

VALUERS' JOURNAL

JUNE 1994

IN THIS ISSUE

- ◆ Marketing Valuers' Myopia
- ◆ Valuations for Mortgage Security and Accounting Information Purposes
- ◆ Financial Analysis of Dairy Farm Conversion - Manawatu
- ◆ Alternative Dispute Resolution
- ◆ Leisure Centres in the 1990s
- ◆ Implications for Property from Resource Management Trends

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NEW ZEALAND VALUERS' JOURNAL

JUNE 1994 ISSUE

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The NEW ZEALAND VALUERS' JOURNAL is the official publication of the New Zealand Institute of Valuers. The focus of the Journal is to publish researched articles on valuation, property investment and related matters, and to encourage the investigation and expansion of the frontiers of knowledge that cover such fields. It seeks to publish reports of decisions of hearings of tribunals, courts, and arbitrations of special relevance to the profession.

The New Zealand Institute of Valuers has a special interest in scholarly research that can be useful in property valuation and development, finance, investment, property management and market analysis, real estate and the valuation of plant. The Editorial Board is willing to work with any potential author who is developing new and exciting ideas.

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All contributions should be typewritten and accompanied by a biographical note of the author. The Editor reserves the right to accept, decline or modify material. Views expressed by the editors and contributors are not necessarily endorsed by the New Zealand Institute of Valuers. Copies of manuscript should be retained by the author as they cannot be returned.

Deadline: two months prior. Each manuscript submitted will be reviewed by the Editor to evaluate its appropriateness for the Journal and assigned anonymously for review by two or more referees.

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INSTIT

CONTENTS

Page		Page	
5	Editorial Comment	19	Valuations For Mortgage Security And Accounting Information Purposes
6	From The President's Pen	32	Financial Analysis of Dairy Farm Conversion In the Manawatu Region
6	NZIV 1994 AGM Report	35	Legal Issues from Kensington Swan
7	Young Professional Valuer of the Year Award	41	Leisure Centres in the 1990s
8	Fellowship Citations	48	Implications For Property From Trends In Resource Management
13	People Profiles	50	Technology Forum
14	April 1994 Council Meeting.	53	Legal Decisions
16	The Fourth Australasian Real Estate Educators Conference	59	Professional Directory
17	Marketing Valuers' Myopia	70	Publications Available from the NZIV

Feature Articles

Page	
17	<p>MARKETING - VALUERS' MYOPIA - A J BRADY</p> <p><i>A review of the effects on the valuation profession following the introduction of the 1986 Commerce Act and the way ahead for marketing the services of Registered Valuers.</i></p>
19	<p>VALUATION FOR MORTGAGE SECURITY & ACCOUNTING INFORMATION PURPOSES - R T M WHIPPLE</p> <p><i>A study of the problems that may be encountered in assessing values for mortgage security and accounting purposes where particular properties do not match established value definitions.</i></p>
32	<p>FINANCIAL ANALYSIS OF DAIRY FARM CONVERSION - I A MCCARTHY</p> <p><i>A computer based study of the viability of farm purchase prices for conversion to dairy farming.</i></p>
35	<p>In the Legal Issues forum contributed by Kensington Swan</p> <p>ALTERNATIVE DISPUTE RESOLUTION - S WILLIAMS</p>
41	<p>LEISURE CENTRES IN THE 1990s DIFFICULTIES IN BALANCING SOCIAL RESPONSIBILITY WITH PROFIT MOTIVES - S G BOND</p> <p><i>A review of local authority involvement in recreation facilities and of the possibilities for change to private sector involvement with a computer based case study.</i></p>
48	<p>IMPLICATIONS FOR PROPERTY FROM TRENDS IN RESOURCE MANAGEMENT - A CROSBY</p> <p><i>A brief review of historical events emanating from lack of resource management and the ways in which resources, the environment and property values may be enhanced with proper management under the Resource Management Act 1991.</i></p>

EDITORIAL COMMENT

The Continuing Importance of Valuer Independence

Independent expert opinion from registered valuers has long been the allmark of the valuation profession in New Zealand and it is suggested this ideal is enshrined in the motto contained in the New Zealand Institute of Valuers crest "integrity & fidelity".

These two words appear again in the first ethic of the NZIV Code of Ethics "SERVICE

1. The first duty of every member is to render service to his clients or his employer with absolute fidelity and to practice his profession with devotion to high ideals of integrity..."

The recent trend of extreme competition in business in New Zealand following economic restructuring and deregulation of most formerly licensed or regulated trades, professions or business has introduced elements of pressure which may not have been previously experienced. The relaxation of restrictions on trading hours, competitive advertising and price controls has provided the incentive for this new competitive environment. The valuation profession, like most other professions, has experienced the effects of competition with periods of fee cutting, in some instances to uneconomic levels, as perceived competition has created a scramble for "market share" of available business.

This fiercely competitive business environment is also obvious among other property professionals as the large expansion of numbers of sales people in the real estate

industry since staffing ratio limits were changed and recent proliferation of mortgage brokers throughout New Zealand has created immense competition for available business in the real estate industry.

What valuers must continue to appreciate is that they are, in most transactions, the only professional who does not have a vested interest in the outcome of the business - an agent is not paid any commission by the vendors until the property is sold, the mortgage broker is not paid any commission by the financial institution until the loan is approved and even a solicitor acting for clients will not be required to provide and charge for services if a transaction is not concluded. The valuer, then, must be seen as the only property professional who is providing an independent opinion which may affect the transaction. And this independent opinion may in fact serve two parties. A valuation assessed for mortgage purposes will advise the proposed lending institution of the suitability of the property as security for lending a particular amount of mortgage funds and it will also advise the proposed purchaser of the relativity of the proposed transaction to current market values. The above-described circumstances may be relevant to either residential, rural or commercial properties, but of particular relevance to commercial properties is another aspect of real estate values where valuer independence is seen as being essential. This is in the assessment of values for assets for company accounting purposes under SSAP 17 and SSAP 28. Values assessed for the various property categories under these standards, to have any validity, must be independently assessed by the valuer. Shareholders or

intending shareholders reading financial accounts or reports of the affairs of the company can then be confident that the valuation figures as shown are fairly represented.

A further field of work in which valuers are almost exclusively involved is for property rental assessments, negotiations, determinations and arbitrations and it is suggested independence is of paramount importance in these assignments.

The Code of Ethics of the New Zealand Institute of Valuers will likely be of further significance through the implementation from 1 April this year of the Consumer Guarantees Act 1993. The Act lays down a set of guarantees or minimum standards which are to apply where services are supplied to consumers. A service is defined under the Act as meaning any right, benefit, privilege or facility granted by a "supplier" pursuant to certain types of contracts, and specifically includes professional services. The Code of Ethics of the New Zealand Institute of Valuers sets various minimum standards for valuation practice and requires under 17A that "a member should observe the highest standards of professional competency expected of a valuer having regard to the nature of the assignment being undertaken". This together with the previously mentioned requirement for integrity and fidelity which it is suggested includes independence, could result in the Code of Ethics being used as the benchmark for application of the Consumer Guarantees Act to the activities of valuers. It is therefore suggested that valuers should steadfastly maintain their independence in completing valuation assessments and so fulfil their obligations in service to their principals.

Trevor J Croot

EDITOR

NEW ZEALAND VALUERS' JOURNAL

Expressions of interest are invited by the NZIV Editorial Board for the appointment as editor of the

New Zealand Valuers' Journal.

Enquiries and expressions of interest should be directed to the Chief Executive Officer, New Zealand Institute of Valuers at PO Box 27-146, Wellington or on telephone (04) 385 8436.

From The President's Pen

This message has been penned immediately following the April council meeting and the subsequent AGM and seminar in Auckland. Council proceedings will be reported on more fully elsewhere, however, I will comment on the major issue dealt with and debated in a forum session of the council entitled "The Way Ahead". The result of discussions was an overwhelming view that the NZ Institute of Valuers vote signalled a positive outlook to change generally and the proposal to widen the profession's base in particular. Our council had earlier been advised that, while the Society of Farm Management would stand back from further negotiations on a merging of interests, the Property Management Institute was extremely positive about further discussions. The NZ Institute of Valuers Council agreed that, in view of the level of support from both valuers and property managers for a "property"

profession, despite the failure of NZIV to achieve the 75% threshold, then further two-way discussions should take place with PMI leadership.

The Council is mindful of the wish of most valuers to retain their identity within a larger professional grouping and any new name proposed to membership in the future is likely to include "valuers", while valuer status and registration in terms of the Valuers Act must also be protected. If acceptable proposals can be developed, these will be put to members as soon as possible but only with your Council's endorsement. That is, if the Council cannot ultimately recommend a new structure for valuers and property managers - in effect a property professional body - then no further action will be taken. It is my understanding that the PMI Council have taken a similar view.

Some members may feel that this has been a painful process but it has provided the Institute's leadership with considerable positive feedback, from employers and end users of valuers' services as well as grassroots membership. Councillors are focusing on the future, and remain committed to ensuring that valuers are fully equipped for the multitude of opportunities that lie ahead - in the next six years and beyond the year 2000.

NZIV 1994 AGM Report

The 1994 Annual General Meeting of the NZIV was held in the Kaikoura Room of the Aotea Centre at Auckland at 4.50 pm on Monday 18 April.

President John Larmer welcomed 85 members of the New Zealand Institute of Valuers and invited guests including the senior Vice-President of the Australian Institute of Valuers and Land Economists, Mr Gary Rothwell. The President extended a vote of thanks to the Auckland Branch Chairman and the Branch for organising and hosting the 55th Annual General Meeting and seminar. Apologies were received and sustained from seven members. The General Secretary declared proxy votes for seven members.

The previously circulated minutes of the previous Annual General Meeting were taken as read and confirmed as being a true and correct record of that meeting. There were no matters arising from the minutes.

The 1993 Annual Report and Statement of Accounts, having been previously circulated were taken as read.

President John Larmer reported that his visits to the branches had been a feature of 1993 and he had enjoyed the opportunity to discuss the merger issue with members. He advised that Council had resolved at their meeting over the weekend to proceed with ongoing discussions with the Plant

and Machinery Institute with a view to focusing on a Valuers/Property Management perspective. The President reported that ongoing liaison had been held with other professions and with the Minister in charge of Valuation New Zealand. He referred to the 1993 Annual Accounts and explained that although a modest loss had been incurred on a "cash" basis the out-turn of the financial year was very close to budget. John Larmer acknowledged the contribution of the NZIV staff and particularly the input of Vice-President Bill Clegghorn on education matters and of the Education Development Officer, Kathrine Fraser.

The Annual Report and Accounts were opened for discussion and Mr J W Charters asked how the outcome of the merger vote could be viewed as positive. The President explained that of those who had voted, the majority voted in favour, although not to the required threshold of 75%.

Mr S L Speedy asked what name would be proposed for any new merged body and suggested that a "straw" vote should be taken at the meeting as an indication for support for the inclusion of the word "valuers". By a show of hands there was an overwhelming preference for retention of the word "valuers".

Mr P J Mahoney raised the matter of the

"silent majority" who had not voted on the merger issue and asked whether this indicated an inactive and indifferent membership? The President replied that this was of concern to Council and that they would be addressing this issue. The Annual Report and Statement of Accounts were then adopted by the meeting.

The meeting agreed to the appointment of Price Waterhouse as the NZIV auditors for 1994.

The President advised that the Notice of Motion before the meeting to amend Rule 49 of the Rules of the New Zealand Institute of Valuers had Council endorsement and the rule change was passed by the meeting.

In General Business President John Larmer announced that Council had conferred Fellow membership status upon:

Bill Burgess	-	Northland
Alistair Nicholls	-	Northland
Robin Bell	-	Auckland
Kerry Coleman	-	Auckland
Brett Smithies	-	Auckland
Brian Hilson	-	Waikato
Gray Townshend	-	Waikato
Earl Gordon	-	Wellington
Peter O'Brien	-	Wellington
Cedric Croft	-	Canterbury/ Westland
Gary Sellars	-	Canterbury/ Westland
Gordon Jones	-	Otago

Members present acknowledged these elevations with acclamation.

The President announced that the winner of the Young Professional Valuer of the Year Award was Marcus Jackson of the Otago Branch. A citation for the Award

was read and Marcus Jackson was presented with the framed certificate. Members acknowledged the conferring of the Award with acclamation.

New branch councillors Steve Baker for Northland, Max Plested for Hawkes Bay

and Chris Orchard for Nelson/ Marlborough were introduced to the meeting by the President, who also advised that John Dunckley had been re-elected as branch councillor for the Otago Branch. The meeting closed at 5.15 pm.

Councillors and invited guests at the April Council meeting 1994.

(standing) (rear)

Alan Stewart (*Canterbury Westland*), Bill Burgess (*Chairman Editorial Board NZVJ*), Roger Stone (*Chairman Services Committee*), John Dunckley (*Otago*), Ross Calderwood (*Valuer General's nominee*), Ted Fitzgerald (*South Canterbury*), John Wall (*Chairman, Professional Practices Committee*), Wade Briscoe (*Southland*), Earl Gordon (*Executive*).

(standing) (middle)

Allan Ford (*Waikato*), Bill Smith (*Wellington*), Chris Orchard (*Nelson Marlborough*), Trevor Croot (*Editor NZVJ*), Bob Hargreaves (*Central Districts*), Gordon Kelso (*Gisborne*), Max Plested (*Hawkes Bay*), Steve Baker (*Northland*).

(seated)

Kathrine Fraser (*Education Development Officer*), Alex Laing (*Immediate Past President*), Garry Rothwell (*Vice President AIVLE*), Bill Cleghorn (*Rotorua Bay-of-Plenty, Vice President*), John Larmer (*Taranaki, President*), Iain Gribble (*Auckland, Vice President*), John Gibson (*Chief Executive Officer*), Brian Kellett (*President IPMV*), Tricia Cameron (*Council Secretary and Personal Assistant to Chief Executive Officer*).

Young Professional Valuer of the Year Award

Presidential Citation

It gives me great pleasure to announce that the inaugural Young Professional Valuer of the Year Award has been conferred on Marcus Jackson.

Marcus is 30 years old and is an intermediate member of the New Zealand Institute of Valuers. He has served as Secretary of his present branch, Otago, and has taken an active part in its affairs. He has valuation experience within both the private and public sector.

Marcus' qualifications include a Bachelor of Science and Bachelor of Property Administration from Auckland University and he is currently studying towards a Bachelor of Commerce in Finance at Otago University.

Marcus has contributed significantly to

the Valuation Profession with published research and writings in the NZ Valuers' Journal March 1991, the Canadian Appraiser 1992, the Appraisal Journal 1994 and NZ Property 1992.

The Award Committee considers that Marcus Jackson brings to the Valuation Profession an outstanding level of technical and professional excellence as indicated by his published works and skill levels in applying both new and traditional methods of valuation to all classes of urban and peri-urban property.

Marcus Jackson is considered by the Award Committee to possess the aptitude, skills, work ethic and maturity to become a leading personality in the Valuation and Property Profession.

I have much pleasure in bestowing on Marcus Jackson the Young Professional Valuer of the Year Award for 1993.

J P Larmer President

MARCUS JACKSON

Fellowship Citations

William Andrew Frazer Burgess

Bill was born on 4 December 1946 and raised in Gore. He became a rural field cadet and worked in North Canterbury and Gisborne before completing three years at Lincoln between 1967-1969. Bill completed his Diploma in Valuation & Farm Management in November 1969, became a member of the Institute in 1970, and was registered in January 1972.

Originally bonded to the Government for

five years, he valued for 10 years in Whangarei and two in Te Kuiti before his final Government transfer back to Whangarei as District Valuer. A short time later he commenced private practice with Coutts Milburn, the firm he now owns.

Since moving into private practice Bill has mainly been involved in the rural and residential valuation fields. His knowledge of rural valuation work is wide-ranging and Bill is held in high re-

gard as an expert witness, appearing before the Maori Land Court, High Court and Northland Land Valuation Tribunal.

Bill is married to Amy, and has three children. His current interests include Rotary, golf, bowls and rugby. He is a Life Member of the Whangarei Old Boys Rugby Club.

Bill has contributed to the local branch of the institute over a long period of time, both as a committee member and for 10 years as Northland councillor.

Bill is held in high public regard, as well as by his contemporaries.

Alistair Charles Nicholls

Alistair was born on 19 July 1945 in Helensville, and was brought upon the family farm at South Head. He received his primary education at Waioneke School, South Head and secondary education as a boarder at Mount Albert Grammar, Auckland.

After completing five years secondary education Alistair received a rural field cadetship with the State Advances Corporation and completed a Diploma in Agriculture (with distinction) in his first year at Lincoln College, before completing the Diploma in Valuation and Farm Management. He graduated from Lincoln in 1967 and commenced work with the State Advances Corporation in Whangarei in 1986.

Registration as a valuer was achieved in December 1970, with Associate status being granted by the NZIV in July 1971. Alistair continued to work with the State Advances Corporation and Rural Bank until the end of 1974. In 1975 he practised as a public valuer and farm consultant on his own behalf

before joining JD Robison & Associates, as a partner. Since that time, Alistair has been primarily occupied with rural valuation and consultancy work involving a wide range of assignments covering Northland, in particular the area between Kaiwaka and Kaikohe. In his 19 years of private practice as a rural valuer and farm consultant, Alistair has built up an enviable reputation as being one of the

leading rural valuers in the Northland district. His knowledge of rural valuation is wide-ranging and he is held in high regard as an expert witness, appearing before the Maori Land Court, High Court and the Land Valuation Tribunal.

Alistair is married to Beverley, and has two children. His interests include a wide range of sporting activities, especially golf, and he is currently a committee member of the Whangarei Golf Club. He is also Northland Councillor for the NZ Golf Association.

Alistair has contributed to the local branch of the Institute over a long period of time, both as a committee member and for the last two years as Chairman. Alistair is also involved with the local branch of the Farm Management Society.

Alistair is held in high public regard, as well as by his peers.

Robin Allen Bell

Robin was born in 1940, and after being educated at Mt Albert Grammar School left for his overseas experience, including a time in the merchant navy, before taking up a position in 1965 as estates manager, Engineering Industry Training Board in London which he held until October 1971.

During this time he sat the University of Reading's correspondence course in Estate Management, and in 1970 completed the course and passed the professional examinations of the Royal Institution of Chartered Surveyors. In 1971 Robin was admitted as an

Associate of the Institution in the General Practice Division, Valuation and Estate Management (ARICS). He also attended the Northern Polytechnic, London during 1967-70 and was awarded the Diploma in General Surveying (Dip.Surv.) in the valuation option.

His professional employment from October 1971 to January 1972 was as a Management Surveyor with Kemp & Hawley, London; until August 1973 as the development executive, Chesterfield Properties Ltd, London, and to March 1974 as a development surveyor with John D Wood &

Co London.

He returned to New Zealand in April 1974 and joined Broadlands Dominion Group Ltd in Auckland as property development manager; was promoted to manager commercial & industrial division, and then property services manager. During this time he attended the University of Auckland (1975-77), was awarded the Valuers Registration Board Prize for distinction and received his Diploma in Urban Valuation (Dip.Urb.Val.) in 1978. Having completed the required NZ professional examinations to supplement his qualification as a Chartered Surveyor, Robin was admitted to the NZIV as an Intermediate member in 1978; obtained Registration in

1981 and was advanced to Associate status in 1982. He was also admitted as a member of the Royal Society of Health (MRSH) in 1976.

Robin was a co-founder of the Property Management Institute (Inc) in 1977, being admitted as an Associate (MPMI) on incorporation of the institute in 1978; a member of the Auckland Branch Committee 1977-82; editor of the PMI Journal 1979; Branch Chairman 1982, and National Councillor 1977-81. He was also a foundation member of the Building Owners and Managers' Association of New Zealand, Auckland Branch executive member from 1975-79, and Auckland Vice-President in 1979.

His services to the valuation profession in New Zealand took shape in February 1979 with a full-time lectureship and then senior

lectureship at the University of Auckland, primarily responsible for teaching the valuation course, and property management until December 1985. He then commenced a private property consulting firm, Procram Services Ltd., which continues to the present. He has had associations with Darroch & Co as a consultant and research director, and editor of Darroch Aspect 1986-87. He was a consultant to Richard Ellis Ltd and a director of Richard Ellis Agency 1989-90. He returned to a 50% senior lecturer's position at the University of Auckland in 1988 and in 1990 became full-time, teaching both valuation and property management.

He wrote the NZIVs textbook Investment Property - Income Analysis and Appraisal, published in 1988, and has been commis-

sioned to rewrite and expand this text as Investment Property Appraisal, due to be published by the NZIV later in 1994. He has also had research and technical papers published by CASLE, in the Property Management journal and taught in the NZIV Distance Teaching Programme. He was advanced to a Fellow of the Royal Institution of Chartered Surveyors (FRICS) in 1984, and as a Fellow of the Property Management Institute (FPMI) in 1985.

Robin Bell has made a major contribution to the valuing profession in New Zealand primarily through his endeavours in the education of valuers and as a professional valuer, property manager and consultant.

The Auckland Branch unanimously recommends him for advancement as a Fellow of the NZ Institute of Valuers.

Kerry Coleman

Kerry was brought up in Milford (North Shore) and attended St Josephs Primary School, Takapuna. Secondary schooling was at Sacred Heart College where he was head prefect in 1966.

His work experience commenced with the Lands & Survey Department in Auckland and from there he moved to New Plymouth and Wellington while studying, through Massey by correspondence, for his rural and urban valuation qualifications.

Kerry joined Takapuna Valuation Department in 1975 where he remained until 1980. During the period 1981-83 he worked in

Hong Kong for the government Rating & Valuation Department, involved in both valuation and research.

He returned to New Zealand in 1983, working in property management and valuation for Auckland City Council, Manukau City Council and Aetna Life Insurance. For the past five years he

has been employed with Bayleys Real Estate as manager of their Property Management, Valuation and Research Division.

Over the years Kerry has contributed significantly to the Institute, being Secretary of the Auckland Branch in the late 1970s and more recently served four years on the Branch

Committee. Kerry was Chairman of the branch in 1992.

Kerry is married to Margaret and they have three children. He is keen on several outdoor sports including tramping and touch. Kerry is very supportive of his family assisting them in coaching both cricket and rugby. While in Hong Kong he was a national selector for the rugby union.

Kerry is held in very high esteem by his fellow NZIV members for his valuation and management skills. His input into branch affairs at both secretary and committee level have been appreciated, thus the Branch has no hesitation in recommending him for advancement as a Fellow of the NZ Institute of Valuers.

Edgar Brett Smithies

Brett Smithies is the manager of the Auckland office and afounding director of the nationwide valuation practice of Darroch & Co. Ltd.

He specialises in the valuation of large industrial and commercial complexes and is frequently called upon to act as an arbitrator and expert witness. More recently he has been involved in major asset valuations throughout the country and managed a team of valuers involved in the Crown Health Enterprises valuation.

Born in 1949, Brett was raised in Auckland. He became a student member of the Institute in 1968. His property career commenced with the Lands and Survey Department in

Auckland, followed by two years working in the building industry in Australia. On his return Brett joined the Valuation Department in Auckland where he worked for three years and completed the Institute urban qualification. He left the Department in 1976 to join Neil Darroch & Associates and has continued in that association ever since.

Brett has contributed much to the Institute and is highly regarded by his peers. In early years he was involved in lecturing and practical examinations, whilst more recently he has been involved in organising the Auckland Branch annual golf day, has provided commentary at seminars for the local branch and lectured in a series of asset valuation

seminars on topics including the valuation of infra-structural assets. In 1993 he chaired the working party commissioned to rewrite the insurance certificate.

He is currently a member of the organising committee for the 1994 AGM and responsible for the programme. During 1993 he was involved in the Standards Seminar.

Brett is married to Christine and has two children. He is a competitive sportsman in golf and marathon running.

Brett maintains a very high professional standard with his advice and expertise being sought by many high-profile clients. His input into Institute affairs has been considerable and the Auckland Branch has no hesitation in recommending him for advancement as a Fellow of the NZ Institute of Valuers.

Brian John Hilson

Brian Hilson was born in London in 1939. His professional career as a Valuer started with Basildon New Town Development Corporation including valuing, management and feasibility studies of commercial and industrial properties as well as extensions to the Town Centre. Before coming to New Zealand

in 1975, Brian spent six years in a central London practice covering a wide range of commercial property in both the UK and on the continent. He emigrated to New Zealand with his wife and three children, settling in Hamilton and worked as a valuer with the Housing Corporation from 1975 to 1978. At this time Brian gained his urban qualification through the NZIV, and New Zealand Registration.

From 1978 Brian has practised as a public valuer in Hamilton, establishing the sole prac-

tice of Brian Hilson & Associates in 1984. Brian is now director of Robertson Young Telfer (Northern) Limited following the merger of the practices in April 1989.

Since passing the urban qualification exams with NZIV Brian has been an active member of the Institute, assisting as an ex-

aminer in the practical and oral exams at that time, and later becoming involved with the local branch committee. Brian's involvement with the branch committee has covered a period of 10 years and he has been a past Chairman of the Waikato Branch.

Since stepping aside from the local branch committee he has become involved at a National level, currently serving on the National Standards Committee of NZIV. On this committee Brian has drafted the residen-

tial standards and assisted with the other standards prepared.

Outside of the valuing profession Brian is very involved with Rotary, having held all positions of office within his Te Rapa Club. Brian enjoys most sports and was a keen cross country runner and cricketer. He still has a keen affection for the London Club, Tottenham Hotspurs.

In England Brian was recognised by his profession as a Fellow of Incorporated Society of Valuers and Auctioneers as well as a Professional Associate of Royal Institution of Chartered Surveyors. He is highly regarded within the professional and business community and is respected for his integrity and broad valuation expertise.

The Waikato Branch fully support Brian's nomination for advancement to the status of Fellow of the New Zealand Institute of Valuers.

Edwin Gray Townshend

Gray Townshend's name is synonymous with the valuation profession in the Hauraki, Ohinemuri, and Thames-Coromandel area

Born in Paeroa and educated at Kings College in Auckland, he returned to the Hauraki Plains where he farmed on his own account until 1973. In 1974 he

passed direct control of his farming interests to his sons and entered the valuation practice of his father, Chas Townshend. He had previously studied accountancy by correspondence through Massey University before switching to valuation and he completed the valuation professional examination (Rural) in 1963.

In 1974 Gray was registered as a valuer, and advanced to Associate in 1975.

His work in the ensuing years saw major involvement in the classification team for the Waihou Valley River Control Scheme where he worked with Les Sole FNZIV. He has, in

addition, been extensively involved in valuation work for the Hauraki District Council, the Waikato Regional Council, and the Thames-Coromandel District Council, and is currently doing special assignments with the Tauranga District Council. The Waihou Valley Scheme has required a continued involve-

ment and Gray has been widely associated with leases throughout the scheme area. Other detailed work of local character has seen him extensively involved for both the major Gold Mining Co's and Waihi in land negotiations and acquisitions.

Gray has consistently supported the Institute at Branch level and at seminars despite the significant distances he has to travel. Recently he has participated in the revision of the replacement insurance form and has acted on the Asset Valuation Standards Committee on river protection works.

His valuation practice has grown over the

years and now functions with two offices under Townshend Cullen Associates. The farming interests remain and a major involvement in local affairs has seen him on the Young Farmers National Executive, the Waikato Presbytery for 5 years, a term on the National Board of general purposes of Masonic Lodge, past-president and member for 25 years of the Ngatea Lions Club, and a member of the local economics initiatives committee and the Businessmen's Association.

It is of interest that a son commences training at Massey University this year to provide a third generation of Townshend's in the valuation profession.

Gray's nomination for the status of Fellowship is, in the opinion of the Waikato-King Country Branch, richly deserved. He has served the community he lives in with distinction and has established both for himself and the profession an enviable reputation. The Waikato-King Country Branch enthusiastically endorses Gray's nomination.

Earl Francis Gordon

Earl Gordon was born in 1946 and commenced his valuation career as a student member of the Institute in 1965, working initially for JH Bethune & Co as an assistant to the legendary Jack Gellatly, later transferring to Gellatly & Robertson, and then in 1966 to the Northern Building Society where he worked in the security department. In 1969 Earl joined the Valuation Department, and over the succeeding years worked in the Wellington and Porirua offices, obtaining registration in early 1971 and Associate status later the same year. He moved to private practice shortly after with Rolle & Co, and then formed Dentice Gordon Kirkcaldie & Co in 1976.

Since 1985 Earl has practised from Wellington on his own account, ably assisted by his wife Adrienne, and has maintained a wide circle of clients including a number of corporate enterprises. He specialises in residential, industrial and city commercial valuations. He has acted as arbitrator, umpire and expert witness on numerous occasions, and his opinions and advice are regularly sought by colleagues.

In spite of the considerable demands of a busy sole practice Earl Gordon accepted an appointment to the Executive Committee of the Institute, of which he is a current mem-

ber, in 1988, and now serves on the Professional Practices Committee having acted as the Institute's nominee to the Management Committee of the Institute of Plant and Machinery Valuers since November 1990. He is also a current member of that Institute's education and examination committee.

Outside his business and professional spheres of activity, Earl Gordon has pursued an active interest in his children's successful participation in cycling, rugby and cricket. He enjoys camping and fishing in his more leisurely moments.

The Wellington Branch is pleased to unanimously support Earl Gordon's advancement to Fellow of the New Zealand Institute of Valuers.

