Introduction

Joel Tabatcher - Acting Director, Real Estate Administration Division

Good afternoon everybody and thank you for joining us. This is the 2nd edition of the PBS, National Office of Leasing Industry Outreach call. For those of you that weren’t with us last month, we kicked things off by announcing the start of the program and then walking through 5 topics. A PDF of the minutes as well as the audio for that session can be found on our website, gsa.gov/leasing and those specific resources are under the Leasing Outreach section. One last note on the last session; it was one way, but that’ll will be the exception not the rule - today’s session will contain a question and answer session after each topic.

Today, we’ll be discussing 2 topics: the length of GSA lease terms and the Reduce the Footprint Memo. For each topic, we have some background information we want to share, then we’ll open it up for questions. In order to avoid any audio issues with such a large group, we’ll be taking questions exclusively through the chat function in the meeting space. I think we’ll have enough time to answer all of your questions, but if we don’t, we’ll address all questions in a written response as part of the minutes for this session - which will be posted on our website.

I think everybody will be really interested in our 2 topics today so I’m going to hand it over to John Thomas and Justin Hawes. John is the Director of our Policy and Program Execution Division and Justin is the Director of our Policy Center. Before we get into the meat of the session, I wanted to let Lance Feiner the Deputy Assistant Commissioner for the National Office of Leasing at PBS say a few words.
Welcome

Lance Feiner - Deputy Assistant Commissioner, National Office of Leasing
Hello everybody, on behalf of Chris Wisner and the entire National Office of Leasing, I welcome you to this call. We are so excited to have initiated this new program of Industry Outreach. Based on participation of our inaugural event we had last month and participation from this call, we could not be more pleased. Each of you as Industry are all important partners to our office. Without these relationships, we would not be able to deliver the workplace solutions to our client agencies at the best value to the taxpayer as we do. We hope everyone on this call finds these conversations meaningful and I would like to remind everybody that anything discussed today as well as the Q & A portion of the discussion can be found at gsa.gov/leasing. There you will find out all of the information about our program and our office including the policy documents that we will talk about on this call today. We are so happy that you all have been able to join us on this call. Thank you.

Topic 1

Joel Tabatcher - Acting Director, Real Estate Administration Division
Great, thanks Lance. Our first topic is the length of GSA lease terms. To provide some background, the feedback we’ve heard from the industry is that GSA is missing an opportunity to obtain lower rental rates because of the way we structure our lease term with termination rights anytime after 5 years. Historically GSA has rarely exercised these termination rights and generally stayed in the building much past the original full term. We have done analysis on this internally and issued guidance to our lease contracting officers that Justin is going to walk us through.

Justin Hawes - Director, Center for Lease Policy
GSA agrees that the use of longer lease terms, in particular longer firm terms, is appropriate for a larger percentage of our lease transactions than has been typical in the past. With that goal in mind and wanting to encourage our regions to pursue longer firm terms, last year on April 20, 2016, GSA issued a policy memo called a Leasing Alert entitled, “Lease Term Strategy” with the intent to encourage our regions, in particular our Lease Contracting Officers, to procure longer lease terms, and longer firm terms, where it makes good business sense.
This Leasing Alert on longer lease terms is accessible for the general public to read on our website located under the “Leasing Policy and Overview” section. I’m now going to recap some of the main points of this Leasing Alert.

First, the Leasing Alert reinforces that GSA has 20 year lease authority and that we should be leveraging GSA’s financial strength by entering into longer leases, and longer firm terms, where appropriate.

Second, GSA has a self-interest in reducing the number of lease procurements and the resulting workload burden on our regions and Lease Contracting Officers through the use of longer lease term strategies.

Third, if GSA is going to pursue longer lease terms for a greater percentage of our leased inventory, we have to do so in a way that does not result in a material increase in vacant leased space.

Our data shows that GSA tenant agencies stay in the same location for an average of 23.3 years (when weighted by size/SF). Despite this fact, the most common lease term entered into by GSA historically has been a 10 year lease with termination rights any time after the 5th year (10/5 firm lease term). Although the Government has a high probability of remaining in a lease for a period well beyond the five years, GSA lessors receive no credit from their lenders for a lease term where the tenant has ongoing termination rights after the 5th year and, therefore, are unable to pass along more favorable rental pricing to the Government.

We also recognize that GSA may experience reduced competition in its lease procurements since some potential offerors will choose not to make their space available if the tenant is seeking the ability to cancel on short notice, even if not applicable until after five years of occupancy. Additionally, since GSA has statutory authority to enter into 20 year lease terms, GSA may be foregoing the benefits of more favorable rental pricing when it seeks lease terms for only a 5 or 10 year period.

With this understanding, the GSA National Office of Leasing issued the “Lease Term Strategy” Leasing Alert last year to encourage our regions, and our Lease Contracting Officers, to pursue longer lease terms, in particular longer firms terms when it makes good business sense to do so. The
entire GSA leasing community came to an agreement on 3 opportunities that would add value when considering a lease term strategy for any particular procurement. These 3 are:

1) GSA’s unique long-term presence in the market. This is to say, the Federal government has always been there in the past and will always be there in the future.

