MARKETING IDLE CORPORATE REAL ESTATE

Respondents to a survey provide the answers on how to unload a company's unwanted real estate holdings.

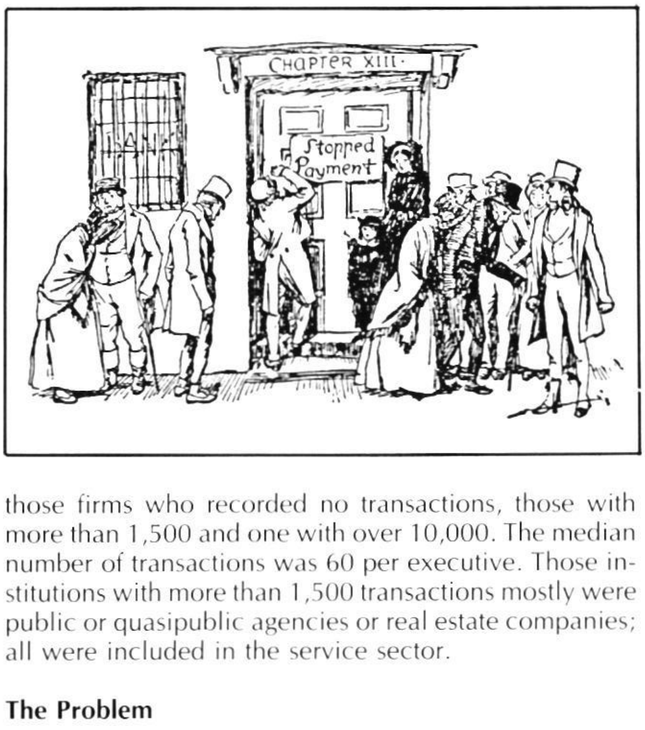
by Hugh O. Nourse and Dorothy Kingery

Corporate real estate directors were surveyed last year on their techniques for disposing of company real estate.[1] What follows is a report on the extent of the problem, their attempts at finding alternative solutions, evaluations of these alternatives and a review of other procedures.

Questionnaires on marketing idle corporate real estate were mailed to members of the National Association of Corporate Real Estate Executives (NACORE), the Industrial Development Research Council (IDRC) and the American Institute of Corporate Asset Management (AICAM). The mailing lists were screened for duplications and 2,176 questionnaires were mailed and produced a 10.6 percent return.

Table 1 shows the percentage distribution of respondents by type of business. Nearly half own properties worldwide and the remaining are equally divided between those with companies whose properties are in less than 10 states and those with companies whose properties are in more than 10 states and Canada. Not unexpectedly, conglomerates and manufacturers are mostly represented by worldwide companies, service businesses are represented by local firms operating in less than 10 states and retailing is represented by firms in 10 or more states.

To grasp the scale of real estate activities in corporations, executives were asked to estimate the total number of leases, lease renewals, purchases and sales transacted by their corporation last year. The survey included those firms who recorded no transactions, those with more than 1,500 and one with over 10,000. The median number of transactions was 60 per executive. Those institutions with more than 1,500 transactions mostly were public or quasipublic agencies or real estate companies; all were included in the service sector.



The Problem

Of the 288 executives who responded, 198 attempted to sell or lease 9,187 properties last year. Although two executives accounted for 2,000 of the 9,187 properties disposed, the remainder still is very large. The median attempts were 10 per executive. As shown in Table 1, manufacturers attempted fewer sales or leases than retailers, conglomerates or service industry firms. This is expected since they are more likely to have fewer facilities.

The problems involved in disposing of the properties were revealed in response to the question, "For these 'as is' dispositions with the longest time on the market, what problems made disposal of the properties difficult?" The most common problems were locations in depressed areas (the oil patch, farm areas), inner cities, small cities,

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TABLE 1

Percent Distribution of Executives by Number of Properties Attempted to Sell or Lease And by Kind of Business

Number of Properties	Kind of Business: Conglomerate %	Retail %	Manufacturing %	Service %	Total %
0	.5	.9	5	2	8
1–5	5	5	11	8	29
6–25	6	13	10	11	40
26 or more	3.7	7	3	8	22
Total	15	26	29	30	100

Total number of executives, 216 (12 missing)

rural areas with old properties, over 50,000 square feet, inadequately maintained or where new or existing comparable vacant space existed. Forty-nine percent of the problems mentioned were for the above reasons and, if poor market was included, this accounted for 57 percent of the responses. Finding a skillful broker also was a significant problem.

