

Asset Acquisition:

Do we have a duty to look beyond
Our Own Immediate Interests?



Our case study in this issue is particularly rich in questions and issues for the would-be **Triple Bottom Line** practitioner. It is the story of the Australian Tax Office's decision to forsake its accommodation in capital cities and replace it with additional, purpose built, space.

This would be a good topic to discuss over morning tea (or an early evening beer) as it has many inter-related strands, and the answers are not immediately obvious, or necessarily uniformly interpreted.

A related topic is the issue of community costs associated with property booms and busts. The case study, the observation and the photographs are drawn from the research work of Dr David Ness, "Accounting for the Effects of Oversupply of Commercial Property" University of Adelaide, 2002 (unpublished), with his permission. Contact: davidness03@hotmail.com

In keeping with the theme of re-use and re-cycle rather than waste existing resources for the sake of something new, the Techniques Section this issue presents a useful chart from the work of Richard Rogers and Anne Power, *Cities for a Small Country* (Faber and Faber, London, 2000, Ch. 7, p. 228)

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Community Consequences of Individual Decisions: The Australian Tax Office



The ATO decided to relocate its capital city offices to new, purpose built locations

In December 1993 the ATO vacated its existing 25 000 sq m of office space {in Adelaide}, including King William Tower (12 860 sq m) and five other leased premises. Staff relocated to two new premises, each of 16 000 sq m, accommodating 700-800 staff. [Ed: Ten years later the original vacated building (see p. 657) is still empty! Of the two new buildings, one (Naylor House) is on the market]

The new capacity came at a time (1993) of gross oversupply in the market

The two new buildings cost \$43 M and \$57 M respectively and the ATO procured its new office space at a time when almost 14% of Adelaide's commercial space was vacant. The plans for the new premises were announced in September 1991 and followed an extensive three-year planning process. Hence, about five years elapsed from initial planning of the premises in 1988 when the property market was buoyant (vacancy rate 5%) to their commissioning in 1993, by which time the market had crashed. As Colliers Jardine stated at the time:

“A last gasp of new development is due for completion in 1993, with the two new developments for the ATO either completed or shortly to be completed. These two new buildings will provide just over 32,000 square metres of space..

There are also specific problems created by the decision of the ATO to develop major accommodation in an oversupplied market. My mid 1994, it is anticipated that the ATO will have vacated about 25 000 square metres of existing stock. Again, much of this is relatively modern.”

The Adelaide Experience was repeated around Australia

The Adelaide experience was repeated around Australia, involving about twenty-five projects in total. For example, ATO procured a new \$80 M building in Brisbane, despite 68 submissions by landlords requesting that existing space be occupied, claiming that a new building better suited its needs. In Perth, the ATO's former 15 000 square metres 12-level building in St George's Terrace was vacated in 1992 when the ATO moved to two purpose-built offices, and put on the market in 1994 for an estimated \$6 million. It was reported that the Federal Government had been seeking a tenant for the vacant property, whilst paying more than \$14 million a year in rent for the two new buildings; this represented a gross rental of more than double that for similar new buildings nearby. ...

Space Waste

A newspaper article headed 'taxing time for secondary space' summed up the problem. The ATO vacated two Sydney CBD office buildings on completion of its regional office building at Hurstville, 'dumping a further 22 000 square metres of space on the ailing secondary leasing market'. Analysts warned that the secondary market had been the big loser during 1992 and 1993 as tenants took advantage of attractive leasing deals to trade up into premium and A grade accommodation.

The Coalition's Space Waste Report highlighted 'the problem of buildings being left idle when departments moved to new accommodation, while the Government was still left to foot the bill on unexpired leases'.



King William Tower, still vacant after 10 years

How did the ATO justify its decision?

According to the Adviser to the Minister for the Arts and Administrative Services:

'...the ATO justified its modernisation program based on efficiency savings and on increased revenue collection as a result of various management reforms.'

What other issues were there?

