

**Public Accounts
Committee**
Parliament of New South Wales



**Report on Brief Review of
the Land Commission of
New South Wales**

Report Number 18

July 1985

The New South Wales Public Accounts Committee is composed of five members of the Legislative Assembly of the New South Wales Parliament. Its functions and powers are defined in the Public Finance and Audit Act and its role generally is to serve as a Parliamentary watchdog of government expenditure to ensure that government organisations are implementing government policy as efficiently and effectively as possible.

1984-85
Parliament of New South Wales

**Public Accounts Committee
of the
Forty-eighth Parliament**

Eighteenth Report

Inquiry pursuant to section 57 (1) of the Public Finance and Audit Act, 1983, concerning the operations of the Land Commission of New South Wales.

(Transcripts of Evidence included as Appendix to this Report)

July, 1985

Committee Members

The members of the Public Accounts Committee as at July, 1985 were:

Mr John Aquilina, M.P., Chairman*

John Aquilina was elected Member for Blacktown in September, 1981. A high school teacher by profession, John Aquilina was a Commissioner of the Ethnic Affairs Commission for two years and the Mayor of Blacktown for four years before entering Parliament.

Mr John Murray, M.P., Vice-Chairman

John Murray, formerly a teacher, was elected Member for Drummoyne in April, 1982. An Alderman on Drummoyne Council for three terms, John Murray was Mayor of the Council for five years, and served four years as councillor on Sydney County Council. He is currently a member of the Prostitution Committee and the House Committee.

Mr Colin Fisher, M.P.

Colin Fisher was elected Member for Upper Hunter in February, 1970. Former Minister for Local Government (1975) and Minister for Lands and Forests (1976), in opposition Colin Fisher has served as National Party Spokesman on Local Government, on Planning and Environment, and on Energy.

Mr Phillip Smiles, M.P.

Phillip Smiles was elected Member for Mosman in March, 1984. A management and marketing consultant since 1974, Phillip Smiles has been involved with entrepreneurial business activities since his teens. Since entering Parliament he has been actively interested in the areas of emergency services, welfare and financial analysis.

Dr Andrew Refshauge, M.P.**

Andrew Refshauge was elected as Member for Marrickville in October, 1983. He previously practised as a Medical Practitioner with the Aboriginal Medical Service and was a past President of the Doctors' Reform Society. He is currently a fellow of the Senate of the University of Sydney.

*Mr Bob Carr was Chairman of the Committee until he was appointed Minister for Planning and Environment on 12 December, 1984.

**Dr Refshauge was appointed to the Committee on 20 February, 1985.



Committee Members. From left: Phillip Smiles, John Murray (Vice-Chairman), Andrew Refshauge,

Secretariat

Frank Sartor, B.E., B.Comm.(Hons), Director

Sue Chapple, B.A.(Hons), Senior Project Officer

Bob Pritchard, AASA, CPA, Advisor on secondment from the
Auditor-General's Office

Christina Assargiotis, Secretary/Word Processor Operator

Lynda Lim, Secretary/Word Processor Operator

CHAIRMAN'S FOREWORD

This report arises from the Committee's examination of the Auditor-General's Report on the financial operations of the Land Commission of New South Wales.

As a result of its initial examination the Committee decided to seek explanations for certain land valuation writedowns and a number of general questions relating to the organisation's efficiency and effectiveness.

It emerged after correspondence from Landcom that whilst accounting practices appeared to accord with Accounting Standards it was very difficult to assess whether the organisation was effective because of a lack of clarity of its objectives.

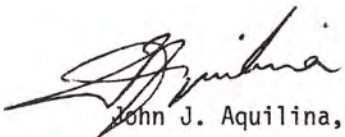
The Committee explored this in evidence with representatives of the Commission and found that although the organisation appeared to be quite efficient and competitive relative to its private sector counterparts its effectiveness was almost impossible to ascertain. It also found that the Commission lacked proper performance measures which is quite understandable since its objectives were unclear.

The Committee is not concerned to question whether Landcom's objectives were appropriate or not, merely to ask what they were. It found that Landcom had interpreted its objectives variously to be: to make land available at the lowest possible price; to promote orderly development by providing a consistent supply of land and by promoting the presence of the private sector of the market, and to promote economic urban development. A close examination of these objectives revealed that they are not completely compatible.

