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Will Recession Cause Towers Significant Shrinkage?

By Dana Rubinstein

New York City's iconic man-made towers might just, should this downturn prove as dreadful as some have predicted, start experiencing some mysterious (and embarrassing) shrinkage. On paper, at least.

Allow us to explain. In English, a square foot translates into a scientifically precise 144 square inches. In New York real estate–ese, a square foot describes whatever the hell the market will bear.

It's true. New York real estate professionals, not merely content to reshape the vernacular of our landscape, also toy with the very vernacular that allows one New York human to communicate with another!

"Every time I explain this to a client, they just look at me wide-eyed," said **Charles Isaacs**, a tenant broker and the president of **CSI Consultants**, on the phone from his Newburgh office. "People don't know about it."

And so Dr. Isaacs wrote a helpful article on the topic, which he posted on his Web site, ***www.npspace.com***. It reads, in part, "The 'rentable area' of virtually every office unit includes a relatively large block of square footage that cannot be used by the tenant or, sometimes, even found, but for which the tenant is nevertheless charged rent. The percentage of the 'rentable area' that's not usable, or under the tenants' control, is known as the Loss Factor."

How it's possible for landlords to inflate square footage every time a building is sold or a lease is renewed is a bit of a mystery. Other cities willingly abide by the Building Owners and Managers Association standards, which proscribe much of this square-footage inflation. Not so in New York City.

The result is the peculiar fact that, over time, skyscrapers, at least on paper, grow in size. Or, as REBNY president **Steven Spinola** said, "It rains a lot in New York." (And skyscrapers, apparently, contain chlorophyll.)

"We [REBNY] establish our own loss factor," Mr. Spinola said. "No criticism to BOMA, [but] we've been doing office buildings for a long time, and we've established rules for how to measure, and the rules require you to tell the tenant what the loss factor is." In other words, landlords can detach rentable square footage from reality as much as they like, as long as they tell their tenants what they're up to.

Take the Moinian Group's 530 Fifth Avenue, which Moinian and the Chetrit Group bought in 2004 for $210 million. The 26-story tower was completed in 1957, and marketing materials obtained by *The Observer* from 1955 indicate that the sixth floor of the building measured 24,400 square feet. Twenty years after the building's completion, the sixth floor's rentable square footage had grown to 29,850 square feet. By 1993, it had grown to 30,578 square feet. And today, according to real estate database CoStar, the sixth floor is now an incredible 34,706 square feet—a full 10,306 square feet larger than the original measurement.

Or check out the growth of 370 Lexington Avenue, a lovely Art Deco building that Sherwood Equities bought in 2008 for $155 million. CoStar describes the building as containing 261,000 square feet. Which is interesting, because in the 1999 marketing materials for the building, it is described as containing merely 232,287 square feet.

Though the materials do helpfully point out that "[a] potential increase in rentable square footage is achievable through a re-measurement of some of the spaces upon rollover of the existing leases. This practice is common in Manhattan real estate investment properties." The marketing materials also note that "using a market-rate loss factor of 26% would result in a 14,414 square foot increase in office space."

David Lebenstein, a tenant broker from **Colliers ABR**, called the issue of loss factor "a sore point with tenants."

"It's one way to get the rents up when the other leases in the building are renewed," explained **CresaPartners**' **Bob Stella**. "It's also a way to pass along escalations."

For example, utilities are normally calculated on a square-foot basis. So "if you have more square feet, the tenant will pay more in electricity bills," Mr. Stella said. "And if you don't do it, your rents will look higher per square foot."

Now, here's the rub. With the commercial real estate market tanking, will buildings start shrinking in size? Will SL Green's 1515 Broadway, which, according to press reports, has grown from 1.7 million square feet in 1989 to 2,056,442 square feet today, lose some poundage?

It's possible. "Where tenants are renegotiating their leases, particularly if it's a good-size tenant, they are modifying measurements to where they were earlier, maybe 10 years ago," Mr. Stella said.

Mr. Spinola wasn't so sure.

"I remember when I was working for the city and we had a lease we had to sign, and I called up the owner, because I knew the owner, and I said, 'You're doing these four things to me, [including increasing] my square footage by 10 percent.'"

The landlord was willing to address three of the four issues. Guess which one he wouldn't touch.

"He said, 'Sorry, Steve, I [re-measured] the whole building.' It was the one issue on which he was not prepared to make a concession."