GOODWIN

Envisioning the New Normal:

Real Estate + Life Sciences

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Part 1: Leasing Models in Life Sciences and How They Correspond to the Life Cycle of a Company

The real estate needs of life sciences companies can be fluid and complex, with early stage companies typically needing smaller flexible space and later stage companies typically requiring larger build-to-suit space. With an equally diverse group of life sciences landlords and business terms on the table, there are many variations of leasing models and terms to be negotiated between the parties. However, perhaps as a result of a natural life cycle of a life sciences company, there are currently three major types of leases emerging in the U.S. for companies seeking space for research and development and laboratory uses.

1. The Flexible License Model: Space for Early Stage and Pre-Series A Companies

The first model, often described as an "incubator," "accelerator" or the "WeWork" model of life sciences, focuses on a service-heavy, short-term approach to providing space. Incubator deals are typically done as licenses versus a full-fledged lease, often running on a month-to-month basis and terminable by either party upon 30 days' prior written notice. Just like the typical co-working model, there is a great deal of flexibility built into what these licenses look like and how much space is available. Some are on a single lab-bench basis, while others can offer several pages of what we like to call "turn-key" services (i.e., you turn the key and you are in the space and ready to operate). Others tout the ability to network with a stable of other entrepreneurs and even VC-funders as a benefit to licensing space. No matter the amenities provided, one thing remains the same: these spaces are attractive regardless of the high monthly price tags because it is one less expense that the user has to invest in to get up and running.

Just how attractive is this incubator or accelerator model? A search for incubator space in the Greater Boston, Massachusetts market came back with almost thirty providers who specialize in life sciences spaces. The current offerings run the gamut from both life sciences and real estate industry-titans like **Alexandria Launch Labs** and AstraZeneca's **Boston Biohub Incubator**, to the rise of incubator-specific asset providers such as **SmartLabs**, which currently has three separate locations within the Boston/Cambridge market and a location in South San Francisco. On the U.S. West Coast (with biotech clusters predominantly in the Bay Area, San Diego and Seattle), this model is similarly popular, with spaces being offered by Alexandria Real Estate Equities, Inc., EvoNexus, JLABS and MBC BioLabs, just to name a few.

In large cities such as New York where space is at a premium and there are extensive restrictions on zoning and permitting for wet lab spaces, incubators not only serve as an affordable workspace option for early-stage companies, but as an opportunity to build small biotech communities within the city, oftentimes near one of the city's universities. Examples include BioLabs in lower Manhattan (affiliated with NYU Langone) and the SUNY Downstate Incubator and BioBat in Brooklyn (affiliated with SUNY Downstate Health Sciences University), in each case taking advantage of the support provided by being associated with a university ecosystem. In up-and-coming markets like North Carolina which boasts the "Research Triangle" area of Raleigh-Durham-Chapel Hill, there are over a dozen incubator providers listed on the North Carolina Biotechnology Center's website.

Incubators are attractive to early-stage and pre-Series A companies as an opportunity to meet and network with peer companies and potential investors and collaborators. Many of these incubators provide educational programming and mentoring opportunities for their companies, as well as host events to attract the biotech community to their spaces. The JLABS incubators, launched by Johnson & Johnson, are an example of how big pharma can actively become involved with supporting and mentoring early-stage companies.

2. The Shorter-Term Lease Model: Space for Series A Companies

The second model, or what we like to call "incubator-lite," has a set list of often capital-intensive services that a landlord is able to provide to its tenants. While these are often done as actual leases, the terms tend to be for shorter periods (often two to three years). The spaces are often taken on an as-is basis, without the large tenant improvement allowances seen with longer-term deals. Landlords maintain more control over what happens in and to the space in terms of tight restrictions on the alterations permitted given the relatively short life cycle of a company in the space.

Services for this model can vary, but most often include conference facilities and common lab support areas and equipment for things like autoclaves and glassware washers/dryers, and the systems (and any required permits) for shared pH neutralization, high purity water, gasses, etc. The prevalence of this type of life sciences offering is often based on the ability of an owner/developer to make an offering on a building-wide basis. In the Greater Boston, New York City and West Coast markets, for example, Alexandria has been able to designate certain buildings in its portfolio to allow for this type of model, known as the Alexandria Science Hotel. King Street Properties new project, InnoLabs, in Long Island City, New York, has the opportunity for at least some of its space to be the latest in this incubator-lite model, with its **online brochure** showing floor plans that are able to accommodate anywhere from a single tenant to up to three tenants on its nearly 46,000+ square-foot floor plates, and a list of amenities targeted toward biotech users.

While the owner benefits from the ability to charge higher rents based on the increased level of service, this model may be attractive to companies who are ready to leave the incubator nest but not quite ready to commit the necessary capital to a long-term lease proposition. Typically start-ups begin thinking about moving towards an incubator-lite model at the time they seek a Series A financing. This is at a time when the company is typically either in the discovery phase or the pre-clinical phase and has grown to a point where it is interested in a larger space where it can determine how to build out and customize such space for its own needs. At the same time the company can benefit from a space that offers some of the common facilities, such as conference space and laboratory support areas, as described above.

3. The Longer-Term Lease Model: Space for Series B Companies and Beyond

The third and final model is more in line with other asset classes, and involves little to no landlord-provided services. Other than perhaps a pH neutralization system in a multi-tenanted building, and possibly the ability to tie into a life safety generator up to a few watts per square foot of the leased space, a landlord often has little to no responsibility outside of the common areas of the property. The leases are often for a 7-10 year period or more, with many times one or two extension options for several years each. Given the investment required by a tenant, this is where we see large tenant improvement allowances, sometimes exceeding $200 per rentable

square foot of the leased space. While this may seem like a large number, given some specialty GMP spaces can more than double that cost on a per square foot basis, this leasing model is also capital intensive on the tenant's end.

By the time a company gets to its Series B or C fundraising rounds and gets to a clinical phase of development, it has grown to the point where it needs to invest in its own space. Companies at this stage of life often need to weigh their financial situation, including their burn rates and pipelines, in order to ensure they are right-sizing their capital commitments for long term leases. Several landlords in this area have also gotten creative with offering a second tier of improvement allowances, which amounts are amortized at a certain percentage on a straight-line basis over the term of the lease. This type of creativity in lease concessions can often be attractive to companies looking to fund significant build out costs.

From the short-term license to the long-term lease, as life science companies move through their life cycle, their needs with respect to physical space will evolve along with the science. With many new owners and investors potentially pivoting towards this asset class alongside industry veterans, it seems like the sky is the limit as to innovation and growth both for and in partnership with life science companies.

Part 2 Preview: Review of Joint Ventures in Life Sciences Real Estate Deals

In the next article in this series, we will consider specific features of the PropSci sector that make a joint venture model an attractive proposition for prospective market players and review the key terms that market players may wish to consider before embarking on a PropSci joint venture.

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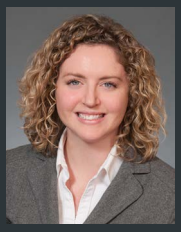

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