

# How to Lease Space For a New Business

By **BARBARA MENDE**

Start-up enterprises can get plenty of advice on writing business plans, choosing Internet services and even buying postage.

But it isn't always obvious how to go about leasing office or retail space. Just finding vacant space can be tricky, while navigating leases can seem like learning a foreign language. Further, unlike residential transactions, commercial real-estate prices and conditions on the lease aren't matters of public record.

Still, finding the right place for your business and negotiating a lease are essential to success. In a sense, signing a lease may be "the most important thing" a businessowner does, says Barry Lang-Hodge, general counsel of LILI-CO of Franklin, Ohio, the second largest Domino's Pizza franchisee in the U.S.

Here are some suggestions to simplify the leasing process:

## **Know what you want and need.**

Location hunting isn't simply a matter of finding an attractive space. Is it convenient for your employees? Are you paying for amenities you don't need? Are there nighttime-security issues? Can you expand if you grow faster than expected? Can you negotiate over remodeling expenses?

Synergixx, a southern New Jersey marketing and media-production firm, decided to locate near a college so student employees would be available round the clock and could walk to work. Tony Fusco, its chief financial officer, found a property in Glassboro, N.J., home to Rowan University.

"We figured out how many people we'd need at one time, how many square feet we'd need for each cubicle, a secure place for the telecommunications, bathrooms and storage areas. It came out to 1,500 to 2,000 square feet, so we got an 1,800-square-foot place."

Mr. Fusco also kept his eye on budget issues. "Entertaining clients would have meant a much dressier center," he explains. "We decided we usually went out to meet our clients and didn't depend on walk-in business." And he checked out the owner with other tenants. "I tried to find out whether there was a big turnover. There wasn't. The people who had been in my unit were there for 10 years."

Unfortunately, some prospective customers hesitate to tell their brokers their top price. "They think if they tell a broker what they can afford," that's the figure the broker will meet, says Toby Frymire, executive vice president of Windsor Realty Group Ltd., a commercial/industrial brokerage in Blue Bell, Pa.

## **Assemble a leasing team.**

Professionals can help, says Michael Permack, president of the Alberta, Canada, branch of Addison, Texas-based Staubach Co., which represents users of commercial, industrial and office space. A commercial real-estate expert can provide negotiating skills as well as guidance on making a space fit specific business needs. For example, one Staubach client wanted to start small -- 1,800 square feet -- but eventually expected to need 30,000 square feet, so a site capable of major expansion was necessary.

Mark Anthony McCray, a marketing professional with offices in Austin and Houston, Texas, has been both a landlord and a tenant. He stresses the need to have a broker experienced in commercial transactions. A friend who was a residential agent helped find Mr. McCray's first investment property and "it took us three times as long to locate property that fit our needs because we were learning as we went along," he recalls. Experienced agents can help deal with pre-existing commitments on properties, locate unlisted properties and provide advice.

Brokers often specialize in certain types of property -- suburban industrial, for instance -- says John Smiley, owner of Leasecraft Leasing Solutions of Calgary, Alberta, which analyzes and negotiates leases for clients across the U.S. and

Canada. Prospective tenants can end up making several cold phone calls or visits trying to learn about prospective sites, he says, but a well-informed agent "can eliminate most of those spaces right off the top."

How do you choose a brokerage? "Call a few companies and check out their references," says Mr. Smiley. "Talk to your friends, or join the chamber of commerce and talk to people there."

Mr. Lang-Hodge notes that brokers may have conflicts of interest. Agents typically get a commission equal to 6% of five years' rent. "The higher the rent, the higher the commission," he notes.

One alternative is to engage a tenant representative or lease consultant to help you negotiate, working on commission or for consulting fees. These professionals have expertise that may, for example, help you win favorable terms for possible expansion, have the landlord to take on more of the renovation costs or complete the documentation.

And if leasing terms are complicated, you may need an attorney and an accountant to help evaluate lease provisions.

