

PROPERTY MANAGEMENT

Fifth Edition



Robert C. Kyle &
Floyd M. Baird, RPA/SMA

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Preface

Property management is a highly specialized but rapidly growing sector of the real estate profession. If they are not property managers themselves, most real estate practitioners will work closely with property managers at some point.

This book provides an overview of the field and describes the major functions of property managers—including their legal and interpersonal concerns and their everyday issues regarding maintenance, accounting, administrative and other activities. It also details specific practices and problems in the management of various types of property: apartment buildings, cooperatives and condominiums, office buildings, retail property, industrial property and government-related property.

This text also reflects the impact electronic technology has had on the industry, as well as the effects fair housing legislation and compliance with the Americans with Disabilities Act has had on all aspects of the property manager's role. Life safety, security and environmental issues are examined as well. Additionally, every chapter ends with a case study. These open-ended scenarios relate real-life challenges faced by property managers and are designed to stimulate class discussion and individual thought.

Property Management is intended for the real estate practitioner who wants a comprehensive introduction to the challenging field of property management, and for the professional manager who wishes to gain new, practical information.

ABOUT THE AUTHORS

Robert C. Kyle (MA, MBA, DBA) is the principal author of this text and president of Dearborn Financial Publishing, Inc., the parent company of Real Estate Education Company, one of the nation's largest publishers of real estate textbooks. Dr. Kyle is past president of the

Association of Illinois Real Estate Educators and the National Real Estate Educators Association, from which he received the Emeritus Award. He has been a member of the Real Estate Advisory Committee of the University of Denver and a former faculty member at Northwestern University. He was on the board of directors of Grubb & Ellis, a full-service NYSE real estate firm. A licensed real estate broker, Dr. Kyle chaired the Educational Courses Committee of the Real Estate Securities and Syndication Institute and served on the License Law Committee and the Continuing Education Task Force of the Illinois Association of REALTORS®. He helped to develop the original text of *Modern Real Estate Practice*, has been a contributor to Real Estate Review and wrote a weekly real estate column in Chicago's *Daily News*. He has been active in many sectors of the industry for more than 20 years.

Floyd M. Baird (AB, JD), the coauthor of the fifth edition, recently retired as vice president and manager of Trust Real Estate for Liberty Bancorp, Inc. of Oklahoma City and Tulsa, Oklahoma, where he was responsible for more than 750 properties of all types throughout Oklahoma and the United States. His property management career began in 1958 when he became executive vice president of a privately owned company owning multifamily, commercial and industrial properties in several states. He has been a national director of the Building Owners and Managers Institute International, selected outstanding local member of the year in 1986, and has conducted seminars for the Institute on real estate law and property management. He has earned the professional designations Real Property Administrator (RPA) and Systems Management Administrator (SMA) from the Institute. His activity in real estate education included serving as an adjunct instructor in property management at Tulsa Junior College and the Continuing Education Center of the University of Oklahoma. Dr. Baird is also a real estate broker and an instructor licensed by the Oklahoma Real Estate Commission. His involvement in real estate education was recognized by the National Real Estate Educators Association in 1983 when he was named a Designated Real Estate Instructor (DREI). As a lawyer admitted to the bar in three states, as well as the United States Supreme Court, Dr. Baird brings both legal and practical knowledge to the property management profession. He now practices law in Temple, Texas.

DEDICATION

The authors wish to dedicate this edition to the memory of C. Donald Kyle and to acknowledge his contributions to earlier editions as a Consulting Editor.

Mr. Kyle began his property management career in Cleveland in the 1920s. While specializing in the management of office buildings, he also handled small and large apartment buildings, clubs, hotels, retail space and industrial properties. During Mr. Kyle's long and active affiliation with the Building Owners and Managers Association, he was director of the Columbus Association, as well as director and president of the North Central District of BOMA, the Cleveland Association and the Cleveland Apartment and Home Owners Association. Mr. Kyle held honorary life memberships in the Building Owners and Managers Association International and in the Cleveland and Columbus, Ohio Associations. His contributions to the property management profession earned him recognition and respect throughout the industry.

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Professional Property Management

The primary function of a property manager is to achieve the objectives of the property owners while generating income for the owners and preserving or increasing the value of an investment property. In other words, the manager attempts to generate the greatest possible net income for the owners of an investment property over the life of that property. It is a common misconception that to be effective a property manager need only collect rents, show space and execute leases. In reality, the property manager's job is far more complex and demanding than is commonly supposed.

