

**BEFORE THE ENVIRONMENT COURT
I MUA I TE KOOTI TAIAO O AOTEAROA**

ENV-2018-CHC-198

IN THE MATTER of the Resource Management Act 1991

AND of an application under section 85 and
clause 21 of the First Schedule of the
Act

BETWEEN **REDMOND RETAIL LIMITED**

Applicant

AND **ASHBURTON DISTRICT COUNCIL**

Respondent

**SUPPLEMENTARY STATEMENT OF EVIDENCE OF CLARK McLEOD
ON BEHALF OF REDMOND RETAIL LIMITED**

Dated 12 April 2019

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INTRODUCTION

- 1 My full name is **James “Clark” McLeod**, and I am a director and shareholder of Clark McLeod & Associates Ltd and Hastings McLeod Ltd, trading as Property Brokers, and I reside in Ashburton.

QUALIFICATIONS AND EXPERIENCE

- 2 I am a property valuer, consultant and licenced salesperson at Clark McLeod & Associates Ltd and Hastings McLeod Ltd, trading as Property Brokers
- 3 My qualifications and experience can be summarised as follows:
 - 3.1 I hold a current Valuer’s Practice Certificate. In 2007 I became a Registered Valuer.
 - 3.2 I am an associate of the Institute of Valuer’s (ANZIV)
 - 3.3 I am a senior member of the Property Institute of New Zealand (SPINZ)
 - 3.4 I am an associate of the Real Estate Institute (AREINZ)
 - 3.5 I hold a Bachelor of Commerce Major in Valuation and Property Management (Lincoln University) Post Graduate in Business (Massey University)
 - 3.6 I am actively involved in Commercial sales and leasing within the Ashburton market.
 - 3.7 I am actively valuing in the Ashburton Commercial property market.
 - 3.8 I have 18 years’ experience and have practiced as a valuer and commercial sales within Ashburton since 2001. This includes my current role as Property Valuer, consultant and licenced salesperson.

EXPERT WITNESS CODE OF CONDUCT

- 4 I have read, and agree to comply with, the Code of Conduct for Expert Witnesses contained in the Environment Court's Consolidated Practice Note 2014 in giving my evidence. All my evidence is within my expertise and I have considered and stated (where applicable) all material facts known to me which might alter or qualify the opinions I express.
- 5 I have no financial interest in the outcome of this hearing.

AMBIT OF MY EVIDENCE

- 6 I have been asked by the company's legal counsel to consider the matters under section 85 of the Resource Management Act. Section 85 has been explained to me to assess whether the building is incapable of reasonable use and whether the heritage listing of the building in the District Plan places an unfair and unreasonable burden on the company as the owner.
- 7 I was the author of a statement that was attached to the Section 85 application lodged in the Environment Court, and this supplementary statement is to be read in conjunction with that first statement, and specifically addresses issues to be decided by the Court.

WHAT CONSTITUTES REASONABLE USE OF THE SITE?

- 8 In my view a reasonable use of the site is for a business activity that complies with the land zoning regulations and permitted building use which provides a reasonable financial return to the owner.
- 9 For one to understand a reasonable use of the property the history of the site's use is important. This building appears to be purpose built for grain and flour merchants circa 1880. Records indicate the building has always been used as a grain store and was purchased by Peter Cates in 1973. Cates Grain and Seed Limited operated from this site for 42 years. The building and site was no longer fit for purpose of grain and seed storage and a move to a modern warehouse building was required. The 1960's extension was the area primarily used within the building and only when at capacity the original building was used. The majority of the time the original building

remained unused as this was not suited to the operation of forklifts. The upstairs warehouse was not accessible by forklift and staff were not permitted in this space for health and safety reasons. In the early days bags of grain were manually hoisted up to this level by rope and this business practice is no longer viable. The site no longer provides reasonable access due to the limited ability to reverse a truck onto State Highway One which is required to manoeuvre a vehicle to load or unload goods at the site. The building had not been functional for some time for the use as a grain store. The high cost to upgrade the building was another contributing factor for Cates Grain and Seed Limited to relocate.

