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## Office building landlords hit a wall with renovation plans

*Tight money makes fixing up space to lure tenants tough*

By **STAN BULLARD**

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If a slow economy wasn't enough, here's one more roadblock to swinging real estate lease deals.

Courtesy of the credit crunch, brokers and building owners say credit is so tight that some landlords are unable to secure loans or tap their current lenders for money to redo their offices for new tenants.

In typical broker-speak, a new euphemism is entering the lexicon during negotiations to ink new tenants for office buildings and high-end office-warehouse properties: "Can the owner perform?" That is, can the owner afford to remake the space and cover other expenses involved in setting up the tenant to do business?

"It used to be that you could assume the owner had the funds to fulfill the transaction," said David Browning, managing director of the Cleveland office of CB Richard Ellis. "Now, part of the discussion is, 'What about the money?' It's adding more complexity to the transaction."

Before the global financial crisis, a building owner could go to its lender for money to gut and remodel space for a new tenant because it would add value to the property. Or, the owner could win a loan to finance the improvements based on the strength of the tenant's credit. No more.

"There are certain owners that, because of the situation with their lenders and reduced occupancy, they cannot get funds to do a major transaction," said Mr. Browning, who would not identify the local haves and have-nots.

David Hales, a partner in the real estate unit of the Calfee Halter & Griswold LLP law firm, said if the amount of money needed for renovations is just \$15,000 to \$25,000, there's generally no problem.

However, if a new lease for a 10,000-square-foot tenant requires \$200,000 to \$300,000 to renovate the offices, "That is a problem," Mr. Hales said.

Mr. Hales says the American Recovery and Reinvestment Act passed earlier this year to stimulate the economy may offer hope. It allows for more U.S. Small Business Administration loans for what are known as "office buildouts," but the spigot for such loans is not yet open.

The push for new tenants is not the only area of the business feeling pangs from the lending shortage; so are existing tenant-landlord relationships.

Michael Cantor, chief operating officer at Allegro Realty Advisors, a Valley View realty consulting company, said tenants often use a weakening market as an opportunity to renew their leases at a lower rent and, as a sweetener, to get the owner to redo their offices.

"This presumes the landlord has the capital to make the deal," Mr. Cantor said. But because of the current credit situation, the typical bargain-hunting opportunity is not always available because some landlords are reluctant to fund — or can't fund — such improvements.

## **Beware of the shark**

A prominent Northeast Ohio real estate developer who discussed the situation on grounds he isn't identified said the difficulty landlords face in securing money for building improvements is as serious as the lack of funds is for new developments, just less visible.

"If loans are available, the (fees) are so high it's not lending — it's loan-sharking," the developer said.

However, because owners need to fill empty space, they find ways to do deals, the developer said. In one case, he said, his company agreed to pay the interest on expenses that its contractors incurred creating offices for a new tenant.

"The contractors were very happy for the work," the developer said. "That's what this is taking."

More common approaches to securing new tenants are for owners to give a tenant more free rent as a lease concession, especially if the tenant can fund its own space improvements, or to get by with minimal low-cost or cosmetic improvements.

Rico Pietro, an office broker at the Cresco realty brokerage in Independence, said the situation puts a premium on finding existing offices that fit tenants. The last few years, tenants often would redo new offices to meet a corporate standard, because financing wasn't a problem.

Now, the as-is deal is king.

James Streff, president of HSB Architects and Engineers, said his firm is doing more designs for new offices than it was earlier in the year, though it isn't yet clear how many of those plans will go through to completion with inked deals.

"We've heard it's a problem from (building) owners," Mr. Streff said. "But I think the owners will find a way to get a deal done if it's a good deal."

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