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Executive Summary

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Glossary of Terms
The Adelaide CBD is changing. As new commercial office space comes into the market, the requirements and expectations of tenants are changing. This presents both a challenge and an opportunity to the owners of lower grade CBD property. The challenge is for owners to maintain the competitiveness of the building, to avoid falling rental values and rising vacancy rates. This publication encourages owners to invest in improving, refurbishing, and repositioning their property as a way to secure future income streams.

This guide discusses a number of considerations in devising viable plans for the future of a commercial property including dealing with heritage features, incorporating ‘green building’ features and the option of a change of use.

There have been concerns in the property industry that the increase in supply of office space is outstripping the growth in demand. This may well marginalise older and lower grade properties which do not offer the quality available in new buildings. Many tenants are coming to expect an improved standard of accommodation, better services and energy efficient features. Successful commercial property will meet these demands and be rewarded for it. The case studies within the guide demonstrate how sensible investment can change the tenant profile, enhance capital value and offer returns in reasonable time frames.

If any of the following statements apply to you, we would like to talk about the options available to you:

- I own commercial property which could be described as lower grade (C or D).
- I have experienced rising vacancies recently.
- My rental values are not rising as much as I would like.
- My property has not been significantly improved for many years.
- I would like to secure higher rentals and longer leases in my building.
- I am unsure of what returns to expect from any investment I make.
- I am worried that new legislation might affect my building in the future.

Adelaide City Council seeks a vibrant and prosperous city and the built environment plays a key role in this. This publication is designed to generate discussion and ideas for the future of your property. In a changing market where supply is increasing quickly, good tenants are priceless.
The Adelaide CBD is experiencing its largest construction cycle of the last 15 years. In 2006, 31,000m² of new office space entered the market, while in 2007-08, a further 90,000m² of space is due to complete. Most prominent among these projects are City Central Tower One on Waymouth Street, 151 Pirie Street and Flinders Link. Further projects are committed, most notably SA Water's new headquarters in Victoria Square.

As with most spikes in supply, there has been a domino effect with developers and land owners reconsidering options for their landholdings. This may well lead to a continuation of the supply cycle beyond 2008, placing greater pressure on vacancies.

Demand and vacancy

Overall, demand for office space has continued to grow, with net absorption in June 2006 amounting to 25,000m². Major corporations have been particularly active in committing to new developments or upgrading to higher quality existing space. Demand for better quality space has become the impetus for the development of the new prime office supply. Over 60% of total space under construction is pre-committed with tenants vacating existing prime (premium and A grade) and secondary (B, C and D grade) space. Virtually all of the pre-commitments are from existing CBD tenants.

