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Municipal Real Estate deployed as a capital asset

Rianne H.A.J.A. Appel-Meulenbroek, S.J.E. Maussen, N. de Bis, B.G. Verkerk

*Eindhoven University of Technology
Faculty of Architecture, Building and Planning
Department of Urban Planning and Real Estate Management
P.O. Box 513
5600 MB Eindhoven
The Netherlands*

Phone +31-402472092

Fax +31-402738488

E-mail: h.a.j.a.appel@bwk.tue.nl

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Abstract

The aim of this study is to introduce the principles of Corporate Real Estate Management (CREM) within the municipal organization. It is presumed that, looking at the private sector's accomplishments in this field, these principles will allow a city council to deploy their real estate in a more strategic manner. In this study a model has been created for implementing so-called Municipal Real Estate Management (MREM) within the municipal organization on the desired level and adjusting the municipal real estate portfolio accordingly. This introduction of MREM will contribute to offering adequate accommodation to the different consumers, which heightens customer satisfaction. At the same time, it will add to the company result, balancing costs and benefits and delivering added value through a better control of risks and creating economies of scale.

Introduction

In the private sector, organizations more and more often look upon their real estate as a capital asset. Local governments, although showing great attention for space (industrial sites, inner-city areas), stay behind in this development concerning “their own” space. Despite the enormous size of their real estate portfolio and the growing complexity of the questions concerning accommodation, they mostly do not manage their real estate in a strategic way. With the introduction of Municipal Real Estate Management, based on the principals of Corporate Real Estate Management, a more strategic management can be deployed.

Local governments in the Netherlands have control of a substantial amount of real estate. This does not only concern city halls and council offices, but also schools, sports halls, museums, community centres and monuments. Management is aimed mostly on the operational accommodation tasks and spread over several services and departments. Consequences are that local governments have little insight in the size or performance of their real estate portfolio and do not know if their users are served in an optimal way.

Estimates of the total municipal real estate stock in the Netherlands vary from 22 to 39 million m² gross floor area with a total replacement value of €29 to €50 billion. Comparing these figures with the joint possession of all members of IVBN (the Association of Institutional property investors in The Netherlands)¹, something over € 40 billion, the strategic tasks are comparable.

Current situation

An estimate of the total municipal real estate stock in the Netherlands, based on the average amount of m² gfa per size-group², comes to 25 million m² gfa (see table 1). Except for offices (about 23% of total stock if 10.000-100.000 res. and 6% if >100.000 res.), it is hard to make a distinction between the different categories (schools, social-cultural, sport accommodations). Data are hard to obtain, because real estate is spread over several departments.

Table 1: total municipal real estate stock

Category (residents)	Average amount of real estate per municipality (m ² gfa)	Number of municipalities	Total real estate per category (1000 m ² gfa)
0-10.000	4.000	89 (18%)	356 (1%)
10.001-25.000	21.000	223 (45%)	4.683 (19%)
25.001-50.000	40.000	114 (23%)	4.560 (18%)
50.001-100.000	140.000	40 (8%)	5.600 (22%)
100.001-250.000	300.000	25 (5%)	7.500 (30%)
250.001 >	450.000	5 (1%)	2.250 (10%)
total		496	24.949

Small towns and cities (< 50.000 res.) constitute 86% of the total number of municipalities, but they own only 38% of the total amount of real estate. Municipalities with 10.001-25.000 even stand for almost half of the towns and cities in the Netherlands (45%), but own only 19% of the total amount of real estate. Cities with 100.001-250.000 residents, on the other hand, stand for the largest percentage of real estate (30%), while they only represent 5% of all municipalities. And the 5 largest cities together own 10% of the total real estate portfolio. A possible explanation is, that large cities, relatively, need to provide for more social facilities and therefore need more real estate. Another explanation might be, that larger cities have better means for real estate management and therefore have a better view of their portfolio.

