

# The Industrial O · U · T · L · O · O · K

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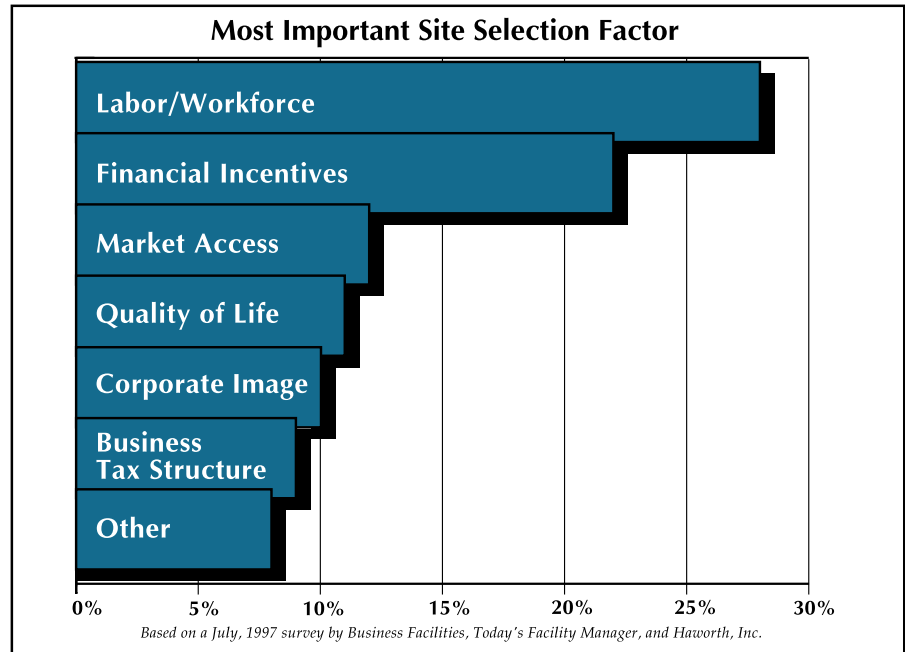
## Something Has Got to Give

As with every new year, we're inundated with myriad predictions and forecasts by experts and eccentrics alike. What can we deduce from the variety of forecasts ranging anywhere from doomsday to utopia for the coming year? Probably nothing. But if you want something to bank on in 1998 it's this: labor is the site selection buzzword.

Labor shortages seem to be the common theme in the U.S. recently, and in many places, unemployment rates have reached all-time lows. Not only did the U.S. experience its lowest unemployment rate in almost two decades last year, it ranked the lowest among 7 major economies (Britain, Canada, France, Germany, Italy, and Japan) at 4.9%.

Further proof of a U.S. labor shortage lies in the survey results of 150 corporate executives who ranked various site selection factors used to

*Continued on page 7*



## The Rich Get Richer

Since the late 1970's, the income gap between the rich and poor in the United States has expanded in nearly every state. According to a study conducted by the Center on Budget and Policy Priorities, the average income of the richest fifth of families grew faster than the average income of the poorest fifth in 48 states as well as the District of Columbia from 1976 to 1996. North Dakota and Alaska were the lone exceptions to this phenomenon. Interestingly, the income of the poorest fifth actually decreased in 44 states and the District of Columbia during this time period.

While wage disparity has been increasing over the long-term, the

poorest fifth surprisingly gained ground on the richest fifth in 13 states from 1986 to 1996. The relative income gap shrank most significantly in Arkansas, Colorado and Minnesota. In contrast, the plight of the poor has significantly worsened in Arizona, Connecticut and New York.

Overall, states with the highest ratio of income between the rich and poor are New York (19.5x), Louisiana (15.9x), New Mexico (14.3x), Arizona (14.2x) and Connecticut (14.2x). Ironically, the greatest income disparity is present in our nation's capital, the District of Columbia at an as-

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## Engineering Tax Out of the Building

Although the construction of new buildings and purchase and retrofit of existing facilities have significant tax implications, few corporate real estate executives factor tax engineering into the real estate planning process. Therefore, lucrative opportunities to reduce income, property, sales and transfer taxes via tax engineering are foregone. The discipline of tax engineering combines the fields of design, construction, accounting, evaluation, and taxation. The resulting documentation minimizes the tax burden of newly constructed or recently acquired facilities. More specifically, tax savings are maximized via conscious decisions to construct a facility in a manner that enables “gray area property”, which typically falls under the real property classification, to be categorized as personal property.

