

Creative Counseling: Preserving the Hawaii Opera Theatre

BY KAREN CHAR, CRE, MAI

BACKGROUND

IN MAY 2010, Karen Char, CRE, president, John Child & Company, Inc. and Christine Camp, CRE, president and CEO of Avalon Group, LLC, both of Honolulu, were honored by The Counselors of Real Estate® with the 2010 James Felt Creative Counseling Award for their work developing and implementing a long-term real estate strategy for the Hawaii Opera Theatre (HOT) in Honolulu. Their work enabled HOT to continue to produce outstanding opera performances and nationally recognized educational programs in Hawaii. The Felt Award recognizes credentialed members of The Counselors of Real Estate whose work most exemplifies excellence and ingenuity in real estate counseling resulting in far-reaching and long-term benefits to a community and its citizens. The following case study describes the process through which HOT was able to turn a liability into an asset.

INTRODUCTION

CHAR AND CAMP'S WORK FOR HOT spanned a four-year period that began in 2005 when Char joined HOT's board of directors. At the time, HOT was faced with making significant cost cuts in order to continue operating. Camp joined the board in 2008. Together, they were able to uncover assets belonging to the opera theatre and develop a plan that included moving its administrative and box offices to a safer, larger location along a major traffic artery and building a more appropriately sized rehearsal hall.

The full plan developed by Char and Camp involved relocating offices, renovating existing property, selling property and obtaining a line of credit. Today, the 51-year-old Hawaii Opera Theatre is maintaining its performance schedule as well as its educational programming.

CASE STUDY:

COUNSELING FOR HAWAII OPERA THEATRE

In 2005, at my first meeting as a new member on the board of directors of HOT, it was explained that financial exigencies required us to consider selling the medical office building that had been donated to HOT. At subsequent meetings, the likelihood of this sale was reaffirmed. HOT, like many performing arts organizations, faced significant challenges in its operating cash flow. However, HOT owned the fee simple interest in two properties:

- Waimanu property
- Beretania Medical Plaza (BMP)

HOT performs at the NBC Concert Hall in Honolulu. Both properties are about two blocks from the Concert Hall.

WAIMANU PROPERTY

DESCRIPTION AND CHALLENGES

The Waimanu property was a consolidation of shabby industrial warehouse properties that housed HOT's administrative and box offices, rehearsal hall, shop and



About the Author

Karen Char, CRE, MAI, ASA, president of John Child & Company, is responsible for developing and managing the company's professional practice that includes real estate consulting, appraisal, and business valuation. She specializes in complex real estate and business

valuation assignments. Char also serves on the board of directors of two non-profits: Hawaii Opera Theatre and Hawaii Women's Legal Foundation (HWLF). The mission of HWLF is to help women and children in need in Hawaii.

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HOT box office, administrative office street frontage, before...

storage. The property had front parcels and a back parcel; no on-site parking. The buildings were originally constructed between 1936 and 1955.

In 2005, the Waimanu property was in disrepair. Despite significant repairs to the roofs twice in the preceding ten years, they leaked whenever it rained and mold was growing in the ceiling tiles and walls. The buildings were clearly in need of major repair, maintenance and renovation to comply with current building code requirements. The health and safety of the staff, volunteers and artists were a major concern.

Historically, HOT had been opposed to financing any capital improvements, repairs or maintenance of its real estate. Instead, HOT had solicited several major benefactors for donations to renovate the Waimanu property—without success. As a result, some board members believed the property was too expensive to renovate and maintain, and strongly advocated selling it and moving out.

As a result, no action was taken and no repairs were made to the Waimanu property. When it rained, furniture was moved, and buckets were strategically placed to catch the water.

BERETANIA MEDICAL PLAZA DESCRIPTION AND CHALLENGES

Beretania Medical Plaza (BMP) was a poorly maintained leasehold medical/dental office building. The leased fee interest in the land was donated to HOT in 1995. Initially the ground rent from the leasehold building was used to pay HOT’s operating expenses. HOT became accustomed



... and after

to collecting ground rent without incurring expenses.

The building has 25,261 square feet of rentable area including a ground floor retail space, and medical/dental office spaces on the second, third and fourth floors. Parking is located on the ground and second levels.