As with a number of other bodies dealt with in previous reports the Committee is again compelled to recommend that clear objectives be established and that the role of Landcom in urban community development be reflected in its objectives, programmes and results.

Only when clear objectives are known can Landcom develop meaningful performance measures and can it too be held accountable to the Parliament and the public for the efficiency and effectiveness of its activities.

I would like to thank members of the Committee for their valuable contributions to this report. I would also like to thank the staff of the Committee, Director Frank Sartor, former Deputy Director Ruth Tait, and Bob Pritchard for their valuable contributions. Lastly I would like to thank Christina Assargiotis and Sandra Vine for typing the report.



John J. Aquilina, M.P.,

Chairman

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BRIEF REVIEW OF LANDCOM

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	. John Henry Plummer, Acting Chairman Land Commission of New South Wales	
	. Brian Charles McElvogue, Investment and Finance Manager, Land Commission of New South Wales	

BRIEF REVIEW OF LANDCOM

Section 1: Summary and Recommendations

The Public Accounts Committee conducted a brief inquiry into the operations of the Land Commission of NSW (Landcom) during 1984-85.

In general, the Committee was impressed with Landcom's efficiency of operation and project management practices but was hampered in its assessment of the organisations effectiveness due to lack of clear objectives.

The major concerns of the Committee focused on the role of Landcom, its relations with the private sector and its overall effectiveness. Underlying conflicts in roles and objectives were also explored by the Committee.

In this brief report, the Committee has made the following recommendations:

- . that the role of Landcom be reviewed in light of current Government priorities; that market segment, pricing policy and policy on profit be determined and that clear objectives be established.
- . that Landcom consider the wholesaling of undeveloped land and joint venture activities, as means of stimulating private sector activity in submarkets dominated by Landcom, without creating undue increases in the price of developed lots.
- . that the Urban Development Committee ensure that its development decisions are based on a full assessment of all costs (including infrastructure, transport and community development costs) and are in line with government policies

- . that the role of Landcom in urban and community development be reflected in its objectives, programs and results
- . that future annual reports include a clear statement of objectives (including any urban development and social objectives) and a comprehensive set of performance measures reporting effectiveness and efficiency in achieving these objectives and targets for the coming period.
- . that the total value of undeveloped land as provided by the Valuer-General be shown in the accounts, at least by way of a note to the accounts.

The Committee wishes to thank the Chairman of the Landcom for his cooperation.

Section 2: Introduction

The Public Accounts Committee expressed interest in the activities of Landcom following the Report of the NSW Auditor-General for 1982-83. In August, 1984, the Chairman of Landcom was invited to appear before the Committee and this appearance was followed by further correspondence and visits by officers of the Committee.

The Committee initially sought the following information

- . The circumstances surrounding the purchase of the parcel of land at Wyong in 1981, which led to a loss due to revaluation of \$1,700,000.
- . A breakdown of the remaining \$4,200,000 of the \$5,500,000 decrease in value of undeveloped land shown in the Income and Expenditure Account for the year ended 30 June, 1983 and comments regarding the circumstances surrounding each transaction that constituted this decrease in value.
- . A breakdown of, and the circumstances surrounding, the valuation writedowns of \$4,420,000 shown in the Income and Expenditure Account for the year ended 30 June, 1983.
- . A breakdown of the sum of \$55,713,000 shown in the Income and Expenditure Account for the year ended 30 June, 1983, including costs per lot incurred in developing both rural zoned land and residential zoned land.
- . An explanation of the Commission's acquisition policies and strategies and how these have lead to overexposure in certain submarkets
- . A breakdown of non-current assets shown in the Balance Sheet as at 30 June, 1983.

- . A breakdown of the investments shown in the Balance Sheet as at 30 June, 1983 and comments on the investment policy followed by the Commission.

To assist its enquiries into the efficiency and effectiveness the Committee also sought a statement of the organisation's objectives. The Committee was not satisfied that the objectives as stated provided a clear guide to action and this led to more detailed enquiries.

As a result of the Committee's enquiries the following major issues emerged that were worthy of comment:

- . organisation objectives
- . performance measures
- . relations with private sector
- . operating efficiency
- . valuation and accounting for land

This inquiry by the Committee was neither comprehensive nor in-depth but it did provide an overview of the effectiveness and efficiency of the organisation and led to the conclusions which are recorded in this brief report.

