VALUERS REGISTRATION BOARD

IN THE MATTER OF an Inquiry under Section32(2) of the Valuers Act 1948

AND

IN THE MATTER OF charges under Section 3l(l)(c) of the Valuers Act 1948 against **VALUER M,** Registered Valuer

BOARD OF INQUIRY:	M E L Gamby (Inquiry Chairperson) H J Puketapu PA Curnow KR Taylor
COUNSEL:	J A L Oliver for the Valuer General D E Smyth for Valuer M
DATE OF HEARING:	11 & 12 May 2009
DATE OF DECISION:	20 March 2010

A letter of complaint was received from the Complainant that Valuer M, had over-valued the subject property. Valuer M assessed the value in June 2005 at $163,000.

The complainant said he was persuaded by the valuation report and purchased the property based on 40% equity and a 60% bank loan expecting that the property value would appreciate in the medium term. He visited the subject area in August 2006 and made enquiries of local real estate agents as to the current market value. He was dismayed, he said, to learn that local agents valued the unit at around NZ$90,000 - NZ$ 100,000 but were not interested in selling the property.

The Complainant alleged in his complaint that he was advised in 2006 by Valuer M's firm that property prices had fallen but he did not consider that they had fallen by as much as 41% in less than one year. The matter was investigated by the Valuer General and in due course an inquiry was ordered.

The complainant provided a copy of Valuer M's valuation. Retrospective valuation reports were commissioned by the Valuer General from two registered valuers, Valuer 1 and Valuer 2, who have expertise in the valuation of central city apartment buildings.

Their valuations and mortgage recommendations compared to those of Mr Kidd are as, follows:

Valuer	**Effective Date**	**Current Market Value**	**Remarks**	**Mortgage Recommendation**
Valuer M	20 June 2005	$163,000	GST inclusive, if any. Valuation "as if complete: At time of inspection under construction and nearing completion.	$107,000
Valuer 1 (22/5/07 Retrospective)	20 June 2005	$137,000 ($100,000-$110,000 if no operator lease in place)	GST inclusive, if any	$67,000
Valuer 2 (17/10/08 Retrospective)	20 June 2005	$115,000 Sale Comparison Approach	GST inclusive, if any	$55,000

The Valuer General wrote to Valuer M who responded and advised that the valuation was made on an "as complete" basis, subject to a completion certificate by a valuer from their firm, which they were never instructed to carry out. Valuer M stated that they would have reassessed the subject unit on completion at between $155,000 and $160,000. They stated that since the date of their valuation, the sales range had stabilised at a lower level of $148,000-$158,000 in the period June-August 2006 which was the date the complainant made his investigations with local real estate agents when in the area.

There was no valuation evidence before the Board that confirmed the real estate agents' advice in the range of $90,000 - $100,000 as at August 2006.

The Charges

The charges against Valuer M are set out below.

(1) Section 31(1) of the Valuers' Act 1948.

That you have been guilty of such incompetent conduct in the performance of your duties as a valuer as renders you liable to a penalty provided· by the Valuers Act 1948 in that in compiling a valuation report dated 20 June 2005 with respect to a property you grossly over-valued the said property.

(2) Section 31(1) of the Valuers' Act 1948.

That you have been found guilty of such incompetent conduct in the performance of your duties as a valuer as renders you liable to a penalty provided for by the Valuers. Act 1948 in that in the above-mentioned valuation report dated 20 June 2005 in respect of the above-described property, you made a mortgage recommendation that was excessive.

On application from Counsel for Valuer M the Board dismissed the charge in respect of the mortgage recommendation that was excessive. The hearing proceeded on the basis of only the first charge.

Background

The subject property is a small studio apartment on the 5th level of the building. Valuer M described it as having a living area of 18.6 m^2. It is a leasehold unit which means that the whole of the land is leased from the lessor at an initial ground rental of $144,000 p.a. plus GST allocated between the various units. The lessee has ownership of the improvements in the subject unit.

The expectation of the complaint and other purchasers was that there would be a tenancy lease in place between the owner of each unit and the lessor, which is a wholly owned subsidiary of a larger corporation. The tenancy lease was to be for an initial term of no less than 10 years with a 7% rental guarantee for 3 years based on the original purchase price. A small furniture package was included in each unit as part of the sale.

Following the initial 3-year period the unit owner would receive a net return based upon a formula as outlined in the lease.

In the event that the complex did not perform as anticipated the unit owner had the right to lease the unit separately on the open market. There is a 10-year right of ·renewal.

At the time Valuer M valued the subject unit the building was at an advanced stage of construction. They valued it "as complete" reserving their position by making their mortgage advance recommendation subject to satisfactory completion. Valuer M was not asked to prepare a completion certificate. their valuation of $163,000 within a range of $160,000 - $165,000 excluded the furniture package.