TABLE 2

Alternative Choices for Disposition

Alternative Choices	Number of Executives Successful	Number of Executives Attempting	Properties Disposed	Properties Attempts
Sold "as is"	173		5044	
Leased "as is"	155	198*	2242	8497*
Renovation, subdivision, etc.	47	60	412	538
Donation	42	51	93	152

*Estimated for both sales and leasing "as is" together.

Alternative Choices For Disposition

Three main alternatives of disposition were explored: disposition "as is"; disposition by renovation, subdivision or other modification; disposition by donation. How did the respondents utilize these approaches? Of the 9,187 properties where disposal was attempted, 7,286 (79 percent) were sold or leased "as is." Six percent of the properties were considered for renovation by 26 percent of the executives and, 78 percent who tried this approach succeeded with 77 percent of the properties. Few tried to donate the property. Only 1.7 percent of the properties were considered for donation by 22 percent of the executives and 42 (82 percent) of these executives succeeded in donating only 61 percent of the properties. In terms of moving properties, real estate executives were successful, however, 1,396 (15 percent) of the properties were not sold or leased at the year's end.

There were no discernible differences in companies attempting to renovate, but there was a definite pattern in donation attempts. Conglomerates and manufacturers attempted to donate more proportionally than retailers and service companies. This may be because large tracts of land are easier to donate and such holdings would tend to be more common among conglomerates and manufacturers. Nonetheless, there was no industry pattern among the successful donations.

Evaluation Of The Alternatives

Selling "As Is"

The great advantage of selling "as is," when the technique quickly yields a good price, is that additional resources are not used for the sale. No new capital is expended to renovate, subdivide or modify the property. This also means that new skills or staff are not needed in real estate development.

Another advantage is that the corporate officers are pleased with the real estate department for generating the quick cash flow, especially when it is needed to improve the year's performance for the stockholders or financial analysts. Also, this quick sale takes less of the real estate director's time and he is free to take on other responsibilities.

One disadvantage of this approach is that the company may lose an opportunity to generate profits from the redevelopment, subdivision or modification of the property.[2]

Another disadvantage is the corporation may be underutilizing its talents. Not every real estate group has the skills required for redevelopment, but many do. A major problem for keeping skilled executives in corporate real estate is the stifling effect of seeing opportunities become available without being able to utilize them for corporate profit.[3]

Also buyers may not be able to visualize the potential for alternative uses without first seeing the necessary renovations and changes in zoning and other environmental constraints already accomplished. It is possible that the increased uncertainty will lower potential selling prices relative to the available opportunity. Similarly, large plants with more than 50,000-100,000 square feet may be slow to move, whereas the same space subdivided into smaller sizes may sell quicker.

Plus, the property may be on the market a long time producing carrying costs for security, etc., that create a cash drain each month the property remains vacant. Or the property could be vandalized which would increase the costs for maintenance and result in a price loss when sold. Of the 155 responses to how executives overcame obstacles to selling or leasing "as is," 71 (46 percent) indicated they somehow changed the terms of sale.

Leasing "As Is"

It may be easier to lease property "as is" than to sell. By leasing, the company keeps control of who uses the property. This could be important if the property was adjacent to other corporate property or if the company wanted to prevent their competition from using a particular site. (This can be more important for retailing than manufacturing.) Also, the company does not give up the potential reversion value of the site at some later time. Another approach, subleasing, may be the only way for a company to get out from under current lease contracts for property that is unneeded and idle or is underutilized.[4]

In offsetting the advantage of leasing "as is," there is the same disadvantage as selling "as is," plus the top management may be unhappy at not receiving a lump sum payment. The company does not perceive that the risk of waiting for the reversion at a later date is reward enough. Because the property is being managed as real estate for other business use, the leasing solution puts the company directly into the real estate business, an option not wanted by most non-real estate corporate managements.