Section 1245 of the federal tax code defines personal property as a) anything related to the manufacturing process or the business being conducted inside the facility, or b) anything that can be taken from the facility (tangible personal property) without affecting its function as a building.

Classifying property as personal rather than real can achieve tax savings via all or some of the following:

1. Accelerated depreciation schedules (real property - 39 year life, personal - typically 5-15 year life) resulting in lower income tax.
2. The avoidance of sales tax in areas where machinery and equipment purchases are sales tax exempt.
3. Diminished transfer tax via lower levels of real property.

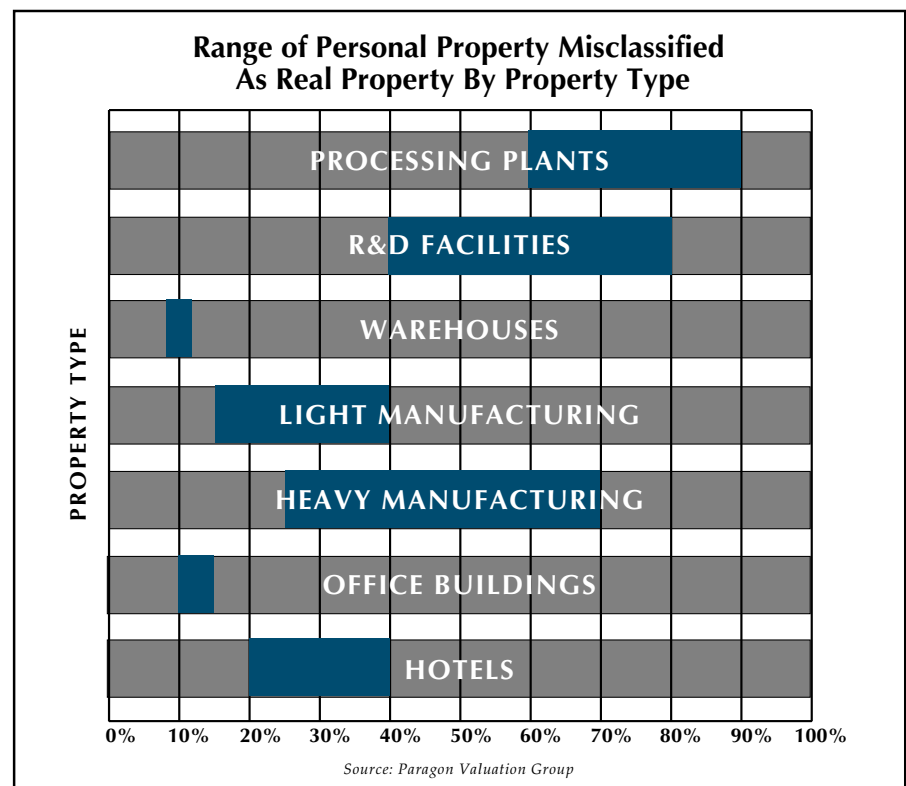
4. Lower property taxes in states where personal tax is exempt or enjoys a lower tax rate.

Examples of tax engineering include segmenting switch gear into 2 panels, and utilizing an independent steel structure to support craneways. Companies which utilize single switch gear panels in facilities must classify this investment as real property. In contrast, tax engineering would mandate the use of two switch gear panels, one for building services and a second for machinery and equipment, computers, security, etc. Under the tax engineering scenario, the conduit and wiring in the second switch gear panel is eligible for the more favorable tax treatment associated with personal property. Another common and substantive tax engineering blunder involves reinforcing the building columns in industrial facilities to accommodate the additional weight of an overhead crane.

Instead of reinforcing existing columns, a tax engineer would mandate the use of a stand-alone support structure. Under this scenario, all of the steel utilized in the craneway and its foundation can be allocated to personal property.

According to tax engineering experts, a significant amount of personal property is regularly misclassified as real property across a broad cross section of commercial and industrial buildings. Estimated ranges of personal property investment typically misclassified in specific types of facilities are as follows:

- Processing plants - 60%-90%
- R&D facilities - 40%-80%
- Warehouses - 8%-12%
- Light manufacturing - 15%-40%
- Heavy manufacturing - 25%-70%
- Office buildings - 10%-15%
- Hotels - 20%-40%. □



## They're Dropping Faster than Clinton's Pants

According to the AM Best Company 1997 Annual Workers Compensation Insurance Market Annual Report, workers compensation premiums continued to decline in 1996. However, these premiums did not decline as rapidly as losses and loss adjustment expenses. In other words, profits increased because costs experienced a more significant decline than premium revenues.

