assessment of $20,400 as opposed to the Defendant's rental assessment of $29,000. The District Valuer stated that the subject property was placed on the market in January 1982 at $180,000 and was subsequently sold for $145,000 in October of that year to the Complainant. Under cross-examination, the District Valuer agreed that the property could, subject to Town Planning approval, be subdivided into three areas relatively easily and that as such he would expect higher rentals to accrue, although he commented that the building had been tenanted on a monthly tenancy to three parties producing a gross rental of only $14,900 per annum. To a question from the Board, the District Valuer replied that to the best of his knowledge the property had not been tenanted on any long-term basis since it was sold in 1981. The District Valuer's evidence concluded the case for the Valuer-General.

The Solicitor for the Defence reminded the Board that his client's instructions had been given subsequent to an unconditional agreement to purchase the property by the Complainant and to the completion of preliminary arrangements for borrowing against its mortgage security. He then called the Defendant who presented his valuation report and supporting sales data. He stated that he was aware of the price at which the property had recently been purchased and his sales evidence generally confirmed the District Valuer's comments that the market in the area for this type of property was variable. In support of his assessed rental of $29,000 the Defendant quoted an arbitrated rent for a property closer to the Central Business Area at a similar rate per square foot and also stated that he had assessed his rental on the assumption that a multiple tenancy agreement could be concluded. He admitted that he had failed to include comment or explanation on this matter in his report and that there would be costs, which he now guessed would be in the vicinity of $30,000 to $40,000, in making alterations necessary for such a multiple tenancy while any such change would be subject to Planning approval. He stated that he now considered his rental assessment of $29,000 to be a little high but claimed that he had been influenced in maintaining that figure by information that the new owner was negotiating with tenants at that level.

Even had that been the case the Board would have expected the Defendant to have made his own careful, thorough and independent analysis of all tenancy options and their consequences, and it is apparent that this he substantially failed to do.

As for his mortgage recommendation of $100,000, the Defendant stated that he was not asked for a recommendation but as a matter of course included one in his report. He had not been aware of Section (3A(a)(iv) of The Trustee Act, and claimed that a number of his colleagues in both valuation and leval practices were also unaware of this limitation. To propose that an alleged general ignorance of the matter should be treated as an excuse is not acceptable to the Board.

The Defendant also advised that the sale which involved his valuation had fallen through and that the Vendors had taken action for recovery against the Complainant. He stated that the Vendor had let the property as at 1 July 1984 for 5 years at an annual rental of $16,730 with the Lessor paying insurance and part of the rates.

The Defendant told the Board that he had calculated a valuation on the subject property on a cost less depreciation basis which produced a figure of $182,500 but disregarded that in favour of a rental approach which produced figures of $197,226 - he then rounded this figure to $200,000 to get "a nice round figure for mortgage recommendation". The Board notes that using the Defendant's figure of $3 per square foot produces a figure of $28,761 and that this, too, was apparently rounded up for the sake of convenience.

The Board also notes the Defendant's final paragraph in his report which reads: "Recent sales evidence indicates an increase in values and this is expected to continue for some time. I have no doubt that the property would be readily sought after if offered for sale at a figure in the vicinity of the assessed figure. The property should therefore afford excellent security".

In considering the evidence before it, as to Charge 1, the Board concludes that this statement was inaccurate. and grossly misleading. Likewise, the Board concludes that the Defendant's report and valuation did display a high level of incompetence.

It notes particularly:

- the rental approach was made on the basis of multiple tenancies which required Town Planning approval, Lessor's consent and an expenditure of $30,000-$40,000, none of which were mentioned in the valuation report.
- The market value assessed by the Defendant was in no way supported by the sales evidence put forward, either by the prosecution or the defence.
- The rental used was pitched at a far too high level, even if the property could have been let in three tenancies.
- The proposal for subdivision into three tenancies was accepted quite uncritically and with no allowance for the substantial costs involved or for the uncertainties of planning approval or for the economic realities of the marketplace.
- That the valuation presented at $200,000 against known recent purchase price of $145,000 was not explained in any way to the client.

Now, having considered all the evidence before it, the Board finds Charge One to be proven.

Charge Two for which the Board has previously recorded the Defendant's plea of guilty, related to his recommendation that the Lessee's interest in the land provided adequate security for a mortgage advance under the terms of The Trustee Act, 1956 and its Amendments. Section 4(3A)(a)(iv) of that Act, specifically provides that no advance should be made except in respect of a lease which "does not require periodic reviews of rental at intervals of less than seven years". It is quite plain that such was not the case concerning the lease of the property for we have already noted the District Valuer's evidence and the Defendant's admission to the effect that this is a 21 year perpetually renewable lease with review of rental on five year rests.

