TURNER DRAKE & PARTNERS

Newsletter

Vol. 2 No. 44

Winter 1992-93

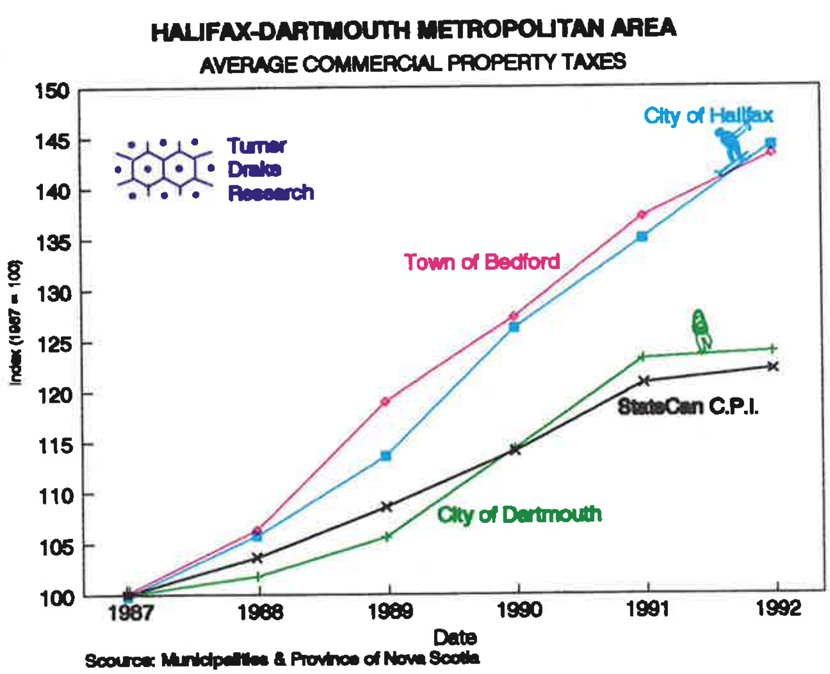
UPDATE

So the recession is over; we are not going downhill anymore? Hmmm, well maybe . . . Here in Atlantic Canada, New Brunswick has weathered the storm better than the other provinces, followed in ordinal ranking by Prince Edward Island, Nova Scotia and Newfoundland. So what is the mood right now, particularly as it impacts upon real estate?

The velocity of money circulating through the real estate sector of the economy has slowed to a snail's pace. The situation is exacerbated by the financial institutions. Shuddering under the impact of the financial difficulties of Olympia and York, Bramalea, Trizec, et al, and presented with the spectacle of trust and insurance companies such as Central Guaranty Trust Company and Sovereign Life Insurance Co. collapsing under the weight of bad commercial real estate loans, the financial institutions are loathe to touch real estate. As a result it is becoming increasingly difficult to obtain mortgages, not just for new purchases but also to upgrade existing properties: so owners of office buildings for example, find it difficult to raise the cash necessary to fund tenant inducement packages. Piling misery on top of misery, are the taxing demands of rapacious government, especially at the municipal level.

Carpe diem! If you are a landlord or tenant, this Newsletter will tell you how to protect your real estate from the covetous designs of government. If you are a lawyer, you should be interested in our comments on expropriation. So put down your bank statement, pick up your coffee, turn off the phone and read . . .

"Fools and their Money are Soon Parted"



Governments at all levels (Federal, Provincial, Municipal) are running out of money. They pay lip service to the concept of reducing their own costs and wait instead for the recession to end (and hence tax revenues increase), or for the new management team to resolve the problem after the next election. The private sector meanwhile is going through a gut wrenching period of re-adjustment that, for some sectors of the economy, will continue for several years. Adding to the private sector's woes is the knowledge that in their fight to be competitive, they have no control over that part of their overhead represented by government taxation. They also have to work within a legislative environment which owes more to history than efficiency. For example there are ten municipalities in greater Charlottetown, P.E.I., a metropolitan area with a population of just 60,000. Apart from the sheer duplication and attendant cost of municipal services, there is the cost of operating in such a fragmented environment. Just try getting information on the availability of industrial sites! And that is only the tip of the iceberg.

