

Financial Feasibility of Co-purchasing Office Space

Prepared for Children and Family Counselling Association of Victoria
(CAFCA)

And three non-profit partners:

Phoenix Human Services Association
Community Social Planning Council of Greater Victoria
John Howard Society of Victoria

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Executive Summary

This research project explored the financial viability of co-purchasing a commercial building for administrative space for Children and Family Counselling Association and its partners: Phoenix Human Services; Community Social Planning Council of Greater Victoria and the John Howard Society of Victoria.

The project looked at several scenarios:

1. purchasing a commercial space with a minimum of 13,523 square feet to co-locate the four agencies.
2. purchasing a commercial space of 20,000 square feet, 13,523 for the agencies themselves and 6500 square feet to lease to non-profit tenants.
3. purchasing a commercial space with a minimum of 20,000 square feet to co-locate the four agencies (including the Phoenix Administrative area)
4. purchasing a commercial space with a minimum of 30,000 square feet, 20,000 to co-locate the four agencies (including the Phoenix Administrative area) and 10,000 to lease to non-profit tenants.

Scenarios also show possible revenues and expenses for recent commercial listings in Victoria that meet some of the requirements. These are: 751 Vanalman for \$2,445,000, 474 Gorge Road East for \$2,990,000.775 Topaz for \$4,800,000.

One-time expenses of approximately include legal fees, environmental assessment, property assessment, and building inspection. Fees for property leasing and management depend on the lease value of the building. Property purchase tax as well as property taxes are based on property value. In every scenario provided, current rents are used as agencies mortgage contributions.

The maximum conventional commercial mortgage the agencies qualify for is \$1,800,000 with a \$600,000 down payment, for a total purchase price of \$2,400,000. There have not been any Victoria listings in the past 2 years, of commercial space for that meets agency needs.

VanCity specializes in Community Business Banking to support non-profit agencies, providing up to 100% financing for agencies who can demonstrate they have the cash flow. Based on financials provided, Vancity Credit union will finance 75% of the mortgage up to a maximum of \$2,250,000. Vancity Capital Corp will finance the remaining 25% at prime plus 3.0%.

Conclusion: In 6 of the 7 scenarios considered, agencies finish in a deficit position ranging from \$179,578 in the first year to \$5,332 in the second year. In Scenario 2 only, the agencies finish with \$18,223 at the end of the second year. **The four agencies combined can reasonably expect to be approved for financing of \$3,000,000 with a total purchase price of \$3,600,000. For this price, they can reasonably expect to find a property that meets their combined needs.**

Commercial Real Estate in Victoria

Properties – Sold

PAST SALES					
ADDRESS	PRICE	DATE	LOT SIZE	BLDG SIZE	\$ / SQ FT
561 Hillside	\$1,070,000	Feb 07	11,056	9,850	\$108.00/sf
791 Cave	\$825,000	Jul 07	8,228	4,925	\$167.00/sf
751 Vanalman	\$2,445,000	Nov 07	33,000	11,937	\$204.00/sf
508 Hillside	\$1,600,000	Dec 07	14,384	8,752	\$182.00/sf
643 David	\$1,125,000	June 08	10,788	10,095	\$111.00/sf
905 Ellery	\$1,690,000	June 08	15,843	10,177	\$166.00/sf
407 David	\$1,425,000	Jan 09	14,400	4,400	\$323.00/sf
Pending	\$925,000	Feb 08	10,000	5,000	\$185.00/sf

Properties – Currently Listed

CURRENTLY AVAILABLE (sample)				
ADDRESS	PRICE	LOT SIZE	BLDG SIZE	\$ / SQ FT
775 Topaz	\$4,800,000	18,556	23,615	\$203.00/sf
474 Gorge	\$2,990,000	27,755	17,000	\$175.00/sf
849 Orono (Langford)	\$2,600,000	29,000	14,000	\$185.00/sf
1120 Hillside	\$1,990,000	9,842	4,200	\$473.00/sf
2925 Bridge	\$1,200,000	7,500	3,000	\$400.00/sf

Provided by Mark Litwin, Associate, Commercial, Industrial and Investment Sales, Leasing and Development, Royal LePage Coast Capital Realty. Other listings attached

Closing Costs

Legal Costs

Each agency must be represented individually by different law firms in the transaction. This cannot be a board member. Ideally, the newly formed entity will be represented by an independent firm. The purchaser is also responsible for the lender's closing costs.

Therefore six sets of legal costs = \$20,000

Property Purchase Tax

Property Purchase Tax (Property Transfer Tax) is a land registration tax. It must be paid when an application is made at any Land Title Office in BC to register changes to a certificate of title.

Property Transfer Tax is payable on the fair market value
1.0% on the first \$200,000 of the purchase price
2.0% of the amount in excess of \$200,000

\$2,000,000 building - \$38,000 property purchase tax
\$3,000,000 building - \$58,000 property purchase tax
\$4,000,000 building - \$78,000 property purchase tax

Environmental Assessment

Depending on the lender, an environmental assessment may be required. Some buildings may already have a completed environmental assessment. In many cases, the realtor negotiates that the seller pays for the environmental assessment.