The Board noted that Valuer M made their mortgage recommendation subject to the following conditions:

1. Completion in accordance with plans and specifications provided.
2. Completion of the proposal to a good tradesman-like standard using only the best materials of their respective kind.
3. Completion is subject to a completion certificate by a valuer from Valuer M's Firm
4. The issue of a Code Compliance Certificate by the local authority."

While all of the conditions above, while technically correct, may not be fully relevant the Board also notes that the complainant did not complain about the amount recommended to be advanced on mortgage. No funds should have been lent based on Valuer M's report without first obtaining a completion certificate, at which time Valuer M would have had the opportunity of reviewing their report should, on completion, they have considered a review was necessary. The Board dismissed that charge.

Valuer M included in their report a significant volume of sales in similar developments.

Valuer M also recorded that they had been provided with a copy of the sales schedule relating to the subject building.

From the sales evidence recorded in the report Valuer M had regard to both sales of new units and re-sales although there is a preponderance of new unit sales. It would be fair to say that, on the evidence before the Board from the other registered valuers, many of the quoted sales are not comparable to the subject development. There is no clear distinction in the report of Valuer M as to variations in sale price that occur as a result of a leasehold interest compared to a freehold strata interest.

Evidence

Valuer 1

Valuer 1 carried out a retrospective valuation following an inspection on or about 22 May 2007, taking into account only evidence that would have been available to a valuer on 20 June 2005.

He noted that Valuer M's valuation was provided on an "as complete" basis and subject to certain conditions. Valuer 1's valuation was undertaken in accordance with the New Zealand Institute of Valuers Valuation Standards relevant at the time, which includes a requirement for a valuer to have regard to both new and second-hand sales evidence (re-sales) where there is a difference between the two bodies of evidence.

Valuer 1 reported that there are 163 strata title investment units in the subject development, comprising six one-bedroom units and 157 studio apartments/ Based on the information contained in Valuer M's report as to area, construction and improvements provided, Valuer 1 proceeded to value the unit principally on the basis of an investment with a guaranteed rental income return for 4.3 years.

Valuer 1 estimated the gross revenue that would be derived from the unit on a market basis and concluded that it would be significantly lower than the guaranteed rental payable over the remaining term of the guarantee of the lease. The difference between the two figures is significant as the guaranteed rental return of $15,694 per annum including GST was, in his opinion, some $8,935 above what could be expected as an investment under normal circumstances. He estimated a net revenue under market conditions of $6,758 taking into account all appropriate outgoings, including the ground rental payable and the estimated body corporate fees which significantly reduce the market derived return.

On the basis of an investment, he calculated that at a 6.5% return, the property would have a value of $136,000 inclusive of the present value of the rental benefit over the remaining 4.3 years.

Valuer 1 undertook a sales comparison approach as a check and concluded a lower value of $104,500 to which he then added the present value of the benefit rental for the remaining 4.3 years of $32,104 to indicate a figure of $136,604. He rounded that figure to $137,000.

After consideration of both methods, he concluded that the market value was $137,000.

Valuer 2

Valuer 2 valued the property "as if complete" based on his inspection of 17 October 2008, at the effective valuation date of 20 June 2005. He was provided with sufficient information to carry out a retrospective valuation assessment utilising base data from Valuer M's report supplied to him by the Valuer General.

He recorded the ground lease detail and provided an apartment layout showing a studio unit of minimum amenities, as a combined studio living area, a small kitchenette as part of the living area and an adjoining ensuite containing a shower, vanity unit and toilet.

Valuer 2 described the unit lease terms, with an initial rental of $13,950 per annum plus GST. He recorded the basis on which rentals would be paid at the end of the guaranteed period.

He reviewed market conditions at or around June 2005 from reports undertaken by his firm around that period. As with Valuer 1, he considered that the annual unit rental return was above the market and undertook his own market assessment based on an estimated furnished market rental of $250 per week less operating costs. He capitalised the net sum of $4952 per annum at 7.5% and added the present value of the over-renting for the balance of the guaranteed lease term. His value on that approach was $92,000.

As a second exercise he carried out a direct market comparison approach, utilising predominantly re-sales and concluded a sales comparison va1ue of $115,000. He adopted the higher value of $115,000 in preference to his investment approach.

The Board noted that the assessment by Valuer M was 18.98% higher than that of Valuer 1, and 41.74% higher than that of Valuer 2.

Under cross-examination, both valuers who undertook the retrospective assessments
agreed that it was difficult to value small apartment units at the time. The range of values confirms that difficulty with Valuer 2 as far away from Valuer 1 in one direction as Valuer M is in the other.