Section 3: Relevant Background to Landcom *

The principal functions of the Land Commission of N.S.W. are the acquisition, development and disposal of land for urban and public purposes.

Landcom was established by the Land Commission Act, 1976, as a response to the land shortages and rising prices of the late 1960's and early 1970's and an offer by the Commonwealth Government in 1973 of financial help to the States. The Commonwealth would assist the States establish land commissions or similar organisations to compete in the land market as public developers to exercise, through competition, a moderating influence on land prices and a stabilising influence on supply.

By the time the Land Commission of N.S.W. was established, the boom which had inspired the original proposal had collapsed. Throughout 1977-79, the Commission operated in a depressed market where it was able to meet strong price competition and turn the situation to advantage by acquiring a substantial portfolio of undeveloped land at favourable prices.

By 1980, Landcom was the largest producer of residential land in the State, with a yield, in the Sydney area of around 3,000 lots per year.

In 1979-81 there was again land shortage and resulting price escalation in the Sydney region. During this period Landcom maintained its prices at levels related to production costs and at times was selling as much as \$10,000 per lot below the private sector. Because of the extremely heavy demand, ballots were introduced as a means of rationing the available supply of lots.

* Derived from information in Landcom Annual Report 1982

In response to this situation, the Government, in mid-1981, directed Landcom to expand its production and that of the Crown Lands Office to achieve a target of 26,000 lots in three years. Landcom achieved its first year target (4000 lots) but not long afterwards the deteriorating economic situation and rising interest rates combined to cause a rapid contraction of the housing market and subsequent targets were not met. Landcom obtained Government approval to adopt a market-led program which would enable it to regulate supply according to demand while avoiding undue financial risk.

Section 4: Effectiveness of Landcom

In endeavouring to assess the effectiveness of Landcom, the Committee encountered immediate difficulty because it lacked a clear understanding of the organisation's objectives.

This question of objectives was pursued with Landcom and is discussed below.

Landcom assesses its own performance in two areas, financial performance and program performance, with financial performance being measured by profit and program performance by the following indicators:

- . Englobo lots acquired (broad acres)
- . lots developed
- . lots sold

The question of performance measures is also discussed in the following pages.

4.1. Objectives in Legislation

Landcom was initially established, as were land commissions in other states, to assist governments to overcome some of the problems of the land boom of the early 1970's: shortages of residential land and the accompanying rapid price rises.

Landcom was set the task of actively competing in the land market as a public developer to exercise through competition a moderating influence on land prices and a stabilising influence on supply.

The objectives of Landcom as stated in the Land Commission Act 1976 reflect this charter:

"(3) In the exercise of performance of its functions, the Commission shall -

(a) make residential land available at the lowest price the Commission considers practicable having regard to the costs incurred by the Commission in relation to the land and the financial resources available for the Commission's continued operation; and

(b) promote orderly and economic urban development".

4.2. Interpretation

When asked by the Committee for its interpretation of this statement of objectives, Landcom replied:

"In its simplest form, the Commission interprets this to mean that it shall acquire and develop raw land, and market the developed blocks in sufficient quantity and at such a price as to exercise a stabilising influence on what it considers to be any undue pressure for price escalation in residential land. The Commission does not seek to maximise profits, often selling land at prices materially below market value where it is considered necessary. However, it does seek to earn surpluses to protect its financial viability to a degree that is consistent with its role of price moderation. Furthermore, it needs to set prices at a level which will continue to encourage reasonably profitable land development by the private sector, thereby honouring its obligation to promote orderly and economic urban development. Given these somewhat conflicting objectives, the setting of prices is a matter of considered judgement".

It seems that Landcom does indeed have somewhat conflicting objectives and this issue is explored in the sections that follow.

4.3. Analysis of Objectives

4.3.1. Land available at lowest price

Landcom operates in a wide range of markets. Most land owned by Landcom is in areas where zoned land is available in large quantities (so-called "broad acres"). This land, when developed, tends to go to the lower cost home buyer. However, Landcom has taken over the Crown Lands operations and therefore has land available in quite expensive areas such as Little

Bay, and East Wahroonga. Also Landcom itself operates in Glenhaven which is a medium to high priced area and in Fairfield which is becoming a medium priced area.

In determining the price at which it will sell a particular parcel of land, Landcom takes into account:

- . production costs
- . the need to ensure its financial viability
- . market forces

Thus the objective of making land available at the lowest price is not strictly adhered to, particularly in more expensive areas, with market price being taken into account.

