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Transparency Needed in Commercial Real Estate

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Certain words and phrases tend to become quickly overworked and trite in our modern lexicon — so much so that they lose meaning and impact.

Take for example, "buy-in," "face time, "icon" (when used to describe a prominent person), "quintessential," "paradigm shift," "specificity," "revenue-neutral," "vetted," and so many other buzzwords and phrases that people typically misuse and, in many cases, misspell. I won't even venture into phrases such as "give a 'shout-out' to."

But there's one word, used abundantly, that needs to stay in the minds and on the lips of those who are in positions of trust in the private and public sectors: transparency.

We talk about transparency in government and the need to be sure that public policy processes are not carried out behind closed doors and that items on the public agenda are given sufficient sunlight so as to allow members of the public to not only know about the issues, but also comment and advocate on those topics as well.

The same need for transparency carries over into the private sector. The lack of accountability and disclosures within the management of publicly held companies had become so rampant a decade ago that Congress passed the Sarbanes-Oxley legislation that requires public companies to disclose more information about their businesses to their shareholders. The penalty for not doing so has resulted in several CEOs and other senior managers winning a trip to a "federally operated gated community" for a spell.

For all the scorn the legal profession endures, the conduct of lawyers is closely watched by the state bar for any signs of problems with disclosures and conflicts of interest when dealing with clients. Same holds true with accountants and most other professional service providers who have a large impact on their clients' legal and business health.

Sadly, the same level of formal oversight and transparency doesn't apply to commercial real estate, an industry whose product greatly impacts a company's business vitality. A recent article reported that office and industrial leaseholds among American companies exceed $1 trillion. Maybe that's not a lot of money to the federal government these days, but it is a considerable sum in the real world. It's commonplace for companies of any size to obligate several millions of dollars for leaseholds. Real estate space typically is second only to payroll in a company's list of expenses.

While most commercial real estate brokerages are not publicly held and therefore not under Sarbanes-Oxley, the need for real estate transparency hasn't been ignored. About the time that legislation was enacted in 2002, the chairman of the Securities and Exchange Commission, Harvey Pitt, warned: "Directors and managers who continue to turn a blind eye toward real estate conflicts within their organizations are, therefore, taking a grave and potentially very expensive risk."

Pitt's tenure as SEC chief might have been embroiled in controversy, but he was correct in recognizing the conflicts of interest that often arise in real estate.

The obvious question then becomes: How can company CEOs and other senior managers avoid real estate conflicts and other problems that could adversely affect their businesses? A couple of pointers are in order.

- Determine independently and in advance how much your company can and should spend on leasing space for business operations. Keep in mind the impact that technology has on reducing the need for storage and even personnel positions. For advice, consult a source who doesn't have a financial stake in how much space you lease and, more importantly, one who's firm doesn't have a fiduciary duty to help landlords get the highest rent possible.

- Bone up on where your office or industrial space needs to be. All too often, a company will pay an unneeded premium to be located where they want to be, or think they need to be, without analyzing other locations that might well satisfy their needs more cost-effectively. Again, use a company and adviser that have no vested interest in the locations under consideration.
- Compile a list of potential real estate brokers and ask those you're considering to give you a list of their company's business and fiduciary relationships with building owners and property managers so that you can evaluate the extent to which that might affect their ability to show all available properties for lease or to properly represent you in negotiating with those parties with whom they have a financial relationship.

We need and expect transparency at all levels in products we buy and use as well as investments we make. That quality needs to apply to business spaces — where we turn the key to open our places of business every morning.

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