

HALIFAX

P.O. Box 1749
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Item No. 9.1.6
Audit and Finance Committee
June 17, 2015

TO: Chair and Members of Audit and Finance Committee
Original Signed

SUBMITTED BY: Richard Butts, Chief Administrative Officer
Original Signed

Jané Fraser, Director Operations Support

DATE: June 1, 2015

SUBJECT: Lease Amendment, Her Majesty the Queen, Public Works and Government Services Canada, 40 Alderney Drive, Dartmouth

ORIGIN

This report originates with a request from Public Works and Government Services Canada (PWGSC) to extend the term of their lease agreement with the Halifax Regional Municipality and renovate their premises at PWGSC's expense with project management provided by HRM.

LEGISLATIVE AUTHORITY

This report, and the recommendations contained herein, are in compliance with Halifax Regional Municipal Charter Section 61, Power of the Municipality regarding property, subsection (5)(c); The Municipality may lease property owned by the Municipality at market value. Leases with a term, inclusive of renewals greater than five (5) years and annual gross rent in excess of \$200,000 require Regional Council's approval.

Halifax Regional Municipality Council approved, Dec 11, 2012, that all budget increases are to be presented to the Audit and Finance Standing Committee, prior to submission to Council.

Halifax Charter, section 93(1) - The Council shall make estimates of the sums that are required by the Municipality for the fiscal year; Halifax Charter, section 79(1) - Specifies areas that the Council may expend money required by the Municipality; Halifax Charter, section 35(2)(d)(i) - The CAO can only authorize budgeted expenditures or within the amount determined by Council by policy; Halifax Charter, section 120(6) - The Municipality may maintain other reserve funds for such purposes as the Council may determine; Halifax Regional Municipality policy on Changes to Cost Sharing for Capital Projects - Changes requiring Council approval; and the Halifax Regional Municipality Reserve Policy - No reserve funds will be expended without the CAO's recommendation and Council approval.

RECOMMENDATION ON PAGE TWO

RECOMMENDATION

It is recommended the Audit and Finance Committee recommend that Halifax Regional Council:

1. authorize the Mayor and Municipal Clerk to execute a lease amendment to extend the term of the lease agreement between the Halifax Regional Municipality (Landlord) and Public Works and Government Services Canada (Tenant) for the premises at 40 Alderney Drive, as per the terms and conditions outlined in Table 2 of this report;
2. authorize the Mayor and Municipal Clerk to enter into Sub Agreements for Lessee's Improvements as per the existing Lease Agreement between the Halifax Regional Municipality and Public Works and Government Services Canada for the premises at 40 Alderney Drive; and
3. approve an increase of \$1,838,270 to Capital Budget Account CB000066 – Alderney Gate VAC and CRA Renovations, with no net increase to the Capital Budget as per the Financial Implications Section of this report, to reflect the cost reimbursement from Her Majesty the Queen, Public Works and Government Services Canada for leasehold improvements to the leased premises; and
4. approve the contribution of the 10% project management fee revenue of approximately \$180,000 to Q135 – Alderney Gate Recapitalization/Leasehold Improvement Reserve to fund future recapitalization projects.

BACKGROUND

HRM entered into a ten (10) year market lease agreement with Public Works and Government Services Canada (PWGSC) for Veterans Affairs Canada (VAC) for 28,941.90 sq.ft / 2,688.79 sq.m of office and storage space on the 3rd and 4th floors at 40 Alderney Drive which commenced on August 1, 2011. In April 2012, the Federal Government announced the planned closure of nine VAC offices by early 2014, as well as the expected downsizing of other office locations. As a result of the changes to the VAC service model, PWGSC determined that a portion of their leased space at 40 Alderney Drive was surplus to VAC's requirements. In November 2013 PWGSC contacted Corporate Real Estate (CRE) staff to request an early partial termination of their lease.

The request was not supported by CRE staff as HRM would be left with a significant amount of vacant space and the loss of approximately \$440,000.00 of gross rent per year. Furthermore, HRM would potentially incur costs associated with marketing, backfilling and leasehold improvement costs for the vacant space. Alderney Gate was purchased by HRM in 2005. The purchase financing is, in part, underwritten by the rent stream from external tenants and the former lease payments by HRM for its premises. Sound accommodation policy allows for a mix of owned and leased property both as a lessee or landlord. The rent paid by PWGSC provides operating cash flow and is a partial offset to HRM's occupancy costs at Alderney Gate.

In December 2014, PWGSC contacted CRE staff regarding an options analysis which was conducted on behalf of another Federal department, Canada Revenue Agency (CRA). One of the options under consideration was to renovate the vacant portion of the existing VAC leased premises and relocate CRA to the vacant VAC space at Alderney Gate. In January 2015, PWGSC decided to pursue this option and entered into negotiations with CRE staff.

DISCUSSION

PWGSC has proposed to relocate approximately 100 CRA employees from Purdy's Wharf, Tower II in Halifax, where they currently occupy 1680 square meters (18,083 square feet) of office space. The renovation and relocation of CRA staff to Alderney Gate is expected to be completed by September 30, 2016 which is the expiry date of the PWGSC lease at Purdy's Wharf.

Under the terms of the existing lease with HRM, HRM is required to enter into Sub-Agreements with PWGSC for the performance of the required renovations, with PWGSC responsible for the full reimbursement of management, design and construction costs to HRM plus a 10% project management fee. Where HRM is acting as an agent for PWGSC all costs of this project are a flow through to PWGSC, there will be some variations from HRM standard procurement policy, however the procurement process will comply with applicable procurement legislation and best practices.

