Report

Review of Land Valuation Methodology

Auckland International Airport Limited

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Commerce Commission
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Attention: Anna McKinlay

Final Report:
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1.0 Executive summary

In our opinion, the valuation has not been prepared in accordance with Schedule A of the Commerce Act (Specified Airport Services Input Methodologies) Determination 2010; and the following report sets out the reasons why we consider the Schedule A methodology has been incorrectly applied.

1.1 Areas of Valuation Report Non-compliance

1.1.1 There appears to be no consideration given to the costs of any zoning changes. See Schedule A, Clause A10 (c).

1.1.2 Insufficient evidence to demonstrate how and why the rates utilised and resulting in the assessment of value for one precinct by the Discounted Cashflow (DCF) method have been adjusted and adopted for the remaining nine precincts. See Schedule A, Clause A10 (h).

2.0 Scope

We have been requested to review the land valuation report disclosed by Auckland International Airport Limited (AIAL), to determine whether the valuation has been prepared in accordance with the land valuation methodology set out in Schedule A. This review is limited to being a review solely of whether the valuation report has correctly applied the methodology. The review does not include a peer review of the actual values.

This review also includes an assessment of whether the land valuations disclosed by AIAL, include land conversion costs as defined in Part 1, clause 1.4 of the Commerce Act (Specified Airport Services Input Methodologies) Determination 2010, namely:

> Land conversion costs means:
>
> costs incurred in:
>
> (i) the holding and levelling of land;
>
> (ii) seawall reclamation;
>
> (iii) sea protection; or
>
> (iv) seawall construction; or

any other costs incurred relating to the conversion of land for use in the supply of specified airport services. The valuation must exclude the value of conversion costs to the extent that they are required specifically to convert the land into that suitable for the supply of airport services (clause A9(11) of Schedule A). In addition, real property to the extent that it is attributable to land conversion costs is not 'land' for the purposes of the Input Methodologies and cannot be revalued as assets under Schedule A (see the definition of 'non-land asset' in clause 1.4(2) and clause 3. 7 of the Commerce Act (Specified Airport Services Input Methodologies) Determination 2010).

The report under review is titled MVAU, Auckland International Airport Limited, with an effective date of 30 June 2009. The report was prepared by Colliers International NZ Ltd. We refer to this valuation report as the report throughout this review document.

In March 2013, we were provided with additional documentation, namely, a letter dated 19 February from Colliers to AIAL responding to the matters raised in our review of the 30 June 2011 valuation, which is also relevant to the review of the 2009 report. In addition we have considered letters prepared by AIAL dated 5 April 2013 and 13 June 2013.

3.0 Compliance with the Requirements of Section A10 of Schedule A

3.1 Identify Land to be Valued

Page 1 of the report, indicates that Collier's were provided with a Land Master List by AIAL. Page 4 identifies the various land areas comprising the total AIAL land portfolio, and page 6 shows these areas in plan form. We note there is a very minor increase in land area over that stated in the 2011 report. While only a high level approach to land identification has been provided we have no reason to assume that this does not reflect the current AIAL land holding. The land appears to have been valued as aggregated and as notionally vacant.

Complies.

3.2 Confirm Land Ownership, Tenure and Areas

Colliers have subsequently to completing their valuation, scanned all the AIAL land titles. This scan has identified the total area of approximately 1553 hectares as being correct and that there were no memorials recorded on title that would have a detrimental impact on value.

We note the total land holding is given as being 1,552.70 hectares. This land area is then reduced by making a deduction (i.e. this land has not been valued) for land utilised for existing commercial areas, PPE land and roads to a total area valued of 1,109.20 hectares (which includes seabed of 230.00 hectares). We note that this area also includes the land set aside for future airport development. Of the total 1,109.20 hectares valued 716.50 hectares forms the Regulated Asset Base (RAB) and 392.70 hectares comprises land for future development. See Section 3.14.4 of this report for further details.

