



Finding Money for Your Medical Office Build-Out

There are many ways to finance this important element

By **Carrie Rossenfeld**

When you ink a new lease or sign a renewal lease for space you currently occupy, you have the opportunity to negotiate for a tenant improvement allowance.

Landlords refer to this allowance as TI dollars, and they offer this money to tenants so they can “improve” their space. Improvements can range from paint and flooring to a full-on construction or renovation project.

The amount of money a landlord will give you is negotiable and varies from market to market. It also depends on how desirable you are as a tenant and how badly the landlord wants to fill up his space.

In general, TI dollars will only cover a percentage of the total build-out cost, and landlords typically only offer enough for standard finishes and materials. If you want an upgrade, you’ll probably need to budget for the additional expense at your own cost, says Trisha Talbot, senior vice president of the healthcare investment group at GPE Commercial Advisors in Scottsdale, Ariz.

In the past, tenant improvement dollars were not intended for a healthcare professional’s furniture, fixtures, equipment and telecommunication installation. But that’s changing, given the current tenant’s market, according to Ben Rosenfield, a principal with Titan Commercial LLC in Chicago. He says some landlords are allowing TI dollars to be used for furniture, phone systems and computer equipment, as well as plumbing upgrades, electrical service for larger medical equipment and gas for lab space.

An unfinished space that needs more work will garner higher TI dollars, whereas a space delivered in finished condition will yield a minimal allowance, says Coleman O’Gwynn, vice-president of healthcare advisory services at Transwestern, a national commercial real estate firm.

You should ask for more TI dollars than you expect to get, and you might be pleasantly surprised. You might also consult a seasoned real estate broker who knows which landlords are willing to give greater concessions (possibly covering all of your build-out costs) as well as how to manage the entire construction process.

When landlords will help you build out

Some landlords will allow you to roll into the lease the build-out costs not covered by TI dollars. This is the easiest solution for you as a tenant, as long as the terms and interest rates are in line with market rates.

However, if your landlord is looking to sell the property to an investor, such an arrangement can look as if the space is garnering above-market rents, which could lower the value and salability of that property.

“If you have a lease expiring in the next year, and you want to stay, but you need to expand the practice, it’s a perfect time to ask for some incentives from the landlord,” says Rosenfield.

Keep in mind that a medical-office build-out is generally more expensive than that of typical office space, so to justify the cost a landlord may require you to sign a longer lease—typically between seven and 10 years, as opposed to a traditional five-year term for general office space.

“In your lease negotiations, get months of free rent at the get-go to finance some of the build-out, and then get tenant improvements from the landlord,” recommends Raphael Darvish, M.D., a cosmetic dermatologist in Brentwood, Calif. “Medical doctors are great tenants since they tend to stay put for a long time and don’t do out of business when the economy goes bad. For this reason, landlords love physicians.”

Other financing methods

A business line of credit can be a good alternative, says O’Gwynn. The money used for your build-out is considered a business cost since the loan would be unsecured. Commercial and industrial loans (called C & I loans) are another option, but often the financial institution will want you to move all your practice’s deposits to that bank in order to qualify.

Banks and private equity do offer programs to finance a build-out, but the interest rates can run between 9 percent and 18 percent and are looked upon as short-term loans. Fortunately, even in the current economy, healthcare professionals are considered a good risk for lenders and can qualify for SBA loans, says Talbot.

You’ll be considered based on your corporate and personal financial strength; a down payment is required and typically starts at 10 percent of the total loan value. (see MOT story on Understanding Your Creditworthiness)