Dolle Building Property Evaluation

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LELAND CONSULTING GROUP

Introduction

Among the properties owned by Clark County is the Dolle Building, a multi-story office building located on a full block in downtown Vancouver.

In late 2014, the County engaged Leland Consulting Group (LCG) to evaluate the Dolle Building and make recommendations as to whether the building should be held long-term by the County; rehabilitated or repositioned; sold as-in; or used in some other way going forward. This memorandum summarizes LCG's analysis and recommendations.

Existing Conditions

Location. As shown in Figure 1 below, The Dolle Building is located at 500 West Eighth Street in downtown Vancouver, just northwest of Esther Short Park. The blocks surrounding the park developed rapidly beginning in 1999, and now include urban-scale condos, apartments, office space, retail and the Vancouver Hilton Hotel/Convention Center. Several downtown development projects have been announced in the last six months, including several mixed-use apartment projects and a new office building (Killian Pacific's 101 Building at Main and 6th Streets).

Figure 1. Dolle Building and Downtown Vancouver

The Vancouver Waterfront, about one-quarter mile south of the property, is planned for high density residential and commercial development. Road and utility infrastructure is under construction as of early 2015, and the project developers have announced that they expect to break ground on five buildings in late 2015. The real estate development environment in downtown Vancouver since 2000 has significantly more momentum than it did in the second half of the 20th century due largely to changing consumer preferences—both young and old Americans are now often looking for interesting, active, mixed-use environments such as downtown Vancouver and Portland.

Zoning. The property is zoned City Center (CX) by the City, which permits a wide range of land uses including residential, commercial, civic, and retail uses at relatively high densities. This flexible zoning is generally a positive for the site and its value.

Basic Attributes. The Dolle Building, shown below, occupies an entire downtown City Block (approximately 204' square, or 41,700 square feet in site size). The gross building area is 36,170, which includes useable tenant spaces (32,101 square feet) and common areas (4,069 square feet). The building has two above grade floors and a basement. Tenants lease space in all three floors. According to the County Facilities Department, the building was built in two phases. The eastern section of the building was built in 1973; the western section was built in 1979. The building's current tenants include attorneys, nonprofits, marketing, and various professional service firms. It was previously occupied by County departments, who were relocated to the Public Service Center following its completion in 2003.

According to County staff, the Dolle Building is one of two County properties that is leased to private and non-profit tenants, rather than being actively used by County departments. However, the other such building is the Center for Community Health, which is occupied by a "unique combination of multiple health and social services" and "provides continuity of care for patients." This Center, therefore, supports core County services and programs such as Public Health and Community Services, whereas the Dolle Building tenants to not support County services.

Figure 2. Dolle Building Exterior

Building Condition. No comprehensive Property Condition Assessment (PCA), which would document each of the building's systems and the cost to maintain or replace them, was available for this study. Therefore, LCG does not have a complete understand of the building's condition, which creates unknowns about future capital and operating costs, and therefore the building's value if it were to be sold.

Table 1 summarizes the information provided by the County about the replacement and upgrades completed for major building systems. Based on the typical life expectancy of building components, the roof and HVAC (heating, ventilation, and air conditioning) likely have some years of useful life remaining. (A PCA or similar would need to be completed in order to be certain, since the life expectancy of HVAC components, for example, can range from 15 to 35 years.)

The County has spent an average of $82,336 per year over the last five years on "routine maintenance" for the Dolle Building, a reasonable amount.

Some work has been completed on the elevators. The building's windows, electrical and plumbing systems, external walls/siding, and fire sprinklers are believed to be largely original, although some improvements may have been done to each of these systems. Many components of these systems are likely to be beyond their useful life, and will likely need to be replaced. Again, this cannot be determined without a complete PCA since the life expectancy of these building components can range from 20 to 50 years, with most less than 40 years. Peeling paint and exposed wood was observed on exterior walls of the building. The building may not meet all current ADA accessibility standards. The building's frame and stairs are assumed to have some years of useful life remaining, since these components generally have longer life expectancies.

