

The Society of
Chartered 
Surveyors

**CHARTERED QUANTITY SURVEYORS
DIVISION**

SUBMISSION TO NAMA

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This brief submission to NAMA is intended to give an overview of the role and skill set of the Chartered Quantity Surveyor and how they can assist NAMA in carrying out its role. It also demonstrates the value they can add to various developments. The submission addresses the following issues:

- 1) **Initial Due Diligence**
- 2) **Project Monitoring**
- 3) **Workouts**
- 4) **Valuation Preparation**

Initial Due Diligence

Chartered Quantity Surveyors are eminently suitable to assess the future viability of an asset and to carry out initial due diligence reports on a development proposal for NAMA. Such reports include advice on:

- Site development issues – survey of site – status of works - feasibility of further development – availability of utilities – adjacent infra-structure – identify abnormal site features - preparation of feasibility studies
- Status of statutory consents – examination of planning permission, fire certificates and building regulations – advice on compliance issues and time-frames; analysis of fees and local authority contributions – change of use implications.
- Validation and verification of costs to date – checking costs incurred to date and summary of outstanding liabilities – forensic audit of all costs
- Risk Assessment – outline of potential risks and weaknesses of proposal through various stages of development – programme delays, increased costs, potential unforeseen items. Identification of any gaps in information, costings or professional advices.
- Review of contractual correspondence – advise on contractual arrangements, requirements of design and sub-contractor warranties, direct agreements, funders warranties, step-in rights, retention of title issues etc.
- Bonds – checking status of bonds, time-limits, cover levels
- Insurances – check developer's/contractor's insurances, cover levels; policy details, excesses, expiry dates.
- Programmes – scrutiny of design stage time-lines followed by checking of tender period and on-site construction programme

Project Monitoring

When the project progresses to construction stage, the Chartered Quantity Surveyor becomes "*the eyes and ears*" for NAMA on the ground. We believe that the ongoing brief for the independent monitor should be expanded to ensure the strictest procedures are adhered to by all parties.

We understand that the Canadian banks adopt a strict monitoring protocol which effectively turns the report requested from the Quantity Surveyor into a condition precedent to any drawdown of funds.

The Monitor's services typically include:

- Checking contractual arrangements, assembling design and sub-contractor warranties, direct agreements, funders warranties, bonds etc.
- Confirm insurances in place and renewal dates
- Review of all costs incurred to date, advising on potential cost over-runs or savings; comparing actual costs against projected expenditure; updating drawdown requirements; confirm that projected cost to complete development equals remaining facility

The Canadian model can also include the following additional steps which will serve to further protect NAMA;

- Verification that draw-downs have been passed on to contractors/sub-contractors, suppliers and consultants i.e. seek monthly statutory declarations from contractors and suppliers that payments have been made
- Review payment ledgers on a monthly basis
- Review all purchases and sales contracts to confirm that sales are secured
- Checking actual progress on site against contract programme
- Completion Report to include collation of all necessary Compliance Documentation – contracts, warranties, O&M manuals, compliance certificates, Health and Safety Files, defects lists and the like.

In summary it is recommended that the Monitor's Reports confirming approval of drawdown are a condition precedent to ongoing funding.

Workouts

While the Valuation and Due Diligence exercise will give a better insight as to the future viability of an asset, it must then be considered how to actually realise the full potential of that asset. This will present the potentially thorny question of what to do with the asset, or if it is clear what to do, then the question becomes how to do it.

For sites or developments where the Developer is in a position to complete the development, following the Chartered Quantity Surveyor's Due Diligence assessment of same, then it may be considered appropriate for him to do so. In this instance the Chartered Quantity Surveyor would undertake the role of Monitor on a more comprehensive basis as outlined above. However where the Developer is not in a position to complete the development, the Chartered Quantity Surveyor can undertake the workout of the development so as to realise its true potential.

In this instance the Chartered Quantity Surveyor will project manage the workout of the asset from its current condition, be that a green field site or a partially complete development. This will entail re-appraising the site to establish optimum potential, either in the short to medium term, or phased over the longer term. Once fully re-appraised and agreement reached as to the optimum solution, the Chartered Quantity Surveyor will project manage the existing or new Design Team to either oversee the completion of the development or re-design and secure planning for any changes or alterations that a re-appraisal might deem necessary. Furthermore the Chartered Quantity Surveyor will oversee the appointment of a new contractor or the re-negotiation with an existing contractor, whichever is deemed best value, to complete construction of the development; this being an area in which the Chartered Quantity Surveyor is eminently proficient.

