Commercial Real Estate

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The Big Ts

Timelines, Terminology, Teams and Tours

The status quo of commercial real estate is changing, and savvy tenants and buyers have become emboldened to question the underlying motivations of their advisors and the quality of the information they provide. This article discusses the Big "Ts" of commercial real estate; Timelines, Terminology, Teams and Tours – the factors that *indirectly* affect a business' total cost of occupancy. Because commercial buildings are fairly generic, these insights will be as meaningful to the medical practitioner as they are to those who utilize office, industrial, automotive, educational, or hospitality space. Armed with an understanding of these concepts, you will be better prepared to make fully informed leasing, buying and investing decisions.

Timelines

Time can be either your ally or your enemy, and waiting until the last minute to think about space, and your options, can cost you plenty. Your *total* cost of occupancy should be constantly on your mind, as should be exploring ways to minimize it. The process of evaluating whether to renegotiate or relocate ideally begins in earnest nine to twelve months prior to the date the stay-or-move decision must be made. This period gives you ample time to tour other properties, gain a clear understanding of the state of the market, and develop leverage among landlords, including your own landlord who will likely need external pressure before granting market rates and concessions.

While the research and identification of suitable properties can take months, negotiating favorable terms and conditions on the best properties can typically be accomplished in seven to fourteen days. Once there has been a meeting of the minds, allot a week to ten days for the landlord to prepare the lease agreement, and two to three weeks to negotiate lease comments and finalize the transaction. Depending on the extent of the tenant improvements, allow thirty days to six months for the space to be made ready for occupancy.

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Terminology

Commercial lease rates are variously quoted as either "full service" (fs), "triple net" (nnn), or "modified gross" (mg), and vary according to how much of the building's operating expenses are included in the base rate. Operating expenses typically consist of property taxes, casualty insurance and common area maintenance (cam). Additional occupancy costs include utility and janitorial expenses.

In a full service lease, typical of Class "A" office and medical properties, the operating expenses, utilities and janitorial expenses are included in the base rate. Most industrial, retail, and many older office and medical buildings, are leased on a triple net basis; where the tenant is charged an amount for the base rate, *plus* a pro-rata share of the operating expenses of the building, their electrical usage and the cost of janitorial services. In a modified gross lease the tenant pays a base rate plus *some* of the operating expenses, as well as the cost of utilities and janitorial services. Regardless of the name the landlord uses to describe its lease, your challenge is to confirm which operating expenses will be charged to you, in addition to your monthly rent, and then convert the economics of competing properties to a common out-the-door price.

To illustrate: An office or medical space with an advertised rental rate of $24 per square foot including all operating expenses (a full service lease) would cost the same as a property advertised at $ 16 per square foot *plus* operating expenses, utilities and janitorial costs totaling $8 per square foot (a triple net lease), or one asking $ 21.00 per square foot *plus* utilities and janitorial expenses of $ 3 per square foot (a modified gross lease).

Teams

A recent phenomenon in the commercial real estate industry is the "team" or "group" concept, where two or more agents from the same company form a mini-agency within the firm. They generally consist of a senior agent (the rainmaker) and one or more supporting, but much less experienced, agents. While teams make a great deal of sense to property owners, who want several people marketing their buildings, canvassing for tenants or buyers, and manning the phones, they are generally a poor choice for tenants.

The reasons for this are twofold. First, the newest members of each team are generally charged with the most important part of the process – research. It is during the research phase that the true needs and urgency of competing property owners are discovered. Second, listing agents are property-driven, meaning they have a fiduciary duty to lease the spaces that they or their team represent…to the exclusion of properties listed by others which may be better suited for your needs and/or are less expensive. *This includes properties listed by the same company, but by other agents on different teams.*

While everyone needs to start their careers somewhere, resist the temptation to permit newly minted "assistants" or "associates" (read: trainees) to use your business for on-the-job training. Instead, seek out and retain an experienced, objective, and client-driven advisor to represent and protect your interests. In the final analysis, your choice of advisors will determine which spaces you are exposed to and how much you will pay.

Tours

If you find yourself being shown only properties represented by one company, you're being "steered." Common ways agents steer prospective tenants or buyers to their listings include suppressing information about other available properties and/or presenting false choices – properties that are clearly less suitable or desirable than the listings controlled by the agent(s). When working with real estate agents or brokers, make certain to clearly articulate your desire to be made aware of *every* suitable space, regardless of which company, team, or group has the listing. This should be discussed at the initial interview and memorialized in writing, with all agents signing the appropriate disclosures.

Another way to minimize or eliminate steering is to simply refuse a dual agency representation arrangement; which occurs when agents from one company represent both property owners and tenants in the same transaction. Common sense should tell you that a dual agency favors property owners, who are assured of achieving the highest rental rates possible; and agents/brokers, who stand to collect both sides of the commission.

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Closing Comments

If you don't have a thorough understanding of how the commercial leasing and buying processes operate, you can save time and money by retaining an advisor that does. When selecting a real estate advisor use the same criteria as you would when choosing your CPA and attorney, namely, confirm that they are in the business of solving your particular problems and do not have any potential, or undisclosed, conflicts of interest. ■

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