Due to the fact that many building systems are likely older than their typical life expectancies, there are likely to be unbudgeted replacement, repair, and maintenance costs at the Dolle Building, though the magnitude cannot be determined based on the information available.

Despite these concerns, the building's interior is clean and the landscaping is well maintained.

Table 1. Dolle Building Systems Summary

Building System	Action Completed		System Age (Yrs.)
		Year	
Roof	Replacement	1997	18
HVAC	Upgrade	2002	13
Elevators	Improvements	Unknown	
Windows	None	1973	42
Electrical	None	1973	42
Plumbing	None	1973	42
External Walls / Siding	Not reported	1973	42
Fire sprinkler system	None	1973	42
ADA: Restrooms & Elevators	None	1973	42

Source: Clark County Facilities Management Department.

Operating Revenues and Costs.

Table 2 shows the operating revenues and expenses for the Dolle Building. (LCG was provided with 11 months of data and extrapolated to estimate complete 12-month revenues and expenses). The building is managed by the Phillips Group Real Estate Investment Brokerage, Management, & Leasing, who provided the revenue and operating expense documentation. Clark County Facilities manages and pays for the "maintenance" projects shown below.

Table 2. Dolle Building: Operating Revenues and Expenses

	2014 Total (Estimate)
Gross Revenue	$375,500
Operating Expenses	$113,800
Maintenance (County)	$82,336
Net Operating Income	$179,364

Source: Clark County, the Phillips Group Real Estate Investment Brokerage, Management, & Leasing.

This operating income is important to this study and the County, since it is recouped by the County, and reportedly used to pay for the County's other operating or capital costs. The Dolle Building income may be used to service bond debt associated with the County's Public Service Center, which was completed in 2003.

The building is seen as a "Class B/C" office property, meaning that it provides space for smaller, less well-capitalized tenants that cannot afford space in more expensive "Class A" buildings such as Vancouver Center office tower at 700 Washington Street, one block west of Esther Short Park. This perception is borne out by the rents being achieved by the building. The average annual rent at the subject property is $13.70 per square foot per year, 38 percent less than the average downtown Vancouver Class A office rent of $22.20 per square foot per year (all rents quoted in this analysis are per square foot, per year, full service, unless otherwise noted). A lease was recently signed for one of the more desirable spaces in the building, on the first floor, at $15.00 per square foot per year. Occupancy at the Dolle Building (79 percent occupied) is also lower than the CBD average of 88 percent.

Office Market Outlook

The future of the downtown Vancouver office market is important since an improving market could mean increasing future revenues for the County, while a deteriorating market would suggest the opposite. There are causes for both optimism and skepticism about the downtown Vancouver office market. On balance, LCG does not anticipate significant tightening of the market in the short or medium term (five years) that would significantly change revenues at the Dolle Building. Causes for optimism include:

- Recent business relocations to downtown. For example, DiscoverOrg, which provides sales leads to information technology firms, will be relocating 120 employees from east Vancouver into 27,000 square feet at 805 Broadway, a Class A office building in downtown Vancouver.

- A general trend towards urban locations in the Portland metropolitan region and across the country. Technology firms are showing a strong propensity for downtown locations in Portland, Seattle, the San Francisco Bay Area, and elsewhere, and this dynamic likely to positively impact downtown Vancouver. For example, of the 457,000 square feet of office space under construction in the Portland-Vancouver region as of March 2015, 100 percent of the space is in "urban" buildings in central Portland (either Downtown, Northwest, or Inner East-Side), none is in the hot office markets of the 1980s and '90s such as Kruse Way, Clark County, or Washington County.
- Announcements of new office construction and major rehab projects, including Killian Pacific's 45,000 square-foot 101 Building, and the Esther Short Building, a significant rehab located one block south of the subject property. The Esther Short Building is a two story office building that was formerly owned by the City of Vancouver. The building was sold to a private developer in 2014, and was subsequently remodeled and filled with a mix of private and nonprofit firms. The Esther Short Building has a more durable structure (steel and concrete) than the Dolle Building, which is wood framed. The more durable structure of the Esther Short Building enables significant rehabs to the interior spaces without modifications to the structure; steel and concrete buildings generally also allow for more flexibility in tenant spaces since there are far fewer columns and load bearing walls than in wood frame buildings.

