

THE FINE PRINT

A COMMERCIAL REAL ESTATE NEWSLETTER FOR LEGAL PROFESSIONALS

Overhead Overruns?

10 Steps to Reducing Occupancy Costs for Law Firms

By Tom Doughty - Colliers International

Faced with rising payroll expense and increasing investments in technology, law firms should consider revisiting, rethinking and retooling their approach to real estate. Since occupancy costs remain one of the largest expense items for most firms—second only to payroll—the implementation of a strategic real estate plan can yield significant cost savings and potentially turn an expense into a competitive cost advantage. The following 10 steps are designed not only to reduce long-term occupancy costs, but also the amount of management time involved in the decision-making process.

1. Prepare early. Law firms should review their options as far as three to five years in advance of lease expiration.

With office space at a premium in many markets, early preparation can provide leverage in lease negotiations in landlord favorable markets. The extra time will allow for a review of creative alternatives such as a broadened geographic search, and consideration of non-traditional opportunities like building rehabs and build-to-suits. In addition, in those markets with rapidly rising rents, it may be advantageous to renegotiate lease terms at the earliest possible date to lock in a lower rate.

2. Designate a team. Create a real estate advisory team consisting of the firm's business manager and real estate professionals.

The ideal real estate team has both internal and external members who understand the long-term business goals of the firm. External members should include brokerage, design, project/construction management, and facilities management professionals. Having experts on board who share the firm's long-term perspective, rather than hiring advisors for

a single transaction, leads to optimized real estate transactions. In place relationships also reduce delivery time for new or ongoing real estate requirements.

3. Organize documentation. Maintain current and complete copies of your leases with all amendments and annual records of rent and pass-through statements.

Organizing your lease documentation is the first step towards developing a lease administration system. For a firm with multiple offices, it allows for better oversight of the entire portfolio and a method to ensure that expenses are appropriately calculated and attributed. A lease administration system assures that payments are made regularly and that important option dates and expansion opportunities are not missed. As many firms have found from painful experience, the costs of missed option dates can be significant.

4. Develop standards. Develop prototypical office specifications with universal planning modules based upon standardized dimensions.

Creating a firm-wide standard design for office layout and furnishings not only solidifies a company's image, but it reduces design costs and expansion delays. Agreed-upon standards eliminate internal negotiation and politics as to office size and space allocation, and provide a basis for making accurate cost projections for new satellite offices.

5. Know your costs. Complete cost segregation studies to isolate the true depreciation life of individual facility components.

After-tax cash flows can dramatically increase with accelerated depreciation of assets. Many firms are

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writing off categories of improvements on much longer schedules than necessary, missing opportunities for improving the firm's cash flow.

6. Know the market. Maintain updated market information for all firm locations. Compare your costs to those of local, regional, and national competitors.

Keeping on top of developments in all markets where a firm is located can highlight short-term changes and longterm trends that may affect rental rates. This practice may also present opportunities to capitalize on shortterm market imbalances that can be advantageous in achieving a more competitive cost structure than competing firms.

7. Keep maintenance records. Maintain an updated list of facility repairs, maintenance costs and capabilities. Identify problem locations and document frequency and repair costs.

This practice provides a valuable archival record of a firm's true occupancy costs, as well as highlights capacity or deficiencies in the firm's facilities (e.g., mechanical, electrical, voice/data wiring). These records also create valuable negotiating leverage for maximizing future space improvements and rental rate terms with landlords.

8. Perform annual audits. Audit lease payments, operating expenses and real estate tax payments on an annual basis.

By reconciling statements on an on-going basis, a firm is more likely to identify inaccurate calculations or payments. The allocation of office building expenses is an art and not a science. Therefore, it is in a firm's best interest to negotiate aggressive audit rights. Further, law firms should consider negotiating up front for the right to appeal real estate tax assessments independent of the landlord. A firm's assessment of the basis for appeal and the likelihood of success may be quite different from a landlord's.

9. Track commuting patterns. Map employee and client locations at least every two years to highlight shifts in demographics.

By regularly reviewing commuting and residence locations of employees and significant clients, opportunities to relocate facilities to more convenient, and potentially lower cost submarkets will become apparent at an earlier date. A regular program of monitoring client locations will also identify the need and/or potential for opening or relocating branch or satellite offices in strategic client locations.

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10. Target flexibility. Make flexibility the critical goal in all lease negotiations by including liberal subleasing provisions, early terminations, renewal, and extension options.

Since even the best laid plans can change, incorporating as much flexibility as possible into leases will give a firm the ability to expand and contract its inventory of space under lease to correspond to the ebbs and flows of its personnel. In addition, termination options can provide an opportunity to renegotiate lease terms when more favorable market conditions exist.

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If you would like more information regarding Colliers International's Legal Resource Group in Portland or any of our comprehensive real estate services, please contact Senior Vice President Gordon King at 503-223-3123.

The Fine Print is a newsletter published periodically on topics of interest to those in the legal industry responsible for office space acquisition and management.

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