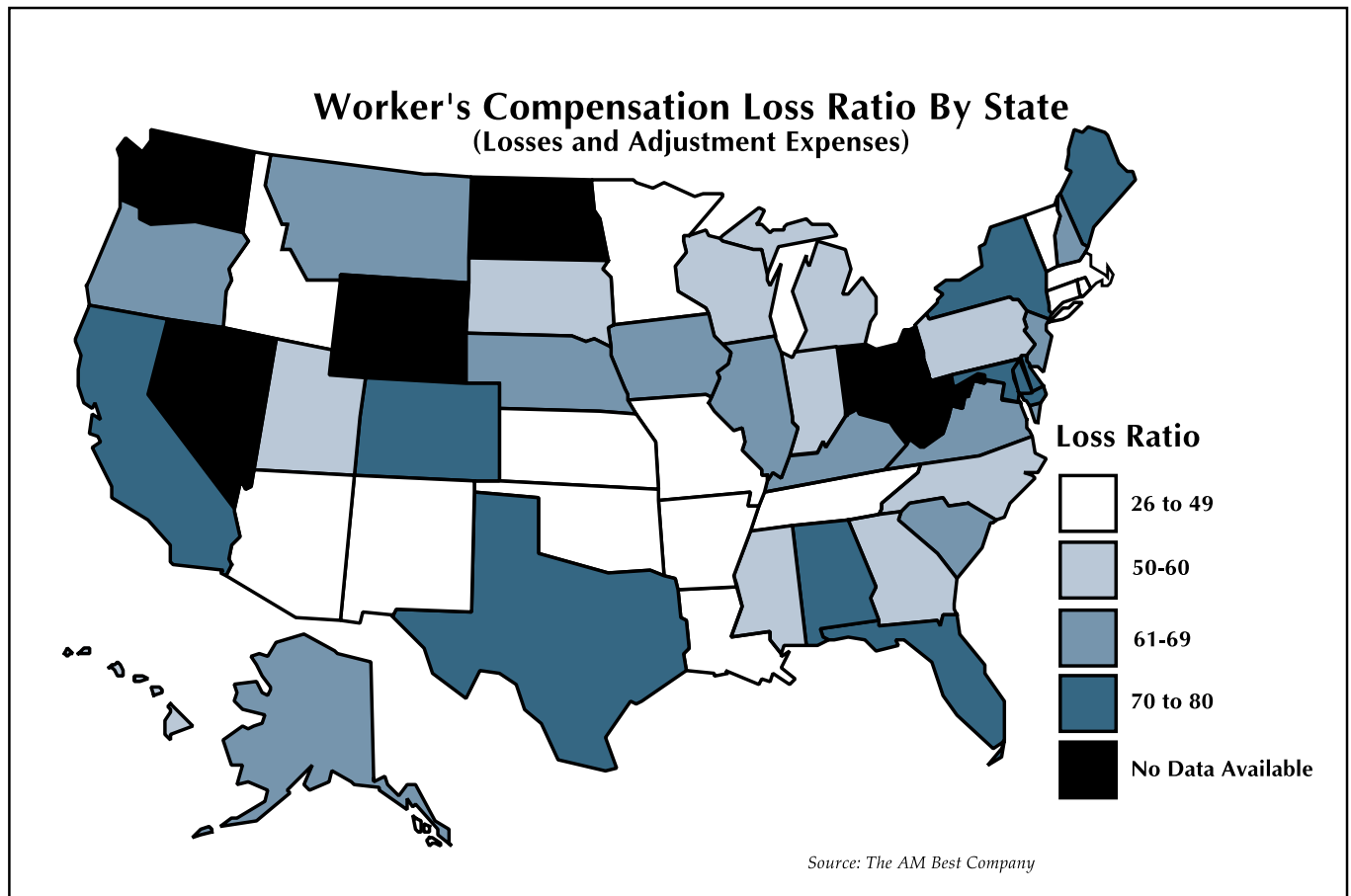
The decline in premium revenue can be attributed to increased competition among insurance providers and the use of large deductible policies

driving down the cost of workers compensation premiums. State reform programs limiting the benefits available to injured workers and employers installing safety and accelerated return to work programs account for the majority of the decline in losses. A reduction in the pool of excess revenues accumulated over the past few years also mitigated a reduction in losses.