By contrast, data analysis indicates the downtown Vancouver office market is not highly dynamic, and rents and occupancy, especially in Class B and C buildings, are likely to remain at current levels or possibly increase slowly. Figures 3 and 4 below show downtown Vancouver office rents and occupancy during the past decade, and show rents and occupancies in 2014 were virtually unchanged from 2005. Thus, there is no compelling evidence that market rents or occupancy are likely to improve significantly in the near future. As of the fourth quarter of 2014, the average rent in downtown Vancouver for all classes of office was $20.41 full service and occupancy was 89.5 percent. Approximately 244,790 square feet of office space is available in the downtown, indicating that, even if absorption exceeded that seen in the past decade, it would take many years before vacancies decrease significantly and downtown Vancouver becomes an environment in which landlords such as the County can expect higher rents.

Figure 3. Downtown Vancouver Office Rents, 2005 to 2014

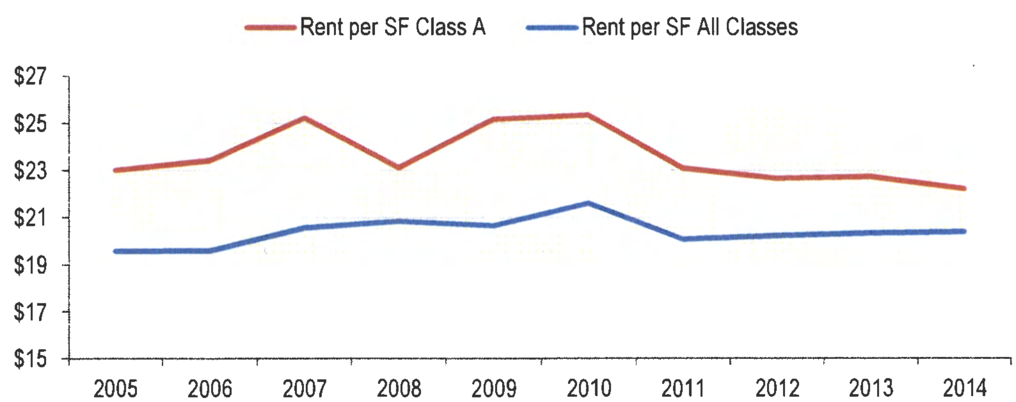
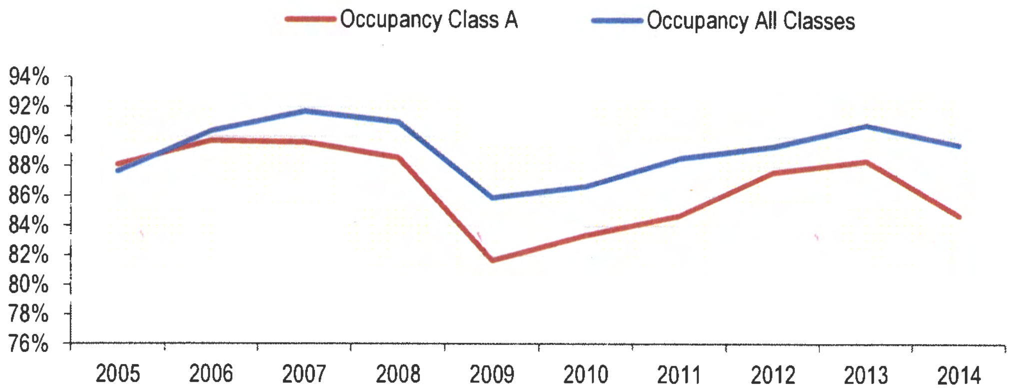


Figure 4. Downtown Vancouver Office Occupancy, 2005 to 2014



Source: CoStar, Leland Consulting Group.