Table 1

<table>
<thead>
<tr>
<th>Project Name</th>
<th>Address</th>
<th>Building Grade</th>
<th>Comp Year</th>
<th>NLA (m²)</th>
<th>Comments</th>
</tr>
</thead>
<tbody>
<tr>
<td>Advertiser Building</td>
<td>31-45 Waymouth St</td>
<td>A</td>
<td>2005</td>
<td>12,500</td>
<td>Adelaide Advertiser HQ</td>
</tr>
<tr>
<td>Commonwealth Law Courts</td>
<td>1 Angas St</td>
<td>A</td>
<td>2005</td>
<td>6,200</td>
<td>Federal &amp; Family Courts</td>
</tr>
<tr>
<td>Finders Court</td>
<td>153 Finders St</td>
<td>A/B</td>
<td>2005</td>
<td>4,290</td>
<td>Four Storey Building Refurb.</td>
</tr>
<tr>
<td>City Central Tower 1</td>
<td>17-29 Waymouth St</td>
<td>A</td>
<td>2006</td>
<td>31,329</td>
<td>18 Level Premium Office Tower</td>
</tr>
<tr>
<td>Finders Link - AIG</td>
<td>76 Finders St</td>
<td>A</td>
<td>2006</td>
<td>12,000</td>
<td>New Headquarters</td>
</tr>
<tr>
<td>KPMG Building</td>
<td>151-159 Pirie St</td>
<td>A</td>
<td>2006</td>
<td>11,547</td>
<td>Major tenant KPMG</td>
</tr>
<tr>
<td>Aust. Central Credit Union</td>
<td>52-60 Light Sq</td>
<td>A</td>
<td>2006</td>
<td>7,200</td>
<td>Major tenant ACCU</td>
</tr>
<tr>
<td>Opalfield House</td>
<td>29 King William St</td>
<td>B</td>
<td>2007</td>
<td>1,740</td>
<td>Strata Offices Refurbishment</td>
</tr>
<tr>
<td>12-18 Gilles St</td>
<td>B</td>
<td>2006</td>
<td>1,470</td>
<td>7 Level Strata Office Building</td>
<td></td>
</tr>
<tr>
<td>Finders Link-Santos</td>
<td>60 Finders St</td>
<td>A</td>
<td>2007</td>
<td>15,500</td>
<td>New Headquarters</td>
</tr>
<tr>
<td>Channel 30</td>
<td>78 Hutt St</td>
<td>B</td>
<td>2007</td>
<td>1,890</td>
<td>New Headquarters</td>
</tr>
<tr>
<td>Former RAA Building</td>
<td>135 Victoria Square</td>
<td>A</td>
<td>2007/08</td>
<td>4,000</td>
<td>Refurbishment</td>
</tr>
<tr>
<td>125-130 West Tce</td>
<td>B</td>
<td>2007/08</td>
<td>2,116</td>
<td>Mixed Use Development</td>
<td></td>
</tr>
<tr>
<td>RAA Site</td>
<td>131-139 Grenfell St</td>
<td>A/B</td>
<td>2008</td>
<td>4,291</td>
<td>First RAA Building – Mixed Use</td>
</tr>
<tr>
<td>City Central Tower 2</td>
<td>121-129 King William St</td>
<td>A</td>
<td>2008</td>
<td>12,376</td>
<td>Pre-commitment to Ernst &amp; Young</td>
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<tr>
<td>521 South Tce</td>
<td>B</td>
<td>2008</td>
<td>2,270</td>
<td>Morted Office Building</td>
<td></td>
</tr>
<tr>
<td>379 King William St</td>
<td>B</td>
<td>2008</td>
<td>2,235</td>
<td>Morted Strata Office Building</td>
<td></td>
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<tr>
<td>Fmr. Paspaco Building Site</td>
<td>372-400 King William St</td>
<td>A</td>
<td>2008/09</td>
<td>21,000</td>
<td>Morted 10 Level Office Building</td>
</tr>
<tr>
<td>City Central Tower 3</td>
<td>Franklin / Bentham St</td>
<td>P</td>
<td>2009/10</td>
<td>16,000</td>
<td>Morted Office Tower</td>
</tr>
<tr>
<td>42-56 Franklin St</td>
<td>A</td>
<td>2009/10</td>
<td>16,000</td>
<td>Morted Office Tower</td>
<td></td>
</tr>
<tr>
<td>73-79 Pirie St</td>
<td>A</td>
<td>2009/10</td>
<td>30,350</td>
<td>Morted Office Tower</td>
<td></td>
</tr>
</tbody>
</table>

Source: Jones Lang LaSalle

Net Lettable Area (NLA) refers to floor area for office use

Figure 1 – Historical and anticipated new supply and vacancy rates

Figure 2
With a sizable amount of prime space due to enter the market, building owners should consider strategies to keep their buildings competitive.

The state government has been active in driving the increased interest in energy efficient workplaces, having pre committed to City Central Tower One and targeting other buildings that can show improved energy efficiency. This is despite the considerable premium attached to such space.

The vacancy rate across the CBD in December 2006 was 7.3%. The prime grade vacancy rate was 4.4% while secondary grade buildings were 8.5%.

Recent pre commitments to quality accommodation and the disparity in prime and secondary grade vacancy reflect the overall flight to quality that has continued in the Adelaide market.

This will place pressure on lower grade accommodation over the next two to three years with vacancy rates rising in consequence.

In particular, it is the C and D grade buildings that are struggling to maintain relevance, with vacancy levels in these building grades at 9.7% and 13.8% respectively.

### Case Study: 29 King William Street

#### Background

This 6 storey secondary grade building was built in the early 1900s. PASCOT Property Developments purchased the property in June 2005 with a view to refurbishing and strata titling the building.