Exclusive of state insurance funds, the AM Best study quantified the total number of insurance premiums by state for 1995 and 1996. As would be expected, the greatest number of workers compensation premiums are written in California (3,673,166), Pennsylvania (1,959,799), New York (1,833,799) and Florida (1,825,871). Comparing 1996 to 1995 figures, the

most significant decline in premiums occurred in Kentucky (-29.9%), Montana (-22.4%), Hawaii (-22.3%) and Minnesota (-22.2%). While most states experienced a decline in the number of premiums written, a few states encountered a significant rise. These include Rhode Island (+42.8%), Florida (+28.9%), Maine (+27.6%) and Oklahoma (+21%).

The study also rated each state on its workers compensation loss ratio, a measure of profitability. More specifically, the loss ratio is calculated as follows:  $(\$losses + \$adjustment\ expenses / \$premiums) \times 100$ . The loss ratio disparity between states is dramatic ranging from most favorable in Arkansas (26) to least favorable in California (88) and New York (88). □



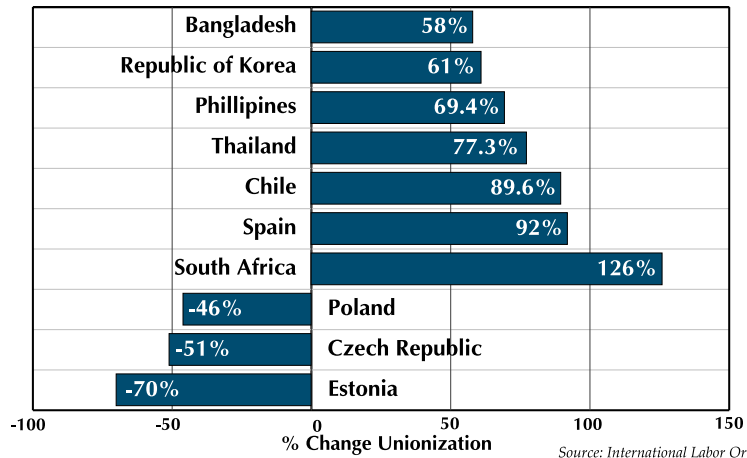
## A World of Unions

According to an international labor organization study, the number of workers belonging to trade unions declined sharply from 1985-1995 in most regions of the world. Although unions lost ground in the majority of countries, the greatest contributing factor to the total worldwide union decline resulted from the end of compulsory union membership in the former Soviet bloc. The most significant percentage declines in union membership occurred in Estonia (-70%), the Czech Republic (-51%) and Poland (-46%). In contrast, unions achieved significant growth in South Africa (+126%), Spain (+92%), Chile (+89.6%), Thailand (+77.3%), Philippines (+69.4%), Republic of Korea (+61%) and Bangladesh (+58%). As a point of comparison, union membership in the U.S. declined by 21% during the same time period.

In terms of current membership levels, the ILO analysis identified approximately 50 countries where less than 20% of the work force is presently organized by labor unions. Major international players with extremely low levels of unionization include Indonesia (3%), Thailand (4%), France (9%), Malaysia (13%), Republic of Korea (13%), U.S. (14%), Venezuela (17%) and Spain (19%).

Countries with extremely high levels of unionization are as follows: Iceland (83%), Denmark (80%), Finland (79%), Cuba (70%), Hungary (60%), Italy (44%), Brazil (44%), Mexico (43%), Austria (41%), and South Africa (41%). □

Percentage Change in Unionization 1985-95



## Electricity Deregulation, Who Cares?

Over the last few years, most of the attention in the electricity industry has been focused on deregulation. While deregulation still holds promise, many commercial building owners have been evaluating the merits of another potential alternative, self generation.

While industrial facilities, hospitals and universities have been generating their own power for decades, commercial buildings were typically left to the mercy of the local electricity provider. However, this may soon change if Sears Tower manager, John Buck Company, is successful in its legal challenge against Commonwealth Edison to produce its own electricity. If victorious, this management firm plans to construct a \$10 million electricity generation plant in the basement of the Sears Tower forecast to reduce electricity bills by \$2 million annually.

