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Best in Law: How a Business Owner Can Weigh Buying vs. Leasing

BB&K Partner Peggy Hosking Examines the Pros and Cons of Both in the *Riverside Press-Enterprise*

By **Margaret A. Hosking**

Making an investment in real estate can be a valuable long-term venture for business owners – one that can continue to generate revenue even if a business moves on or is sold.

The buy-versus-lease consideration is something many business owners will eventually face. What do you do? Do you buy a business space or continue to lease? Pros can outweigh cons when it comes to investing in commercial real estate. The move, however, may not be right for every business.

There are a few points to consider before taking the plunge into commercial property ownership.

First, ask: What are the advantages of owning versus leasing commercial real estate?

If you have an attractive lease in a great location, you may not want to consider purchasing.

On the other hand, it is easier to control fixed costs when you own the property. Owning a building creates security in that you will not have to renegotiate a lease – or lose your location to another tenant.

Loss of a lease can create significant relocation costs and you may not be able to secure favorable lease terms.

You can also maintain more control concerning repairs, maintenance and improvements if you own. If you have a retail business, you may want to repave the parking lot or paint your building more frequently than a landlord. Or, you may wish to customize improvements to improve business efficiency.

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If improvements are planned down the road, the property may serve as security to finance enhancements.

There may also be tax advantages to owning your own property, such as building depreciation, incentives for energy-efficient upgrades and building improvements.

If you have future plans to expand your business, you may purchase a property larger than your current needs and lease the extra space creating additional income.

Consider the long-term plan for your business. Will you sell and retire? Retain ownership of the property and lease it to the next business owner? Or will the real estate make the business more attractive to a buyer?

Next, take a look at the business' current cash flow. Do you have the cash flow to purchase? What financing is available through your existing banking relationships? Will you take on a tenant (or two) to cover expenses until your business is large enough to take over the entire space?

Don't hesitate to discuss a potential real estate acquisition with your attorney and accountant. Typically, they have good working relationships with commercial real estate agents and lenders and can help you structure an acquisition in the most advantageous way for your business.

Even if your current bank doesn't have a loan product that is suitable for your needs, there may be other programs to consider, such as private loans or an SBA 504 loan from the U.S. Small Business Administration.

Interest rates have been very appealing for the past several years. However, this may not continue. Is now the time to lock in your interest expense for the future?

When purchasing commercial real estate, business owners should consider setting the property up in a separate entity. There are distinct advantages to holding real estate separate from your operating entity.

For example, you might purchase real estate through a trust, thus allowing the transfer of the real estate through your estate plan. Or, consider an LLC. Members of the LLC may be family members, business partners or private lenders. Holding real estate assets separate from your operating business assets may also safeguard a business from potential liability.

Finally, holding real estate in a separate entity allows you to retain the real property if the business is sold, maintaining a revenue stream as a landlord.

Commercial real estate assets also have a good risk/reward profile compared to other investments like stocks, savings or bonds. Owning real estate not only gives businesses leverage, but also has the potential for high cash earnings, equity accumulation and numerous tax breaks.

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