Peter Conor O'Brien

Peter O'Brien is a principal in the Appraisal Group of Companies, registered valuers, real estate agents and property consultants based in Lower Hutt City. He was born in 1951 and completed his schooling in New Plymouth.

He commenced his employment with the former Department of Lands and Survey before being appointed as a land purchase officer in the Ministry of Works and Development in April 1973.

In 1979 he was appointed Assistant District Property Officer, Wellington, being responsible for all assessments of value and negotiations for purchases, rentals and leases of residential, commercial and industrial properties in Wellington. In August 1981 he joined PR Holmes and Associates as a valuer and set upon his own account as PC O'Brien Public

Valuer in October 1984. During the next five years the practice expanded and in 1989 was merged to become a part of the Appraisal Group of Companies. Peter obtained registration as a valuer in July 1978 and was granted Associate Membership in August of the same year. He is also a full member of the Property Management Institute. He has pursued an active role in the institute of Valuers and has served several terms as a Wellington Branch committee member, with two terms as Chairman. He has acted as an examiner on behalf of the institute for the practical and oral examinations for students for the years 1980, 1981 and 1982. He has been a member of the Institute's Entrepreneurial Services Committee and has served on the interviewing panel for all applicants wishing to be

advanced to Associate Member status of the institute. He periodically sits on the Land Valuation Tribunal as an expert valuer.

Peter is highly regarded by members of the profession and the commercial community. Whilst having over the years undertaken all facets of valuation, more latterly he has been involved in the assessment of mainly commercial and industrial property and is often called upon as an arbitrator and umpire in relation to disputes on value. He is regarded as an expert in the assessment of compensation and the acquisition and disposal strategies for portfolio management.

The Wellington Branch is unanimous in its recommendation that Peter Conor O'Brien be elevated to the status of Fellow in recognition of the regard and repute he is held by the commercial community and among members of the valuation profession.

Cedric Spencer Croft

Cedric Croft was born in 1952 and raised in the Loburn area of North Canterbury. He was educated at Christ's College, and graduated from Lincoln University with a B.Agr.Com. in 1974. He gained his initial valuation experience in the Rural Bank in Southland and Whangarei and attained NZIV Associate status in 1981.

Cedric began his teaching career as a lecturer at Lincoln University in 1987, and currently is a senior valuation lecturer under

Professor Terry Boyd in the Property and Finance faculty at Lincoln. He has contributed numerous articles to the NZ Valuers' Journal, including three co-written with Professor John Baen. His contribution at branch level has always been exemplary, including a period on the branch committee, but most

noteworthy has been his willingness to assist with branch educational activities. More recently he has had a big input into the annual two-day valuers seminars held at Lincoln every August.

He was awarded a citation by Lincoln University as the outstanding lecturer in July 1991, which is a measure of the esteem in which he is held by his peers in the education arena.

He has had very considerable input in a supervisory role over thesis work undertaken by valuation Masters students. His expertise in a wide range of essentially rural valuation matters is widely acknowledged, with two areas in particular where he has focused assessment of lessees' interest and partial interests, and the area of resource consents. More recently, he has also taught most of the

papers involved in urban valuation. In his leisure time Cedric devotes his energies to running rural land in the Lincoln district and for many years now has held his

pilot's licence. He still pursues that interest and is currently Vice-President of the local Aero Club.

Cedric is widely respected amongst the valu-

ation fraternity, with his wise counsel sought on a wide range of valuation issues. His nomination for Fellowship has the full and unanimous support of the Canterbury/Westland branch committee of the NZIV.

Gary Russell Sellars

Gary Sellars practices in Christchurch as a valuer with the valuation and property consultancy firm of Fright Aubrey. He has been with the firm since 1985 and a partner since 1986.

He was born in Christchurch in August 1954 and educated at Riccarton High School. At age 17 he joined the Valuation De-

partment in Christchurch, initially as a clerical cadet before being appointed to the valuation staff two years later in 1974. Gary gained the NZIV professional (urban) qualification in 1977 and was registered and became an Associate of the Institute in that same year.

In 1981 Gary resigned from the Valuation Department and took up a post with the Hong Kong government as a valuer for four years,

before returning to Christchurch and commencing in private practice with Fright Aubrey.

Gary is very competent, well respected and highly regarded as a valuer in the Canterbury area and the wider South Island region. Over more recent years he has focused predominantly on the commercial, industrial

and investment property sectors and has considerable experience in the arbitration and litigation arenas.

Gary has always been a strong and regular supporter of the Institute and its activities. For the past six years has been a member of the Canterbury/Westland Branch Committee; the last two as Chairman, performed with considerable distinction. For the past two years he has also been a member of the South

Island executive of the Building Owners and Managers Association (BOMA). He made a valuable contribution as a subcommittee chairman for the Organising Committee of the Fourteenth Pan Pacific congress held in Christchurch in 1988.

Gary is a prominent sportsman having played senior club rugby in Christchurch and Hong Kong. Since his rugby playing days he has coached and managed rugby teams and he is currently president of the Albion Rugby Club in Christchurch. Over the past three years he has also been an active triathlete.

Gary is married to Alison and they have two sons.

The Canterbury/Westland Branch Committee unanimously supports this recommendation for advancement to Fellowship status within the Institute.

Gordon Jones

Gordon Jones is the principal of Gordon Jones Associates, registered valuers in Dunedin, having commenced as a sole practitioner in 1983 and now employing one registered valuer.

Gordon was born in Oamaru, North Otago on 3 April 1950. He was educated at Waitaki Boys High School, then spent one year

with his father's real estate firm in Oamaru and in 1969 moved to Dunedin to take up a cadetship in valuation under John Macpherson at JO Macpherson, registered valuers. Gordon studied through the NZ Technical Correspondence Institute and completed the NZIV Profession (Urban) examinations in 1972. He gained registration as a valuer and Associate status of the NZIV in 1973 and in that same year left Dunedin and New Zealand for overseas experience, travelling

to London. He worked as a surveyor (valuer) for Gerald Eaves, a leading firm of surveyors in London City, gaining experience in a wide range of commercial valuations. After about nine months he was employed by Hawes & Co a firm of residential surveyors at Wimbledon for a further period of

about six months. Gordon returned to Dunedin in 1977 after extensive travelling in various parts of the world, rejoining his old firm, which had become Macpherson & Associates, for the six years until he commenced his own practice.

Gordon Jones has been a member of the Otago Branch NZIV continuously for more than ten years and has been the Branch Newsletter editor for more than 15 years. He has a particular interest and expertise in motel valu-

ations and motel rental assessments and has contributed an article on the topic to the New Zealand Valuers' Journal.

Gordon is married to Vivienne and they have three children who are or have attended the George Street School where Gordon has been a member of the Parents Teachers Association. He is a member of North Dunedin Rotary and his leisure activities revolve around outdoor pursuits, particularly tramping, skiing, mountain biking and kayaking. Gordon Jones has contributed significantly to the affairs of the Otago Branch NZIV over a long period particularly in his capacity as newsletter editor and committee member. He is highly regarded as a valuer in Dunedin and Otago both by his clients and his fellow practitioners. The Otago Branch Committee unanimously recommends his elevation to the status of Fellow of the New Zealand Institute of Valuers.

People Profiles

Iain Gribble

there's the committee working to obtain the Pan Pacific Conference for Auckland in the year 2000, of which he is also a member. Iain describes himself as a "general practitioner". A valuer who tackles anything of an urban nature, and puts that down to his many years working with the Valuation Department. He has since drawn on his broad Government experience and not specialised, handling most types of urban work.

Iain holds a Diploma in Urban Valuation from the University of Auckland. In 1967 he became an urban field cadet with the Valuation Department, and continued to work for the Government until 1987, moving around New Zealand and rising through the ranks to become Chief Valuer in Wellington, before moving into private practice, back in Auckland.

"It was time for a change, and time to get back to valuing more hands-on", he said. He joined the Auckland office of Robertson Young Telfer (Northern) Limited, a national valuation practice. In 1989 he became a

principal of the company.

Iain is concerned that some valuers are currently underselling themselves and their services, and consequently setting their fees at a level not commensurate with their worth. "They do not realise that they are putting their livelihood at risk with each valuation completed. They must put the appropriate time and effort into the job and charge accordingly - A fair recompense for their efforts and expertise."

"Registered valuers put their registration on the line every time they complete a valuation. However, with the economy picking up there will be more work for members and hopefully it will reverse this trend."

Iain is married to Heather and they have five children, four boys aged 15-21, and one girl, five years old and who is "spoilt rotten". Iain has been involved with the boys' sports, coaching cricket and soccer and doing other parental duties at school and clubs, but is now devoting most of his spare energy to the NZIV, - not ballet.

As Auckland is the largest branch with about 450 members, being NZIV Branch Councillor involves Iain Gribble in a lot of work, just ask his wife!

In addition, he is the NZIV Junior Vice-President and sits on about eight national or branch committees or subcommittees. These include the National Executive, Professional Practices and Standards Committees, the Committee reviewing the insurance certificate, as well as that organising the 1994 AGM and Conference in Auckland. Then

John Dunckley

ferent from valuation. I saw the effect cash flow has on property, and at that time in the early 1980s, farming was very difficult", he says. "It was a total change from Valuation New Zealand, where they never asked to see a cash flow, consequently they only saw half of the property", Mr Dunckley says.

He moved to another private firm where he specialised in motels and hotels, which are purely cash flow driven; then four years as a director of the South Island company Simes Valuation and as a shareholder of Darroch & Co Ltd. He is one of five valuers in the Dunedin office.

He has moved from farming to commercial property, and on to major portfolios. Developing valuation portfolio methods for clients such as the Ministry of Agriculture and Fisheries.

"The Government sector property philosophy had been different to commercial property. But values now must ultimately be based on cash flow or some other measure, given the current economic reforms. Even

more so if they are specialist in nature," he says.

For one year he worked closely with Coopers and Lybrand developing a methodology and value process for the Crown Research Institutes. "It was interesting, and we also developed a methodology to value the tertiary institutes. It has developed to where 90 percent of my work is sourced in the North Island," he says.

It's the changing nature of the work he likes, the variety and the practical aspects. "Developing ideas can only come from doing it." John is married to Ellen and they have four children ranging in age from 19 to 8. One attends university, two high school and one is at primary school. The oldest and youngest are girls. He and his wife are developing a 10-acre block with the ultimate aim of subdivision. In the meantime they graze some livestock there.

He likes to keep fit, enjoys a run at lunch-times, and has competed in some veteran events.

An interest in the practical side of farming took John Dunckley, NZIV councillor for Otago, to Lincoln College to undertake a Bachelor of Commerce Degree, majoring in Valuation and Farm Management. He freely admits he had never heard of valuation before attending Lincoln College. However, when he left Lincoln College he joined Valuation New Zealand and spent six months in Christchurch, before being transferred to his home town of Dunedin, where he has remained since.

He later joined Reid Farmers as a farm financial controller. "It was challenging, very dif-

April 1994 Council Meeting.

Report By The Editor

The April 1994 meeting of the Council of the NZIV was held at Rose Park Hotel, Parnell, Auckland on Saturday 16 and Sunday 17 commencing at 8.30 am. President John Larmer welcomed all councillors including new councillors Steve Baker Northland, Max Plested Hawkes Bay and Chris Orchard Nelson/Marlborough. He also welcomed invited guests including Garry Rothwell the President-Elect of the Australian Institute of Valuers and Land Economists, Brian Kellett the President of the Institute of Plant and Machinery Valuers, and members of Executive. An apology for lateness was received from Gordon Kelso, Councillor for Gisborne who was delayed by airline schedules.

The minutes of the previous Council meeting were approved as a true and correct record of that meeting. From matters arising Council agreed that reciprocity discussions should be pursued with the Institutes of Surveyors of Hong Kong, of Singapore and of Malaysia at the 17th Pan Pacific Congress in Japan.

Chief Executive John Gibson advised Council that present membership of the NZIV is 2150 and of those 1006 hold Annual Practising Certificates. President John Larmer reported the result of the member referendum for the merger proposal with the NZ Society of Farm Management and the Property Management Institute was that insufficient votes were recorded in favour of the merger for it to proceed. The President advised that the Council business plan objective to broaden the base of membership of the NZIV is likely to be frustrated by the Valuers Act 1948 and this view has been reinforced by an opinion received from the Institute lawyers Kensington Swan.

Vice-President Bill Cleghorn presented a report received from Mr Ian McLean on legislation which provides for the Valuer-General as nominated valuer. His report advised that the NZIV should take a cautious approach to promoting any changes to legislation and that representations for wider registered valuer recognition should be left until particular Acts arise for review and in consultation with the Valuer-General. Council received the McLean report and agreed that the President arrange to meet with the Valuer-General to discuss the contents of the report and the inclusion of registered valuers together with the Valuer-General as nominated valuer in any future legislation or review of existing legislation.

Committee Reports

Executive Committee

President John Larmer advised that the committee has arranged for the review of the upgrading of the NZIV computer system. He reported that considerable time has been spent by executive in organising a bid for the Pan Pacific Congress to be held in Auckland. Discussions had been held with the Minister for Valuation, Mr Marshall, to inform him of current issues involving the NZIV, particularly the proposed merger with NZSFM and PMI. Chairman of the special committee for review of the NZIV insurance certificate, Ian Gribble, reported that the new insurance report form is now being finalised although some further discussions are being held with the Insurance Council of New Zealand regarding the definition terminology to be used.

Professional Practices Committee
Chairman John Wall reported that a large number of complaints against members are continuing to be received and expressed particular concern that the Valuers Registration Board has advised there is no time limit in which complaints may be received. The Valuers Registration Board has also advised that their jurisdiction relates only to registered valuers undertaking valuations of land and buildings. These matters are to be further discussed between Council and the Valuers Registration Board.

Marketing Committee

Chairman Alan Stewart reported that Mr Ron Garland from the Marketing Faculty at Massey University has been retained as the marketing co-ordinator for the management of the NZIV marketing research programme. He advised that MRL has been retained to undertake the marketing research, with a report to be completed by July 1994 at a cost of \$25,000 within the Marketing Committee's current budget. An additional \$5,000 is to be spent on a marketing survey within NZIV membership and is also part of the present budget. Mr Stewart advised that Consultus are no longer retained as public relations consultants but confirmed other consultants advice will be sought from time to time as required.

Council conferred Fellow membership of the New Zealand Institute of Valuers on:
William Andrew Frazer Burgess Northland
Alistair Charles Nicholls Northland

Robin Allen Bell	Auckland
Kerry Coleman	Auckland
Edgar Brett Smithies	Auckland
Brian Hilson	Waikato
Edwin Gray Townshend	Waikato
Earl Francis Gordon	Wellington
Peter Conor O'Brien	Wellington
Cedric Spencer Croft	Canterbury/ Westland
Gary Russell Sellars	Canterbury/ Westland
Gordon Jones	Otago

Forum Session

Immediate Past President Alex Laing conducted a forum session on future development of the New Zealand Institute of Valuers, into which all Councillors had some input.

Services Committee

Chairman Roger Stone reported that there had been nine new subscribers to the computer sales list but that ten subscribers had been lost from microfiche sales. Sales of space in the Directory of valuers holding Annual Practising Certificates has progressed well. He advised that private sector initiative has already been shown by the valuation profession in developing computer software for sales data.

Council agreed that with the discontinuance of the Services Committee the responsibility for publication of Professional Practice Directory will be taken up by the Marketing Committee, responsibility for the publication of Statscom will be taken over by the Editorial Board and the marketing and distribution of sales data would become the responsibility of the Marketing Committee.

Council agreed that a review of Modal House Costings should be undertaken by a subcommittee comprising Roger Stone, Rod Jefferies, Garry Muir and the NZIV Chief Executive Officer John Gibson.

Reports Of Nominees To External Organisations:

Association of Business-Related Professions

President John Larmer reported that this association is virtually in recess through lack of interest.

Massey University Foundation

Vice-President Bill Cleghorn reported that funds have been provided by the Foundation for the professorial chair research projects and staff travel grants for overseas study. He advised of the sudden death of Mr Graeme Bringans, the Chairman and that Mr Neil Darroch has very recently been appointed as Chairman.

Real Estate Valuation and Property Management Education Foundation
President John Larmer reported that the responsibilities of the Foundation had now been fulfilled.

Land Professionals Mutual Society
Mr Earl Gordon presented the report in the absence of Mr A L Macalister, the NZIV nominee to LPMS. The report noted that there has been a gain in membership from 249 firms to 270 firms and a gain in valuer members from 127 to 131. There has been a significant fall-off in claims or alerts received by the LPMS during the last year.

Institute of Plant and Machinery Valuers
Mr Earl Gordon, the NZIV nominee to the IPMV reported that there has been a small increase in the membership of this Institute. The Annual General Meeting and Conference was held in Christchurch in March. It was well attended in terms of total Institute membership and was a successful event. The IPMV is in a sound financial position and he was pleased to advise that no complaints against Plant and Machinery Valuers had been received by the Management Committee of IPMV. President of the IPMV Mr Brian Kellett reported that continuing professional development is now mandatory for IPMV members. He advised that Earl Gordon has recently been made an honorary member of the IPMV.

International Affairs

Australian Institute of Valuers and Land Economists
President-Elect of AIVLE Garry Rothwell reported on affairs of the Institute with particular reference to the effect on residential valuation work of deregulation of the financial sector in Australia. There has been a significant increase in the requirement for drive-by assessments for residential properties. The Australian experience with these types of valuation is quite different to the New Zealand experience in that in Australia those assessments are regarded as carrying the same liability to the valuer as a formal valuation and report.

Branch Reports

All Councillors reported on the activities in their branches for the year, except for Gordon Kelso who was absent, and all advised that activity and participation levels from members was generally good and that branches were mostly in a reasonable financial position.

Financial

Chief Executive Officer John Gibson reported on the continuing stability of the financial position of the New Zealand Institute of Valuers.

NZIV Committee Appointments Iain Gribble was appointed Chairman of the Standards Committee following the retirement of Graeme Horsley.

Professor Bob Hargreaves was appointed Chairman of the Editorial Board following the retirement of Bill Burgess.

Mr Evan Gamby was confirmed as the NZIV nominee to the Valuers Registration Board.

General Business

Council debated at length the future direction of the New Zealand Institute of Valuers following the result of the membership referendum on a proposed merger with the NZSFM and the PMI. After full discussion Council agreed that the President and Vice-President of NZIV should enter into negotiations with the PMI to establish a basis for the formation of a new parent organisation focused on a wide-base property professional membership and that the NZSFM should be invited to attend appropriate meetings with observer status. Council agreed that the name "valuers" should be included in the name of any new parent organisation and that the requirements of the Valuers Act 1948 would have to be met by any new parent organisation. A model structure for a new parent organisation is to be submitted to the October 1994 Council meeting for consideration and respective membership approval to form any new parent organisation will be sought by 31 March 1995.

Editorial Board

Chairman (retired) Bill Burgess reported that the changes desired by Council for a more modern format and more human-interest articles in the New Zealand Valuers' Journal had been implemented in the March 1994 issue. A new production editor, Anna Hudson, of Visual Impact had been appointed and a new contract arranged with a printer in Wellington. President John Larmer thanked Bill Burgess for his contribution to the New Zealand Valuers' Journal through his long term as Chairman of the Editorial Board and welcomed Professor Bob Hargreaves, Councillor for Central Districts Branch, to his appointment as Chairman of the Editorial Board.

Trevor Croot, editor of the New Zealand Valuers' Journal, reported that very satisfactory service is being received from the new production editor, Anna Hudson and the new printers in Wellington. Format changes to the Journal have been implemented with satisfactory results although photograph reproduction quality needs to be improved. This is being addressed. Trevor Croot advised that a satisfactory flow of material for publication is being received with most articles being derived

from the university-based seminars. He expressed some concern that papers or potential papers for publication from local branch seminars are not being made available to the editor, and requested that councillors should take an active role in obtaining copies of papers for possible publication.

Trevor Croot notified Council of his resignation as editor of the new Zealand Valuers' Journal to be effective not later than the end of this year.

President John Larmer thanked him for his contribution as editor of the journal.

Education Board

Chairman Bill Cleghorn reported that three sessions for Distance Teaching Seminars will be held this year. Details are being finalised for the lecture tour by Dr Crosbie in spring. Financial aspects of the valuation Hui held at Albany toward the end of last year are being analysed and a small profit is expected. Bill Cleghorn advised that sales of text books continue to be satisfactory and that education module development is being continued. Another volume of Valuers Registration Board decisions is being published in the near future. He reported that the Education Board has determined that achieving Continuing Professional Development as mandatory by 1 January 1995 will not be possible and that the date for achievement should now be extended to 1 January 1996. Education Development Officer, Kathrine Fraser reported to Council and suggested that the success of CPD implementation will lie heavily with branches.

Standards Committee

Chairman (retired) Graeme Horsley reported that he has recently returned from a meeting of TIAVSC held in Scottsdale, Arizona, USA from 21 - 25 March, which was attended by representatives from 26 countries and chaired by Lincoln North of Canada.

The major matters discussed were the relocation of the TIAVSC Secretariat from the RICS in London to the personal secretary of Lincoln North in Canada, and in future the Secretariat will move with the Chair; Mr Horsley has been involved in a revision of the Constitution to TIAVSC and Standards 1, 2, 3 and 5 have been signed off. AVS has been updated to AVS 4 and the original AVS 4 has been put on hold and is to be reviewed by a subcommittee made up of Australian and New Zealand representatives. Several new standards have been proposed and are to be drafted over the next twelve months including - Going Concern Valuations; Plantation Valuations; Treatment of Plant & Machinery; Depreciation Bases.

Graeme Horsley reported that the rewrite of NZIV Valuation Standards is proposed to be published in an A5 ring-binder format, and included will be the NZIV Rules, Code of Ethics, Asset Valuation Standards, Background Papers on:

- (a) The Asset Valuer
- (b) The Valuers Relationship with the Auditor
- (c) The Valuers Relationship with the Client
- (d) The Valuers Relationship with other Experts
- (e) The valuation of Public Sector Assets
- (f) Depreciated Replacement Cost - Public Sector

Practice Valuation Standards including:

- (a) The Valuation of Residential Properties
- (b) The Valuation of Residential Properties for Mortgage Purposes
- (c) The Valuation of Rural Properties
- (d) The Valuation of Suburban Commercial Property, and Information Papers

He advised that the committee is seeking

to have research papers written on Discounted Cash Flow, Contaminated Land and Standard Terms of Engagement which will ultimately be published as "Information Papers".

Graeme Horsley further advised that over the last six weeks he has personally conducted seminars on "Market Value" at all branches throughout the country except for Canterbury-Westland at Christchurch and the Wellington and Auckland branches. All seminars have been well attended and very well received by attendees.

President John Larmer thanked Graeme Horsley for the very significant contribution he has made to the NZIV, particularly through his chairmanship of the Standards Committee and for the personal commitment of time he had given which was exemplified in his recent nationwide lecture tour.

Westbrook House Body Corporate 66017

Chief Executive Officer, John Gibson reported that the painting programme for

the building had been undertaken with a very satisfactory result.

Office Bearers 1995:

Councillors to retire by rotation in February 1995 are:

Alan Stewart	Canterbury/ Westland
Gordon Kelso	Gisborne
Chris Orchard	Nelson/ Marlborough

Ted Fitzgerald advised Council that he will be retiring as Councillor for South Canterbury from 1995.

A forum session for discussing the ways in which branches can be assisted to perform was facilitated by Mr Erroll Millar of Wellington and councillors participated fully in the discussions.

Council was visited by a full representation of the Valuers Registration Board under the Chairmanship of the Valuer-General, Hamish McDonald whereupon matters of common interest were discussed.

The Fourth Australasian Real Estate Educators Conference

Auckland 26-28 January 1994

Report by Sandy Bond

The conference began as a New Zealand initiative, and was the result of an identified need to establish a forum to enable property academics and practitioners to publish their research, as well as for the furthering of knowledge in real estate education.

The first conference was hosted by Lincoln University in December 1990, with the second and third conferences being hosted by universities in Adelaide and Sydney.

This was in line with a decision to hold the conference in New Zealand every third year, with the intervening years in Australia,

Hence, this year's conference was hosted by the Department of Property, University of Auckland. Over 100 property educators, researchers and practitioners attended from nine countries including: the United Kingdom, South Africa, Northern Ireland, Korea, Malaysia and Nigeria, to name a few. This diversity of cultural background provided an excellent forum for the exchange of information and ideas.

The theme of the conference was "Meeting the Challenge of a Global Property Market". Sessions covered not only education and training introducing a wide range of innovations in course design and teaching methods, but also a range of issues relating to property development/land

economy; finance/ investment; management; marketing; valuation and research.

The presenters included a broad range of property professionals, from real estate trainers and property academics to industry practitioners, thus attracting papers across a wide spectrum, enabling a whole range of real estate issues to be discussed. The conference was well organised with morning and afternoon sessions split into three parallel sessions. These allowed delegates a choice of sessions to attend and with such a diverse range of property interests represented, was very appropriate. Professor Tom Whipple from Curtin University of Technology, Perth provided the keynote address on "Valuation for Long Term Decisions".

This year's programme had a panel discussion on the future of the Australasian Real Estate Educators' Conference. This open forum provided the opportunity for all delegates to participate in discussion and sharing of ideas on this topical issue. In particular, the ongoing debate over the name of the Association highlighted the two main issues which related to the geographic area to include in the title and whether it be limited to educators. The need to broaden the title from "Australasian" to incorporate the wide geographical spread of delegation was acknowledged, and the possibility of expanding the title from "Educators" to

encompass practitioners as well, was considered. However, the original aim of the conference was readdressed, and due

to the disparity of views on these issues no consensus was reached and the matter was deferred to the Pacific Rim Real Estate Society's inaugural meeting which followed the conference. At this meeting, it was agreed that the AREEC would continue, but under the auspices of the Pacific Rim Real Estate Society's Conference. The 1995 conference venue was selected with Frank Blackwell offering to host it at the Royal Melbourne Institute of Technology. Twelve members of the PRRES were nominated to an interim executive whose main task is to develop the PRRES constitution and to deal with related setting-up issues during 1994 to ensure everything is in place for the second annual meeting in Melbourne in 1995.

The social activities of the conference included an opening cocktail evening, and an evening of hilarious entertainment with the French wine connoisseur at "De Vines" restaurant, Lincoln Vineyard. These functions provided the opportunity not only to mix socially, renew old acquaintances and meet new friends, but also to exchange ideas. All in all, the conference was most enjoyable, and enhanced by the presence of the Whitbread yachts berthed at the city wharfs for viewing, together with the associated festivities.

Marketing - Valuers' Myopia

by A J Brady

The Council of the New Zealand Institute of Valuers at their October meeting agreed to permit the Marketing Committee of the Institute to undertake some research into the perception the market has of valuers, and the place of valuers in that market.

This primarily is to aid practitioners and the Institute in targeting specific areas for future marketing effort.

The objective of this paper is to develop some background from which we as Valuers should view and interpret the research results and to stimulate some thought and discussion away from the traditional view we have of our business and the market within which we operate. In the first instance it is appropriate to define some of these terms.

Many people mistakenly think of marketing as only promotion, or advertising. However, marketing is defined as the process by which individuals and groups obtain what they need and want through creating and exchanging products and value with others. Conversely, advertising is defined as any paid form of non-personal presentation and promotion of ideas, goods or services, by an identified sponsor.

There is thus a significant difference between the two, with marketing identifying what is needed, wanted and demanded, and the product then modelled to meet those needs, wants and demands and the exchange occurs when these criteria are met (Kotler, 1991).

Professional Background

Many of you will be aware of and will have worked in the regulated environment that existed in New Zealand up until the mid-1980s and the restrictions those regulations placed upon members of professional organisations and their activities. The New Zealand Institute of Valuers and its members were no exception and had taken great pains to distance themselves from the marketplace. Consequently, many practitioners had a feeling of anathema towards all forms of promotion and self-advertising. This position was supported by a Scale of Fees and the prohibiting of professions to advertise in any shape or form. These restrictions created effective barriers of entry thus protecting the established professionals from new entrants' competitive edge, namely marketing and price.

The passing of the 1986 Commerce Act saw the abolition of these constraints upon

the professions and has resulted in a wide variance in the quality and usefulness of advertising/marketing, together with the level of fees charged. In most circumstances it has seen a reduction in the gross income of many professional practices.

The regulated environment had therefore developed protected professions and in the valuers' case, we determined what the client would get, when he/she would get it and for how much. The free market ethic had no place in the thought processes of the practising valuer and relatively speaking, competition was minimal.

The public perception of professions has now changed dramatically and as claims for professional malpractice have grown in number, so too has the public attitude that professionals and their actions should be more open to public scrutiny and the same economic forces that influence everyone else. Accordingly, our profession is now driven by the market's perception of valuers and their worth or need in the market and it is important for our survival that we understand and meet those needs.

Business Development

Within the regulated environment, particularly during the 1970s, one of the principal sources of work in the residential sector for valuers was also protected since the availability of mortgage finance was restricted by government regulations limiting the ability of trading banks to advance funds to their housing and commercial sectors. By and large, the greatest source of mortgage finance therefore became available through trust funds administered by solicitors. It was standard practice for administrators of these trust funds to obtain valuation advice to protect their interest in the event something went awry. There was no negotiation on the fee charged or type of valuation report provided, as the administrator of the trust funds accepted that valuers should meet the requirements laid down by the Institute. Deregulation enabled the trading banks to move into the mortgage market and the traditional source of valuation work began to 'dry up'. Banks have now adopted a more competitive approach to the residential mortgage market in particular, and often do not require a valuation report, and if they do, have nominated their own standards and fees. This is evidenced by lists of approved valuers who meet banks' requirements and the tendering or quotation of fees.