Of course, the corporate management may consider the lease solution as an intermediate step to a final sale. In fact, the lease "as is" may get around some of the disadvantages of the sale "as is" because potential investor buyers can actually see the lease revenues and be willing to pay an appropriate price for the present value of those benefits plus potential reversion. A better price may be received by taking this step before selling.

Renovation, Subdivision And Other Modifications

To overcome the disadvantages of selling or leasing "as is," it may be necessary to consider subdividing, renovating or other modifications of the property. Some responses from the survey indicated this approach only was used when necessary for a particular situation. Of the 155 responding to ways of overcoming selling or leasing "as is," only 28 (18 percent) indicated they altered the property for the buyer.

The greatest advantage of subdividing or renovating is the higher price received for the property and the return on the marginal investment in redevelopment. Over half the executives who were successful indicated it was the market for the change that made it work. Other advantages, however, also are possible. The renovation process keeps the property ready for the buyer and reduces vandalism. Although the time for redeveloped properties to be on the market ranged from 1-36 months, the mean only was nine months, and the median only six months. Eighty-three percent of the executives indicated that the time on the market for these properties averaged one year or less. Redevelopment also makes very visible the properties potential alternative uses.

Since corporations tend to invest in businesses rather than projects, they often reject redevelopment as outside the mission of their business even when it can be profitable. Of the 159 executives who would not redevelop idle property for disposition, 61 (38 percent) indicated such risk was outside the skills of their business and an additional 18 (11 percent) indicated their company was "not in the real estate business." Thus, 79 (50 percent) said this was a reason for not using that approach. This was particularly true among manufacturers who, rather than retailers, conglomerates, or service sector executives, more often suggested they were not in the real estate business. This is true since retailers are more concerned about position in space for strategic reasons and are more inclined to set up branches and new stores. Nonetheless, a number of these companies should look more closely at the extent of their real estate dealings.

An additional advantage of redevelopment is the goodwill it can yield for the corporation in a local community. The attempt to renovate older property where appropriate in inner city or small town areas, may spark a turnaround for an area that generates community support. In addition, it can make the location more attractive and can replace lost job opportunities.

The disadvantage of redevelopment is the need for increased resources—capital, time, talent and judgment of development risk—which may not be necessary to sell the property for a good price. Or, even if redevelopment is considered, the return relative to risk may be less than other alternative options. But this argument only was given by 34 (21 percent) of the 159 executives who did not use this approach.

Development certainly is a risk, and there is no guarantee of success even after physical, zoning, pollution and other obstacles are overcome, i.e., older properties may be unsuitable for renovation, and this may not be discovered until the work begins; internal staff skills may not be sufficient; the market for the finished renovation may have disappeared by the time the work is completed.

Conversely, several executives indicated they were successful in subdivision or renovation because few changes were required so the resources needed weren't extensive. As one executive said, it may be possible to take the risk out of a sale by solving environmental and zoning regulatory problems. Just reducing these uncertainties can increase the price more than proportionate to the effort.

Donation Of A Property

The executives responding to the survey resoundingly recited the disadvantages of donation. This option usually is not considered unless selling the property will be difficult and its final price would be below book value. Unfortunately, the tax law is such that if the price is below the adjusted basis, it is better to sell the property for a loss and give the money to a charity than to donate the property.[5] Of the 135 executives who indicated they did not use donation last year, 93 (69 percent) recited its economic disadvantage; several indicated it would establish a bad precedent; 20 said that donation is not an option for leaseholdings or for certain institutions and public agencies.

Yet, some executives found donation to be a useful approach since the tax write-off was an advantage. The Trust for Public Lands, to whom two properties in the sample were donated, suggests the best donation is a bargain sale when the property is sold for a price equal to adjusted basis or slightly higher. This reduces long term capital gains taxes. They point out that the present value of such sales may be greater than a direct sale at market price.[6]

From the corporation's viewpoint, no new resources have to be invested in the property to donate and the donation creates goodwill in the community. Properties were usually donated to municipalities, churches and other civic organizations, while a few were presented to educational institutions. The Conservancy was mentioned three times and the Trust for Public Lands was named twice.