- 10 A reasonable financial return derived from current market conditions could be a gauge of what a may constitute a reasonable use.
- 11 General market returns for different property types within the Ashburton market are;

Ashburton Indicative Market Yields

<i>Property</i>	<i>Lower Market Cap Rate</i>	<i>Upper Market Cap Rate</i>
Quality commercial	6.5%	7.5%
Quality retail	6.5%	7.5%
Average/poor retail	7.5%	9.0%
Average/poor commercial	7.5%	9.5%
Quality industrial	7.0%	8.0%
Average/poor industrial	8.0%	10.0%

- 12 Due to the age of the subject building and building design, I would classify this building as an Average/Poor Industrial property due to the nature of improvements. This market yield range of 8.0% to 10.0% is an expected net market return prior to consideration of earthquake strengthening remedial costs.
- 13 The building is classified “earthquake prone” and Ashburton District Council has issued notice that the building has a limited life in its current condition and cannot be occupied after 23rd May 2023. The foreseeable remedial cost should be considered when determining if the heritage

listing places an unfair and unreasonable burden on the owner. The cost to strengthen and refurbish the building has been provided as evidence by Stewart Harrison and incorporated in the total outlay required;

Purchase Price (Sept 2014)	\$800,000
Strengthening & Refurb Costs	\$2,630,000
Total Cost	\$3,430,000

I do note that the original purchase price of \$800,000 did include the neighbouring leasehold site. This leasehold site provides no significant improvement value as this site comprises no buildings and land is predominately asphalt.

- 14 The market rental of this subject building for the current or similar use would be in the vicinity of \$71,500 p.a. plus GST and outgoings. Which analyses below;

<u>Rental Area Analysis</u>	<u>Area</u>	<u>\$/m2</u>	<u>Market Rent</u>
Offices	130.0	70.0	9,100
Office extension	74.8	45.0	3,366
Warehouse	1,056.7	45.0	47,552
Shop-separate	82.8	65.0	5,382
Workshop-separate	83.7	45.0	3,767
Storeroom-separate	57.7	40.0	2,308
Upstairs storage	534.0	-	-
	2,019.7	35.4	71,474
Current Market Rental Say:		\$	71,500

- 15 The original purchase indicates a market return of 8.94%

$$\frac{\text{Market Rental}}{\text{Original Purchase Price}} = \text{Yield}$$

$$\frac{\$71,500}{\$800,000} = 8.94\%$$

- 16 It would be expected the market rental would experience a lift post strengthening and refurbishment. We consider the existing market rental

will likely have a lift of around 20% this equating to a market rental of \$85,800 p.a. When considering the return on investment after strengthening and refurbishing this equates to a 2.50% yield. This return is substantially below a market return of 8.0% to 10.0%.

$$\frac{\text{Market Rental}}{\text{Total Cost}} = \text{Yield}$$

$$\frac{\$85,800}{\$3,430,000} = 2.50\%$$

- 17 The market would see value of this property in the yield range of 8.0% to 10.0%. Therefore minimal expenditure would be recouped in bringing the building up to current code. Adopting a yield/capitalisation at the midpoint of the market range at 9.0% for an average/poor industrial property the indicative market value of the property after strengthening would be a marginal increase in value on the purchase price to \$953,000. Therefore the economics for strengthening this building provide a significant loss;

Original Purchase Price	\$800,000
plus Strengthening & Refurb Costs	<u>\$2,630,000</u>
Total	<u><u>\$3,430,000</u></u>
Less Value Post Strengthening @ 9.0%	\$953,000
Profit/Loss	-\$2,477,000
Return on Investment	-310%

- 18 To refurbish and strengthen the existing building with the estimated foreseeable expenditure, this places an unfair and unreasonable burden on the owner with an estimated loss of -\$2,477,000. Even if there is some market variation on these figures the loss is so significant the result would be an unreasonable burden to the owner.
- 19 When considering a hypothetical redevelopment of this site to office, retail, hospitality or another alternative use the economics would be similar. There would be further cost involved to change the use and modify and convert the existing structure.