Newsletter is published by Turner Drake & Partners Ltd., Real Estate Counsellors, Brokers & Valuers
6182 North Street, Halifax, N.S. B3K 1P5 Tel.: (902) 429-1811 Fax.: (902) 429-1891

There is also provincial and municipal infighting as governments compete against each other, funding public projects or providing grants to encourage firms to settle in their area. Thus the taxpayers of the City of Halifax can sleep soundly in their beds knowing that $6 million (by some estimates) was spent on land acquisition and road improvements to encourage the Price Club, a discount retailer, to locate in their Bayers Lake Industrial Park even though the company was reported as having already made the decision to move into the area, albeit across the harbour in the City of Dartmouth. Similarly the taxpayers of the Town of Bedford can enjoy the quiet confidence of knowing that their little town has poured approximately $19 million into Bedford Basin to create the site of a new town centre . . . strategically located around a sewage treatment plant. Aaah! The aroma! Is that money we smell a' burning . . . or something a little less salubrious? (To be fair the municipality argues that their project was never meant to be financially self supporting and that they have actually created $11.0 million of public open space in addition to the $5 to $6 million they hope to recoup from land sales . . . me thinks they confuse cost with value!).

This type of fiscal lunacy is not restricted to Nova Scotia, nor we suspect to the Atlantic region. We confidently predict that it will continue unabated. We also predict that it, and the failure of the public sector to come to grips with its operating costs, will result in an increasing demand for more tax revenue, especially at the municipal level. The graph on the previous page shows the average taxes paid by a commercial property in each of the three municipalities that comprise the bulk of the Halifax - Dartmouth metropolitan area, plotted against the baseline Consumer Price Index. (Our choice of these municipalities was dictated by nothing more sinister than the fact that we had the data readily at hand. Other examples abound throughout the region . . . elsewhere in the land too we presume).

Halifax, N.S. Commercial Building	Real Estate & Business Occupancy Taxes as a % of Total Operating Expenses
A	40%
B	42%
C	48%
D	38%

Source: Turner Drake & Partners Ltd. Field Survey

So what is the moral of this tale? **Adopt a defensive posture.** Whether you are a tenant, or a landlord, you should analyze the taxing history of the various municipalities that comprise the metropolitan area in which you wish to be situated and make your location decision accordingly. The accompanying table details the results of an analysis of four commercial buildings picked at random, in the City of Halifax. It details a typical tenant's tax load (Business Occupancy plus Real Estate) expressed as a percentage of their pro-rated share of the building's operating cost (including Business Occupancy and Real Estate Taxes but excluding rent). Somewhat staggering isn't it?

The municipality's past behaviour appears to be an indication of its future taxing patterns too: old habits die hard. So, if you intend to occupy or own a property for a specific period of time, go back and investigate the municipality's taxing history for at least the same period. Don't be fooled by the mill (tax) rate. The base date for assessing property changes periodically (every year in New Brunswick and Prince Edward Island, each three years in Nova Scotia, and at five yearly intervals in St. John's, Newfoundland). We'll be glad to assist you, if you are unsure on how to proceed.

Sometimes you have no choice: considerations other than real estate costs dictate where your business has to be located. In those circumstances all you can do is to take every opportunity to scrutinize your assessment to ensure that you are not unfairly assessed. If you are a tenant you will need your landlord's co-operation in this exercise.

PROPERTY TAX DIVISION

Edmundston Mall, Edmunston, N.B.
($50,000 in tax savings)

Nova Scotia - this is a tri-annual re-assessment year. Assessment Notices were mailed on the 18th January and you have 21 days from the date shown on the Assessment Notice, in which to appeal. Your assessment will probably have decreased from 1992, but don't be deceived, your taxes may well increase! The aggregate assessment for non-residential property has gone down in most municipalities so the tax rate will go up, even if the municipality does not increase its operating budget. However, the municipality will not notify you of your tax liability until the period for appealing your assessment has passed. (All municipalities in Nova Scotia have recently changed their tax year so that it no longer coincides with the assessment year). In addition the Province is introducing legislation to eliminate Business Occupancy Tax and to roll it instead into the Real Estate Tax. The Province estimates that Real Estate Taxes will increase by 30% as a result and (a double whammy) the property owner will now, in effect, pay Business Occupancy Tax on any vacant space. Previously this was untaxed. This will probably not take effect until 1994; however since 1993 is a tri-annual re-assessment year your new (1993) assessment will remain the same in 1994 and 1995 unless you successfully appeal it.

