

Property management: an electric utility view

by R.J. Smith

It seems unavoidable that any corporation that is to be successful in property management must get into land development.

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Like most of you involved in real estate for the electric utilities, our primary interest has been land acquisition and right of way acquisition for as long as anyone can remember. We were kept busy acquiring land or land rights for power plants, substations, and transmission lines until the late 1970's. Over the past few years the demand for electricity has not been growing as rapidly as anticipated and the requirement for land has decreased. In fact in the Eastern U.S. the acquisition of land for utilities has decreased to almost nothing for many utilities. Figure 1 illustrates this point quite well. There has been a marked decrease in land acquisition at Baltimore Gas and Electric over the past ten years. For example, 31 parcels of land for right of way were acquired in 1975 and only 7 in 1983.

Figure 1. Acquisitions of Land

	Land Acquisition		R/W Acquisitions	
	Parcels	Acres	Parcels	Acres
1974	12	225.6		
1975	2	40	31	34.7
1976	—	—	31	34.7
1977	2	11	26	97.6
1978	2	41.5	97	217.3
1979	3	.24	56	151.6
1980	—	—	19	74.8
1981	7	305	17	75.2
1982	2	77	9	3.8
1983	1	.04	7	15.5
Totals	126	1611.6	299	746.8

Many other utilities are experiencing the same reduction in work load. The question is what is to be done with a real estate staff of highly trained professional people who have many years of experience when there is very little acquisition work to do?

Over a long period of time most electric utilities found they had accumulated large amounts of land for various uses such as:

1. Power plant sites
2. Water reservoirs
3. Transmission lines



4. Hydro-electric projects

5. Substation sites

Some of this land is fully utilized, but much of it is not. Transmission lines are a good example of this underutilization. The large structures are several hundred feet apart depending on the voltage in the lines, but the land between the structures is only required for a wire crossing. A note must be inserted here regarding transmission lines. Many of the large electric utilities in the East, particularly those operating in metropolitan areas, acquire transmission line right of way in fee simple rather than by easement. Easement acquisition is the traditional method of acquiring transmission line right of way, and is still used by many utilities. However those that made the decision to acquire all transmission line right of way in fee simple 10 or 15 years ago had a good reason. In densely populated metropolitan areas such as the Baltimore-Washington area it is often very difficult to acquire right of way for an electric transmission line. If the right of way is acquired in fee simple the utility has more flexibility in planning new facilities since the right of way is available for future use. Economics can also be a factor. If you go back to construct three lines on one right of way you probably

will pay about three times the fee simple value of the right of way and you will still only have an easement. Therefore, in metropolitan areas where right of way is quite often used for multiple facilities, it is advantageous to acquire it in fee simple.

Regardless of whether a utility acquired transmission line right of way by easement or fee simple ownership the utility in all probability has vast land holdings. As was the case with most corporations in the U.S. these land holdings were generally ignored over the years. If someone contacted the real estate department and requested to lease a piece of unused land the utility might have agreed to accommodate the request. It was also very unusual to sell any unused land. Almost everything was held for possible future use. Many of you reading this article, who are in utility real estate departments, will recognize the following scenario.

The utility has a ten acre parcel of land in a growing community on a major highway that was acquired about twenty years ago. The use for which the property was intended never materialized, but now it is in the untouchable category "held for future use." The property has very good potential for development. In fact, many developers have inquired about its availability. There is no specific plan for this property, but the Planning Department has stated that they might build a substation there some day. The Real Estate Department, realizing the potential of the property, has tried several times to convince the Planning Department that there are other sites that could be acquired for a substation in the future when it is required. However the standard reply always seems to be, "We must retain this property for future use. What does it matter anyhow? We are not in the real estate business."

Where do we stand today?

We have seen already that there are probably vast amounts of underutilized land held by utilities. To manage these land holdings requires highly trained, experienced people who are often already in the Real Estate Department Staff. Many utility Real Estate Departments have been long involved in most of the following activities, if not all of them.

