



THE MAKES OR BREAKS

OF ADAPTIVE RE-USE TO RENTAL APARTMENTS

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The return to in-office work following the COVID-19 pandemic is moving slower than the Canadian commercial real estate sector has hoped for. National commercial office vacancy rates are at an all-time high at 17.6% as of the end of 2023, according to Altus Group¹. This trend has some owners and developers examining adaptive re-use of existing commercial office buildings to residential rental apartments.

While attractive at face value, when income statements yield dramatically lower revenues, the excitement to pivot and convert office space to residential apartments is not financially viable for every vacant office building. The following are some key considerations for developers to narrow their search to take advantage of this opportunity.

Zoning and permitting

The primary advantage of conversions is the advancement of construction in comparison to a site re-development (i.e., the ability to capitalize financially and environmentally on the existing shell and structure). This leg up can easily be lost in the process to comply with residential municipal zoning requirements through the site plan control process. If purchasing a commercial office building for adaptive re-use, performing a planning study in the due diligence phase to identify requirements to avoid or minimize zoning amendments is a must.

Fenestration and floor plate

Floor plate efficiency is paramount to a successful residential apartment complex. Office buildings do not have the same code requirements for natural light as residential buildings do. As such, fenestration – the layout of the windows – will dictate where bedrooms and living spaces go in a unit if

you're trying to work within the existing building shell and structure. In some buildings, this results in long, cavernous suites with wasted floor area on corridors or costly base building modifications.

Equally, the dimensions and shape of the building floor plate constrain efficiency. Square-shaped floor plates are common for offices, which lend to multiple corridors in converted residential apartment buildings. Rectangular buildings with shallower depths offer the ideal footprint to convert. Generally, targeting underutilized Class B or C office space is a good place to start. Alternatively, lower-rise square office buildings can be converted into a unique podium for over-build adaptive re-use projects, through these projects carry significant investments and project schedules.

Incentives

Possibly the biggest marker or breaker of conversions is the renewed proposal and availability of government financial incentives. The City of Calgary is at the forefront of office-to-residential conversion projects, offering a \$75 per square foot incentive and fast-tracked approvals to spur a strategic revitalization of their downtown. The program has been so successful that application intake is temporarily paused while the City tops up funding². The City of Edmonton and City of Toronto have both had councilors laud Calgary's approach, initiating examination of the feasibility of their own incentive programs for office-to-residential conversions to combat their respective housing shortages^{3,4}. CMHC has offered the Rapid Housing Initiative since 2020, with conversions a frequent strategy to meet the aggressive timeline requirements of the affordable housing funding stream⁵.

In the U.S., the federal government has also initiated steps to incentivize commercial-to-residential conversions, even proposing to offer sale of government building stock⁶. Being aware of and obtaining funding through incentives can push a traditionally unviable project into reality.

While each conversion project carries its own inherent risks, identification of these key factors in the planning and site selection phases is impressive to success.

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SOURCES:

¹ Canadian Office Market Update – Q4 2023, Jennifer Nhieu – Altus Group, January 10, 2024 (<https://www.altusgroup.com/insights/canadian-office-market-update/>)

² <https://www.calgary.ca/development/downtown-incentive.html>

³ <https://secure.toronto.ca/council/agenda-item.do?item=2023.PH7.9>

⁴ <https://pub-edmonton.escribemeetings.com/Meeting>.

⁵ <https://www.cmhc-schl.gc.ca/professionals/project-funding-and-mortgage-financing/funding-programs/all-funding-programs/rapid-housing>

⁶ <https://www.whitehouse.gov/briefing-room/statements-releases/2023/10/27/fact-sheet-biden-harris-administration-takes-action-to-create-more-affordable-housing-by-converting-commercial-properties-to-residential-use/>