

PURCHASING VS. LEASING: IS IT TIME TO BECOME YOUR OWN LANDLORD? With Vice President, Suzanne Lee

What to consider in your office options

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Question:

Owning one's commercial office space is far less common than leasing. What are some of the advantages of owning?

Suzanne Lee:

For one thing, an owned asset in most markets, and depending on the property's condition or suitability for improvements, provides an opportunity to create future value. This makes mortgage payments on a commercial property a strategically prudent investment when properly maintained.

Additionally, interest rates remain at historic lows and will remain so for the foreseeable future. Using a Small Business Administration loan, one may lock-in a loan with rates still hovering between 4.5 and 5.5 percent for up to 25 years, with only 10 percent down. However, lending requirements have become significantly more stringent recently. Even if you do not remain in the building long-term, there is potential for significant upside in its resale.

Q: By owning, you become your own landlord. What are some of the other financial upsides, in terms of having more control over your business?

A: Certain costs associated with owning and operating commercial property, such as interest payments, depreciation and property taxes, are tax-deductible. Many companies find this to be economically favorable compared with leasing, particularly on a post-tax basis. And, putting yourself in your own space can bring excellent opportunities for corporate image-building. You have near-complete control over signage, design, amenities, parking and nearly every other aspect of your business as reflected in your base of operations. This may be especially beneficial for specialized businesses, where improvements are specific to a particular industry, healthcare for instance.

Q: What are some downsides to owning?

A: You have all the day-to-day responsibilities of a landlord. Repairs, maintenance, insurance, security - all these land in your lap. Although such tasks can be outsourced to a property management firm, many first-time owners underestimate the time involved. As compared with leased space, which can be upgraded to suit tenants, properties for sale are typically available only in their current condition, which may not be a

perfect fit for your needs. However, this issue can be addressed by having rehabilitation or improvement funds built into the financing.

As opposed to leasing, where costs are amortized over many years, you may have significant upfront costs before move in. The down payment and other closing costs could significantly impact a business's short-term cash flow. Additionally, many buyers have time remaining on a lease at their previous space and may be responsible for debt service on the purchased property, along with their lease payments, while waiting for their lease to expire.

Other risks of ownership include the danger of outgrowing your space, or conversely, encountering a need to downsize. Your options are limited in both instances. And, in general, by being an owner, you are entering into a second business as a landlord/investor, subject to all the ups and downs of real estate values.

Q: It is still a tenants' market out there. What are some of the top advantages of leasing?

A: Responsibilities are far fewer and flexibility is greater with respect to facilities management. Many landlords will provide excellent, professional build-outs or improvements to suit your precise needs. Leases are generally easier to budget. Landlords still offer good-credit tenants top-line concessions in the form of low rental rates, free rent, tenant improvement allowances, discounted parking, signage and moving allowances. Early lease renewals - "blend and extends" - provide an excellent way to restructure the lease and significantly reduce occupancy costs in advance of a tenant's scheduled lease expiration.

Q: What about the new Financial Accounting Standards Board (FASB) rules? Will that change the lease vs. buy analysis?

A: Under current FAS13 standards, leases are treated as "off-balance sheet" transactions which many businesses prefer. However, with the proposed changes to lease accounting, leases will be "coming on" the balance sheet. This will make the financial impact of leasing more comparable to owning real estate.

To learn more on how FASB may affect you, [click here](#).



SUZANNE LEE specializes in representing companies and organizations in the leasing, purchase and sale of commercial real estate. As part of Transwestern's corporate advisory services team, she is responsible

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