1. Acquisition of property including the determination of requirements, locating sites, making or obtaining an appraisal, negotiating, and closing the purchase. The above are all included in acquiring properties in fee simple or acquiring easements. Property exchanges which are becoming more popular would also be included in this area, as would condemnation.
2. Disposal of property including determination of value by appraisal, advertising or some other method of getting information on the property to prospective purchasers, negotiating with prospective purchasers, and closing the sale. Contributions and gifts of property are also included.
3. Granting easements including obtaining approval from Operating Departments, determination of value, negotiation of consideration, and execution of deeds.
4. Management of land includes leasing land held for future use and underutilized land, leasing company owned houses, and protection against trespassing and encroachments. Licensing transmission line right of way would also be included in this category.
5. Leasing of office space primarily for the corporation's use. Coordination of space needs, space availability surveys, negotiating lease proposals, negotiating rentals and terms of the lease are the functions that are performed. It is possible that leasing company owned space could be included if there is any to lease.
6. Leasing warehouse space and miscellaneous property includes studies for the location of the facility, studies of lease versus purchase or build, availability surveys, negotiation of rental and terms of lease.
7. Assistance to relocated employees could include purchasing the home from a relocated employee by the company or coordinating the activities of a contractor to purchase the home. In either case the home is resold and the company pays all or a part of the transaction depending on the Company's Employee Relocation Policy.

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8. Review of tax assessments and determination of tax liability, and discussing increases in assessment with the tax assessor. Any Real Estate Department that is capable of performing all of the above functions has the capability of handling any real estate transaction regardless of its complexity. Most utilities have very competent people who can be depended on to handle matters of the utmost complexity and importance.

Where do we go from here?

Nothing has value unless it has use for someone, and land many times requires the expenditure of large amounts of cash before it can be made useful. A parcel of unimproved land that is zoned improperly has little value until the zoning is changed. For example a large parcel of land zoned for agricultural use may be valued at \$3,000 per acre in Maryland. If the zoning is changed to light manufacturing, that land can suddenly be valued at \$70,000 per acre. The act of rezoning has increased the value of the land \$63,000 per acre. The land has not changed, but the use of it has. Carrying our example farther, if roads are constructed and sewer and water installed, the value of the land may increase to \$100,000 per acre. The changes that have taken place have cost someone something, probably several hundred thousand dollars, but the expected return is very high; therefore the investment is worth making.

In addition a property may have an excellent location but may not be large enough or have sufficient road frontage



Parking space for auto dealer on the right-of-way.

to be a viable property to a prospective developer. It therefore may be necessary to acquire additional property adjacent to the prospective property in order to create a more desirable site for development. In this case the old adage is true, you sometimes have to spend money to make money.

Land development

It seems unavoidable that any corporation that is to be successful in property management must get into land development. The question, is does the corporation take an active or passive role in land development?

There are four management models that have been identified which typify the approach any firm will have to real estate. It must be understood that these models are general in nature and may not fit every company exactly. The four models are:

1. Passive Acquisition/Disposition Model

In this model all of the decision making regarding acquiring or disposing of property is delegated to the operating departments. Excess property no longer needed for company operation is given to the Real Estate Department for disposition. The Real Estate Department, in addition to acquiring property and disposing of property, may also lease office space for the company, but this is not always true.

The majority of American companies fall into this category. Real Estate normally does not pose day-to-day challenges; therefore it falls down on the list of management priorities. These are the companies that "are not in the real estate business." This model involves no risk.

2. Active Acquisition/Disposition Model

The Real Estate Department takes a more aggressive approach. Real estate is recognized as an asset that requires some management. Central management of the assets is common. The Real Estate Staff is actively involved in any lease, sale, or purchase; but they are not interested in development for non-corporate uses. They can and do occasionally engage in development packaging. A master plan may be put together for a property that has a higher use than its current use. The zoning may even be changed. However, the property is then normally sold to a developer. This model involves minimum risk.

3. Passive Developer Model

The Real Estate Department is generally a line department measured by the profitability of its operation. Land that is excess to the corporation needs is normally the responsibility of the Real Estate Department. They do however acquire land for the express pur-

pose of development. Properties can be packaged in a manner similar to the Active Acquisition/Disposition Model.

In this model one additional step is taken and that is the joint venture. The corporation generally acts as the passive partner in the joint venture by contributing the land. Of course this also means that the bulk of the profits go to the other partner in the venture. The risk of the corporation is somewhat higher, but they can not lose more than the value of the land which is normally not more than 25% of the total value of the project.

4. Active Developer Model

This model involves the most risk and also requires the most experience on the part of the Real Estate Department. The Real Estate Department normally will operate as a subsidiary to the parent company in this model. The subsidiary then takes on the role of sole developer. The corporation will offer excess properties to the subsidiary, but many times they are rejected because of little potential. There is still a need for a Corporate Real Estate Department to manage the Corporate assets. The biggest complaint of Active Developers is that top management has little understanding of the economics of real estate development, and have unrealistic expectations regardless of the timing of a project and the cash flow achievable.