### **Understand commercial leases.**

"You can learn about [available] space on a lot of Web sites," says Mr. Permack. "What you can't get are the details of the transactions. You may find out that someone paid \$15 a square foot, but not that they also got a lot of cash inducements." Mr. Frymire suggests visiting several spaces, including some that are already leased, to gain knowledge about going rates.

Proceeding without such research "is like going to Wal-Mart and looking on the shelves and not being able to see what's in the boxes," says Mr. Smiley.

Perhaps a new tenant's biggest problem, says Mr. Frymire, is failure to understand the different types of leases.

In a gross lease, you pay a flat amount per square foot, and that number may increase annually based on a fixed amount or the Consumer Price Index. Or you might have a "triple net lease" where the payment is net of taxes, insurance and common-area maintenance. Tenants are billed separately for those items, based on the percentage of the premises they occupy. "In office spaces, it may equal the basic rent," says Mr. Lang-Hodge.

There are many variations. Triple net costs might be allocated on the basis of leasable area, or area actually leased - which would increase your cost in a mostly vacant building. Some landlords charge management fees, usually 15%, on top of triple net costs. It's even possible you're assessed all of a building's costs if you were the only tenant and the rest was vacant.

"Get the shortest lease possible," says Boston attorney Jeanne Cosmos. "If you're a start-up, you don't know where you'll be in three or five years." In addition, Mr. Frymire points out, company owners may have to sign personally on the lease and may not want large obligations on their books when they look for financing. Tenants expecting to expand may want a location with a great deal of similar space they could conceivably move into.

Landlords will want to raise rates on short-term leases, but because they don't want the hassle of looking for tenants, "you might get better rates than you think," Mr. McCray notes. "Landlords will give more concessions on price, repairs, contracts [and] amenities than most tenants ask for."

Tenants who don't study their leases thoroughly can be surprised, says Mr. Lang-Hodge. "Suppose you started a small retail shop, renewed your five-year option, and after a year you want to sell out. Then you find out you can't sell your business because the landlord has the right to keep you from assigning the lease."

### **Negotiate, negotiate, negotiate.**

With so many lease variations, there's ample room for negotiation. One of the areas is interior construction. "Say there are two deals -- one at \$15, one at \$18" a square foot, says Mr. Smiley. "If you got \$15, you may think you got a better deal. But the guy who paid \$18 may have gotten a \$30 [per square foot] allowance" to pay for needed improvements.

Construction needs, Mr. Smiley points out, are highly individual. "A lot of offices need a couple of corners and a lot of windows. If there's only one executive office, you may need to do a lot of construction." Construction costs built into the

rental rate won't show up as loans on the company's balance sheet. In this sense, he says, it's often beneficial to "use the landlord as a bank."

Mr. Lang-Hodge notes that some leases provide that tenants who have ever been in default lose all their other rights. "If you thought you had an option to renew, but you were late with rent once in your second year, you may not have that option," he says. He says he makes sure to include wording in the lease that says the tenant shouldn't then be considered in default and therefore would still be able to renew.

He also recommends that retailers negotiate exclusivity clauses to ensure they'll be the only business of their type in the building. "If you have a small pizza shop in a strip center, you'd like to know you'll be the only one."

In his negotiations, Mr. Fusco requested a dumpster, and the landlord proposed to get one for the building, with every tenant contributing a certain amount. "I told him I could get one for much less [than the landlord was going to pay], so we negotiated," says Mr. Fusco. They even negotiated who changed the light bulbs. "We agreed that we'd do the regular ones, and he'd do the fluorescent ones."

### **Consider alternative arrangements.**

Professionals and owners of very small enterprises, according to Mr. Smiley, have special problems: "There's never any [space] small enough for one or two people." However, he says, already-outfitted executive offices "are a fantastic option for individuals." Professional-office buildings, which are rarely in downtown locations or areas zoned for business, may work for professionals, but businesses often aren't allowed to rent space in them.

"We leased space in a small-business incubator," reports Detrick DeBurr, a Dallas information-technology consultant. "The paperwork was a little more than normal, and we had to follow a few more rules, but the cost savings more than made up for any inconveniences."