

HOW TO MAINTAIN A HEALTHY PROPERTY

BY STEVE BERGSMAN



With High Vacancies in Local Markets, Maintain Building Attractiveness, Client Confidence to Prevent Tenant Flight

Except in a few markets, one of the residual effects of the economic downturn has been a significant increase in vacant office and industrial space as companies downsized, went out of business, or simply rationalized business operations into other existing locations.

These kinds of corporate shifts are, unfortunately, not unusual in the property management business. However, during the recession and the slow-recovery of the past few years, the situation became more acute for owners and property managers. Despite lower net operating income, or NOI, renewed efforts had to be undertaken to keep as many tenants as possible, as newer and more modern buildings — also with empty space — were luring away customers from older, once stabilized properties.

Owners and managers had to rethink that age-old property question, “How do we maintain the structure, keep it attractive and make sure it is still a healthy investment?”

Due to the severity of the downturn, the same problems were occurring in hard hit markets such as Las Vegas, as well as what were considered healthy markets, such as Washington, D.C.

There has been an incredible opportunity over the last two to three years to take advantage of the market to trade up, observes **Matthias Schmitt, SIOR, MCR, CCIM**, AIA, a senior vice president with West, Lane & Schlager Realty Advisors in Washington, D.C. “It’s been a flight to quality. Ten years ago, tenants couldn’t afford to be in a Class A- building, but now they can.”

To which he adds, “maintaining and repositioning your building is incredibly important. Tenants are looking for stable, well-capitalized ownership and managers that are willing to invest significant capital into their buildings, whether it’s to rejuvenate the HVAC, make cosmetic changes to the lobby, or create a fitness center.”

The term “flight to quality” has become an industry cliché, but it works so people use

it. Down the east coast, in Charleston, S.C., **Stacy Smith, SIOR, MCR, CCIM**, a principal with Colliers International, notes, “in the boom years, a lot of tenants were forced into B and C product because there were no other options. Now there is a big shift in perception and tenant demand. They want improved buildings and newer buildings that are more efficient and have better security. There has been a flight to quality.”

There is that phrase again.

Johnson sees two trend lines emerging in his city. The first involves the local owners who are either resistant to change or don’t have the capital to invest in their buildings. He predicts this group will see increased vacancies in their buildings.

On the other hand, occupancy success has come from national and even regional developers “who have an overall understanding of how to convert older buildings to make them more appropriate, from better door systems to redoing floors to modernized lighting, painting and re-landscaping.” This makes the client happier.

So what are these older properties — something built for a big manufacturer early in the 20th century? Not really. Mostly, they are in business parks constructed in the 1980s and 1990s.

“A 100,000-square-foot building constructed in the 1990s, as long as it is functional and has yard space, and has someone willing to put in decent lighting and clean up the structure, will have demand again,” says Johnson. “In contrast, a 50,000- to 100,000-square-foot building from the early 1980s with a 16-foot-clear located in the middle of the city on two acres, will have to be re-converted into something other than industrial.”

Although this sounds extremely simple, the best way to keep tenants happy to the point where they want to stay in your building is to address the obvious — keeping operational functions running smoothly; maintaining communications; and most of all understanding individual tenant needs.

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Richard Mason, SIOR, IIM, is not only a partner with Commercial Realty Specialists in Newport Beach, Calif., but the owner of commercial buildings as well. He knows many tricks and tips about making sure his properties remain the number one choice for tenants.

“Keeping a property healthy and keeping the rent flowing means keeping the tenants happy,” he says. “And one of the things that makes tenants unhappy is if building maintenance is not kept up, such as an elevator system that is constantly not working. These small things can frustrate a tenant and once they experience lack of service, they might start thinking, ‘maybe I need to pay more in another building to get better service.’”

In regard to operational equipment, one of the biggest concerns should be HVAC, he adds. “Once one of these go down, it will get uncomfortably hot inside the property and nobody will want to be there. This creates ill will because employees can’t work where it’s sweltering and now the tenant will complain, ‘Look, I have to let my employees go home because they can’t work in this sweltering building.’” Mason recommends having the HVAC maintained on a quarterly basis and if there is a problem that needs to be repaired it can be planned ahead of time. Also, if repairs are needed then tenants have to be informed to give them time to adjust.

Conversely, tenants will sometimes see a problem, not inform the landlord, and then just sit and simmer, which is why, even if there is not a property manager on-site, one should visit the property regularly and check in with the tenants. Mason gives the example of a sprinkler head that broke, which meant that cars were getting sprayed with water and parts of the parking lot were being flooded. “That doesn’t make the tenants feel warm and fuzzy,” Mason suggests.

In most California locations, smoking is a significant issue. While smoking is banned in buildings, less thought is given to places people can go to smoke. “If the outdoor smoking section is placed in an area where other tenants still have to wade through a cloud, this really angers people,” he says. “I’m representing a company now that will be relocating because the smoking area was too close to the entrance of the building.”

Small problems, as well as the large ones, bother tenants, which is why landlords should strive to maintain excellent relations. Once that relationship is blown, it is hard to get it back. “If landlords are good at these relationships, they can keep a tenant even if the company is paying a slightly higher lease rate in a similar building down the road,” says **Richard Mason, SIOR, IIM, RE**, a managing partner with Cardinal Partners in Charlotte, N.C. “How well a landlord handles the problems that turn up is a lot more important than many landlords realize.”

During the heart of the downturn, one of the bigger deals in the Charlotte market was a company that leased one million square feet of space because the decision-maker at the

company decided the landlord of its existing building wasn’t professional enough.

