

Jerry Alexander took an unloved building in his local community and transformed it into a business hub and restaurant. But that's not all, this property had an interesting past ...

JAIL HOUSE SENTENCED TO BECOME A CMO INVESTMENT

Interview & words:
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BACKGROUND

Like many, Jerry started his career in property with BTLs back in the early 2000s. He moved on to undertake some refurbishments and developments, but quickly discovered that they didn't generate enough money for him. He needed to find bigger deals.

After a lot of networking and searching, he found a small office building comprising 27 units. He completed the purchase and subdivided it into 36 different sized serviced offices.

He has since continued to add large commercial premises to his portfolio.

Although I didn't seek to do commercial investment," Jerry says, "it's purely all we do now.

His offering includes offices, warehouse units, storage and some leisure space. All of his buildings are multi-lets, most of which are large enough to have their own on-site staff. As a result of his successful strategy, he has coined the term CMO – commercial multiple occupancy.



THE PROJECT

This property was the first historical building that Jerry had worked on. It was near to his home and the local authority had placed it for sale on the open market. Although he usually prefers to buy off-market, Jerry submitted a bid regardless. Out of five bids, theirs was accepted.

Built in 1826, the property consists of three distinct areas: a jail, a mortuary and an old courtroom. At the back of the building was an area which had been used as the jail yard. Its original purpose was to conduct general court proceedings and a county holding area for those who were tried and convicted before being transferred to another prison. After only 20 or 30 years, they stopped using it as a jail, but continued using the court into the late 20th century. For 150 years, the local authority weren't quite sure what to do with the jail. Since then, it has had several uses, but nothing that sustained. However, the benefit of remaining in public ownership meant that the structure of the building had been kept in good condition with good fire casing and alarm systems.

It had been vacant for three years prior to Jerry purchasing it, after being used as offices for the local authority. Although it was the oldest property he had worked on, it wasn't that different to his previous projects. He knew a commercial multi-let would work well in the building. The bank agreed and, as they had a good record, secured funding for the purchase and development.

"But of course, you don't know what you'll find when you start lifting up the floorboards ..."



21-25 HIGH STREET KINROSS

Type of property	Commercial Multiple Occupancy (CMO)
Relevant history for the property	The property was originally built in 1826 and formed the County Court, Prison, Mortuary and Jail yard.
Strategy for this property	Fully redevelop into a CMO, build restaurant space extension and hold for the long term.
Purchase price	£181,000 purchase cost. This is the only building we have secured through a bidding process. We were one of five bids.
Open market value	N/A
Purchase/ Acquisition costs	£186,000 (legals £5K)
Funding method(s)	Bank debt £250K. Plus £200K JV loan.
Deposit paid	£0
Amount of funding	£250,000 Bank . £200K JV loan
Borrowing rate(s)	1.75% over bank of England base rate for bank debt on Cap & int 20 year repayment profile. 6% on JV loan
Monthly mortgage/ funding payment	£1,416 + £1,000
Total money in	£450,000
Personal money in	£0 (Albeit with leverage against other property held)

THE BUYING PROCESS

There was a lot of interest in the property, so Jerry and his team tried to work out how many other people were planning on submitting a bid, and for how much. The sellers stipulated a closing date of 24th June 2013 for best offers.

Part of the submission process was to outline what each bidder wanted to do with the building. After all offers were

received, the vendors chose what they felt was the best bid.

The biggest challenge in the buying process was to generate a valuation on the building. Most valuers based the price by looking at what the property was currently worth as a commercial letting in the current market, minus all costs.

THE STATE OF THE BUILDING

As the building services had not been upgraded for many years, most had to be replaced, including the plumbing, electrics and heating. Outside, a small part of the roof had some water damage, which needed to be repaired.

Inside, the walls needed stripping back to expose the stonework after years of being covered up. Most of the original furniture and features had gone from the courtroom, however they did find some large original picture frames and fireplaces, one of which still had the Georgian cast iron casing.

The building naturally split into three parts. The ex-jail was on the left-hand side, offices that used to belong to the sheriff and other important people were on the right, and the courtroom was on the first floor, in the middle.

Jerry's team extended the ground floor middle section, which provided the perfect space for a restaurant, and the courtroom is now a coworking space, where it is used by a dozen or so different businesses.

The old mortuary is now the toilet block for the restaurant. The rooms still had the stone slabs, one of which even still had a head block. There was a hole at

the end of the slabs for fluids, which were channelled away through a drain in the corner.

During the renovations, they found the old meter and lead piping from when gas was made locally to provide lighting for the building.

In the jail wing, some of the cells had already been altered prior to purchase. All had windows and vaulted ceilings. One still had the original jail door, which is now a distinguished feature of the office space. The cells work well as one or two-person offices. Fortunately, the only body they found was the old prison dog.