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"is is now the customer who determines what is wanted, when, and how much will be paid."

Roles have now been completely reversed; the customer, or client, is now determining what is wanted, whom they will engage, and how much they will pay for valuation services.

Continued complaints of 'fee cutting', and recent focus on standards, continuing professional development and education in general have indicated that valuers have not yet recognised and adapted to the deregulated environment and the subsequent reversal of their role in the property sector. This phenomena is not unique, for as long ago as the mid-1960s, the American railroad companies and even Hollywood experienced like-phenomena.

"The railroads didn't stop growing because the need for passenger and freight transport declined - that grew. Nor are they in trouble today because the need was filled by other modes of transport, but because that need was not filled by the railroads themselves. They allowed others to take customers from them because they assumed themselves to be in the railroad business, rather than the transportation business. The reason they defined their industry wrongly was because they were railroad-oriented. They were product-oriented, instead of customer-oriented. Hollywood barely escaped being totally ravaged by television. Actually, all the established film companies underwent drastic reorganising. Some simply disappeared. All of them got into trouble not because of television's inroads to their market, but due to their own myopia. As with railroads, Hollywood defined its business incorrectly, thinking of itself in the movie business, when it was actually in the entertainment business. 'Movies' implied a specific, limited product. This produced a fatuous contentment which from the beginning led producers to view television as a threat. Hollywood scorned and rejected television when it should have welcomed it as an opportunity - an opportunity to expand their entertainment business.

Today, television is a bigger business than the old narrowly defined movie business ever was. Had Hollywood been customer-oriented (providing entertainment) rather than product-oriented (making movies), would it have gone through the physical purgatory it did? I doubt it. What ultimately saved Hollywood and accounted for its recent resurgence was the new wave of young writers, producers and directors, whose previous success in television had decimated the old movie companies and toppled the big movie moguls" (Levitt, 1960).

It is worth noting this was written in 1960, but it still applies today and in my view has a direct correlation to the position that valuers, particularly those in private practice, are presently finding themselves in. Valuers are product-oriented. We have an obsession about the quality and standards of our education and reporting, to the exclusion of the fundamentals of a modern valuation practice. Education and standards have a place, but because they have such a high profile, valuers are not customer-oriented. It is now the customer who determines what is wanted, when, and how much will be paid.

The continual complaint from valuers of other practitioners cutting fees is an example of their inability to accept these demands of the market. The valuer perceives it as a cut fee; the customer sees it as obtaining a better deal. What's the difference?

During the 1970s and 1980s, the valuation profession experienced considerable growth. One of the assumed strengths of our profession lay in the apparently unchallenged superiority of our product. There appeared to be no effective substitute for it. Levitt refers to the mind-set that this growth cycle can produce:

"If thinking is an intellectual response to a problem, then the absence of a problem leads to the absence of thinking. If the product has an automatically expanding market, then not much thought is given on how to expand it".

With deregulation and increasing litigation following the 1987 crash, the quality of our product has come under a shadow. Quite correctly we have focused on education and standards to improve our product, but we have neglected to ascertain that our product remains relevant.

Valuers today are continually focusing on what they've always done and are attempting to outdo each other by improving on what they are already doing, without considering the other opportunities that may be available for the skills they have. It is my perception that practising valuers and the Institute have continued to focus on the product through continuing professional development and the ratification of our standards to the exclusion of the generic product and marketing. The product has been defined in the narrowest possible term and the deregulated environment has shown that there is never any guarantee against product obsolescence. The deregulated, and recessionary economy has seen less work available for valuers across the full spectrum of commercial, industrial and residential property, and in many localities there has been an increase in the number of valuers establishing themselves in practice, either in small partnerships or in larger groups. The focus of most valuers has been to increase their share of the market, with an accent on the product and production. With that focus and the removal of the restrictions on advertising, many valuers and practices have adopted an advertising campaign, of sorts, and termed it in their own minds, marketing. As noted above, advertising is defined as any paid form of non-personal presentation and promotion of a service by

an identified sponsor. Advertising therefore focuses on the needs of the seller, whereas marketing focuses on the needs of the buyer. Advertising is preoccupied with the seller's need to convert his product into cash, whereas marketing has the focus of satisfying the needs of the customer by means of the product and the cluster of things associated with creating, delivering and finally, consuming it. A truly marketing-minded valuer tries to create value-satisfying services that the client will want to buy. In other words, what the valuer offers is determined by the buyer, not by the seller.

The effectiveness of much of the advertising undertaken by valuers that I am aware of could be seriously questioned, but there is sufficient material on that topic to provide another paper.

Conclusion

Professional practice across a wide range of occupations will require significant changes in attitude and perception to achieve success in the 21st century. There are numerous examples of professional bodies and practitioners struggling to adapt to this new reality. A recent example of solicitors in Invercargill offering free holidays in Australia to clients, and the subsequent Law Society reaction showed the wide range of attitudes current within their profession. The New Zealand Institute of Valuers and its members are no exception, and their needs to be a considerable reappraisal of what business we are in and our attitudes to the customer, competition and our fellow practitioners.

Research being undertaken by your Institute is the first stage in attempting to identify some of the customer needs and wants. And if the research is read from a perspective of outside, looking-in, instead of inside, looking-out, some data may well be of considerable benefit in promoting original thinking and innovative action. This may be the opportunity for many practitioners to reappraise their current position in the market and plan a more focused strategy for the future. For, if you don't know where you're going, any road will take you there.

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Valuations For Mortgage Security And Accounting Information Purposes

by R T M Whipple

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He is a prolific author and has edited a number of significant books on property valuation and has had previous papers published in the New Zealand Valuers' Journal.

What Is Value?

In his classic text on valuation, Bonbright (1937) devotes the first five chapters to probing the meaning of value. He stresses the vital importance of ascertaining, in any given case, the

purpose for which the valuation is sought: "... an intelligent valuation of property is

out of the question, without reference to the purpose for which the valuation is desired ..." (op. cit., p.7). This is because with value', .. the various meanings are closely intertwined and shade into each other with almost imperceptible gradations. Not only are they difficult to distinguish - the choice of that particular meaning which is most appropriate for a given purpose is often highly controversial ... " (op. cit., pp. 37-38).

As part of his wide ranging enquiry, he reviews the meanings the US Courts have placed on "market value, or fair market value". He distinguishes the following interpretations:

"First sense: price which the property would actually bring if presently offered for sale, with reasonable time for negotiation." (p. 56).

"Second sense: valuation based on current

market prices of substantially similar commodities." (p. 57).

"Third sense: hypothetical sale price as between a willing buyer and willing seller." (p. 59).

"Fourth sense: cost of

replacement through purchase on the market place." (p. 61).

Fifth sense: 'justified selling price' or

'normal selling price'." (p. 62).

Following his review of these senses, he concludes:

Our own preference, at least in the field of appraisal, is for the previous definition of market value, under which a valuation of property means merely an attempt to estimate the price for which the property could be sold by some stipulated seller to anyone else the conditions of the assumed sale being left for selection by reference to the purpose for which the valuation is being made. So defined, market value will not qualify as a basis of legal appraisal save in a rather limited number of cases. But no alternative definition of Value will serve as a jack-of-all-trades. The use of 'market value' as the verbal basis for settling all varieties of legal disputes represents a uniformity of mere words

rather than one of principle. The multiformity of value standards is only concealed, not avoided, by the accepted legal definition of market value as the price at which the property would be exchanged between a 'willing buyer' and a 'willing seller'. (op. cit., p. 65).

Faced with the many meanings of the word "value", Bonbright urges the necessity of first understanding the purpose for which the valuation is required before adopting the definition of value which is to guide the work.

Expressed more succinctly: there is no one value for all purposes. Given this, then advocating a standard definition of value cannot be logically sustained.

We can reach this same conclusion by another route and thereby confirm the good sense of it.

Value Definition Follows Problem Analysis

Valuations commence with uncertainty and they end in uncertainty. They commence in uncertainty because a client is undecided as to a course of action or seeks support for a course of action already planned or undertaken.

This realisation places valuation directly in the problem solving area and points to the first step in conducting a valuation - defining the problem.

This paper was presented at Seminars sponsored by Westpac Banking Corporation and conducted by NZIV at Wellington on 7 February and at Christchurch on 10 February 1994.

Problem definition leads in turn to:

- (a) defining the property rights which are to be valued,
- (b) formulating the definition of value relevant to the problem and
- (c) identifying the data that problem solution call for.

To make these elements more concrete, a simple example will be presented.

Consider the following questions and scenarios that could equally well refer to the some property a central area office building, say.

(a) Liquidity Problem

"I am contemplating the sale of this property. To overcome a looming liquidity problem I have to sell within three months yet I don't want to give it away. What price am I likely to receive in that time frame and what should my asking price be?"

(b) Prospective Lender

"I am considering a loan advance against the security of this property. Our lending policy is to require a loan-to-value ratio of 0.8 and a debt coverage ratio of 1.2. If we make the loan, is it likely that our desired ratios will be maintained over the next five years, given that loan repayments start at the end of year four? If the loan fails, what would be the likely cash realisation price and what kind of buyer would be interested in the property?"

(c) Prospective Investor

"I am thinking of adding this property to my portfolio. It has been offered to me at \$50,000,000. I want to make sure I am not being 'over charged' for it. Is that the price it is likely to fetch on today's market? If I do buy it, the risk-return characteristic of my portfolio will be thrown out of balance unless, over a ten year holding period, I can achieve a three per cent average real growth in rents and a five per cent per annum real growth in capital value."

(d) Local Government Revenue

"Our Valuation Department is revaluing this part of the city such that the rating base is the assessed annual value of each building."

(e) Resumption Officer

"This building is to be resumed for statutory purposes. What valuation do you fix by way of compensation for the interests involved?"

It is clear that each of these five scenarios presents a different problem, a different definition of value is appropriate to each and each of them calls for different data and work programme.

Most so-called standard definitions of value incorporate assumptions such as the parties being willing but not anxious, neither acting under duress, both being fully informed, the property being freely exposed to the market, a bid by a buyer with a special interest being ignored and so on.

To apply such a definition to the first case would be inapt: the definition would require data relating to transactions which do not meet the requirements of this situation and the result would be at best inconsistent and, at worst, misleading. This client is not interested in locating a buyer who is not anxious to buy and he would assuredly want to know if there were a party who had a special interest in buying. The current selling price of the building is certainly relevant to the intending mortgagee but this is market value in a qualified sense. A mortgagee in possession usually wants to liquidate a property quickly and at a net figure which leads to a complete recovery of the loan money outstanding. The law requires that the lender recover the maximum possible net cash on behalf of the mortgagor. Regardless of standard definitions of value, the result is often a mortgagee's sale in which the time exposed to the market is a few weeks. Standard definitions of value view the parties as being in an equal negotiating position with market supply and demand in equilibrium. A building in possession of the mortgagee is usually regarded by buyers as having a rather highly motivated vendor when it reaches the market. Other facets of the lender's problem require for their solution an estimate of likely net operating income, debt service and selling prices over the stipulated period, a comparison of this with the loan balance outstanding, various solvency measures and an identification of the most probable type of buyer on repossession (if that takes place).

The prospective investor calls for a different set of questions to be answered. He would want to know the property's probable selling price and the identity of likely competitors. More particularly, however, he needs to know the figure which it is sensible for him to pay having regard to his particular requirements - not the requirements of some average imaginary buyer. This latter component is not addressed at all by standard definitions. The local area rating officer will need a value estimate prepared in compliance with the definition of value set forth in the relevant legislation and as elaborated upon

by the Courts. It is likely that restrictions on title and restrictive lease provisions will be ignored - matters that could be of profound significance to a "normal" buyer.

Finally, the resumption officer will require a valuation to be prepared under a definition specified by the enabling legislation and as elucidated by the Courts following an identification of all the interests involved. This could include the fee simple as encumbered by the present leases, lessees' interests and possibly other heads of compensation such as disturbance.

A valuation report prepared for any one of these clients would be of limited usefulness to the others, even though based on the same facts. This is because the issues to be addressed upon which each has different decisions to make are quite disparate.

Hence, before commencing a valuation, the valuer must clearly define with his client the issues that are to be resolved and the exact scope of his services needed to assist with problem solution. To say, in effect: "Mr. Client, I don't know what your problem is, but the standard definition of value is your answer", is absurd.

Value in Use and Value in Exchange

If asked the value of his home, a person would undoubtedly reply giving a dollar amount. That, however, is the answer to another question for it says how much value it has. There is much confusion in everyday language as between the nature of value unmeasured and the magnitude of value. The answer does not inform the inquirer as to the nature of its value but its magnitude.

It is important to understand that value does not arise out of exchange. The nature of a property's value is determined independently of exchange. One way to know the magnitude of a property's value, is to take it into the market place. But before it will be demanded in an exchange transaction, it must have value in use. The market informs as to how much value it has, not the nature of its value (Pearce, 1987, p.15). The inherent components of value in use are presented to the market. Buyers assess those components, strike a subjective attitude to them and translate this into bids to buy. These features may be regarded as points favourable to the property and points unfavourable to it - or, utility and disutility. The evaluation of a property's features is referred to as "productivity analysis".

In practice a property cannot be taken to the market every time a problem requires

for its solution an estimate of the magnitude of its value. We have to estimate it indirectly and that is the task of the valuer. His work revolves around answering the question: if this property were taken to the market, what price would it fetch? We regard price as a measure of the magnitude of its value because money is the common denominator of exchange. Other elements of value peculiar to the

issues addressed are superimposed on that basic building block - the price it will probably fetch. Hence, the valuer needs to assess the property's productivity and attempt to understand how potential buyers will evaluate its productive features in forming bids to buy. In this, he first examines the nature of the property's value and, from this, proceeds to estimate the magnitude of its value.

Price, therefore, is the outcome of a behavioural process. In estimating price, the valuer per force has to forecast the behaviour of buyers and sellers. Before potential buyers will bid for a property they must be convinced of its usefulness - either actual or potential. Their understanding of "usefulness" is an outcome of their perception of its productivity. Certain uses will attract higher purchase bids in the market than other uses. This means, therefore, that the valuer must determine the use to which the property will most likely be put.

Ultimate Principles Of Valuation

The central fact of valuation, then, is productivity. Human responses to a property's utilities and disutilities underlie the price that is bid in order to enjoy the stream of net benefits it confers. Desirability begets price.

The following sequence obtains:

Productivity -> bids to buy > price in exchange

Equivalent words are:

Value > valuation -> value quantified It cannot be stressed enough that the value a thing has is its productivity. Much confusion would be avoided if, in the discipline of property valuation, the word "value" was restricted in its application to the concept of "productivity" - i.e., the kind of value the property has. Price is how much value it has. Instead of using the word "value" with a dollar connotation, we would be far better off by using the term "estimated price" - or its equivalent. Price is value quantified. Since it is price that is to be estimated and as each property is unique, the valuer's starting point is an inventory and appreciation of the property's particular utilities and disutilities. Productivity assessment, therefore, is at the very foundation of valuation. Without this, the discipline of valuation does not exist. The valuer who fails to engage with productivity analysis does not engage in the discipline of valuation.

Methodological Considerations

Following the inventory and analysis of productivities, an assessment is made of how they will be greeted in the market place and, from this, an estimate of price follows. Per force the valuer must become involved with the psychology of price formation in the mind of buyers. Herein may be found one of the great challenges to researchers in valuation: if we are to

understand how productivity is translated into price - the very essence of the discipline - we must engage with its psychological dimensions.

Because every property has an unique set of productivities attaching to it, the valuer needs to assemble relevant data for each assignment. In short, the process is always an inductive one.

Such uniqueness means that, in valuation, no general purpose pricing model is available (Lusht, 1988). Each assignment is a case study. Hence, it is necessary to adopt an intellectual approach which is relevant to the problem to be addressed, conformable with the available data (or that which can be gathered at reasonable cost), which incorporates checks for internal consistency and which is within the competence of the particular valuer. We shall refer to this below as "an appropriate conceptual framework".

Price is the outcome of exchange in the market place and cannot arise independently of it. Consequently, evidence of value quantified is data relating to actual exchange prices fetched recently for comparable properties.

Of course, more than productivity can arrest price. Other factors include the balance between supply and demand, the state of the capital markets and so forth. These are characteristics of the market not of the property and therefore unrelated to its productivity.

When the property is notionally "taken" into the market, a fixed set of property characteristics is deemed to be exposed to a changing environment. Since the market can shift dramatically in a very short time, three consequences follow:

- (a) Price is estimated as at a defined date.
- (b) The same bundle of productivities, if

introduced to different market environments, will most likely command a different price. For this reason, the valuer must study the state of the market at the time the presumed transaction takes place and understand how different kinds of market arrangement have their peculiar affect on prices.

- (c) A definition of market price which specifies certain characteristics of the market or possessed by buyers (it frequently amounts to the same thing) may not coincide with the characteristics of the market that has produced the transaction prices relied upon. The resulting estimate is not price as fetched in a market having the defined characteristics. The specifications incorporated in such definitions are a major cause of fuzzy thinking in the valuation and legal professions - as will be seen in the final section.

Since the supply of property resources is short term inelastic, the major determinant of short term price is demand. Therefore, in estimating price as at a defined date, attention is centred on the manner in which buyers are most likely to react to the particular set of productivities.

Conclusions Proper to the Valuation Process

One aspect of the nature of the conclusion arrived at by the valuation process derives inexorably from its estimative nature - i.e., from the fact that the property is not in fact exchanged for money. Estimated money-price is a forecast of an event that has yet to take place - the actual exchange referred to. Hence, certainty is limited to that of opinion.

The other aspect is that valuers estimate the price that is expected to be obtained on a specified day. It is usual to assume that an orderly approach to the market has taken place up to the date of valuation and

the task is to assess the price most likely to be obtained on the day of valuation (usually the date on which the property was inspected),

Our pricing models, therefore, estimate

only short-run price - not long-run price. This distinction is of concern when the planning period of the decision maker is taken into account.

The most frequently recurring situations

when the distinction between short and long run prices are relevant relate to the valuation of fixed assets and mortgage securities. These will be considered below.

Short Run And Long Run Price

The real estate market is never in equilibrium. When demand runs high, more and more investors enter the market (or developers add to the stock) to profit from the new demand. As developments take time to complete and as the level of demand obtaining when projects reach completion is very difficult to assess, an oversupply of space results. Developers withdraw from the market, new construction comes to a halt and there is little construction activity until demand catches up to fill the space that has been completed. Developers are hesitant to re-enter the market until there is a considerable amount of pent-up demand. After a time, the process begins again.

The result is that property values, especially in the commercial sector, are quite cyclical.

When a boom collapses, a significant number of tenants contract their space requirements or, what is worse, cease business. In any city, there will be up to, perhaps, a dozen new buildings either so far into construction that the work cannot cease or recently completed and in various stages of letting-up.

In a very short space of time, great expectations are dashed on the shoals of economic reality. The new buildings, to attract tenants and to offset even partially the not insubstantial operating costs, offer rentals at a very low rate or other incentives to attract firms out of less competitive buildings. Even if this tactic succeeds in filling the space, the net annual income, when capitalised, frequently results in a sum less than the cost of development. A result is that the lower quality buildings remain empty - or substantially so. This is in spite of the fact that they may be well managed and financed. Hence, their economic obsolescence is hastened and their lives cut short by many years. The task of converting them to their next best use is a daunting one. Value write-downs are inevitable and uncertainty is heightened.

The valuation of real estate in times of economic recession is especially difficult because of the heightened uncertainty, most buyers have withdrawn and there

may well be no transactions to guide the assessment process. As soon as a boom breaks, sales effected prior to that are non-comparable - the market is now a radically different one.

Under these conditions the question of value is a conundrum confronting many: building owners, shareholders, tenants, regulators, the accounting profession and others.

Reasons for Preferring Long Run Price Estimation During a Recession

To attract investors and to secure and maintain needed lines of credit, building owners prefer their books of account to disclose a steady increase in key variables such as asset values, profits and dividend payments (they are interrelated, of course). Variability signals risk. Sudden declines in items such as these can lead to spectacular share disposals and the calling in of loans. If, for example, an entity's debt to equity ratio increases suddenly, loan covenants may be breached. But, whether they are or not, lenders soon become nervous when such indicators are out of line with industry norms. An inevitable result is an increase in the cost of capital accompanied by added difficulty in servicing the sources of capital.

Why, because of a sudden slump in current values (i.e., short run price) should a hitherto solid entity be put at risk because its debt to equity ratio has been increased as a consequence?

Surely, the argument goes, there is a long term value which reflects the worth of the assets to an entity which has no intention of selling them in the short run?

Further, it is claimed, such valuations, based on short run prices, are an imperfect information source for decision makers. If, for example, long term lenders, especially, were confident that the long run value of the secured real assets was assured, loans would not be called in, liquidity would be retained and the entity would trade out of its short term difficulties. In this way there would be no premature destruction of capital and shareholders would not have to be satisfied with the proceeds of a liquidation sale - a return to them of less than they

would obtain when short run prices recover.

Calls for the use of long run values are made usually when the market is in recession. Figure 1 is a very rough illustration of the dilemma confronting owners, lenders and others.

Imagine we are at time t_2 . As time passes and as values rise toward the next peak, changes in asset values reflect the trend desired: a steady increase. Under this circumstance, there usually is no call for the estimation of long run price.

When a boom breaks, the decline in asset values is very sudden - more so than the sine curve in Figure 1 suggests. While it may take a few years to move from a trough to a peak, the reverse journey is one usually of only a few weeks.

The trough is rarely of short duration. Figure 1 has been drawn with considerable artistic license. Troughs may persist for several years. It is during this period of fairly stagnant activity that the issue of asset valuation becomes particularly acute. As indicated on the Figure, calls for the use of long term values are typically made in periods roughly from time t_1 to just past the ensuing trough.

The gently upward-sloping straight line in Figure 1 represents what it seems is usually envisaged as the trend in long term value or price in the long run. It is a representation of the secular trend in prices - i.e., with speculative cycles removed. Alternatively, it may be regarded as a part of a very long cycle.

Sometimes advocates of long run price point to its usefulness in curbing speculative enthusiasm when the market is riding high.

Is such a solution feasible? Before answering this questions it is necessary to examine the origin of the idea of long run or "normal" value.

Long Run Price in Neoclassical Economics

The origins of this concept may be found in the writings of the classical economists. One such was John Stuart Mill who referred to it as "natural value". Marshall, a neoclassical economist, used the term "normal value".

Natural or Normal value would be reached if the system had sufficient time

for the various forces to work themselves out and come to rest - a state of long run equilibrium which would see the emergence of long run or normal price.

It is best to refer to Marshall's own statement on the conditions requisite to the formation of normal value:

... society substitutes one undertaker for another who is less efficient in proportion to his charges. We may call this, for convenience of reference. The principle of substitution.

The applications of this principle extend over almost every field of economic enquiry.

... we assume that the forces of demand and supply have free play: that there is no close combination among dealers on either side, but each acts for himself, and there is much free competition that is; buyers generally compete freely with buyers, and sellers compete freely with sellers. But though everyone acts for himself his knowledge of what others are doing is supposed to be generally sufficient to prevent him from taking a lower or paying a higher price than others are doing. This is assumed provisionally to be true both of finished goods and of their factors of production, of the hire of labour and of the borrowing of capital.

(V, iii, 3-4, p. 341, original emphases)

A few pages later we have:

This is the real drift of that much quoted, and much misunderstood doctrine of Adam Smith and other economists that the normal, or "natural", value of a commodity is that which economic forces tend to bring about in the long run. It is the average value which economic forces would bring about if the general conditions of life were stationary for a run of time long enough to enable them all to work out their full effect.

(V, iii, 6, p. 347, original emphases)

The last sentence is a good statement of the theory of normal value.

One of Marshall's conclusions is:

In a stationary state then the plain rule would be that cost of production governs value.

(V, v, 2, p. 367)

That this conclusion is vaguely perceived by owners of realty subjected to declining values would seem to underpin their stance. If short run price is less than cost, then the cost incurred could be justified if long run price is used instead. The problem of declining asset value once the peak has passed is then defined away.

Critiques of the Theory of Normal Price

It is interesting to refer to the views of some of his contemporaries on the topic of normal value - or long run price.

Devas (1925, pp. 239-242), in reviewing the theory of normal value, advanced three criticisms of it.

First, the conditions advanced by Marshall as necessary to bring about normal value are inconsistent with the facts. In this, he has an ally in von Mises (1928, p. 125) who, in reviewing the theory of long run equilibrium, wrote:

Since it always requires some time for the market to reach full 'equilibrium', the 'static' or 'natural' prices, wage rates and interest rates never actually appear. The process leading to their establishment is never completed before changes occur which once again indicate a new 'equilibrium'. At times, even on the unhampered market, there are some unemployed workers, unsold consumers' goods and quantities of unused factors of production, which would not exist under 'static equilibrium'. With the revival of business and productive activity, these reserves are in demand right away. However, once they are gone, the increase in the supply of fiduciary media necessarily leads to disturbances of a special kind.

All of the assumptions given by Marshall are violated in the property market.

Groups do not compete freely, there are "combinations" and knowledge is imperfect. The principle of substitution does not

work smoothly.

Devas' second criticism is that, with the passage of time, the world becomes more complex, not less. Time, therefore, does not rectify temporary disturbances but introduces newer ones.

Third, there is a false analogy in the model advanced by Marshall. While it is perfectly proper to hold various factors constant in the physical sciences, this is impossible in the social sciences. One should not argue from the physical to the social sciences as they are different aspects of reality. Ruskin (1860, pp. 127-128) states it well:

... the disturbing elements in the social problem are not of the same nature as the constant ones; they alter the essence of the creature under examination the moment they are added ...

The thinkers just quoted, Devas, Mill and Ruskin, were all known to Marshall and are cited here to give an inkling of the richness of the discourse that characterised the times. Indeed, references to these three may be found in Marshall's pioneering work.

Coming to the present, it would be inappropriate to attempt an evaluation of the concept of normal price in the contemporary economics literature. We refer, nevertheless, to Wendt's very fine review of the intellectual influences affecting valuation theory and practice. Following his account of Marshall and other classical and neoclassical economists' contribution to the theory of normal value, he concludes:

The economic theory of the equivalence between long-run normal costs and normal prices not only lacks explicitness in the meaning attached to the words used, but appears to describe merely a tendency which might apply under assumed conditions WHICH DO NOT EXIST. Viewed in this light, the theory furnishes a highly insecure foundation for appraisal [valuation] procedure.

(Wendt, 1974, p. 217, emphases added)

We support this conclusion.

Long Term Concerns And The Mortgage Lender

Preliminary Matters

Those who take a long term view of income earning properties include, as noted above, mortgage lenders and certain users of accounting information. There is some overlap between the two groups but the distinction will serve present purposes.

In this section, attention is centred on mortgage lenders and how their concerns might be met in various parts of the real estate cycle.

One outcome of the steady state conditions in the real estate investment market following the depression and between the

inter-war years is the tendency to ignore the cyclical nature of the real estate market and to regard short run prices as marking a level that is expected to persist. Nothing could be further from the facts. It is imperative that those who take a long term position in property come to terms with the cyclical nature of this particular investment vehicle.

In this respect, real estate can be deceptive. Because bricks and mortar are solid and immobile, the idea of real estate price swings seems somehow unnatural.

Rather than adopt the theory of normal or long run price and ignore the cyclical nature of real estate markets - and thus an important component of their reality - it is far better to take it explicitly into account in a feasibility framework.

The gist of our argument is this: the estimation of short run price in a cyclical environment is of limited usefulness to an intending mortgagee. To address other concerns, the perspective needs to be widened to a feasibility analysis framework.

To make these introductory comments more concrete, we take the case of an income earning building which is fully let, or nearly so, and which is to be assessed for mortgage security purposes. The client, a major lender, is considering the advance of a large loan for a period of, let us say, fifteen years.

In approaching this assignment, the valuer must engage very carefully in an analysis of its productivity as discussed above, derive an estimate of the price it would probably fetch in the current market and check this against a number of DCF analyses. Included is a detailed study of each lease as part of the productivity analysis and an assessment of individual tenant risk. This is a very considerable work programme and it may well entail the contribution of relevant professionals such as mechanical engineers and property managers.

Such a programme is, however, standard fare to which is to be added a treatment of the issues confronting the intending mortgagee as part of the loan decision process.

Informed lenders view such properties as cash generating vehicles. The key question is to determine the extent to which the building, over the term of the proposed loan, can maintain its cash flow so as to meet all the demands on it. The ability to do so will vary as the cash flow responds to the cyclical forces determining the trend in its direction at a given point in time.

If the demands are not met, the question arises as to the price it would fetch in default of mortgage payment and when this may be likely.

The building's present market value is of interest in checking that the loan-to-value ratio falls within lending policy for that kind of building leased to the kinds of

tenant presently occupying it. Given, however, the cyclical nature of property values, such a ratio loses much of its meaning. Loan balances, especially for the first few years, reduce but little, but when a boom breaks, values decline rapidly and the ratio becomes a poor index of security. It is clear from the concerns just briefly reviewed that an estimate of current selling price addresses only a small part of the financier's concerns. With that understood, let us proceed.

