

Medical Office Space “Just What the Doctor Ordered”

By Sam Scaffide, SIOR



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If there is one given in searching for a prescription to take our failing economy out of its present intensive care status, one needs only to first ask the question, “What do people really want more than anything else, and are willing to spend their last dime to get?” The answers are simple: to live longer, feel healthier, and look younger. This is the reason why only healthcare and medical-related businesses and practices have not only come through this recession unscathed, but will act as a catalyst to bolster employment nationwide.

One need only leaf through the want ads in newspapers across the country to see that more than 50 percent of the jobs being offered are related to physicians, dentists, hospitals, healthcare, or medical educational training. What then must we, as SIORs, do to find the right formula to recognize and fulfill their appetite for space? There is no clear-cut answer to this question, but after developing, building, leasing, condominiumizing, managing, or selling more than 20 medical buildings in

four separate office parks within the past five years—and specializing in more than 40 different healthcare disciplines—perhaps I can give you some insight or some guides to follow.

First, get rid of any of those thoughts you may have had that the marketing and leasing of medical office space is no different from that for general office space. They are not the same.

What Factors Make Medical Office Space Different from General Office Space?

- Medical practices follow population growth patterns such as in the development of new hospitals and surgery centers. These patterns create the need for multiple locations.
- Because of the extent and the nature of tenant improvements required for medical office space versus general office space, as well as the time it takes for a medical practice to develop its position in the marketplace, leases of 10 years or longer are not unusual.

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- Dentists and doctors are fiercely independent, slow to react, and difficult to pin down, so be ready to work long weekends and after hours on short notice. However, once you develop a working relationship with, and an understanding of, a particular practice, your efforts will be rewarded because doctors will be more likely to work with you exclusively to represent their future needs and will recommend you to related practices.
- As you continue to gain experience and become market savvy, those existing medical clients or medical park developers may look to you or your firm to market any available spaces they may have or to manage buildings or even an entire medical office park.
- Because doctors and medical groups usually align themselves with hospitals or surgery centers, they are often the early recipients of valuable information concerning discussions and proposals for new hospital locations to be developed. This valuable information will allow you to make early inroads to future leasing commissions or sales commissions on land or buildings.
- It is often stated that 99 percent of doctors, dentists, or medical practices refer you to another doctor, dentist, or medical practice. In fact, unlike general office users, medical users often prefer to locate in the same park, or even in the same building or in adjacent space as those practitioners with whom they share referrals (e.g., a pediatric dentist would like to be near a

pediatric orthodontist or pediatrician, and an orthopedic practice would like to be near a physical therapist or podiatrist).

How Medical Leases Differ from General Office Leases

The terms and conditions of medical leases will inherently differ from those of general office leases. Here's why:

- Medical leases are almost always triple net or absolute net leases.
- Because medical practices are often set up either as a professional corporation or as an LLC which distributes its income to the various partners at year end, they often have financials that are not acceptable and, in almost every case a personal guaranty will be required from either the managing member of the firm or some or all of the individual members of the partnership.
- Preliminary plans may require three or four revisions prior to being developed into full construction drawings. In most cases, medical groups will not be prepared to pay for preliminary plans. But they will pay for final construction plans as part of your final construction budget.
- Both preliminary plans and final construction plans may also have to be forwarded—for approval—to various state and/or federal agencies in addition to any local governmental agencies, particularly if

the practice will require either a Certificate of Need or a Letter of Non-Reviewability—if the practice is going to conduct surgical procedures. Some of these approvals can take nine months to a year.

- Because plumbing is required for exam rooms and other medical equipment-related access, the cost of construction for standard medical office space is usually 20 to 30 percent greater than that of general office space. To save your client money, try to locate in a building where the developer intentionally

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left the floor in a dirt condition so the concrete could be poured after the plumbing was installed. This could save as much as \$75-\$85/linear foot in the cost to cut the concrete. Some practices such as imaging centers require additional electrical and floor support, as well as lead-lined walls.

- Because doctors, dentists, and other medical groups are always in an expansion mode, and because of the initial cost of improvements to their original space, they may request the option to expand into an adjacent space via a right of first refusal.
- Doctors like to own their space and/or their own buildings, so it is important to consider keeping options for growth open and firming up details in the lease so that the terms and conditions are not a point of contention upon lease renewal. Items such as exclusives, options to purchase and right of first refusal are all considerations that need to be discussed at the same time that regular lease terms are being discussed and negotiated.
- I cannot emphasize enough that medical practices prefer, either up front or at some point in their growth, to own their own building. If you wish to gain a profile as a medical practice expert, it would behoove you to take this into consideration, even if you are negotiating a lease for a start-up practice. The details of an option to purchase or a right of first refusal should be spelled out in the Special Stipulation section of the lease. For those practices that wish to purchase or build-to-suit, I have also found it invaluable to meet with local banks early on in the process and get written quotes on lending rates. Lenders that hold owner-occupied medical office buildings as their #1 choice will usually quote their best loan proposals, which make cash-on-cash returns easy to calculate.
- Large medical groups often require exclusivity for their particular discipline and may ask for exclusivity for companion disciplines that might also be a part of their medical group (e.g., a large family practice group might contain internists, orthopedic associates, and lab facilities and may ask for exclusivity for each one).

Features that Medical Practices Prefer in Their Search for New Medical Space

Now that you have the basic information of how medical practices differ from general office users and some of the basic differences you might anticipate in lease negotiations for medical space, here are some pointers on what medical practitioners look for when searching for a space:

- Good access and visibility.
- Single-story buildings with front-door parking ratios of five spaces per 1,000 rentable square feet of office space.
- Attractive landscaping and building architecture.
- Maximum window exposure.
- Great sign exposure for the site, including multiple locations for signage such as a main marquee sign and building and door signs without logo restrictions.
- Ample tenant finish allowances or “turn-key.”
- A minimum of a one-year builder’s warranty.
- A developer with a good reputation in leasing sales and management.
- Should you decide to focus your attention on medical office space, we hope this basic information will be “just what the doctor ordered.”SM

If you wish to receive specific examples of language for exclusivity, first option to adjacent space, right of first refusal, and options to purchase, please email us at perimetermgmt@bellsouth.net.

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