The building was also C listed and in a conservation area. In Scotland, the heritage listings go from C to A, whereas in England and Wales it's Grade III to I.

Having a C listing meant that the council were able to act on behalf of Historic Environment Scotland and the government. They are able to comply and act on a certain set of rules, whereas with Grades B and A – or II and I – conservation officers are actively involved from the start of the project.

The council's planning department will assess the planning application as a Grade C listed building, but will consult with Historic Scotland if they feel they need to.

The only part of the property that was protected was the exterior. Jerry had planned to keep the character of the building and decided early on to not change the façade. Any historical features were emphasised throughout the project and they focused on them in their planning proposal. Jerry and the planning department worked together from the beginning of the process, and apart from a few minor changes in paint colour, there wasn't anything they said they couldn't do.





MAJOR LEARNING CURVES

Most of Jerry's lessons came from learning about specific building practices relating to historical buildings, such as testing the lime mortar. The stonework at the front of the building was very detailed, but at the back it was more like a rubble wall. The pointing there was loose and covered a large area, and they had to find someone to make a matching lime mortar.

The best thing they did was getting an architect involved from the beginning of the process, who created a heavily detailed document for their planning proposal. It included information such as the historical aspects and what they were going to do to remain as sympathetic as possible to the building's history, while still creating a reasonable use.

As part of this, they had to anticipate what might have been asked by Historic Environment Scotland or the council, and getting the relevant professionals to provide the answers.

The other key challenge for Jerry was dealing with trades. It was the first site that he had developed which was completely vacant upon purchase. In previous developments Jerry has had customers in at least part of the properties which has meant phasing the works. However on this project there was a lot more to do, so it was fortunate the whole building was vacant and everything could be worked on at the same time. The project was managed by Jerry and his team. Although there was no conflict to note, they had problems with different trades getting in each others' way and a lot of people trying to do detail work in small spaces.

From start to finish, the project took 20 months. They phased the work to get paying customers in their offices as soon as possible.

Managing expectations of customers was important, but they were fortunate that the building had two sets of stairs, which allowed for minimal disruption.

COST OF WORKS

Project duration	20 months
Architects fees	£12,000
Planning costs	Not entirely sure, about £1,500.
Planning duration	Four months
Asbestos survey	Already in place
Damp survey and report	None taken. Previous damp proofing course installed.
Other costs	£3,000 on structural engineer.
Skips	£3,100
Site prep and demolition	£3,750
Substructure	£7,000
Drainage and incoming utilities	£2,600
Structural works	£12,000
Superstructure	£27,300
Doors	£2,100
Windows	£7,350
Roof	£13,500
Plumbing	£29,500 + £59,000 for Biomass boilers
Electrics	£23,000
Flooring	£9,500
Decoration	£11,000
Tea points	£600
Kitchen appliances	£650
Bathroom	Toilets £9,500
Floor & wall tiles	£1,250
TV & WiFi	£2,750
Key system	£2,450
Alarms / CCTV	£6,500
External lighting	£3,250
Blinds / curtains	£2,800
General Labour costs	£3,500
Furniture	£5,500 We recycle and make a lot ourselves.
Total costs	£270,450

FEATURE

RANT

BEGINNERS

DEVELOPMENT

INVESTING

FINANCE

LANDLORD

EDUCATION

EVENTS

VALUATION & INCOME

Post-works valuation	£650,000 - £700,000
Re-mortgage amount	No remortgage, just leverage for the next one.
Money back out	£0
Money left in	£0
Monthly income (per unit if more than one)	£8,333
CMO bills included	Average Monthly costs £2,870
Monthly mortgage payment	£1,416 Cap and Int. plus £1K per month for JV partner loan.
Monthly costs	£5,286
Net monthly cash flow	£3,047
% Return on money left in	Technically we have £200K- £250K of equity left in, but we leverage that for the next project.

TIME AND BUDGET

This project didn't come in on time or budget. The extension for the restaurant ended up being bigger than his original plans, which meant that it took longer.

Jerry's biggest frustration, certainly in the early days of the project, was the resources and managing to find enough trades that could do the work when it needed to be done. They tried to fund some of the work through cash flow from when the office spaces started to be rented out, but for future projects they are considering using more joint venture finance to be able to accelerate the process of redevelopment.

LOCATION AND DEMAND

"If it hadn't been close to where I live, I probably wouldn't have done it," Jerry admits. But it was local, and therefore easy to manage, and it doubled up as his head office. Ordinarily, he prefers larger sites which cater to at least a town or a city centre. His portfolio, apart from his latest project in Dundee, are all in or near to regional towns. The buildings range from 7,000 sq ft to 21,000 sq ft. Their largest is an out-of-town space which works very well for offices and storage solutions.

