

**Report to
Rapport au:**

**Finance and Economic Development Committee
Comité des finances et du développement économique
5 October 2021 / 5 octobre 2021**

**and Council
et au Conseil
13 October 2021 / 13 octobre 2021**

**Submitted on September 22, 2021
Soumis le 22 septembre 2021**

**Submitted by
Soumis par:
Derrick Moodie, Director / Directeur
Corporate Real Estate Office / Bureau des biens immobiliers municipal, Planning,
Infrastructure and Economic Development / Services de la planification, de
l'infrastructure et du développement économique**

**Contact Person
Personne ressource:
Peter Radke
Manager, Realty Initiatives and Development Branch/gestionnaire, Initiatives et
Mise en valeur en immobilier
613-580-2424, 12551, Peter.Radke@ottawa.ca**

Ward: SOMERSET (14)

File Number: ACS2021-PIE-CRO-0015

**SUBJECT: Lease Renewal – 370 Catherine Street – Employment and Social
Services Central Office**

**OBJET: Renouvellement de bail – 370, rue Catherine – Bureau des Services
sociaux et d'emploi du secteur Centre**

REPORT RECOMMENDATIONS

That the Finance and Economic Development Committee recommend that Council:

- 1. Approve the renewal of a lease between City of Ottawa and 370 Catherine Street Operating Limited Partnership for 5,541.76 square metres of office space at 370 Catherine Street for a term of 10 years commencing November 1, 2021 and expiring on October 31, 2031 along with two early termination options, , for a total base rent consideration of \$4,220,641 plus HST for the initial five years of the 10-year term;**
- 2. Delegate authority to Director, Corporate Real Estate Office to finalize and execute the lease agreement and to negotiate market rent for the remaining five years of the 10-year term in accordance with the term's conditions detailed in this report.**

RECOMMANDATIONS DU RAPPORT

Que le Comité des finances et du développement économique recommande au Conseil municipal :

- 1. d'approuver le renouvellement de l'entente de location entre la Ville d'Ottawa et le 370 Catherine Street Operating Limited Partnership pour un espace de bureau de 5 541,76 mètres carrés, situé au 370, rue Catherine, pour une durée de dix ans, soit du 1^{er} novembre 2021 au 31 octobre 2031, comprenant deux options de résiliation anticipée du bail, d'un montant total pour le loyer de base de 4 220 641 \$, TVH en sus, pour les cinq premières années de la location de dix ans;**
- 2. de déléguer au directeur du Bureau des biens immobiliers municipaux le pouvoir de conclure et d'exécuter l'entente de location et de négocier le loyer à la valeur marchande pour les cinq autres années de la location de dix ans, conformément aux conditions de la location détaillées dans le présent rapport.**

BACKGROUND

Ottawa's Employment and Social Services (ESS) Branch has the responsibility for the delivery of the Ontario Works program under contract with the Province of Ontario and includes financial assistance and employment services. ESS clients are typically those

with the most barriers to employment and other services and many are single parents and new Canadians. These programs are delivered at four centres geographically spread across the City to facilitate access to the key social supports, which include Child Care subsidy, Home Support Services, and the Domiciliary Hostel program. The four centres are located at 370 Catherine Street (Central); 2339 Ogilvie Road (East); 100 Constellation (West); and 2020 Walkley Road (South).

The Community and Social Services Department (CSSD) has been located in Ottawa's central area since 1995 when the former Regional Municipality of Ottawa-Carleton approved a five-year lease with Three Seventy Catherine Limited for office space in a portion of the top two levels of a three-level office building at 370 Catherine Street together with 80 outside parking stalls. An Amending Agreement the following year added additional floorspace to the leased premises, which incorporated the entire top two floors of the building. The CSSD continued operating its Central District Office from the top two floors, Suites 200 and 300, providing a wide range of integrated community and social service supports to residents of Ottawa. That lease expired on October 17, 2001.