The View Near the Peak of the Cycle

To focus the discussion further, refer again to Figure 1 and assume the assessment is being made as the market is approaching a peak. Yields have recently been bid down and the market is booming.

If the lender were given only an estimate of what the building would likely sell for now - i.e., short run price, it would be a most foolish action to base the loan amount on a valuation benchmarked to boom prices.

When prices have been advancing for a period and when the characteristics of a boom become evident, the peak of the cycle lies ahead - but how far away is impossible to tell.

In this circumstance, the analyst has to make a range of assumptions as to when the peak is likely to be reached and the likely consequences thereafter.

Not long after the peak becomes fact, rental values will fall as rent reviews become due, tenants may default on their leases or negotiate lower rents in order to stay in occupation, others still will either reduce their space requirements or be made bankrupt. In any event, net income will fall initially to a level lower than that prevailing at the time of the valuation.

The valuer needs to identify those tenants most likely to be affected by the adverse conditions and make rental loss allowances accordingly. It is here that a knowledge of past booms and their aftermath is of great assistance. After all, valuers are trained to reason from analogy.

In short, the procedure entails the construction of a range of scenario analyses each with its various annual solvency and risk measures. The latter are of considerable use in portraying for the lender the likely ability of the property to meet debt obligations over the years.

Depending upon various outcome, a set of active loan management policies can now be drawn up at the start. In a given case the analyses may show that loan servicing will become impossible when the downturn

arrives. In that case, the prudent decision is not to proceed with the loan.

In another case it might be shown that net cash flow for the first two years will be rather lean but show every likelihood of increasing thereafter. In that case, the initial advance might be restricted to that which the net income can prudently service. Following that, and if income picks up as predicted, a further advance of principal might be made. Or, the whole of the loan may be advanced at the outset with a graduated payment schedule agreed - one that best matches the ability of the project's cash flow to effect repayments. If the scenario analyses indicate that the building may become non-competitive to a critical degree ten years hence, say, then another set of issues affecting the lending decision come to the fore. Perhaps the most probable use will have to be changed at that time and this may bring about an income diminution. What, then will the likely next best use be? Who would be the most likely buyer type and what price would likely be paid? How does that compare with the prospective loan balance at that time?

Extending the lender's brief to cover these additional, but highly relevant, concerns raises questions which are very difficult to answer and the advice tendered would need to be appropriately qualified. Nevertheless, the valuer is the expert in these matters; that expertise may legitimately be sought by the client and specified in the letter of engagement.

The result of the scenario analyses, therefore, is a range of possible present values which are then compared with the amount of the loan sought and balanced with the loan-to-value ratios and other criteria applied by the lender.

None of these long range views constitutes a formal estimate of price except in a normative sense and given the position in the real estate cycle we are presently assuming. They are best regarded as limited forms of feasibility analyses aimed at probing whether or not the contemplated loan makes good sense from the lender's point of view and, if so, how much and upon what conditions. That precisely is the issue confronting the lender.

By the same token, a similar approach should be taken, in the market context assumed in this discussion, to advise an equity investor the sum of money that should be bid for the property and the terms that should accompany it. The resulting price estimate is usually referred to as "investment value" - a result which is client-specific.

The View From the Trough

Difficult as the kind of assignment just described is, we now move to an application which is even more demanding: decision making when the market is humping along the bottom of a trough.

When the market is depressed there is little or no activity. Such leases as are negotiated usually run with incentives shrouded in secrecy. Additionally, there are few, if any, property sales. In such times, the valuer has little evidence available to make the use of traditional models or price estimation possible.

The progress of commerce, however, cannot be held up awaiting the time when valuers' preferred inputs are available - that could be years away.

To focus the discussion, two situations will be reviewed in outline to give an idea of the approaches that might be adopted.

First, take the case where a new building has become a casualty of the recession. Perhaps only ten per cent or so of the space was leased just at the peak of the boom. Net cash flow is negative because outgoings exceed income. The position is complicated by the fact that the leases which are in place prescribe rental levels now no longer attainable. Indeed, it would not be unusual if the existing lessees had not already succeeded in having their leases restructured and a lower rent agreed. As there are no comparable sales or evidence of recent lease transactions, how does one ascribe a value to such a building? The fact that there are currently no buyers for the building and that it is only partly leased does not mean it is worthless. In such a situation, the valuer has to resort to a normative approach. Normative methods are employed when there are no market data available that are relevant to the problem being addressed and there are no market participants who can disclose their price fixing rationale. Chart 1 refers. In the case of an income earning property, as assumed here, the valuer has no option but to adopt a DCF approach to a number of scenario analyses. Each scenario is constructed so as to incorporate different assumptions derived from a careful review of the following matters (among others): the macro economic outlook, competitiveness of the local economy, resultant demand for space by tenant type, the competitive position of the building and so forth. From this kind of information, an assessment, for each scenario, is then made of the rate at which the building will be let over various time periods, the tenant types

most likely to be attracted to the building, their rent paying ability, the course of future outgoings and other relevant matters.

In this way, a half dozen or so different "futures" are constructed and a present value derived from each. Note that the macro and market analyses precede the financial analyses. The former provide the rationale for the latter. The range of present values thus established suggests the transaction zone from which the valuer has the unenviable task of selecting the one regarded as most probable.

In this process the market is dredged for any information pertinent to the problem. It may be possible to identify one or two leasing transactions that could shed some light on how participants view future prospects.

Is the result of this normative process an estimate of "market value"? Yes, but in a qualified sense. Although a careful productivity analysis is carried out, the way in which those productivities will be received and priced by the market cannot be objectively established. The "pricing" is a product of the valuer's assumptions as to behaviour of the system and the actions of imaginary buyers and sellers within it.

The procedures just described are very familiar to securities analysts and are known as "fundamental analysis" - for which see any standard text in the area, such as Fischer and Jordan (1975).

Before passing to the second example, a variant on the existing one is presented. Assume, now, that a couple of sales have been effected of new office buildings which are only partly leased. The capitalisation rate disclosed on analysis may be, say, only 1.5 per cent - or it may even be negative. How might a valuer use this information?

The valuer has to become adept at manipulating data until some useful measure is discovered. In the case just described, one approach would be to allocate the proportion of recoverable and non-recoverable outgoings to the leased areas, assess the net income produced by them and capitalise at the investor's target rate. This is then deducted from the sale price and the residue divided by the net unleased area to determine a sales price per unit of unoccupied space. The latter may be applied to the vacant parts of the building which is the subject of the valuation because it represents the present value, in the mind of the buyer, of the income stream anticipated from the vacant space (including resale) over that investor's time horizon. If

several sales lead to a similar result, so much the better. The buildings would need to be similar in quality, location, design, age, finishes, efficiency, building areas, site area ratio etc.

Would this procedure lead to an assessment of market price? Yes, because the productivities have been compared with actual market data and price inferred from that.

The second example introduced is that of an elderly building from which tenants have been attracted to newer ones. This, as noted above, is a common occurrence in the aftermath of a boom and it presents particularly troublesome valuation problems. Here the net income may be insufficient to service debt obligations and there seems little prospect of re-leasing its vacant areas. The lender is probably growing anxious.

The fact that the building is in such a state does not mean that it is worthless.

Essentially, the problem reduces to ascertaining the property's most probable use under the altered conditions. The objective is to explore alternatives and thereby ascertain that use which best fits the various constraints comprising the problem setting. Once the institutional restraints (such as political acceptability, social responsibility and legal sanction) have been met, the market and economic aspects of the remaining candidate uses are assessed in defining final feasibility.

The conclusion will vary, naturally, with the individual case. In a particular instance it might be concluded that the most probable use is for a redevelopment site which will not ripen for a period of several years. In the interim, the best use may be to demolish the structure and use the site for a car park. That would be a rather drastic outcome but, if the analyses have been competently done, capital restructuring can be put in place and the agony absorbed rather than prolonging the bleeding of cash in the hope that the market for the space, as presently configured, will improve. In short, the studies have been addressed to a defined problem, information for decision making has been derived and a purposeful plan of action can be initiated.

As above, the result incorporates an estimate of market value in a qualified sense because the property is not confronted with actual market data. Feasibility analyses are carried out by a team of relevant experts such as market analysts, engineers, quantity surveyors, land economists, property managers, lawyers and valuers. The nature of the problem will

dictate the identity of the specialist disciplines required for its solution.

Nevertheless, the outcome is to provide a range of expertly derived information and opinion bearing on the decisions that need to be taken by building owners and their lenders. In this way, orderly policies can be derived which are designed to preserve value rather than destroy it by resorting to a "fire" sale.

Trying to solve such problems by bringing to bear the philosophy of a willing buyer and a willing seller whose minds somehow converge on the agreement of fair value or long run "normal" price discloses the irrelevance of the traditional approach to valuation under today's conditions.

Those who contemplate taking a long term position in commercial real estate will find (indeed, many have found) that the range

of information required for making an informed decision is only partly met by resorting to a valuation which estimates short run price. The usefulness of such a valuation is seriously compromised when the estimated price is that purported between parties having characteristics specified in most definitions of value that simply do not exist. We turn to this below.

Aspects Of The Valuation/Accounting Interface

Following Phin (1985), the users of accounting information may be subdivided into three: those who read accounting statements, those who prepare accounting statements and those who audit them (the accounting profession). Each has a different emphasis on the kinds of demands they place on an accounting information system.

Those who read accounts do so in order to make a decision. They are a diverse group with a diverse set of demands and include potential and existing shareholders, lenders and securities analysts, business competitors and regulators.

Because they are concerned to make right decisions they expect valuations of realty to be relevant, logically consistent and reliable.

Valuations performed from period to period need to be logically consistent if they are to be useful in assessing management performance in the deployment of fixed assets. As investors and lenders make comparisons between entities, the valuations performed need also to be consistent across entities. This means that there must be an agreed conceptual framework within which valuations are carried out. Phin (op. cit.) makes the same observation in relation to accounting standards.

The valuations need to be relevant to the decision that has to be made. Hence the value estimate reported must be capable of being given a meaningful interpretation. Does it mean, for example, that the real assets could be expected to realise the figure assigned following an orderly approach to the market? Is it net of realisation costs (a considerable item in real estate disposition)? Is the valuation basis one such that the estimated price would not be paid in the current market?

A key ratio used by investors and lenders is the net tangible asset backing per share. This indicates the return to shareholders on winding up the affairs of the entity. If the valuation basis is one which is not

relevant to the market in its current state, this ratio loses its meaning.

The reliability requirement is usually checked by

looking to the standing of the individual or organisation that has done the work and their general reputation in the valuation of the class of assets concerned. Here one requires lack of bias and freedom from error.

It is in the areas of reliability and consistency that valuation standards have a role to play and this also is taken up below; The accounting profession looks to the prudential standards prescribed by their professional bodies and those standards which have the force of law.

Accountants and auditors are concerned with consistency, reliability and objectivity. Consistency in that two competent valuers assessing the same asset will derive similar results. Objectivity in that the price estimates have an identifiable factual basis rather than being the outcome of a process of opinion or judgment.

Where more than one value could sensibly be ascribed to an asset, the auditor would adopt the lowest figure in the interests of prudence.

The preparers of accounting information are concerned with the benefit: cost ratio in providing information. One cost is that of giving information to competitors. They seek valuations that meet their needs and those of other users at minimum cost.

They would prefer a flexible approach to valuation standards such that the benefit of any doubt can be swung to provide a favourable position rather than an alterna-

tive basis that will produce erratic changes in the value of the entity's underlying assets.

The extent to which the outcome of the valuation process can provide input to an accounting information system that meets all these criteria is now reviewed.

Apart from the competence of the professionals involved, two matters are relevant to the discussion: one, the very nature of the discipline of valuation - what, above, was referred to as "conclusions proper to the valuation process" secondly, the extent to which the valuation profession is prepared to adopt an appropriate conceptual framework. Attaining the latter is, in large part, an institutional constraint necessitated by the lack of a general pricing model in real estate.

The conclusions proper to the valuation process are that it is estimative and produces only a prediction of short run price. The estimative nature makes it impossible for valuers to meet the accountants' desire for reliability - that is, reliability as measurement. Valuation and uncertainty are inextricably intertwined. Hence, asset values reported for accounting (and, indeed, all other purposes) should quote the transaction zone arrived at by the valuer and the most probable price within that zone. This recommendation is incorporated in Australian Securities Commission (1992, paragraph 29). The degree of certitude is that of opinion; this means that the requirement for objectivity cannot, in the limit, be met either.

The estimation of short run price means inevitably that reported asset values will show the same cyclical movements as the market for the asset class and location concerned. The kinds of feasibility analyses reviewed in the previous section may be useful for corporate planning and could be incorporated in directors' reports. But their outcome, with one exception, are entirely unsuited for use in an accounting

information system. The exception is that normative methods simply have to be used in the absence of sales data but should be assigned a separate classification in the balance sheet and noted accordingly.

This means that corporations need to manage their debt and equity raisings so as to take cognisance of the cyclical nature of asset values. The preparers of accounts may be expected to resist attempts to mark such values to market unless revaluations are sought at "strategic" points on the real estate cycle so as to iron out major swings. To do so, however, is to negate the requirement for relevance and reliability.

To attain the desirable characteristics of relevance and consistency, we look to an appropriate conceptual framework. This is necessitated by the lack of a general pricing model. This lack can be counterbalanced to a degree only if a logically consistent approach to problem solving is adopted by valuers at large and incorporated in recognised asset valuation standards. It is in this respect that a reference to the work of the International Assets Valuation standards Committee is in order. At the time of writing (December 1993), only a part of the draft of the new standards is available and so it is neither appropriate nor possible to initiate a thorough review.

Nevertheless, sufficient has been released to permit a few preliminary comments to be offered. Before doing so, it is noted that the new standards, due to be published in 1994, contain much that is praiseworthy. The political hurdles that must have been overcome to secure agreement from thirty-eight professional valuation organisations from as many countries is a feat in its own right. The 1994 standards will overcome some of the serious defects contained in the earlier set.

While it is true that the Standards allow the adoption of value definitions appropriate to the problem to be addressed there is a passionate concentration on the given definition of market value. This emphasis will guarantee its application in circumstances when it is wholly inappropriate. Quite apart from that, the definition itself is seriously defective.

Here are some relevant excerpts from the draft 1994 standards:

Preface p.10: Professional Valuers avoid the unmodified term "value", substituting instead some adjective which describes the particular type of value involved. Market Value (or

"Open Market Value" in some countries) is the most common type of value associated with asset valuations. It is discussed below. Although common usage possibly dictates a market understanding that Market Value is intended in the absence of a statement to the contrary, it is especially important that even Market Value be clearly identified and defined in each such assignment.

p.11: Under the TIAVSC Standards, Market Value is defined as:

The estimated amount for which an asset should exchange on the date of valuation between a willing buyer and a willing seller in an arms (sic) length transaction after proper marketing wherein the parties had each acted knowledgeably, prudently, and without compulsion.

p.11: ... it is important to stress that the professionally derived Market Value estimate is an objective valuation of identified ownership rights to specific property as of a given date.....

IVS I p.1 4: The expression Market Value is not synonymous with the term Fair Value as it commonly appears in accounting standards. Unlike the Market Value definition explained above, Fair Value in accounting anticipates a sale which may occur under different circumstances and conditions than those prevailing in the open market for the normal orderly disposition of property. These include the possibility of a sale under short-term distress situations or other circumstances not contemplated in the Market Value definition. To avoid confusion or misunderstanding, the Market Value estimate reported by a Valuer will carry with it an explanation of terms and conditions upon which the estimate of Market Value applies.

IVSIA p.10: The concept of Market Value presumes a price negotiated in an open and competitive market, a circumstance which occasionally gives rise to the use of the adjective "open" before the words "Market Value". The words "open" and

"competitive" have no absolute meaning. The market for one asset could be an international market or a local market. The market could consist of numerous buyers and sellers, or one characterised by a limited number of participants. The market in which the asset is exposed for sale is not a definitionally restrictive or constricted market. Stated conversely, the omission of the word "open" does not indicate that a transaction would be private or closed.

Comment

The definition of market value falls within the class labelled "normative". Normative elements cannot be applied objectively. To do so, the valuer is forced to invoke a personal value system because the application rules cannot be specified.

For example, the notion of a willing buyer or seller is a relative one. A's idea of what constitutes willingness and the price outcome associated with that state may well differ from that adopted by B. Both A and B may be equally conscientious and committed to professionalism and may in fact use exactly the same data but, with the best will in the world, their notions will almost certainly differ and their price estimates will differ in like manner. By definition, value disparity is built into a process, the desirable characteristics of which include consistency and reliability. Specifying a willing buyer and a willing seller is, as discussed elsewhere (Whipple, 1991), consistent with the hypothesis of market equilibrium a state never found in the property market. This harks back to the classical economics view of long run price. Although the Committee says that the concept "be clearly identified and defined", it falls into one of the logical traps surrounding the construction of a definition. The word "value" has many meanings and one is mindful of McMichael's quoting fifty-four varieties of the term. To define that which is uncertain in terms of elements which themselves are uncertain breaches one of the rules of the logic of definitions. Jevons (1886, p. 110) rates it thus:

There is no worse logical fault than to define *ignotum per ignotius*, the unknown by the still more unknown. With subjective parties assumed, how can an "objective valuation" be arrived at?

Because of variability in conception of the terms, the interests of consistency over time and across entities will not be met.

The situation is, however, more complicated than this. There is the injunction regarding knowledge, prudence and lack of compulsion.

A well known characteristic of the real estate market is the scarcity of information. Even a valuer lacks information. Given this lack, how is a valuer to assess whether or not the parties to a transaction relied on were knowledgeable? Attempting to assess whether or not the parties were prudent imposes an investigatory task upon the valuer that Freud probably would find impossible. The market is constantly being made by "fools". How often have we heard the comment, following news of a standard setting sale, "only a fool would pay (sell for) that much"? Yet, it may well set a new level which, the next day, is regarded as "prudent".

Specifying lack of compulsion smacks of an overhang from older definitions which incorporated the requirement of being "not anxious". In every transaction there is an element of compulsion. If one were not compelled to buy or sell, the market would cease to exist.

Given an exchange price for a comparable property, given that it is possible to judge that the parties were not completely knowledgeable, were imprudent to a degree and exhibited some anxiety in reaching a decision, how does the valuer adjust for these imperfections and, at the same time, retain even a shred of credibility?

What constitutes "proper marketing" for a property is also a very difficult issue to address.

Price is the outcome of a behavioural process. Normative definitions which specify certain behavioural attributes ignore the fact that behaviour is far more complex than the definitions require. There is, however, a potentially darker aspect to consider. Because all these normative elements involve value judgments, it is quite possible for any or all of them to be given an interpretation which will assure that a preconceived conclusion can be supported. Herein lies the flexibility preparers may be expected to view with favour but which, if it were invoked, may lead to a different view

being expressed by the readers of accounts, regulators and the accounting profession. The adoption of normative definitions always opens the way to this kind of problem.

In short, all the qualifiers would seem to impose the requirement to regard the market as being something other than it is. Under that sanction, it is not possible to attain a balanced reading of it. The upshot is to forswear relevance as well as consistency.

A Positive Definition

The Committee would do all a service were it to draw a sharp distinction between positive and normative definitions of value and discuss the situations in which either may be appropriate. As stressed above, the selection of a definition must follow an analysis of the problem to be addressed (the Committee acknowledges this but fails to discuss adequately the importance of different definitions and their consequent data requirements).

In most commercial applications, the users of the information produced by the valuation profession want to know what the property in question can be sold for. That is specifically a positive view on life - positive in that the data are given rather than being the product of assumptions which are not associated with the data. Ratios such as net tangible asset backing per share then have some meaning.

The following definition is due to Ratcliff and may be found in Graaskamp (1977, p. 8):

The most probable price is that selling price which is most likely to emerge from a transaction involving the subject property if it were exposed for sale in the current market for a reasonable time at terms of sale which are currently predominant for properties of the subject type.

This definition recognises that price is the outcome of a behavioural process and that price predictions cannot be made with perfect accuracy. It does not require assumptions as to bargaining positions, that the parties are fully informed, prudent and all the other intellectual debris found in normative definitions of value.

The positive approach to price estimation takes the world as it is. As de Bono (1978) has it:

In the real world ... we have to cope with what is, rather than what we have constructed in our minds. (p. 66) .

Valuation assignments are difficult enough without introducing the complication of the hypothetical actions of hypothetical parties, sure to be endowed with the valuer's own value system and hence not of the market, in those cases where there are real people abroad making real decisions which make up the market the valuer has to interpret. Bertrand Russell (1946, p. 495) observes:

... if everything in some science can be interpreted without assuming this or that hypothetical entity, there is no ground for assuming it. I have myself found this a most fruitful principle in logical analysis.

If the only evidence relates to fire sales, then that sets the mark of the market at that time. Such a circumstance would need to be reported, of course. To assume the market is otherwise and derive a value estimate which is an hypothetical outcome of hypothetical bargaining by hypothetical people is to journey through Wonderland. To quote Devas (op. cit., p. 244), such prices are "mere creatures of the imagination" and have no place in an accounting information system.

Where there are no actors in the market, there is, of necessity, no market evidence. Faced with the problem of imputing a price to property under that circumstance, the valuer has no option other than to adopt normative methods of valuation. This process may or may not start with a normative definition of value - that will depend upon the results of the analysis of the particular problem. The previous section illustrated some applications of this approach.

Given, however, the desirable characteristics of relevance and consistency, the sooner we shift to a positive approach, the sooner will the demands of an accounting information system be met (or more nearly so) and the sooner will the relevance of the valuation profession be established.

One wonders, however, to what extent the question of normative definitions is a practical issue. Professor Ratcliff used to say that the fuzziness associated with the "willing buyer - willing seller" hypothesis really is of no account. Why? Because valuers simply don't do that. Why? Because nobody can. If this is so, then the issue resolves itself to one of faithfulness in standards setting. Why? Because our several professional bodies appear to say we do what we don't - and can't! A more charitable and, one would hope, a more realistic assessment is that the proponents of the willing but not com-

pelled parties, on the one hand, and most probable price on the other, are attempting to attain the same end. For ease of reference, the former will be labelled "Traditional" and the latter "Contemporary" - although it is appreciated these labels are not entirely satisfactory.

Note the double arrow on Figure 1. Its purpose is to illustrate that similar properties can sell for a high as well as a low price. The "true" price is where the graph intersects the double arrow. It is not difficult to associate the low price with a "fire" sale. Here the vendor is under duress but the buyer is very willing so as not to miss a bargain. Likewise, one could associate the high price as between a vendor who is not willing to sell and a buyer who is very highly motivated to buy.

Hence, one presumes the intent of the Traditionalists is, by definition, to exclude sales so "tainted", and arrive at a figure close to the "true" value - in the illustration, where the graph and the double arrows intersect. This they hypothesise to be the price willing but not compelled parties should agree to pay.

The contemporaries, on the other hand, would regard the intersection point as the most probable price. In this sense, it could be argued that both parties are aiming at the same end. We must then ask: of the two, which is intellectually the more rewarding, useful to the client and consistent with the canons of professionalism? Both recognise that there can well be a transaction zone. The Traditionalists, however, tend to shun the extremes whereas the Contemporaries incorporate them explicitly into their approach: the wider the zone, the less the certainty - and rightly regard that as information useful to decision makers. The Traditionalists, bound by their definitional approach, run the risk of not being able fully to use this information. The International Committee says as much because extremes reflect "circumstances not contemplated in the Market Value definition". Whereas the Contemporaries can avail themselves of probability theory, the Traditionalists foreclose this option - and are the poorer for that. The Traditionalists tend to spurn uncertainty: the Contemporaries recognise it is inevitable and treat it positively.

Traditionalists are in trouble when the only sales evidence is extreme. Assume, for the purposes of illustration, that the only transactions effected in recent times were "fire" sales. By their definition, and if they remain faithful to it, value is something greater. But how much greater?

That is impossible to tell since no empirical evidence is available as a bench mark. They can only fall back on either the normative approach illustrated earlier or the oft-heard assertion that "we valuers KNOW the value of the property".

This latter is worth pursuing a little further. Recall, under the circumstances assumed, there is no sales evidence pointing to where the double headed arrow intersects the curve. If value is something that "valuers KNOW", it can only be derived intuitively. Now, intuition is "uninfected knowledge" (Flew, 1979, p. 177). By definition, it is a mental process which can neither be communicated nor, as a necessary consequence, taught. If it cannot be taught, the discipline of valuation, if it is to rest on this principle, ceases to be one. Furthermore, a valuation report cannot document how the value estimate was arrived at - which probably explains the poor intellectual calibre of game reports and the esteem in which the profession is held as a result. Neither does it meet the rigour underlying accounting standards. Faced with an intuitively derived estimate, auditors then have the task of deciding its worth and whether or not it has any useful place in an accounting information system. The place of judgment in valuation is acknowledged but this mental process is different in kind from that of intuition.

Under the conditions posited, the International Committee pushes the discipline straight down the intuition path because the sales evidence available are an outcome of "circumstances not contemplated in the Market Value definition" (supra). But the true position goes beyond this: since the definition is unreal, no evidence ever will - regardless of where the market cycle currently is. Without exception it demands intuition. Valuers who invoke the definition but who eschew intuition also eschew the willing buyer-willing seller premise - and this explains Ratcliff's position referred to above.

The Contemporaries, on the other hand, accept reality and use "fire" sales to estimate the most probable price. It has a factual basis. It marks the market. Only a fictional answer can be given to the question: what would willing, informed, but not anxious parties, if any existed at the date of valuation, agree to? Mortgagees, the users of accounting information and others are not interested in a fictional figure open to the charge that it merely

serves the interests of the owner.

The Contemporaries see productivity as kind of value and price as value quantified. The task, then, is to estimate the price the property will probably sell for.

The state of the market (reported

"The task, then, is to estimate the price the property will probably sell for."

upon, of course) is taken as given - a positive view, not a normative one. The

market is dredged for all information and this is used in estimating probable price. Value quantified is the price most likely to be obtained regardless of whether the market is a buyers' market, a sellers' market and so on. The property is worth what it will fetch at the time; when we depart from this conception we are lost. The Traditionalists confuse value and price. Rather than seeing productivity as kind of value, they see value as arising from the interplay of normative elements that do not exist. Certain information is "not contemplated" - which is to say it is excluded, even if it be the outcome of actual market transactions.

The International Committee's definition sees the market as being in equilibrium - whereas the real estate market never is. The most usual kind of market arrangement is that of an oligopoly - but the Committee will not admit transactions arising from an oligopoly (or any other type of market arrangement which is not in equilibrium) because they are "not contemplated" in their definition of market value. Having defined value in the terms adopted, the Committee of necessity defines the kind of market arrangement that gives rise to the transactions "contemplated". The criteria for the admission of "contemplated" transactions is a market arrangement that never exists.

Since the contemporary approach is realistic, it supports professionalism. Because it is tied to a secure theoretical underpinning, it is intellectually enriching and capable of further development - e.g., risk analysis. The Traditional approach can make none of these claims. Time will be spent to better purpose if all concerned focus on the content of an appropriate conceptual framework, as in Chart 1, rather than chasing after definitions that are illusory.

Interprofessional Protocols

The valuation of real assets is becoming increasingly a collaborative exercise involving the expertise of a number of disciplines. This is partly a product of the complex nature of modern income earning buildings and the recognition, following

the collapse of the boom of the 1980s, that the estimation of market price must take into account the market prospects of the building over an acceptable forecast period. It is becoming increasingly difficult to sustain the proposition that valuations divorced from market studies are credible. If the contribution of other professionals is not to be encouraged, the statement of limiting conditions in the valuer's report will be so broad as to rob it of much of its usefulness.

This underscores the need to establish the extent of protocols between valuers, accountants and other professionals and the degree to which one may be permitted

to rely on the input of the other.

The valuer has prime responsibility to draw attention to aspects requiring information input from other professionals: e.g., legal interpretation of obscure lease

clauses affecting the probability of receipt of income; state of mechanical plant if likely to incur added running costs: compliance with fire regulations and so forth.

There is a need to establish the extent to which the valuer will be allowed to rely on information provided by databanking sources, revenue forecasts provided by the owner's asset manager, accounting interpretation of past data expressed in accrual form, market demand estimates from market analysts and so forth.

"The valuation of real assets is becoming increasingly a collaborative exercise involving the expertise of a number of disciplines."

This latter also raises the issue of acceptable method as between valuers and accountants of handling tenant improvements, lease incentives, leasing fees and the treatment of intangibles.

The establishment of a set of protocols applicable to the various disciplines would need to be a rather detailed affair if it is to be useful and the inter-professional negotiations will be marvellous to behold. Once established, they then need to be viewed in the context of the law of professional negligence. One would assume, however, that acceptance by the accounting profession and incorporation into relevant accounting standards would provide adequate legal sanction.

Much work in this area has yet to be done. A useful start, however, may be found in Gibson (1987) and Goodwin (1993).