The building is listed on the City of Adelaide Local Heritage Register, being an early example of concrete construction in Adelaide. The original concrete structure has been retained and a modern façade will be added, bringing more natural light into the building. Two additional floors will be built, adding value to the property by increasing the floor space ratio.

#### Motivation

PASCOT Property Developments have previously successfully refurbished and strata titled Passcot House at 28 Grenfell Street in 2000, resulting in the occupancy of the building increasing from a low 19% to 100% occupation. This development had indicated to the developers that there was latent demand for quality, well located, strata titled office accommodation in the Adelaide CBD.

#### Result

The refurbishment will provide basement, ground and seven upper levels of office accommodation. The refurbishment has attracted significant interest from smaller owner-occupiers and private investors who value the opportunity to invest in well located CBD property. This picture is an impression of the completed project.

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Rents

Recent demand for good quality space has been reflected in strong growth in prime gross effective rents during the past 12 months of 13.5% to now average $256 per square metre. Secondary gross effective rents have seen modest growth in the past 12 months to now average $143 per square metre.

Incentives on a 10 year market lease were stable at between 15-20% for prime grade stock, but were significantly less for renewals or shorter lease terms (10-15%). Increased supply over the next two years may place upward pressure on incentives.

Secondary stock incentives on a new 10 year lease are running between 25-30%

CASE STUDY:

31 Franklin Street

Background

31 Franklin Street is a six storey office building that was vacant for many years after falling into disrepair. Each of the upper floors comprises approximately 220 square metres and total NLA is 1,258 square metres.

The building was purchased with vacant possession by Global Intertrade in April 2003 for $1.425m. At the time of purchase, the building was considered unsuitable for occupation due primarily to non-compliance with access and egress requirements of the fire safety regulations.

Motivation

The purchasers saw an opportunity to refurbish and secure tenants, being mindful not to overcapitalise. The building was pitched at the price sensitive end of the market. The refurbishment included upgrading the fire services, providing a new façade, minor improvements to the lobby and services, and basic maintenance, cleaning and upgrading to individual floors. Total refurbishment costs were kept within a tight budget, amounting to under $0.5m.

Result

Marketing of the building commenced in late 2005, by the end of 2006 the building was 83% leased. Once fully leased, the building should provide the owner with a return on investment in the order of 8% and a capital value circa $3m.
Office markets in Australia are relatively mature in comparison with those in other parts of the Asia Pacific region. Such mature markets tend to be characterised by relatively little new construction entering the market and a larger stock of older buildings.

Ageing of Office Stock
New construction activity across Australia’s major CBD office markets has averaged less than 3% per annum of total existing stock over the past decade. In Adelaide, the level of new construction has been a very low 0.45% of total stock per annum. Even the high levels of activity between 2006 and 2008 will average only 3% of the current existing stock.

As a result, the average age of office stock across Australian CBDs is rising, ranging from 25 years in Brisbane to 31 years in Adelaide (Table 2). Almost 50% of Adelaide’s total office floor area was built in a 13 year period between 1981 and 1993. Two thirds of office buildings were built more than 25 years ago. A number of older office buildings have been withdrawn from the market and now lie idle. These building present opportunities for either refurbishing as offices or adaptive re-use for a variety of other uses including residential apartments or student housing.

Major refurbishment activity in Adelaide has been relatively high over the past ten years when compared to the level of new construction. In most cases, full refurbishment of buildings has occurred following the pre-commitment or departure of the major tenant rather than undertaken on a purely speculative basis.

Vacancies
Given tenants’ preference for modern, better quality space, vacancies tend to be lower in prime grade stock than in older, secondary stock. Figure 8 illustrates the disparity between prime and secondary vacancy rates. While the new prime quality space coming in Adelaide will initially see both the prime and secondary grade vacancy rates increase, it is expected that over time, the flight to quality will see prime vacancy rates improve at the expense of the secondary market.

A clear rental differential exists between prime and secondary space, providing owners with solid financial reasons to reposition their asset.
**CASE STUDY:** 242-244 Pirie Street

**Background**
This property was purchased by the current owners in 1994 with a view to converting the upper level to residential use. The property was in a poor state of repair but was well located, being within easy reach of the commercial heart of the CBD and the cafes of the East End. Undercover parking for two cars is provided via Moger Lane.