In the early 2000s, the lessees were nearing retirement and not interested in maintaining the building, as required in the lease agreement. The building required capital improvements, repairs and maintenance. In 2003, the lessees gifted the leasehold interest in the building to HOT rather than make the required repairs and capital improvements.

Initially HOT had been collecting ground lease rent. Through the donation of the leasehold interest, HOT was now managing a medical office building and carrying the operating expense for the vacant spaces in the building.

In 2005, the leasing status of the building was as follows:

Lease term	Percent of building
Lease expires in 2014	22 %
Lease expires in 2006	20
Month-to-month	26
Vacant	32
Total	100

HOT could not lease the vacant space and was in jeopardy of losing existing tenants because of the building’s condition. (After visiting the property, one board member exclaimed, “I wouldn’t bring my dog to a vet in this building.”)

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Water damaged ceiling tiles, before...

Many of the board members wanted to sell the property “as is” to fund HOT’s operations. Similar to its position on the Waimanu property, the board was opposed to financing repairs and maintenance.

COUNSELING PROCESS

In 2005, HOT had 66 board members. With the exception of four residential realtors, a retired real estate attorney and myself, the board members had limited commercial real estate expertise. Because of the experience and comfort level of several bankers and financial advisors (active and retired), the board had a strong preference for liquid investments. The board had seriously discussed selling its real estate.

The concept of a long-term real estate strategy began in 2005 when a task force was formed to study HOT’s financial needs and its real estate.

The task force requested pro bono services of a structural engineer. It obtained an analysis and bid from a roofing contractor. The structural engineer opined that the buildings were structurally sound; however, the spaces were not being used efficiently. The roofing contractor provided recommendations that would temporarily seal the roof leaks at a reasonable cost.

To educate the HOT decision makers, I made a series of presentations to the task force, steering committee and eventually, the board of directors.

1. With regard to BMP, I explained that the building must be repaired and maintained to attract new tenants, regardless of whether it was to be sold or retained.



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The task force forwarded the recommendation to the steering committee. The steering committee forwarded the recommendation to the board for approval. The board approved the renovation of BMP to be funded by a short-term mortgage loan in February 2005.

2. With regard to the Waimanu property, I explained that HOT should consolidate and “right size” (downsize) its operations and sell a portion of the property (front parcels) to fund the renovations and repairs required for the smaller property (back parcel) and for operating losses.

HOT staff maintained that the current space was already too small. The task force and the steering committee did not recommend action. However, an informational presentation explaining the situation was made to the board in December 2005.

In December 2006, Joshua Dachs, an internationally known professional theatrical consultant, was visiting Hawaii. For a small fee, he visited the Waimanu property and met with HOT staff. He reported that HOT has very little room to “right size.” He said that other theatrical companies have larger shop areas and HOT must plan for long-term growth in staffing. He recommended rebuilding or renovating the entire Waimanu property to achieve a larger footprint and efficiency.

Dachs’ report was not helpful to the task force. HOT already had tried unsuccessfully to raise funds for capital improvements to the existing facility. Therefore, if nothing was sold, financing was the only option. A loan

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for rebuilding or renovation could only be repaid through excess operating income. There was no excess income.

In January 2007, I presented Dachs' report to the task force and steering committee. In addition, I presented worksheets showing that the cost of real estate in Hawaii was substantially higher than on the mainland and that HOT could not afford Dachs' recommendations.

The task force and steering committee were stumped. Rain continued to soak the ceiling tiles, grand piano, opera library and all of the interior spaces. Buckets of water were everywhere.

In 2008, CRE Christine Camp joined HOT's board of directors and the task force. As a new member and real estate counselor, she independently reviewed and analyzed HOT's financial needs and real estate situation. She saw the vacancies in BMP as an opportunity. She recommended moving HOT's offices to BMP and renaming the building.

Christine's company had an architect on staff. Under Christine's direction, the architect visited the property and interviewed the HOT staff to understand their operations and real estate requirements. The architect produced conceptual architectural studies and construction cost estimates. He designed alternative floor plans that fit HOT's administrative and production functions into the back parcel. He met with HOT staff and convinced them that the smaller spaces would function adequately. (Lesson learned: Have an architect prepare conceptual plans before attempting to downsize an organization's facilities!)