King William Tower was occupied by over 600 staff of the approximately 1300 ATO workforce at the time but presented major difficulties in performance and technology upgrade. Employees were prepared to take industry action over accommodation issues. The upgrading of the building was dismissed at an early stage because of the costs involved, the mediocre result that could be achieved and the very expensive staging process that would have ensued. Just one aspect of ATO requirements was the need to retain high volumes of records on the premises, best in secure basement storage. The existing King William Tower had no basement area for storage and was also considered unsuitable for refurbishment because of:

- a) the restricted 2.5 metre ceiling height
- b) twenty year old plant and extra air conditioning needed to cope with computer loads;
- c) lack of car parking;
- d) difficulty in accommodating data cabling risers;
- e) limited floor plate size; approximately 500 square metres

It is worth noting that, until the early 1990s, the federal government had an unofficial role in establishing office accommodation standards and led the way in areas such as air conditioning performance, occupational health and safety, security, natural lighting and space allocation on a functional basis. Some of the special requirements for the Adelaide buildings, which together would house in excess of 1000 computers, were:

- a) the cable reticulation for data and communications required larger riser shafts;
- b) the sophisticated security system required its own riser shaft;
- c) the heat output from the equipment required special air conditioning
- d) power supply to and within the buildings was far in excess of that required for a non-computer environment;

- e) particular security needed to protect ATO confidential information;
- f) 80% of office area was to be within three metres of an external window.

What was the market reaction to the ATO decision?

The ATO proposals were vigorously opposed by the Adelaide City Council, the State Government, the Local Government Association, the National Trust, and the then Building Owners and Managers Association. The market argued that the required standards were too high and that the ATO should have adopted or modified some of the existing higher quality stock. Nevertheless, the ATO dismissed suggestions that its standards were too high, claiming they were 'similar to those found in Commonwealth or good quality commercial buildings'.

What was the real estate industry's responsibility?

The government's intentions were clearly evident to the real estate industry well before the event, yet speculators still proceeded with new premises – not designed to ATO standards – whilst the two ATO buildings were on the horizon. A former employee of the Australian Property Group questioned 'Why the Commonwealth and its staff should have been used to bail out speculators who could not see the glut for the greed!'

Did the ATO consider it should consider wider community interests?

Radio commentator Keith Conlon asked Wally Elliott, the ATO Accommodation Project Manager:

Is there a responsibility ... to consider more than the direct need; community interest, city interest, Planning Review interest? Is there a greater responsibility on a very big federal department to take into account more than your strict immediate needs?

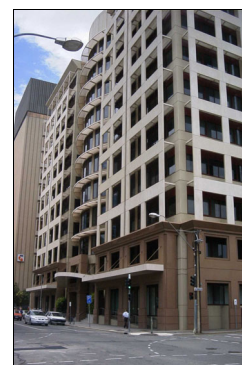
To which Elliott replied hesitantly:

I... I don't think so.... Our mission ... is... to come up with two purpose-built buildings to suit our needs.

What options did the ATO have?

What options did the Federal Government have? It could have chosen to spread the ATO workforce over several CBD premises, albeit within upgraded accommodation. It could have taken up two or three of the slightly lesser quality (than ATO standards) speculative premises vacant in the CBD, or it could have done as it did and commissioned (pre-committed) leasehold, specifically designed premises with longer-term stability. According to the Liberal Party's Waste Watch Committee, though, the ATO agreed to pay around 16% more than the average city rate for office space, meaning taxpayers would need to find nearly \$1m extra each year for the total bill.

A few years after commissioning (1996), the ATO needed to reduce its demand for city offices because of staff reductions. The two buildings were leased from the developers rather than owned, but with a lease commitment of 'at least a decade', which constitutes a substantial commitment of funds. By May 1996, the ATO had begun to reduce its city offices throughout the nation to meet federal government cost cutting targets. In Adelaide, the ATO accommodation plans to vacate its Naylor House accommodation in May 2003 and consolidate in its Waymouth Street office, by which time the wheel will have turned full circle from when it vacated its single King William Tower premises.