The refurbishment included a complete gutting of the building, removal of exterior paint and restoring original stone work, adding a large balcony over Pirie Street and the creation of an internal courtyard.

**Motivation**
The owners decided to make a lifestyle choice to relocate from the eastern suburbs to the inner city. This property had the potential to not only provide them with an inner city residential address but income from the ground floor commercial tenancies and studio apartment that shares the first floor level with the main residence.

It is also ideally located for the owner to operate her consultancy business - whose clients include a wide range of city based businesses and government departments.

**Result**
While the motivation for renovating and converting this building was primarily lifestyle, the end result has been an income generating property that also provides the convenience of CBD apartment living without the ongoing costs of management and strata fees.

**Refurbishment Strategy**
The decision to refurbish is based upon adding value to an asset. It hinges around the need for re-positioning a building in the context of the market and attracting and retaining tenants to maintain or increase income streams. Projects must demonstrate a sound return on investment (ROI) and care must be taken not to over capitalise.

In the 1980s and 1990s Australia’s CBD office markets witnessed several significant refurbishments where owners gutted buildings to reposition them for the next leasing cycle. However in today’s market, the focus is on more strategic and minor refurbishments such as adding a retail element to the ground floor, improving the lobby and upgrading services.

The drivers of these more staggered refurbishments are lower capital expenditure and the difficulty in obtaining vacant possession or access to all of the building in a suitable timeframe to warrant a major refurbishment.

Refurbishment can have a positive impact on a building’s rental and occupancy levels as well as capital value in the following ways:-

- Capital value can be increased via successful refurbishment;
- The sale process often provides the impetus for refurbishing, with prospective owners identifying opportunities to add value and change the tenancy mix;
- Refurbishment can re-position a building in the marketplace (e.g. from B to A grade), allowing owners to increase value via higher rentals;
- Refurbishments can protect a building from obsolescence and potential loss from tenants vacating to superior space;
- In markets where tenants are willing to pay a premium for better quality space, refurbished property can attract new tenants more quickly, thus reducing letting voids.

**When is the right time to refurbish?**
Experience suggests that office buildings will require a major refurbishment every 20 – 25 years to remain competitive. Timing of the refurbishment is critical to success.

While the project timing for each property will depend on a combination of market and building specific factors, four major indicators of the most appropriate time to undertake a refurbishment can be identified:

- When a significant gap emerges between the rents being achieved in a particular property and those in new space entering the market;
- When a building loses tenants and finds it difficult to attract new tenants, resulting in prolonged periods of vacancy in excess of competing properties;
- When a building loses a major tenant;
- When a major tenant’s lease renewal is approaching, offering added incentive to stay.
REFURBISHMENT DECISIONS

Adelaide City Council can provide information on heritage related issues
Increasingly tenants are seeking buildings demonstrating environmentally sustainable principles
Some smaller tenants are very price sensitive – understanding the market is key

Heritage Buildings
The City of Adelaide has some 417 buildings on the Register of State Heritage Items, mostly residential and public buildings. There are 20 State listed buildings that currently provide significant office space in the Adelaide CBD office market. Most of these are either C or D grade buildings or have been substantially redeveloped, retaining just the façade of the heritage item (for example the Myer Centre facades to North Terrace).

The Adelaide (City) Development Plan requires that development of State or Local Heritage Places “should not diminish its heritage value or structural integrity and should conserve the substantial whole of the place". This adds complexity to the refurbishment of heritage listed buildings and any works should be carefully planned. Professional advice should be sought on elements of the development which may have heritage implications.

Since 1988 the Adelaide City Council has provided the most substantial local government heritage incentives scheme in Australia, reimbursing private owners of heritage places with part funding for conservation work that meets specific requirements. Last financial year Council committed more than $1 million to support built heritage.

Work that may be eligible for a heritage grant includes:
• Documentation
• Conservation works
• Special projects where customised assistance will be provided to owners of listed places that face large, complex or significant conservation challenges
• Emergency works where stabilisation works or hazard remediation works are urgently required.