During that same period, the CSSD was operating its Employment Resource Centre at 880 Wellington Street. However, Regional Council at its meeting of June 14, 2000 received a confidential report regarding the Strategy for Social Services Delivery Sites and the strategic direction for the Central District. That report supported the co-location and integration of the Employment Resource Centre at 880 Wellington Street with the Central District Office at 370 Catherine Street. The lease at that location was due for renewal on September 30, 2000. When the remaining two floors at 370 Catherine Street became vacant, staff saw an opportunity to consolidate its operations within the Central area. As a first step in establishing a strategic direction, operations would be moved from 880 Wellington Street to 370 Catherine Street, which would become the social services delivery site for the Central District.

On August 28, 2000 the Ottawa Transition Board approved the First Lease Amending Agreement with Three Seventy Catherine Limited, adding 2,783 square metres (m²) of new premises to the existing leased premises by including the building's remaining ground level Suite 100 and lower-level Suite B100. The agreement provided availability of 110 ground level parking stalls together with an option to renew the lease of the new leased premises for one additional term of five-years. The original lease of upper two levels Suites 200 and 300 was due to terminate on October 17, 2001, with an option to renew for an additional term of five years. Therefore, with a view to bringing termination

dates into conformity, the term of the New Premises, was set at six years and one month, terminating on October 31, 2006.

Pursuant to report [ACS2002-CRS-RPR-0011](#), Council approved renewing the lease for Suites 200 and 300 for a period of five years and two weeks, commencing October 18, 2001 and terminating on October 18, 2006. This resulted in the lease of the upper two levels of the building being co-terminus with the lease of the lower two levels of floorspace. The renewal included 22 additional on-site parking spaces and an option to renew for a further term of five years.

On February 25, 2003 the City entered into a Lease Amending Agreement with Oxford Properties Group Inc., formerly Three Seventy Catherine Limited, confirming rental rates for Suites 100 and B100 and amending rental rates for Suites 200 and 300.

Pursuant to report [ACS2005-CRS-RPM-0032](#), Council authorized staff to renew the lease at 370 Catherine Street for all four levels in the building, involving 5,541.76 m² of office floorspace, for a term of 10 years commencing November 1, 2006 and terminating October 31, 2016. Council also approved designating 370 Catherine Street as a Municipal Capital Facility (MCF) for the purpose of establishing realty tax exemption under the Municipal Act due to the municipal use of the facility (MCF By-law 2006-386, registered 18 October 2006 as Instrument OC651343). Council's direction was subsequently formalized by a Second Lease Amending Agreement that provided the City with 44 on-site parking spaces and 96 off-site parking spaces together with options to extend the lease term for either five years or 10 years.

Pursuant to report [ACS2016-PAI-REP-0014](#), Council again authorized staff to renew the lease at 370 Catherine Street for all four levels in the building, involving 5,541.76 m² of office floorspace, for a term of five years commencing November 1, 2016 and terminating on October 31, 2021. Council's direction was subsequently formalized by Third Lease Amending Agreement.

DISCUSSION

OPTIONS EXPLORED

ESS delivers services at four centres across the City. In negotiating prior lease renewals for three of these centres, namely, 2020 Walkley Road, 2339 Ogilvie Road and 370 Catherine Street, each of the terms were positioned to expire in 2021. This afforded ESS staff the opportunity to explore service delivery planning options and related renegotiation of lease agreements. With uncertainty created by the impacts of

COVID-19 and future provincial changes to the client's service delivery model, ESS requested the Corporate Real Estate Office (CREO) to undertake a strategic approach to re-negotiating lease agreements to allow for early termination clauses at specific intervals and cost savings, where possible.

ESS staff determined it would be in the City's best interest to continue operations in the two existing locations and to renew both leases, but with newly negotiated termination agreements. The lease for 2020 Walkley Road has been renewed and will expire on April 30, 2024. The lease for 2339 Ogilvie Road has been renewed and will expire on July 14, 2031, subject to provision for early termination after three and a half years and eight and half years. The lease for 370 Catherine Street expires November 2021 and is herein being recommended for renewal.

