

SMART START



## THE SCIENCE OF SECURING OFFICE SPACE

*Six things to consider before signing a lease.* BY DAN GONZALEZ

It may not get much press, but real estate is the second-highest cost for most companies. Decisions based only on short-term needs ("Let's get this space now—it's pretty cheap!") can cripple long-term growth. To avoid this ready-fire-aim thinking, follow these steps to make sure any potential office space supports your startup's long-term vision.

### Develop benchmarks

Benchmarks will help you set cost controls. How are competitors using their space now, and how will they in the future? How much space do they allocate per employee? This can range from 125 square feet per person for a call center operation, to an average of 200 to 250 square feet per person for an open plan layout with work stations. What are they paying per person per square foot? Most of the renowned technology markets have a shortage of space, so rent costs may not be easily negotiable (see "The Going Rate," p2).

Nonetheless, rent costs may not be the most important factor in relocation for startups. Consider two buildings; one in a suburban area with a lower cost per square foot, and one in an urban location with a higher cost. If the lower-cost site is not as accessible to customers and staff, does not convey the impression of a dynamic company, and does not offer room for expansion, then the lower cost becomes insignificant.

### Make your real estate support your business goals

If going public or getting acquired is your exit strategy, your balance sheet should have

as few liabilities as possible. This means you shouldn't try to purchase your own building. A surprising number of startups think it is better to "build equity" in the business, but this instead may tell investors and suitors that you have debt that needs to be serviced.

### Look for buildings with local landlords

Many buildings are owned by pension funds, real estate investment trusts, and other conglomerates. The primary goal of these landlords is to increase the value of the asset, so they generally have less motivation to help a local startup with fluid needs such as expandable space. Local landlords offer a greater chance for personal and regular interaction, and they may be more willing to negotiate for concessions such as a renovation.

Still, even a local landlord must be comfortable with your startup status and ability to make payments. You may need to offer a letter of credit, a personal guarantee, or an annual escalation in rent in exchange for a lower security deposit. Have these tools ready and begin the process long before you need the space.

### Know your technology needs

Fiber-optic networks and telecommunications providers are critical for many startups, so be wary of "riser management." (Risers are the conduits that carry wires from floor to floor and to each tenant's suite.) Companies such as Hotwire, Allied Riser, and OnSite Access pay building owners for access to these risers, then sell

their services to the tenants. Landlords, therefore, can limit access to a few providers, so know the policy on this and whether you have roof rights for antennas and satellite dishes. If mission-critical systems will go into the new space, know how dependable the power source is. Check with the local utility to see how often the power goes out, and determine whether a backup generator is available. Also, find out if the suite has enough power. Today's tenants need about six to eight watts per square foot.

Since startups often operate during non-traditional business hours, they'll have to pay extra for heating, ventilation, and air conditioning (HVAC). Some hours may be complimentary, but there should be caps on the additional costs specified in the lease. Additional HVAC could, based on the location, be anywhere from \$25 per hour to several hundred dollars. So if you occupy 10,000 square feet and use an average of two hours additional HVAC five days a week, then you are paying an additional \$2.40 per square foot per year, or \$2,000 a month.

### Negotiate for a lease that gives maximum flexibility

For a startup that expects to double in size in one or two years, signing a five- or 10-year lease is a surefire way to put a kink into the growth plan. If you can't get an ideal lease term, be sure to include clauses for subleasing, termination and renewal.

Subleasing part of your space now is a great way to ensure you get the extra space



you will need later, and it boosts cash flow. The best sublease clauses have no conditions, such as having the landlord approve the subtenant. Termination clauses let you out of the lease if the landlord can't provide expansion space, for example. An option to renew a lease is also critical, especially in low-vacancy markets where a landlord could otherwise force you to leave and lease the space at a higher rate. Have parameters specified in the clause so rates can't be doubled or tripled.

Another critical area in all leases is the default section. Landlords can use this to cite tenants for infractions and make them move. Penalty language should be limited to quantifiable damages such as nonpayment of rent or failure to carry insurance, not subjective offenses such as leaving lights on or parking in a reserved spot. And there should be a reasonable time allowance to remedy the defaults.

### The Going Rate

Office space is scarce in almost every high-tech mecca, and that means startups face hefty lease rates. Here's what it costs to set up shop in some of the country's most desirable high-tech addresses.

(All rates on an annual basis)

#### Austin, Texas

Loop 360, \$27.50 per sq. foot

#### Boston area

Cambridge, \$35 to \$40 per sq. foot

Western Route 128, \$24 to \$34 per sq. foot

#### New York City

Silicon Alley, \$27 to \$33 per sq. foot

#### San Francisco

South of Market (SoMa), \$41 to \$51 per sq. foot

#### Seattle area

Kirkland, \$35 to \$40 per sq. foot

#### Silicon Valley

\$45 per sq. foot

#### Washington, D.C. area

Dulles Toll Road, \$21 to \$33 per sq. foot

Source: CB Richard Ellis, The Staubach Company

### Don't try this by yourself

You're probably not an expert at the accounting, legal, and real estate needs of the business. Tenants should use a team of advisers who know the dynamics of startup technology companies and the real estate market.

These should include executives in real estate, architecture, construction, and data/telecommunication. Your real estate advisers ideally should not have business relationships with landlords; some do, and there can be a clear conflict of interest if they are negotiating with a landlord on behalf of a startup.



### CONTACT INFORMATION:

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