Although on-site generation is only a feasible alternative for the largest commercial buildings, new technology developed by Allied Signal may make self generation a reality for smaller commercial operations as well. The company has developed a turbo-generator power system that is suitable for smaller commercial operations. The turbo-generator is reasonably compact with dimensions of 3 wide, 5 6 deep, and 6 tall, weighs less than 1,000 pounds, and burns gasoline, diesel fuel and natural gas. While individual units generate only 75 kilowatts of electricity, multiple units can be linked together to provide up to 1 megawatt of power. Originally developed for third world markets lacking power infrastructure, these units are suitable for restaurants, hotels, schools and small industrial establishments. At only \$25,000-\$30,000 per unit, self generation may become increasingly popular among small commercial operations, even if deregulation significantly lowers electricity costs. □

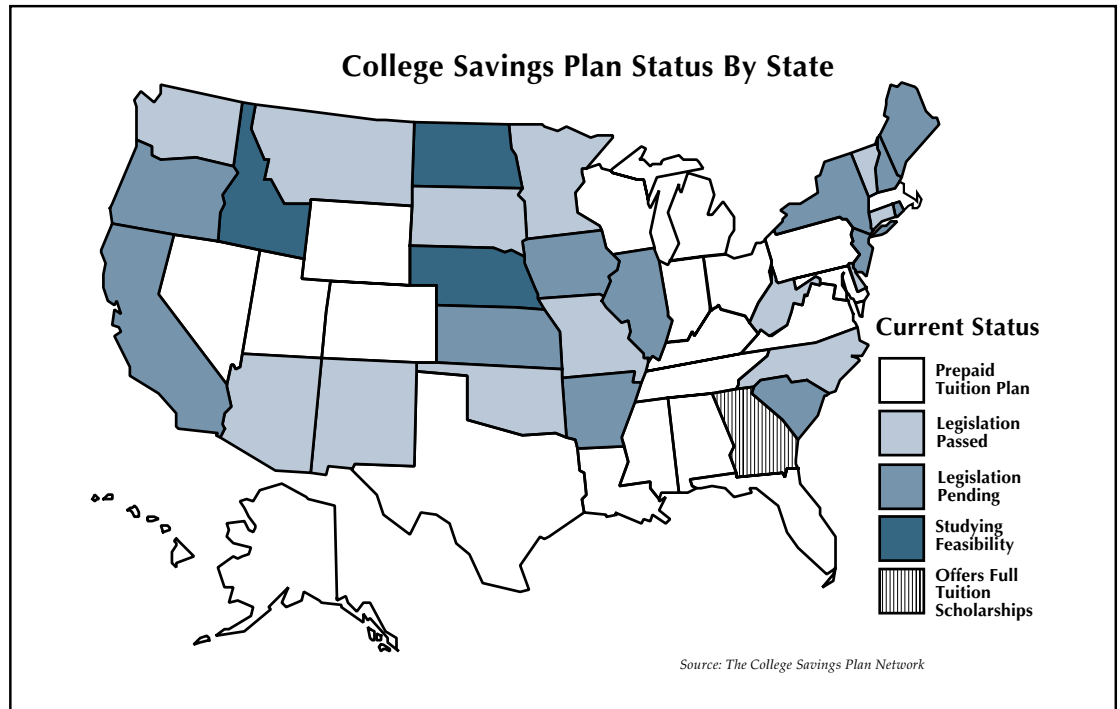
## College Bills for Infants

In 1986, Michigan created the first prepaid college tuition program. Since its inception, 15 other states have adopted similar plans and more than 36,000 Americans have utilized this mechanism to attend college. Today, college savings plans have approximately 730,000 participants accounting for \$3 billion in contributions and earnings. These figures are forecast to increase to 1,791,000 and \$6.5 billion by 2006, respectively.

After Michigan's adoption of its savings plan, most states were quick to consider creating their own program. However, implementa-

tion was slow due to the unknown nature of IRS treatment of these entities. While the IRS has changed the tax treatment of these plans several times over the years, a trend toward less or no taxation is evident.