RENEWAL

The current lease between City of Ottawa and 370 Catherine Street Operating Limited Partnership identifies the leased premises to be Suites 100, 200, and 300 and lower-level Suite B100 and 50 on-site parking spaces located at 370 Catherine Street as well as 96 off-site unreserved parking spaces located at 350-360 Catherine Street for building clients and staff. Accommodations Planning has confirmed the leased premises have a combined total rentable area of 5,541.76 m². The lease is due to terminate on October 31, 2021.

In accordance with terms of the Third Lease Amending Agreement and in consultation with ESS, CREO provided written notice to the Landlord that the City was exercising its option to extend the term of the lease for a further period to commence on November 1, 2021, subject to approval by Ottawa City Council. Rather than continuing to amend a dated original lease and multiple subsequent amendments, both parties agreed to recognize the renewal by way of a new lease agreement moving forward.

TERM OF LEASE

CREO sent a non-binding proposal to the Landlord, focusing on term of lease requirements provided by ESS. That proposal included a five-year lease renewal with an option to early terminate, allowing the City to vacate the leased premises after a period of three years. The proposal also included a continuation of both on-site and off-site parking agreements together with one further option to extend the lease for an additional term of five years.

Since a five-year term with an early termination option was not seen to be conducive to the Landlord, the Landlord responded by proposing a renewal term of 10 years, having two early termination options, allowing the City to vacate the leased premises after periods of four years and nine years.

The parties subsequently agreed to a term of 10 years, with two early termination options, each having a 12 months' notice period. The first termination option is to be exercised at any time between April 1, 2024 and May 31, 2024 and the second to be exercised at anytime between April 1, 2029 and May 31, 2029. These options would provide the City the ability to vacate the leased premises after periods of three and a half years and seven and a half years and would provide flexibility for City office accommodations changes that may result from a post-pandemic workplace as well as future office consolidation strategies. The parties also agreed to one further option to extend the lease for an additional term of five years. ESS agreed with this settlement.

EXISTING RENT

In accordance with Section 4 in the Third Lease Amending Agreement dated June 7, 2016, the annual rent payable plus estimated recoverable operating expenses for the leased premises during the final term of the existing lease, November 1, 2020 to October 31, 2021, is \$1,777,284 as follows:

	Area: Square Meters	Unit Rent / square meter	Total
Above Grade Suites 100, 200, 300	4,166.19	\$ 172.23	\$ 717,543
Below Grade Suite B100	1,375.75	\$ 69.97	\$ 96,261
On-Site Parking - 50 spaces @ \$85.00/space/month			\$ 51,000
Off-Site Parking - 96 spaces @ \$115.00/space/month			\$ 132,480
Total Base Rent - Term year ending October 31, 2021			\$ 997,284
Operating Cost - Prior four year average			\$ 780,000
Total Estimated Lease Cost - Term year ending October 31, 2021			\$ 1,777,284

PROPOSED RENT

In accordance with the City's Leasing Procedures, an appraisal report estimating the subject property's current market rent must be completed. When the estimated market rent for the term of the lease is greater than \$1,000,000, two reports are required with at least one being prepared by an independent real estate professional. In this case, both the City and the Landlord obtained rental appraisal reports from independent real estate professionals.

An appraisal provided to the Landlord by an accredited appraisal firm estimated the Net Effective Rent per square foot for above grade Suites 100, 200 and 300 should increase incrementally from \$166.84 to \$177.61 per m² from years one to five and to \$191.07 for years six to 10. Net Effective Rent for below grade Suite B100 should increase incrementally from \$64.59 to \$75.35 per m² from years one to five and to \$83.42 for years six to 10. Gross Effective Rent for the above grade Suites 100, 200 and 300 for the first year of the renewal term was estimated to be \$344.46 per m², which estimates Operating Costs of \$177.61 per m² for the above grade Suites 100, 200 and 300 for the first year of the renewal term. Parking rate for both on-site and off-site spaces from years one to five was estimated at \$125 per space per month and \$150 per space per month from years six to 10.