The conflict in the objective as stated is that Landcom is expected to sell land at the lowest price and yet coexist with the private sector.

At present, Landcom has certain cost advantages when compared with private sector developers (see Section 4.3.2 below), and these are passed on to land buyers in the form of lower prices. The 1982-83 Landcom Annual Report states:

"Based on market prices prevailing at the time of sale, it is estimated that average prices charged on the 2,961 lots sold in 1982-83 were some \$3,000 below market prices of comparable land. Whilst this margin per lot is considerably lower than in the past two years, it still represents a subsidy to Landcom buyers of between \$8.0 million and \$10.0 million, which amount would otherwise have been added to the net operating surplus for the year".

Part of this subsidy occurs, as stated, because Landcom is not required to make a profit. But part is a cross-subsidy from the wider community because Landcom does not pay a significant number of Commonwealth and State taxes and charges. An estimate of the extent of the subsidy as a result of the non-payment of certain charges is provided on page 13.

For this reason, it is important to ask who benefits from Landcom activities. In evidence before the Committee, Landcom stated that there was no particular segment of the community aimed at in the production of its land but that the efforts of the Commission

"pander mainly to the lower or medium income buyer, but not exclusively".

It seems therefore that the market served by Landcom is not dissimilar to that served by major private developers and the Committee questions whether the cross-subsidies enjoyed by Landcom under these circumstances are justified. This question is pursued in Section 4.3.2. below.

In recent discussions with the Committee it was suggested by Landcom that

"the prime role of the Land Commission is to provide affordable land to low income people".

Such a role might justify the existence of cross-subsidies but can be at odds with the published objective of land price moderation which is described in Section 4.3.2.

The Committee believes it is timely that the role and objectives of Landcom be reviewed in light of current Government priorities.

The question of financial viability is also relevant here. Landcom does not appear to have a clear policy as to what profits and profit margins should be achieved.

The Committee recommends that the role of Landcom be reviewed in light of current Government priorities; that market segment, pricing policy and policy on profit be determined and that clear objectives be established.

4.3.2. Orderly Development

This objective has two components:-

- (i) consistency of supply
- (ii) continued presence of the private sector in the market.

(i) Consistency of supply

When Landcom was first established it became very active at St Clair in Western Sydney. In depressed market conditions, the Commission supplied lots at cheaper prices than private developers; with the result that private developers withdrew from the market. At the same time, Landcom acquired substantial quantities of undeveloped land at favourable prices.

According to Landcom, it now aims to supply more land in times of heated demand and to withdraw from the market in times of depressed demand in order to achieve land price moderation. However Landcom notes that it is very difficult, because of the size of its operations, to quickly turn off production of lots when the market demand falls.

(ii) Continued presence of the private sector in the market

According to Landcom, their overall target is to have a one third market share.

What seems to happen in practice is that the land development market is broken up into a number of submarkets each of which is dominated by either Landcom or individual private developers.

Landcom has explained that it dominates some submarkets because when it enters a submarket, private developers frequently withdraw from active participation in the market (cease developing land) because they are 'wary' of Landcom and because the Commission's cost structure is seen to

be lower. It seems that only owner/builder/ developers can now compete with Landcom, and so in many submarkets, Landcom ends up with a 90% market share.

The implications of this are as follows:-

- . In those submarkets where Landcom is present, it tends to dominate and the reason it dominates is that it offers land at low prices;
- . In those submarkets where a private developer dominates, Landcom is not able to regulate prices.

It is quite possible, that on a macro level, the actions of Landcom do promote a more orderly supply of land. It certainly would appear to be controlling prices. In this regard, the Commission cited South Australia where the role of the Land Commission had been changed to releasing broad acres of land to private developers.

It was claimed that, as a result, developed lot prices have increased in the order of 30% over the last twelve months which is substantially greater than increases in New South Wales over the same period.

However, in N.S.W., there is considerable ill-feeling between private developers and the Commission. Charges from the private sector include:

- . Landcom has unfair cost advantages;
- . it manipulates prices to send private developers out of business;
- . it has "locked-up" broad acres around Sydney.

Much of the criticism from the private sector centred around the cost advantage supposedly enjoyed by Landcom (discussed below).