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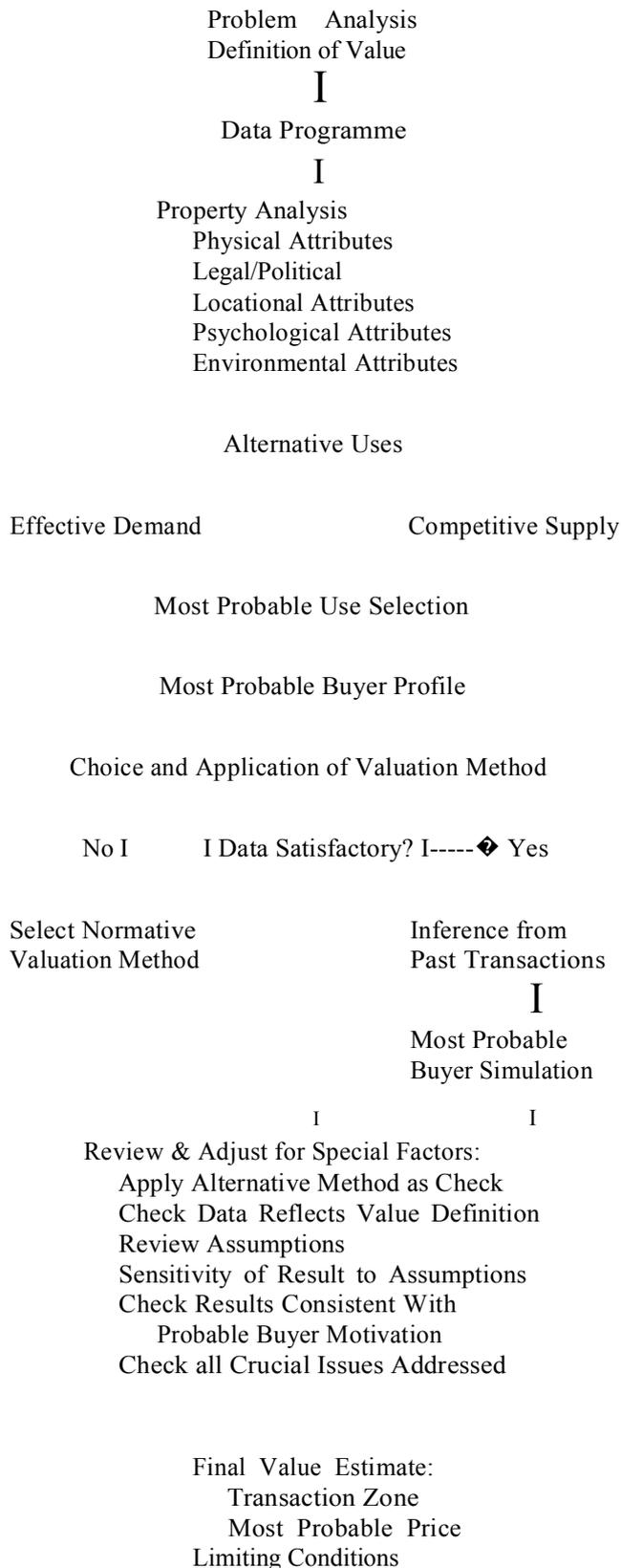
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Figure 1: Crude Illustration of Trend-Cycle in Property Prices

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Chart 1

Valuation Process



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Financial Analysis of Dairy Farm Conversion In the Manawatu Region

by I A McCarthy

Iona McCarthy is a lecturer in valuation at Massey University. She is a registered valuer and graduated from Massey in 1980 with a BAgrSci and in 1992 with a DipBusAdmin (Distinction). Iona McCarthy was employed as a valuer with Property Brokers, Palmerston North and returned to a lecturing position at Massey University in 1988. Iona has been dairy farming in partnership with her husband for 15 years and has practical experience of converting land for dairy production.

Introduction

There has been considerable investment interest in the dairy industry throughout New Zealand. Prices paid for operational dairy units have increased rapidly since early 1992 and many hectares have been converted for dairy production. This paper reviews an investigation of the relationship between the sale price of fully improved dairy farms and the sale price of farms suitable for conversion to dairy production, plus, the cost of required improvements in the Manawatu region in early 1993. The financial viability and financial profitability of dairy conversion are analysed using computer spreadsheet models.

The region studied contains all the land within a 40 kilometre radius of Tui Milk Products Limited factory at Longburn. The area is extensive and variable and includes the fertile alluvial soils of the river flats, the peat soils of the Opiki, the sand country of the West coast and the heavier clay country of the North. Dairy farming in the region tends to have been concentrated on the alluvial and peat soils and heavier sand country. However, with the current trend to dairying some more marginal country is now being brought into dairy production.

The trend to dairying is well illustrated by supply changes to Tui Milk Products Ltd. Prior to 1991 the number of dairy conversions in the Tui Milk Products supply area were in the range of 10-15 per annum and this tended to be matched by a similar number ceasing supply. In the spring of 1991 conversion to dairying was promoted with a series of seminars and workshops. This resulted in 55 new suppliers to the Company in 1992/93 (approximately 27 new suppliers in the region studied in this paper) and 34 in 1993/94 (approximately

20 new suppliers in the region studied). A further 36 applications have been accepted to supply in the 1994/95 season.

Cost of conversion to dairying can vary greatly between properties depending on the nature of the property and the level of existing improvements. For this reason it was decided the most appropriate approach for this investigation would be to analyse the costs of converting three separate case study farms that the author had access to in 1992.

Case Study Farms

The case study farms are located in the Manawatu region and were all available for purchase or lease within the defined period of study (1/6/92 to 31/1/93). In each case market evidence was considered to be *bona fide*. Properties of varying size were chosen to investigate the effect of economies of scale. The three farms were all considered to be very suitable for conversion to dairying with the two most important features being identified as soil type (free draining fertile soils) and location (within close proximity of Tui Dairy Company factories). These farms are not

representative of all dairy farms in the region. They are on highly productive soil types and are representative of the most productive dairying land in the Manawatu region.

The first property is located five kilometres south of Woodville and is 50.7 hectares in size with an additional 6.8 hectares of leasehold land adjoining. The farm was dairied on until 1982 and has been intensively cropped since then. It provides a small-scale conversion proposition, with conversion made more desirable due to existing improvements. This farm has been converted for the 1993/94 season.

The second property is located seven kilometres southwest of Palmerston North in the Kairanga and is 93.38 hectares in size. The farm was intensively cropped for many years prior to 1992. At sale date new

Table 1. Analysis of Dairy Farm Sales

Sale No	Sale Date	Sale Price Land/Ha	Total Sale Price/Ha	Total Sale Price/Kg. MF	Production Per Ha
1	Dec 92	\$12,982	\$17,082	\$35	486
2	Dec 92	\$10,497	\$15,668	\$35	449
3	Dec 92	\$8,967	\$13,586	\$34	398
4	Dec 92	\$9,558	\$13,521	\$31	438
5	Dec 92	\$7,529	\$13,624	\$32	426
6	July 92	\$8,726	\$13,125	\$34	391
7	Dec 92	\$4,525	\$8,228	\$30	273
8	Jan 93	\$4,600	\$7,886	\$29	271
9	Dec 92	\$4,792	\$6,945	\$34	204

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pastures were all well established. This farm provides a medium-scale conversion proposition and has the potential to become a very desirable and highly productive dairy unit. The farm remains a cropping/fattening unit.

The third property is located at Cheltenham and is 303.37 hectares in size. The farm has been run as a mixed cropping, fattening and breeding unit and provides a large-scale dairy conversion proposition.

This farm remains a cropping/fattening unit.
Analysis of dairy farm sales

In order to compare purchase and conversion with purchase of an existing unit, it was first necessary to analyse sale prices of operational dairy units. Table 1. summarises the results of analysis of operational dairy farm sales in the region studied. Sales 1 to 5 are all very good economic units on superior silt, peat or silt-loam soils. The total sale price for these properties is within the range of \$13,500 to \$17,000 per hectare, with three of the five properties selling at around \$13,500 per hectare. Sales 6 and 9 are on clay-based soils and sales 7 and 8 on sand country.

Sale 6 comprises four separate blocks and although farmed as a dairy unit has potential for sale as lifestyle blocks. This would appear to have inflated the sale price of the property. Sales 6 to 9 are economic units but on inferior soil types and this is reflected in the total sale price per hectare which ranges from \$7,000 to \$8,200. The total sale price per kilogram milkfat is from \$29 to \$35, with an average of \$32.60. There is very little difference in total sale price per kilogram milkfat between soil types. (Average for superior soils \$33.40/kg.mf., average for inferior soils \$31.70/kg.mf).

Table 2. Dairy Farm Development Costs

BUILDINGS	cowshed
	dwelling
	calf rearing facility
	hay and implement storage sheds
OTHER IMPROVEMENTS	fencing
	water supply
	races
	power supply
	effluent disposal
OTHER CAPITAL EXPENDITURE	capital fertiliser
	pasture renovation
	drainage
	supplementary feed
	dairy company shares
	consultants fees

Table 3. Summary of case study properties

Farm Property	Woodville	Kairanga	Cheltenham
Farm Sale Price	\$540,000	\$1,300,000	\$3,500,000
Farm Area (ha)	51	93	303
Sale Price \$/ha	\$10,650	\$13,900	\$11,500
Cost to Convert	\$126,000	\$304,000	\$490,000
Cost to Convert \$/ha	\$2,485	\$3,255	\$1,615
Total Cost of Unit	\$666,000	\$1,604,000	\$3,990,000
Total \$/ha	\$13,136	\$17,176	\$13,115
Milkfat Production Year 1	15,210	31,500	75,000
Milkfat Production Potential	22,815	40,500	120,000
Total \$/kg mf yr 1	\$44	\$51	\$53
Total \$/kg mf potential	\$29	\$40	\$33

Analysis of dairy conversion propositions

There are two separate issues in the analysis of a dairy conversion proposition. First the cost to purchase a property needs to be considered. Second the development costs need to be assessed.

In this study actual market evidence was used for the three case study farms so the cost to purchase was known. Development costs were calculated after detailed inspection of the properties.

Development costs vary greatly between properties and it is essential that investors ensure costings are as accurate as possible. Potential areas where development could be required and costs incurred on a dairy conversion property are outlined in table 2

Dairy Conversion on the Case Study Farms

Two of the case study farms were sold in late 1992 and the third was tendered for lease on the open market. This market evidence was used in conjunction with estimated development expenditure in order to assess the cost of conversion. Table 3. summarises the costs of converting the case study farms.

The total cost per hectare of the Woodville and Cheltenham farms are very comparable to the cost of operational dairy units on similar soil types. The total cost per hectare of the Kairanga farm is considerably higher and lies at the top end of the range of sale prices of operational dairy units. The effects of economies of scale can be seen in comparing costs to convert per hectare between the three case study properties. The Cheltenham farm cost is considerably lower than the other two. The Kairanga farm has very high costs of conversion due to the lack of on-site improvements (especially a metal source) and the need for drainage. The Woodville farm has lower costs due to existing improvements and an on-farm metal source.

Price of the conversion properties per kilogram milkfat when analysed in year one of production is \$10 to \$15 higher than operational units. However, when potential is realised, price per kilogram milkfat is comparable to operational units. Time to realise full potential varies, depending mainly on fertility levels, pasture species and drainage. For the case study farms potential should be realised within two to four years.

Financial Analysis

The realistic evaluation of the financial viability and financial profitability of a farm purchase or development proposal is critical for the potential investor.

Financial viability is concerned with determining whether it is possible to obtain capital to fund the proposal and studying future cash flows to ensure cost commitments can be met. The financial profitability as stated by McCrea et al (1990) ... takes into account all of the benefits and costs associated with the project for a given time period and provides a comparative figure for project ranking according to some given criteria of investment worth. (p.32)

In this study two evaluation tools have been used. First the cash flow in year one is examined in detail to ensure viability. Second, profitability is assessed with calculation of the net present value over a five year period. Most investors are interested in analysing the after-tax returns of an investment given their specific financing arrangements. The most appropriate analysis is to derive the after-tax net present value, including inflation and finance in the model, discounting at the investor's nominal after-tax required rate of return on equity capital.

A computer spreadsheet was used to develop two models for the financial analysis of investment in a farm purchase and development. The two models were

used to analyse the case study investments. A base assumption of 50% finance in the total property value was made for all case studies. For the net present value analysis, a post-tax nominal discount rate of 7% was used (based on a pre-tax, risk-free rate of 7.5% plus a 3% allowance for risk). It was important to examine sensitivity of financial outcomes to alteration in the variables of highest risk. The areas of greatest risk in return on the case study farms were milk-solids production and milk-solids payout. The two models included sensitivity analysis on alteration in payout and production.

Financial viability and financial profitability of the case study properties

The spreadsheet models were used to examine the financial viability and financial profitability of the three case study farms. A summary of the results is provided in the attached appendices. Results showed that investment in either the Woodville farm or the Cheltenham farm was financially viable and financially

profitable, with average efficient production levels and increasing payout. This implied required production levels in year 1 of 250-300 kg mf per hectare increasing to 450-500 kg mf per hectare by year 5, and a payout of \$6.00-\$6.50 in year 1 increasing to \$7.50 by year 3 and remaining at that level for years 5 and 6.

Investment in the Kairanga farm was only financially viable and financially profitable if very high production levels were achieved with an increasing payout.

Production levels of 400-450 kg mf per hectare increasing to 600-650 kg mf per hectare were necessary. These levels of production are only achieved by the top 5-10% of Tui Milk Products suppliers.

Conclusions

This investigation led to the conclusion that in January 1993 the cost to an investor considering purchase of farm land for dairy conversion was comparable to the cost of an operational unit. There was no discount for reduced income expected during a development phase.

In this buoyant property market it ap-

peared that investment in farm land for development for dairy production was financially viable and financially profitable under average efficient management if the payout continued to increase. The researcher would suggest that the risk associated with fluctuations in future payout is too great to warrant investment in a dairy conversion proposition in 1993. Computer spreadsheet models can readily be developed to completely analyse any investment proposition. Given the fluctuations in farming returns in recent years it is considered essential to completely analyse the financial viability and profitability of any investment taking full account of the risk inherent in the specific investment.

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Appendices

Appendix 1: Woodville

Output from model I (financial viability) is summarised in table 4.1.

Table 4.1. Model 1. sensitivity analysis, Woodville

SENSITIVITY ANALYSIS

To show post-tax farming surplus/deficit with varying payout and production

Payout	Kg milkfat/ha								
	200	250	300	350	400	450	500	550	600
\$4.00	(84,413)	(74,864)	(65,314)	(55,765)	(46,216)	(36,667)	(27,118)	(17,568)	(8,019)
\$4.50	(79,136)	(68,268)	(57,399)	(46,531)	(35,663)	(24,794)	(13,926)	(4,004)	4,256
\$5.00	(73,859)	(61,672)	(49,484)	(37,297)	(25,109)	(12,922)	(2,238)	7,205	16,287
\$5.50	(68,583)	(55,076)	(41,569)	(28,062)	(14,556)	(2,477)	7,788	17,863	26,837
\$6.00	(63,306)	(48,480)	(33,654)	(18,828)	(4,722)	6,546	1	7,642	27,491
	37,252								
\$6.50	(58,029)	(41,884)	(25,739)	(9,594)	3,299	15,565	26,394	37,014	47,592
\$7.00	(52,752)	(35,288)	(17,824)	(1,953)	11,320	23,547	35,052	46,492	57,918
\$7.50	(47,476)	(28,692)	(9,909)	5,065	18,949	31,367	43,669	55,960	68,200
\$8.00	(42,199)	(22,096)	(3,195)	12,083	25,935	39,123	52,286	65,384	78,451

SENSITIVITY ANALYSIS

To show pre and post-tax farming surplus
pre-tax ROI
pre and post-tax return on equity

with variation in payout, production of 300 kg/ha

Payout	Surplus/deficit Pre-tax	Surplus/deficit Post-tax	Pre-tax ROI	Pre-tax ROE	Post-tax ROE
\$5.50	24,710	(41,569)	0.08%	0.13%	-7.51%
\$6.00	32,315	(33,654)	0.96%	1.50%	-4.08%
\$6.50	39,920	(25,739)	1.83%	2.87%	-4.65%
\$7.00	47,525	(17,824)	2.71%	4.25%	-3.22%

LEGAL ISSUES

ALTERNATIVE DISPUTE RESOLUTION ("ADR")

by S Williams

Introduction

For the most part, traditional methods of dispute resolution have tended to be adversarial in nature. Given that in almost every field of human endeavour disputes are probably inevitable from time to time, and are generally destructive, it is surprising that society has not developed more sophisticated ways of dealing with conflict. However, there now seems to be something of a minor revolution taking place in the way society is looking at the resolution of disputes. There is a growing awareness in many parts of the world (unfortunately not everywhere) that the traditional methods of resolution of conflict are unsatisfactory and that there are alternatives. Negotiations of international conflicts and disputes in recent years have demonstrated the trend.

The problem with litigation

At the level of the private disputant, this trend has coincided with an increased dissatisfaction with the traditional (non-violent) means of resolving disputes the courts. It has often been said, sometimes by judges, that at least 50% of the people who appear as parties before our civil courts go away having lost, and a fair proportion of those who, at least on the face of things, have won nevertheless also go away unhappy. This may be because the court case has cost them more than they have gained. It may be because, in the process, the parties to the dispute have fallen out completely and the chances of a continuing relationship have been destroyed. It may be because the case has taken years to come to a conclusion. It may be because even the winning party sometimes feels that his real concerns have not been addressed.

There are other disadvantages with our traditional system of litigation. Not only is it expensive, but it is also terribly draining on the resources of the parties. It is limited

in terms of the solutions that can be imposed. Generally, for example, the courts can only order things like specific performance of agreements or the payment of money sums as damages. Although in defamation cases the courts can recommend that the defendant apologise to the plaintiff, the courts generally have no power to order a party to apologise for a wrong that may have been committed. They have no power to look outside the boundaries of the dispute before them for solutions.

Litigation is also highly unpredictable. Lawyers will often tell you that they lose the cases they expect to win and they win the cases they expect to lose. Litigation is also time consuming and expensive. Generally speaking this is not the lawyers' fault. The law seems to get increasingly complex, and more often than not these days the circumstances leading up to a dispute are confused. Technology allows so much to happen so fast, and transactions can become so complicated and intricate that their analysis from both the factual and legal points of view when it comes to litigation is time consuming and difficult. The prospect of appeals lengthens the time before one can look forward to a court case being finally resolved.

Parties also have no control over the result. Things are taken out of their hands. The tendency in traditional litigation is to keep the parties apart. One of the consequences of this is that often the parties do not hear the other side's case (much less attempt to understand it) until they hear it for the first time in court. Had they done so earlier they might have been more inclined to settle.

I suspect that there would be few litigants who, having had their day in court, would not have wished the matter to have been settled in some other way.

There has thus been a rapidly increasing

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disillusionment amongst both private and commercial litigants as to the effectiveness of the litigation process for the resolving of disputes. Indeed many lawyers share the same misgivings. It is not the fault of the courts. They are victims of the same circumstances of complexity I have described. Given the role that the courts play, the very nature of their processes almost necessitates delay. All this is of course not to say that the courts do not have a major role to play in the resolution of disputes between citizens and I will come back to this later. What it does mean, however, is that there are a large number of people who have disputes to resolve these days who are saying that there has to be a better way.

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What is ADR?

As a consequence of this disillusionment there has grown up a whole range of alternative (and legitimate) ways of resolving disputes. Collectively they have come to be known as Alternative Dispute Resolution or ADR. All of these different ways of resolving disputes are real alternatives to the use of the courts.

ADR has been around in the United States (where the disadvantages of litigation I have described are manifest) for some years. Australia has also had its proponents. In New Zealand, ADR has been seen as comprising arbitration more than anything else. But throughout the world in more recent years various forms of ADR have gained in popularity and the same thing is happening in New Zealand. For example, there is an organisation known as LEADR, which is an off-shoot of an Australian organisation. Its name stands for Lawyers Engaged in Alternative Dispute Resolution and it is an organisation consisting principally, but not exclusively, of lawyers who are practising various forms of alternative dispute resolution. The interest in ADR amongst lawyers recently has been considerable and LEADR in New Zealand is going ahead in leaps and bounds.

Negotiation

The range of ADR techniques is often likened to a spectrum. At one end of the ADR spectrum is a simple unassisted negotiation between the parties to the dispute. It may be thought that people have been negotiating their disputes for centuries and that would of course be true. However, what is happening now is that people are being trained how to negotiate, and not in an adversarial way but in a constructive way which produces a result that both parties are happy with. The classic story which is often told to demonstrate the benefits of "win/win" negotiation is the story of the two daughters each of whom was making a claim for the last orange in the fruit bowl. One argued that she had asked for it first. The other argued that it was her turn. Their mother was called in to decide who should get the orange. Depending on which version you listen to (and some would say depending on whether the mother was acting as a judge or an arbitrator) the mother "solved" the problem either by giving the orange to one daughter or the other or by cutting it in half and giving them half each. However, if the negotiation process had been such as to get to the real interests of the parties, rather than concentrating on their rights, it

would have been found that one daughter wanted the orange for its juice and the other wanted it for its rind to make an orange cake, and thus each would have been able to be satisfied without detriment to the other.

Arbitration

At the other end of the spectrum is arbitration. Some would say that arbitration is not a form of alternative dispute resolution at all because it has most, if not all, of the disadvantages of litigation in the courts, plus the added disadvantage that one has to pay the arbitrator. It does, however, have some advantages, notably in the present context that the parties can, if they want to, agree on a more flexible procedure, and I think it is entirely appropriate to regard it as being within the range of ADR techniques.

Those in the middle

In between a simple unassisted negotiation at one end and arbitration at the other end of the spectrum, there is a range of ADR methods or techniques, all of which are themselves flexible and adaptable. One can even have a combination of two or more of these methods or techniques in a dispute resolution procedure tailored to the particular case. Fundamentally, however, they comprise:

- Mediation
- Conciliation
- Case presentation
- Independent expert appraisal
- Mini trial

What all of these methods or techniques (including negotiation and arbitration) have in common is that they all depend to a greater or lesser degree on the parties' agreement to the process. You cannot force a party to negotiate, for example. If the parties have agreed beforehand (such as in a commercial contract, in a construction contract or in a lease) that they will mediate or conciliate any disputes which arise, they may be forced to go through the process, but they won't be bound to the result unless they agree with it. Even arbitration cannot be imposed on a party unless he has agreed to arbitrate (although in some cases the court has power to order a dispute before the court to be referred to arbitration), but of course an arbitrator's award is binding and enforceable in the same manner as a court judgment.

Mini Trial

Dealing with these "middle of the range" ADR methods in reverse order, a mini trial is just what it says - a hearing by an independent person, normally a lawyer, at

which the parties present abridged versions of their cases and the independent "judge" then gives a decision. It is not binding but the decision may be heavily influential to the parties in their subsequent attempts to settle the case. The advantages are that both parties get to hear each other's cases and they get an independent assessment of the likely outcome if the case were to be the subject of a full trial. The disadvantages include the possibility that one side will just use the mini trial as a fishing expedition whilst keeping its own cards close to its chest. It can also be used as a means of delaying final determination and it can be expensive.

Case presentation

Case presentation involves senior executives of the parties in dispute being attended by representatives of these same parties who present brief summaries of their cases to the senior executives who then, with the benefit of having heard both sides, attempt to negotiate a settlement. This has the advantage that fresh minds are brought to the dispute at a level above any personal or emotional considerations which often influence the protagonists directly involved in a dispute.

Independent expert appraisal

Independent expert appraisal involves an independent third party being asked to investigate the matter in dispute and then to give his or her opinion. Again this is not binding on the parties but may be heavily influential. It is less formal than a mini trial, with the independent expert taking a greater role in getting to the bottom of the matter rather than being dependent on what he is told by the parties. The joint commissioning of a valuation report on the basis that its findings will not necessarily be accepted is an example of this type of ADR.

Conciliation

Conciliation and mediation are, apart from arbitration and simple negotiation, the two most common forms of ADR presently in use in New Zealand. They have not been widely used but are rapidly gaining in popularity. They are very similar. Both involve the parties in a structured negotiation with the assistance of an independent third party. In a conciliation, the third party (called the conciliator) will, in addition to assisting the parties to negotiate, come to his or her own conclusion as to the solution and will make that known to the parties to help them settle the matter. This may be done on the basis that the conciliator issues a decision which is

agreed to become binding unless either of the parties indicates non-acceptance of the decision within a certain time period.

Mediation

Mediation is the particular form of ADR which is being focused on by LEADR. I believe it is the most promising because it is probably the least adversarial and the parties have total control over the outcome. This means that the parties' chances of preserving their relationship are maximised and they are more likely to want to make the solution work, so that problems of enforcement are minimised.

Mediation is a structured negotiation process whereby an independent third party (the mediator) assists the parties to agree on their own solution to the dispute. Although the process is structured, it is not inflexible. Unlike a conciliation, the mediator does not take sides, and indeed remaining neutral is a crucial aspect to his role. The mediator must build up the trust of the parties because an important element of the process is the private sessions which the mediator will have with each of the parties in turn at which they may confide in the mediator, on a confidential basis, as to their underlying concerns.

The mediator works to get to the underlying interests of the parties, which may have nothing to do with their strict legal rights and obligations. It is popularly thought that a "hidden agenda" is behind at least three-quarters of disputes. For example, a party may be sticking to his guns simply because he is too proud to accept that he may have been mistaken. Often a court never gets to hear about the hidden agenda and certainly in most cases cannot deal with it within the scope of the matters before it. In mediation, a settlement can be reached without that party acknowledging that he was mistaken.

The mediator tries to flush out these underlying interests. He then assists the parties to work towards a solution with which they are both happy. Because their underlying concerns and interests have been met, they are more likely to be comfortable with the result than in a case where those concerns and interests have not even surfaced, let alone been dealt with. The role of the mediator is to persuade the parties to focus on their underlying interests and concerns and to move away from fixed positions that often cloud the real issues.

It is the mediator's function to act as a facilitator. The success of the process depends to a large extent on the quality of

the mediator. He or she should be a creative problem solver, a good listener, a person who is able to keep confidences and a person who inspires confidence. The mediator must know how much to intervene and how much to stand back.

Speed

Mediation has some real advantages. It is quick. There is no reason why a mediation cannot be organised, and the dispute settled, within a matter of weeks of the dispute arising. Even very complicated disputes can be disposed of quickly because the mediation process is not normally concerned with coming up with the correct factual or legal answer to the problem. It is concerned with arriving at a solution which, as I have said, may have nothing to do with the parties' legal rights. The parties' legal rights often do not coincide with their real concerns and interests and the mediation process is designed to satisfy the latter rather than the former.

Less cost

Mediation is considerably less expensive than litigation. Because the process does not involve a detailed analysis of the facts and the law (and therefore what might take two weeks of court hearing time might only take a day in mediation), the legal fees are much less and the time and resources spent by the parties are considerably reduced.

I hasten to add that lawyers remain very much part of the process. A lawyer may of course act as the mediator. But in any event most mediators prefer to have the parties legally represented at the mediation. Many people feel more comfortable having their lawyer with them for support and advice and the lawyer, especially if trained in mediation, can play an important role in helping the mediator to get to the parties' interests and to work through to a solution. The lawyers may also be required to draw up the settlement agreement to make sure that it has legal force and is workable.

Control

Very importantly, the parties have control over the solution. They do not have to accept the solution unless they are happy with it. This means that both parties come away from the mediation happy. Relationships are generally preserved and indeed the very solution to the dispute may involve the establishment of a continuing relationship which would not otherwise have occurred. Relationships may thus be enhanced.

Range of remedies

Mediation offers a limitless range of remedies, as has already been mentioned. A party can agree to apologise (which may be all that the other party was looking for); he can agree to give discounts off the cost of future supplies; he can agree to do further or other work; he can agree to vary the terms of a contract.

Another advantage of mediation is that it can deal with disputes amongst several parties. For example, it has real potential in environmental disputes or in landlord/tenant/subtenant disputes.

Confidential

Mediation is conducted on a without prejudice basis and is confidential. Within the constraints of the law, what is said in the mediation cannot be revealed or used against the parties later.

The skills of a mediator

Theoretically anybody can be a mediator. Desirably only those who are trained in the process should act as such because an untrained mediator can do more harm than good. Conversely, mediators who are trained in the dynamics of conflict and the numerous and fascinating techniques for drawing out and resolving conflicts can work wonders. Thus the current training of mediators involves not only the teaching of the process of mediation but also familiarisation with the various skills required, for example:

- to break deadlocks
- to correct imbalances of power between two negotiating parties
- to separate out and put to one side the superficial positions and concerns of the parties and to get to the real issues and interests
- to de-emotionalise the dispute
- to identify points of agreement
- to help people see not only the strengths but also the weaknesses of their case.

Co-mediation

Co-mediation involves mediation with the assistance of two or more mediators, each appointed by one of the parties. This can provide some comfort to a party who may be concerned that a sole mediator may take sides with the other party. It also enables the mediators to share the burden of the process on the basis that two heads are better than one. It can also be important where the parties are of different racial, ethnic or other backgrounds.

The process

A typical format for a mediation would involve the mediator having a preliminary discussion with each of the parties to introduce himself, to obtain a commitment to the process and to arrange a time and place for the first meeting. At the first meeting, the mediator will make an opening statement and will then ask each of the parties in turn, in the presence of the other, to say what he wants to say about the dispute. The mediator will endeavour to establish the issues and some options for resolution. There may then be a private session with each of the parties in turn (called a caucus) which is confidential and at which the party can make known to the mediator any other factors or concerns which are on his mind. There will then be a further joint session, possibly followed by subsequent caucuses and joint sessions. During all of this time, the mediator will be endeavouring to guide the parties towards a solution.