ATO Waymouth Street

Should this have been foreseen?

The Tax Commissioner, Michael Carmody, accepted responsibility for overspending on accommodation, but blamed it on having to plan ten years ahead.

"We had to make decisions many years ago about our future accommodation needs if we were to take the opportunity to get government funding for our decentralisation and re-accommodation program. At the same time we had to make predictions about staffing levels up to 10 years ahead. No-one faced with those lead times could get it exactly right." [Ed: c.f. the need for 'scenario planning' described in recent issues of SAM]

Can over-building be justified? The Benefits

One of those involved in the project at the time, later attempted to justify the decision :

So what were the benefits to SA? Money was invested in SA, employment and training was afforded to many, a substandard building was removed from the equation and over 1400 staff were afforded first class accommodation in return for improved work performance. The benefits to the construction industry were tangible with works for many... I simply put it that \$100 million of taxpayers' money was invested in improving the Adelaide stock of office accommodation.

Can over-building be justified? The Costs

However, the problem is that the substandard building was not 'removed from the equation'. It has remained substantially empty since it was vacated in late 1993, and this has entailed costs for the Australian Government and taxpayers, as well as the city. Inadequate allowance was made for the disposal costs in the ATO equation, although the ATO did consider the question of 'what happens to the buildings the ATO vacates when the new buildings are available?

As later events revealed, the prediction [produced by this consideration] that the empty space would be taken up in the short term, and the estimated sale price of \$15 million, were completely unrealistic.... The difficult task of finding tenants for the vacate King William Tower was seen by ATO and the Australian Property Group as the responsibility of Australian Estate Management, another arm of the government. These costs were therefore not factored into the ATO equation.

[The argument here] is not concerned with the costs to the building owner – players in the market should not be prevented from making a poor business decision themselves. Rather the thesis focuses on the cost to the community of such decisions. In the case of the ATO, some of the costs were:

- a) detrimental effects on visual image of city, especially at ground level (hoardings, grime, and graffiti);
- b) negative perceptions for investment due to the widely known vacancy;
- c) reduced rate revenue for the council to fund city services;
- d) economic effects on businesses in the vicinity, e.g. cafes;
- e) safety and security concerns due to the reduced building maintenance and possible squatters.

In addition to the above costs to the wider community arising from the displaced former ATO premises remaining vacant for many years, the decision to procure new premises led to other costs, including those related to environmental impacts. These include the energy required to construct new facilities and the associated greenhouse emissions, plus the waste associated with the eventual disposal of the existing building. ■



The Community Costs of Property Booms and Busts

A problem for others and none of our concern? Consider -

Costs that impact business flow on to the community

Overbuilding has resulted in massive costs to business and many of these costs ultimately flow on to the community that invests in insurance, property trusts or superannuation funds. Reporting on the dramatic consequences of the 'construction binge' in the US in 1991, *The Economist* reported:

"While the buildings were going up, they were a marvel. Completed, they were a nightmare. Empty... offices produce no income; interest goes unpaid; the banks themselves begin to suffer. Collateral that is unused and, in the short term, unsellable, is not collateral at all. Once property assets lose value, bankers have to rein in their lending to everybody, not just to those cursed property men. Tighter credit tips economies into recession and, in recession, nobody expands into new offices... So the pain gets a further twist. Economies are first boosted by construction, then bashed by it!"

Waste means missing out on opportunities

"The principal cost of overbuilding [in Australia] during the late 1980s boom was an opportunity cost. Billions of dollars borrowed overseas, on which the nation later paid a massive bill, were not invested in industry that would have allowed Australia to trade its way out of the recession. Nor was it invested in social and physical infrastructure, which could have added to the general welfare. Investment was channelled into office development, inflating Australia's overseas debt without contributing to the solution of the country's balance of payments crisis. According to Lennon, the glut 'squandered capital that could have gone into real jobs and real industry'"