2) GSA’s 20 year lease procurement statutory authority. In other words, GSA is permitted to lease space up to 20 years.

3) GSA’s greater use of true renewal options as opposed to relying on terminations rights in the soft years.

In addition to the Leasing Alert which I just highlighted, the GSA National Office of Leasing has added an extra data point on our market research report, called the Bullseye Report, that we provide to our Lease Contracting Officers in the field prior to them awarding a lease. This extra data point on our Bullseye Report takes into account multiple factors regarding our customer (i.e., SSA, IRS, FBI, etc.) and the market (city, what other federal presence, etc.) and then will recommend to the Lease Contracting Officer whether or not a longer lease term is appropriate for a specific project.

Finally, in addition to our Leasing Alert on longer lease terms and our Bullseye Report that recommends longer lease terms to our Contracting Officers when it makes sense, the National Office of Leasing has been meeting quarterly with each individual GSA region to review that region’s expiring lease workload and provides advice and guidance on lease term strategies for replacement, follow on leases.

We believe with this 3 prong approach: 1) Issuing a Leasing Alert on longer lease terms last year, 2) Adding an extra data point to our Bullseye Report that recommends doing longer lease terms where it makes sense, and 3) The National Office of Leasing meeting quarterly with each region to review their expiring lease workload and provide input on lease term strategies --- will ultimately, over time, lead to a greater percentage of our lease transactions showing longer lease terms, and in particular, longer firm terms.

In fact, GSA believes, and the data is starting to demonstrate, that these 3 efforts are already paying off. Our data shows that 20% of leases made effective in fiscal year 2015 had a firm term of 10 or more years; however, that number grew to 25% the following fiscal year in 2016. The trend is continuing upward in this fiscal year of 2017, and we suspect the same upward trend as we continue to make progress in this area. While we still have room to grow, GSA National
Office of Leasing, our regions, and our Lease Contracting Officers have fully embraced this idea of longer lease terms and longer firm terms as a way to capitalize on GSA’s financial strength and the resulting improved rental rates being offered to the Government.

Joel, I’ll turn it back over to you.

**Topic one Q&A**

**Joel Tabatcher - Acting Director, Real Estate Administration Division**

Ok, great thank you Justin. That’s some good background and a nice update on the stats, it’s good to hear the numbers are representing a change in mindset. So now, we’ll open it up for questions.

1. How does GSA handle customers who will not sign an occupancy agreement for the term that GSA thinks they should?

**Justin Hawes - Director, Center for Lease Policy**

So this exact point is a good question because it is directly in the leasing alert. The leasing alert talks about the idea of the OA and our client agencies who may want to commit for a certain period of time. But if we are in a market and it makes good business sense to the government, there are some factors laid out in the leasing alert. The LCO under their discretion can pursue a longer lease term. Some of those factors are as I talked about the Bullseye Report, does it talk about a longer lease term? Is the location a regional headquarters building or a field office location? Does the customer have a need for specialized build out space? Is this going to be a built to suit or lease construct project? Is the customer going to use substantial RWA funds? Is there a strong likelihood of another customer backfilling the space? These are the factors that allow the discretion of deciding if a longer lease term makes sense.

**Joel Tabatcher - Acting Director, Real Estate Administration Division**

2. There seems to be a disconnect on recent SFO's where it is economically advantageous to lease for 20 years, but project is running into lease scoring issues. How can we get through this?

**Justin Hawes - Director, Center for Lease Policy**
The longer our leases are executed the greater the chance we run into scoring issues. If we have a 20 year lease, we have a chance of running into capital scoring and when we have capital scoring, we can run into issues. If the LCO completes a scoring report or analysis and it scores as a capital lease then they will reevaluate the lease term.

**Joel Tabatcher - Acting Director, Real Estate Administration Division**

3. If a Bullseye report indicates that it’s appropriate for a leasing specialist to sign a long term lease is this mandatory?

**Justin Hawes - Director, Center for Lease Policy**

Our LCOs are the ones that have the authority to bind the government on a lease. A Bullseye report is just a recommendation and it is the LCO’s discretion and if it makes business sense then they may ultimately decide to go with a longer term lease.

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**Topic 2**

**Joel Tabatcher - Acting Director, Real Estate Administration Division**

Great thank you everybody for the questions. We’re going to move on to the next topic which is is reduce the footprint. I’m going to hand it over to John to discuss this further.