Cost advantages enjoyed by Landcom as compared to the private sector include:

- . Landcom has compulsory acquisition powers.
- . Landcom is not required to make a profit.
- . Landcom does not have to pay taxes on profits.
- . Landcom does not have to pay land tax and the major part of council rates.
- . Another distinct advantage is the Crown exemption clause which allows Landcom to be exempt from normal conditions of development approval imposed by local councils. These conditions can only be imposed with the consent of the Minister for Planning and Environment. This clearly allows for more expeditious processing of development.

The extent of the subsidy accruing to Landcom as a result of these advantages has not been quantified.

With regard to land tax and council rates, however, Landcom comments in a letter to the Committee dated 8 July, 1985,

"Based upon the undeveloped stocks held by the Commission at 30.6.85, it is estimated that total nett revenue which could have been achieved for Council rates is approximately \$1,000,000 and in regard to Land Tax \$900,000."

Cost disadvantages experienced by Landcom as compared to the private sector include:

- . Landcom has to comply with government regulations concerning employment; particularly public service conditions.
- . Other disadvantages of being a government body include demands for information (from the Public Accounts Committee for example). It was claimed that something like 30% of staff time is spent dealing with the supply of information to government and the public.

- . Additional charges related to the early provision of community facilities.
- . Landcom is expected to, and has produced, lots in times of recession when the private sector has ceased operations.
- . Landcom is expected to produce "the perfect product" in the eyes of the public.

Areas in which Landcom felt there were no differences between itself and private developers were:

- . operating efficiency
- . cost of finance
- . cost of contractors
- . information about land releases

Weighing up the respective advantages and disadvantages, there is little doubt that Landcom is able to operate at lower cost than private sector developers.

As Landcom comments in its letter to the Committee dated 18 September, 1984: "Perhaps a gradual increase in Landcom prices in the lower priced submarkets might encourage a return of the private sector".

Whilst it is a matter of Government policy whether Landcom should be cross-subsidised by other agencies, and therefore is not for the Committee to comment, the Committee believes that the extent of any cross-subsidies should be quantified and regularly reported.

As discussed, Landcom has somewhat conflicting objectives in that it is expected to compete with and yet encourage the private sector. To date, Landcom has focused on its role as a land developer in direct competition with private enterprise. This has resulted in far from harmonious relations with the private sector.

Strategies for improving relations and fostering private sector activity might include the sale by Landcom of broadacres of land to private developers (wholesaling) or joint ventures in land development.

The 1983 Annual Report records successful participation in joint venture developments and the intention to enter into further such arrangements where circumstances permit.

A September 1984 letter to the Committee described current activities of Landcom in the wholesaling of land. It appears that Landcom is testing wholesaling in a few submarkets to see whether it has the desired effect of forging closer ties with the private development industry and freeing Landcom's own resources for use elsewhere - without an undue increase in the price of the final developed lots.

The final result had not been assessed at the time of writing. However, according to Landcom,

"the private development industry via the Urban Development Institute of Australia have announced that they are in favour of Landcom engaging in this practice, subject to the circumstances and conditions surrounding each sale".

The Committee does not believe that Landcom should change its role and become solely a land wholesaler rather than land developer. The Committee recommends that Landcom continue wholesaling undeveloped land, and participating in joint venture activities.

4.3.3. Economic urban development

The second objective of Landcom, as stated in the Act, refers to the promotion of economic and orderly urban development.

From the Government point of view, three issues are important here

- (i) that Landcom operate efficiently and effectively
- (ii) that government urban development decisions are based on a full assessment of all costs: local development costs, infrastructure costs, community development costs (hospitals, schools, public transport etc.)
- (iii) that urban development decisions are in line with Government policies such as urban consolidation and regional development.

The conflict for Landcom is that it is in the land development business while also being an arm of government. It is generally in the interest of Landcom if

- . broad acres of land rather than small parcels are released for development (broad acre development is more economical).
- . any rural land owned by Landcom is rezoned at an early date
- . infrastructure and community development costs are not passed on to land buyers but are paid for by the broader community
- . standards for services are kept as low as possible to keep costs down

However these decisions are not necessarily in the interests of the Government, the community or the future residents.

In establishing a new community, it is desirable to have rapid community development with access to jobs, transport, schools, shops and other community facilities. The choice can be between higher priced land close

to established communities and services or lower priced land in more remote locations with higher infrastructure costs and with a greater risk of the development of community problems and attendant social costs.