Complies.

3.3 Zoning

Page 5 of the report identifies the existing zoning for the various airport land parcels. It also identifies two new plan changes (PC 13 and PC 14) that are expected to become operative in the short term. These changes will bring the airport land holdings into a new Metropolitan Urban Limit (MUL) and will introduce new business zones.

Page 6 to 12 discusses the likely use and zoning for the land in its highest and best alternative use and some ten land use precincts have been established.

We note that residential development would be a non-complying activity under the new zones, and Colliers state that in their view there would be no risk to achieving development in the form envisaged. They are silent however on whether there would be cost involved to permit such development.

Does not comply.

3.4 Determine Highest and Best Alternative Use

To assist with this part of the valuation process, AIAL commissioned Common Ground (an urban design, land use planning consultancy – who also provide infrastructure design, masterplanning and project direction and management services) to develop a land use plan identifying likely future land use options for the AIAL land holding. The final plan identifies a range of likely uses including residential, commercial, industrial and reserve areas.

Colliers believe that the Common Ground land use plan is defendable from both a planning and development perspective.

Complies.

3.5 Resource Management Considerations

While the plan is high level, we have had to assume that the land use plan prepared by Common Ground will have considered surrounding uses, existing services, residential growth requirements in the area, retail and business requirements, reserves and existing road networks as would be expected. Unfortunately a full copy of their document "Market Value Alternative Use Report" was not provided.

Complies.

3.6 Subdivision Considerations – Land Development Plan

The land use plan developed by Common Ground has provided a layout containing ten distinct precincts, these being identified as:

- Harbour Edge
- Urban Village
- Golf Village
- Urban Centre
- Marine Village
- Waterfront Village
- Puhinui Village

- Wiroa Village
- Eastern gateway Village, and
- Productive Village.

All areas are predominantly residential in nature with smaller amounts of commercial/industrial development.

We believe that the plan as identified provides sufficient evidence in terms of the rationale for the selection of the various land uses and the areas of land identified for those uses.

Complies.

3.7 Determine Market Demand

Pages 10 through 23 of the report establishes that general market and economic analysis has been undertaken within the Auckland region to establish the supply and demand and potential market absorption for all the uses identified in the master plan.

Absorption of all lots has been considered over a seventeen year period given the significant size of the land holding. We are satisfied that the conclusions as to market demand are realistic estimates.

Complies.

3.8 Determine Development Direct Costs

Colliers have not commissioned an engineering company to assess the direct costs of development. This has instead been based on their own knowledge. The costs they have allowed for include civil works and earthworks. They have additionally allowed for an escalation of these costs over the full development period. There is no further detail on what is included in the civil works, but the assumption would be that this allows for all other physical construction costs other than earthworks such as roads, water/stormwater/sewer, and telecom/gas/power.

While it would be preferable for the subdivision of a land holding of this size to have had specialised engineering input to help determine direct costs, there is no evidence to suggest that Colliers do not have sufficient experience to make their own assessment.

Complies.

3.9 Determine Development Indirect Costs

Colliers in their hypothetical subdivision calculation have allowed for indirect costs such as marketing/selling costs, legal fees and the developer' profit and risk. They have also allowed for the developer's holding costs, management, development contributions and contingencies.

Complies.

3.10 Undertake Market Research

Appendix 5 of the report provides residential and commercial block land sales evidence that has been analysed by Colliers. Primarily this considers sales in 2008 and 2009. However as there has been very limited direct evidence (and certainly no sales of land approaching the size of the subject land) further evidence has been provided going back to 2001.

Several of the older sales are of large parcels situated relatively close to Auckland International Airport. Colliers however have stated that these sales have not influenced the valuation due to their relevant dates.

On page 25 Colliers also refer to valuation work that they have undertaken on various large scale residential developments within the Auckland region and based on this work they have then assessed rates for net commercial zoned areas and rates for the various housing types. Colliers have since provided additional sales data to support their analysis.