The Province has also indulged in some eleventh hour jiggery pokery with residential assessments. They have reneged on their commitment to re-assess residential properties at the same (1st January 1991) base date as the commercial properties and have rolled back the residential assessments to the former (1st January 1988) base date. The effect will be to re-adjust the tax load so that it bears more heavily on non-residential properties (this **is** an election year!).

Million $Dollar$ Man

Tom Mills, the Manager of our Property Tax Division is an expert in property assessment. Tom holds the CAE designation of the International Association of Assessing Officers and of course is an accredited appraiser. He has eighteen years' experience in property tax work. Property tax assessment is a specialist field requiring a different focus and skills set than property appraisal. The proof of the pudding is in the eating. Tom and his staff save our clients in all four Atlantic Provinces about $1.0 million per year in taxes. He has formulated a set of decision rules that you can utilize as a preliminary screening device to determine whether you are overassessed. They were mailed to property owners in the Province on the 18th January: please give us a call if you did not receive your copy.

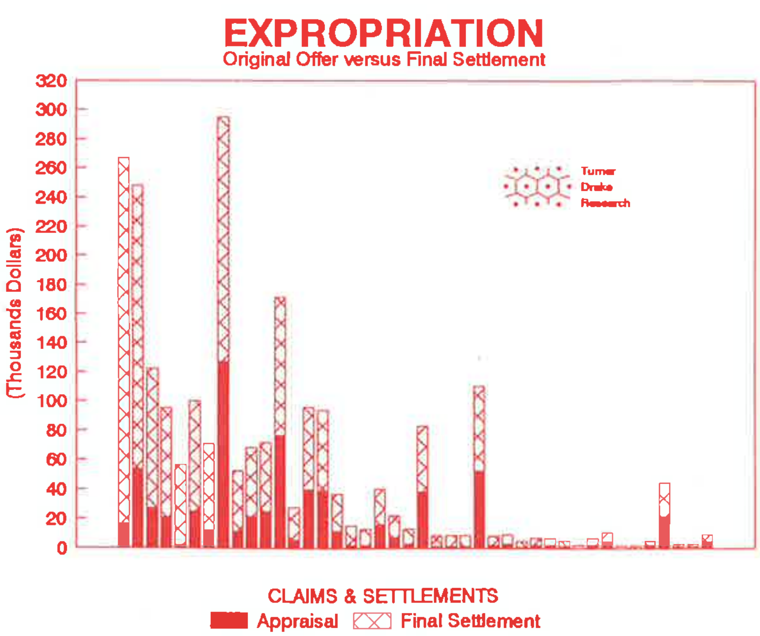
If you have Manufacturing and Processing Equipment, Tom is adamant that you should appeal your assessment. Not all components of equipment are assessable. Last year we saved some of our Nova Scotian clients $20,000/year in taxes on their Commercial Equipment Assessment. We will be happy to advise you on the appropriate wording to use for your grounds of appeal.

Newfoundland - St. John's - your tax notices were mailed in mid December and the 21 day appeal period has now expired. We are undertaking an increasing amount of tax work in St. John's so if you have appealed, particularly if you own an office building, please give us a call (1-800-567-3033). **Corner Brook** property owners: hang in there, you will receive your 1994 assessment notice in June.

Prince Edward Island & New Brunswick - we successfully alleviated clients' tax burdens last year. We look forward to working our magic this year too.

CONSULTING DIVISION

Mainly for Lawyers (Expropriation)



Most acquiring authorities attempt to negotiate a settlement with the property owner, prior to expropriation. It has been our experience that, unless the acquiring body is the Federal Government, the property owner will not be notified of his/her rights under the Expropriation Act. Indeed, even after the property has been expropriated, it is highly unlikely that the acquiring authority, unless they are the Federal Government, will so advise the property owner. Some legislation, such as the Federal and Nova Scotia Expropriation Acts, provides that the property owner be entitled to proper legal, appraisal and other professional advice.