Phase 1 assessment - \$3,000 – is usually sufficient if the building is clean and has been used for administrative purposes.
Phase 2 assessment - \$25,000 – may be required if there are concerns that previous occupants had hazardous chemicals or dangerous goods on site.

Building Appraisal/ Property Assessment

Building is evaluated to confirm a reasonable purchase price. The appraiser looks at the features of building, and comparable listings and rental values.

Building Appraisal - \$2,500

Building Inspection

Most lenders will insist that a commercial building be inspected by a structural engineer. The engineer will recommend specific obvious improvements. Additional quotes may be required.

Building Inspection - \$1,500

Other Considerations

Property Tax

Property Tax is based on a property's value on July 1 of each year.

The City of Victoria

Property tax is calculated on the assessed value

\$2,000,000 building - \$44,000 taxes

\$3,000,000 building - \$66,000 taxes

Council can approve a full or partial exemption. Agencies must apply every year for exemption . "Don't count on it- some non-profits do not get approved". See attached Policy

The District of Saanich

Property tax is calculated on the fair market value

\$2,000,000 building - \$42,000 taxes

\$3,000,000 building - \$63,000 taxes

Process for exemption - Submit a letter by October 31st for the following tax year. Saanich Council votes to deny or to approve a full or partial exemption. Then BC Assessment Authority applies the exemption. BC Assessment Authority can appeal the exemption.

Criteria – Building must be owned by a charitable, philanthropic or other non-profit organization.

"Staff can't make any promises. However, until now Saanich Council has liberally applied the exemption for the full amount to qualifying agencies"

The District of Oak Bay

In the past, Oak Bay has not approved permissive tax exemptions for non-profit organizations. Property tax is calculated at \$13,9139 for every \$1,000,000.

\$2,000,000 building - \$27,828 taxes

\$3,000,000 building - \$41,7417 taxes

Property Management Fees

Management fees – 5% of the rental value

Leasing services – 5% of the negotiated lease over the initial term (usually 5 years) with 2% on renewal (if applicable), plus MLS costs (if applicable).

Qualifying for a Mortgage

Conventional commercial mortgage

Regular commercial mortgage - 20 year amortization, 35 % down

Best Case Scenario - 25 year amortization, 25% down payment

Competitive Rates – possibility of discounted rates

The maximum conventional commercial mortgage the agencies qualify for is 75% of the purchase price.

Down payment - \$600,000

Financing - \$1,800,000

Total Purchase Price \$2,400,000

The agencies combined are in a strong cash flow position but financing is limited due to the 25% or \$600,000 down payment. There have not been any Victoria listings in the past 2 years, of commercial space for \$2,400,000 that meets agency needs.

Financial statements must demonstrate cash flow (current rent, profit and amortization) to cover the mortgage payments. For every \$1 in mortgage payments, the borrower must usually demonstrate a cash flow of \$1.25.

VanCity – non-conventional commercial mortgage

Competitive rates and 25 year amortization,

Community banking experts work closely with agencies to customize the mortgage package

Vancity will consider mortgage financing for non-profit agencies for up to 100% of the purchase price. Subject to a more thorough review, Van City Credit Union will finance the agencies 75% with an additional 25% from Vancity Capital Corporation.

Loan from Vancity Credit Union - \$2,250,000

Loan from VanCity Capital Corporation - \$750,000

Total Mortgage - \$3,000,000

In the attached scenarios, the first loan (or up to a maximum of \$2,250,000) is priced at 5.75% and the second loan is priced at Prime + 3.0% (6.50% today)

Robert Marus - "Van City will look at individual situation and lend up to what agencies can afford to pay"

Vancity will look for:

- Cash flow: current rent, amortization and profit
- Management and governance, who and how long
- History of organization, length of service; at least 5 years of financials
- What has happened in bad times? how have they handled crisis?

Recommends: "Think about needs rather than about fitting into a typical commercial lending formula"

Create a wish list about sharing services and creating efficiencies. What ideals are we looking for?, rather than simply "making it work". Demonstrate that the agency can increase or sustain services.

Phoenix has the most financial strength in the group; John Howard is also strong.

Commercial Space for Lease

Commercial expenses include: property taxes, building insurance, repairs and maintenance, common area maintenance, general utilities and property management fees. It can also include additional expenses specific to a building. Net leases are in favour of the landlord so that in a fully tenanted building, the landlord normally only pays for capital expenses and mortgage. The triple net (NNN) expenses of the building are divided amongst all the tenants, according to their square footage. Many commercial investors estimate that triple net expenses will be "30%" of the leasing fees.

Other considerations include tenant inducements and tenant improvements.

Board Members

Board members do not have the ability to pledge, assets, mortgages or encumbrances". Board Directors must make this type of decision at the AGM or through a Special Resolution Board Meeting.

Financials

Projections 1-3 based on actual listings

Projections 1-3 based on agency needs

Co-purchasing Space Requirements

Mortgage Table

Sources

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Background Material

Office Co-ownership Questionnaire
ENP Grant Proposal
Correspondence
Policy Research
Comparative Market Analysis – Current Listings and Past Sales