**John Thomas - Director of our Policy and Program Execution Division**

I wanted to provide some background on the Reduce the Footprint memo and then get into GSA’s role in the implementation of it as well as some feedback we’ve heard from our industry partners. In terms of background, in May 2012, OMB issued OMB Memo 12-12 to promote efficient spending to support agency operations. Section 3 of M-12-12 directed agencies to move aggressively to dispose of excess properties held by the Federal Government and make more efficient use of the Government's real estate assets. Further, it established the requirement for agencies to "freeze" the size of their civilian real property portfolios. In March 2013, OMB issued Management Procedures Memorandum 13-02 to outline, in broad terms, the implementation process for OMB Memo 12-12. Under OMB's Freeze the Footprint policy, agencies have reduced their FY 2012 office and warehouse baselines by 24.7 million square feet from FY 2013 through FY 2015. OMB estimates that this reduction will result in $300 million annual cost avoidance in FY 2016 and all subsequent years.
In March 2015, OMB issued the National Strategy for the Efficient Use of Real Property (National Strategy) and OMB's Reduce the Footprint policy to build upon these successful efforts and establish a strategic framework by which agencies would manage their real property portfolios to improve efficiency, consolidate and dispose of unneeded properties, and improve mission effectiveness. In addition, this guidance established a Space Design Standard for Office Space, which required agencies to establish a design standard for maximum useable square feet by workstation for use in the design of owned and leased domestic office space, including GSA occupancy agreements.

The policy applies to all space renovations and new acquisitions for all agency components. Agencies are not required to retrofit existing space to meet the standard specified by their policy. Agencies also are not required to apply the standard to replacement, succeeding or superseding leases, executed by the agency or by GSA, if the agency can demonstrate that application of the standard is not cost effective.

For GSA, this Memo directed us to provide agencies with an annual report containing a comprehensive accounting of a given agency’s real property. This file contains data on agency’s own leased and owned real property as reported by the agency into the Federal Real Property database as well as data on any real property owned or managed by GSA. Agencies use this data to work with OMB to set a square footage reduction target at a portfolio level.

GSA has been investing heavily in the upfront planning function of our agency. The goal of the resources we’ve dedicated to the planning function is to provide our customers with a comprehensive plan for their requirement which includes space planning, market research and a cost benefit analysis with each alternative. The goal is to assist our customers in making location specific decisions while keeping in mind the portfolio level reduction target.

GSA’s goal is to provide space that meets the mission requirements of the agency and GSA works with agencies to make cost-effective decisions concerning their lease requirements. However, there still may be situations where the financial interests of the lessor and the mission requirements of the Government do not align. Such situations may result in a small space reduction that provides only marginal savings for the government and that impose a financial cost on the landlord by leaving an untenantable block of space within the building. GSA cannot procure and pay for space that is not going to be utilized.
Having said that, we have heard from you that some folks in the field, both GSA and our customers, are applying the Reduce the Footprint policy indiscriminately to lease transactions with no apparent benefit to the Government. We recognize that the OMB memo does not require the application of the new “reduce the footprint” design standard to replacement, succeeding or superseding leases, if the Government can demonstrate that application of the standard is not cost effective. To raise awareness and understanding of this policy, our office will be re-emphasizing the policy set forth in the OMB guidance and providing additional training to the GSA regional offices.

If you have specific questions about the Reduce the Footprint policy, you can email us at leasingoutreach@gsa.gov.

Topic 2 Q&A

Joel Tabatcher - Acting Director, Real Estate Administration Division
Great, thank you John. So now, we’ll open it up for questions. We’ve received a few in the chat box but if you have any, please chat them in now

1. Is it the Government’s policy to apply the Freeze the Footprint standard to all lease transactions?

Response: John Thomas - Director of our Policy and Program Execution Division
No. The Freeze the Footprint policy only applies to new acquisitions for all agency components. Agencies are not required to apply the standard to replacement, succeeding or superseding leases, if the agency can demonstrate that application of the standard is not cost effective.

Joel Tabatcher - Acting Director, Real Estate Administration Division

2. What happens when an agency occupies an entire leased building that was constructed specifically for the agency’s space requirement and, after applying the freeze the footprint policy, the space requirement is reduced from 10,000 square feet to 9,000 square feet? How should a building owner with such a situation address the likelihood that there will be an unmarketable block of space due to the Government’s space reduction?

It is the responsibility of the offeror to determine how to subdivide its space so that space not
required by the Government can be leased by other tenants.

**Joel Tabatcher - Acting Director, Real Estate Administration Division**

3. Does the Lease Contracting Officer have any discretion in accepting a larger amount of space than the amount specified in the Request for Lease Proposals?

No. Payment will not be made for space which is in excess of the amount of ABOA square footage stated in the lease.

**Joel Tabatcher - Acting Director, Real Estate Administration Division**

Well that’s all we have for today, thank you very much for your participation. GSA really does appreciate the dialogue and insights you in the industry provide. As I said, we’ll be posting the minutes and audio for this session to our gsa.gov/leasing website.

Next month’s session will be on net of utility leases. In order to have focused conversation on the technical aspects of this topic, GSA will be hosting a small group session. We are looking for representation from across different parts of the industry to ensure that we get the right knowledge base and perspective at the table. If you are interested in participating in this small group session, please email leasingoutreach@gsa.gov. One last note - as with all session, the minutes from that the small group discussion about net of utility leases will be posted to our website the week after.

Thank you again for your time and have a good rest of your day!