A consideration with unknown impact on the market is Columbia Waterfront LLC's plan to build more than one million square feet of office on the Vancouver Waterfront (for context, there are currently about 900,000 square feet of Class A office space in downtown Vancouver). While this has the potential to attract significant attention and major new office tenants to Vancouver, it will also double the size of the Class A market and potentially dilute the market for Class A office space. The impact will depend on the construction schedule and economic conditions in place when buildings are completed and are leasing space. A rapid construction schedule or weak economy will negatively impact the office market.

Strategic Asset Management

Several principles of real estate asset management should be considered for the Dolle Building.

Asset Categories. First is the distinction between core, non-core, and transitional real estate, which LCG defines as follows:

- **Core:** A real estate investment that directly support's Clark County's mission. This would include the Public Service Center, Courthouse, jail, and other facilities that are used on a daily basis and are required in order to advance the County's core services such as law and justice, public health, public works, environmental services, or other functions. Since the Dolle Building is occupied by non-County tenants, it appears that the building does not directly advance the County's core services. Core assets are more likely to be County-owned and deserve a proactive approach to facilities planning and maintenance.
- **Non-Core:** Real estate that is ancillary but not integral to delivering on the core mission. An example from the healthcare industry is senior housing located near a major hospital. This real estate is not required to perform the organization's core business (healthcare), however, it may benefit the both clients and the organization itself. Therefore, it may be better for a partner organization (private or nonprofit senior housing company) rather than the hospital to own and manage this real estate. Non-core real estate is more likely to be leased than core real estate, since this can allow the organization more flexibility and lower capital cost.

  Non-core real estate assets are strong candidates to be declared surplus, and therefore be candidates for disposal (sale) or strategic transfer external third-party partners, since the core organization is rarely structured to provide consistent, long-term management of this assets. LCG sees the Dolle Building as a non-core asset.

- **Transitional:** A real estate asset that is core today but could be non-core soon due to consolidation, relocation, expansion in new facilities, obsolescence, or a changing business strategy. These assets require careful consideration since the organization needs to understand how they may be useful in the future, what actions would need to be taken to upgrade them to a useable condition, etc.

Building Condition Assessment and Maintenance. For core real estate assets, it is important for organizations to take a proactive rather than reactive approach to the assessment of building conditions and adequately budgeting for maintenance and repairs. If the Dolle Building were to be held by the County long-term, the County should undertake assessment and budgeting for the building.

As mentioned above, such a Property Condition Assessments (PCA) would be conducted in compliance with ASTM standards and include an evaluation of the building's roof/envelope, plumbing, electrical, HVAC, fire safety, accessibility, and potentially other components. Cost estimate for maintenance, restoration, or replacement could be included in the initial scope of work, or in follow up scopes. The cost of a PCA for the Dolle Building is estimated at $2,500 to $5,000.

Recommended Maintenance and Repair Budgets. Industry standards used to estimate the amount of money that should be set aside for major capital maintenance and replacement vary.

A report published by the Building Research Board and National Academy Press ("Committing to the Cost of Ownership: Maintenance and Repair of Public Buildings," 1990) recommends 2 to 4 percent of the current replacement value of the building (i.e., full purchase or reconstruction cost) be set aside annually for major capital maintenance and repair costs. Assuming that the building's replacement (purchase of a like building) value is between $2 and $3 million, the recommended annual maintenance and repair budget would be between $40,000 (at 2 percent) and $120,000 (at 4 percent). The County's current "routine maintenance" budget of approximately $82,000 per year is within this range; however, as is detailed above, it is not clear that all the building's systems are current, and therefore this general industry-standard recommendation may not be adequate.

