OPTIMIZING PROFESSIONAL SERVICES REAL ESTATE PORTFOLIOS FOR EVOLVING NEEDS

After a period of rapid change during the pandemic, evidence suggests hybrid work is here to stay. As professional services firms adjust to **shifting workplace norms** — reevaluating their real-estate portfolios and workforce policies — one overarching priority has emerged: flexibility.

RATIONALIZE THE REAL ESTATE PORTFOLIO

Recent market volatility and uncertainty have added complexity to the shifts already underway in corporate real estate. The combined pressures of high inflation, rising interest rates and an ongoing talent shortage should create a sense of urgency for businesses to rationalize their real estate portfolio and develop a comprehensive workplace strategy. This process can reduce unnecessary costs and leasing liabilities while companies reimagine the workplace to better support business objectives and workforce needs.

Generally, there continues to be a disconnect between senior leadership and staff about workplace policies. Trends show leadership prefers more in-office time, whereas employees prefer a higher degree of flexibility in determining where, when and how they work to maximize productivity. But senior leadership should keep in mind that the office by itself does not create culture and engagement; it is an enabler for the development of that culture.

Therefore, the most critical element is not where one works but rather access to resources. Access to managers, coworkers and other support is required. That access can be achieved through many channels, not just through in-office time. Using accessibility as the foundation for creating a workplace strategy will drive the greatest success in developing an innovative and engaged workforce. The goal should be progression toward agile space, not more space, and the end result can also deliver material cost savings.

Portfolio optimization may seem like a daunting task, but the steps are straightforward. Start by understanding the current state as a baseline across people, process and technology. Examine the portfolio holistically and benchmark total occupancy cost internally and externally. Design the future state, including a workplace strategy that supports the mission, vision and values of the organization. Identify gaps between current and future state.

From there, build a robust implementation roadmap that may include specific actions, such as:

- Evaluating organizational structure to ensure it is optimized with the right roles, capabilities, responsibilities, layers and spans.
- Analyzing the insource/outsource balance — reconsider what is core to real estate and facilities management.
- Completing contract compliance audits for material outsourced master services agreements and contracts.
- Blending and extending locations that are near the end of their term — relevant to those locations that remain core to the company.
- Reviewing the technology stack to improve integration, automation and data analysis.
- Redefining fit-out standards that align to the workplace strategy.
- Subleasing underused space.
- Redesigning space to address shifting needs (i.e., a mix of collaborative and focus spaces).
- Implementing hoteling to enable greater flexibility than dedicated desks and offices (i.e., move away from a 1:1 seating ratio).

Flexibility is an imperative, allowing an organization to be responsive to ongoing volatile market conditions. Signing short-term leases or leases with early termination options, expanding functions that can be outsourced/contracted, using co-working space and other tactics will create a nimbler corporate real estate portfolio.

DEVELOP AND UPDATE THOUGHTFUL WORKFORCE AND WORKPLACE STRATEGIES

Every professional services organization should have a cohesive, forward-looking workforce policy and workplace strategy that clarifies options for hybrid and remote work. Gather employee input to understand how different departments, functions and roles conduct work, and then shape the policy accordingly. Communication and employee buy-in are vital to policy implementation and adoption. This can be accomplished through well-structured employee surveys that incentivize honest feedback and include active involvement from leadership.

Workforce policy should vary by the specific role or department and prioritize different ways of working. Consider the following three examples:

- Employees in legal departments often function well at their desks in the office; they may also have professional obligations around confidentiality that present challenges for remote work.
- Sales teams are often in the field to meet with clients or prospects, and may benefit from a remote work policy.
- IT professionals may be suited to a hybrid approach that balances remote work (e.g., monitoring systems and leveraging cloud-based platforms) with in-person tasks (e.g., solving network or hardware problems and meeting with employees about device issues).

A policy is not the same as a proclamation. For example, a blanket proclamation would be a high-level directive that is unstructured and does not drive the intended behaviors, such as: “everyone must be in the office at least three days per week.” By contrast, a policy defines why employees need to be in the office three days per week, and it could even specify which days if the main purpose is to drive productivity, encourage collaboration and strengthen corporate culture. A structured policy also allows leadership to plan for space needs, amenities and services, which can help leverage economies of scale throughout the organization and potentially reduce total occupancy cost.

Inflexible policies are more likely to meet resistance — or even lead some employees to seek jobs that offer greater flexibility. The policy should fit employees’ work habits and encourage workplace engagement. Giving agency to middle management helps them address their direct reports’ specific needs and avoid pushback about overly rigid policies.

A fully remote model may pose challenges for maintaining company culture. A flexible policy with an in-person component can support collaboration and connections between colleagues. Each organization should assess its own needs to determine the workplace model that will most successfully balance key business objectives and employee needs.

5 TAX CONSIDERATIONS FOR REMOTE AND HYBRID WORK

Tax is an important factor in any cost-benefit analysis of real estate. Adopting new workforce models can impact operating expenses and tax liability, so it is important to forecast both the initial and longer-term impact of any changes. Consider the following five areas when developing or updating workforce policies.

1. **Jurisdictional variation:** Decisions about the real estate portfolio and hybrid work have implications for state and local taxes (SALT) that vary by jurisdiction. Some jurisdictions impose an additional rental tax. New York City, for example, taxes a business tenant on rent paid in Manhattan under the Commercial Rent Tax, while Florida imposes a sales tax on the tenant for rental payments to the landlord. San Francisco, on the other hand, levies a tax on landlords that applies to leases and subleases.

2. **Credits and incentives:** It is also critical to understand all applicable tax **credits and incentives**, especially when expanding or relocating. The site-selection process should maximize incentives and weigh business objectives against the benefits and risks of potential sites. For companies benefitting from SALT credits and participating in incentives programs, a change in employee headcount in a jurisdiction or a change in commercial office space may impact the terms of their tax and financial business incentives. Such changes should be addressed with the applicable economic development agencies.

3. **Property tax:** A property tax assessment can reveal **opportunities for an appeal and reduction.** Businesses should assess any potential advantages afforded by certain filing positions or potential discounts for early payment. A remote workforce may result in a business having personal property located in the state that is subject to a tax filing.

4. **Remote work and payroll withholding taxes:** Tracking the location of **remote employees** is another important factor that impacts state and local payroll withholding taxes and business taxes. To avoid undue surprises, organizations should have a system in place to determine proper withholding jurisdictions for remote and hybrid employees' payroll. State payroll withholding requirements vary greatly, with some states requiring withholding where the employee provides services (whether in office or remotely). However, six jurisdictions, notably including New York state, may require withholding for nonresidents assigned to the New York office despite the fact that they work remotely outside New York State most of the tax year. This is known as the convenience of employer rule.

5. **State and local business tax nexus:** Many businesses will be expanding their tax nexus footprint into jurisdictions where they have no offices but do have employees working remotely. Businesses are encouraged to periodically evaluate their state and local corporate income/franchise tax filing obligations, as well as partnership filing obligations based on the location of the workforce.

For more information, visit BDO's **State and Local Tax practice** and the **Site Selection and Incentives practice**. You can also view our **SALT Health Check** and **Global Equity Mobility Solution** for additional support.

FOSTER A STRONG CULTURAL CONNECTION

Now is the time for professional services firms to review their real estate holdings. An optimized portfolio can provide a competitive advantage, and delaying a portfolio review may prove costly. By right-sizing the real estate portfolio based on business and workforce needs, companies can support their people while achieving key objectives and driving continued success.

Contact BDO's dedicated **Professional Services practice** to speak with one of our experienced professionals and learn more.

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