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# To Buy Or To Lease?

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## "TO BUY OR TO LEASE?" THIS IS ONE OF THE MOST IMPORTANT BUSINESS DECISIONS THAT EVERY COMPANY MUST CONSIDER AT SOME POINT.

The conclusion can differ for two companies of the same size in the same industry, as the factors require weighing where the business is in terms of its place in the maturity cycle.

For example, leasing may make sense for a rapidly expanding start up company that is burning through cash for expansion and whose needs for space are increasing. Flexibility to adapt to these changing needs and a need to re-invest profits make this decision simpler.

In contrast, a mature business may prefer to control its location and will have stable space needs and a along tern view toward property appreciation, plus a desire to control costs. As such, they may be a more ideal candidate to buy.

Between these two extremes there are many companies that need to look inward to determine how to weigh the buy vs. lease decision based on the advantages and disadvantages of each and how these options fit their individual business plans and cash situations.

Some of the reasons companies and firms cite to buy office space include:

- Investment (equity growth)
- Personal control of domain (no dependence on landlord to modify or improve the space, or grant consent to tenant to do so

- Business continuity (no threat of costly business disruption based on landlord's decision top not renew lease)
- Customize space to subjective needs (adding value to a company asset)

- Tax benefits (the ability to write off financing interest and depreciate the building)
- Deferral of payment of the capital gains tax at time of sale under Internal Revenue Code Section 1031 by arranging an exchange of a "like-kind Property."

To purchase office space, financial institutions often require a 20% down payment to obtain a load. This means tying up money in a long term commitment, which is often difficult to liquidate quickly.

Partnerships face additional risks. Often when there is a partnership dispute or dissolution, all of the assets of the company are tied up until the business is divided and liquidated. In such circumstance it may take sometime until the equity is made available.

Buyers that leverage considerable debt against the property value should analyze their monthly ownership costs and factor in debt service. The monthly expense could far exceed monthly lease payments and the equity build-up could be extremely slow. Moreover when evaluating the monthly costs one must consider the taxes, insurance, maintenance, and potential disaster recovery cost.

A major benefit to ownership is the ability to write off costs associated with acquiring and owning the real estate, Deductible ownership costs include mortgage interest, real estate taxes, insurance, repairs and maintenance. Over the ownership period, this can add up to significant savings.

According to Scott F. Berger, CPA with Kaufman Rossin & Co. commercial property is typically depreciated over a 39 year life; however, certain building costs can be recovered over shorter write-off periods, thereby accelerating cash-flow. This is accomplished by carving out shorter-lived assets that are normally embedded in a building's construction or acquisition costs. In some cases, the speed is 15, 7 or 5 years. Accelerated depreciation can save businesses thousands of dollars.

Additionally, upon disposition, capital gains taxes must be paid to the government if the property appreciates, and if it does not appreciate, losses can provide a shelter for other income.

Alas, while ownership has its privileges, it is not for everyone. Many companies benefit more from a leasing arrangement because it provides:

- Flexibility to address changes in the company because some firms can't forecast their needs more than 3-5 years out.
- Savings in capital (other investment opportunities may be more profitable)
- Ease with which to quickly increase or decrease square footage or even dispose of the space entirely when not encumbered by ownership
- Less risk and obligation because landlord is responsible for maintenance and repairs of the property
- Lower monthly payments that enable executives of growing companies to re-invest their business capital, reduce company debt, or pay interest on business rather than the up capital in a down payment on a purchase
- Tax benefits that allow a company to deduct the rent and general operating expenses associated with their office space.

The freedom and flexibility associated with leasing can provide office tenants with easier exit strategies when unanticipated change affects them. Some of these exit strategies are sub-leasing and assignments as well as negotiation of lease terminations with landlords. These devices can help companies change course with minimal dedication of time and risk. These rights, however, are not automatically granted. Often they must be negotiated up front in the original lease so they can be exercised later if necessary.

While there's no sweeping rule for deciding whether to lease or own your business' commercial space, the pivotal question is: Based on a carefully analyzed cost comparison between similar space for lease and purchase, do the rewards justify or outweigh the risks?

Fortunately, you are not alone. An exclusive tenant/buyer representative will take the time to understand you company's industry, history, and anticipated future. They will know your investment position and objectives, and working with your expert tax and legal counsel, and will help you make the right decision.

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