By appointing a Chartered Quantity Surveyor to project manage the workout of developments the Chartered Quantity Surveyor can provide a one-stop-shop for the successful completion of developments, from their existing state through to final conclusion and handover, complete with all relevant warranties and compliance documentation.

Valuation Preparation

Cost and **Sales** are the two factors that must be considered in the preparation of any Valuation.

We understand that establishment of the Current Market Value of the assets is well underway by the individual banks and these will shortly be submitted to NAMA for review.

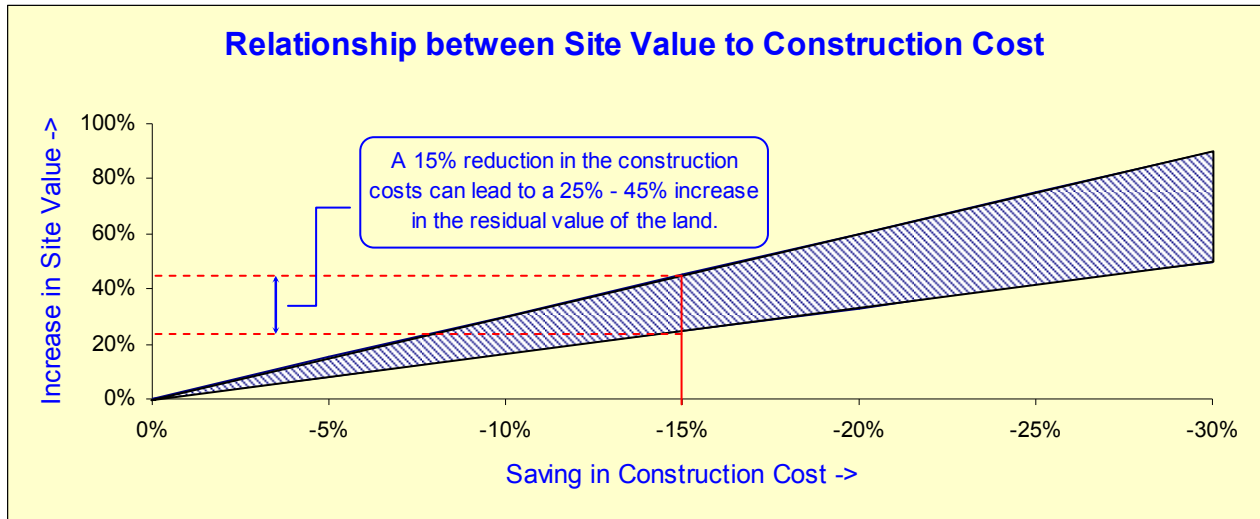
Construction costs have dropped significantly (*ref. SCS Tender Index published 21/9/09*) over the past 12 months and it is very important that accurate, up to date costs are used when preparing these valuations. The use of average building cost data for different building types published by various surveying practices is not suitable as a basis for valuations as the tables are out of date and are only an indication of average construction costs.

Construction Cost is a very important variable in establishing a proper market valuation and each project should be independently examined by a Chartered Quantity Surveyor to arrive at a true current market valuation.

As shown in the example set out on page 5, a 30% change to the construction cost through Value Engineering and the impact of current tender levels has the effect of changing the site write-down from 84% to only 12%.

The second example, which should be viewed separately from the first example, shown on page 6 relates to the effect on the site value when the borrower / bank have included a construction value in the residual valuation which is too low. The valuation submitted to NAMA shows a site write down of 21%. Following due diligence, carried out by the Chartered Quantity Surveyor, the true construction cost is shown as €137m as opposed to €115m. This has the effect of over-valuing the site by 96% i.e. €27m as opposed to €53m.

Whilst these are only two examples, there are many more examples that span either side of these figures. The key message is that construction costs as a variable must be considered carefully in the valuation equation.



The graph above describes the relationship between construction cost and site value which is illustrated further in worked examples on the following pages.

It is imperative that proper independent cost estimates of the construction costs are prepared for the current valuations. There are a number of different ways that this can be achieved but in essence it involves the cost consultant being responsible for entering the correct cost information into the residual valuation.