UNDER THE DISTRICT PLAN WHAT USES CAN BE MADE OF THE BUILDING?

- 20 The District Plan permits Residential, visitor Accommodation, Community, Recreational, Retail (limited to 500m² & excluding service stations) & Commercial Activities. The activities permitted in the District Plan would likely require a change of use consent departing from the previous industrial activity. A change of use would require many aspects of the building to be upgraded to Building Code including, accessible facilities, fire and earthquake strengthening. Resource consent would be required for a retail space greater than 500 square meters. These permitted uses are not the intended primary use for this industrial building. There would be significant cost required for a change of use to meet the requirements of the Building Code this being over and above the costs identified from Stewart Harrison.
- 21 With the additional cost involved for a change of use the economics for redeveloping this property would be further reduced.

IS THE SITE CAPABLE OF FURTHER DEVELOPMENT WITH THE BUILDING IN SITU

- 22 The building design is not well suited to being developed. There would be significant physical challenges with structural pole supports throughout the building foot print. Pole supports would detract from a retail use and limit the nature of business for which the site could be developed. Furthermore other uses may require natural light which would prove difficult to achieve with a change of use as this industrial building is long and has been developed up to all boundaries.
- 23 There is significant financial loss of developing the site with the building in situ. This is evident in points 16, 27 and 28.

WHETHER DEMOLITION OF THE BUILDING EXTENSIONS (1950s ONWARDS) ENHANCES REASONABLE USE OF THE BUILDING?

- 24 In my view the demolition of the 1960's extensions further reduces the reasonable use and economics of the building. The 1960's building is more usable than the original grain store and this was evident with Cates Grain and Seed Limited using this extension as the primary warehouse and

leaving the original warehouse unused for the majority of the time. The removal of the extension further reduces the economic feasibility of a redevelopment. The redevelopment of the entire building is not economic to do so and by removing the more modern part of the building with the better clear span structure compounds the issue with a proportionally higher development cost. If the building is reduced in size the usable building area is reduced. Rental is usually based on a building floor area and therefore the potential rental return is also reduced.

- 25 A further limitation is the restricted access to the rear of the site. If the extension was demolished access would be required through the original building. There is no easement or access right on the adjoining vacant leasehold site.
- 26 My previous report provides hypothetical alternative uses and the estimated costs associated with development. Any redevelopment of the existing structure was not financial feasible.
- 27 I have considered the financial implications of this proposal with the development cost of this proposal based on Stewart Harrison's estimated strengthening and refurbishment cost of \$1,990,919.

<u>Development cost with Removal of 1950's Extension</u>	
Purchase Price (Sept 2014)	\$800,000
Strengthening & Refurb Costs	<u>\$1,990,919</u>
Total Cost	<u><u>\$2,790,919</u></u>

- 28 I have assessed a market rental with the removal of the 1950's extensions. This reduces the available rental that can be achieved from the building. I have added an additional rental for the surplus land that would be created from removing the extensions.

Rental Assessment with removal of 1950's Extensions

<u>Rental Area Analysis</u>	<u>Area</u>	<u>\$/m2</u>	<u>Market Rent</u>
Offices	90.0	\$70.0	\$6,300
Office extension	74.8	\$45.0	\$3,366
Warehouse	244.7	\$45.0	\$11,012
Shop-separate	82.8	\$65.0	\$5,382
Workshop-separate	83.7	\$45.0	\$3,767
Storeroom-separate	57.7	\$40.0	\$2,308
Upstairs storage	534.0	\$0.0	\$0
	<hr/>		
	1,167.7	\$27.5	\$32,134
Plus 20% Post Strengthening & Refurb			\$6,427
Plus Surplus Land (750m2 @ \$600/m2 @ 5.0%)		\$30.0	\$22,500
Market Rental			<hr/> <hr/>
			\$61,061

- 29 The costs associated with strengthening and refurbishing the original building is proportionally higher. The reduction of the building floor area also results in a reduction in the overall rental from the premise which reduces the return.