Over time, Council has contributed to some significant flagship heritage projects such as the Beehive Corner and West’s Coffee Palace, among numerous other residential and commercial projects.

The Heritage Incentive Scheme covers buildings listed on the Register of State Heritage Items or either of the two local listings (City Significance and Townscape). State listed properties may be eligible for a grant from the State’s Heritage Branch of the Department for Environment and Heritage.

Further information can be obtained from Adelaide City Council through the website www.adelaidecitycouncil.com/heritage or by telephone on (08) 8203 7445.

Environmental Sustainable Design (ESD)
Increasingly, major corporate and government tenants are seeking buildings that demonstrate environmentally sustainable principles.

The South Australian Strategic Plan has a target to reduce energy consumption in government occupied buildings by 25% within 10 years. Preference will be given to office accommodation with a high Australian Building Greenhouse Rating (ABGR) rating1 for all new leases and leases renewed after June 2006. Several major companies have adopted similar selection criteria, indicating a growing awareness by the corporate sector of ESD principles.

City Central Tower One is the first building in Adelaide and the largest in Australia designed to achieve the 5 star ABGR rating. Most other new buildings are seeking to achieve a 4.5 star rating. The challenge is for building owners to at least improve on their existing energy ratings.

Implementing environmentally sustainable initiatives in existing buildings can result in significant increases in capital value. Simple and cost effective solutions exist to increase building performance that will pay for themselves within realistic time frames.

While tenants currently may not be willing to pay a premium rental for buildings with sustainability features, some will soon come to expect a discounted rent to occupy buildings that do not have these features. By 2007 vendors of commercial buildings will be required to demonstrate their energy consumption to potential purchasers as part of the due diligence process. Energy efficiency measures for commercial and public buildings were introduced into the Building Code of Australia from 1 May 2006. The changes reflect the commitment of federal and state government to reducing greenhouse gas emissions.

The new measures require all commercial and public buildings to achieve minimum levels of energy efficiency through performance based and deemed-to-satisfy provisions for building elements:
• The thermal performance of walls, ceilings, floors and glazing including shading in order to avoid or reduce heating and cooling;
• The sealing of buildings to reduce energy loss through leakage;
• Natural ventilation and internal air movement, where appropriate, to avoid or reduce the use of artificial conditioning;
• Engineering services including:
  - Lighting systems
  - Air conditioning, heating and ventilation systems
  - Hot water supply systems

Building owners should ideally seek to achieve an ABGR of 3-3.5 stars as a minimum to remain competitive in today’s marketplace.

In addition to the ABGR Rating for energy efficiency within office buildings, the Green Building Council of Australia has developed a broader measure of environmentally sustainable building techniques known as Green Star.

Its assessment also incorporates the ABGR rating. Green Star assessments are awarded up to a maximum of six stars, this representing “World Leadership” status in incorporating ESD techniques.

When undertaking refurbishment works, building owners should consider some of the following strategies to comply with ESD principles:
• Review the facade performance and incorporate shading devices or low ‘e’ glazing panels where practical;

1The Australian Building Greenhouse Rating (ABGR) scheme rates office buildings according to their greenhouse gas emissions by awarding a star rating on a scale of one to five.
Case Study:
33 King William Street

Background
This 18 storey secondary grade building was completed in 1970 and has a net lettable area of 10,250sqm. A major refurbishment was completed in 2000 at a cost of approximately $3.5m. This project was supported by Adelaide City Council’s former Smart Buildings Programme, which provided $97,500 towards refurbishment of the building, including funding towards installing a fibre optic spine with primary and secondary nodes allowing high speed connections to each floor.

Motivation
The owner sought to reposition this prominent King William Street building in order to attract both private and public sector tenants. Given its location on the corner of Hindley Street, there was an opportunity to reconfigure the former banking chamber for food outlets.

Result
The building was successfully repositioned as a competitively priced B grade space.
Occupancy rates have increased from around 30% prior to refurbishment to 90%.
Rent levels have increased moderately from approximately $190/m² gross to $230/m² gross. Significantly, the incentives required to secure and retain tenants have reduced substantially.