Figure 1 displays the structure of a Dutch municipal organization. It shows that the different services/departments in practice are usually responsible for their own real estate. This counts for both the accommodation for the own organization (council offices, city halls, municipal wharfs and shops) as for fulfilling the need for social facilities (educational accommodations, social-cultural accommodations, other). Earlier study³ showed that over 62% of municipalities have a decentralized management of their real estate. The interviews and questionnaire recently spread

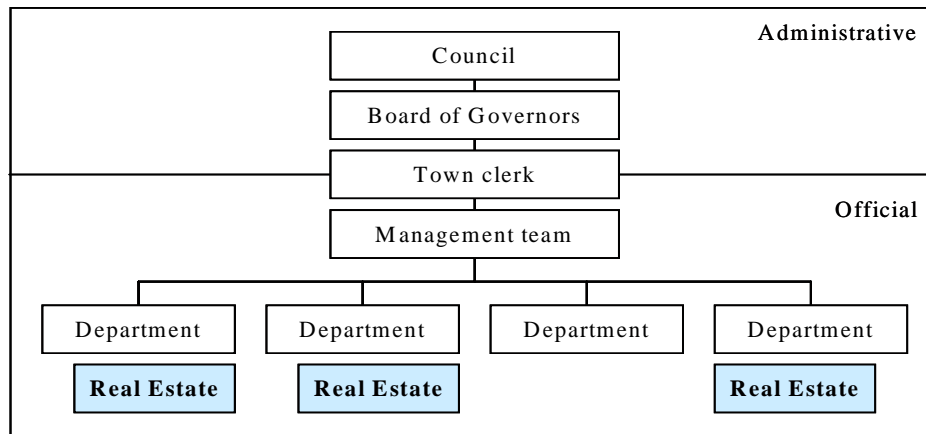
¹ (www.ivbn.nl) members include pension funds, insurance companies and share funds. Together these members represent approx. 90% of total Dutch institutional property capital.

² 110 municipalities, split over 6 size-groups, have received a questionnaire; response was 23%

³ Kohnstamm e.a. (1995) Management in municipal organisations

among employees of municipalities confirmed this, with 72% of the municipalities indicating that at least three different departments are involved with real estate management tasks (e.g. Management and maintenance, Ground affairs, Education and well-being, Sport recreation and culture, Finance).

Figure 1: municipal organization



Results also showed that real estate plays a minor role in government policy and that a policy for real estate is lacking. Most municipalities do not have a supporting real estate department and the municipal administration hardly shows any attention for real estate unless in case of excess situations⁴. The fragmentation leads to poor (internal) communication and the unavailability of sufficient data. The interviews also showed that data systems are not linked.

Lack of clarity about main data of the municipal real estate stock (composition, maintenance condition, tenants with corresponding number of m²'s) combined with insufficient real estate knowledge leads to deficits in for example maintenance. The growing complexity of the questions concerning real estate, both spatially and financially as for the number of parties involved, demands professionalism of the organization. Complexity combined with scarcity of means leads to tension, which pleads for a central, cost efficient and strategic municipal policy.

The added value of municipal real estate

Over 80% of the respondents indicated finding real estate important to very important as a mean to make their policy concrete. Real estate serves as support of social and dependent organizations like community work, shelter, education etc.. At the same time, it offers a council the possibility for steering spatial processes and with that the quality of their spatial surroundings (e.g. restructuring area). By owning the real estate used to accommodate a community centre, sports hall or swimming pool, the council can influence the further development of an area.

Other aspects of added value ascribed to real estate are⁵:

1. Means for controlling implementation of changes
Real estate can be used as leverage in reorganizations, mergers, cultural

⁴ Van Spaandonk (2001) Activities, processes, relations and bottlenecks

⁵ Van Hettema e.a. (2001), Meulenberg e.a. (1997), Konickx (1998), Wildeboer e.a. (2001), Elfrink e.a. (1993), Rijkenberg (2001), Van Langen (1995), Vijverberg (1998)

changes etc. De construction of a new city hall can bring organizations together.

2. Contribution to image
3. Attracting personnel
4. Efficient use of space/flexibility
5. Financial influence

In many organizations real estate is the second largest cost item. Through sale/lease-back constructions, re-development and outsourcing it might be possible to release money.

6. Social value

Real estate has cultural and architectural values and has a large influence on its surroundings. Often, municipal real estate has an initial role in area development.

7. Risk control

Risks can be controlled by preventing inflexibility in real estate supply. Also the location can influence the potential for a new destination of a site.

