FEBRUARY 01, 2021

A BETTER WAY TO THINK ABOUT THIRD-PARTY CAPITAL REAL ESTATE SOLUTIONS

With the office and retail real estate sectors in shambles, many real estate analysts and health care capital market experts ponder the resiliency of the health care real estate sector. Given the continued demand for health care services even during the pandemic, these pundits tout that investing in health care real estate is a good thing. And it probably is a good thing. See recent headline: Investors View Medical Office Building as Safe Haven Assets.

This article indicates a 'safe haven' to investors; but what does this mean for a hospital whose credit profile and building occupancy create nearly all the value for this real estate? Despite pandemic relief packages, many health systems and hospitals will see serious revenue shortages. Relatively few will see increased margins. Even without the pandemic, hospital margins continue to be squeezed by declining reimbursements and pricing pressures.

So to our hospital friends – while REITS want to own your buildings, collect 2-3% annual rent escalations and then report year over year 'same-store growth' all driven by your credit and occupancy profile – what do you get out of this? Sure – you get a "cash" influx when/if you sell to a third party. But nearly all of the residual value of the asset goes elsewhere; leaving you with very little, if any, long-term value while surrendering a great deal of short AND long-term control.

WE BELIEVE THERE IS A BETTER WAY

It's called a Non-Profit Real Estate Foundation ("NPF"). And next to direct hospital or health system ownership, we have yet to find ANY third-party capital structure that offers better cost savings, short and long-term control flexibility, capture of long-term accretive value and more balance sheet flexibility.

For the past several months, Hall Render Advisory Services has been educating our clients about the Nonprofit Real Estate Foundation Model. We have hosted multiple webinars and had personal conversations with a few dozen hospital and health systems across the country. This model provides dramatic occupancy cost savings and value creation for our clients as compared to third-party developer or REIT ownership.

REAL RESULTS

We recently assisted a client that had been leasing three ambulatory centers from a third-party developer with 10-12 years remaining on each building lease. The client 'purchased' the facilities from the landlord utilizing an unrelated Nonprofit Real Estate Foundation. The Foundation then stepped in to finance and purchase the buildings and re-structure the client leases.

The result was an immediate 40% reduction in lease expense in the first year and a savings of nearly 50% over the initial 10-12 year term of the leases. The client will save more than $13 million vs the prior lease structure over the next 10-12 years and stands to save even more if property tax exemptions are secured by the participating foundation, The Centurion Foundation.

Under new accounting rules, approximately 30% of the value of the transaction was booked on health system's balance sheet. We believe the balance sheet impact of the NPF model is generally less than other private third-party options and a significantly smaller impact than direct hospital ownership. Yet, the foundation model enables flexible and economically favorable direct ownership options.

OPPORTUNITY

- Build-to-Suit development
- Reverse monetization utilizing non-profit foundation
- Sale/Leaseback
- Re-Structure fully leased assets

As our clients search for ways to cut costs and generate savings in 2021, we believe implementing the NPF structure may represent their single largest savings opportunity, given the heavy operating expense burden of real estate. Hall Render Advisory Services can help clients explore opportunities in their existing real estate portfolio and also assist them in structuring and executing new projects in the most advantageous way.

Please contact us to discuss the potential benefits in utilizing a Non-Profit Real Estate Foundation.

- John Marshall at (317) 670-8527 or jmarshall@HallRenderAS.com; or

Hall Render Advisory Services ("Advisory Services") is a wholly-owned consulting subsidiary of Hall, Render, Killian, Heath & Lyman, P.C. Advisory Services acts as a real estate advisory to clients in various real estate transactions. Advisory Services does not provide legal services, nor is a registered broker-dealer or a registered municipal advisor. Advisory Services does not provide municipal advisory services to entities or obligated persons under Section 15B of the Securities Exchange Act of 1934. HRAS does not provide advice or recommendations concerning swaps or other derivatives or other municipal financial products or concerning the structure, timing or terms of the issuance of municipal securities.