



Janice K. Brewer
Governor

Kathy Peckardt
Interim Director

ARIZONA DEPARTMENT OF ADMINISTRATION

OFFICE OF THE DIRECTOR

100 NORTH FIFTEENTH AVENUE • SUITE 401
PHOENIX, ARIZONA 85007

(602) 542-1500

MINUTES OF THE MEETING

LEASE COST REVIEW BOARD

December 1, 2014

1. **Call to order and roll call.** Chairwoman Nola Barnes called the meeting to order at 3:01pm, Monday, December 1, 2014, in Room 101 at 100 N.15th Avenue, Phoenix, Arizona 85007.

Members Nola Barnes, Janie Terry, Anna Velarde, and Mike Neary and Clerk Sara Sullivan were present. Member Jack Brown was absent.

2. **Ratification of the action taken on the Agenda from the meeting of June 27, 2014.** Nola Barnes stated that this item is to estimate an average private sector lease rate of \$19.90 per square foot per year for fiscal years 2016 and 2017.

Mike Neary moved to ratify the board estimate an average private sector lease rate of \$19.90 per square foot per year for fiscal years 2016 and 2017. Anna Velarde seconded.

The motion carried unanimously of members present.

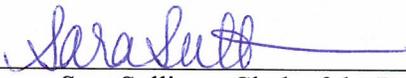
3. **Ratification of the action taken on the Agenda from the meeting of August 8, 2014.** Nola Barnes stated that this item is for the recommendation to the ADOA director of a \$14.88 rental rate charged to State agencies using office space and a \$5.39 rental rate be charged to State agencies using storage space in State-owned buildings for fiscal year 2016.

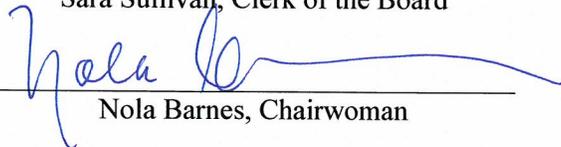
Anna Velarde moved to ratify the board recommendation of a \$14.88 rental rate charged to State agencies using office space and a \$5.39 rental rate be charged to State agencies using storage space in State-owned buildings for fiscal year 2016. Janie Terry seconded.

The motion carried unanimously of members present.

4. **Adjourn.** Without objection or further comment, the Chairwoman adjourned meeting at 3:11pm.

Respectfully submitted:


Sara Sullivan, Clerk of the Board


Nola Barnes, Chairwoman

**FY 2014 Lease Cost Review Board (LCRB)
ADOA Recommendations for Privately Leased Office Space
ARS § 41-793**

Background

Pursuant to ARS § 41-793, before July 1 of each even numbered year, a Lease Cost Review Board (LCRB) estimates an average square foot dollar cost [Rate/Rentable Square Foot (RSF)] for the following two fiscal years for the leasing of private sector office space. The LCRB last agreed on estimates of an average Rate/RSF in 2012 for FY 2014 and 2015. The 2014 LCRB will adopt estimates for an average Rate/RSF for FY 2016 and 2017.

The LCRB membership consists of the Arizona Department of Administration (ADOA) Director or its designee and four members appointed by the ADOA Director, including three directors of other State agencies or their designees, and a staff member of the Joint Legislative Committee (JLBC), for a three-year term. The 2014 LCRB agency membership includes:

- ADOA Designee
- Arizona Department of Economic Security (DES) Designee
- Arizona Department of Corrections (ADC) Designee
- Arizona Department of Public Safety (DPS) Designee
- JLBC Staff

The directive of the LCRB is to: 1) estimate an average Rate/RSF for the following two fiscal years for leasing privately owned office space, and 2) recommend to the ADOA Director a rental rate charged to state agencies for using space in State-owned buildings, by July 1 of each even numbered year.

ARS § 41-793 also directs ADOA to review and approve all agency leases for private sector office space, excluding the Board of Regents (Universities). Day-to-day lease administration and property management functions are de-centralized to individual State agencies, though ADOA terminates leases on behalf of state agencies to affect ADOA-initiated space consolidations and fiscal funding out scenarios.

ADOA Data by LCRB Year

ADOA's brief analysis of its active leases as of June 4, 2014, which are primarily Class B office space, for even-numbered years' 2012 and 2014 includes the following:

Year	Active Leases	Rentable Square Feet (RSF)	Annual Cost	Annual Rate/RSF
2012	282	2,966,518	\$47,801,300	\$16.11
2014	244	3,200,522	\$50,317,100	\$15.72
	-13.12%	7.89%	5.26%	-2.42%

In summary of the foregoing ADOA lease data, since the LCRB convened in 2012, State agencies are leasing more RSF in fewer leases at a reduced annual rate/RSF. ADOA approved 19 leases in the prior two fiscal years that exceeded the LCRB FY 2013 and FY 2014 adopted average of \$19.40/RSF. Please see the attached Private Sector Lease Report as of June 2014.