Return after removal of 1950' Extension

$$\frac{\text{Market Rental}}{\text{Development Cost}} = \text{Yield}$$

$$\frac{\$61,061}{\$2,790,919} = 2.19\%$$

- 30 This proposal also results in a significant loss of capital as the value of the property does not recoup strengthening and refurbishment costs. Furthermore there is a write off of value as the most usable and functional part of the building (1950's extensions) are demolished. This proposal results in a capitalised market rental of \$61,061 equating to a value of \$678,000 less than the original purchase price of \$800,000. I note this value would be less than an unencumbered land value. This would be the reality as the land value is encumbered with the heritage listing and reduction of the land use rights. The loss of capital would likely be;

Development Cost	\$2,790,919
Less Value Post Strengthening & Refurb @ 9.0%	\$678,000
Profit/Loss	-\$2,112,919
Return on Investment	-264%

31 I thought it would be prudent to provide a hypothetical financial model for the construction of a new warehouse onto the back of the original heritage building. For simplicity I have considered a warehouse to be consistent with the current use. I consider alternative uses of retail, offices and hospitality would provide a similar financial loss. The development cost for these alternative uses greatly increases from that of a warehouse. There would be a corresponding increase in rental for the alternative uses however I expect this to be relative to the development cost so therefore would not vary greatly.

Hypothetical warehouse extension development

750 m2 @ \$1,200 /m2 =	\$900,000
Plus Purchase Price (Sept 2014)	\$800,000
Plus Strengthening & Refurb Cost	<u>\$1,990,919</u>
Total Development Cost	<u>\$3,690,919</u>

32 I have applied a rental to the entire site reflecting a higher rental for the new warehouse development.

Hypothetical warehouse extension market rental

<u>Rental Area Analysis</u>	<u>Area</u>	<u>\$/m2</u>	<u>Market Rent</u>
Offices	90.0	\$70.0	\$6,300
Office extension	74.8	\$45.0	\$3,366
Warehouse	244.7	\$45.0	\$11,012
Shop-separate	82.8	\$65.0	\$5,382
Workshop-separate	83.7	\$45.0	\$3,767
Storeroom-separate	57.7	\$40.0	\$2,308
Upstairs storage	534.0	\$0.0	\$0
	<u>1,167.7</u>	<u>\$27.5</u>	<u>\$32,134</u>
Plus 20% Post Strengthening & Refurb			\$6,427
New Warehouse Extention	750	\$65.0	\$48,750
Market Rental			<u>\$87,311</u>

- 33 The rental return does not increase significantly enough to justify further investment to redevelop the property incorporating the original heritage building.

Return after modern warehouse extension to original building

<u>Market Rental</u>	=	Yield
Development Cost		
<u>\$87,311</u>	=	2.37%
\$3,690,919		
Total Development Cost		\$3,690,919
Less Value Post Strengthening @ 9.0%		\$970,000
Profit/Loss		-\$2,720,919
Return on Investment		-340%

HAS THE OWNER REASONABLY EXPLORED ALTERNATIVE OPTIONS FOR THE REASONABLE USE OF THE BUILDING AND SITE?