Property management, one of the fastest-growing areas of specialization within the real estate industry, is emerging as a managerial science. Today, property managers must have at their fingertips the knowledge, communication skills and technical expertise needed to be dynamic decision makers. They also must be versatile—they may be called on to act as market analysts, advertising executives, salespeople, accountants, diplomats or even maintenance engineers. Interpersonal skills are needed to deal effectively with owners, prospects, tenants, employees, outside contractors and others in the real estate business.

Titles for those engaged in the property management profession have not become standardized. Each organization has its own system of defining job categories, with responsibilities varying according to the type and extent of properties managed. A property manager with the title "Vice President-Director of Real Estate," for example, may perform the duties of a facility manager or an asset manager (discussed later in this chapter).

DEVELOPMENT OF THE PROPERTY MANAGEMENT PROFESSION

The demand for effective, professional property management began in the last decade of the nineteenth century and continues to increase today because of a radical transformation in the nature of urban real estate. This reshaping of cities had its origin in three developments:

1. The creation of the steel frame building and the invention of the electric elevator;
2. The construction of multifamily apartment buildings; and
3. The development of suburban areas.

The structural advantages of the steel frame building, coupled with the perfection of the electric elevator in 1889, made possible a significant advancement in property construction—the highrise apartment and office building. Construction of all types of multifamily apartment buildings, which burgeoned in the 1920s, also contributed to the change.

The expansion of public transportation and the increase in ownership of automobiles following World War II enabled young couples to move to the suburbs where they could purchase their own homes. The evolution of the shopping center as a result of this population shift helped to decentralize the traditional downtown concentration of commerce. A commercial development exodus that is still in progress followed suburban residential development. After residential development came shopping centers; office buildings and light industry followed. This suburban trend has been modified in some areas by the revitalization of central cities, but strongly continues today. In recent years, the realignment and centralization of ownership of investment properties by large institutions and groups of investors have continued to increase the demand for professional property management.

Today, most professional property managers work in one of two capacities: as an employee of an owner of extensive properties or as an independent manager for several owners. The latter are often referred to as *third-party managers*.

A professional property manager must have a comprehensive understanding of the economic forces at work in the real estate market. He or she must be able to evaluate the property in terms of operating income, forecast its potential for the future and construct a management plan that reflects the owner's objectives while remaining flexible enough to adapt to future changes in the market. A property manager must become a specialist skilled in space marketing, tenant psychology, the legal aspects of the landlord-tenant relationship, maintenance procedures and accounting. These and related topics are treated in detail in Chapters 2 through 10.

GROWTH OF PROFESSIONAL ORGANIZATIONS AND DESIGNATIONS

George A. Holt, owner and manager of a 16-story Chicago skyscraper, recognized that property managers need to meet occasionally to learn and exchange information. He invited his colleagues to a dinner meeting, the outcome of which was the formation of the Chicago Building Managers Organization. The organization held its first national meeting in 1908, with 75 people in attendance. Subsequent meetings were held in Detroit in 1909; Washington, DC, in 1910; and Cleveland in 1911 (at that time a national Building Owners Organization was founded). By 1921, a number of groups had formed in the nation's larger cities and organizational changes were required: the Building Owners and Managers Association (BOMA) became a national federation of local and regional groups. Later, as chapters were

organized in Canada, England, South Africa, Japan and Australia, the name was changed to the Building Owners and Managers Association International.

Most early BOMA members were office building managers, with some participation from apartment and loft building managers. Apartment owners and managers in most of the larger cities formed their own associations during the 1930s, and a national apartment owners' association was created in the 1940s.

The depression of the 1930s had a profound influence on the evolving property management profession. The numerous business failures and real estate foreclosures of this era placed much of the nation's real estate in the hands of mortgage-lending institutions, such as trust companies, insurance companies, associations, credit unions and banks. For the first time, a large volume of income-producing property was owned by corporations. Many of these financial institutions formed their own property management departments. The newly formed management departments employed contractors and builders, but spent little thought and less action on the economics, advertising and merchandising of the income property. Such considerations were relatively unexplored at the time and no facilities were available for training persons in these vital aspects of property management. Property owners soon learned that a landlord has to do more than select tenants and collect rents, and as the need for more sophisticated management techniques became apparent, the property management profession gained stature.