An external appraisal provided to the City by an accredited appraisal firm estimated the Gross Effective Rental Rate as of October 31, 2021 to be between \$306.78 and \$322.93 per m². Based on information provided by the Landlord, operating costs for the year 2021 are estimated to be approximately \$182.99 per m². As a result, the Net Effective Rental Rate as of October 31, 2021 for above grade Suites 100, 200 and 300 would be in the range of \$123.79 to \$139.93 per m² and \$64.59 per m² for the below grade Suite B100.

BASE RENT NEGOTIATIONS

Annual rental payments for 370 Catherine Street involve two fundamental components - base rent to occupy the leased premises and operating costs to maintain the leased premises. In this case, the lease is fully net to the Landlord and the leased premises include the entire building. Accordingly, the City is responsible to pay base rent for all premises within the building and all operating costs incurred by the Landlord in maintaining the entire property. Leased premises for above grade Suites 100, 200 and 300 contain a total area of 4,166.19 m². Leased premises for below grade Suite B100 contain a total area of 1,375.57 m² for a total office area of 5,541.76 m².

CREO initiated rental negotiations by proposing a base rent at the lower end of the range set out in the City's appraisal, which recognized the high level of uncertainty of the current and future office market in estimating office rental rates. This was followed by appraisal reconciliation discussions with the Landlord, which respected the ESS requirement for early lease termination that, while very beneficial to the City, added significant increased risk to the Landlord.

Although CREO agreed to the Landlord's request for a 10-year lease, subject to early termination options, it dismissed the veracity and relevance of rental cost estimates

proposed by the Landlord that extended over the entire term due to the uncertainty of the future office market. Accordingly, CREO proposed establishing annual rental rates during the initial five years of the 10-year term with rental rates over the remaining five years of the 10-year term to be renegotiated based on the then prevailing market conditions. As indicated in recommendation two of this report, delegated authority is being sought for the Director of CREO to negotiate market rent for those remaining five years of the 10-year term.

The parties ultimately reconciled a base rental rate of \$156.08 per m² for above grade Suites 100, 200 and 300, which essentially split the difference between the lower end of the rental range set out in the Landlords appraisal and the upper end of the range set out in the City's appraisal. Both parties agreed to have the \$156.08 rate fixed for five years, which is a reduction of \$16.15 per m² from the currently paid rent. Also, the parties agreed to fix the base rent for below grade Suite B100 at \$69.97 per m² for the same five-year period.

Both parties agreed to a parking space rate of \$125 per space per month as a gross rate as supported by both independent appraisals and made further deductions to reflect the desire of the Landlord to create a net rate reflective of the anticipated cost recoveries. Ultimately, a net rate of \$83 per space per month fixed for the first five-years of the term was negotiated. The Landlord also agreed to reduce the number of off-site, unreserved parking spaces from 96 to 48 reflective of ESS desire to reduce the number of parking stalls. For the remaining 48 spaces the Landlord will install and manage, at its cost, a pay-for-use arrangement.

OPERATING COSTS

The subject lease is fully net to the Landlord and all operating costs associated with the building and parking lot are recoverable from the City as additional costs as is standard for office leases. Actual operating costs provided by the Landlord over the period 2016 to 2020 average \$781,148 or \$187.51 per m². As part of entering into a new lease, the Landlord has agreed to a full building operating efficiency review of the current building expenses to ensure that the building remains competitive to comparable office building operating expenses. For the purposes of estimating an operating budget and total gross consideration for the first five-years of the term, the current average recoverable cost stated above is estimated for year one of this lease, with years two to five escalated at a 2 per cent inflationary rate.