The mediator applies various techniques towards assisting the parties to develop a solution. One technique, for example, is the "agreement in principle" approach whereby the parties are encouraged to agree to a particular solution on the assumption that certain specified concerns can be met in some way, and then the parties set about to try and deal with each of those concerns. This not only makes the parties feel that they are making progress (and therefore they want to continue talking) but it also helps to narrow the dispute in their minds.

An important requirement of the process is that the persons negotiating must have authority to reach an agreement and cannot take refuge in the need to go back, for example, to a board of directors for instructions.

Potential

Mediation has been used in New Zealand for some years in the family law and employment fields but its potential is not limited to those areas. It is now being used to settle all kinds of disputes, including major commercial disputes.

There are moves afoot in some overseas courts to require mediation to be attempted before a court hearing date can be obtained and the New Zealand courts are starting to think in similar terms. The Department of Justice has recently introduced a pilot scheme for case management in the High Court which is being trialled at the High Courts in Auckland and Napier. This scheme is stated to be part of an on-going process "to improve the efficiency and cost-effectiveness of the judicial system". Apart from providing for a greater degree

of judicial control over the progress of cases through the court system, the scheme places an emphasis on the exploring of ADR options such as mediation. The parties, as well as their counsel, are actively encouraged to consider such ADR options.

Many commercial documents are now incorporating ADR clauses providing for such things as mediation and conciliation either as alternatives, or in some cases as compulsory precursors, to arbitration or litigation.

Some of New Zealand's biggest companies have been parties to mediations and the feedback is extremely positive. Statistics show that something over 80% of disputes that are referred to mediation result in a successful settlement, and that is a pretty good strike rate. Of course it will be said that probably those disputes that have been referred to mediation are the ones that are most likely to settle. But I must emphasise that it is not only disputes where the parties are co-operative and amicable which can be referred successfully to mediation. Mediation is perfectly suited to disputes in which the parties are bitterly opposed to each other and in major personal conflict. In fact for some reason these are the very sorts of situations in which mediation appears to work best.

However, there are some cases which are clearly not suited to mediation. An example is a situation in which a precedent is sought to be established which will have binding effect in future similar situations. It is also true to say that there are some cases in which it is just impossible to get the parties to talk to each other. One or both of them want their day in court whatever the result. And of course the court always needs to be there as a forum of last resort, to provide both the incentive to settle and the means to enforce the settlement.

Mediation is most effective where the parties are both desirous of settling their dispute, where they have or may have an on-going relationship and where there is some external pressure to settle.

Relevance to Valuers

It is hoped that those who might read this article will find some interest in the trend towards ADR for personal or business reasons if not for professional reasons. However, there could be significance for valuers in relation to valuation or rental disputes. Where valuers cannot agree, they usually go to arbitration and in many cases that may still be necessary. However, there may well be cases where a more creative solution can be found. It may be,

for example, that a lessee faced with a rent increase which he can ill-afford may be able to compensate the lessor in some other way which may be as attractive to the lessor as it is to the lessee. Or the lessee may be prepared to commit himself to an increased term in return for the rental staying the same. Often in a rental dispute these sorts of solutions are never even contemplated by the parties, and there is something to be said for having a procedure which at least allows them the opportunity of doing so.

"Pendulum" Arbitrations

The concept of a pendulum arbitration is also one designed to encourage settlement of disputes, particularly disputes involving differences as to quantum. Where in such a case the parties, to say a rental dispute, agree to embark upon an arbitration, the traditional situation is that each party invariably takes an extreme position in the knowledge that the arbitrator is almost certainly going to come down somewhere in between. There is an assumption that the more extreme your position, the more likely the arbitrator is to fix a rental closer to your position than to the other party's position. In a pendulum arbitration, the arbitrator is asked not to fix the rental at whatever level he considers appropriate but is asked to pick either the rental contended for by the lessor or the rental contended for by the lessee. In this way, both parties are encouraged to contend for a rental which is as "honest" as possible and the parties may thus end up arguing only over a very small difference. In turn this might lend itself to settlement without the need for the arbitrator to be involved at all.

In the United States, they have a variation on this theme called "MEDALOA" (an acronym for "Mediation and Last Offer Arbitration"). Under this variation, the parties have a mediation which may narrow down their differences but, if they cannot bridge the final gap, the mediator suggests that they present their final positions (either to the mediator or to some other independent person) who is then authorised only to select one or the other, and the selection is binding. This can act as an incentive to both parties to compromise even further.

Conclusion

ADR really is the flavour of the month in the dispute resolution industry at the present time. But I also think it has a big future, and all those involved in disputes and their resolution need to be aware of what it involves and, I suggest, we all have a responsibility to promote it.

(Continued front Page 34)

The Woodville farm investment is financially viable only at comparatively high levels of production and payout. To return a post-tax surplus, in year I with a payout of \$6.50, production levels of 400 kg/ha need to be achieved. Examination of the returns to equity and investment at the most likely production level of 300 kg/ha and payout levels ranging from \$5.50 to \$7.00 show very poor initial returns.

Output from model 2. (financial profitability) is summarised in table 4.2.

Table 4.2 shows the net present value, at 7% discount rate, of investment in the Woodville property for good and average scenarios. Examination of the results shows that the investment is only financially profitable with average efficient production levels if payout increases.

Table 4.2 Model 2. Woodville

Payout Per Hectare	Production Year I			
	250	300	350	400
Good Scenario¹				
\$6.00	(155,735)	(33,189)	86,547	204,752
\$6.50	(82,098)	47,801	175,322	298,775
Average Scenario²				
\$6.00	(363,232)	(260,380)	(158,361)	(59,394)
\$6.50	(287,170)	(176,260)	(67,729)	36,832

¹ Payout increasing by 50c/year for years 1-3 and static for years 4 and 5. Production increasing by 50kgmflh/year.

² Payout static for 5 years. Production increasing by 50kgmflh/year.

Appendix 2: Kairanga

Output from model 1. (financial viability) is summarised in table 5.1.

Table 5.1 Model 1. sensitivity analysis, Kairanga

SENSITIVITY ANALYSIS

To show post-tax surplus/deficit with varying payout and production

Payout	Kg milkfat/ha								
	200	250	300	350	400	450	500	550	600
\$4.00	(167,161)	(150,210)	(133,259)	(116,307)	(99,356)	(82,405)	(65,453)	(48,502)	(31,551)
\$4.50	(157,794)	(138,501)	(119,208)	(99,915)	(80,622)	(61,329)	(42,036)	(22,743)	(3,450)
\$5.00	(148,427)	(126,792)	(105,158)	(83,523)	(61,888)	(40,253)	(18,619)	3,016	20,188
\$5.50	(139,060)	(115,084)	(91,107)	(67,131)	(43,154)	(19,178)	4,799	23,322	40,080
\$6.00	(129,693)	(103,375)	(77,057)	(50,738)	(24,420)	1,898	22,897	41,241	58,687
\$6.50	(120,326)	(91,666)	(63,006)	(34,346)	(5,686)	18,913	39,294	58,278	77,069
\$7.00	(110,959)	(79,957)	(48,956)	(17,954)	11,369	34,239	54,787	75,116	95,424
\$7.50	(101,592)	(68,249)	(34,905)	(1,562)	25,607	48,214	70,105	91,942	113,702
\$8.00	(92,225)	(56,540)	(20,855)	12,724	38,507	62,034	85,401	108,704	131,953

SENSITIVITY ANALYSIS

To show pre and post-tax farming surplus pre-tax ROI

pre and post-tax return on equity

with variation in payout, production of 350 kg/ha

Payout	Surplus/deficit	Surplus/deficit	Pre-tax ROI	Pre-tax ROE	Post-tax ROE
	Pre-tax	Post-tax			
\$5.50	57,511	(67,131)	1.70%	2.82%	-5.64%
\$6.00	73,261	(50,738)	2.50%	4.14%	-4.26%
\$6.50	89,011	(34,346)	3.30%	5.46%	-2.89%
\$7.00	104,761	(17,954)	4.11%	%	6.78% -1.51%

The Kairanga farm investment is financially viable only at comparatively high levels of production and payout. To return a post-tax surplus, in year I with a payout

of \$6.50, production levels of 450 kg/ha need to be achieved. Examination of return to equity and investment at the most likely production level of 350kg/ha and payout

levels ranging from \$5.50 to \$7.00 show very poor initial returns.

Output from model 2. (financial profitability) is summarised in table 5.2.

Table 5.2 shows the net present value, at 7% discount rate, of investment in the Kairanga properly for best and average scenarios. Examination of the results shows that the investment is only financially profitable with production levels considerably higher than average efficient and increasing payout.

Table 5.2 Model 2. Kairanga

Payout	Per Hectare Production Year 1			
	Good Scenario	300	350	400
\$6.00	(475,147)	(258,548)	(47,259)	1 61,899
\$6.50	(327,118)	(99,297)	125,159	344,347
Average Scenario				
\$6.00	(891,105)	(703,811)	(523,556)	(348,764)
\$650	(733,736)	(537,787)	(347,014)	(160,384)

Appendix 3: Cheltenham

Output from model 1. (financial viability) is summarised in table 6.1.

Table 6.1 Model 1. sensitivity analysis Cheltenham

SENSITIVITY ANALYSIS

To show post-tax farming surplus/deficit with varying payout and production

Payout	Kg milkfat/ha								
	200	250	300	350	400	450	500	550	600
\$4.00	(301,080)	(244,576)	(188,072)	(131,568)	(75,063)	(18,559)	31,145	69,229	107,087
\$4.50	(269,857)	(205,547)	(141,237)	(76,927)	(12,617)	40,583	83,670	126,532	169,162
\$5.00	(238,634)	(166,518)	(94,402)	(22,286)	39,334	87,652	135,579	183,077	230,374
\$5.50	(207,410)	(127,489)	(47,567)	26,896	81,167	134,253	1 86,767	239,163	291,427
\$6.00	(176,187)	(88,460)	(732)	64,235	122,599	1 80,260	237,754	295,047	352,255
\$6.50	(144,964)	(49,430)	36,837	100,572	163,555	226,148	288,528	350,767	412,826
\$7.00	(1 13,740)	(10,401)	68,187	136,653	204,345	271,869	339,183	406,290	473,396
\$7.50	(82,517)	24,064	99,261	172,344	245,071	317,496	389,659	461,813	533,967
\$8.00	(51,294)	51,287	130,145	208,035	285,628	362,933	440,135	517,336	594,527

SENSITIVITY ANALYSIS

To show pre and post-tax farming surplus pre-tax ROI pre and post-tax return on equity

with variation in payout, production of 250 k g/ha

Payout	Surplus/deficit		Pre-tax ROI	Pre-tax ROE	Post-tax ROE
	Pre-tax	Post-tax			
\$5.50	145,323	(127,489)	2.50%	4.16%	-5.64%
\$6.00	1 82,823	(88,460)	3.27%	5.44%	-4.26%
\$6.50	220,323	(49,430)	4.04%	6.73%	-2.89%
\$7.00	257,823	(10,401)	4.81%	8.01%	-1.51%

The Cheltenham farm investment is financially viable at slightly higher levels of production and payout than initially budgeted on. A post-tax surplus is returned at a payout of \$6.50 with production levels of 350 kg/ha and payout levels ranging from \$5.50 to \$7.00 show poor initial returns.

Table 6.2 Model 2. Cheltenham

Payout	Per Hectare Production Year I			
	Good Scenario	200	250	300
\$6.00	(899,984)	(178,996)	519,267	1,196,587
\$6.50	(521,036)	(238,896)	978,483	1,695,233
Average Scenario				
\$6.00	(1,950,530)	(1,356,755)	(767,272)	(202,017)
\$6.50	(1,569,531)	(926,669)	(299,634)	297,527

Output from model 2. (financial profitability) is summarised in table 6.2.

Table 6.2 shows the net present value, at 7% discount rate, of investment in the Cheltenham farm for best and average scenarios. Examination of the results shows that the investment is only financially profitable with average efficient production levels if payout increases.

Leisure Centres in the 1990s

Difficulties in Balancing Social Responsibilities with Profit Motives

by S G Bond

Introduction

Sport and fitness have played an important role in creating and shaping New Zealand's national image. The importance of physical activity to health is well documented and the announcements of the August 1991 New Zealand budget significantly reducing ACC entitlements and shifting health costs onto the individual have reinforced the need for individuals to take responsibility for their own health and safety.

In line with government policy to promote access to sport and fitness for all New Zealanders and in response to the trend toward physical fitness, the number of facilities to accommodate this has grown dramatically. For example, in Palmerston North alone there are around nine fitness centres servicing a population of only 70,000.

America and Canada have been leading the way in terms of the growing popularity of exercise and facilities to service this. Comprehensive health clubs offering a diverse range of facilities from swimming pools and squash courts through to indoor running tracks and creches have become very popular and convenient places to achieve fitness and social goals. These clubs cater to a whole spectrum of exercise

and sporting needs under the one roof. In a climate where wind and rain predominate for many months of the year, as they do in these countries, such indoor sporting facilities appear very attractive compared to the outdoor alternatives.

In New Zealand very few multi-purpose sports facilities exist owing partly to the debate over who should provide them. Those that have been developed are relatively new and have been provided mostly by local bodies. However, over recent years with the growing trend towards a "user pays" philosophy, as well as demand for greater public accountability and more efficient resource management, public provision of such sports facilities has been questioned. Alternatives are being considered.

Part of the debate relates to the ability of local bodies to successfully develop and operate this type of facility. It appears they have tended to lack a commercial orientation as well as the necessary experience and expertise. One alternative to overcome this deficiency is to involve the private sector in some form of joint-venture and employ expertise in the areas of development, marketing and management, which are crucial to the success of the project. Alternatively, the private sector could take over this role altogether.

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This paper outlines research undertaken to determine private development feasibility. The question of public versus private ownership is addressed and an economic feasibility case study of establishing a multi-purpose sports complex is investigated. This is measured in terms of the potential demand for the facility, given the competition from existing facilities and the level of fees that could reasonably be anticipated. The revenues are then correlated with the costs of developing and operating the facility. Given that the facility may be viewed as providing a service to the community, the non-financial benefits are also considered in an attempt to achieve a balance between social responsibilities and profit motives.

Public Provision - The Role of Government

Government involvement in recreation provision can be traced to around the turn of the century when local bodies were providing parks, swimming pools, museums and libraries. However, their involvement has been somewhat erratic and is marked by three major attempts to influence the physical health and welfare of people by encouraging physical fitness and the promotion of physical recreation.

According to Stothart (1981) the first attempt was in 1937 with the creation, by Act of Parliament, of the Physical Welfare and Recreation Branch of the Department of Internal Affairs. This encouraged local government to spend more on recreational facilities. However, the start of World War II combined with a lack of trained leadership, undefined goals, and some incompetent administration led to the

abandonment of some programmes.

The second attempt of the government to become directly involved in recreation began in the late 1960s and early 1970s. The Labour government passed the Recreation and Sport Act 1973 and created a Council for Recreation and Sport as an advisory body. The Council's responsibility was to promote, encourage, initiate and fund sport and recreation programmes and policies for the benefit of all New Zealanders. At this time, most

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facilities comprised council buildings such as town halls and churches which were simply utilised for alternative sporting purposes. It was not until the late 1970s that councils started building specifically designed multi-purpose sport centres, in line with overseas trends.

Two reviews into public involvement in

sport and recreation conducted in 1985 led to the establishment of the Hillary Commission for Recreation and Sport on 1 April 1987. "Unlike the former ministry and council, which obtained virtually all of their resources from government, the commission, being an independent body, is endeavouring to obtain a substantial proportion of its funds from the commer-

cial sector and sponsorship. This change in funding approach reflects a changing attitude in the community which is increasingly challenging the proposition that access to sporting activities is not a privilege but a right which should be guaranteed by the state." (Cushman, 1989, p 142)

What is the Rationale for the Provision of Sport and Recreation Through Public Funding?

It is frequently argued that market failure and imperfections often necessitate public intervention in the market economy.

According to Jensen (1992, p 163) "Increased government expenditure on physical leisure was found to be justified where it led to the fulfilment of one of the following objectives:

- The provision of a good or service which may be described as a "merit good" or a product which the government believes is beneficial and will not be consumed in appropriate quantities without the existence of government assistance.
- A more efficient allocation of resources so that they flow to uses which maximise social welfare.
- The altering of the distribution of income in such a way that it conforms more to the general preferences of New Zealand Society".

Jensen identifies the benefits of policies that increase physical leisure participation as follows:

Savings in terms of reduced health expenditure, additional years of life and decreased incapacity.

Usefulness as a part of programmes to reduce crime.

- The enhancement of the quality of life of New Zealanders by promoting individual well-being, social participation and cohesion.
- Where it leads to international sporting success, physical leisure participation is helpful in marketing of exports and promotion of New Zealand as a tourist destination.

According to Jensen's view consumer preference patterns would not lead to the appropriate allocation of resources required to achieve government's objec-

tives. Public intervention aims at an allocation of resources that deviates from that reflected by preference. Here, economic concern for efficiency takes second place to objectives the community considers more important.

According to Collins (1989) another reason for public involvement in sport and recreation development is that the scale of development is often unavoidably large relative to existing capacity and demand. That is, development often requires a high price per unit for some years before the volume builds up to a larger more efficient level, and so places it beyond the means of most private developers. Also, often the most profitable use of a resource is not necessarily going to be a sporting one. Collins suggests that if it were left to the market process, sporting facilities would not be provided at all.

The Changing Scene: User Pays

The financial recession and severe balance-of-payments problems facing the New Zealand government in the late 1980s led to a control of public spending on welfare. This together with the introduction of a "user pays" philosophy has resulted in the development of a set of guidelines establishing the degree of public funding and its relationship with private and community funding. Cushman (1989, p 143) outlines these in broad terms:

"where the benefit of sport is private and individual, then the cost should remain with the individual; where the benefit is shared by a group such as a club or geographical area, then the cost should be shared by the individual and the group; where the benefit is to the nation's well-being, then the government should share the costs (Sport on the Move, 1985). While in practical terms the implementation of this

"benefit" principle is not being applied strictly, due to problems posed by individual cases, it does nevertheless represent the general policy direction of sports funding in present-day New Zealand."

The intention of a "user pays" philosophy is to help share the financial burden of providing publicly beneficial goods and services. A user charge is considered to be the most equitable way to make a person contribute to the cost of a service. Thus, only those who use the resource are required to pay. Further, this serves as a rationing device whereby consumers who have paid are likely to use resources more efficiently than those who have not. This is particularly significant as the increased importance and popularity of sport and fitness in recent years have placed greater demand on facilities and in turn greater emphasis on resource allocation.

According to Collins (1989 p. 525) "pricing may also make possible a more accurate evaluation of market benefits derived by consumers from sport and recreation, thus assisting planning and allocation decisions at both local and national levels." He notes that levies may also encourage private development where private providers would no longer have to compete with free public provision. However, he suggests that prices need to be set at a level that will ensure maximum efficient use of the resources and that will not work against the achievement of the defined goals.

A factor in determining pricing of a sporting or recreational good or service, Collins suggests, is the extent to which that good or service is considered to fall within the realm of merit goods. He says "This in turn will determine the appropriate level of public finance involved, that is, full public provision versus user pays complemented by public subsidy versus conventional market pricing" p.526.

The Multi-Purpose Sports Complex: Potential for Private Ownership

The multi-purpose sports complex which is the focus of this paper offers an extensive range of facilities including squash courts, weight rooms, restaurants and cafes, swimming and spa pools, saunas, aerobics rooms and other amenities such as in-house specialists, social clubs and massage rooms. These complexes not only cater to a wide range of sporting and recreational activities but are often used to host sporting events, exhibitions, conventions and other visitor-attracting activities which add to the economic base of a region through the multiplier effect.

As mentioned, given the advent of "user-pays" and the general acceptance now by consumers that they will be required to pay for the use of sport and recreational facilities, it is timely for private developers to get involved in the provision of these without having to compete with

what was previously free public access to facilities given by the public providers. Indeed, in this period of government restructuring and privatisation, public providers themselves are now required to compete with private providers in terms of efficiency and cost-effectiveness. It is likely that the most efficient alternative will qualify for, or at least attract public sector financial support.

Private investors are likely to be attracted to facilities that are self funding and where the potential for profit exists. This is certainly the case in the United States and Canada where individuals are willing to pay a lot of money to use or join fitness clubs, and private investment is common (Gimmy and Woodworth, 1989). In New Zealand only the more sport-specific facilities such as squash courts, tennis

clubs and fitness centres are privately provided. Very few examples exist of privately run multi-purpose sports complexes.

Many of the large sports complexes in New Zealand such as those being developed in Upper Hutt, North Shore and Rotorua are owned and operated by local authorities. This reflects not only the huge capital expense involved in establishing such facilities which are often non-economic, but also their service nature. To date, these have achieved limited success either due to poor design or poor management. According to Griffin (1991) even some well designed facilities have failed to work to their full potential simply because Councils have not had a clear philosophy or understanding of how centres should be managed.

Are Multi-Purpose Sports Complexes Economically Feasible? - A Case Study.

It is argued that if these expensive indoor sport and leisure facilities were economically feasible the market mechanism would work to ensure their provision, without the need for the public sector to get involved. A case study of developing a multi-purpose sports complex in Palmerston North was investigated to determine the economic feasibility of this argument.

The multi-purpose sports complex was selected for study as it was felt there is a market for such a facility in Palmerston North, despite the number of smaller facilities available. The reasoning behind this is that a multi-purpose complex as envisaged, meets a specific need for diversity not currently met by existing facilities, through the wide range of activities it provides. Fitness is "faddy" and it has been found that for new participants motivation drops off after about six weeks. Therefore, fitness centres offering other services, activities and benefits such as sports massage, sunbeds, body building and step Reebok classes keep customers interested and are more likely to succeed as a result. Should customers get bored with one activity, there are then others to choose from. Membership levels are considered to be far more stable over time within a multi-purpose complex compared

to the typical fitness centre. However, keeping up with the play in terms of what customers want and new innovations is still vital to success.

It has been shown that demand for fitness services tends to be highly income-elastic. For example, gym membership was reported to have decreased after the share market crash. This finding is important in planning the timing of the development. With New Zealand's economy in the recovery phase, and with the local economic situation in Palmerston North looking healthy and ready to grow, it was considered that the time was right for development.

Without conducting a survey of public perception of charges in order to measure the elasticity of demand or to ascertain the likely level of demand (which was beyond the scope of the study), an economic and demographic analysis of the Palmerston North market was instead conducted to assist in determining demand levels. The potential market was identified together with the likely competition. Once the level of demand and fees had been estimated a site was selected and the overall facility concept established. (Refer to Appendix I and 2 for an overview of the process).

The costs and revenues involved in the project were estimated. Recognising the difficulty in making accurate predictions of likely future events, various scenarios were considered and sensitivity analysis carried out to determine what impact these have on likely returns. The financial criteria upon which the feasibility would be judged was established and applied in a discounted cash flow analysis. (Refer to Appendix 3 for a summary of the statistics).

Adopting a discount rate of 11.5%, the internal rate of return calculated for the most likely scenario was -23.10, indicating that the cash flows plus reversion did not even cover the initial cost over a five year holding period. The Net Present Value was calculated at -\$4,755,333. These results indicated that in terms of purely financial criteria, the centre would not be feasible.

However, given that the facility could be viewed as providing a service to the community the non-financial benefits needed to be considered. A much lower rate of return may be deemed acceptable given the social and political implications of the development. The involvement of a local authority in the ownership and control of the complex needed to be considered.

Public Sector Involvement: Sharing the Responsibilities and Risks

Acknowledging Palmerston North City Council's active role in promoting and encouraging participation in sport and recreation, reflected by the number of facilities it already provides, the proposed facility was seen as an ideal development opportunity for the Council to become involved in. Also, as a result of the Council being in tune with the city plan and community needs, together with its relatively sound financial base and funding sources, it was felt that their involvement would help ensure that the facility would be planned and developed to meet those needs, and that it would have the financial support required to make it work. Thus, Council's involvement in the project was seen to be to the benefit of the city as a whole.

There are a number of possibilities available for the joint control and ownership of a sporting complex as follows:

- (a) Council owns the whole complex, i.e. land and buildings, and leases or franchises it to a body to operate.
- (b) Council owns the land and grants a long term lease to a body which will own the improvements and either

operate the complex or sublease this to another body.

- (c) That the whole complex including land be owned by a body established for that purpose.

A "body" is likely to be set up specifically for the purpose of owning and operating the complex or parts thereof in a way that will enable the Council to obtain a degree of influence. The kinds of "bodies" which could be established for the purpose are

- (i) An incorporated society
- (ii) A company
- (iii) A trust

As an example, the Upper Hutt City Council is working in conjunction with the Rimutaka Community Sports Trust in the design, construction and funding of the Rimutaka Sports Complex. The Council has made land available for the project as well as a financial contribution (funded by way of a loan, the servicing costs being met by community rates levies). The Trust is seeking a grant from the New Zealand Lottery Grants Board to help fund the remainder. The facility ownership/management is yet to be

negotiated between the Council and the Trust. However, regardless of any arrangement entered into, the Council has undertaken to ensure that the facility remains a community asset.

It is recommended that to balance social responsibilities with profit motives a joint-venture between the Palmerston North City Council and a private investor is the best alternative. This will help ensure that not only will a properly designed sports centre targeted to a particular market segment be planned, which is essential to achieve optimum operating results and profitability, but that good management is employed. According to John Hulbert, private developer of Glen Innes and Port Erin Pools, the physical form in itself will not be successful without committed and motivated management teams. From the evidence to date, it does appear that private operations are often more highly motivated than public providers and succeed as a result (Young, 1993). Therefore, by combining resources and expertise a joint-venture is likely to be more successful.

How to Assess Non-Financial Feasibility

It would normally be at the Council's discretion to decide whether the non-financial benefits of the proposal outweigh the financial burden that such a complex would impose. Yet due to recent legislative changes and demand for greater accountability in the public sector, even the councils are required to show a return on assets owned. Inefficient assets are no longer considered acceptable. For example, the Local Government Amendment Act (III) and Public Finance Act, both of 1989 require local authorities to adopt modern accrual accounting procedures to better measure and identify the effectiveness and efficiency of activities. The procedures require the definition and valuation of assets used in carrying out these activities and the reporting of costs associated with these assets.

According to Reid (1991) "The previous mechanism for deciding at which point the Government invested in property was established by the 10% discount rate. Under this guideline the Government expected to receive a 10% return, above the inflation rate, on any capital investment." However, under the new legislation the assets of local authorities are subject to

a "capital charge" which does allow Government to calculate the rate of return appropriate for the type of investment owned, and thus recognises that some specialised or community assets may show a rate of return below what is considered "normal" for non-specialised assets.

Bob Lang (1991, p.1), Director of Property, Manukau City Council, justifies these below-normal rates by saying that it is a legitimate function of a local authority to manage and develop property for the purpose of achieving planning and city development objectives". He says it can be a cost-efficient means of achieving a desired outcome (e.g. the establishment of a reserve or facility)". He believes that the acquisition, development and management of property in all these circumstances must include risk assessment, but suggests that this must be aligned to the goals and priorities of the local authority. However, whilst these "below-normal" rates may be justifiable, they do not provide any guidance for the manner in which valuers employed by Councils should value such assets, as required to under the Acts. This continues to cause

much discussion amongst property professionals.

This has highlighted the real difficulties local authorities are facing. With the change in focus to profitability and accountability they are being required to balance social responsibilities with the need to be efficient and maximise profit in a commercial sense. Property in public ownership, according to McKenzie (1991), now has a multi-purpose role in today's environment, achieving three primary objectives:

1. The provisions of property assets to ensure essential services. Assets such as sewage treatment stations, water treatment stations, road maintenance depots etc., fall within this category.
2. Social and development role. This is the retaining of uneconomic property or the use of cash-flow to invest in uneconomic property on the grounds of social or community benefit. Properties within these classifications would be community halls, libraries, swimming pools, parks, etc.
3. Business and profit role. These are properties held by the council in a purely profit motivated role earning market related rates of return and cash-

flow. This role has been further emphasised by the competition created from the shift in public service provision to the private sector. For example, Cabinet approval has recently been given for the partial privatisation of the prison system. Allowing private contractors to compete in offering prison services will help ensure that such services are supplied in the most cost-effective manner. In turn, this is expected to improve the returns on the land and buildings used to produce those services, which may attract further investment from the private sector.

Valuers face similar difficulties to the local authorities. They are being required to value these assets which are used to provide services in the national interest but that are also now required to show a return. The traditional valuation approaches employed assume that property is purchased and held for financial gain and that it will be utilised to meet that purpose. These methods assess a value figure which reflects a one-sided economic viewpoint only. This has been criticised as

Conclusion

For a multi-purpose sports facility to succeed it must be well planned and researched. A specific target market needs to be identified and the facility purpose-built to meet that market. The facility must be cost-effective, well managed, publicly approved and financially supported. Surveys of public opinion to ascertain their needs and willingness to pay are useful. An economic impact assessment would also be helpful and may aid in avoiding public opposition where they can see the wider benefits to the community of such a facility. It is suggested that with the right mix of public and private sector input this is possible. Young (1993 p.1) recommends that Councils' involvement be more of a coordinating one. The feasibility case study provides much useful information for determining the likely cash-flows involved in developing and operating such a facility. However, as the complex will ideally remain a community asset its feasibility cannot be assessed solely in terms of a "normal rate of return". The non-financial benefits that will accrue to the city must also be considered. Councils must determine what rate of return would be acceptable given the social and political implications of the development to adequately balance profit motives with social responsibilities.

too narrow taking no account of aesthetic, political or utility values.