The owners, having recognised the importance of an ongoing refurbishment and maintenance programme, have undertaken an upgrade to the façade and are now considering upgrades to the foyer and lifts.

Re-engineer existing building control systems or install new building management and control systems to optimise plant operating strategies and performance;
Install sub metering on electricity and water systems to enable monitoring and analysis;
Install high efficiency, low loss lighting and lighting control systems;
Install high efficiency chillers and add variable speed drives on pumps or fans where appropriate;
Instigate co-mingled waste recycling programmes for paper, cardboard, reusable stationary, drinks containers and other recycling programmes such as composting for food waste;
Install AS 3666 compliant cooling towers to minimise water leakage and install other water saving devices such as low flush toilets, automatic sensors on urinals and flow restrictors on hand basin taps.


Refurbishing Lower Grade Buildings
Adelaide’s ageing office stock has been a key ingredient in the recent flurry of new development activity. While demand for office space has grown steadily, it is unlikely to keep up with the supply boom between 2006 and 2008.

With increased stock on the market, there will be greater competition between secondary building owners for tenants. This provides a dilemma for owners of lower grade office stock which is becoming obsolete.

Owners can elect to:
• Do nothing and risk losing income through declining occupancy, increased running costs through poor maintenance, and falling effective rents;
• Consider withdrawing the building from the market;
• Redevelop their asset;
• Sell the building;
• Consider a change of use or;
• Refurbish.

The flight to quality suggests that the market for secondary space is diminishing. However, a significant proportion of Adelaide’s office tenants are price sensitive, and will not be drawn to the prime space. Their requirements are for good clean office space at a competitive price that provides reasonable comfort and services.

As the standards expected by tenants rise, even at the lower and older end of the market, owners will need to urgently consider refurbishing these properties in order to retain their clients.

Often with older buildings, a more creative solution to the future of the building is required. As part of the city’s Workforce Growth Plan, Adelaide City Council has launched a programme to assist in the refurbishment of lower grade properties.

In 2007 Council will be offering assistance towards planning refurbishments. The programme can offer up to 50% towards professional fees incurred developing a commercially viable concept plan for buildings which are currently under occupied and in need of renewal. These buildings must be located within the city (core or frame) or North Adelaide.

For more details contact Adelaide City Council on (08) 8203 7518.
What Tenants Want

Virtually all recent construction activity in the Adelaide office market has been tenant led rather than speculative. These tenants have shown a preference for purpose built accommodation aligned to their corporate objectives.

Typical requirements are greater energy efficiency, a more efficient floor-plate with a side core rather than a traditional central core and better building services.

Given that the requirements of large tenants can be better accommodated in newer buildings, it is not surprising that new or refurbished buildings typically outperform older secondary stock in achieving higher rentals and lower vacancies.

However, many smaller tenants are price sensitive and will be drawn toward lower grade space, (see Refurbishing Lower Grade Buildings).

It is therefore important to know what type of tenants will be attracted to the asset, what do these tenants want from a building and what has worked for other similar buildings?

Table 3: Changing Tenant Requirements

<table>
<thead>
<tr>
<th></th>
<th>Today</th>
<th>Ten years ago</th>
</tr>
</thead>
<tbody>
<tr>
<td>Floor-plate size</td>
<td>1,500 - 2,000 sq.m</td>
<td>1,000 sq.m</td>
</tr>
<tr>
<td>Floor-plate configuration</td>
<td>Demand for more efficient floors, could involve side core configuration.</td>
<td>Little attempt to consult with tenants. Most buildings were central core.</td>
</tr>
<tr>
<td>Lifting</td>
<td>Reduced waiting times / improved control systems. Enhanced features within lifts (eg live TV feeds).</td>
<td>Emphasis on waiting time and lifting capacity.</td>
</tr>
<tr>
<td>Air conditioning</td>
<td>Greater flexibility / multi zones on individual floors. Cheaper after hours use.</td>
<td>Shift to VAV systems with control at individual floor level.</td>
</tr>
<tr>
<td>Security</td>
<td>Individual floor access</td>
<td>Central – in lobby only</td>
</tr>
<tr>
<td>Other issues</td>
<td>Retail space, coffee shops, ATMs. Concern with environmental management / green issues</td>
<td>Foodcourts More concern with external appearance than quality of internal working environment.</td>
</tr>
</tbody>
</table>

Source: Jones Lang LaSalle

There are a number of issues to consider when undertaking a refurbishment.