To achieve more of these added value components it is necessary to deploy real estate in a more strategic manner. Many private companies nowadays try to do this by practicing corporate real estate management (CREM). With CREM a central real estate organization is responsible for the real estate stock and real estate is deployed to support the primary process of the user. The CREM-organization operates in a tension field of three interests. First, the strategic interest which adjusts the real estate to the organisation's strategy. Second, the functional interest which deploys the real estate to support the primary process of the user. Finally, the financial interest can be mentioned, for which real estate must be deployed for as low costs as possible (cost effective rent) and is used to generate financial means. The goal of the CREM-organization is to find an optimal balance between these interests.

Already in 1993 five different levels were distinguished within CREM⁶, called: Business strategist, Entrepreneur, Dealmaker, Controller and Taskmaster. The taskmaster deals with the operational maintenance of buildings (maintenance plans). The Controller performs also tasks to obtain insight in for example the accommodation costs. The dealmaker makes the step towards actively solving CRE-problems for the users (market analysis, post occupancy evaluation). The entrepreneur has the extra task of dealing with real estate policy and determining accommodation scenario's. The business strategist also looks at the overall policy and makes sure that accommodation is integrated with a company's strategy.

Turn to Municipal real estate management (MREM)

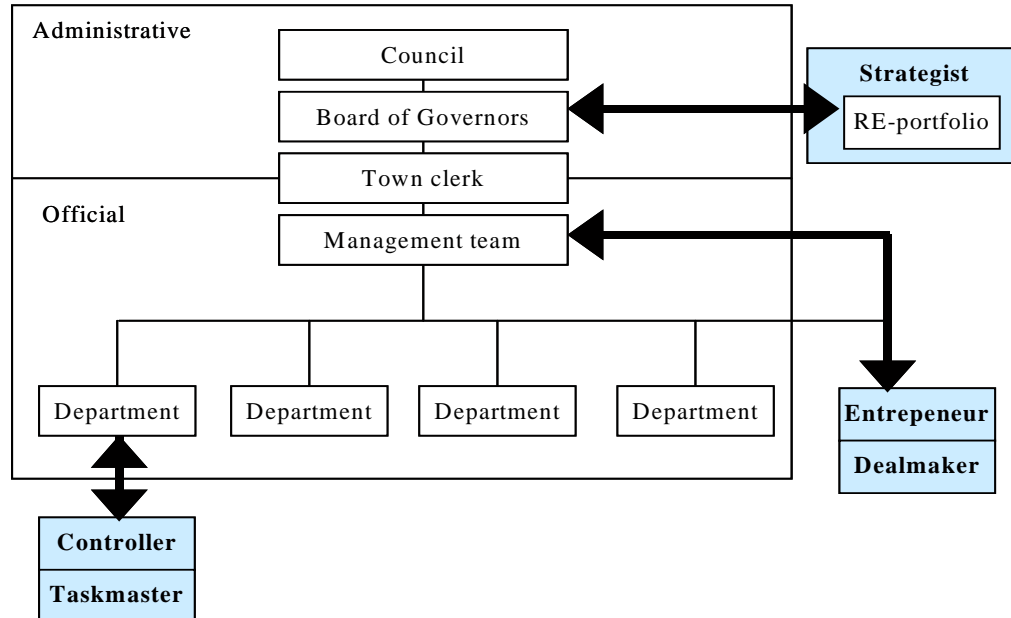
Following the private parties, the national Dutch Government Buildings Agency started implementing CREM in 1999 as one of the first public parties in the Netherlands. The two main reasons behind this decision were financial deficits and the need to deliver more decisive and customer-oriented services. Now, also some city councils are trying to implement the principles of CREM.

Depending on the goals of the council, the desired MREM-level can be determined. Each level is positioned differently in the municipal organisation and receives

⁶ M. Joroff e.a. (1993) CRE 2000 phase one

different input (see figure 2). At the level of the Taskmaster and Controller the input takes place through the departments, which are managed by the management team. The MREM-organisation is part of a department and is being managed by the director of the department in question.