Conclusion

Recommendation. Based on the above analysis, LCG recommends that the County declare the Dolle Building a surplus property and prepare to dispose of the property in a way that maximizes the County's financial and non-financial goals. Upon sale of the property, the proceeds of the sale should be transferred into the Clark County Investment Pool or other County investment fund that generates a low-risk revenue stream that can be used for other purposes. The County's Investment Policy includes a list of authorized and suitable investments, which include US Treasury obligations, municipal bonds, mutual funds, and a number of other instruments that meet the County's investment goals of "safety, liquidity, and return on investment." See http://www.clark.wa.gov/treasurer/documents/Investment_Policy-2013.pdf)

LCG makes this recommendation for several reasons:

- The Dolle Building is not a core asset since it is not directly supporting the County's core services.
- The building's condition and full cost of future maintenance and repair are not fully known, and therefore the revenue stream that the County enjoys could be significantly reduced or eliminated in coming years. One or more significant capital upgrades, such as new windows, electrical,

HVAC, or plumbing systems, external walls/siding, ADA improvements, or other, could significantly reduce or eliminate operating revenue for several years.

As summarized below, sales of other recent comparable properties in downtown Vancouver indicate that a reasonable range of sales values for the property are between $2.1 and $2.9 million. This should be further evaluated through an appraisal and will depend on the condition of building systems. If these funds are invested, a reasonable high-end yield would be 2 percent, or $42,000 to $58,000 per year. The return could be lower if the sale proceeds are invested in the general County Investment Pool.

Highest and Best Use. LCG's assessment is that the building's highest and best use by a private sector owner or developer is a combination of short-term use as an office building, with potential upgrades and rehab, and medium- to long-term demolition and redevelopment as a residential or mixed use project. Such a redevelopment would likely be comparable in size or scale to surrounding projects such as Esther Short Commons or Heritage Place Condominiums, though the exact program (i.e., number of apartments or condominiums, commercial area, etc.) would depend on market conditions at the time of construction. Based on these two potential future uses, potential buyers are likely to estimate their potential purchase price based on the building's value as either an "as-is" office building, or "raw land" available for redevelopment after demolition.

Potential Approaches to Disposition. The County has two primary approaches to the disposition of the building: a traditional sales approach, and a public-private partnership approach.

- **The traditional sales approach** is more straight forward and assumes that the County's primary goals are to dispose of the property relatively quickly, transfer the proceeds to a lower-risk investment fund, and return the property to the tax rolls, where it will continue to generate private benefits and public tax revenues.

  The steps involved may include: a declaration of surplus; conducting a property conditions assessment; appraisal in order to establish the property's market value; engaging a broker to market the building; and selling the building through a purchase and sale agreement. Note that the property should be appraised under two potential future uses—mixed-use with five stories of apartments over retail, and ongoing office use—since it is not clear which use will result in a higher value for the site. The County has stated that an auction process may be required for sale; however, LCG's experience is that public agencies can often sell property through this traditional method rather than auction. For example, the City of Vancouver's Esther Short Building was not sold via auction. However, the County should review its bylaws and the Revised Code of Washington (RCW) in order to confirm that an auction is not required.

- **The public-private partnership approach** should be used if the County has defined additional goals it wants to achieve at the property that go beyond effective stewardship of public funds—for example, if the County wants to achieve downtown revitalization, environmental, or other goals via the sale of the property. This process would likely take longer and might require the County and other partners such as the City of Vancouver to define its desired goals. The steps involved may include definition of goals and values; stakeholder engagement; property assessment and appraisal as above; followed by a thoughtful Request for Qualifications (RFQ) / Request for Proposals (RFP) which encourages developers to come forward with creative ideas for the site that achieve multiple public goals.