Owners should be looking for opportunities to improve the return from the property. This may include upgrading the building services, increasing floor space ratio, converting the space to a more appropriate usage and developing additional car parking.

A strategic refurbishment programme needs to consider the following factors:

- The tenancy schedule
- The timing of construction costs
- The downtime in the rental income stream
- The most efficient construction approach
- The leasing plan for the property
- The prevailing market conditions.

When embarking on a refurbishment, a checklist should cover the following issues:

- What tenants want – what are tenants demanding from their space?
- Heritage requirements – what are the compliance regulations?
- Sustainability & ESD – tenants are increasingly using ‘green’ design as a criteria for location selection.
- Compliance – major refurbishments require compliance under several building regulations, including the Building Code of Australia (BCA).
- Change of Use – this is likely to result in a change of classification under the BCA as well as a change of use under the Adelaide (City) Development Plan.
- Duty of care – requirement for the tenants, contractors and general public.
- OH&S – legislation exists around access and essential services including fire systems and emergency lighting.
- Building services – tenant requirements are currently focused on back-up energy, air conditioning, lift systems and security.
- Dispute resolution – disputes can often compromise the timing and quality of the project. Provisions for this should be built into the contract.
- Minimising disruptions – a plan needs to be communicated to tenants demonstrating the owner has taken every effort to minimise the impact.
- Moral rights – building owners should consult the original design team where possible, prior to making modifications to the external façade.
CASE STUDY:
45 Grenfell Street

Background
45 Grenfell Street is an 18 storey secondary grade office building of some 12,785 square metres in a high profile location.

The building was purchased by local private investor Thomco P/L in December 2001 for $15.57m. At the time of purchase, the lease profile was relatively poor and competition in the B grade market was strong. A minor refurbishment of the building was considered necessary to reposition the building as higher quality, competitive space.

The refurbishment included a remodelled lobby and pressure cleaning the facade.

Motivation
This former prime grade building required a face lift to enhance its appeal to both existing and future tenants. The head tenant, Vero, was nearing the end of its lease term and was considering its future accommodation needs.

Result
The refurbishment works has vastly improved the entrance to the building and street appeal. Vero has not only been retained as the major tenant but has expanded within the building. At the time of sale, the building was 97% occupied compared to 54% just two years earlier.

The asset was sold to OFM Funds Management $23 million in early 2006, representing a 47.7% increase in capital value in just over 4 years.

Compliance
Compliance with development and building legislation is required prior to embarking on a refurbishment programme. In the first instance it is advisable to contact the Adelaide City Council for guidance on a specific project and to determine if a Development Application is required.

Under the Building Code of Australia, fire safety regulations often present the most onerous and costly compliance matter to owners undertaking a refurbishment programme. Requirements include items such as emergency exits, fire detection systems, emergency warning and intercommunication systems, fire sprinklers, and emergency lighting.

Building surveyors may withhold certification and require modifications if builders do not comply with legislative provisions concerning access and facilities for people with a disability. Disability discrimination claims under state and federal legislation may result in orders for the building owner to pay damages and undertake reasonable acts such as improving access.

Amendments to the Commonwealth Disability Discrimination Act (DDA) are currently being considered. When they come into force it will be unlawful to discriminate against people with disabilities with regard to premises access.

For further details on requirements that projects might be obliged to fulfil, contact the Development Assessment Team at Adelaide City Council on (08) 8203 7185 or (08) 8203 7203.
Case Study: 86-88 Waymouth Street

Background
This former Commonwealth Bank premises was purchased by the current owners in 2001 with vacant possession. The two-storey building had been purpose built as a bank and provided approximately 1,000 square metres of floor area over two levels.

The refurbishment included removing the existing partitions, upgrading the two floors including new ceilings, and an upgrade of services, including air conditioning, lift and access. The work was undertaken on a speculative basis.

Motivation
The owners consider that the building has long term redevelopment potential, given its site area of 943 square metres, wide frontage to Waymouth Street (18 metres) and location in the core of the CBD. In the medium term the owners considered the building had significant potential to provide a secure income stream through undertaking a cost effective refurbishment.

