Commercial Guide

Looking to open or expand your business in office or retail space, or just curious about opportunities to invest in commercial real estate? We at CORE have extensive experience in the world of New York City commercial real estate and are available to assist you. This guide touches on some key topics within the commercial arena.

OFFICE OR STORE VS. APARTMENT

How does an office lease or store lease in New York City differ from an apartment lease?
Office leases are typically for a minimum of 5 years and can stretch to terms of 15 or 20 years. Retail leases are most often for 10 to 15 years. Shorter term sublease office spaces are often available as are "pop-up" brief retail leases.

The typical tenant protections enjoyed by residential tenants may not apply to commercial tenants.
For example, there is no such thing as a rent-controlled or rent-stabilized office or store tenant. Unless a commercial lease contains an explicit tenant renewal option, a landlord is not obligated to extend the lease term for an existing tenant beyond the lease expiration date specified in the lease. The landlord can increase the rent a commercial tenant pays by whatever the market allows upon the expiration of a lease.

For office tenants in New York, the square footage for which a business pays rent can be 30% - 40% greater than the square footage on which carpet can be laid and furniture installed.
Rentable square feet for office space in New York City typically reflects a "loss factor" while retail space generally is marketed and leased on a usable square foot basis. Generally, loss factors are higher for partial floor office spaces than for full occupancies, because common areas like corridors, elevators and lobbies are apportioned on divided floors into each tenant's square footages. This means full floors are generally more efficient and cost effective than partial floor occupancies.

WHAT DOES A COMMERCIAL BROKER DO AND WHO PAYS A COMMERCIAL BROKER'S FEES?

When working with a tenant, commercial brokers identify space availabilities to meet a tenant's requirements (location, accessibility, size, cost and amenities), model the financial implications of a commercial lease, negotiate business terms with landlords and participate in the lease negotiation coordinated by attorneys for the tenant and landlord.

Commercial brokers can also represent landlords in positioning and marketing available space and negotiating lease transactions.

Brokers also work with buyers of user and investment commercial property to identify acquisition opportunities and negotiate purchases of commercial and mixed use buildings and office and retail condominiums. Owners of these assets are also typically represented by commercial brokers in marketing them for sale.

Generally, all brokerage commissions are paid by owners (landlords), even to brokers who are exclusively representing a tenant. The major exception is in the acquisition of buildings where an owner selling a commercial asset only pays the broker who represents him or her and the buyer's brokers are compensated by buyers.

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GO-TO EXPERTS

In addition to a commercial broker, there are a range of professionals involved in commercial transactions and occupancy planning. These include:

- Real Estate Attorney
- Architect
- General Contractor
- Furniture Vendor
- IT Consultant
- Movers

IF I LEASE SPACE, HOW DO I KNOW I AM NOT PAYING TOO MUCH RENT?

A broker may provide relevant lease or sale completed transactions ("comps") and analyze the terms of a potential transaction in light of recent comps and historical market trends and forecasts. The magnitude of landlord concessions (tenant improvement allowance and free rent) in office or retail leases as well as a tenant's credit worthiness will also impact the negotiated lease rent.

In addition to rent, a commercial tenant typically pays for electricity according to a direct meter, submeter or on a rent-inclusive basis. Office and retail leases are generally "gross" leases which means a tenant rent includes the tenant's share of building operating expenses and taxes in the first year of the lease term. After the first year, tenants typically pay a "tax escalation" which is their proportionate share of increases in the building's taxes above the building's taxes in the first "base" year of the lease. Tenants also pay either their proportionate share of increases in the building's operating expenses above the "base" year operating expenses ("operating escalation") or pay fixed annual increases compounded over the base year's rent in lieu of an operating escalation.

WHY IS BUYING RATHER THAN RENTING OFFICE OR RETAIL SPACE NOT ALWAYS PREFERRED?

It may appear particularly attractive for many businesses to purchase an office or retail condominium, rather than leasing space because an owner would then never face increases in rent (though other occupancy expenses typically increase such as utilities, taxes and maintenance charges). However, in New York City, there are factors that may make leasing space equally or even more attractive than purchasing:

- Availability of office and retail condos is extremely limited in New York City and a space's accessibility to talent or visibility to customers may prove more important than how a space occupancy is financially structured.
- A business's capital invested in a condominium is not available to be deployed to otherwise support working capital and business investment.
- Commercial condominiums are relatively illiquid and do not typically provide the flexibility of leased space in which a tenant may negotiate to expand or contract its occupancy depending on business needs.
- Condo owners are typically responsible for the expense of all renovations, while tenants may negotiate lease concessions to offset renovation expenses or negotiate for a landlord to build or modify a space installation entirely, or partially, at the landlord's expense.

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WHAT IS A CAP RATE AND WHAT DOES IT MEASURE?

A cap (capitalization) rate is the rate of return for a real estate investment based on the net income the property is expected to earn. A cap rate is calculated by dividing the net operating income (NOI) by the property value. The NOI is the annual income of the property less expenses. The cap rate is usually expressed as a percentage and makes it easier to assess and compare potential investments. Cap rates across most real estate asset classes in New York City have dropped since the Great Recession, as interest rates have remained low and property values have generally increased. The cap rate is a popular tool for evaluating different real estate investments, but it should not be the sole factor particularly when making longer-term investments where growth or decline in income and property value should also be assessed.

WHAT IS A 1031 TAX FREE EXCHANGE?

Under Section 1031 of the United State Internal Revenue Code, the exchange of certain types of investment property may defer the recognition of capital gains (or losses) and therefore defer any capital gains taxes otherwise due. To be eligible, the properties exchanged must be "like kind," i.e., of the same nature or character. The property to be exchanged must be identified within 45 days and received within 180 days. 1031 Exchanges provide a potentially powerful and unique tax benefit to real estate investments.

WHERE ARE THE FASTEST GROWING TECHNOLOGY AND CREATIVE FIRMS CHOOSING TO OPEN THEIR OFFICES IN NEW YORK CITY?

Recently firms as diverse as Hewlett Packard, Anheuser-Busch, Red Bull, Cadillac, Unilever and Amazon have established new significant occupancies in New York City. All chose a side-core, former industrial building ideally suited to create a customized, activity-based and team-oriented office space. In neighborhoods like Chelsea, Tribeca, Williamsburg and SoHo, these firms find accessibility to creative and tech talent in architecturally significant, renovated structures and in neighborhoods with diverse and high-quality housing, shops, restaurants and other amenities.

CORE agents are here to ensure your experience is easy, seamless and positive.