



Office Space: Lease VS. Buy

Many businesses reach a point in which they are curious as to whether it would be beneficial for them to purchase office space rather than continue to lease office space. While every business is different there are a few common factors that should be taken into consideration when evaluating whether buying office space would be better than continuing to lease office space. We will take a look at some of the pros and cons to purchasing compared to continuing to lease office space.

- 1. Cash Outlay** - Typically if you are planning to purchase an office, you can expect to make a down payment of between 10% and 25% of the purchase price, depending on the lender and your credit. When you lease office space you won't need to put down nearly as much. With good credit, the typical outlay is the first and last month's rent which is only about 10% to 15% of the cash outlay required when purchasing office space.
- 2. Opportunity Cost** – With the large outlay of cash required to purchase office space, the opportunity cost of that money needs to be taken into consideration. What return would you expect to receive on that money compared to the return you would expect to receive if you invested the money back into your business or into other investments?
- 3. Fixed vs. Variable Cost** – When you buy office space, you have a good idea what your costs will be over the long term. This is especially true if you have a long term fixed rate mortgage. If you lease office space, the market will dictate what you will end up paying for rent over the long run.
- 4. Growth Considerations** – The growth phase of your business should be a major consideration in making the lease vs. buy decision. If your company is relatively new and/or in a high growth mode, leasing would allow more flexibility and fewer constraints to that growth. On the other hand, if your company is mature and stable, buying office space is great way to meet your future office space needs.
- 5. Property Management** – You've heard the expression, time is money. If you own office space, it needs to be managed. You can either hire out the function or do it yourself. Many businesses with long term growth plans buy more office space than they need and rent out the expansion space. All the more need for good property management.





6. **Appreciation** – One of the primary goals of buying office space is to generate long term increase in value through market appreciation. A good idea in a healthy market and usually successful over the long term. It is usually a good way to add to your retirement fund, but keep in mind that recent commercial real estate cycles have come in 10 year periods.
7. **Tax Factors** – Lease payments are usually fully deductible, but many expenses of owning office space must be written off over longer periods of time of up to 39 years. The good news if you buy is that you get to take depreciation on the improvement portion of the property and can usually deduct all of your interest payments. When considering the tax factors it is always very important to consult with your attorney and tax professional about the legal and financial considerations to owning office space.
8. **Cash Flow Analysis** – The devil's in the details. In order to really understand the financial aspect of purchasing office space, you need to prepare a detailed comparative net present value cash flow analysis which takes into consideration your predictions on the future including holding period, anticipated appreciation vs. rental increase, interest rates, and cost of expenses increases. It is a good idea to do three different analyses, optimistic, realistic and pessimistic, to help determine your margin of error. It seems like a daunting task, but we have programs available to help you do this analysis.
9. **The next Step...**
While the evaluation of the leasing office space vs. buying office space decision seems somewhat overwhelming, there is help. Getting advice and assistance from a commercial real estate professional who is involved in the business day in and day out can significantly improve not only the accuracy of any analysis, but in general simplify the process. Many of the lease vs. buy factors can only be decided by you, but having a helping hand in the areas where office space expertise is important will assure you of making the best possible decision.