THE RESTAURANT

The idea for the restaurant came about through discussions with a friend, who later became a business partner. Although there were a few options on what to do with the ground floor space, including other food and beverage outlets such as a café, they decided on opening a restaurant. While he could have leased the space out to another business, he decided to bring it in-house as it was so local to him. It now has 35 staff and is open from 9am to 11pm, seven days a week.

It sits on the ground floor, and has taken up a few of the back jail cells – one of which has been partly converted into a wood fired pizza oven.

Jerry's business partner in the restaurant has now moved on to another project, allowing Jerry to buy him out and he can now begin to integrate the food and beverage operation into his main workspace business. He hopes that it will benefit other customers on other sites. Part of his long-term goal is to develop more of these types of buildings, but larger, where they can provide offices, shared space, food and beverage facilities and even possibly a gym.

He wants to create a place where people can work as well as have the options of several facilities. He aspires to support a blend of lifestyle, leisure and work.



Jerry likes to take on buildings that other people don't know what to do with, especially if they're already cellular. He then creates a space for small businesses to support each other.

Although location for a commercial let is important, it isn't quite as important as with a residential investment. Jerry recently conducted a survey of one of their centres and discovered that most of his customers didn't live locally. Some were travelling up to 15 miles a day to work there, because the facilities being offered were exactly what they were looking for.

He finds customers for his spaces in several ways, including networking, signage, word of mouth, referrals and online activities. He has found that there isn't one key area that works.

There are a few brokers online who market small office spaces. It took approximately six to eight months for the property in Kinross to be fully let, however this was mainly due to the phasing of the spaces becoming

available. As soon as an office was available, it was let – they never had an empty space.

They tend to offer 12-month licences to occupy an office or space. It provides security for both Jerry and the customers. Jerry knows that he will have an income for that space for the coming year, and the customers have a reliable place of work for the next 12 months. Equally, it allows some flexibility to adjust the rent according to the market.

While some people like commercial property to be let for 20 or 30 years, the flexibility of licensing for 12 months allows the growth of value of the building, by incrementally increasing rent as time goes by. *"When I started this process, I was looking for lots of passive income,"* Jerry says. *"That's what houses were all about and that's why I wanted a bigger deal. Then I discovered I'd got myself a job, which was looking after a multi-let building."*

It was at this point Jerry realised that he needed a team to manage the business and so he could take on more buildings. It's not dissimilar to serviced accommodation – having one or two units may not require a team, but once there's 10, 15, 20 units, a team can deal with any additional ones much easier.

ADVICE FOR OTHERS

"Make sure your strategy or your exit has looked at all the angles, not just the one you're used to. It doesn't have to be residential – you could do commercial."

Rather than converting to residential, commercial property can be a fantastic strategy for cashflow. The income of renting apartments will unlikely match the income from commercial lets.

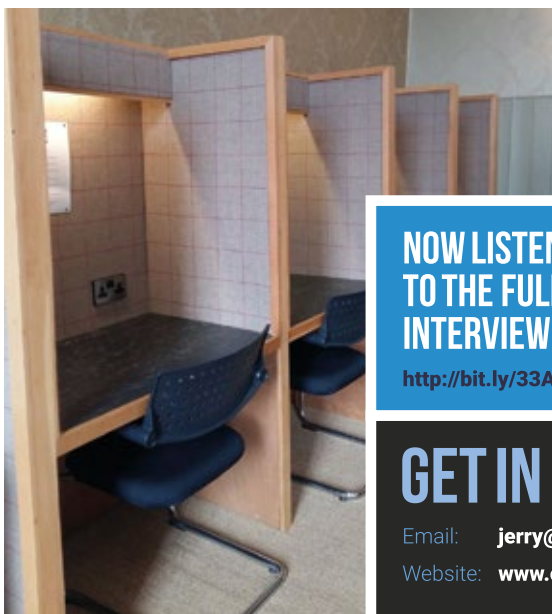
His advice is to consider how can you unlock the value of the asset as a potentially more lucrative commercial investment, which can provide several tax benefits over residential.

Although on the outside Jerry's business is mainly letting out office space, his main business is buying commercial buildings at a low price. He redevelops them and lets them out to rebuild the property's value. Over time, the income increases and he can leverage it to buy the next project.

Jerry says: *"Walk in with your eyes open. Budget both time and money with a good percentage over what you think it's going to be."*

Done right, the CMO model can significantly increase the net income which will push up the building's value. It could be the ugliest building in the world but increasing the net income will also increase the value.

In comparison, Jerry has found residential valuations incredibly frustrating. A nicely renovated terraced house will unlikely be worth much more than the one sold next door.



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