



Report accepted and recommended by the City Manager:

  
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Date:

*Jan 16 2015*  
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## Purpose

The purpose of this report is to seek Council approval to enter into a new lease with an existing tenant at 738 Johnson Street, for the period December 1, 2014 to November 30, 2017. A location plan and photographs are attached in Schedules A and B respectively. The premises are a retail unit in the City's parkade on Johnson Street, and are occupied by Study Wise International Student Centre Victoria Ltd.

## Background

Financial information

square feet, the unit is the smallest of the five retail units on the ground floor of the Johnson Street parkade. In common with the other units, it suffers from a lack of storage space and old plumbing and electrical systems. Heating is provided by means of two hot air blowers which are barely adequate for the space.

The proprietor of Study Wise, Sang Woo Park, established his business in 2007 arranging language tuition and home stay for overseas students, mostly from Korea. He was previously the manager of a similar agency in Victoria. Study Wise is now contracted to UVic for the purpose of promoting the university's English language program. As the City's tenant since January 1, 2008, he has always paid his rent on time and has proved to be an entirely reliable tenant. The lease was last renewed December 1, 2011.

## Issues and Analysis

The rent for the three years to November 30, 2014 was \$17,520.00 **Financial information** per annum; however, this amount included property taxes. The proposed rent, as agreed with Study Wise, is \$14,224.00 **Financial information**, plus property taxes of \$3,297.74 (2014). The proposed rent is net of property taxes in order to align this unit with the adjacent premises. The market report from DTZ Victoria, the City's letting agents for the retail units at the Victoria Conference Centre, attached in Schedule D confirms that the proposed rent is fair market value as the "market rates are likely in the low to mid-teens on average". The following factors are particularly relevant:

1. The age and condition of the premises as outlined above. Also, the subject units do not have a strong street presence to attract passers-by, being somewhat hidden under the second floor of the parkade, as shown in Schedule B.
2. The location in the 700 block of Johnson Street. It is directly across the street from a large empty commercial building (727 Johnson), and is also close to the Cool Aid Community Health Centre which supports patients who are homeless, vulnerable due to mental illness or disabilities, living on very low incomes or who have addiction challenges.
3. The current vacancy rate in the downtown core. Some commercial landlords are believed to be offering incentives to existing tenants and/or renewing leases at the same or lower rents in order to retain them and avoid having empty premises.

The City's other three leases on Johnson Street also expired November 30, 2014 (one of the units is empty as it was last used as the elections office). The proposed total revenue (rents and property taxes) from the four subject units will increase from \$89,036.80 to \$96,962.25 per annum, an increase of almost \$8,000, as shown in Schedule E. The rental income from all leased properties in the City's operating budget for 2015 is projected to be \$710,000.00.

In addition to paying rent and property taxes, the tenant is also responsible for all utilities. There are no common area charges or operating costs.

## **Options and Impacts**

Council has two options in this matter:

1. Grant a new lease to the existing tenant at a fair market rent, or
2. Seek a new tenant at a fair market rent.

In order to find a new tenant for the premises, the City will need to market the property through a commercial realtor who would typically charge 5% of the rent received over the term. At \$14,224.00 per annum over three years, this would amount to a fee of \$2,133.60.

Given the number of vacant commercial properties in the downtown core currently, including many small office suites, 738 Johnson would likely remain empty for a significant period of time. For instance, one of the retail units in the Victoria Conference Centre has been empty since May 2014 despite being marketed through DTZ Victoria. There is, of course, no opportunity to recover the rent and property taxes lost as a result of the premises being vacant.

A new tenant would almost certainly require some landlord improvements to be carried out and/or a rent free period, typically three months (\$3,556.00). Even then, the rent achieved is unlikely to be much, if any, higher than has been agreed with the existing tenant. Finally, although references are obtained, there is always an element of risk involved with any new tenant, particularly if it is a start-up business.

The recommended course of action is to grant a new lease to the existing tenant on similar terms other than the rent adjustment outlined above. By doing so, the City will continue an existing relationship with a well-established business and a reliable tenant it knows well.

## **Recommendation**

That Council authorizes the Mayor and Corporate Administrator to execute a new lease in a form satisfactory to the City Solicitor, for premises at 738 Johnson Street with Study Wise International Student Centre Victoria Ltd. for a period of three years commencing December 1, 2014 at a rent of \$14,224.00 per annum, subject to the publication of the statutory notices required by the Community Charter.