New methods of valuation are required that take into account the wider issues raised through public accountability and that fully acknowledge the purpose and potential of the assets valued. Further, with the introduction of the Public Finance Act 1989 and more particularly the Resource Management Act 1991 such methods need to reflect the non-marketable intangible qualities of property. This legislation highlights the need to consider the impact of various land use decisions on the environment. In the absence of new methods which encompass non-economic aspects of value the valuation profession shall be required to rely on the traditional approaches.

As part of this discussion, while considering the various aspects of value, it is important to realise that feasibility also has generally been judged from a solely economic viewpoint. The market derived financial criteria used as a yardstick for measuring feasibility is relatively easy to assess. But what of a non-financial

yardstick? How will this be assessed? This is the dilemma facing Councils. They have no clear objectives or methods for determining the overall feasibility of a project and thus no yardstick on which to base their decisions. Councils need to determine to what extent they are prepared to subsidise the project before the financial burden is considered to outweigh the benefits both financial and non-financial. In line with Young's (1993) findings, Councils need guidelines in order to establish specific goals and objectives with feasibility studies which specifically address those taking account of specific constraints and limited resources.

Without these explicitly stated, a feasibility study is futile, the object of which is to determine whether or not a project meets certain criteria. Should the project outlined be determined feasible the advantage of Council and private investors working together is that they can share not only the financial risks but also their resources and expertise.

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Appendix 1

Case Study Overview

The sports and fitness industry in Palmerston North has seen an increase within the last 5-10 years not only in participation due to a heightened awareness of the benefits that can be derived from exercise, but also an increase in the number of facilities to take advantage of this trend.

However, there are no multi-purpose sports facilities currently available in Palmerston North, with the exception of Massey University Recreation Centre. Expectations are that with the addition of a new centre further demand will be generated. The centre, by providing a full range of facilities under one roof, will be able to cater to the needs of families, disabled and sporting groups which are not yet fully satisfied by the existing centres.

While the subject site of 2.9 hectares bounded by Main, Church and West Streets currently has low pedestrian flows, it has high traffic flow and hence a high profile potential. Once developed it is envisaged pedestrian flow from the city will increase, but with customers more likely to come by car or bicycle, due to the "perceived" distance from the city being too far to walk for most.

Due to the lack of statistical information regarding the current supply and demand for sports facilities and the likely future requirements for these, it was difficult to estimate with any degree of accuracy the likely levels of demand for use of the proposed development.

Market indicators such as vacancy and rental levels, retail sales, employment levels, likely demographic changes and convention centre activity were relied on to help estimate the potential demand, and income levels. Likewise, operating cost data was not readily available and reliance had to be placed on general levels for commercial buildings in the Palmerston North CBD, budgeted cost data of the proposed Rimutaka Sports Complex, Upper Hutt, and other sources such as

Rawlinson's Construction Handbook. Despite these limitations development costs and net incomes were estimated under various scenarios and discounted cash-flow analysis applied to determine the returns expected under each of these. Market derived criteria was used to evaluate the economic feasibility in terms of the internal rate of return (IRR), net present value (NPV) and initial return. This clearly indicated that the proposal is not economically feasible. However, the non-financial aspects were considered to determine the project's overall feasibility. As the proposed development meets two important Council objectives:

(i) The development of land specifically set aside for such a purpose,

(ii) The establishment of a facility that will accommodate community needs and compliment the heavily used Manawatu Sports Stadium,

it is considered that the proposal is ideally suited to Council's task.

As a community asset the Council must decide whether the non-financial benefits of the proposal outweigh the financial burden that the complex would impose to determine its overall feasibility. On the basis that they do, a joint-venture between the public and private sectors is recommended to best achieve a balance between meeting social responsibilities and profit goals.

Appendix 2

Case Study: Steps

1. Economic analysis

To help forecast future demand and income potential.

2. Demographic analysis

To help forecast quantity and type of potential demand.

3. Market segmentation

To help define each major type of demand and determine future growth potential; seasonality of demand; facility requirements; price sensitivity etc.

4. Competition

To help quantify level of demand and to price competitively.

5. City description

Identify strengths and weaknesses that may impact on the development.

6. Neighbourhood analysis

To identify the likely impact of this on the development's status; image; style of operation to choose; ability to attract and service a particular market segment.

7. Site selection

The suitability of the site is important to the economic viability of the project and its overall value.

8. Facility concept

A properly designed centre is essential to achieve optimum operating results and profitability.

9. Demand/Average rate analysis

A feasibility requires the level of demand to be quantified and fees to be established.

10. Cost/Revenue estimates

Alternatives need to be considered and checked against market criteria to determine economic feasibility.

11

1. Feasibility

The financial criteria is estimated and the cost/revenue estimates matched against this to determine economic feasibility.

12. A decision is made as to whether the project will be feasible or not.

Appendix 3

Case Study: Summary Statistics

Steps:

1. Economic

Palmerston North has a more diverse and stable economic base than New Zealand as a whole. Education and defence has led the city's growth. Business confidence remains high.

2. Demographic

The 20-29 age group is the largest, followed by the 30-39 age group and over 60s.

3. Market segmentation

Four markets were identified: students; family; business; meeting and convention.

4. Competition

Main competitors: fitness centres; swimming pools; sports clubs.

Average prices:

membership to fitness centres @ \$352pa
casual visit to fitness centre @ \$5/class
Club memberships: squash \$179pa
tennis \$120pa
running \$75pa

Student discounts offered.

7. Site selection

The 2.92 hectare ex-railway land bounded by Main/Church and West Streets has good frontage to main arterial routes; adequate space for expansion; vacant; ready for development; central location; good profile; and appropriately zoned "Future Urban Development".

9. Demand/Average rate

Membership:

families 200 @ \$850pa
students 130 @ \$520pa
over-60s 60 @ \$520pa
other 160 @ \$650pa
casuals 40 per day @ \$6/class
or \$10/visit to facility.

10. Cost/Revenue estimates

Revenue:

membership fees \$372,800
casuals \$55,280
pool hire \$10,000
sports hall hire \$75,000
meeting room hire \$24,000
rental retail areas \$136,250
Total revenue \$673,330

Operating expenses:

administration \$291,400
swimming pool \$145,000
building \$103,194
Total operating expenses \$539,594

Costs:

building \$4,343,218
fittings and fixtures \$178,980
car parks \$210,000
land \$750,000
interest \$296,039
Total costs: \$5,778,237

11. Feasibility

The major variables that have been adjusted include:

- (i) Rate of revenue increase after year three 2.5% and 5% pa
- (ii) Rate of rental growth 0%, 8%. 12% reviewed after three years

Worst Cost/Revenue Scenario

Rev. Inc.	Inflation	Rent Inc.	Total Cost
0%	5%	0%	\$5.80m

Best Cost/Revenue Scenario

Rev. Inc.	Inflation	Rent Inc.	Total Cost
5%	0%	12%	\$5.43m

Most Likely Cost/Revenue Combination Scenario

Rev. Inc.	Inflation	Rent Inc.	Total Cost
2.5%	2%	8%	\$5.43m

As indicated in the table, the most likely cost/revenue combinations fall between the best and worst combinations. Assuming a discount rate of 11.5% none of the scenarios meet this required rate of return.

Finally, an analysis has been carried out to

Scenario with OPEX reduced 20%

- 1. Most likely
- 2. Best

Even with OPEX reduced neither scenario meets the 11.5% required rate of return.

Note that no probabilities have been attached to the various outcomes due to the lack of reasonable basis to determine this.

12. Conclusion

Applying the foregoing criteria to the subject proposal the following results are obtained:

(a) IRR

The most likely scenario, shows an IRR of 23.10 which indicates that the cash flows plus reversion do not even cover the initial cost. Even

(iii) Rate of inflation 2% and 5%

(iv) Initial cost of development - 175 vs 100 carparks

- Land purchase at \$75 per m2 vs \$50 per m2

Therefore - Total cost at \$5.8m vs \$5.43m.

(v) Net present value: Discount rates range from 10-12.5%

To summarise, the best, worst and most likely cost/revenue combinations are shown below.

	NPV @ 11% (\$)	IRR
Worst Cost/Revenue Scenario	-5,968,979	ERR
Best Cost/Revenue Scenario	-4,122,894	-16.39
Most Likely Cost/Revenue Combination Scenario	-4,738,875	-23.10

	NPV @ 11.5% (\$)	IRR
Worst Cost/Revenue Scenario	-5,966,924	ERR
Best Cost/Revenue Scenario	-4,152,641	-16.39
Most Likely Cost/Revenue Combination Scenario	-4,755,333	-23.10

determine the effect of a 20% reduction in operating expenses on NPV and IRR using the best and the most likely cost/revenue combinations. This is to take account of possible errors in the estimation of these items. The results are as follows:

NPV @ IRR

	NPV @ 11%(\$)	IRR
1. Most likely	-3,736,193	-13.44
2. Best	-3,190,331	-7.98

under the most optimistic scenario the project would not meet the required rate of return of 11-11.5%.

(b) Net Present Value

All of the scenarios show negative net present values reflecting the loss over five years that the project would suffer.

The proposal fails to meet the financial criteria of the market and is clearly not feasible. However, non-financial criteria must also be considered before a decision is made to proceed with the proposal or not.

Implications For Property From Trends In Resource Management

by A Crosby

Allen Crosby is Manager of Development Planning for Kingston Morrison Limited, planners, architects, engineers and scientists, of Auckland. He holds a Bachelor of Engineering (Civil) degree, and a post-graduate Diploma of Town Planning. He is a member of the Institution of Professional Engineers of New Zealand and a member of the New Zealand Planning Institute. Allen Crosby has wide experience in urban development and urban renewal in New Zealand and overseas, having played a significant role as Chief Town Planner in the modernisation of Hong Kong in the 1970s and 1980s.

Following the implementation of the Resource Management Act 1991 we are experiencing significant changes in the way we now try to manage our physical resources (including land and buildings) which are affecting the way we attach value to them. These are not only introducing new uncertainties, but, I believe are part of an uneven platform in a continuum of changing resource management.

The Past

Let us look briefly at the past.

Resource Management, or the lack of it, has had a profound affect on the value of property since before people first settled on the land.

The history of cities has been a dynamic cycle of growth, maturity, and decay. Sometimes with rebuilding carried out in a different form on or near the original site. The ancient Indus Valley City of Moenjo Daro (in what is now Pakistan) appears to be a classic case of the transitional nature of past cities in the absence of sustainable management of local resources and the inability to predict, or cope with, relentless natural forces.

In spite of the well-planned city with sophisticated sewerage system, busy port, trading centre and sophisticated society which appeared to be thriving about 2500 BC, Moenjo Daro was practically abandoned by 1500 BC. By 1900 AD, it was buried in silt from accreting shoreline and tectonic upthrusts. Today, there are no signs of the forests or vegetation that would have supported its ceramic industries and affluent lifestyles.

There are many examples of this in the past.

The famous Ziggurat of Ur (from where we get our term 'urban') once dominated a thriving city on the banks of the Euphrates River in the so-called 'Cradle of Civilisation' at about the same time as the Indus cities thrived. It now stands alone and desolate in the salty waste of southern Iraq.

Looking closer to home, Maori migrated to Aotearoa from the tropics about 1,000 years ago to steadily transform the 'treasure chest' landscape destroying much fauna and flora and its value. So much so that, at times, it would have been difficult for them to survive, judging by archeological evidence.

When the 'Pakeha' Europeans started settling here less than 200 years ago, they accelerated the denuding of much of the remaining natural vegetation (often on young, vulnerable slopes) in their determination to establish British pastoral farms in the South Pacific.

This process continues.

Only a few years ago, New Zealand taxpayers were paying for unstable 'marginal land' to be denuded of vital manuka and other stabilising vegetation to increase available farmland for carrying livestock. We are continuing to pay for the aftermath as cyclonic storms and heavy rains take particular toll of these areas - illustrating the high cost of unsustainable land management.

What have we learnt and how are we adapting?

The Present

I will concentrate mostly on the present trends under the following topics:

- The Resource Management Act 1991
- The Objectivity of Sustainability
- The 'Environment'
- The Hierarchy of Controls
- The Types of Activities
- The Criteria for Evaluation
- The Challenges

The [S5 (1)] Purpose of the Resource Management Act 1991

The main purpose of the Resource Management Act 1991 (RMA) is to promote the sustainable management of natural and physical resources.

Sustainable Management

'Sustainable Management' is defined in the RMA as meaning the use, development and protection of natural and physical resources.

In a way, or at a rate, which enables people and communities to provide for their health and safety while:

- (a) Sustaining the potential of natural and physical resources (excluding minerals) to meet the reasonably foreseeable needs of future generations.
- (b) Safeguarding the life supporting capacity of air, water, soil and ecosystems.

- (c) Avoiding, remedying or mitigating any adverse effects of activities on the environment.

Environment

Environment is also defined in the RMA as including:

- (a) Ecosystems and their constituent parts including people and communities.
- (b) All natural and physical resources.
- (c) Amenity values.
- (d) The social, economic, aesthetic and cultural conditions.

Types of Consents

Under the RMA there are now 5 types of resource consents.

Namely:

- 1) Land Use Consent
- 2) Subdivision Consent
- 3) Coastal Permit
- 4) Water Permit
- 5) Discharge Permit

Categories of Activities.

In:

- 1) Permitted Activity
- 2) Controlled Activity
- 3) Discretionary Activity
- 4) Non-Complying Activity
- 5) Prohibited Activity

Criteria for Evaluation of Consents

The RMA actually specifies at least 17 different criteria which consent authorities are required to observe in the processing of their regulatory instruments or applications for resource consent: These are under 4 different categories of each of different status or significance.

Namely:

- a) Sustainable Management
The Main Purpose (involves 4 different elements).
- b) Treaty of Waitangi
To be taken into Account as a special section of National priority.
- c) Matters of National Importance
Five such matters which are required to be recognised and provided for.
- d) Other Matters
'Particular regard to' 8 other matters are also required. These are:
 - Kaitiakitangi (guardianship)
 - Efficient use and development of natural and physical resources
 - Maintenance and enhancement of amenity values

- Intrinsic values of ecosystems
- Recognition and protection of the heritage value of sites, buildings, places or areas
- Maintenance and enhancement of the quality of the environment
- Any finite characteristics of natural and physical resources
- Protection of habitat of trout and salmon

Matters of National Importance

The matters of national importance which must be recognised and provided for are:

- a) Preservation of natural character of coastline
- b) Protection of outstanding natural features and landscapes from inappropriate subdivision use and development
- c) Protection of areas of significance
 - Indigenous vegetation
 - Habitats of indigenous fauna
- d) Maintenance and enhancement of public access to and along coastal marine areas, lakes and rivers
- e) The relationship of Maori and their culture and traditions with their:
 - Ancestral lands
 - Water
 - Sites
 - Waahi Tapu
 - Other Taonga

The Challenges

I see the following challenges currently facing property valuers in New Zealand because of the current statutory approach to resource management:

- Inconsistencies from lack of national policies
- Greater uncertainty with use of performance standards
- Greater uncertainty with variations of types of plans
- Delays from demands for further information
- Additional costs from daunting lists of conditions
- Uncertainties and liabilities from contaminated sites
- Limitations on coastal development
- Increased caution on environmental management with personal liability
- Increased value of coastal areas.

The Future

What of the future for resource management in New Zealand? I foresee:

- Greater diversity of controls
- More national policies
- A national coastal policy statement (which is under action)
- A national regime for managing hazardous substances (which, we are advised, is also under action)
- Greater monitoring and review of consents
- Amendments to the RMA
- Changes to regional policies and district plans to conform to national policies
- Increase in private changes to district plans
- Increased pressure for sustainable farm management
- Greater emphasis on social and human resources
- Realisation of limitation of statutory controls
- More creative developments for permitted and controlled uses.

In respect of greater monitoring and review of consents I refer to the recent publication: 'Investment Certainty under the RMA' released by the Ministry for the Environment, and recommend that all valuers obtain, study and comment on this.

Conclusions

In conclusion, I consider that:

- We are undergoing major changes in the way we attempt to manage our natural and physical resources and this will have increasing impact on the values we attach to property.
- There will be an increasing degree of uncertainty in some districts as new types of statutory instruments are tried and more emphasis is given to assuming environmental effects and more reliance is placed on performance standards.
- There will continue to be uncertainty with the responsibilities and values of possible contaminated sites until most are properly audited and cleaned up.
- There needs to be greater cognisance and integration of the social and human resources and costs before fuller realisation of sustainable management of resources can be achieved.
- There will continue to be changes and uncertainties in resource management but the long term risks can be minimised by striving towards more sustainable management.

TUHOIOIOSY

fORUM

Compiled by Ian Mitchell

Welcome to the second edition of Technology Forum. In this issue, articles cover aluminium joinery maintenance, building technology, and DOSLI's digital cadastral database, information technology. I am sure you will find these articles interesting.

Don't forget, if you have a particular skill or knowledge in a technology

related field, I would be interested in hearing from you or receive any articles you may wish to submit for publication in Technology Forum. I can be contacted at Darroch & Co PO Box 27 133 Wellington, (04) 384 5747 or through the NZIV national office.

Ian Mitchell

DOSLI's Digital Cadastral Database. Access to Digital Cadastral Data for New Zealand Nears Reality

by D Crowe

A giant digital map of surveyed land parcel boundaries in New Zealand is nearing completion. The digital map known as the DCDB (Digital Cadastral Database) includes details on more than 1.8 million individual land parcels. Data from approximately 18,000 paper record maps has been converted into digital format by the Department of Survey and Land Information (DOSLI).

What is the DCDB?

The DCDB or Digital Cadastral Database is designed as an integrated Geographic information System. It is orientated towards the storage, manipulation and output of spatial information, rather than merely being a map production system or an extended computer aided draughting tool. It has the ability to combine data sets originating from different sources, to process and present data, to update and modify data and to manage that data for informed land management.

The functions of the DCDB are:

- to provide an information system for use within DOSLI with

efficiencies in access, distribution and maintenance over existing manual systems

- to provide integration with other related data sets and outputs for the wider GIS/LIS community.
- to provide the spatial component for Land Information Systems (LIS) in New Zealand

Its Content.

The DCDB records the geographic location of land parcel boundaries, legal roads, railways and waterways, and includes statistical mesh blocks from Statistics New Zealand.

Linked to each land parcel is a range of attribute data including legal description and area, street address, reference to survey plan of definition, the status of some government held land and mesh block number.

The database also holds administrative boundaries such as electoral/regional authority, local authority, ward etc. These are derived from the mesh block layer, are

related to the cadastral boundaries and are consistent with statutory definition.

The spatial data contains a hierarchy of "source codes" to advise on the accuracy of all boundary positions. Our original goal was to build a graphical digital database with an overall accuracy of one metre in urban areas and ten metres in rural areas in relation to the surveyed position of boundaries. Our priority to complete the database as quickly as possible has meant that accuracy greater than this has only been achieved in some places. Efforts to continually improve this to half-metre accuracy or better using new

survey information, including the use of Global Positioning Systems (GPS) are continually being made through the addition of new data and special projects. The data is structured into many layers and networks and then further broken down into separate feature codes with unique feature identifiers for every data element in the database. This allows the data to be organised in a logical manner which helps simplify and clarify data relationships and enables the user to better understand and analyse the data.

Its Uses.

The DCDB will be used for a variety of applications that extend beyond the Department's internal requirements. It is a key component to central government's initiatives in building a national Land Information System (LIS). Matching land data records from Valuation NZ, the Land Titles Office, the Maori Land Court and the DCDB is now occurring in Auckland. The outcome of this exercise will see a pilot LIS emerge and the development of a public graphical index inquiry system to increase access to these land records.

Computerisation of the cadastral records offers greater flexibility and improved efficiency in handling both digital and hard-copy outputs. The beauty of the system is that users of the data can customise it for their own use and integrate it with other digital databases such as location of utilities, natural resource patterns and so on.

For example, a local authority might want to attach information such as zoning or

land use classification, owner or occupier names etc to individual properties. Or a real estate agent may wish to link sales information, movements and property availability to street address location to better manage their business.

Inquiries using data from the DCDB and combined with other data sets could graphically portray distribution of property sales, distribution of property by capital value, proximity of properties to amenities - there are many possibilities

Its Availability

Data from the DCDB is available right now through three types of outputs.

- Reports or listings of textual data can be produced containing all or selected attributes over all or selected parts of the database.
- Hard-copy plots for a wide variety of graphic products containing user specified features to user defined scales and format are available.
- Digital data comprising any combination of spatial and attribute data are available. The data can be modified to suit user needs and can be translated to a variety of software platforms. Digital data is released under a licence agreement.

Public On-Line Access

While data from the DCDB is being used in a variety of applications by many local authorities, gas water and electric utilities, private property developers and other public and private sector organisations, it is not yet accessible through an on-line

system. DOSLI expects to have on-line access operating in a pilot site in Christchurch by the end of this year. The pilot will mean that for the first time users of spatial land information - including the public - will be able to access the department's cadastral records via a computer terminal. This will eliminate waiting for a paper record map being used by someone else and will enable instant multiple user access to all data in the system.

Once the pilot system has completed trials in Christchurch the facility will be extended to all our Departmental offices. Eventually it will be possible to extend on-line access to the likes of real estate companies, land survey companies, local authorities, insurance companies and other large organisations.

Enquiries about any of the above can be made at any office of the Department of Survey and Land Information.

Author Profile.

Doug Crowe holds the position of Director Cadastral Database in The Department of Survey and Land Information. He is responsible for the development and implementation of a Digital Cadastral Database (DCDB) for New Zealand, a project he has been working on for the past ten years. During this period Doug has also worked closely with developments for a national Land Information System (LIS). He has a wide background in New Zealand's cadastral mapping and land titles systems.

Aluminium Joinery

Is It Really Low Maintenance?

by Robyn A Phipps, BBSc BArch hons.
Agricultural Engineering Dept. Massey University

In the last twenty years aluminium joinery has gained considerable market appeal under the guise of being a cheap alternative to timber, durable, and a low maintenance material. Indeed this is the marketing approach of many aluminium joinery manufacturers, but is this the whole picture? Recent cases where the joinery has

corroded and required premature maintenance or complete replacement, have drawn attention to the need for a greater understanding of the foibles of this product. This paper outlines the causes, warning signs and preventive measures which should reduce the incidence of corrosion.

Aluminium *Au Naturale*

Aluminium bare of any protective coatings is called "mill finish". It is recognisable by a silver surface, which readily dulls when exposed to air. In most climatic conditions it will develop a dark surface discolouration and a rough pitted texture. This doesn't necessarily mean the bulk of the material has any structural or weather-tightness fault, but the appearance is certainly downgraded. The exposed aluminium is also vulnerable to corrosion from other incompatible materials. Fortunately few New Zealand manufacturers supply mill finished aluminium.

Surface Finishes

Most aluminium joinery is supplied with a factory applied surface finish either anodising or powder coating. Both finishes have merits and limitations, depending on the thickness of the coating and the environment to which it is exposed. Both finishes require regular maintenance to prolong their appearance. Anodising is the process of chemically thickening the natural oxidising surface film. This gives a thin, dense "barrier" layer, topped by a thicker, porous coloured layer and a sealer coat. The plain anodised material has a satin silver appearance, or a dye can be added to the process which can give a limited range of colours, typically shades of bronze, or black. Other colours are generally recommended for interior use only, by the Architectural Aluminium Association, due to cases where the dyes have been susceptible to differential fading.

The thickness of the anodised film can be varied. Typical thicknesses are between 13-24 microns. Generally a thicker anodised film gives more protection, however the airborne chemicals which attack unprotected aluminium can still attack anodised aluminium in some conditions.

Anodising cannot be touched-up to cover any film damage. It is often good insurance to pay for a protective coating to cover the anodising while the frames are being transported, stored or installed on site. If damage occurs then the choices are limited; completely replace the anodised item, paint in-situ the whole frame or live with the damage.

Powder coating is formed by fusing a powder resin onto the metal surface and then oven curing. This gives a deep glossy paint finish similar in appearance to wet

applied paint, but it is generally much tougher and more durable. It may have a slight orange-peel finish, and the range of colours is reasonable although not extensive. Powder coating is more resistant to alkaline and acid materials than anodising, but can still be damaged at the cut ends and attacked by concentrated cleaning materials.

Touch-up paints are available, but these are formulated and applied in a differing process and can be expected to weather differently so the original match may be lost.

As with all paint finishes, powder coating can eventually be expected to fade, dull and caulk, especially in strong sunlight. Frequently the north and western facing joinery requires earlier attention than shaded joinery.

Danger points

Sharp corners are most vulnerable to surface degradation, particularly for anodised surfaces. The early sign that attention is needed is a lighter coloured strip on the exposed edges where the coating has worn thin. Cut ends, corners and drainage holes are should be carefully checked for signs of deterioration. Another vulnerable situation is the sloping frames of conservatories, roof lights and garden windows. In these situations the slope may permit a thin film of water to sit before evaporating. Both the water film and any salts left after the evaporation can accelerate surface deterioration.

Incompatible Materials

Aluminium is corroded by some other metal and by alkaline materials.

The common metals which cause aluminium to corrode are copper, brass, bronze and thinly galvanised mild steel. All of these metals should be isolated, including; traces of the offending metal borne in water runoff from claddings, flashings, spouting, solder etc. Even copper that is present in CCA (copper chromium arsenate) treated timber will cause aluminium to corrode if in contact.

Alkaline materials also cause particular concern. These include concrete and mortar, the runoff from up to three months old masonry, and bird-droppings. If aluminium comes into contact with wet cement products it should be washed immediately. The Architectural Aluminium Association also list other aggressive agents as "certain timbers in damp or

newly treated form, plaster, dust, paint, lime, chemical stains or other contaminants present during building operations".

Anodising and powder coating reduce the risk of corrosion, however any scratches in the finish, cut ends, corners, drilled drainage holes which are not coated with a finish, crevices which retain salts, areas which are sheltered from rain washing and proximity to incompatible materials all present locations susceptible to corrosion.

Maintenance and Refurbishment

To maintain a satisfactory appearance of the joinery and the integrity of the coating and the aluminium, it is important that the whole frame should be washed with mild detergent and water every six months. In coastal environments and where the joinery is protected from rain washing, this should be increased to up to every month. This is particularly important for anodised finishes.

Regular washing will extend the life of the finishers. However, all materials deteriorate with time. BRANZ studies have shown that anodising and powder coating finishes will require refurbishing after 12 to 20 years. Discolouration, fading and chalking are amongst the first indications that refurbishment is required.

If the finishes, especially powder coating, are severely deteriorated then expensive and time-consuming preparatory work is required prior to refurbishing.

Refurbishment treatments include, thorough washing, thorough sanding and the application of a vinyl etch primer followed by an in-situ wet paint system. Paint systems which are recommended for recoating aluminium joinery include acrylic alkyd-based enamel, acrylic-urethane or polyurethane. Manufacturers usually recommend one of the urethane systems as they are more durable and tougher, but they are also more expensive.

The life of the refurbished paint will depend on the exposure to aggressive elements and the standard of maintenance. BRANZ suggests the approximate life expectancy as follows:

Alkyd-based enamel	4 - 5 years
Acrylic	10 years
Urethanes	10 - 15 years

From here on the paint finish will require ongoing recoating and much of the original appeal of the low maintenance product may be lost.

Legal Decisions

Valuation of land subject to cross leasing arrangements for calculation of annual rental Renewal of Glasgow leases Relevance of potential or realised cross leasing in valuation Calculation of fair annual ground rent of the land demised Whether cross leases are "improvements" - Assessment of cross-leases for different rents - Valuation of Land Act 1952, s 2; Valuation of Land Amendment Act 1970.

In The Court Of Appeal Of New Zealand

C.A. 248/93

Under the Declaratory Judgements Act 1908

In The Matter of Lease No. 264241

Between The Hawke's Bay Regional Council a regional council duly constituted under the Local Government Act 1974, of Napier

Plaintiff

And Maxwell Charles Plested Napier, Registered Valuer and Heather

Jane Plested his wife

Defendants

Coram: Cooke P,
Casey J.
Hardie Boys J.

Hearing: 24 November 1993

Counsel: L.H. Chisholm and M.B. Lawson for Appellant R.P. Wolff and G.L. Lang for Respondents

Judgment: 17 December 1993

Judgment Of The Court Delivered By Cooke P.

This is a test case relating to the relevance or otherwise of cross leasing arrangements when valuations are made to fix rentals on the renewals of Glasgow leases. By a proceeding commenced in the High Court on 3 June 1993 the Hawke's Bay Regional Council applied for certain declarations. On 14 October 1993 Doogue J. ordered the removal of the proceeding into the Court of Appeal pursuant to the Declaratory Judgments Act 1908, s.7.

The Council as successor to the Hawke's Bay Harbour Board has vested in it 1553 sections, most of them used for residential purposes, which are subject to perpetually renewable leases. Of those sections, 207 have now been cross leased into 563 separate residential units. One such section is lot 31 on deposited plan 12692, 761 square metres more or less, being all the land in certificate of title E1/53 (Hawke's Bay Registry) and being subject to lease 264241 ('the head lease')

whereunder the defendants, Mr and Mrs Plested, are current lessees. The relevant lease is for 21 years from 16 November 1971 with perpetual rights of renewal for terms of 21 years.