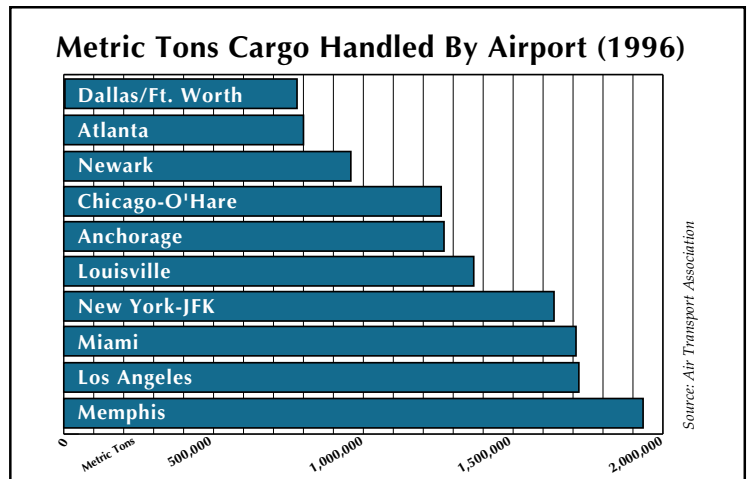
For this reason, legislation to adopt or feasibility studies to explore this issue are currently underway in most states. A map depicting the prepaid tuition status of all states is outlined to the right. □



## Where Air Cargo?

As would be expected, Memphis, the main hub of the Federal Express operation, handled more metric tons of cargo than any other airport in the U.S in 1996. Surprisingly, Louisville's airport, home of the UPS transportation hub, ranked only fifth at 1,368,520 metric tons. Los Angeles, Miami and New York's JFK ranked second through fourth at 1,719,449, 1,709,906, and 1,636,497, respectively.

The sixth through tenth positions for air cargo were rounded out by Anchorage, Chicago O'Hare, Newark, Atlanta, and Dallas-Ft. Worth airports. □



## Union Hope

While union organizing trends have been largely negative in recent years, a review of labor election data for the first 6 months of 1996 and 1997 suggests an improving situation for unions in the U.S. During this time period, representation elections (elections occurring at facilities presently not organized by the union which filed the election petition) increased from 1,374 to 1,479, or 7.6% in 1996-1997. In contrast, the number of decertification elections (elections to determine whether an existing union should cease from being the bargaining agent of the unit which the union already represents) decreased 15.1% from 238 to 202.

During the time period examined, unions also experienced a rise in the number of successful union representation elections, as well as the percent of wins in these instances. In the first half of 1996, unions were victorious in 652 elections, or 47.5% of those held. Total election victories in January-June of 1997 (728) outpaced the 1996 level by 11.6%. The percentage of union victories in these instances also showed modest improvement at 49.2%.

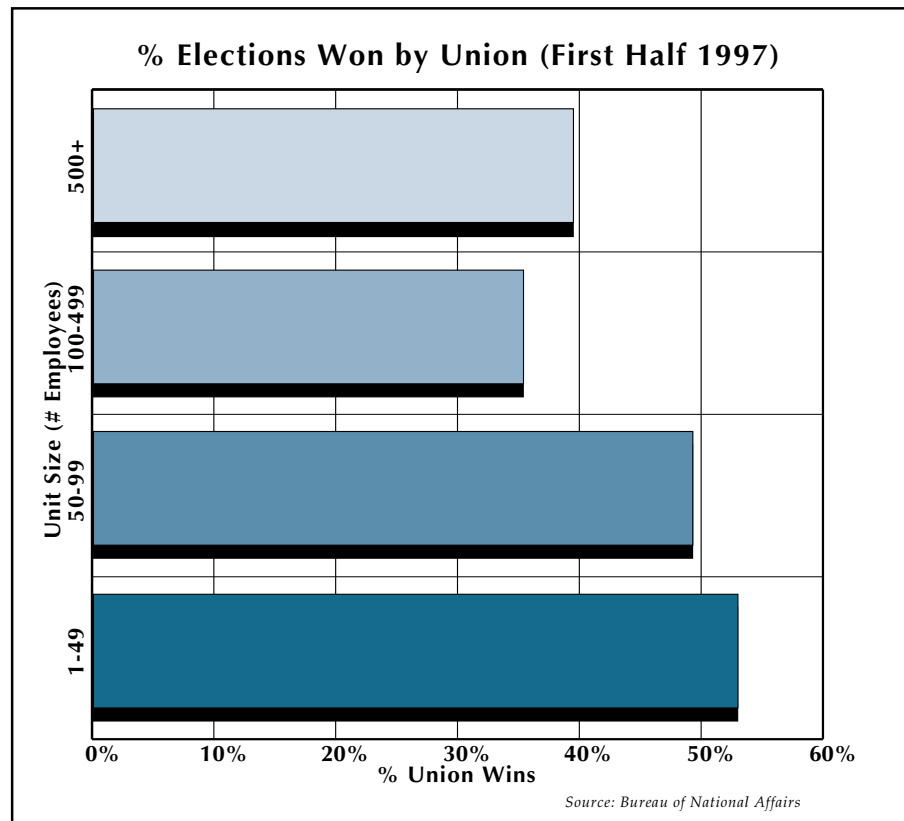
In addition to the increase in representation elections, the number of voters eligible to participate in these elections rose from 98,748 in the first half of 1996 to 109,163 for the same period in 1997. In successful union elections, the number of eligible voters increased 15% from 36,978 to 42,501.