Some acquiring authorities support their offer with an "appraisal". It has been our experience that these appraisals do not adequately address all of the heads of claim, if indeed they address them at all. In order to test the validity of these "appraisals" we ran a statistical analysis on the initial offers to the property owners and compared them with the final settlements. We found that:

(1) An offer supported by an appraisal was no more accurate than an offer where no appraisal had been prepared at all! (All of the appraisals had been prepared by individuals holding the AACI designation i.e. they were accredited appraisers of the Appraisal Institute of Canada).

(2) The final settlement bears no real relationship to the initial offer: on average it is 3.1 times the original offer but there is a wide variation. Initial offers, whether they are supported by an appraisal or not, should therefore be ignored since they are neither valid nor reliable.

Valuing the loss suffered by a property owner from a road widening, powerline or other right-of-way is a specialist field. Most "accredited appraisers" have no education in the subject (their course material consists of one 3 hour lecture!) so the results uncovered by our analysis are not surprising. This lack of knowledge is evident in the appraisals we are asked to review. Most of them have been completed using a "cookie cutter" approach as part of a mass appraisal of the right-of-way. They completely ignore the specific effects on each property and are not worthy of serious consideration. There are a few appraisers in the Atlantic Region with the specialist knowledge necessary to competently assess compensation: however they appear to be employed by acquiring authorities but rarely; presumably because of cost considerations or other reasons. As a consequence it is always necessary to subject the acquiring authority's appraisal to scrutiny by an expert in the field. Often the appraisal is of such low quality that peer review is impossible and it will be necessary to undertake a proper valuation. Our senior staff have the necessary education, training and experience in expropriation work and undertake assignments throughout the four Atlantic Provinces.

Get expert valuation advice for your clients: our free brochure on expropriation "Beware of Strangers Bearing Gifts" is available for the asking.

BROKERAGE DIVISION

Our Brokerage Division is very active in leasing (retail, office, industrial) and sales (industrial, commercial, investment property and raw land for development). We focus primarily on properties located in the Halifax-Dartmouth Metropolitan Area though our marketing reach extends across the country because our client base is continent wide. We also work with brokers throughout Atlantic Canada and co-operate with them to provide additional marketing reach of an indepth nature.

Sales

Industrials - there is a good selection of properties available and purchasers are re-entering the market. Most buyers are arbitragers or owner occupiers who are interested in acquiring the property now, with as little financial commitment as possible, in the expectation that rents and capital values will start to rise again. Since most of the real estate being offered for sale is "distressed property", the vendors, usually financial institutions, are "willing to deal" on mortgage terms. There are excellent buying opportunities available: we believe that this is the optimum time to buy. **Retail -** there is an excellent selection of shopping plazas available. However most of the vendors are under no compulsion to sell and are holding out for pre-recession prices. However a number of strip malls will come to market shortly, placed there by motivated vendors. These should present buying opportunities for an aggressive manager. **Apartments -** there is a moderate demand for apartment buildings in Halifax Peninsula South but the available properties are overpriced. A number of apartment buildings will be coming to market in Dartmouth's Highfield Park area. Income streams from apartment properties here are of poor quality. However, provided the properties are acquired at a price which provides a high return (commensurate with risk) they are a speculative "buy". Widows and orphans should pass on this opportunity though. There is a steady and strong supply of apartment buildings for sale in Spryfield. Demand continues to be steady and non-existent: excellent buying opportunities exist for masochists. **Sub-Division Property -** we have a 694 acre sub-division in the Lawrencetown area which is very suitable for homes in the $100,000 to $120,000 range. The low downpayment (5%) and mortgage rates have really stimulated this sector of the residential market and we anticipate that housing starts will strengthen into a boom this year. The mild winter (so far!) is helping too. Serviced land in Dartmouth is diminishing rapidly: Montebello and Portland Estates are the only major subdivisions still available. Cole Harbour too is running out of serviced building land; so Lawrencetown is developing steadily. This subdivision is a good land banking opportunity for a residential developer.

Excellent financing is available from the vendor. **Automobile Dealership** - this is an opportunity to buy into burgeoning Sackville, the Metropolitan Area's major suburb which already boasts a population of over 31,000.