In 1933, a group of property management firms created the Institute of Real Estate Management (IREM) as a subsidiary group of the National Association of REALTORS® (NAR). Currently, all those wishing to join IREM must satisfy education and experience requirements and must pass examinations given or approved by IREM. They are then awarded the designation of Certified Property Manager (CPM) in recognition of their professional status as property managers and their affiliation with IREM. The institute grants qualified management firms the designation of Accredited Management Organization (AMO).

BOMA International sponsors an educational program for property owners and managers through an independent organization, the Building Owners and Managers Institute (BOMI), established in 1970. Individuals with several years of experience in the field and who have successfully completed the program's courses receive the professional designation of Real Property Administrator (RPA). For training building maintenance personnel and facility managers, IREM has developed courses of study for Systems Maintenance Administrators (SMA) and Facilities Management Administrators (FMA). To promote professionalism in the specialized field of retail property management, the International Council of Shopping Centers (ICSC) has developed a series of courses that lead to the designation of Certified Shopping Center Manager (CSM).

The National Apartment Association (NAA), created in 1939, sponsors courses for Certified Apartment Managers (CAM), Certified Apartment Maintenance Technicians (CAMT) and Certified Apartment Property Supervisors (CAPS).

CLASSIFICATION OF REAL PROPERTY

Real property is defined as the earth's surface extending downward to the center of the earth and upward into space, including all things permanently attached thereto, by nature or by human hands. Manufactured attachments are referred to as *improvements*. Given this comprehensive definition, it follows that real property management can cover a wide spectrum of duties. For example, because minerals and agricultural crops are considered to be part of real estate, the management of mines and farms could be considered real property management. In these cases, though, the process of mining or farming is more significant than the management of the land itself. Activities of this nature represent specialized business enterprises and hence will not be covered in this text.

Large enterprises with extensive holdings of real estate, such as hotel and motel chains and grocery and other specialized retailers, will have a property management department staffed with experienced property managers. However, most professional property management involves structures built on real property that are not intrinsic to the operation of a business or industry. For the purposes of studying specialized property management, real estate can be divided into four major classifications: residential, commercial, industrial and special-purpose property. Each type of property requires a different combination of knowledge and skills on the part of the manager. The following is an overview of each type of property.

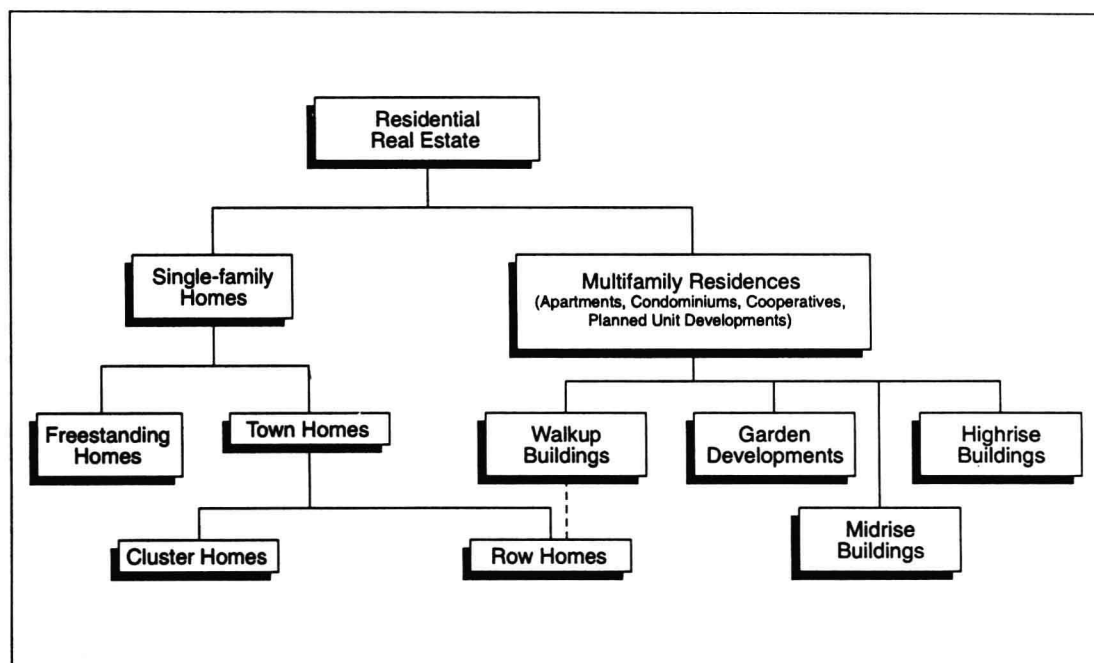
Residential Property

Residential real estate, including privately owned residences as well as government and institutional housing, satisfies the basic shelter needs of our population. It is the largest source of demand for the services of professional property managers.