Consistent with recent years, the percent of elections won by the union in the first half of 1997 tended to be significantly higher in cases involving smaller unit sizes. The highest win ratio involved the 1-49 unit size sub group (52.9%) followed closely by the

50-99 cohort (49.2%). The success rate was substantially lower among the 100-499 and 500+ sub groups at 35.3% and 39.4%, respectively.

Similar to unit size, win ratios vary significantly by industry. According to 1996 figures, unions were substantially more effective winning elections in the finance/insurance/real estate

(59.6%) and service (58.5%) sectors. Unions also experienced considerable success in the construction trade (51.8%). The manufacturing and mining industries provided the most significant organizing resistance with extremely low success rates of 37.8% and 28.6%, respectively. □



## The Walker Companies on the Web

To find out more about our Real Estate, Consulting, and Development Services group, visit our new web site @ <http://www.walkerco.com>. View up-to-date detailed maps and charts on critical site selection issues, available buildings throughout the Southeast, and a list of The Walker Companies' exclusive agencies.

# The Industrial O·U·T·L·O·O·K

*Something Has Got to Give – continued from pg. 1*

make corporate location decisions. Two-thirds of those surveyed indicated their most recent project required the relocation of employees, and 28% ranked labor/workforce as the most important site selection issue. Financial incentives fell just below labor/workforce, with 22% of the respondents ranking it at the top of their list.

The survey included a breakdown of the results by industry. Labor/workforce was the number one site selection issue for the Automotive, Electronics, Machinery/Equipment and Plastics industries. It was also among the top 3 site selection factors

for the Chemicals/Petrochemicals, Computers, Food Processing and Pharmaceuticals/Medical Products industries.

Why is labor so tight? It seems there is an abundance of corporate site selection activity. Almost two-thirds of those surveyed said they were currently involved with a project, and 78% indicated their site selection projects either added new jobs, or retained existing ones. Furthermore, only one in five corporations engage in “right-sizing” or “reorganization” initiatives, which means no mass layoffs. In other words, more jobs are being created, while fewer workers are added to the labor pool through layoffs, etc. And industry isn’t slowing down much, either. Accord-

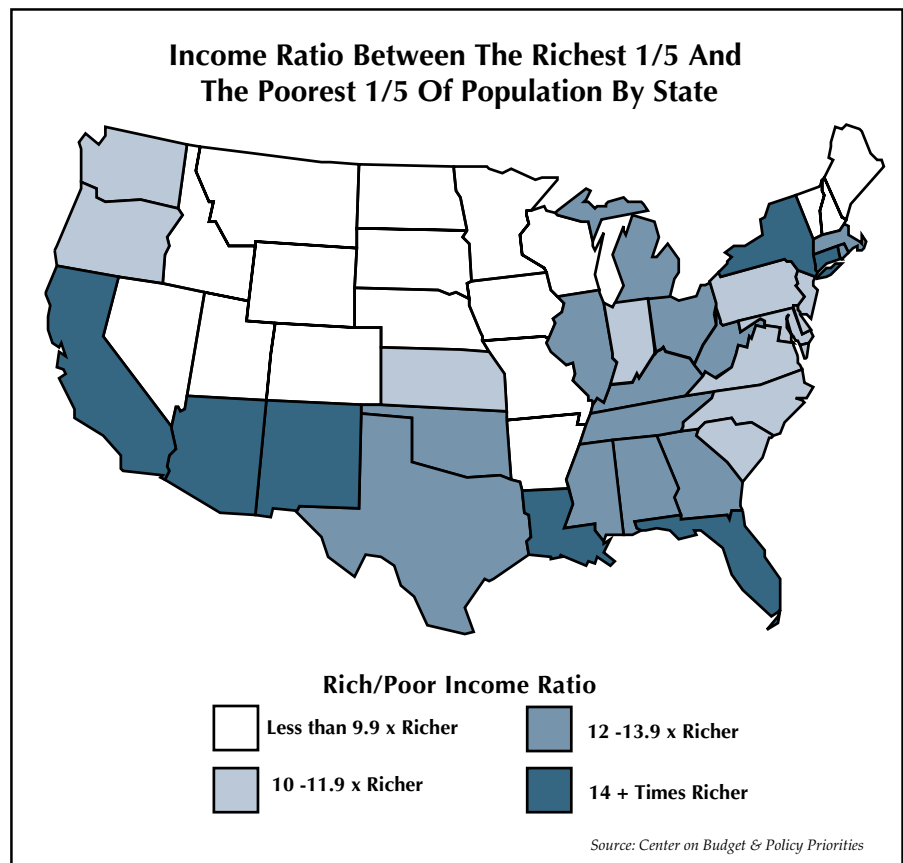
ing to a survey of 50 economists, gross domestic product (GDP) expansion in the U.S. is estimated to be 2.5%. With a low unemployment rate and an economy with a lot of momentum, something has to give.