Figure 2: Relationship MREM-levels in municipal organization

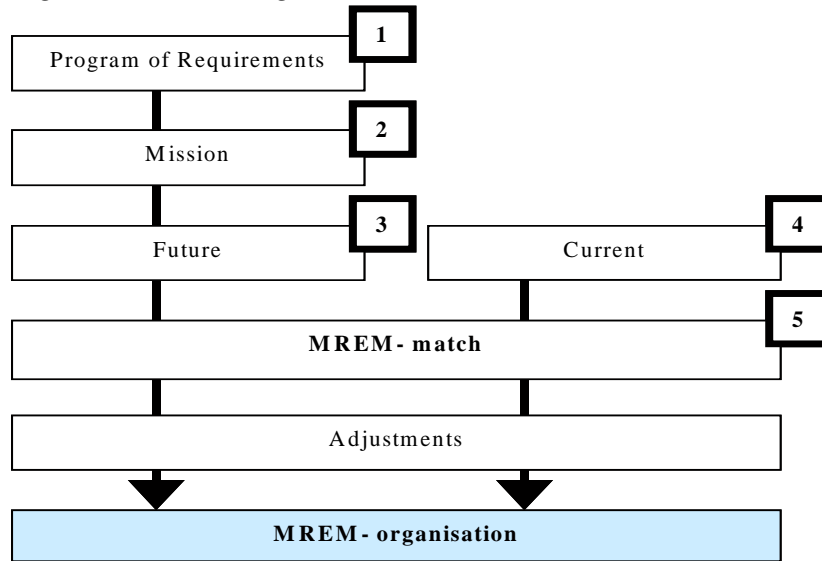


In case of the Entrepreneur and Dealmaker, the real estate organisation forms a separate department. The management team, consisting of the Town clerk and the directors of the different departments (so also a director Real Estate), forms the directorate of the Civil Service. They are responsible for executing the municipal policy, through which MREM is informed of the primary process and the organization.

MREM at the level of the strategist can influence policy from a higher level and takes place on the Board of Governors. The Board of Governors determines the municipal policy, which, after the council approves, can be implemented by the Civil Service.

A method has been set up for introducing MREM within the municipal organisation, consisting of the following steps (see figure 3):

Figure 3: Introducing MREM



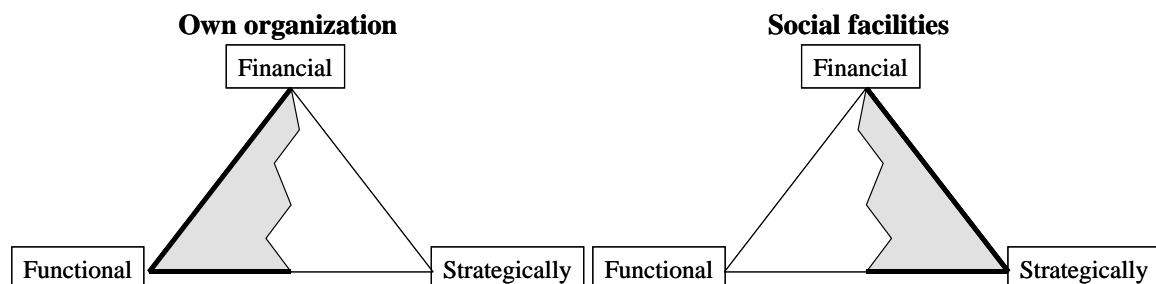
1. Formulating a Program of Requirements (PoR) consisting of limiting conditions, starting points and goals.
2. Based on the PoR, the mission, vision and goals of the MREM-organisation are determined.
3. Based on step 2 and the advantages per MREM-level, the desired MREM-level is chosen.
4. The current situation is analysed, based on strategy, organization structure and tasks/products.
5. Trough matching the current and future situation the necessary adjustments come forward.

After making the adjustments an optimal MREM-organisation has been formed and can start looking after the tasks that have been appointed to them.

Composition of the Municipal real estate supply

As mentioned, the goal of the CREM-organization is to find an optimal balance between the three interests (financial, functional and strategically). The weight differs, depending on the type of municipal real estate (see figure 4). It turns out, that the weight for social facilities lies heavier on strategic interests, while the real estate for the own organization mainly needs to support the primary process and thus the functional interests.