Leasing

We are pleased to announce the appointment of Russ Allen as the Leasing Consultant in our Brokerage Division.

Russ joined us six months' ago when he returned to the (comparatively) balmy weather of Nova Scotia from Alberta. He has extensive experience in leasing and shopping centre management in the Maritimes and Western Canada. Russ is well used to coping with difficult leasing situations so the type of creative leasing packages that are now the norm, rather than the exception in these economic times, are grist to his mill.

Russ reports that there is increasing activity for office and industrial space. Tenants have come to the conclusion that it is now "decision time": the rental market has bottomed out and the economy is on the mend. They realize that the tenant inducement packages currently offered (leasehold improvements, rent free periods) may not be available six months' hence. There are grounds for their concern. Landlords are no longer as willing to "deal" on lease rollovers, apparently confident that their negotiating position is strengthening. **Office** demand is being stimulated by two types of activity, in roughly equal proportions: businesses downsizing or upgrading. Expansion, or tenants new to the area, are the exception rather than the rule. Businesses that are downsizing have apparently come to the conclusion that the end of the recession will not bring growth for them, so they are taking advantage of the present leasing situation before landlords withdraw their inducement packages and start raising rents. Businesses who are upgrading, are often not expanding their space, but wish to capitalize on the present leasing situation before the upswing robs them of the opportunity. The same situation pertains with respect to **industrial** demand. However most industrial tenants appear to be upgrading, seeking the same size, but higher quality space, for the same rent, rather than downsizing. **Retail** demand continues to be very soft and we anticipate that it will further weaken during the first quarter of 1993.

CITY PROFILE - ST. JOHN'S

Down . . . But Not Out

The denizens of this fair city possess a fine sense of humour, an indispensable asset in a place where you always seem to be walking into the wind. Perhaps it is this foible of nature, never having the wind at your back, that has developed in the citizens of St. John's the knack of living for today: tomorrow after all is another day. So in a city located in a province beset by problems, optimism not pessimism, prevails. "She'll be right" is a colloquial expression of another island on the far side of the world. In Newfoundland, as in its native New Zealand, it is a fitting sobriquet. Hibernia may hang in the balance, the cod fishery may be beyond coddling: St. John's is still soldiering along.

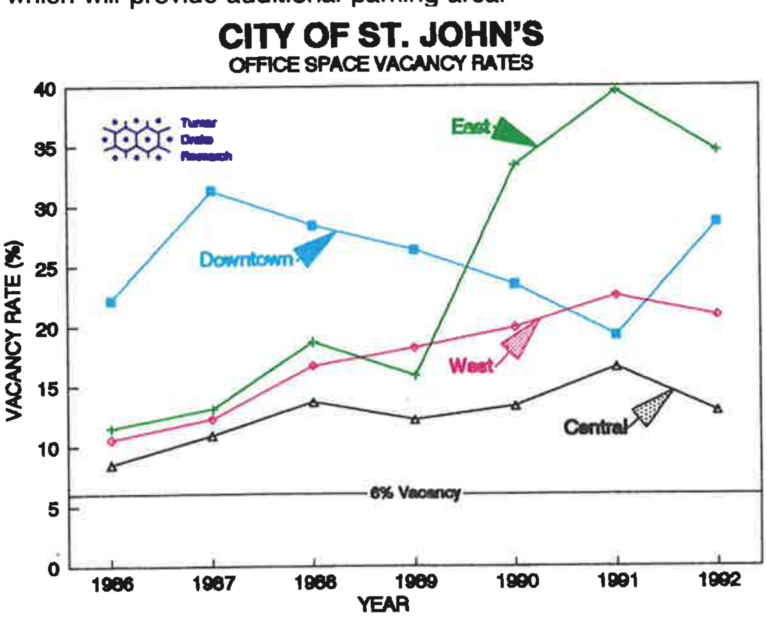
There are some wounds though. This melange of multi-coloured mirrors (see photograph) would be a credit to any city and the developers, Cabot Place Developments Ltd. and the Manufacturers Life Insurance Company can be rightly proud of it. The 276 room Radisson Plaza Hotel and Convention Centre and the two office towers, Cabot Place Phases I (NLA 137,000 ft.^{2}) and II (137,000 ft.^{2}), were to be joined by a third office tower of similar size. However Phase II, the pink tower still stands empty: mute testimony to Hibernia hopes that have yet to materialize.