The terms and conditions of the current lease agreement are outlined in Table 1 below.

Table 1

CURRENT LEASE - TERMS AND CONDITIONS	
Property	40 Alderney Drive, Dartmouth, NS
Landlord	Halifax Regional Municipality
Tenant	Her Majesty the Queen, Public Works and Government Services Canada (PWGSC)
Occupied by	Veterans Affairs Canada & Canada Revenue Agency
Location/size	1) 3 rd Floor - 994.59 sq. m / 10,705.68 sf office and 30 sq. m/322.92 sf storage space, 2) 4 th Floor - 1544.20 sq. m / 16,621.63 sf of office space, and 3) P1 - 120 sq. m /1291.67 sf of storage space in the parkade.
Gross Rent	\$275.00/m ² office space & \$110.00/m ² storage space, for a total of \$714,667.25 per annum + HST. Gross rent includes operating costs and property taxes, which may be adjusted annually based on CPI per the terms of the lease.
Current Term	Ten years – August 1, 2011 – July 31, 2021
Special Conditions	Right of Early Termination on or after July 31, 2019

As part of the accommodation proposal to collocate VAC and CRA in the Federal lease space at Alderney Gate, staff and PWGSC have negotiated a lease amendment which provides a five year lease renewal for PWGSC, extending the total lease term until 2026 at the gross base rental rate of \$275.00/m², plus any annual adjustments for operating costs and property taxes. All tenant lease improvements will be at PWGSC's expense.

The \$275/m² is well supported as a competitive market value. The low bid for CRA's tender in 2014 yielded turnkey bids in Halifax at \$252m² with a high of \$300m² with \$252/m² being the approved bid for new Class A office space in suburban Halifax.

Table 2

LEASE AMENDMENT – TERMS AND CONDITIONS	
Renewal Term	Five years – August 1, 2021 – July 31, 2026
Gross Rent	\$275.00/m2 office space & \$110.00/m2 storage space, for a total of \$714,667.25 per annum + HST. Gross rent includes operating costs and property taxes, which may be adjusted annually based on CPI per the terms of the lease.
Special Conditions	1) Right of Early Termination on or after July 31, 2019, is deleted from the lease agreement. 2) Renewal in 2021 must be for at least 465 sq. m / 5000 sf of office space.

FINANCIAL IMPLICATIONS

The execution of the lease amendment will ensure that the annual rent from this lease to the lease revenue account for Alderney Gate Facility Management cost centre (W203.5151) will continue at a rate not less than \$714,667.25 until at least 2021. It further ensures rent of at least \$127,875.00 per annum from August 1, 2021 to July 31, 2026 in the event PWGSC only exercise their minimum right of renewal at 465 sq. m.

The leasehold improvement project, estimated at \$1,838,270 and charged to capital project account CB000066 – Alderney Gate VAC and CRA Renovations, is planned to begin work by July 2015 and to extend for 15 months to September 2016. The total actual project cost will be fully reimbursed by PWGSC within 60 days following acceptance of the “Final Certificate of Completion”, per the terms of the lease agreement.

Budget Summary: Project Account No. CB000066 – Alderney Gate VAC and CRA Renovations

Opening Balance	\$ 0
Add: Budget increase (funded by PWGSC reimbursement)	<u>\$ 1,838,270</u>
Total account balance	\$ 1,838,270
Less: Leasehold Design & Construction	<u>\$(1,838,270)</u>
Balance	\$ 0

Per the terms of the leasehold improvement project agreement, PWGSC will pay HRM a 10% project management fee. Staff wish to contribute this revenue of approximately \$180,000 to the Alderney Gate Recapitalization/Leasehold Improvement Reserve Q135, in addition to regularly budgeted annual reserve contributions, to support future building recapitalization projects.

COMMUNITY ENGAGEMENT

N/A

ENVIRONMENTAL IMPLICATIONS

There are no environmental implications associated with this report.

ALTERNATIVES

Council can choose not to approve the lease amendment, which would leave the terms of the current lease agreement, including the right of early termination, in place. This is not recommended as it is expected that without the approved lease amendment, the tenant will exercise the right of early termination potentially creating additional expenses in the form of holding and lease-up costs associated with the vacant space. Staff has negotiated a lease amendment, at market terms and conditions, securing a low risk revenue stream from PWGSC.

ATTACHMENTS

Floor Plans – Alderney Gate – 3rd and 4th Floor

A copy of this report can be obtained online at <http://www.halifax.ca/council/agendasc/cagenda.php> then choose the appropriate meeting date, or by contacting the Office of the Municipal Clerk at 902.490.4210, or Fax 902.490.4208.

Report Prepared by: Marcia Connolly, Coordinator, Leasing & Accommodations, Corporate Real Estate,
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Report Approved by: _____
Peter Stickings, Manager, Corporate Real Estate, Operations Support, 902.490.7129

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Financial Approval by: _____
Bruce Fisher, A/Director of Finance & ICT/CFO, 902.490.4493

NO.	DESCRIPTION	AREA (SQ. FT.)
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THIRD FLOOR TOTAL NET AREA = 28963
THIRD FLOOR TOTAL GROSS AREA = 4384

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Notes:
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