Valuer 3

Valuer 3 prepared a report at the instruction of Counsel for Valuer M. That report was undertaken in May 2009 and is also a retrospective valuation as of 20 June 2005, It was not before the Board until the date of the hearing.

Valuer 3 acknowledged that he was provided with the reports of Valuer M, Valuer 1 and Valuer 2. He was therefore in the rather privileged position of knowing the values of all three valuers before he undertook his own assessment.

Valuer 3 referred to New Zealand Valuation Guidance Note 4 (NZVGN 4) of Property Institute New Zealand (PINZ) which requires that when valuing houses under construction, or houses to be built or previously unoccupied new houses, a valuer must have regard to both new sales and re-sales of similar 'properties. Where a valuer considers that there is likely to be a significant difference between the value of a new house and its re-sale value in the same condition, he must report both values and comment on the differential.

Valuer 3 should have referred to the NZVGN 7 of the New Zealand Institute of Values (NZIV) which was operative at the time Valuer M undertook their valuation. However, the wording and purpose of the two guidance notes are essentially the same and nothing of substance to this inquiry turns on the error.

Valuer M assessed the valuation as a new property at $152,000 and as a re-sale under the comparative sales approach at $141,000. Under the cash flow approach (investment) he assessed a value of $130,000 and adopted a concluded value of $135,700. The Board notes that this concluded value is very similar to that of Valuer 1, being towards the middle of the two extremes of Valuer 2 at $115,000 and Valuer M at $163,000.

Valuer 3 carried out similar assessments to that of Valuer 1 and Valuer 2 by considering both the income approach (cash flow) and direct sales comparison approach on both new sales and re-sales. He went one step further and discussed the merits of each valuation approach.

In valuing the property, Valuer 3 considered that, by comparison with new previously unoccupied apartments, the value of the property would be $152,000. He found a lower value by comparison with re-sales or. as an investment property and reported accordingly.

Valuer 3 records the following at page 20 of his report after confirming his valuation as of 20 June 2005 of $135,700.

"Given the two-tier market the value adopted is less than the value as off the plans sales but only by 10.7%. While this is outside the accepted tolerance of +/- 10% it is only marginally so. "

I would comment however that it would not be unreasonable for someone to pay in excess of $135,700 given the earlier sales evidence within the subject development. This figure would approach my valuation at $152;000. "

Valuer 3's evidence confirmed to the Board the difficulties of valuing in the market at the time and the issues to be addressed in terms of the guidance note.

The matter to be tested by the Board is the market value of the unit at the time of valuation. Valuer 3's concluded valuation of $135,700 is close to that of Valuer 1 and significantly departs from Valuer M. However, he also records that off-the- plans and as new, the apartment could have commanded a price of $152,000 by comparison with market evidence in the same development which is not materially different to the figure of $150,000 as a new unoccupied apartment assessed by Valuer 1. Valuer 2 may have had regard to new sales but does not report a "two- tiered" market as that term is often used to distinguish a value assessed by comparison only to new apartment sales and a value assessed by comparison with re-sales.

The comparison between Valuer 3's upper level of value at $152,000 (as new by comparison with other new sales in the development) and that of Valuer M at $163,000 is within 7.2% and between Valuer 1's upper level of $150,000 and Valuer M's $163,000 is at 8.67%.

While it must be reaffirmed that Valuer 3's valuation of the apartment was at $135,700, not $152,000, and Valuer 1's was $137,000 being some 19%-20% distant from Valuer M, it must be remembered that Valuer 2 saw fit to value the unit at only $115,000 which is some 15% below the market assessment of Valuer 3 and approximately 16% below the market assessment by Valuer 1.

The Board concludes that, based on the evidence before it, there was the possibility of a wide range of opinion. Valuer M figure is clearly well above the market and does not address NZVGN 7. However, it is not so much above the market that it could be described as grossly excessive, given the range of valuation evidence, not all of which the Board is satisfied answered fundamental questions required to be addressed in accordance with the Institute's standards at the time.

The complainant's concerns as to what happened in the market after 20 June 2005 (the valuation date) cannot be placed at the door of Valuer M. Whether the market fell to the extent that the real estate agents indicate is immaterial. None of the valuers was instructed to provide a valuation as at August 2006, or indicated that the property was worth only $90,000 and $100,000 as at June 2005. The market advice the complaint received was in August 2006, over a year after the valuation date in a falling market.

<u>Decision</u>

The Board having considered the evidence and read the final submissions of Counsel for the prosecution and the defence, concludes that Valuer M overvalued the subject project at the subject development, but that the charge is not proven to a standard sufficient to find that Valuer M grossly over-valued the property.

Evan Gamby

Inquiry Chairperson
20 March 2010