All corporations normally fall into one of these models, but it is possible that a company can be between models. For many years electric utilities were in the role of Passive Acquisition/Disposition and some are still there. There is a trend toward more active management of properties. In my opinion it is not very likely that many electric utilities will move all the way to the Active Developer Model. It is possible however for a good number of them to be Passive Developers. This can generate income and provide a good return on assets that otherwise would not be utilized fully.

In order to manage real estate most effectively, it is necessary to identify properties already owned that may have

potential for development. These can be vacant properties, or improved properties, but they must be considered to have another use that will provide a better return than the present use. In the case of a utility it could be a parcel of land that is vacant and being held for future use. If the land has a highest and best use that is not for a substation site it is a potential site for development. It could also be an office building or a service center which has potential for a higher use such as a hotel or multi-tenant office building. To determine the potential of the property it is necessary to do a Feasibility Study. This study can be done by staff people in the Real Estate Department if they are qualified, or it can be done by a consultant. In either case it is necessary to be innovative with ideas regarding what can be done with the property.

After it has been determined that the property has development potential it must also be determined if there is anything else that is required to put together a development package that will be attractive to a developer. Some of the things that could be required are:

1. Acquisition of additional land
2. Change in zoning
3. Reserve sewer capacity if there are problems in the area with sewer moratoriums

Once the development package is assembled it then must be determined if the land should be sold or leased to the developer or if a joint development should be sought. It is necessary to evaluate the economics of each of these alternatives to determine which will produce the highest return to the utility.

It takes time and effort to put together a development package, but if the property truly has potential the returns will make it all worthwhile. It is also an exciting and fascinating business.

Facilities Management

Another part of Property Management that tends to be overlooked by many electric utilities because they are so oriented to land is the management of their facilities. Office buildings, shops, warehouses, power plants, anywhere people work should be included. If you work for an electric utility, or even if you don't, ask yourself this question. "Do we wait until something is broken before we

fix it, or do we have planned maintenance?" If you wait for something to break before you fix it you are not really doing property management.

A property manager can be assigned to a group of properties, but he should be the sole person responsible for everything going on at these properties. Included in this is:

1. *Renovations* — no renovations should be made unless the property manager approves the concept and the expenditure of funds.

2. *Land acquisition* — if land can be acquired to improve the property it must be approved by the property manager.

3. *Land sales* — if part of the property is no longer needed for its operation the sale must be approved by the property manager.

4. *Maintenance* — maintenance should be planned ahead, but must always be cleared through the property manager.

5. *Space allocations* — any department occupying any of the properties assigned to a property manager must get permission before changing any space occupied.

6. *Security* — security is also the responsibility of the property manager and any changes in security must be approved by the property manager.

7. *Janitorial service* — any requests for new construction from any of the Department Managers must go first to the property manager.

In short the property manager is responsible for everything that happens on the properties assigned. The budget is the control mechanism; therefore planned projects will be included in the budget and unplanned ones may or may not be done depending on the cost and funds available. This is really the most effective and economical method of managing improved properties and it works equally well for facilities that are owned or leased.

The organization is normally centralized but only within a region. Each property manager reports to someone higher within the organization so the ultimate decisions will be made according to what is best for the overall corporation and not what is best for one region or another.

The property manager must have the capability within his organization to do

some economic evaluation. When new facilities are to be constructed the property manager must be able to determine if the best course is to own the facility or lease it. If it is decided to lease, then an evaluation must be made to either lease from a developer who will build to your specifications or to build the facility and enter into a sale and leaseback agreement.

Electric utilities are no different than any other corporation regarding property management. Property management, if done properly, is as near to being universal in the real estate field as you will find. The functions performed are the same no matter whether you are doing them for a chemical company, a railroad, or an electric utility.

Property management touches almost all aspects of commercial real estate from acquisition to leasing and even sale and leaseback. It is fascinating business, and it can be very profitable for your corporation. Even the Facilities Management portion of the business is profitable because it is so cost effective. Properties that are managed effectively are more efficient and therefore costs of operation are reduced.

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Every member will
receive a ballot in
late August.**

**The issue is
political activity.**

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ballot — we need to
hear from every
member.**