What does this mean for corporate site selectors? According to the January 1998 Kiplinger Washington Letter, employers are turning to executive recruiters for good leads on middle-management candidates, and to community college graduates to take jobs as computer/electronics specialists, technicians, machinists, etc. Employers planning to relocate in the near future may want to consider bringing staff along with them to get the project staffed and operational. □

*The Rich Get Richer – continued from pg. 1*

tounding 28.2x. On the other hand, the most even income distributions are present in Utah (7.1x), North Dakota (7.3x), Vermont (7.5x), Wisconsin (7.7x), and Iowa (7.9x).

Economists argue the main cause of the growing disparity is rapid technological changes (which has increased the value of skilled workers), the decreasing clout of unions, numerous manufacturing industries moving operations offshore, and the growth in low paying service jobs. Foreign competition and poorly paid immigrant workers are also cited as minor contributing factors. While the statistics certainly paint a grim picture for America’s poor, reality is likely worse because this analysis fails to account for capital gains and individual earnings in excess of \$100,000. □



## The Southeastern Industrial Real Estate Market

The Walker Companies' in-house research department utilizes the proprietary WISER (Walker Industrial Site Evaluation and Review) database system to track available industrial facilities (over 40,000 square feet) in eight Southeastern states, profiling more than 100 variables on every building. We maintain information on buildings throughout the region, including rural areas or "2<sup>nd</sup> tier" communities. From this database we are able to run a multitude of reports which give excellent "snapshots", as well as in-depth analyses of the industrial real estate market and its various segments.

The following table is a summary of the Southeastern

industrial real estate market which is defined as available manufacturing and distribution facilities typically located in non-metropolitan/secondary markets. The market currently consists of 954 available buildings throughout 8 Southeastern states, totaling 145,465,452 square feet.

*The Industrial Outlook* will feature articles, tables and graphs whose focus will be available buildings, facilities recently sold/leased, and the issues and factors that shape the market. Topics that will be covered in coming issues include: 1.) a state-by-state

comparison of speculative construction, 2.) a comparison of building value between states and 3.) value by quality, age of building, time on market, distance from interstate, etc. Please direct any suggestions or comments related to the industrial real estate market to David J. Sink in our Atlanta office. □

| Available Industrial Buildings in the Southeast |                    |             |                    |             |
|---|--------------------|-------------|--------------------|-------------|
| As of February 15, 1998                         |                    |             |                    |             |
| State   | Total Available SF | % of Market | Avg SF of Building | # Buildings |
| Alabama   | 8,103,905          | 5.6         | 142,173            | 57          |
| Georgia*  | 47,322,030         | 32.5        | 147,881            | 320         |
| Kentucky  | 7,930,185          | 5.5         | 130,003            | 61          |
| Mississippi                                     | 10,787,025         | 7.4         | 182,831            | 59          |
| North Carolina                                  | 29,671,532         | 20.4        | 159,524            | 186         |
| South Carolina                                  | 14,761,406         | 10.1        | 150,627            | 98          |
| Tennessee                                       | 15,835,518         | 10.9        | 147,995            | 107         |
| Virginia  | 11,053,851         | 7.6         | 167,482            | 66          |
| <b>TOTAL</b>                                    | <b>145,465,452</b> | <b>100</b>  | <b>153,565</b>     | <b>954</b>  |

\*Includes buildings in Atlanta 100,000 square feet or larger

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