  There are many, many permutations of public-private partnerships, which depend on the public sector's goals. Many public-private partnerships actually require additional investment from the public sector. For example, in order to achieve the desired outcome of revitalization of the downtown and Columbia Waterfront, the City of Vancouver has partnered with Columbia Waterfront LLC and has invested capital and staff time to improve roadways, railroad under crossings, and park space. The perceived long term benefits are to the general community, as well as to tax rolls through long-term property and sales tax receipts on the waterfront site, and a catalytic "ripple effect" of greater surrounding investment.

Without a clear definition of the goals to be achieved through a public-private partnership, it is difficult to recommend a specific strategy.

Preliminary Review of Comparable Sales

LCG conducted a preliminary review of comparable land and office building sales for this analysis in order to provide the County with an understanding of the general range of values at which these properties have transacted in recent years. This analysis is not a substitute for an appraisal, which would be a more detailed analysis and take into account the condition of each building sale (current rents and vacancy, physical attributes, parking, market timing, etc.) in order to establish their comparability to the subject property, and a property valuation.

Table 3 shows three downtown Vancouver land sales and one current listing ranging from $41 per square foot (a current property listing) to $53 per square foot. The 400 W. Mill Plain site was purchased in June 2014, is now under construction, and will be the site of the West 15 Apartment building, a five-story, 120 unit affordable apartment project. The Esther Short Building parking lot land shown below was sold by the City of Vancouver to a private developer, who may build apartments on the property. If the 41,700 square foot subject property (site area) were worth $50 per square foot of land, the value would be $2.0 million.

Table 3. Downtown Vancouver Land Sales and Listings

Address	Status	Date	Amount	Site Area	Value PSF
Dolle Building (Subject Property)				41,700	
400 W Mill Plain Blvd (15th & Columbia)	Sold	6/30/2014	$2,700,000	50,885	$53
Esther Short Building (W Vancouver #5 Block 39)	Sold	2014	$1,800,000	36,155	$50
500 E. 15th Street	Listing	3/1/2015	$1,200,000	29,000	$41
West Vancouver Block 10	Sold	1/14/1994	$2,000,000	42,681	$47

Source: CoStar, Leland Consulting Group.

Table 4 shows three comparable office building sales in downtown Vancouver, and two other office building sales that are likely significantly more valuable than the subject property. The former City Hall building appears relatively comparable given that it occupies a full City block and contains a similar amount of rentable building area (RBA); however, it has more parking in a structured parking lot (3.5 spaces per 1,000 square feet of office space). If the 36,170 square foot subject property (building area) were worth $58 per square foot, the value would be $2.1 million; if the building were worth $80 per square foot, the value would be $2.9 million.

Table 4. Downtown Vancouver Office Sales

Address	Notes	Sale Date	Sale Amount	RBA (SF)	Site Area	Value PSF
Dolle Building (Subject Property)				36,170	41,700	
Most Comparable						
Former City Hall, 210 E 13th St	Built 1966, parking ratio 3.5	4/10/2013	$2,010,000	34,456	40,000	$58
Pacific Tower, 915 Broadway St	Built 1975	2/22/2013	$3,200,000	40,000	40,000	$80
400 E Evergreen Blvd	Historic NW Academy Bldg.	1/29/2015	$4,309,000	56,163	52,272	$77
Other Buildings						
Esther Short Bldg, 610 Esther St	Concrete/steel bldg., 1992 renovation	3/21/2014	$3,246,030	32,034	48,352	$101
1111 Main St	Not comparable, Class A Office	9/30/2014	$10,890,000	87,984	10,400	$124

Source: CoStar, Leland Consulting Group. RBA: Rentable Building Area.

(Note that total property value listed for the building in Clark County's online assessment / property information center is $4,799,700, or $132.70 per square foot of building space. This value is more than double to sales price per square foot of the former City Hall, and 66 percent higher than Pacific Tower. LCG recommends that the property be reassessed taking into account recent sales values of Class B/C office building sales in downtown Vancouver.)