

Evaluation/Potential Benefits of Proposed New Plymouth District Council (Waitara Lands) Bill

Client: New Plymouth District Council

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TelferYoung (Taranaki) Limited



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PROPOSED WAITARA FREEHOLDING PROCESS – POTENTIAL BENEFITS TO LESSEE

The New Plymouth District Council is currently in the process of preparing a local Bill in respect of the Waitara Lease Portfolio; part of which includes provisions to offer the lessees freeholding. The following is intended to provide answers to anticipated questions.

What are the principal changes?

Currently the leases do not include any rights to freehold and so this will be a new option or benefit not previously available to the lessee.

Under this proposal the right to freehold will run with the land; that is, it will be transferrable. If the property is sold as leasehold, the new lessee will still have the right to exercise freeholding.

Is this a one-off opportunity to freehold?

The option to freehold can be exercised at any time and it is the lessee, not the lessor that triggers the exercise. Once the Bill is law, the Council as lessor is likely to write to the lessees asking if they are interested in freeholding and setting out the process that needs to be followed. If the lessee declines at that time then the option to trigger the process at some later date remains and passes to any new owner.

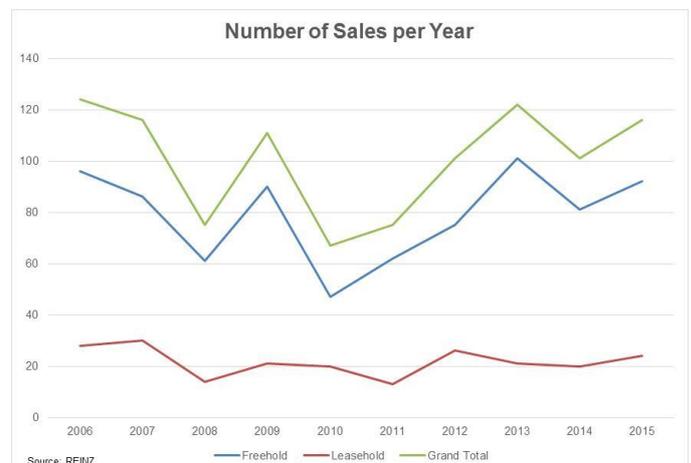
What happens to my existing lease?

The leases existing terms are protected and remain unchanged. Should they wish, a lessee can continue to lease the property (in perpetuity) based on the existing lease terms. Freeholding is not compulsory, but (if the Bill is passed) will become an option.

If freeholding occurs, the lessees current leasehold interest will merge with the freehold (the lease is cancelled) and a new freehold title (or Computer Register) will be issued in the lessees name.

How will freeholding affect the value of my property?

There is the possibility of improved saleability which could lead to improved value. The following graphs displays the difference between freehold house prices and leasehold house prices in Waitara over the last ten years and also the number of sales over the same period.



Our own observations are supported by discussions with real estate personnel (working in the Waitara locality) which indicate that demand for leasehold property has improved, this on the back of renewed expectation that freeholding may eventually become available.

If we again refer to the graphs shown above, the data for average sale prices indicates that currently there is a clear margin in value between freehold and leasehold property that is roughly equivalent to the underlying value of the land. From this one might reason that freeholding is a viable exercise.

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Owning the property outright as opposed to owning the improvements but leasing the land, means that any future improvement in the land value will accrue to the current lessee. That is, once they have acquired the freehold, the lessee, who becomes a freehold owner, will get the full benefit of any increase in property value. Of course the reverse is also true.

With current low interest rates there is also the potential for this exercise to be cost neutral, or nearly so, for lessees. That is, the costs associated with borrowing and repaying the money to acquire the freehold (this based on interest on borrowing not capital repayments) are likely to be similar to the rental paid to the lessor; particularly so if the rent has recently been reviewed or is about to be reviewed.

Freeholding also has the potential to enhance the options available to the lessee which could possibly include improved financing options, property development or subdivision. Obviously banking requirements or planning and building regulations would still apply.

Once freeholding becomes a definite right, it is also likely that leasehold properties may attract interest from a wider range of purchasers. That is, purchasers who would not consider leasehold properties may consider them if freeholding is a guaranteed option. Greater demand usually reflects in shorter selling times and can lead to increase in prices.