Single-Family Homes. Freestanding, single-family homes are still the most popular form of residential property in the United States. According to the Census Bureau, 60 percent of U.S. housing is owner occupied. Single-family, owner-occupied homes do not require professional management. However, while single-family homes that are used as rental properties are often managed directly by the owner, there is a growing trend toward professionally managing such properties, particularly condominiums and vacation homes. Many large corporations hire property managers for homes vacated by employees who have been transferred.

The cost of a typical freestanding, single-family home has risen from an average of \$25,000 in 1970 to many times that figure in most of the country today. The average varies from region to region; for instance, it is much higher on the West Coast. Rising construction costs and a decrease in the availability of usable land have resulted in the growing popularity of town houses (or row houses), condominiums and cooperatives, discussed below.

Multifamily Residences. Rising land and construction costs have also stimulated the growth of multifamily housing. According to the Boeckh Index of Construction Costs, the expenses of erecting a building have more than doubled since the base year of 1967, and they continue to increase steadily. The economy of design and land usage inherent in multifamily

FIGURE 1.1 Residential Real Estate Categories

housing allows for a lower per-family cost of construction. Thus, multifamily residences are a rapidly growing segment of the national residential real estate market.

Multifamily residences can be held under various forms of ownership. Small properties of two to six units are often owner occupied and owner managed, whereas most large highrise apartment complexes are professionally managed for their investor-owners. Cooperative and condominium apartments are largely owner-occupied buildings governed by boards of directors elected by the owners. These boards usually hire professional managers for their properties.

Structurally, multifamily residences can be classified as either garden apartments, walkup buildings, or highrise apartments. Each type is unique in its location, design, construction, services and amenities. Figure 1.1 illustrates the interrelationship of several types of residential real estate structures.

Commercial Real Estate

Commercial real estate includes various types of income-producing properties, such as office buildings, shopping centers, stores, gas stations and parking lots. A commercial property is generally considered to be a “public accommodation”—a private entity that provides goods, services, facilities or accommodations to the public. Thus, even though commercial premises are privately owned, the public has certain rights to use them.

There are two principal categories of commercial real estate:

1. Office property and
2. Retail property.

Office Property. Like multifamily residences, office property can be lowrise (walkup) offices, garden developments, highrise complexes or office parks (sometimes called business parks). Whether an office property is situated in a downtown commercial district or in a suburban development, its success is determined by its location relative to the prospective work force, transportation facilities and other business services.

Office property can have several tenants or a single occupant who may or may not be the owner. A number of major corporations occupy their own real estate for business purposes. Such real estate is often referred to as institutional property and is sometimes under the supervision of the corporation's own property or facilities management department. Some multiple-tenant office properties accept any financially qualified business or organization, whereas others cater to one type of business. Medical complexes, dental complexes and trade centers are examples of multiple-occupancy, single-use properties. Management of office property is discussed further in Chapter 13.

Retail Property. Retail property, the second major category of commercial real estate, includes freestanding buildings, traditional shopping centers designated by size (strip centers, neighborhood centers, community centers, regional shopping centers and superregional malls) and specialized centers, such as off-price, factory outlet and specialty centers. The freestanding, single-tenant building is often owner occupied and owner managed. Strip centers usually consist of four to ten stores located on a corner of a main thoroughfare and are designed primarily for convenience shopping. Neighborhood centers are the next largest, containing 15 to 20 retail outlets. Community centers may consist of 20 to 70 stores and serve an even larger area.

Regional shopping centers and superregional malls located in suburban areas are a development of the past 35 years. They have been one of the major contributing factors to the decline of the centralized urban commercial district. The size of these shopping centers and their diverse tenant mix make professional management a necessity. The success or failure of a shopping center often hinges on the property manager's ability to assess the market, to conduct sales promotion and public relations and to act swiftly and decisively. Regional shopping center management provides one of the greatest challenges to the skills of the professional manager.

Factory outlet malls have become increasingly common specialty shopping centers; they offer brand names at discounted prices. The general categories of commercial real estate are illustrated in Figure 1.2.

Industrial Property

The industrial process converts raw materials into finished products. It comprises all activities involved in the production, storage and distribution of goods. Industrial property includes all