The Urban Development Committee is responsible for advising the Government on the rezoning of land for urban development. This Committee has the primary responsibility of ensuring Government objectives are met, while taking into account sectional interests such as Landcom. It is in the interests of the community if all costs are considered in weighing options for urban development.

Although the primary role of Landcom is the provision of land at minimum cost, it does have a role in the development of the local community. In 1982-83, a Community Planning Unit was formed.

"The establishment of the Unit emphasises the Commission's commitment to fostering community development and facilitating the provision of services essential to the well-being of new residents" (page 19 of 82-83 Report).

The Committee believes that Landcom should receive recognition for its achievements in community development and that this activity should be managed in the same way as its mainstream activities.

The Committee recommends

- (a) that the Urban Development Committee ensure that its development recommendations be based on a full assessment of all costs (including infrastructure, transport and community development costs) and are in line with Government policies and planning objectives.**
- (b) that the role of Landcom in urban and community development be reflected in its objectives, programs and results.**

4.3.4. Performance Measures

In publishing its performance and plans, Landcom is constrained by the fact that it is operating in a very competitive market, with much of its data being of commercial significance.

In the 1983 Annual Report, key statistics were published for the year of the report and the preceding year. These statistics related to: lots sold; sales revenue; development expenditure; land acquisition expenditure; funds employed; land trading account gain; and surplus for year. Other statistics were contained in the body of the Report. Details of performance in specific markets were not included for reasons of competitive market information.

The Committee notes the improvement in Landcom's annual report but suggests that future annual reports also include a clear statement of objectives (including any urban development and social objectives) and a comprehensive set of performance measures reporting effectiveness in achieving these objectives and targets for the coming period.

Section 5: Efficiency of Landcom

5.1. Cost of Lots

As discussed above, Landcom is charged with making residential land available at the lowest practicable price. In the 1982-83 Annual Report, an estimate is provided of the price differential between Landcom and private sector land:

"Based on market prices prevailing at the time of sale, it is estimated that average prices charged on the 2,961 lots sold in 1982-83 were some \$3,000 below market prices of comparable land".

This differential occurred because:

- (a) Landcom is not required to make a profit
- (b) Landcom is exempt from certain taxes and charges and so has a cost advantage. (See Sections 4.3.2. and 4.3.1.)
- (c) Landcom appears to utilize modern management techniques. In correspondence with the Committee, Landcom claimed it had similar operating efficiencies to private developers.

The Committee has no reason to dispute this claim and is impressed with the commercial approach taken by Landcom in endeavouring to keep costs to a minimum. Initiatives listed by Landcom include the following:

- . competitive tendering for contract work wherever possible
- . pressure on suppliers of services to keep costs to a minimum
- . adherence to workable, economical technical standards
- . the establishment of a policy on the dual use of drainage of open space reserves.
- . the contesting of some requirements of local Government authorities.

"A project review to assess the currently anticipated financial outcome is usually performed at least annually, and more importantly just prior to when the precinct is to be put out to tender. In this way the Commission does not allow the development process to proceed unless it is satisfied with the projected financial outcome. A further project review is conducted at the conclusion of development when the costing, which is then far more certain, is used in consideration for the setting of the price of the individual blocks of land. Thereafter throughout the selling process further project reviews may be conducted."

Thus Landcom and private sector developers use similar systems with project managers, external consultants and contractors. This system provides flexibility as demand changes and minimises costs. Landcom keep a register of consultants and their fees are determined taking into account scales of fees issued by the professional bodies. In discussion, the Chairman of Landcom claimed that Landcom had been paying fees at a significantly lower rate than the private sector but that at present the fees were similar in some professions.

The overall impression gained, from discussion and examination of Landcom project documentation, was that Landcom was managing its projects in a very professional way.

5.3. Wyong Project

In a report dated 2 November, 1984, the then Auditor-General made the following comments on land acquisition policy:

At page 117 of Report No. 12, the Public Accounts Committee refers to a continuing examination of aspects of the operations of the Department of Environment and Planning, Land Commission and Macarthur Growth Area in respect of land acquisition and development.

In the main the Land Commission's operations have been profitable but one particular acquisition could serve as a useful case study of the Commission's feasibility and acquisition procedures. In 1981 the Commission acquired a parcel of land in the North Wyong area for \$1.8 million. The Commission files contain references to private valuations as far apart as \$1.4 million and \$3.3 million. Feasibility

studies also set out a range of possibilities for cost and availability of sewerage services - a major factor in readying the land for sale.