In or about 1973 three semi-detached residential flats were erected on lot 31. On 26 January 1987, with the consent of the Harbour Board as the then lessor, cross leases were registered for the purpose of creating separate leasehold estates for those flats. Composite certificates of title were issued in the Hawke's Bay Registry of the Land Transfer Office for the flats, numbered respectively L4/365 for flat 1, L4/366 for flat 2, and L4/367 for flat 3. It is necessary to go into the mechanics of the cross leasing. In this case they were as follows. It is convenient to omit references to Mr and Mrs Rawcliffe who were previously co-lessees with Mr and Mrs Plested.

The Conveyancing Structure of the Cross Leases

On the fee simple title E1/53 now vested in the Council a memorial was entered that the following leases of lease 264241 to the Plesteds are vested in them as tenants in common in equal shares for a term of 5 years 11 months and 3 days commencing on 12 December 1986. Three leases are then enumerated; they are thus subleases expiring one day before the expiry of the head lease. For each there is given a lease number, a flat number, a flat plan number and a composite title reference. It is noted that the composite title 'includes 1/3 share in leaseholds' and that there are rights of renewal. Variations and extensions of terms have since been recorded - the head lease being extended to and including 16 November 2013 and the subleases being extended to and including 15 November 2013. That is the current state of the fee simple title, and there can be no doubt that it shows that the persons in whom the composite titles are vested are sublessees' each with also a one-third share in the head leasehold.

Of the composite certificates of leasehold title, that relating to flat 1, CTL4/365, may be taken as an illustration. It shows the parent certificate of title and the lessor's title as E1/53 (the Council's fee simple certificate) and the lessee's title is given as registered lease 264241. The composite certificate has its own lease number, 472062.3. It certifies that the Plesteds are seised of an estate of leasehold in the 761 square metres being lot 31 on deposited plan 12692 as tenants in common in equal shares as to an undivided one third share. The composite certificate goes on to

witness that the Plesteds are seised as tenants in common in equal shares of an estate of leasehold '(subject as aforesaid)' create by lease 472062.3 for a term of 5 years 11 months and 3 days commencing on 12 December 1986 in flat 1 on deposited plan 19912. The quoted words in brackets are customary general words in a certificate of title under the Land Transfer Act 1952. In this case they have particular relevance to a memorial on the composite title recording that the head leasehold estate is subject to 'the following subleasehold interests', the three subleases then being specified. The other composite titles follow the same pattern. At present the Plesteds remain the sublessees or cross lessees, not having assigned the rights pertaining to any of the flats. We were informed from the bar that Mr and Mrs Plested do not live in the property but let the flats.

The plan on the composite title is a reproduction of deposited plan 19912 and is a flats plan. It shows the whole of the land in lot 31 on deposited plan 12692 and how that has been dealt with by delineating the three flats and their appurtenant areas and the common areas. Subsequently the variations and extensions of the head lease and the subleases have been registered on the composite title as on the fee simple title.

The registered sublease or cross lease of lot 1 may likewise be taken as an example. It begins by describing the lessors, the Plesteds, as tenants in common in equal shares of the whole leasehold under lease 264241. It describes the lessees (i.e. the sublessees) as the Plesteds as tenants in common in equal shares of 'land and flat' described as flat No.], certificate of title L4/365, on deposited plan 19912 'which is part of a building erected on the said land, comprising flats Nos. 1, 2 and 3...' It states the term as the 5 years 11 months 3 days already mentioned. The covenants conditions and agreements set out in

certain schedules are part of the lease (i.e. the sublease) and there are definitions of 'flat share' and 'land share' in terms of one third shares.

The scheduled covenants conditions and agreements are extensive. A key provision is a covenant by the lessee (i.e. the sublessee) not without the written consent of the lessors (i.e. the sublessors) to use or enjoy any part of the land except the flat and an appurtenant area and an access area - the latter only for the purposes of reasonable ingress and egress by vehicle or on foot. It is material to note also that the sublessee covenants to remain the owner of a land share in the head leasehold while he continues to be a sublessee under the sublease; and to pay all charges and rates separately charged or levied in respect of the flat and the sublessee's undivided share in the leasehold or, if there are no separate charges and rates, then to pay to the sublessors the sublessee's land share of the charges in respect of the whole. Among the mutual covenants is clause 31(b) -

- (b) Lessee to pay share of Head Lease rental

That the Lessee will upon demand in writing by the Lessors pay to the Lessors or a person nominated by the Lessors a Land share of the rental from time to time payable under the Head Lease and any other moneys by the Lessors in the performance of their obligations thereunder or in or about any renewal thereof as hereinafter provided.

There are various other references to the terms of the head lease, all of them confirming that the grant and contract are essentially of and for a sublease with associated rights in the head lease.

The Provisions of the Head Lease

The relevant provisions of the head lease as to valuation are as follows:

10. That not earlier than nine calendar months and not later than three calendar months before the expiry by effluxion of time of the term hereby granted (if such term shall not have been previously determined by forfeiture or otherwise) the Board shall cause two (2) separate valuations to be made by a person whom the Board reasonably believes to be competent to make the valuation the aforesaid valuations being -

- (a) a valuation of all improvements as

defined in Clause 32 hereof then on the said land hereby demised.

- (b) a valuation of the fair annual ground rent of the said land hereby demised not taking into account the improvements as defined in clause 32 hereof so that the rent so valued shall be uniform throughout the whole term of the renewed lease.

32. THAT in this instrument the word "improvements" shall (save as herein-after provided) be deemed to have the same meaning as is given to that word in "The Valuation of Land Act 1951" as amended by Section 2 "Valuation of Land Amendment Act (No.2) 1970".

In relation to the 21 year term of the head lease which began in November 1992 the parties are agreed that there are three possible methods of valuing the land in the process of calculating an annual rental, namely:

1. Ignoring cross leasing and potential, \$33,000 land value.
2. Including potential for cross leasing, \$36,000 land value.
3. Including realised cross leasing, \$54,000 land value.

Neither side contends for the first method. Clearly the potential of the site for lawful cross leasing falls to be taken into account, just as would zoning. It seems that the Harbour Board had and now the Council have a policy of ignoring cross leasing potential where there is only one dwellinghouse on the site and no cross leases. The Court has not been asked any question regarding this policy and no more need be said about it.

The choice is between the second method, which is propounded by the defendants, and the third method, which is propounded by the Council.

Prima facie the answer is straightforward. What is required is 'the fair annual ground rent of the said land hereby demised not taking in account the improvements as defined in clause 32 hereof...' The process of ascertaining the land value and applying thereto a percentage such as five percent is common, although not obligatory in law (see *Wellington City v. National Bank of New Zealand Properties Ltd* [1970] N.Z.L.R. 660) and has been followed by the valuers in this case. In principle it should make no difference for the purpose of the argument if some other process were followed, for it is still the fair annual ground rent of the *land hereby demised* that has to be ascertained.

In principle the demised land is the land in which the head lessor has the fee simple. It is axiomatic that the existence of the head lease itself must be put out of account. What has to be ascertained is the fair annual value of a lease of the fee simple; it is not a valuation of the lessor's interest or the lessee's interest under the head lease. The law has repeatedly been so stated. See for instance *Cox v. Public Trustee* [1918; N.Z.L.R. 95, 101], a decision of a Full Court of the Supreme Court delivered by Hosking J; in *re an Arbitration between Napier Harbour Board and Faulkner* [1930] N.Z.L.R. 184, 189, per Myers C.J. in the Supreme Court, *Valuer-General v. Lalich* (Hamilton High Court M.466/79: judgment 18 December 1981), a decision of the Administrative Division delivered by Bisson J. And if the head lease, in which the cross lessees have acquired interests, has to be put out of account, the same must apply to the subleases or cross leases whereby they have acquired further interests at the same time. The cross leasing is a mode of dealing with the head lease and is totally dependent on the head lease for its existence. Such was the gist of the argument presented to us for the defendants by Mr Wolff. *Prima facie* the argument is sound in principle and supported by authority. Unless there are compelling reasons to the contrary it should be accepted.

For the Council Mr Chisholm laid stress on the accepted fact that the existence of cross leases results in increased market value. That begs the question, for one has to go on to ask the market value of what? In truth the market value is of the land with the leases, which is not the value to be ascertained.

Mr Chisholm also stressed that the cross leases are not 'improvements' within the definition in the Valuation of Land Act 1952, s.2, as amended in 1970. That does appear to be correct under both the original 1952 definition and the amended definition. But it is fallacious to suppose that the cross leases are therefore part of the land or relevant to the value of the land for the purposes of the head lease. Such value as they have either is absorbed into the values of the flats and the property as a whole or is the value of assignable rights in and under the head lease. *McKee's* case, now to be dealt with more fully, supports this conclusion in principle.

In *McKee v. Valuer-General* [1971] N.Z.L.R. 436 our predecessors in this Court were called upon to decide whether a

conditional use consent for multi-unit flats, which was taken to relate to the construction of particular buildings and had been duly implemented by building, should be taken into account for Government valuation purposes in assessing the unimproved value of the land. The answer was in the negative. (A passage in *Elwood v. Valuer-General* [1989] 1 N.Z.L.R. 554, 559, a case to be discussed shortly, is incorrect in stating the decision in *McKee's* case.) The decision was that in assessing the unimproved value the valuer must put the consent on one side as if it had not been obtained, and assess the value of the land without it but with the chance of obtaining such consent. In their joint judgment Turner and Richmond JJ. at 444-5 said of a conditional use consent not yet acted upon:

It may of course possibly happen that the valuation is made at a stage where consent to conditional use has been obtained, but the buildings have not actually been commenced. In such a case, depending possibly on the terms of the consent, it may be that the owner is in a position virtually to assign the benefit of the consent with a transfer of the land. If this is possible, no doubt the price which he receives will reflect the value to the purchaser of the consent. But this still does not mean that the value of the consent is to be ascertained and included in the unimproved value. Nor on the other head does it mean that the consent is an "improvement". The consent already obtained is something not to be included at all in assessing the unimproved value. The valuer must put the consent on one side, as if it had not been obtained: and assess the value of the land without it, *but with the chance of obtaining another similar one.*

When the question of the valuation of Lady McKee's property came again to this Court as *Re 110 Martin Street, Upper Hutt* [1973] 2 N.Z.L.R. 15, it was necessary to decide whether any alteration should be made in the agreed capital value in the light of the judgments at the earlier stage and statements therein that the consent was not an 'improvement'. The Court now decided, in a judgment delivered by McCarthy J., that no change needed to be made, as the value of improvements was a residual figure, it being neither necessary nor desirable to attempt to value the improvements individually or collectively. Thus, while an argument at the first stage that a conditional use consent was analogous to a hotel

licence was (no doubt rightly) rejected and condemned as 'ingenious' (see [1971] N.Z.L.R. at 439 and 446), the McKee litigation establishes that for Government valuation purposes a conditional use consent is not part of the unimproved value but is either subsumed in the value of the improvements or a right not within the scope of Government roll valuations. Insofar as the case provided any analogy, it therefore, helps the defendants rather than the Council in the present case.

At first sight the decision of this Court in *Elwood v. Valuer-General*, already cited, is more helpful to the Council. It again was a Government valuation case, but it related to a cross leasing of the fee simple. The appellants, having respectively an undivided one third share and an undivided two thirds share in the fee simple of residential land, cross leased to themselves for the purpose of occupying separate flats and garages. The Court, in a judgment delivered by McMullin J, held that the system of cross leasing provided the benefits of a limited method of subdivision and should in principle be treated in the same way for valuation purposes as if it were a subdivision, on which view the realised potential fell to be taken into account in assessing land value for Government valuation purposes. But in that case the Valuer-General had assessed the two flat and garage properties as separate properties: see the report at 557. The passage just cited in the judgement records that there were in that case two separate leasehold certificates of title and two separate fee simple certificates of title. As is apparent from the figures given on the same page, the assessment was of the augmented value of each fee simple interest. The judgement does not specify the Valuer-General's authority for valuing on the basis that there were two separate properties, but from the written submissions lodged for him in that case it emerges that he relied on the general reference to 'each separate property' in what is now the Valuation of Land Act 1951, s.8(1). Section 8 (2), referring to land 'capable of separate occupation', had not then been enacted. The important point is that these references to 'each separate property' and 'land capable of separate occupation' have no counterpart in the head lease in the present case.

In the present case the ability of the Valuer-General to treat the cross leased flats as separate properties is not in issue. If he does so, *Elwood's* case may be in point, subject to the consideration that here the cross leasing is of a leasehold interest,

not a fee simple interest. But *Elwood* was not a case on the interpretation of a head lease. It is accordingly distinguishable, for the rights of the parties to the head lease must be governed by their contract and the established principles relating to such contracts.

Consequently we do not consider that in arriving at the fair annual ground rent the Council is entitled to have taken into account the added value conferred on the property by the cross leasing scheme carried out by the defendants. What can be taken into account is the potential for cross leasing. The agreed figures applying to this case have already been given.

Reference was made in argument to the judgment of Gregg J. in *Valuer-General v. Radford* [1993] 3 N.Z.L.R. 721. The main issue before the Judge in that case was whether the burden of existing leases should be taken into account in valuing the fee simple interest for the purposes of the Valuation of Land Act 1951. That again is not an issue relevant to the present case. Insofar as Gregg J. held that redevelopment potential was properly taken into account, his judgment is in accord with the present judgment.

We were referred, but without detailed argument, to the history of local authority control of cross leasing. The provisions mentioned included the Local Government Act 1974, ss.271 and 314 (both now repealed.); the Resource Management Act 1991, ss.218, 407, 408, 412 (the latter now repealed) the Resource Management Amendment Act 1993, ss.193 and 196. Counsel for the Regional Council said that henceforth new cross leases are classified as subdivisions and require resource consents. This is apparently so. The ease or difficulty of obtaining such a consent, and any likely conditions, would be relevant in assessing potential, but otherwise the varying extent of local authority control in the past and in the future does not affect the conclusions that we have stated.

There remains one other major issue. It is whether the Council can directly assess the cross lessees for different rents, treating the three cross leased flats as separately assessable and of values differing because of their positions in the building and on the site. As between the Council as head lessor and the other parties to the head lease as lessees (who will include all authorised assignees sharing in the head leasehold estate) each lessee is liable for the full rent. There appears to be no reason, however why the Council

should not demand different portions of the total ground rent, if properly assessed as already explained, from the various head lessees as they are from time to time. The contrary was not argued. Their rights *inter se* are governed by clause 31(b) in Schedule D to the cross leases, which has been set out previously. For practical purposes the Council's differentiation will normally be decisive against the various lessees in any issue between them and the Council.

Issues between the lessees from time to time are outside the scope of the present proceeding. There is no reason why a differentiation made by the Council should not be accepted by them by consent; but it would not be appropriate in this proceeding for the Court to say more.

The statement of claim propounds a number of specific questions. The answers that can in our opinion be given appear

sufficiently from his judgment. We do not think it appropriate to give any further answers.

The case will be determined accordingly. There will be no order for costs, as an arrangement has been reached.

Solicitors:

Willis Toomey Robinson, Napier, for Plaintiff

Elvidge & Partners, Napier, for Defendants

Rental arbitration Whether to set aside umpire's award Whether the umpire made errors in law Determination of "current market rental" - Whether objective or subjective assessment required Whether consideration of comparable lease terms required.

In The High Court Of New Zealand
Wellington Registry

C.P. 740/91

In The Matter of the Arbitration Act 1908
Between Continieau Investments Limited

Plaintiff

And Telecom Corporation Of N.Z. Limited

Defendant

Hearing: 7 October 1993

Counsel: J.O. Upton Q.C. for plaintiff
I.D.R. Cameron and P.W. Michalik for defendant

Judgment: 20 October 1993
Judgment Of Barker ACJ

This is an application under the Arbitration Act 1908 ('the Act') to set aside or alternatively to remit the award of an Umpire delivered in a rental arbitration. The defendant entered into an agreement dated 14 March 1988 to lease an office building in Lower Hutt for a term of 12 years from 17 July 1987 with a right of renewal for 12 years. The then landlord was Chase Wellington Properties Limited. The present plaintiff is that company's successor in title.

The lease is a very comprehensive document. It provides for an annual base rental for the first three years with rent reviews due on 17 July 1990, 1993 and 1996. The base rent may then be increased in accordance with the provisions of the lease. A "ratchet" clause provides that the rental for a renewed term is not to be less than the rental currently being paid. The lessee has to pay the operating expenses of the building.

The document sets out an elaborate procedure for rent reviews; the goal of the

procedure is to ascertain the "current market rent" an expression found several times. Disregarding provisions about time limits, the procedure can be summarised thus. The lessor must first notify the lessee of the lessor's assessment of the current market rent for the purpose of any forthcoming review. If the lessee does not agree with that assessment, then the lessee may make a counter-offer. If that is not accepted by the lessor, the parties are required to enter into negotiations to resolve the dispute. If these negotiations are unsuccessful, then the parties have to appoint valuers "to jointly determine the current market rent of the premises". Before proceeding to make their determination, the valuers are to agree upon and appoint an umpire. There are machinery provisions for selecting an umpire in case the valuers do not do so. If the valuers are unable to agree on their determination, then "the current market rent" shall be determined by the umpire, whose determination shall be final and binding on the parties hereto. The umpire is required to have due regard to any evidence submitted by the valuers as to their assessment of the current market rent of the premises and shall give his determination and the reasons therefore in writing.

The following provision states matters which shall be both disregarded and regarded by the valuers and the umpire -

- "(1) In determining the current market rent, the valuers or umpire shall:
- (i) be deemed to be acting as expert(s) and not as arbitrator(s).
 - (ii) disregard:
 - (aa) the value of any goodwill attributable to the Lessee's business and the value of the Lessee's fixtures and fittings in

- the Premises
- (bb) any interest in the Premises created by this Lease;
- (cc) any deleterious condition of the Premises if such condition results from any breach of any term of this Lease by the Lessee;
- (dd) any rent abatement, allowance for fit out or any such allowance or payment (if any; made by the Lessor to the Lessee by or at the commencement of or during the term of this Lease.
- (iii) have regard:
 - (aa) to the terms and conditions of this Lease and in particular to the period of time until the next Review Date and to the Lessee's obligation to pay a contribution to the Operating Expenses of the Building PROVIDED THAT in determining the Base Rent payable the valuers or umpire as appropriate, shall not take into account or make any allowance for any deduction or discount for any increases in contribution to the Operating Expenses of the Building payable by the Lessee between the relevant Review Date and the next following Review Date or date of termination as the case may be;
 - (bb) to the rental value of comparable premises.
- (iv) consider the Premises as used for commercial office purposes or any other use to which the Premises may be lawfully put;
- (v) regard the Premises on a floor by floor basis without a discount or premium where the current market rent is to be determined for more than one floor;
- (vi) assume that all covenants on the part of the Lessee and the Lessor

contained in this Lease have been fully performed and observed;

- (vii) make no deduction on account of any concession otherwise required to secure a tenant
- (viii) take into account the general condition and quality of the Premises and of the Building other than any deleterious condition caused by the Lessee."

For assessment of rental for the 3 year period beginning 17 July 1990, the procedure stipulated in the lease went full circle. The valuers nominated by each party having been unable to agree, the rental fell to be determined by the designated umpire, Mr R.L. Jefferies, Registered Valuer of Auckland. After hearing counsel and witnesses and the submissions of the arbitrators over some three sitting days, the umpire issued a written award on 10 May 1991. The umpire also "took a view" in that he inspected the subject premises and the comparable premises referred to in submissions. Annexed to his formal award is a comprehensive document, lucidly expressed, setting out the basis of and the reasons for his decision. The umpire concluded that the base rent for the new three year term, from 17 July 1990 was to be \$763,595, exclusive of GST.

The plaintiff's claim that the umpire made errors of law on the face of the record in that: (a) as a matter of construction of the lease, a subjective assessment of the rent was required and not an objective one; (b) the umpire was not entitled to take account of allegedly restrictive or onerous lease terms or conditions in the lease; (c) as an alternative, he did not identify such clauses or give reasons as to why he regarded them as restrictive or onerous. The plaintiff submitted that the award should be remitted back to the umpire.

I proceed on the basis that the annexure to the actual award, stating the umpire's reasons, is to be construed as part of the award. That seems to have been his intention bearing in mind the requirement for reasons in the lease. See *Max Cooper & Sons Pty Ltd v. University of New South Wales*, [1979] 2 NSWLR 257 and *Manukau city v. Fletcher Mainline Ltd*, [1982] 2 NZLR 142, 160.

I approach the assessment of the plaintiff's submissions, in the light of the following dicta of Cooke P in *Manukau City Council v. Fencible Court Howick Ltd* (1991), 1 NZ Conv C 190,871 at 190,872-3

- (a) "Where the parties have agreed to arbitration the Court should not allow

the finality of the award to be destroyed except for truly compelling reasons".

- (b) "Post-arbitral litigation is not to be encouraged".
- (c) "At the present day there is a strong judicial respect for arbitration as a valuable mode of dispute resolution. When an expert arbitrator or umpire has acted impartially (and here the challenge to the umpire's conduct has not been renewed on appeal) the Court should be slow to be persuaded to strike down the decision. The mere possibility of a different result should not normally be enough to justify judicial "intervention". There should be no assumption that an error in expounding the meaning of the contract was or may have been material. The onus should be the other way. In my opinion the Court should not set aside an arbitral award on the ground of error of law unless satisfied affirmatively that the error made a difference to the decision or at least probably did so.'.

Moreover, the law is clear that it is not "misconduct" (in the technical sense) for an arbitrator to come to an erroneous decision on fact or law. See *Russell on Arbitration* (20th ed.) 422 and *Manukau City v Fletcher Mainline Ltd* (supra) at 146.

Here the umpire stated in his award that he had applied his experience and expertise to the interpretation of the facts; he referred to the submissions made by both arbitrators. He inspected the relevant premises. Counsel for the parties addressed him and witnesses gave evidence. Although the umpire acknowledges that he was required by the terms of the lease to be a valuer/umpire and not a legal umpire, he considered the various legal references, few of which were new to him. It is clear from reading the award as a whole, that the umpire proceeded on the objective basis of rental assessment; i.e. what a hypothetical prudent lessee would pay in rental for this particular building, taking into account such restrictive or onerous lease terms and conditions which the hypothetical lessee would take into account.

The first argument for the lessor was that, as a matter of construction, the rent review clause required the rent to be assessed on a subjective basis as opposed to the objective basis used by the arbitrator. In other words, the umpire had to take into account all the considerations that would have affected the minds of the

particular parties had they been negotiating for the rent themselves within the framework and terms and conditions of the existing lease. This type of assessment is typified in the line of cases of which *Thomas Bates & Son Limited v Wyndham's (Lingerie) Ltd* [1981] 1 All ER 1077; *Lear & Anor v Blizzard* [1983] 3 All ER 662 and *Jefferies v Dimock* [1987] 1 NZLR 419 are the frequently-cited examples.

In *Bates*, the lease referred to "such rents as shall have been agreed by the lessor and the lessee" and in *Lear* to "a rent to be agreed between the parties hereto or in default of agreement at a rent to be determined by a single arbitrator".

The distinction between the two tests is well known and has recently been discussed by the Court of Appeal in an unreported decision, *Sextant Holdings Limited v New Zealand Railways Corporation* (judgment 19 March 1993).

In the words of Richardson J in that case, the objective test requires "valuers to enter the world of notional markets populated by hypothetical lessors and lessees and assumes a notional letting on the same terms as the subject lease except for the amount of the rent". The subjective test (according to the same learned Judge) "looks to what the particular lessor and lessee would consider a reasonable rent in their circumstances. Although requiring an objective assessment, it may call for consideration of circumstances not relevant to a pure market test such as who paid for the improvements and the profitability of the business carried on by the lessee."

McKay J saw the distinction as being between clauses which require a rent to be fixed for the premises by valuation and clauses which focus on the parties as, for example, by referring to a rent to be agreed between the parties or, in default, by arbitration.

Tipping J saw the objective clause as looking at the premises and what they would reasonably command by way of rent in the market; the subjective clause looked to what would be a fair or reasonable rent as between the particular parties. Tipping J also pointed out that, in a long-term lease, it is inherently unlikely that a lessor would have intended a rent-review clause which would leave the lessor vulnerable to the particular economics of the current lessee's business.

In the *Sextant* case, the Court of Appeal upholder Neazor J's view at first instance that the valuation of "the fair annual rent of the land hereby demised" fell to be

"assessed" on the objective standard. A prohibition against taking into account improvements was found in that lease as it is in the present.

Both McKay J and Tipping J in *Sextant*, discussed the decision of the Full Court of the Supreme Court of Western Australia in *Ricciardello v Caltex Oil Australia*, [1991] A.N.Z. Conv. Reports 445. There Malcolm CJ drew a distinction between the expression "market rent", where the rent is determined on the open market basis having regard to rents for comparable premises, and the expression "fair rent" where the rent is determined on the basis of what it would be fair for the particular parties to have agreed under their lease, having regard to all the circumstances relevant to any negotiations between them of a new rent from the review date. The case is authority for the proposition that the words "market rent" provide an indicator of the objective approach.

Counsel for the plaintiff, in submitting that the lease in this case called for the subjective assessment, stressed the provisions in the lease requiring negotiations; only if they broke down, then and only then, were valuers jointly to determine and agree the current market rental, having regard to the terms and conditions of the existing lease.

I am unable to accept this submission. The reference to "current market rental" occurring several times in the lease is a clear indication that the hypothetical lessor/lessee objective standard of rental assessment is appropriate. In *Sextant*, "fair rental" was held to come within the objective test. I think the present case is a stronger instance of the objective standard being required. The umpire correctly embarked upon his task which was to assess the market rental which term predicts the objective approach.

As was pointed out by Richardson J in the *Sextant* case, there can often be little difference between the two approaches. It was not demonstrated to me that there would have been any marked difference had the umpire approached his task on the *Bates* subjective basis. Applying the *Manukau v Fencible* approach mentioned earlier, I should find it hard to be satisfied affirmatively that any error of law of this description would probably have made a difference to the umpire's assessment. I am satisfied that the umpire's approach was correct and the first ground of challenge must fail.

Dealing next with the plaintiff's remaining submissions; the umpire records that,

in coming to his decision, he had considered comparable properties which had been mentioned in submissions. These properties are tabulated in an annexure to the lease with abundant detail. The umpire carefully assessed each comparable lease document to see to what extent the subject lease differed. He made some allowance in assessing the comparable rentals by reference to what he considered onerous clauses in the subject lease.

The plaintiff submitted that the umpire should not have compared lease conditions but should only have had regard to rental value of comparable premises. According to this argument, if lease terms were meant to have been compared then there should not have been a valuer/arbitrator but a lawyer/umpire.

The umpire found that some aspects of the subject lease were more restrictive than the comparable and that this fact would affect the mind of the hypothetical prudent lessee. He was entitled to use his knowledge and judgment in coming to his assessment.

The umpire said at p.5 of his award -

"If an adjustment is to be made, and I conclude some should be, it can only properly be made in the valuation process of comparable by comparable adjustment, along with other differences, so as to compare "like with like". Only where all the comparables have identical lease terms and the subject only was different, could an adjustment (if warranted) be made at the end of the process (on a single percentage or other uniform basis). In practice this would be most unlikely to be the situation - though for restricted use or absolute prohibition of assignment clauses (rarely encountered) it could arise. I therefore reject the uniform and overall 7/2% deduction made by Miss Jansen, but accept that in principle adjustment for any different terms and conditions needs to be made, as appropriate, where such differences would materially affect the rental that would be agreed between a (willing and prudent) lessee and lessor. My approach has been to examine the lease for each comparable in turn, and where particularly material clauses are present or absent, by comparison, to make a judgment whether this would affect the mind of a prudent lessee, and if so make an appropriate percentage (or per m² per annum) adjustment in arriving at the indicated rental for the subject premises. Such allowances can only be subjective in the absence

of empirical evidence, and I have exercised my own "expert" judgment in this regard in these comparisons between the comparable leases and the subject premises lease. The effect of the allowances, should, however, be reasonable, especially when taken along with other adjustments between comparable for physical differences in the location, quality, presence or absence of building services and the like."

In my view, the umpire was not obliged to give further reasons for his adjustment. Even had he been more specific regarding the terms he felt were onerous, there is no affirmative indication that such identification would have made any difference to his award. See *Manukau v Fencible* and *Sextant*. In the words of Tipping J in *United Sharebrokers Ltd v Landsborough Estates Ltd & Anor* (unreported Christchurch, C.P.298/89, 18 May 1990) at p.17 -

"No doubt what constitutes current market rental is not an easy matter to determine in those circumstances, but I do not regard that essential question as being simply a question of law. It is in reality a mixed question of fact and law. The key point for present purposes is that the umpire is not shown to have misdirected himself in law or to have overlooked any relevant principle of law in coming to his assessment of current market rent. Indeed the matters which an expert umpire is obligated to take into account in a case of this kind are essentially a question for his expert assessment after having listened carefully to the evidence and representations that the parties wish to put to him."

Bearing in mind the cautions of the *Manukau City* case, I consider there are no grounds for upsetting this award or for ordering it to be remitted to the arbitrator for further final consideration. The parties got what they bargained for - an impartial and expert assessment by an umpire who took into account all relevant matters and approached the determination of the current market rental on an appropriate basis.

The application is therefore dismissed with costs to the defendant of \$1,000 and disbursements.

Solicitors:

Jacobs Florentine & Partners, Palmerston North, for plaintiff

Morrison Morpeth, Wellington, for defendant

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