Example of the effect of Value Engineering by QS on site value:

€300m development in 2008

€300m Sales development (say 2008)

| | |
|-------------------------------|---------------|
| Sales: | €300 |
| Less Costs: | |
| Planning Contributions | €8 |
| Construction | €153 |
| Professional fees | €15 |
| Selling Costs | €3 |
| Finance | €15 |
| | (€195) |
| Available for Site & profit | €105 |
| Deduct Profit (15% on cost) | (€39) |
| Site Value (incl. acq. costs) | €66 |

1

€225m development in 2009

(€300m x -25% = €225m)

| | |
|------------|------------------------|
| €8 | No change |
| €153 | No change |
| €15 | No change |
| €2 | Reduced by 25% |
| €15 | May increase |
| | (€194) |
| €31 | |
| (€20) | Target 10% p |
| €11 | -84% write down |

2

3

Assume 25% drop in property prices

Redesigned €225m development in 2009

| | |
|------------|-----------------------------|
| €8 | No change |
| €107 | Redesign + Deflation (-30%) |
| €14 | Decrease |
| €2 | No change |
| €15 | Debt reduced vs. time TBA |
| | (€146) |
| €79 | |
| (€20) | Target 10% p |
| €58 | -12% write down |

4

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Value Engineering

Redesign & Cost Scheme

€58m / €66m = -9%

- 1 Value of site in 2008
- 2 Property prices fall by 25%
- 3 25% fall in prices results in 84% write down on site value
- 4 Project Value Engineered and repriced by QS; 30% saving with no effect on Sales
- 5 Profit level maintained; construction saving goes to site
- 6 Site value now €58m ~ write down of only 12%

.....value of underlying asset (i.e. site) increased by 72%

Page 5

Example of unrealistic construction figures by borrower..

€300m development in 2008

€300m Sales development (say 2008)

Sales: €300

Less Costs:

| | | |
|-------------------------------|------|--------|
| Planning Contributions | €8 | |
| Construction | €153 | |
| Professional fees | €15 | |
| Selling Costs | €3 | |
| Finance | €15 | (€195) |
| Available for Site & profit | | €105 |
| Deduct Profit (15% on cost) | | (€39) |
| Site Value (incl. acq. costs) | | €66 |

1

€225m Valuation in 09

(€300m x -25% = €225m)

| | | |
|------|---------------------|--------|
| €8 | No change | |
| €115 | Reduced by borrower | |
| €11 | Reduced by borrower | |
| €2 | Reduced by 25% | |
| €15 | May increase | (€152) |
| | | €73 |
| | | (€20) |
| | | €53 |

2

3

Assume 25% drop in property prices

Figures after Due Diligence

€225 ✓

| | | |
|------|---------------------------|--------|
| €8 | No change | |
| €137 | Based on accurate cost | |
| €14 | Corresponding increase | |
| €2 | No change | |
| €15 | Debt reduced vs. time TBA | (€177) |
| | | €48 |
| | | (€20) |
| | | €27 |

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Carry out Due Diligence on construction cost

€27m/€66m = -59%

- 1 Value of site in 2008
- 2 Property prices fall by 25%
- 3 25% fall in prices shown by borrower as only a 21% write down on site value
- 4 Due Diligence carried out by NAMA advisors which shows construction costs as being too low.
- 5 Profit level maintained; construction saving goes to site
- 6 Site value now €27m NOT €53m; site over-valued by 96% i.e. €27m as opposed to €53m

...due diligence highlights over valuation of site by 96%..

Conclusion

Whilst the primary focus of NAMA to date has been on matters pertaining to valuation, the Society believes it is timely to highlight the valuable role that Chartered Quantity Surveyors can provide to NAMA. Chartered Quantity Surveyors have a unique skill set that enables them to enhance due diligence considerations, play a critical independent role in the ongoing project management of assets and to have a significant impact on valuations.

In this volatile market where construction tenders are proving extremely difficult to predict, it may prove detrimental to the overall process to use summary level and outdated information as a basis for valuations. In an equation of two parts both must be treated with equal importance.

We would be delighted to discuss some of the challenges outlined in this brief submission and look forward to hearing from NAMA in this regard as appropriate.