He also prepared cost estimates for alternative scenarios. Christine reviewed the cost of building administrative space into the existing building with the shop space (on the Waimanu property) and compared it to the cost of building tenant improvements in BMP. Christine determined that it was cost effective to build out and occupy space in the medical office building rather than build new office space in the shop building.

Christine presented her analysis, alternatives and recommendations to the task force, which approved and forwarded the recommendations to the steering committee.

RECOMMENDATION

The composition of the steering committee and board, with limited real estate expertise and a strong preference toward liquid investments, made difficult our task of

advancing what we analyzed to be the logical and best course of action. It was critical that we collaborate toward a strategic initiative of educating the steering committee and board members with a comparative analysis in a format that could be easily understood.

In September 2008, the steering committee recommended the following long-term real estate strategy for approval by the board:

1. Permanently move the administrative offices to BMP;
2. Obtain a line of credit of \$500,000 to pay for the tenant improvements and move;
3. Sell Waimanu front parcels to pay for renovation of the back parcel;
4. Renovate the Waimanu back parcel to accommodate the rehearsal hall, shop and storage.

The strategy was presented in small group presentations to allow ample time for individual board members to understand the strategy and financing requirement.

In November 2008 the board unanimously voted to accept the task force recommendations.

NEXT STEPS

Christine, who is a licensed broker, now had the task of selling the Waimanu front parcels. By November 2008, the real estate market had stagnated. However, with creative thinking and several months of negotiation, Christine sold the property by identifying the most motivated potential buyer—the property owner across the street who needed the property for long-term expansion.

In April 2009, HOT's staff moved into its new offices in the building now known as Hawaii Opera Plaza. Thus, the building that was to be sold to fund operations continues to provide investment income to fund operations, and the HOT staff and volunteers enjoy a healthy and safe work place from where they produce outstanding opera performances and nationally recognized educational programs.

A new task force was formed to complete the renovation of the back parcel. The task force included Christine, a structural engineer, architect, land planner, and other board members.

COUNSELING SKILLS

To develop and implement a long-term real estate strategy for HOT, we undertook a careful and lengthy process of

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understanding the issues and facilities required to produce great opera in Hawaii. We used our combined expertise and experience related to:

- Real estate valuation;
- Feasibility studies;
- Highest and best use analysis;
- Management of office and industrial properties;
- Site selection;
- Development;
- Brokerage;
- Project management.

In addition, we used our counseling skills to communicate the real estate alternatives and recommendations in a manner that was understandable to a nonprofit board comprised of opera enthusiasts.

RESULTS OF HOT'S LONG-TERM REAL ESTATE STRATEGY

An important measurement of the livability and vitality of a community is the prominence of its culture and arts. Opera is the most sophisticated and expensive performing art. In the United States, opera's dramatic stages and highly specialized artists require significant private funding and/or endowment. In Hawaii, the cost to produce opera is high because of the cost of construction and/or shipping of the stage sets, airfare and housing to bring in the artists, and costs associated with doing business (for example, union labor).

Without developing and implementing a long-term real estate strategy, HOT would have been required to make significant cost cuts, or worse.¹ Instead, in 2008 and 2009,

Charity Navigator gave HOT a four-star rating. Only four other opera companies in the United States have achieved Charity Navigator's highest rating. HOT was the highest rated opera company.

Because of its long-term real estate strategy, HOT has been able to:

1. Continue to produce great opera;
2. Continue to offer its nationally recognized educational program to Hawaii's school children;
3. Fund its operating losses for fiscal years ended May 31, 2009 and 2010;
4. Upgrade its facilities by moving its administrative and box offices from dilapidated warehouse space in an industrial district to healthy and safe offices in a commercial office building along a major traffic artery;
5. Celebrate its 50th anniversary in 2010;
6. Plan for 50 more years of grand opera in Hawaii. ■

ENDNOTE

1. Since 2008, the following opera companies in the United States have closed, are in bankruptcy or have suspended operations:
 1. Orlando, Fla.
 2. Baltimore, Md.
 3. Hartford, Conn.
 4. Orange County, Calif.
 5. Western Massachusetts
 6. Augusta, Ga.
 7. Opera Pacific
 8. Florida Grand (cutbacks in productions)
 9. Connecticut Opera