For the 1982-83 accounts, the Valuer-General placed a figure of \$500,000 as being an appropriate current value. A provision was made to cover the decrease in value in that year's accounts so bringing the carrying value down to \$500,000. At 30 June, 1984 the carrying value was \$625,000.

Subsequent to the 1982-83 accounts, reference by me to an independent consultant produced the observation that the market for development sites had collapsed by April, 1981. Whether or not the purchase by the Commission was sound, is beyond the scope of my present reviews. However, as an examination of the circumstances may assist the Public Accounts Committee in its review of practices and procedures, a copy of this Report is being sent to the Committee."

An examination of the relevant Landcom file, by officers assisting the Committee, revealed that early in 1981 Landcom discussed with senior officers of Wyong Shire Council the land shortages, and rapidly escalating prices, in the Shire. The project in question was the largest consolidated parcel of land in the "release" area and Landcom started negotiations for its acquisition.

Prior to purchasing, Landcom was aware of most of the disadvantages of the site, which included: sewerage not available for 3-5 years; partly affected by transmission lines; possible landslip areas; and proposed medium density zoning in view of possible stability problems and to preserve tree cover. The possibility of mine subsidence problems had not been indicated by Council or other authorities.

Two private valuations were obtained prior to purchase. The highest valuation of \$3.3 million was based on the then going rate for similar blocks of raw land in the vicinity. This method appears to be out of favour in valuing circles and inappropriate in view of the large area involved. The lower valuation of \$1.4 million was based on anticipated selling prices over a three stage release and taking into account subdivision costs and likely profit and risk factors. This method

appears to be a sound one for arriving at a purchase price. The risk, however, is that it involves the making of certain assumptions which may not eventuate.

The purchase price of \$1.8 million was \$400,000 higher than the lowest valuation and averaged \$4,286 per lot. The excess over the lowest valuation averaged out at \$952 per lot. The Committee is unable to determine whether \$1.8 million was a fair price at the time of the purchase, but does not believe it was grossly exorbitant.

The subsequent general fall in land prices did not last as long as elsewhere in this part of Wyong. The Gosford/Wyong Land Market Study prepared by Hirst and DeFina in May, 1983, indicated that selling prices in nearby areas had recovered virtually to the level existing at the time of the Landcom purchase.

About October, 1983, the Valuer-General valued the Wyong parcel at \$500,000. This increased to \$625,000 as at 30 June, 1984. Englobo land which is not actually being developed (as in this case) is valued by him at current market value. However, the Commission had unsuccessfully asked for it to be valued as "trading stock in the hands of the Commission". Landcom sees itself as a trader with considerable ability to remove obstacles to its development projects. The Valuer-General's Office sees limits to this ability. In this case, for example, Landcom's continuing difficulties over the sewerage connections.

The Valuer-General's Office will value land as trading stock only if it considers the land is ripe for development. That is, that there is convincing evidence that zonings have been approved, sewer and other facilities are readily available, etc. The valuation for this parcel at \$500,000 appears to be based, not on its rural value, but on its "potential" value. Until sewerage and other problems are solved, the Valuer-General's Office would not be likely to regard it as trading stock.

Landcom's private valuer seems to have used the trading stock method to arrive at his 1981 valuation of \$1.4 million. While inbuilt risks, such as the sewer, did surface later they do not detract from the legitimacy of the valuation given.

Allowing for an element of "crystal-ball gazing", the trading stock method seems the most useful in determining a purchase price. Where land is held for a lengthy period prior to the physical prerequisites for development being attained, the Valuer-General's Office "potential value" is more useful for financial statements. Such use should not automatically be assumed to mean that money has been lost on the acquisition.

As a general comment, quoting unexplained valuation figures in financial statements and notes does not help the reader. Terms such as "fair market value" and "current market value" lack precision. They should be qualified by a brief explanation of the basis upon which they have been assessed and the purpose for which they were intended. In the final result, the only true value of land is the price the buyer will pay.

In summary, it is apparent that Landcom could have explored more rigorously every possible adverse factor prior to purchase but the Committee recognises that there are inherent risks in buying land before zoning and availability of facilities are finalised. If no risks are ever taken, Landcom's profitability as a developer could well be diminished. It appears that the risks taken by Landcom in this particular project were no greater than those taken by private developers.