What is the process?

Before freeholding can occur, the proposed Bill needs to be passed. Once the Bill is law, the Council as lessor is likely to contact the lessees and enquire if they are interested in freeholding. If the lessee indicates that they are interested, Council will then commission a valuation (of the unimproved land value) and once this is available, advise the lessee of this value. The lessee has the right to obtain their own independent valuation. If this differs from the valuation the Council obtained, and the parties cannot agree on a final figure, an arbitration process will apply.

What is unimproved land value?

“Unimproved land value” can be defined as “*sale value of freehold land as if no improvements of any description had ever been carried out*”. That is, the unimproved land is the asset that is leased. This is the land set within the existing environment or neighbourhood but assumed to be devoid of all improvements and therefore in an unimproved state or condition. Therefore the value is assessed on what the land was like when it was first leased and excludes:

- + improvements on the land; these are structural improvements including house, other buildings and fences.
- + any improvements to the land; these are developmental improvements including excavation, access, and retaining walls.

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PROPOSED WAITARA FREEHOLDING PROCESS – POTENTIAL BENEFITS TO LESSOR (NEW PLYMOUTH DISTRICT COUNCIL)

The New Plymouth District Council is currently in the process of preparing a Bill. The Bill will apply to endowment land held by the Council and currently leased to numerous individuals within the Waitara area. If the Bill is approved, the lessees will gain the right to freehold their properties at a price to be determined by independent valuation.

While the passing of this Bill will create a number of benefits to the lessees; the most obvious being the right of freehold which is not currently available under their standard lease terms; the following looks at the benefits or potential benefits to the lessor.

Firstly, it removes an element of contention that has been attached to this lease portfolio for many years. For a considerable period of time the lessees have been petitioning the Council for the right to freehold. If passed, the Bill gives them that right.

The Bill also repeals existing legislation that tends to restrict the Council's ability to use funds generated from this portfolio. Existing legislation restricts how the income can be used, currently only for certain harbour works or bridge repairs (parts of this work no longer a function of the New Plymouth District Council operation). The new legislation proposes a Statutory Board to be set up and that monies generated from the lease portfolio be used for the benefit of the Waitara community. The Taranaki Regional Council will receive funds from the Waitara endowment lands as well.

The proposed Board will comprise joint representation from the Council and Te Atiawa. This and other initiatives could be viewed positively and part of an ongoing process for working with and alongside Te Atiawa.

Over a period of time, as the freeholding process occurs, the level (and expense) of managing this portfolio will diminish. Currently there are some 778 leases, each of which requires a certain level of individual management to ensure rentals are paid and to deal with lease renewals and transfers. One might assume that any reinvestment of capital (generated from the freeholding process) will be undertaken in larger investment parcels.

It is too soon to try and predict how many lessees will take the opportunity to exercise their new freeholding rights. Some will decline because they see economic benefits in the current historic (set some time ago) rents that they enjoy and others will simply not be able to afford the process. However, for those that have had recent rent reviews or are about to have a rent review, the process could be relative cost neutral and therefore appear attractive. By cost neutral we mean that with current low bank lending rates, the interest incurred on any borrowings needed to purchase the freehold could roughly equate to the cost of the current rent.

The following few facts and figures help demonstrate the current position of this portfolio.

Current Data on Waitara Leases	
Number of Leasehold Properties	778
Average rent paid per property as at 31/12/2015 - total portfolio	\$1,432
Average rent paid per property as at 31/12/2015 - residential only	\$1,567
Average rent on residential assessed 2014/2015	\$4,339
Average residential section value (2013 Rating Valuations)	\$90,245
Overall return - total rental to total portfolio	1.82%
Return based on 2014/15 assessments	4.92%
Number of leases about to be reviewed 2016/2020	211
Current deposit rates (Kiwi Bank 90 day rate at 4/3/2016)	3.75%
Current Reserve Bank Bond rates (issue Oct 2015)	3.50%
Current Bank Lending rates - 2yrs (as at 4/3/2016 - medium of all lenders)	4.99%
Current Bank Lending rates - 3yrs	5.10%
Current Bank Lending rates -4yrs	5.25%

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