The Best Alternative

With the alternatives for disposition subject to the variety of advantages and disadvantages that have been enumerated, how is the best one chosen? Theoretically, the solution is arrived at by estimating the present value of selling "as is" compared to the present values of leasing "as is," subdividing, renovating or other redevelopment or donating the property.[7] Other advantages and disadvantages also have to be considered. As already mentioned, redevelopment may be eliminated because the company is not in the real estate business. Does that mean considering alternatives is wasted? Quite the contrary. A disadvantage of selling or leasing "as is" is the inability to identify potential buyers and to have those buyers visualize what can be cone with the property. So the present value analysis becomes a selling tool to show the possibilities for the property.[8] The technique also may identify a higher selling price by targeting a particular market. Nonetheless, one executive who was interviewed said this approach might be an implied warranty that if the buyer failed in a suggested development approach, the corporation might be sued.

Implementation

The first question to ask when trying to sell property or when deciding on alternative approaches is who are the likely buyers? Executives were asked what procedures they followed in this search for potential buyers. Their responses are shown in Table 3.

Most executives said brokers were used to indicate buyers but identifying an excellent broker often was a problem in selling or leasing properties "as is" since many contracted out the marketing function. Still 53 percent of the executives kept track of who is looking for space in the same business, and six percent utilized networking among comparable executives at like companies to identify potential buyers for "as is" sales or leasing. Also nine percent employed advertising techniques as a way to identify buyers.

Over half of the executives undertake in-house or contract out for a study of the site's highest and best use. Manufacturer and conglomerate executives are more likely to use such studies than those in the retail or service sectors. For some properties the highest and best use study is unnecessary because the characteristics of the property indicate a particular buyer. Nonetheless, sometimes selling "as is" without considering other possibilities only may be the easiest and not the best way.

Some companies, especially those in retailing, avoid selling to competitors. Of the 44 executives who said they avoided selling to a rival, 24 were in retailing, 7 were in conglomerates, 8 were in the service sector, and only 5 were in manufacturing. The choice is a marketing consideration and reflects geographic placement by companies who do not want to give a position to a particular competitor.

TABLE 3

Procedures Used In Identifying Potential Buyers

Procedure	Executives Responding Number	Percent
Identify excellent brokers	210	92%
Keep track of who is looking for space in the same business	120	53%
Undertake or contract for study of highest and best use of site	119	52%
Avoid selling to firms in the same business	44	19%
Selling techniques — sign, phone, mail, etc.	20	9%
Networking	13	6%
Adjacent landowner	5	2%
Other	3	1%

Since so many executives responded by citing the necessity of choosing a good broker, the follow-up question to corroborate their answers was, "What role do brokers play in the disposition process?" Only six percent of the executives did not need a broker, and often the broker was used as a consultant or sales/leasing agent or as both.

The respondents had definite opinions on the usefulness of alternative techniques for notifying potential buyers on the availability of property. Putting a sign out was identified by the executives as the most useful technique. As shown in Table 4, when the very useful and useful responses were combined and the not useful and no responses were combined, putting a sign on the property was a clear first.

TABLE 4

Usefulness in Establishing Contact with Buyers

Techniques	Very Useful/Useful	Not Useful/No Response
Sign on property	88%	12%
Flyers	65%	35%
Ads in local newspaper	59%	41%
Surplus property lists of professional associations	52%	48%
Ads in trade journals	45%	55%
Notify State Department of Industrial Development	43%	57%
Telephone canvass	40%	60%
Ads in *Wall Street Journal*	27%	73%

Using this same approach, flyers, ads in local papers and association surplus property lists also were found useful. The techniques considered less helpful were ads in trade journals, state departments of industrial development, telephone canvassing and ads in the *The Wall Street Journal*.

As expected, executives in retail and service industries did not find state departments of industry useful; flyers also were less helpful to retailers while conglomerates found them most beneficial; retailers found signs more useful than other executives.