Impacts are felt far beyond the real estate industry

The aggregate write-offs and 'provisionings' by Australian lenders during 1991-1994 were estimated at A\$28 billion, much of this due to non-performing real estate. Since banks need to maintain a bank capital adequacy ratio of 10 per cent, this level of write off would have resulted in major lending reductions and Kummerow estimates that office oversupply must have been a major cause of the severe early 1990s Australian recession

What can the Asset Manager do (see back page)

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1. The Economist 1991, Growth's Dead Weight, Editorial, 15 June, pp 13-14
 2. Low, N.P. & Moser, S.T. *The Causes and Consequences of Melbourne's Central City Property Boom*, Urban Policy and Research, 1991 Vol 9, no 1, pp 5-26, p.5
 3. Lennon, Michael, ABC Radio Transcript, 18 Sept 1991
 4. David Ness, "Accounting for the effects of oversupply of commercial property" unpublished PhD thesis, University of Adelaide, 2002, p.53
 5. Kummerow, Max *A System Dynamics Model of Cyclical Office Oversupply*, Journal of Real Estate Research, Vol 18, No. 1 1999, p233-254

Recycle! Revitalise!

RECYCLE OLD BUILDINGS	REVITALISE & REDESIGN OBSOLETE INFRASTRUCTURE	FREE-UP LAND USE
▼	▼	▼
Organise design competition for restoring, adapting, converting and re-using older inner neighbourhoods and streets	Preserve and extend coherent street pattern – create small manageable open areas as part of street pattern	De-zone and mix uses
▼	▼	▼
Create local 'master or action plans' with residents for renewal of decayed neighbourhoods and estates	Support innovative design, new ideas for 'remaking' places	Encourage urban pioneers with strong incentives for restoration – urban 'home steading' – urban self-build
▼	▼	▼
Encourage new ideas about street activity to enhance attraction of inner neighbourhoods (e.g. home zones, tree planting)	Create bus links, cycle lanes, pedestrian routes to link up decaying inner neighbourhoods	Support social entrepreneurs with 'community chest' of small grants for innovation
▼	▼	▼
Develop new uses for old buildings	Protect and restore local landmarks – parks, libraries, churches – re-use for new activities	Provide incentives for using small infill sites
▼	▼	▼
Maximise infill sites for innovative, blended new buildings	Plant trees, create small green spaces	Remove blight, clean up land, enforce the sequential approach
▼	▼	▼
Give incentive for re-use rather than demolition	Re-engage community activists, support voluntary activity, neighbourhood wardens	Enforce nuisance orders on empty property and land

Chart 1
The Lessons of City Centre Revival applied to Inner Neighbourhoods

Source: Richard Rogers and Anne Power, *Cities for a Small Country*
Faber and Faber, London, 2000, Ch. 7, p. 228

What can the Asset Manager Do? (cont. from page 660)

Be aware! And ensure your decision-makers are aware. All of the arguments on page 660 are the wider life-cycle consequences of over-building. Often approval is given for new developments because of the short-term boost to employment. But by focussing on the short-term construction gains, the likelihood of getting 'bashed' by the longer-term fall-out is increased.

Many public sector decisions are very large in scope relative to the communities that are affected – see the ATO case study in this issue.

Is the lesson, perhaps, that public sector decision makers (whether building or approving) need to take into account the wider social and environmental consequences of their decisions?

New Template

To access go to www.amqi.com

Resource Library Page—"Tools and Templates"

Project Initiation. It pays to get involved early

Directors get CEO sign off on projects before discussing it with the asset manager and/or colleagues in IS, who only then get to note whether the project is viable or can be done within the allocated budget?

The State Library in Western Australia overcame this problem by developing a simple project initiation template. This ensures that by the time the CEO gets to consider it, he knows that all relevant parties have already been involved in the planning process.

Rob Didcoe has submitted his basic template to the "Tools and Templates" collection at the Resource Library, www.amqi.com He writes: *"Obviously plans etc would be added. It is a pretty basic form really but does try to get project proponents to consider some important questions before going to far down the path."*

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