Market Area Rates

Market Area data for both the Phoenix and Tucson Market Areas for the First Quarter 2014 indicates persisting high vacancy rates and tenant favorable conditions. Although long term forecasts through 2017 project improvement in Arizona's economy, there is no expectation that the commercial lease market will improve significantly for several years. While market conditions slowly improve, the market is still tenant favorable; however, market conditions vary dramatically depending on the Metro Phoenix submarkets. For example, Tempe and Chandler appear to be recovering much quicker than the Midtown Phoenix and Northwest Phoenix submarkets. Generally, Rates/RSF outside the Phoenix Market Area,

including the Tucson Market Area, Flagstaff, and other less urban areas, will reveal less competitive market conditions because there is less space inventory. Special or unique space requirements will reduce the flexibility of negotiation leverage in almost any Market Area. Summarized, the Phoenix and Tucson Market Area data for First Quarter 2014 reflect the following:

First Quarter 2014 Average Phoenix Market Area

All Classes	Central Business District	Class A	Class B	Class C	Vacancy Rate
\$20.93	\$23.47	\$24.51	\$20.13	\$15.57	17.8%

First Quarter 2014 Average of Tucson Market Area

All Classes	Central Business District	Class A	Class B	Class C	Vacancy Rate
\$18.89	\$18.57	\$21.97	\$18.98	\$15.62	12.80%

The First Quarter 2014 Market Area data reflects the average of Landlord quoted/asking Rate/RSF in Arizona’s two primary Market Areas. ADOA’s data reflects the average *negotiated* Rate/RSF. ADOA adjusted the foregoing Market Area rates to reflect rental occupancy taxes of 2.5%. ADOA Rate/RSF data includes occupancy taxes – the published Market Area Rate/RSF do not.

FY 2016 and FY 2017 Recommendation

As the lead agency of the LCRB, ADOA proposes the LCRB adopt the FY 2014 average Rate/RSF for privately owned office of \$19.90/RSF for FY 2016 and FY 2017 to reflect an average of Market Area conditions and ADOA’s commitment to ensure agencies negotiate Rates/RSF below a Landlord’s quoted/asking Rate/RSF.

Recommended Maximum Private Sector Lease Rate

(Full Service Rate/RSF, including occupancy taxes)

FY 2016	\$19.90
FY 2017	\$19.90

Agencies submitting leases to ADOA for review and approval that exceed the Recommended Maximum Private Sector Lease Rate must provide written justification for the rate.

Janice K. Brewer
Governor



Brian C. McNeil
Director

ARIZONA DEPARTMENT OF ADMINISTRATION

GENERAL SERVICES DIVISION

100 NORTH FIFTEENTH AVENUE • SUITE 202
PHOENIX, ARIZONA 85007

(602) 542 - 1776

Date: August 13, 2014

To: Brian C. McNeil
Director, Department of Administration

From: Nola Barnes
General Manager
GSD Building and Planning Services

Re: 2014 Lease Cost Review Board State-owned Rental Rate Recommendation

Background:

Pursuant to A.R.S. § 41-793, before July 1 of each even numbered year, a Lease Cost Review Board (LCRB) is directed to recommend to the Arizona Department of Administration (ADOA) Director, a rental rate charged to State agencies for using space in State-owned buildings. A.R.S. § 41-792.01 requires the ADOA Director to make a recommendation for the allocation of a varying sum to the Capital Outlay Stabilization Fund (COSF) each year and requires the Joint Committee on Capital Review (JCCR) to determine the rental rates charged to State agencies after ADOA recommendation. The legislative budgeting process informally surpassed the foregoing JCCR process since approximately 2006, which continues.

The 2014 LCRB membership consists of the ADOA Director or its designee and four members appointed by the ADOA Director, including three directors of other State agencies or their designees, and a staff member of the Joint Legislative Committee (JLBC), for a three-year term. ADOA also includes a staff of the Governor's Office of Strategic Planning and Budgeting (OSPB) as a non-voting advisory. The 2014 LCRB agency membership includes:

Nola Barnes, ADOA Designee

Michael Neary, Department of Economic Security (DES) Designee

Janie Terry, Department of Corrections (ADC) Designee

Ana Velarde, Department of Public Safety (DPS) Designee

Jack Brown, JLBC Staff (non-voting member)

Will Palmisano, OSPB (non-voting advisory)

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Recommendation:

For FY 2016, the 2014 LCRB recommends an increase in COSF rental rates charged to State agencies using space in State-owned buildings to support increased building renewal projects in the State's deteriorating facilities. ADOA suggests a rate of \$14.88 for Office Space and \$5.39 for Storage Space (see attached calculator). It is a 14% increase over the FY 2015 COSF rate.

The 2014 LCRB recommendation for FY 2016 supports: 1) O & M of ADOA managed buildings at current service levels, including utilities, 2) \$12,889,000 of ADOA Building System building renewal projects (assuming the amount is appropriated exclusively from COSF), and 3) a portion of the State's annual State Health Lab COP payment. The suggested rate does not address increased operating service levels for ADOA tenants or the accrued deferred maintenance in the ADOA Building System as described in the FY 2015 ADOA Building System Capital Improvement Plan (CIP) <http://gsd.azdoa.gov/assets/documents/CIP2015.pdf> (\$435,000,000). The building renewal figure of \$12,889,000 represents the FY 2016 building renewal formula for buildings that contribute to COSF.

Please let me know if you have any questions regarding the LCRB's FY 2016 recommendation for the COSF rental rate charged to State agencies for using space in State-owned buildings. You can reach me by telephone at 602-542-1954 or by email at nola.barnes@azdoa.gov.

Attachments

cc: Jeff Grant, Deputy Director, ADOA
Paul Shannon, Assistant Director, ADOA
William Hernandez, Assistant Director, ADOA
Michael Neary, LCRB DES Designee
Janie Terry, LCRB ADC Designee
Ana Velarde, LCRB DPS Designee
Jack Brown, LCRB JLBC Staff
Will Palmisano, Fiscal Analyst, OSPB