- 34 This property has been for sale and lease since 18th July 2017. During this time the property has been listed with Property Brokers- Hastings McLeod Ltd. The initial marketing campaign invested over \$3,000 advertising the property for sale or lease. This marketing campaign involved all the usual advertising avenues including print media and listed over multiple websites. A large signboard 2.4 meters by 1.2 meters advertising the property still remains on site. There has been moderate to low enquiry from all the advertising. Enquiry to purchase this property has not proceeded beyond initial discussions. When a buyer has been informed of the listed heritage status and the likely limitations of developing a heritage building, the buyer has seen this as a significant impediment. This impediment is further compounded with the required earthquake strengthening plus upgrades requirements for change of use. These factors have resulted in no further correspondence or inspection of the site.
- 35 There has been marginally more enquiry for lease of the property. The enquiry to lease again has only been preliminary investigations attracted

from the State Highway One frontage. Inspections of the property did occur from potential Lessees. The enquiry has been from marginal business activities. These activities included separate enquiry from; Pop up play ground with inflatable children's play equipment, skate park and go cart racing.

- 36 There is currently no demand for a hospitality premise in Ashburton. Hospitality businesses have generally struggled within the district. A redevelopment of this property in to hospitality would not be a financially viable option. An example of a conversion to hospitality was undertaken by the Ashburton Licencing Trust known as "The Trust". This redevelopment was a smaller scale and lower stud industrial shed/workshop in Somerset Lane which was converted into a night club and bar. The conversation was costly and the business struggled to make a reasonable return. The business was well supported and proved popular in the town however the small population base struggled to generate sufficient sales revenue. This premise has been closed down and is fully fitted out for hospitality and has been available for lease for a number of years.
- 37 There is difficultly trying to convert a building that was developed for the specific use and in this case the specific use of a flour and grain store. When a building has become obsolete for the intended purpose it was built, it is generally difficult to remove the obsolescence of the building for an alternative use. An extreme example of this is if a service station was to have a change of use the majority of the building structures would be obsolete as the improvements would not be very well suited to other business activities.
- 38 The Ashburton commercial property market tends to be a conservative market with rental levels lower than many other towns in the wider Canterbury region.
- 39 Current demand for older industrial buildings of this nature is low. The industrial market has experienced demand for quality modern precast buildings with integrated data and technology facilities. This demand has

been evident within the growth in the Ashburton Business Estate. The foreseeable demand for the subject building is low and I believe this will remain low. Modern day businesses are not well suited to the building layout and design. It was for this reason the previous tenant Cates Grain and Seed limited moved to a more modern premise after being at this site for over 42 years.

- 40 Current demand for other Business A zoned premises is moderate. There are a number of vacancies within the town and suburban premises. There is moderate activity within this Business A space with a number of new lettings within the town. The majority of activity has been within the industrial/service sector as businesses have expanded and developed at the Ashburton Business Estate. The same demand has not been experienced with the subject property site.

ARE THERE ANY OTHER REASONABLE USES OF THE SITE THAT COULD BE PURSUED?

- 41 In my opinion there is no foreseeable economic use of the building.
- 42 The only uses I could envisage for this building would be low value activities that would not provide an economic return. I see the main use of this building as a secondary storage facility of commercial goods, vehicles or similar. This solution would only be short term until earthquake upgrading is required prior to 23rd May 2023. After this time the building will not be available for public use and it is unclear at this stage if the building will be able to be used at all even for storage.
- 43 After 23rd May 2023 there will likely be significant implications on obtaining insurance on the building and any items in the building. No further commercial use of the building would be likely without insurance.

WHAT IS THE DEVELOPMENT POTENTIAL OF THE SITE IF THE BUILDING WAS DEMOLISHED OR REMOVED?

- 44 The development potential of the site is significant due to the State highway One frontage and large land holding within close proximity to the town centre. This property could be developed for a variety of business

uses. Maximising the use of the site would likely see the site developed for a business specifically requiring high exposure from State Highway One.

CONCLUSION

45 In my opinion the building is obsolete in both location and design. The building provides little commercial use from the demands of the modern business environment. Any redevelopment of the site using the existing building structure is not financial feasible and therefore the building is an impediment to the land. Any redevelopment using the original listed heritage building would place a significant financial burden on the owner as the refurbishment and strengthen costs of \$2,630,381 would not be able to be recuperated from the market in either rental or capital gain.

Clark McLeod

12 April 2019