Schedule A  
Location Plan



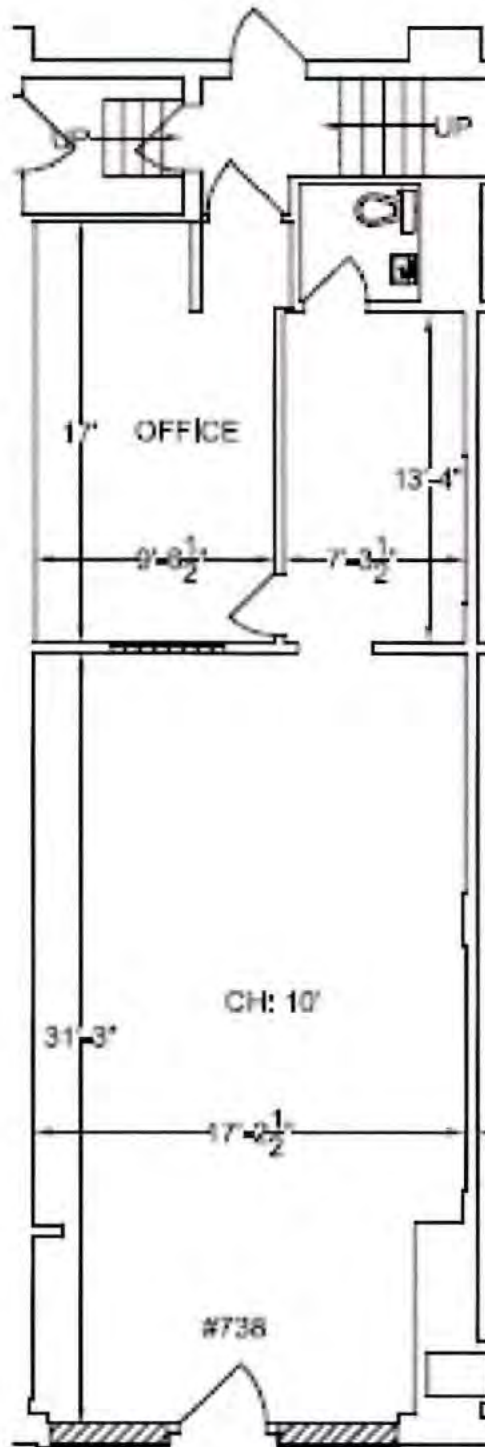
**Schedule B  
Streetscape**



Store Front



Schedule C  
Floor Plan







## Market Conditions

### Retail Market

Similar to the national economic climate, the Greater Victoria retail market continues to demonstrate resilience to external economic pressures and offers exciting new developments and renovations that are changing the retail landscape and attracting new businesses to the region. In the past few years Greater Victoria had an estimated 700,000 square feet of new space added to the market, which is largely a result of the completion of Phase One and Two of the 'Uptown' development in addition to several smaller mixed-use developments such as the Atrium, the Hudson, and the Oriental Hotel. The significant amount of new supply added to the retail market has affected both suburban and downtown markets.

Greater Victoria continues to attract national and international tenants, however local retailers have been more cautious in their growth and expansion activities. The downtown streetfront vacancy rate increased in 2012 to approximately 8.5% from 7.5% in 2011 and 6.0% in 2010. Vacancy rates in 2013 decreased slightly to 6.5% however the absorption was largely due to smaller local retailers obtaining space at drastically reduced rates. In 2014 that trend continued with stable vacancy but further reduction in rates.

Lease rates vary considerably within the retail market due to location and exposure, existing improvements, parking, signage, access, etc. There is also economies of scale related to the size of the premises and differences based on use (ie. restaurant vs. fashion vs. pharmacy). In recent years it has been challenging to attract a retailer to any given space, as there has been limited demand in downtown Victoria. The most active tenants in the retail market in recent years include: fitness, pharmacy, food markets, restaurants, and dollar stores. Fashion retailers have focused primarily on suburban shopping centres throughout Greater Victoria, for which many have undergone significant renovation programs in competing for those key tenancies.

Tenant inducement such as fixturing and free rent periods as well as a tenant improvement allowance are generally required in most transactions. Tenant improvement allowances range from \$20 to \$40 PSF on average, plus the landlord's base building work, all of which serve to reduce the effective PSF rate downward considerably. Comparable rates in the neighbourhood for streetfront retail space range significantly, but for properties in the 700 block of Johnson (which is considered a less desirable area for retail in the City) are on average from \$10.00psf to \$16.00psf net, in confidence following are examples of lease transactions / offering(s) in the immediate area:

716 Johnson Street  
1483 Douglas Street  
1319 Broad Street  
1327 Broad Street  
639 Johnson Street

Third party business information

Note: Retail rates vary considerably depending on the specific block, building and improvements in place. There are lots of examples of rates that are above \$20.00psf, however there are also plenty of retail lease transactions downtown that are in the \$10.00 to \$15.00psf net range. The 700 Block of Johnson is a challenged area for retail and as such, it's our opinion that market rates are likely in the low to mid-teen's on average.

**Schedule E  
Johnson Street Retail Units**

<u>Unit</u>	<u>Tenant</u>	<u>Sq Ft</u>	<u>Current \$/Sq Ft</u>	<u>Current Rent/Taxes</u>	<u>Proposed \$/Sq Ft</u>	<u>Proposed Rent/Taxes</u>
			<b>Financial information</b>		<b>Financial information</b>	
#726 2014 Taxes	Sockeye			\$ 28,524.00 \$ 7,426.40		\$ 30,495.00 \$ 7,541.40
#738 2014 Taxes	Study Wise			\$ 17,520.00		\$ 14,224.00 \$ 3,297.74
#742 2014 Taxes	Election Office					
#744 2014 Taxes	Scruples			\$ 14,910.00 \$ 3,713.20		\$ 15,872.00 \$ 3,679.82
#748 2014 Taxes	Kim's			\$ 13,230.00 \$ 3,713.20		\$ 17,520.00 \$ 4,332.69
				<b>\$ 89,036.80</b>		<b>\$ 96,962.65</b>
				<u>INCREASE</u>		<u>\$ 7,925.85</u>