

Using single R/U ratio – Will this method be the new way?

By William B. Tracy, MBA, NCARB

Leasing 100% of the rentable area in a commercial property is the Holy Grail of leasing because this preserves the asset value of the property. However, the ability to achieve this goal and maintain it over time is highly dependent on the skillful application of the R/U ratios of a property. Sometimes called the “load factor”, the R/U ratio, which represents rentable area divided by usable area, is a key tool for allocating the rentable area of a property to each of its tenants.

The original version of the Building Owners and Managers Association Standard published in 1915 did not employ an R/U Ratio but simply measured rentable area as the space actually occupied by a tenant, measured “from plaster to plaster”. If a landlord was fortunate enough to lease a full floor to a tenant, he had a windfall because a full floor tenant can utilize space that multi-tenant floors need for corridors. Conversely, a floor that changed from single to multi-tenant lost rentable area. This volatility over time in the rentable area of an office building was a problem for property managers, appraisers and other stakeholders in the property.

It wasn't until the 1980 version of the BOMA Standard that the R/U ratio was incorporated to allocate common areas to multiple tenants on a floor-by-floor basis. This solved the rentable area volatility problem, but created another one. Because the 1980 BOMA standard computed R/U ratios on a floor-by-floor basis, tenants on a floor that had a lot of common areas got a raw deal. Their R/U ratios were significantly higher than the R/U ratios on other floors of the building. For example, the ground level entry lobby resulted in high R/U ratios for first floor tenants. This became a problem for landlords who had to slash R/U ratios to make deals on the ground level of their building. Slashing R/U ratios resulted in loss of rentable area and property value.

To fix this problem, in 1996 BOMA introduced a revised measurement standard that for the first time included a building R/U ratio. That standard, which is still the current one, included two R/U ratios; the floor R/U ratio distributes floor common areas (toilets, etc.) among all tenant on a floor, and the building R/U ratio distributes building common areas (building entry lobby, etc.) to all floors of the building. This method employs R/U ratios that are unique to each floor of a building and it actually over-corrected for the high R/U ratio problem for first floor tenants under the 1980 BOMA standard. While being reasonably successful in smoothing rentable area volatility over time and limiting R/U ratio variation among a the floors of a building, it still requires landlords to apply a unique R/U ratio to each floor, complicating marketing, leasing and property management. As a result, many landlords are now adopting a modified BOMA method that incorporates a single multi-tenant R/U ratio for use on all floors of a building.

Landlords and tenants alike are discovering that use of a single building R/U ratio for all floors can be tricky. Incorrectly implemented, it can result in wide variation over time in the rentable area of a property, even more extreme than those caused by the 1915 BOMA standard. Since it is not currently sanctioned by BOMA, use of a single R/U ratio exposes a landlord to liability if the BOMA standard is cited as the measurement standard.

Correct application of a modified-BOMA single R/U measurement method requires some skill and significant attention to documentation. The author has developed and applied a single R/U method over the last 10 years and found that it will achieve the goal of

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realizing all the rentable area of a building initially and maintaining this over time with little or no variation. Not even the current BOMA standard can achieve this stability, which has become especially significant in light of the role that property asset valuation serves to underpin commercial mortgage backed securities (CMBS) and similar investment vehicles.

This method has been documented and submitted to the BOMA Floor Area Measurement Committee at their recent meeting in Miami as the basis for a new optional method to be incorporated into the next update of the BOMA standard. For those who are interested in how it works, a detailed description can be found at

<http://www.buildingareameasurement.com/1ru.pdf>.

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