Investment Due Diligence:
Evaluating
Income-Producing Commercial Properties

How Investors Assess Performance, Tenancy, & Upside Potential

By **Chuck Heller, SIOR** | *Executive Vice President*

Commercial real estate has long been one of the most reliable vehicles for building wealth – but only when you buy the right asset at the right price with a clear-eyed understanding of what you're getting into. For investors acquiring income-producing properties, due diligence is the process of separating the genuine opportunity from the deal that only looks good on paper.

This final article in our four-part Commercial Real Estate Due Diligence series addresses the investor's perspective: how to evaluate financial performance, assess tenant quality, understand the lease structure, and identify where the real upside lies in a commercial investment.

"Investment due diligence is about understanding the story a property tells over time, not just today's rent roll. You want to know where this asset is going – not just where it's been."
— Chuck Heller, SIOR, Executive Vice President

Investment Due Diligence vs. Owner-Occupant Due Diligence

As we noted in Article 1, the investor's due diligence framework is fundamentally different from an owner-occupant's. When you're buying to occupy, you're evaluating fit for your business. When you're buying to invest, you're evaluating the asset's ability to generate reliable income and appreciate in value over time.

Physical due diligence still matters – but the lens changes. For a NNN-leased investment where the tenant bears maintenance and operating costs, a worn HVAC system may be less urgent than for a gross-lease multitenant building where those costs fall to you. Context is everything.

Evaluating Financial Performance

The Current Rent Roll

The rent roll is the starting point for any investment analysis. It tells you exactly who is paying what, when their leases expire, and what escalations are built in. During due diligence, verify the rent roll against actual lease documents – don't rely solely on what the seller tells you.

Key items to confirm:

- Current rent rates for each tenant vs. market rates – is the property over- or under-rented?
- Lease expiration dates and renewal option terms
- Base rent escalations – fixed annual increases, CPI adjustments, or flat rates
- Tenant concessions still in place – free rent periods, landlord-funded improvements, etc.
- Operating expense recovery structure – gross, modified gross, or NNN

"I always tell investors: the NOI the seller presents is the best-case story. Your job during due diligence is to stress-test that story. What happens if a tenant doesn't renew? What happens if the roof needs replacing in year three? A well-underwritten deal survives those scenarios."

— Chuck Heller, SIOR, Executive Vice President

Analyzing Expenses

Income is only half the equation. A thorough review of operating expenses – property taxes, insurance, utilities, maintenance, management fees, and capital reserves – is essential to understanding true net operating income (NOI) and the accuracy of the seller's presented financials.

Request three years of operating statements and verify major expense line items against actual invoices where possible.

Tenant Creditworthiness and Responsibility

The quality of your tenants is arguably the most important factor in a commercial investment. A property's income is only as reliable as the tenants producing it.

Evaluate each tenant's:

- Credit profile – for national or publicly traded tenants, credit ratings and financial filings are available; for private tenants, request financial statements
- Lease guaranty structure – personal guarantees, corporate guarantees, or letters of credit
- Operating history at the location – long-tenured tenants with demonstrated sales or operational success carry less renewal risk
- Industry and business health – is the tenant in a growing or contracting sector?

In NNN lease investments – where the tenant is responsible for taxes, insurance, and maintenance – the creditworthiness of the tenant is particularly critical, since their financial health is directly tied to your ability to collect rent and maintain the property.

Understanding Upside Potential

Sophisticated investors don't just buy what a property is today – they buy what it can become. During due diligence, analyze the potential upside across three timeframes:

Short-Term: Built-In Escalations

Review the lease documents for scheduled rent increases already in place. These escalations represent guaranteed income growth without any action required on your part, and they directly improve your yield over time.

Mid-Term: Re-Tenancy and Repositioning

What happens when leases expire? Analyze the spread between in-place rents and current market rates. If tenants are paying below market, lease renewals or re-tenancy represent an opportunity to improve income. Conversely, if in-place rents are above market, renewal risk is elevated.

Consider also whether the building could be repositioned – a multi-tenant office building converted to medical or flex use, or a retail center repositioned for a different tenant mix – to capture higher market rents or serve a stronger demand driver.

Long-Term: Redevelopment

In select situations, land value, location quality, or zoning flexibility create longer-term redevelopment optionality. This is more relevant for certain retail locations and underutilized industrial sites in growing submarkets.

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In south central Pennsylvania, we've seen investors unlock significant value in properties that others overlooked because they only evaluated current income. The Harrisburg and York markets in particular have pockets of strong repositioning and redevelopment opportunity if you know where to look."

– Chuck Heller, SIOR, Executive Vice President

Financing and Its Impact on Investment Returns

Financing terms fundamentally shape the return profile of any commercial investment. Key considerations during due diligence include:

- Loan-to-value (LTV) ratios – most commercial lenders will lend 65–75% of appraised value
- Interest rate and term – fixed vs. variable rates carry different risk profiles
- Debt service coverage ratio (DSCR) – lenders typically require NOI to exceed debt service by 1.25x or more
- Prepayment penalties and loan assumption possibilities – relevant if you plan to sell before maturity
- Personal vs. non-recourse debt structure

The financing period often runs concurrently with physical and business due diligence. Your lender will typically commission their own appraisal and environmental review, so coordinating these timelines with your broker is important to keep the deal on schedule.

Closing Thoughts: Due Diligence as a Discipline

Across all four articles in this series, one theme has emerged consistently: due diligence is not a hurdle to clear on the way to closing. It's the professional discipline that separates informed buyers from reactive ones, and successful long-term investors from those who learn hard lessons on their first deal.

Whether you're an owner-occupant evaluating your first commercial property in Lancaster or York, or an experienced investor adding to a portfolio across the Harrisburg region, the fundamentals of sound due diligence remain the same: be thorough, work with qualified professionals, and let the facts guide your decisions

"Every great deal I've been part of over the years has one thing in common: the buyer did their homework. Due diligence is where that homework gets done. My job is to make sure my clients ask every question that needs to be asked – before it's too late to ask it."

– Chuck Heller, SIOR, Executive Vice President

Exploring CRE Investment Opportunities in South Central Pennsylvania?

The Harrisburg, York, Hershey, and Lancaster markets offer compelling investment opportunities for buyers who know where to look. Chuck Heller's deep market knowledge and transaction experience help investors identify assets with strong fundamentals and genuine upside potential.

Contact Chuck today to explore available investment properties.

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About This Series

This article is the final installment of our four-part Commercial Real Estate Due Diligence Series. We hope these articles have given you a solid foundation for your next acquisition. For the full series, visit Landmark Commercial Realty's website or contact Chuck Heller directly.