The Committee also considers that the pre-purchase valuation of \$1.4 million and the Valuer-General's later "potential" value of \$0.5 million were each properly assessed at the times they were given and for the purposes they were meant to serve.

5.4. Performance Measures

The Committee was satisfied from its overview of project management and internal project documentation that a system of performance measures is in use within the organisation. It also appreciates the possible commercial significance of Landcom performance data.

The Committee recommends however that further efforts be made to identify performance measures relating to efficiency suitable for publication in the annual report.

Section 6: Valuation and Accounting for Land

6.1. Decrease in value in 1983 Accounts

The Income and Expenditure account for the year ended 30 June, 1983 showed a decrease in the value of undeveloped land of \$5,500,000. In reply to an inquiry from the Committee, Landcom provided a detailed breakdown of this decrease in value and the total provision of \$6.7 million.

The following figures were extracted from this reply:

Concerning undeveloped land at 30 June, 1983:

Total book value	= \$65,248,988
Total Valuer General valuations	= \$75,461,000
Total variation	= \$10,212,012
Writedown provision 30 June, 1982	= \$ 1,200,000
Increase in provision for 1982-83	= \$ 5,500,000

According to Landcom's letter to the Committee dated 10 November, 1983:

"The provisions result from those undeveloped land properties where the book value of the property (including accrued interest and other charges) exceeds the value assessed annually by the Valuer-General. In cases where the value of undeveloped properties exceeds the book value, no account is taken of this upward revaluation - in other words, they are not offset as a credit against the total provision for the properties for which the cost exceeds the value. The principle is that if a loss is foreshadowed (even at that early pre-development stage), a provision for decrease in value is made ...

One final point on this subject is that the provision for decrease in value required by this process will vary considerably upwards or downwards from year to year, emphasising the volatility of the provision account, which should be regarded as a warning sign and not a specific loss".

The Committee accepts the conservative accounting practices adopted by Landcom, as they have the advantage of giving early warning of possible future losses.

The Committee notes however that although an increase in provision of \$5.5 million has been provided, the total valuation of land by the Valuer-General is higher than book value by \$10.2 million. The Committee believes that this information should be available to the public.

The Committee recommends that the total value of undeveloped land as provided by the Valuer-General be shown in the accounts, at least by way of note.

6.2. Wyong Project

A major item in the provision for decreases in value of undeveloped land was a parcel of land at North Wyong (Project 134) purchased in 1981. This parcel accounted for \$1.7 million of a total decrease in value of \$5.5 million in 1982/83.

In response to a question from the Committee, the Commission provided additional detail and explanation in their letter of 10 November, 1983, viz:

"At 30 June the book value of this investment was \$2,129,335.06, the detailed components being:

Land Purchase	\$1,800,000.00
Cost of Purchasing	13,950.00
Capitalised Interest	314,027.06
Preliminary Studies	<u>1,358.00</u>
	\$2,129,335.06
Valuer General's Valuation	<u>500,000.00</u>
<u>Variation</u>	<u>\$1,629,335.06</u>

Provision for Decrease in
Value 1983 Accounts \$1,700,000.00

As to an explanation for this large provision, the following is submitted:

Three of the assumptions made in the feasibility study on which our original purchase price was based have been undermined by later developments.

- (i) The Council has altered its strategy for the provision of sewerage, and this is likely to significantly delay the time at which the estate can be developed and sold.
- (ii) Contrary to earlier advice from the Department of Mineral Resources, there is now a possibility that the estate will be subject to the provisions of the Mine Subsidence Act. This may reduce the realisable market prices for developed lots.
- (iii) The market for developed lots in the Wyong Area is currently weak, although medium term forecasts remain unaffected.

Investigations on these matters are continuing and we are therefore not yet in a position to give a firm view of the future profitability of this project. Consequently, we have accepted the Valuer-General's figure, although we are inclined to consider it unduly low."

The difference in the valuations obtained by Landcom from its private valuers and from the Valuer-General was discussed in subsection 5.3 of this Report. The difference of \$1.3 million between the valuations is included in the provision for decrease.

The Committee considers that, in the circumstances, Landcom has adopted a prudent accounting treatment. The extent of losses, if any, on this project cannot be accurately determined until after the land is sold.