Complies.

3.11 Application of Market Evidence

Due to the scale of the holding, directly comparable evidence was not able to be obtained by Colliers and as such they have primarily utilised the DCF approach. Again due to the scale of this land holding, the DCF approach has been performed over one of the ten precincts only, with the resulting rates per hectare and per household unit being used as the base line for the wider holding applying those rates after suitable adjustment for factors such as location, density, yield and timing to produce a notional value of the entire holding. Unfortunately, there is little detail on just how these adjustments were made. As the majority of the land holding is valued using these adjusted rates, I believe further clarification should be sought. As it stands there appears to be insufficient rationale for the rates used to be sure the market evidence is being correctly applied.

The final value arrived at by the DCF method has been cross-checked against expected values for large holdings on a per hectare basis. We further note the value as been apportioned between the land forming the RAB and the land held for future development.

The response by Colliers to this same point raised in the 2011 report review, unfortunately did not provide the additional information sought. While valuer judgement is understood, some further detail around the adjustments used for factors such as location, use, density etc., would have been useful to clarify the totals arrived at.

A reader of this report ideally should be provided with information on how these adjustments were applied and in my view this would be required under the information disclosure regulatory regime under Part 4 of the Commerce Act.

Does not comply.

3.12 Reconciliation of Approaches

Reconciliation of the values arrived at by the two valuation approaches has been made.

Complies.

3.13 Preparation of Valuation Report

A relatively complete valuation report was prepared incorporating all disclosures as required by the relevant valuation standards.

Complies.

3.14 Other Considerations

3.14.1 The proposed MVAU development plan includes land that was reclaimed for the existing runway. In as far as this land has been valued at market rates rather than at cost, this appears to be acceptable under Schedule A.

3.14.2 Colliers advise that the value of the sea wall has not been incorporated into the land value.

3.14.3 The valuation does not make any deduction or allowance for any remediation costs. This complies with Schedule A.

3.14.4 We note that the valuation must include all land used to provide specified airport services held by the airport: Under the IM airports are allowed to recognise a revaluation of land (only) when all airport land held is simultaneously revalued. This includes land currently used to provide specified airport services, and any future development land. Of the total land holding of 1,552.70 hectares, 443.50 hectares have not been valued. These comprise:

Existing commercial core	414.60 hectares
Other PPE land	11.00
Roads	17.90
Total	443.50 hectares.

There has been no value ascribed to these areas, or details with respect to title etc provided. This appears to comply with Schedule A.

3.14.5 Of the valued area of 1,109.82 hectares, a further three land areas are shown to have no value in the MVAU valuation, although in reality the value of these areas is incorporated into the rates and values assessed for the various precincts e.g. the land fronting the sea has apparently had per hectare/per household unit rates adjusted to reflect the benefit that the AIAL ownership of the seabed has on the land precincts fronting the sea. While the seabed has not been valued as such, its value has been incorporated. The three areas of this type include:

Seabed	229.90 hectares
Coastal margin	6.60
Open Space	146.10
Total	382.60 hectares.

From AIAL's perspective, it would appear as though ownership and control of the seabed adjacent to the runway is advantageous, however I do not believe that this ownership would be of benefit to a MVAU valuation and nor would we expect an owner of the land (as valued under a MVAU approach) to acquire or require ownership of the adjacent seabed. We do not believe that inflating the land values under the MVAU for ownership of the seabed complies with Schedule A. We note Colliers response to this issue in the 2011 review states that ownership of the seabed is irrelevant and values were not increased as a result. This contradicts the statement on page 25 of this report *"have reflected the benefit of the control of the seabed in our concluded lot values and therefore underlying precinct values."*

4.0 Conclusions

Generally, the requirements of Schedule A appear to have been followed however, there are a couple of areas where further and more detailed research should have been undertaken to ensure full compliance – notably in the sales analysis and resulting rate and value conclusions and the possible costs of any zoning changes.