Central Business District

St. John's, perhaps more than any other city in Canada other than Ottawa, has been fashioned by the Federal Government. Thanks to the latter, the area (City population [1986]-97,215; C.M.A. population [1992]-164,000) has a superb road network which ensures that most of the urban hinterland is easily accessible. During the last decade this has resulted in much of the commercial development taking place outside the City's central business district. Office development has migrated to greenfield sites on, or proximate to the Crosstown Arterial/Prince Philip Drive ring road.

The Provincial government lent impetus to this process when it constructed the West Block, a 300,000 ft.^{2} office complex adjacent to the Confederation Building, and drained demand from the downtown. Crown corporations such as Newfoundland and Labrador Housing Corporation and Newfoundland Hydro have been part of this trend. The Federal Government too appears to prefer peripheral locations and is currently building the R.C.M.P. headquarters near the Northwest Atlantic Fisheries Centre, 3 kilometres east of the C.B.D. Some private sector office development has migrated to suburban locations such as the O'Leary Industrial Park, but it has not turned its back on the downtown to the same degree as the government. It is an interesting dichotomy.

Tony de Jong, the Director of Planning for the City of St. John's argues that decentralization of office space is a natural process and that developers, whether public or private, will choose the location that best suits them: land ownerships in the downtown area are fragmented; services are old; and there are topographical constraints. Notwithstanding this philosophical rationalization, the result of the syphoning off of public sector office demand from the C.B.D. is to deny it the polish and relative affluence normally exhibited by a provincial capital. In addition the pattern of new development in the central business district lacks focus and is randomly distributed. This sporadic pattern of development is partly a response to physical, historical and planning constraints. The latter, the result of public concern about the threat posed by new development to the heritage of the old city, restrict development in much of the downtown to four storeys. Recent redevelopment has therefore occurred on the periphery of the old commercial area. Thus there is a major redevelopment (Radisson Plaza Hotel; Cabot Place - see photograph) on the western periphery and another in the east end (The Baine, Johnston Centre; Fort William Building; Hotel Newfoundland) with other modern office buildings (Journey's End Hotel; Sir Humphrey Gilbert; T.D. Place; Fortis Building; Atlantic Place; Scotia Centre) scattered infrequently between. The planning controls restrict much of the development activity in the old downtown to renovation projects. The former Royal Trust tower was renovated in 1989 and renamed the Fortis Building, by Fortis Properties, a subsidiary of Newfoundland Power. The building occupies a prime site on the waterfront, and the renovation has breathed new life into the property. Fortis Vice-president John Walker, has a well focused strategy for his company and its property holdings. Fortis has already renovated the Harris & Hiscock Building- NLA 10,000 ft.^{2} (since renamed the Vogue Building) a smaller, two storey building in the same block and is currently doing so with a second similar office property, the Delgado Building-NLA 10,800 ft.^{2}. Two more properties have just been purchased, also in the same block, 50 Harbour Drive-NLA 10,000 ft.^{2} which is in near leasable condition, and an old warehouse which will provide additional parking area.



Source: City of St. John's Planning Department

We have plotted the vacancy rates for office space in the various parts of the city on the accompanying graph. Normally, when the vacancy rate in the existing office inventory falls to 8% developers start assembling land for redevelopment. A major expansion of the office inventory usually takes place when the vacancy rate in the existing inventory has fallen to the 6% baseline. As the graph indicates, office development in St. John's is not for the faint hearted. The euphoria over Hibernia encouraged overbuilding and the Province did not help when it built its own space, the West Block. The pattern of new development in the downtown area, constrained as it is by physical, historical and planning considerations does not maximise value and contributes to the vacancy rate. The large increase in the downtown vacancy rate in 1992 is due to the opening of Cabot Place Phase II. Office properties in the C.B.D. continue to be a "speculative play"; however now that Hibernia appears to be back on track St. John's is worthy of serious consideration by investors with deep pockets, an appetite for risk, and the right local partner.