



Review Real Estate Leases for Possible Savings



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As the economic downturn lingers, business leaders find themselves repeatedly scrutinizing budgets. Hoping one more round of cuts will give them the cash they need to weather the storm, they separate spending plans into two categories, set aside fixed expenses and dive into variable costs looking for a few more dollars to trim.

Unfortunately, with that initial separation of fixed and variable expenses, some businesses mistakenly set aside a source of potential savings: lease terms. Knowing they're multi-year contracts, businesses assume these agreements – and the costs associated with them – are not open to review.

Savings often can be found, though, if not in the bottom-line cost of the lease, then in some of the associated expenses. What's more, in discussions with your landlord, you might find opportunities for mutually beneficial changes. However, you're unlikely to discover any of these opportunities without a thorough review of your lease agreements.

Act now

Too many businesses sign leases and then ignore them until a few months before the termination date. While they routinely review other long-term agreements and make changes, they overlook the opportunity to submit leases to the same kind of critical assessment.

The problem with this approach is that it assumes the most basic component of a lease agreement – cost per square foot – is the only component with a bottom-line impact. But this mindset overlooks a variety of factors – from space usage and efficiency to operating expenses – that also could affect your lease expenses.

To avoid taking a narrow view, conduct a full review of lease terms, assess your organization's true cost of occupancy and, with that information in hand, consider changes that could boost your cash position.

Take a walk

Contrary to what you might be thinking, this doesn't mean you should immediately sit down to re-read your lease. For now, put aside the paperwork, grab a notebook and take a walk through your space with your real estate advisor.

On this tour, you'll want to look at such things as how efficiently space is being used and, if you're in a multi-tenant building, your use of shared areas. Make a list of such things as building amenities that could factor into your cost, or needed upgrades.

Don't just look at your interior space, though. Consider how exterior areas work for your organization. Have changes in your business affected your needs in terms of access or location? Do you have the right amount of parking or delivery areas?

In considering these and other factors, you'll then ask yourself a final question: How does the overall space fit with your plans and outlook for the future?

Dive in

Now it's time for you and your advisor to dive into the lease itself, reviewing such factors as the space you're renting compared to the amount of space you actually use. You'll consider whether you're paying for unneeded storage spaces, common spaces or amenities.

You'll also want to review the section of the lease addressing operating expenses. These are expenses – such as taxes, utilities, etc. – that are passed through to you directly by the landlord. Typically, a base for these costs is set when a lease is signed, but changing conditions could warrant a change in that cost.

Other factors that won't deliver an immediate bottom-line impact but could offer value in other ways would be the timing of the lease (What's the end date?) and flexibility (What are the terms for breaking or extending the lease?).

Do the math

So, you've walked through your space and reviewed your lease, and you feel confident that reasonable lease adjustments could save you money. Maybe you think it's time to leverage your market power and seek a new space or negotiate lease changes. Before you pick up the phone to talk to your landlord, though, consider other factors that could affect your decision: the cost of making a move, or the cost to your landlord of keeping or finding a new tenant.

Initially, it might seem like relocating your office is the obvious choice. You could find a lower rate and get signing incentives from a new landlord. But don't make that choice without carefully reviewing other costs associated with a move – from the price of moving a firm to the costs resulting from workplace disruption.

Give and take

So how does all of this work in real life? Consider the case of an area trade association. Among other things, a lease audit revealed that the association was paying for storage space it no longer needed, and also for unbudgeted overages in operating expenses.

At the same time, the association recognized that it would be interested in staying in the space beyond the current lease terms, and that the space would not need updates any time soon. Although its lease was not set to expire for two more years, the association took these matters to the landlord.

What the association discovered was that the landlord was more than willing to discuss the lease. The two sides arrived at mutually beneficial terms, with the landlord agreeing to remove the storage space from the lease with no penalty, and to update the "base year" for operating expenses. In exchange, the association agreed to extend its lease for five more years, and to defer improvement allowances.

The bottom line? The association lowered its lease cost by 20 percent over the remainder of the existing term.

The key to all of this is not to wait until your lease term is coming to a close to review your lease options. After all, if you shop for something only when you absolutely need it, you won't get the best deal. However, if you shop around without the pressure of a deadline, you put yourself in a position to leverage market conditions and opportunities to get a better deal.