Result
Local photographic company, Studio 2000 has leased the building on a 10+5 year lease providing a secure income stream and enabling the owners to recoup the cost of the upgrade in less than 10 years.

The owners estimate that the capital value has tripled in the five years since purchase.

Change of Use
An alternative to a full office refurbishment may be a change of use or conversion to strata offices. Numerous former office buildings have been converted to other uses, with some of the more prominent ones listed in Table 4.

Both Franklin Central Apartments and the Medina Grand Hotel are heritage listed buildings, with the conversions offering accommodation with a high level of character not normally provided in modern apartment and hotel developments. Such developments present the owner with a point of difference that may assist in marketing the building.

Strata titling an office building provides an opportunity for small companies to buy as an alternative to renting. It also allows small investors to purchase into well located CBD property that may have been otherwise price prohibitive.

For further details on possible change of use issues and possibilities, contact the Development Assessment Team at Adelaide City Council on (08) 8203 7185 or (08) 8203 7203.

Duty of Care; OH&S
Owners have a duty of care to provide a safe working environment to all building users.

To comply with OH&S regulations, building owners and refurbishment contractors are required to provide adequate access in and around the building during the refurbishment process. Additionally they are obliged to ensure the continuation of essential services during works such as fire detection and paths of egress and exit to ensure that occupant safety is not compromised during the works.

Other hazards to existing tenants, their staff and their business operations that could lead to public liability claims include:
- potential flooding
- blackouts and interruptions to the power,
- data and telecommunication systems
- disturbance of hazardous materials such as asbestos products.

Both owners and contractors risk substantial fines if they are found to be in contravention of OH&S regulations.

For further details contact SafeWork SA on 1300 365 255 or www.safework.sa.gov.au

Table 4: Selected Major Change of Use Projects in Adelaide CBD

<table>
<thead>
<tr>
<th>Project Name</th>
<th>Address</th>
<th>Year</th>
<th>Notes</th>
</tr>
</thead>
<tbody>
<tr>
<td>Franklin Central Apartments</td>
<td>Bentham Street</td>
<td>1999</td>
<td>Conversion of office building to 64 apartments in 1999</td>
</tr>
<tr>
<td>Chancellor Hotel</td>
<td>12-18 Currie Street</td>
<td>2000</td>
<td>Conversion of former Bennett &amp; Fisher Building to hotel (formerly Quoten Hotel)</td>
</tr>
<tr>
<td>UniHouse</td>
<td>160 Rundle Mall</td>
<td>2001</td>
<td>Conversion of former Bank SA offices to 98 apartments (student housing)</td>
</tr>
<tr>
<td>Rendezvous Allegro Hotel</td>
<td>51 Waymouth Street</td>
<td>2002</td>
<td>Conversion of office building to 4 star hotel of 202 suites</td>
</tr>
<tr>
<td>Medina Grand Treasury Hotel</td>
<td>142-160 King William Street</td>
<td>2002</td>
<td>Conversion of former Treasury Building to an 80 suite Hotel</td>
</tr>
<tr>
<td>King William Tower Apartments</td>
<td>65 King William Street</td>
<td>2004</td>
<td>Conversion of former ATO Offices to 126 residential apartments.</td>
</tr>
<tr>
<td>UWA Apartments</td>
<td>21 King William Street</td>
<td>2006</td>
<td>Conversion of former bank to 70 apartments for international students.</td>
</tr>
</tbody>
</table>
Building Grades

The classification of building quality by grade follows the classification system adopted by the PCA. The system has five grades: Premium, A grade, B grade, C grade, and D grade.

Premium and A grade are collectively referred to as Prime grade, whilst B, C and D grade is referred to as Secondary grade.

Effective Rents

Effective rents take into account the value of concessions or incentives used in the leasing of office space. The effective rents are estimated by converting incentives to a percent value, amortising the present value of incentives over the term of the lease and deducting the amortised value from the face rent.

Incentives

Incentives are assumed to apply to a 1,000m² plus letting in a prime building for a period of 10 years. Incentives will generally be much less for shorter lease terms.