One of Culbertson’s clients, a national insurance company with 31,000 square feet of space, relocated because the manager’s car was broken into and she never felt the property manager directly addressed the problem nor gave her confidence the property was safe. “Resentment built up and eventually the company relocated,” Culbertson says.

Be proactive. Culbertson points out that it definitely helps relationships if the landlord takes the time to understand his clients. Culbertson gives this very simple example—many new tenants are small, up-and-coming tech companies, which tend to use less paper, need smaller desk tops but crowd more people into leased spaces creating high occupancy ratios.

“One of the things we realized early on,” he says, “was that if you increase occupancy of the building by 30 percent, not only do you need more parking, but usage is far harder on mechanical systems, and surprisingly, plumbing. If you have more people in the offices than originally designed you need to put in higher quality toilet and plumbing equipment.”

Levin in Washington, D.C., takes the adage, “get to know your clients,” one step further. In his world, most office tenants fall into one of three categories, law firms, trade associations, or non-governmental organizations. While technically all tenants should be treated equally, in reality different needs mean different responses.

For example, economic pressures have dramatically changed the law firm world. The firms want to be in well-appointed buildings where they can attract and retain good talent, however, the local law firm is being squeezed.

“The days of the 300,000-square-foot partner offices are gone,” Levin says. “Law firms are looking to get more efficient, perhaps with 25 percent less space. In second generation buildings they can’t get more efficient, in newer buildings with smaller floor plates, they can. Landlords have to be creative to keep existing relationships with law firms.”

It’s also tough to keep trade associations as the new preference is to be near Capitol Hill because of the lobbying they do. They want to be close to the members of Congress. The NGOs don’t usually take up a lot of space, so as Levin points out, “the smaller non-profits just want to be valued and not treated as a blip on the spreadsheet. A lot of institutional owners don’t have the ability to do that, but they should.”

Finally, all successful landlords and property managers stress the fact that there should be good communication and contact between the tenant and whoever is managing the office or industrial property.

Communication starts from the very beginning of the process, or as **Richard Mason, SIOR**, principal and owner of Pla

TIPS FOR KEEPING A HEALTHY INVESTMENT

□ **Geenty, SIOR**, principal in The Geenty Group Realtors in Branford, Conn., has owned, with a partner, a business park in the Connecticut town of Old Saybrook. Geenty has kept the eight-building, 240,000-square foot park for 27 years. On average, the business park rarely shows more than 3 percent vacancy, but last year there were a number of downsi gings and the vacancy rate shot up to 30 percent. A number of new tenants will reduce that aberration. The Old Saybrook Business Park has a facilities manager on the grounds of the property. Below are Geenty's suggestions for keeping a property a healthy investment □

□ Facilities manager has daily contact with tenants. In addition, both owners visit tenants at least once a year.

□ Tenant recognition program. Often an annual party. Sometimes, it's nothing more than having the local Good Humor truck come by and deliver free ice cream sandwiches.

□ Maintain landscaping. Pruning of shrubbery can be important to tenant feelings of security as over-grown shrubbery gives miscreants a place to hide.

□ Maintain building and grounds. Activities should be scheduled regularly, i.e., parking lot is re-stripped every three years, steel exit doors repainted every three years to prevent rusting.

□ Beware of copper thieves by installing exterior video cameras to deter thieves. Each roof-top HVAC can be wired for an alarm.

□ Lease expirations and upcoming option renewal dates should be in a "tickle" file so either situation can be addressed ahead of time.

□ Through active communication, anticipate if a tenant is going to expand or contract. Be flexible and try to retain the tenant that may be contracting.


• Maintain cash flow. If the rentals are not in the office before a certain time frame prior to expiration of the grace period, call the tenant as a courtesy to make sure that the rent is received before the deadline to avoid the onerous later fee, of, for example, 10 percent.

Commercial Realty in Columbia, Mo., likes to say, "to me a healthy property begins when you secure the tenant," to which he adds, "when you have frank discussions at the beginning, it is usually carried through."

Two areas of contention that come up, Land suggests, are the occasional tenant who doesn't pay rent on time, and in the triple-net world, tenants who don't live up to their end of the contract. Sometimes the problem is with the landlord, who is just not paying attention.

"Occasionally, a client will tell me, 'I have this great triple net property.' And I say, 'have you driven by it recently?' 'You have trees growing out of your gutters.' Triple net is only a good property if your tenant is actually taking care of things. If not, then you need to remind them of their responsibility or take it on and figure out how to bill it back to them."

As for being late on payments, it's much easier to solve this problem if everyone is communicating with each other. "If the tenant starts to struggle and calls up to say, 'my industry is changing, I have a problem, but I have a plan as to how I can succeed,' you can work with that tenant," says Land. "If the tenant doesn't communicate and just keeps getting later and later in rent payment, that's a different situation."

He adds, "It's ama zing how many times I have had landlords come to me and say, 'this guy is four months behind in rent.' I say, 'have you had any conversations with him?' The answer is no. So, I say, 'do you think the tenant is just going to wake up on the fifth month and pay you the other four months?' The minute the tenant is three days late or 10 days late or whatever your comfort one is, you need to be in communication." 

ABOUT THE AUTHOR



STEVE BERGSMAN is a nationally recognized financial and real estate writer. For more than twenty-five years, he has contributed to a wide range of magazines, newspapers and wire services, including the New York Times, the Wall Street Journal Sunday, Global Finance, Executive Decision, and Chief Executive.

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