RECONCILED RENT

The parties have reconciled annual base rental payments, operating costs and parking costs for the initial five years of the 10-year lease as follows:

	Area: Square Meters	Unit Rent/ square meter	Year 1 Total	5-Year Total Estimate
Above Grade Suites 100, 200, 300	4,166.19	\$ 156.08	\$ 650,259	\$ 3,251,295
Below Grade Suite B100	1,375.75	\$ 69.97	\$ 96,261	\$ 481,306
On/off-Site Parking - 98 spaces @ \$83.00/space/month			\$ 97,608	\$ 488,040
Total Base Rent			\$ 844,128	\$ 4,220,641
Estimated Operating Cost			\$ 780,000	\$ 4,059,151
Total Base Rent Plus Operating Cost			\$ 1,624,128	\$ 8,279,792

CONCLUSION

Employment and Social Services (ESS) Branch and Corporate Real Estate Office have reviewed existing ESS locations and service demands, consolidation opportunities within existing facilities and alternative office sites on the open market and have determined it is preferred to extend the tenancy at 370 Catherine Street.

The COVID pandemic has created uncertainty within the office rental market, and it is noted that tenants have been reluctant to commit to longer term lease agreements. Typically, Landlords expect tenants to agree to a standard five-year term, but with shorter terms the Landlord will expect a premium. In this case, the Landlord has obtained a 10-year term that will be conducive to the Landlords business desires. However, without committing to a premium rental arrangement the City has secured two early termination options, which will allow it to vacate the leased premises after periods of three and a half years and seven and a half years. This is an important aspect of the lease agreement as it will provide flexibility for City office accommodations changes that may result from a post-pandemic workplace as well as future office consolidation strategies.

Total base rent consideration for the initial five-years of the 10-year term is proposed to be \$4,220,641 and building operating cost is estimated to be \$4,059,151, plus HST. This proposal reflects an anticipated savings to the City of \$153,156 per annum based on the current expiring lease base rent and parking costs. The Community and Social Services Department has accepted the reconciled settlement, which is in keeping with the changing market conditions supported by two rental appraisals prepared by two independent, accredited appraisal firms.

In light of the foregoing considerations, staff recommend that Council delegate authority to Director, Corporate Real Estate Office to finalize and execute the lease renewal agreement in accordance with the terms and conditions detailed in this report.

RURAL IMPLICATIONS

There are no rural implications associated with the recommendation of this report.

CONSULTATION

Corporate Real Estate Office consulted with ESS and Legal Services in the completion of this lease renewal.

COMMENTS BY THE WARD COUNCILLOR

Ward 14 - Councillor Catherine McKenny – Councillor McKenny is aware of this report.

LEGAL IMPLICATIONS

There are no legal impediments to implementing the recommendations in this report.

RISK MANAGEMENT IMPLICATIONS

There are no risk implications associated with the recommendations of this report.

ASSET MANAGEMENT IMPLICATIONS

There are no asset management implications associated with the recommendations of this report.

FINANCIAL IMPLICATIONS

Base rent for the initial five-years of the 10-year term is \$4,220,641 and building operating cost is estimated to be \$4,059,151, plus HST. This reflects an anticipated savings to the City of \$153,156 per year. Rental rates over the five remaining years of the lease are to be renegotiated at the then prevailing market conditions. Funds for this renewal are available within existing budgets.

ACCESSIBILITY IMPACTS

There are no accessibility impacts associated with the recommendations of this report.

ENVIRONMENTAL IMPLICATIONS

There are no environmental implications associated with this report.

TERM OF COUNCIL PRIORITIES

This report's recommendation supports the following strategic priorities of City Council:

- Financial Responsibility (FS): Practice prudent fiscal management of existing resources and make sound long-term choices that allow City programs and services to be sustainable.
- Healthy and Caring Communities (HC): Help all residents and visitors enjoy a good quality of life and a sense of community well-being by providing healthy, safe, secure, accessible and inclusive places and services.

DISPOSITION

Upon approval by Council, Corporate Real Estate Office, in consultation with Legal Services will finalize and execute the lease renewal agreement in accordance with the terms and conditions detailed in this report.