Figure 4: weight of interests



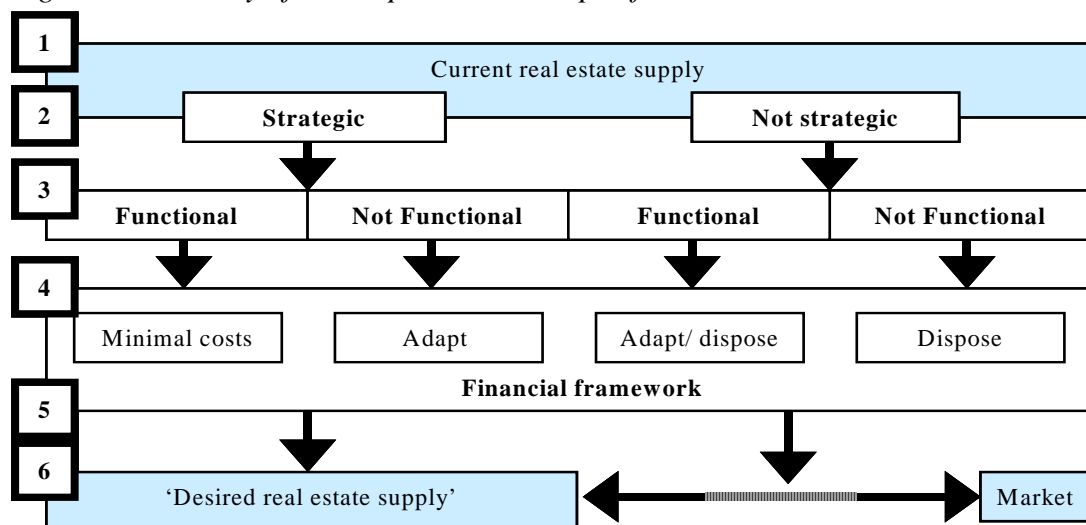
These interests are of importance for the composition of the demanded municipal real estate portfolio. Figure 5 describes how to determine in six steps if a property belongs within the municipal portfolio or not. First, it is necessary to determine if the property fulfils a social need or supports the own organization. Then, you evaluate if the property has a strategic role and if it is functional or not. Applying the different portfolio-strategies in step 4 needs to take place within the financial framework, to assure the feasibility of the outcomes. If feasible, the strategy can be implemented to arrive at the desired real estate supply.

Strategic property will always be maintained and if functional, no adaptations are necessary, although it is possible to strive for a further minimising of costs. Strategic property that is not functional needs to be adapted within the financial framework. For non-strategic property that is still functional, several possibilities exist:

- a) In case of property for the purpose of social facilities, it needs to be disposed of (since it does not fulfil a social need if it is not strategic) or adapted for use by the own organization.
- b) In case of property for the purpose of the own organization, it can be maintained (since it is functional), but disposal or adaptation within the financial framework may lead to savings and revenues.

Non-strategic and non-functional properties need to be disposed of. These objects are not usable for the organization and can be demolished, redeveloped or sold, depending on the financial framework.

Figure 5: inventory of municipal real estate portfolio



Conclusions

City councils mainly execute the operational accommodation tasks. Strategic thinking is often lacking. The municipal real estate is split up over the organization, with the consequence that there is hardly any insight in the functioning of the real estate supply and the stock is hardly ever regarded on portfolio level. Executing a central, cost-efficient and strategic policy is therefore impossible.

Through applying MREM within municipalities a professional central real estate organization arises. By doing so, a more strategic deployment of real estate is possible and bottlenecks in managing the real estate portfolio can be dealt with. Managing the real estate stock on a central level creates insight in supply and allows a better

utilization of real estate stock, thus delivering an optimal contribution to the primary process of the different users.

The introduction of MREM contributes to offering adequate accommodation to the different consumers, which heightens customer satisfaction. At the same time, it adds to the company result, balancing costs and benefits and delivering added value through a better control of risks and creating economies of scale. The experience within the Dutch city of Enschede shows us, that the recently started MREM-department already yields its benefits. Also the city of Eindhoven is reshaping its MREM, showing great similarities with the principles of CREM.