A sign on the property is effective relative to the other techniques, since it is a notice of availability to all who pass by the site. It is so useful that often a sign is the only technique used to sell a property—no brokers, no flyers, just a sign. With retail site selection being so sensitive to position, retail searchers will designate a target area and look for available locations. Signs are an effective mode of advertisement for this purpose. However, manufacturing sites, depending on the situation, may be close to market, transportation, labor or materials. In this case, signs may not reach the potential user.

Property Disposal In Communities Where A Closing Has Significant Impact

A sensitive situation occurs when a firm closes in a community where the company significantly impacts on the area's total employment. Retail firms saw no problem here, but one firm responded that corporate policy on the issue could not be disclosed and another indicated they had a systematic policy of not establishing plants in such situations. Since this argument has not appeared in location literature, it would be useful to know whether it is common for firms not to locate in small towns because of the closing problem. When a company had to shut down a facility, survey respondents indicated it was wise not to create any surprises, to work with local community leaders to find another user for the facility who would hire the displaced workers, to give generous severance pay, to assist workers in finding new jobs and relocation, and to hire local lawyers to assist in the negotiations.

Summary And Conclusion

The real estate executives who participated in the survey disposed of 85 percent of the available properties. However, not known is whether this disposition obtained the greatest present value net of costs. There is information that donation, the least used disposal approach, also showed a poor record compared to the attempts made.

Property redevelopment was tried by more executives with more properties and with a much better record of disposition than the donation approach. However, redevelopment was minor compared to selling or leasing "as is." The latter requires an important marketing effort to identify what the buyer of a particular property might demand, and then to use the corporation's resources to meet the request and produce a good profit. Properties moved fast once redeveloped, nonetheless, most executives considered the approach unnecessary, or not usable because the funds were not available. Companies were reluctant to invest in the redevelopment of surplus property because they were not in the real estate business; the return relative to the risk was considered not appropriate; or either the development skills, or ability to understand the risk were not present.

Redevelopment is not necessary for all properties, but it might be a solution for those aging or large facilities with over 50,000 square feet in inner cities, small towns, rural areas and other depressed real estate markets. It is not known if the executives who sold or leased their properties "as is," chose this approach because it provided the quickest and greatest cash with no investment on the part of the seller, because it was the easiest solution or because their company would not allow real estate development.

The best solution may be the quick sale of property "as is" to another firm in the same industry. But some of the responses suggest that more effort could be directed at identifying the potential users of a property. Whether or not such ideas are used for redevelopment, they would help suggest target selling prices, and they would yield cash flow estimates that could be used in selling the property to potential buyers.

NOTES

1. This study was funded by the Homer Hoyt Institute, the American Institute of Corporate Asset Management and the American Society of Real Estate Counselors.

2. Baird, Robert E. "More Innovative Approaches for Surplus Properties," *Industrial Development* (July/August 1984): 14-17. Bolan, Lewis. "Disposing of Excess Real Estate: Techniques and Considerations," *Industrial Development* (November/December 1982): 19-20, 29-33. Brown, Robert Kevin. *Corporate Real Estate: Executive Strategies for Profit Making*, (Homewood, IL: Dow Jones-Irwin, 1979): 87-109. King, Jonathan and Johnson, Robert E. "Silk Purses from Old Plants," *Harvard Business Review* (March/April 1983): 147-156. Martin, Thomas J. and Gamson, Melvin A. "Adaptive Re-use Gives Life to Old Buildings," *Real Estate Review* (Fall 1976): 28-33. Schaefer, James T. "The Real Estate Profit Center: Making the Most of Hidden Assets," *Industrial Development* (September/October, 1980): 6-10. Smith, Leland F. "Turning Obsolete Buildings Into Income," *Industrial Development* (July/August 1984): 9-13.

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7. Jewett, Lincoln C. "How to Market Surplus Real Estate," *Harvard Business Review* (January-February, 1977): 7-10; Jewett, Lincoln C. and Troen, Mark L. "Mining Corporate Real Estate Assets for Cash," *The Real Estate Finance Journal (Summer, 1986): 46-55.*

8. *Ibid.*