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New Uses for Office Space



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Reviews of recent papers, including the most recent NAOP publication, indicate that at the end of 2021, national vacancy rates for office space settled at 17.6%. However, with job growth expected to continue, office use employment is likely to reach pre-pandemic levels by the middle of this year. Despite these projections, the outlook for the demand for office space remains in doubt. Return-to-office timetables have been pushed back as new COVID-19 variants and uncertainty about the path of the virus emerge. It is clear, however, that the COVID-19 pandemic has changed the way work is conducted. Remote and hybrid work models are very popular with employees, and most likely will stay on as employers attempt to satisfy the needs of a post-pandemic workforce.

Reflecting the possible decline in the need for office space, investors are considering new uses for existing space. Adaptive reuse, which is the process of repurposing a vacant or underutilized building and converting it to another use, is being strongly considered for several reasons. Adaptive reuse can be as much as 20% less costly than building from the ground up. Adaptive reuse also allows the historic character of a neighborhood to be maintained and is considered more sustainable, as there is less construction required to convert a building than to create a new one. In addition, permits and other required approvals may be easier to obtain than for new construction.

As the housing market remains strong, the potential for adaptive conversion of office space

to multi-family residential properties becomes economically viable. Also, as the need for more affordable housing has become a serious problem in many areas, providing more housing units in centrally located areas becomes more important.

Adaptive reuse can optimize the operational and commercial performance of a building by transforming obsolete spaces to serve entirely new purposes. A conversion to multifamily housing will likely be more successful in markets where multifamily vacancy rates are lower than office space vacancy rates, and rent growth is expected to exceed office space rent growth.

The feasibility of converting a building to residential use involves many factors: most notably, the prospect of higher net operating income for the investor under residential use, a building structure that is amenable to a residential transformation and a regulatory environment that does not hurt the viability of a conversion project.

A wave of adaptive reuse projects involving the conversion of office buildings into life science facilities is indicative of the increasing demand for life science facilities. The life science sector has experienced significantly increased importance in large part due to the pandemic. Bio-tech and pharma firms are racing to develop treatments using the genomics breakthroughs that produced the COVID-19 vaccines. Consequently, the need for more office space represents an opportunity for an adaptive reuse

from traditional office space to flex space for life science labs and administrative work. Converting an office building into a life sciences lab is more expensive than other reuse projects due to the special systems needed for ventilation, cooling and moving equipment. However, the benefits for investors include the fact that the life science industry is less sensitive to fluctuations in the economy and is therefore less impacted by recessions. Life science employees are more likely to work on site, necessitating space for a full workforce. Additional factors supporting conversion to a life science use is the significant investment from IPOs and venture capital. These firms are more likely to have the funding to commit to longer (and more expensive) lease terms.

Another opportunity for adaptive reuse is the conversion of office buildings to medical office facilities. While the demand for medical office space has consistently been higher than for traditional office space, over the next 10 years, the 65 and over population is expected to be the fastest growing demographic in the U.S. Properties located in areas with good access to hospitals, specialized medical treatment centers and intensive care units are good candidates for conversion. Infrastructure considerations include parking, drop off/pick up, zoning and power/life safety redundancy.

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