The Board cannot accept as mitigation that this is a matter which is not widely known to Valuers. In the Board's view, all Registered Valuers must be fully conversant with all those parts of The Trustee Act which relate to their actions in making valuations and mortgage recommendations. Failure to show such an appreciation must be treated as a breach of competence. The Board rejects the submission by Counsel for the Defendant that as the valuation was not made for mortgage purposes, the consequences of an incorrect mortgage recommendation were less.

Penalty

The Board treats both of these breaches as serious and accordingly has given lengthy consideration to the suspension or removal of the Defendant's name from the Register of Valuers. However, as these are ifrst offences under the Valuers' Act, we have opted for the lesser penalties as set out in Section 33 of the Act and accordingly by the powers thereby vested in us, reprimand the Defendant on both charges and fine him the sums of One Thousand Dollars ($1,000.00) as to Charge One and Four Hundred Dollars ($400.00) as to Charge Two.

NORTHLAND:

COUTTS MILBURN & ASSOCIATES-
REGISTERED VALUERS AND PROPERTY CONSULTANTS
89 Cameron Street, Whangarei,
P.O. Box 223, Whangarei.
Phone (089) - 84-367 and 84-655.
W. A. F. Burgess, Dip.V.F.M., A.N.Z.I.V.
C. S. Coutts, A.N.Z.LV., F.R.E.I.N.Z.
G. T. Hanlon, V.P.U., A.N.Z.I.V.
L. T. O'Keefe, F.N.Z.I.V.

ROBISONS
REGISTERED VALUERS
P.O. Box 1093, Whangarei,
Phone (089) - 88.443 and 89-599
G. J. Bacon, Dip.V.F.M., A.N.Z.I.V.
J. F. Hudson, V.P.U., A.N.Z.I.V.
A. C. Nicholls, Dip.V.F.M., A.N.Z.LV., M.N.Z.S.F.M.
T. S. Baker, V.P.U., A.N.Z.I.V.
R. L. Hutchison, Dip.Urb.Val.
G. S. Algie, Dip.Urb.Val., A.N.Z.I.V.

AUCKLAND:

ABBOTT, CARLTON, LAWTON & CO. -
REGISTERED VALUERS AND PROPERTY CONSULTANTS
225 Great South Road, Greenlane, Auckland,
P.O. Box 17-063. Greenlane.
Phone (09) 548-061, and 541-522.
Waiheke Island Office,
Phone (0972) 7718.
W. J. Carlton, Dip.Ag.. Dip.V.F.M.. A.N.7 T V.
R. D. Lawton, Din.Urb.Val.(Hons.). A.N.Z.T.V.
R. McG. Swan, Dip.Urb. Val., A.N.Z.I.V.
S. R. Marshall, Dip.Urb. Val.(Hons)., A.N.Z.I.V.
S. H. Abbott, A.N.Z.I.V., F.R.E.I.N.Z. (Consultant).

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BARRATT-BOYES, JEFFERIES, LAING & PARTNERS-
REGISTERED VALUERS
4th Floor, Quay Tower, 29 Customs Street \Vc,t. Auckland,
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D. B. C. Barratt-Boycs, B.A.(Hons.), F.N.Z.I.V.
R. L. Jefferies, Dip.Urb.Vnl., B.C.A., F.N.Z.I.V., M.P.M.I.
R. W. Laing, A.N.Z.I.V., A.R.E.I.N.Z.
M. A. Norton, Dip.Urb.Val.(Hons.), A.N.Z.I.V.

C. F. BENNETT (VALUATIONS) LIMITED -
PROPERTY VALUERS AND CONSULTANTS
9th Floor, Countrywide Centre,
280 Queen Street, Auckland.
P.O. Box 5000, Auckland 1,
Telephone (09) 799-591.
Registered Valuers
R. M. McGough, Dip.Urb.Val., F.N.Z.I.V., M.P.M.I.
A. G. Hilton, M.D.A., A.N.Z.I.V.
C. N. Chamberlain, Dip.V.F.M., Dip.Ag.,A.I.V., A.N.Z.I.V.
L. V. Brake, A.N.Z.I.V.
M. J. G. Steur, Dip.Val., A.N.Z.I.V.

D. E. BOWER & ASSOCIATES -
REGISTERED VALUERS, PROPERTY MANAGERS, PROPERTY AND INVESTMENT CONSULTANTS
Coach House Lane, 273 Parnell Road, Auckland,
P.O. Box 37622, Parnell,
Phone (09) 795-720.
David E. Rower, Dip.Urb.Val., A.N.Z.I.V., A.R.E.I.N.Z., M.P.M.I., A.N.Z.I.M.
Mark F. Tictjcn, B.Agr.Comm., A.N.Z S.F.M.
Kenneth A. Chambers, Dip.Urb.Val.(Hons.), LL.B.(Hons.)

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