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Real Estate Best Practices: What Companies Doing Business with the Government Should Know Structures

Find space close to where I live. Keep the rent low. Do a short term because I'm going to grow. Sound familiar? Each of the above are well known goals for technology and government service companies faced with a real estate decision. Many view their real estate as some type of chore that comes up every few years that they simply want to get out of the way so they can go back to running their business. However, companies seeking to adhere to best practices should consider how multiple aspects of real estate impact their business.

One of the initial considerations for any executive is lease versus buy. For any company, all of the classic reasons for owning (building equity, depreciation, fiscal and operational control) are initially attractive, and the problems include minimal flexibility, initial investment and property management responsibilities. For government contractors, the Federal cost standards and practices may pose additional challenges regarding restrictions on passing through certain rental costs as reimbursable or allowable expenses when financed ownership of the underlying asset (building or space) is present.

Emerging companies face additional pressure to implement prudent business practices. Depending on the company's growth strategy, the contractor may be seeking a mentor-protégé relationship, outside funding or an acquisition. Each of these strategies will cause the company to thoroughly examine business practices, including those pertaining to real estate. Subcontractors are subject to audit by their prime contractors, and overpaying in rent (particularly when the company executive is the landlord) may raise concern.

However, there's far more to analyze than rent to properly assess the prudence of a company's real estate. While a good accountant can determine how appropriate real estate costs are for a particular company and a good attorney can provide guidance on the ramifications of legal clauses within a lease or contract, a commercial real estate broker focused on the area and the industry can benchmark all aspects of the company's facility solution to the market to ensure that the company is observing sound strategic, financial, operational and cultural best practices.

Strategically, companies should consider their short and long term growth strategies in determining the proper lease structure and flexibility requirements. Expansion, contraction, renewal and termination options all have value for emerging companies. A termination right may be attractive for a potential acquirer, and a renewal right can insulate a company from market pressures and avoid a disruptive relocation. At the same time, contraction options mitigate losses from unsuccessful contract bids and provide a cost-recovery mechanism when employees are pulled to customer site locations, while expansion options can allow the company to grow while minimizing operational disruption. Companies should also view their facility as a strategic marketing tool, especially if customers and partners visit them. Building signage and customized build out will add to expenses, but may satisfy a strategic objective that can pay dividends over time. There is also a flip side to this in that sometimes presenting a "humble" appearance resonates with your customer signaling that you are a prudent manager and not one charging them too much because you live in a "high rent district".

The financial implications of a facility go beyond the rental rate. Examining the optimal working environment is key prior to getting started. Evaluating alternatives such as private offices, open workstations, or some combination will have an impact on the amount of space required which naturally translates into the overall cost. Oh, and don't forget the furniture. Many a budget has been blown when not incorporating this component into the space configuration and cost decisions. Make sure they are line items in any comparison matrix you use to select your facility.

On the operational side, performing due diligence on facility options is important to ensure that the company conforms to all government security requirements and provides for an efficient flow between business units. Certainly, companies leasing space for government employees per the provisions of a contract must adhere to government facility requirements, but contractors themselves are facing increasing security requirements under the Unified Facilities Criteria. Standards such as redundant systems, Secured Compartmentalized Information Facility (SCIF) space and access controls are not uncommon for companies managing sensitive information for the government. In addition to security requirements, the company should organize and plan a facility such that it provides the flexibility for growth while keeping key business units together for optimal workflow.

Clearly, fulfilling contracts with employees at the customer site is advantageous to staffing within the facility not only because of lower real estate costs, but there are also other non real estate related benefits such as obtaining security clearances for staff. In some instances it's easier to obtain a security clearance while working in a government facility. For employees servicing contracts that need access to the company facility, shared space (otherwise known as "hoteling") is a more economically efficient alternative to designated space for each employee; however, this cost-savings technique may not align with the company's culture. In an area with only 2% unemployment, companies cannot only focus on financial and operational efficiency to succeed; they must also provide an attractive environment for their employees. With skilled (and particularly cleared) personnel in strong demand, companies need to offer incentives to attract and retain top talent.

Salaries and benefits are one aspect, but offering employees a challenging platform to utilize their skills along with a comfortable environment with the desired amenities can have a strong psychological impact. Something as simple as not having to pay for convenient parking or having a good place to eat lunch can reduce the potentially high cost of turnover.

Real estate can be viewed as a simple exercise of finding space, but more strategic government contractors utilize a process that aligns real estate with their business goals and then benchmarks their solution to the market on a regular basis. Annual operating expense reviews, market updates and efficiency studies are all important checkups to ensure that your real estate is properly positioned to enhance your business.

This article was provided by Mike Norris, a senior associate at Scheer Partners Inc. (www.scheerpartners.com), a leading provider of commercial real estate consulting services. He can be reached via email at mnorris@scheerpartners.com.