WOODSIDE HEALTH

Real Estate
Education Series

Lease vs. Buy
Which is right for you?

Focusing on your core medical expertise, whether that be ophthalmology, family medicine, dentistry, or any other medical field, can yield the greatest economic returns for you personally.

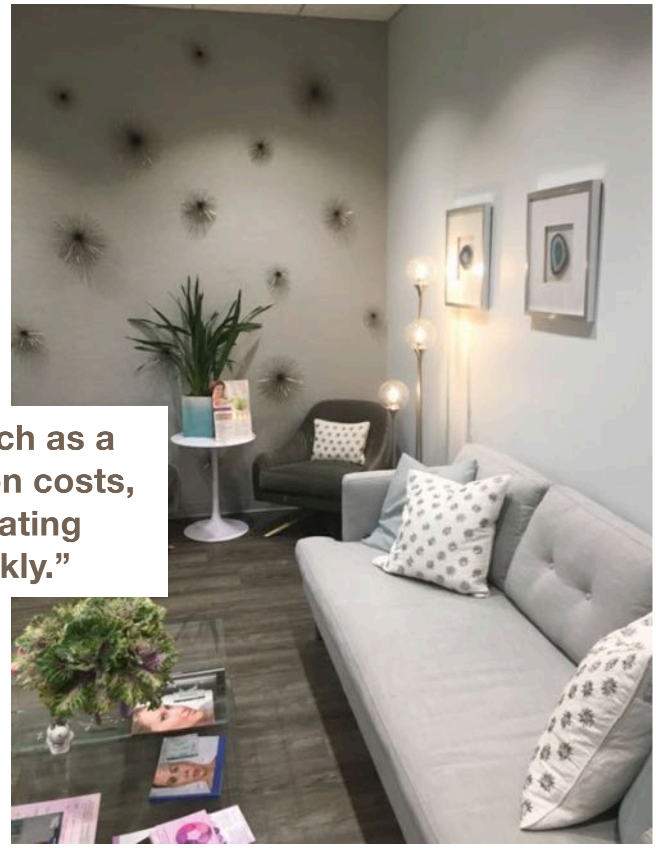
Most of us do not grow our food, fix our own cars, or build our own medical equipment. Doing these things may save a little money, but your time is likely better spent in your areas of expertise. Similarly, studies show medical professionals tend to be far more profitable when they lease space rather than buy and manage their own building.

If you've considered buying a building, you may be interested in comparing the lease vs. buy scenario. In this paper, we'll briefly explore four aspects of decision making: Financial Requirements, Risk, Flexibility, and Opportunity Cost.

Ted Barr
Principal

Financial Requirements

Leasing your space carries lower up-front costs, whereas owning typically requires more capital up-front. Ownership expenses such as a down payment, transaction costs, renovation costs, operating cash and operating reserves can add up quickly. Leasing can help practices preserve liquidity, which is particularly beneficial to start-ups and practices looking to fuel growth.



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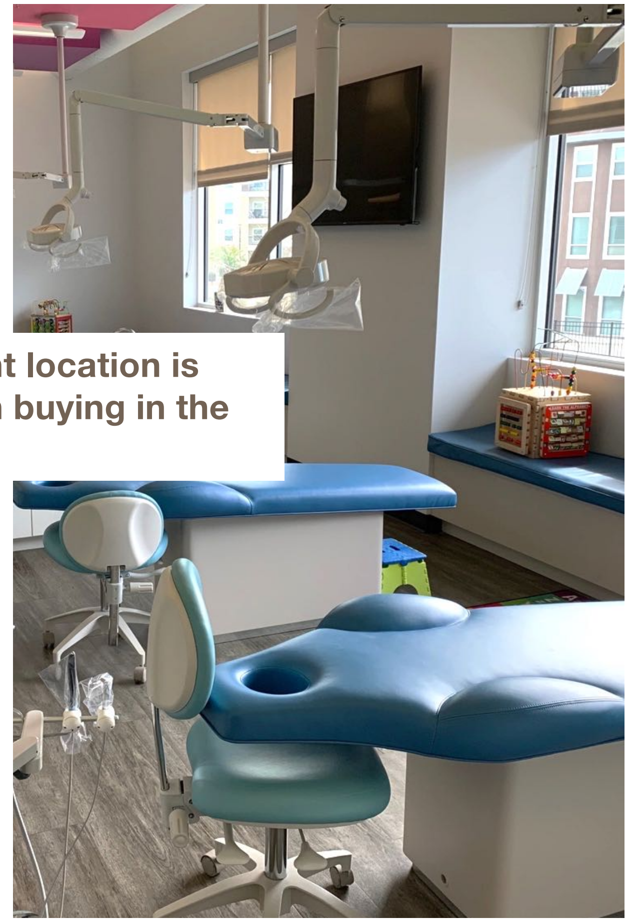
Higher up-front costs of ownership can pay off, however. Owners can build equity and make long-term commitment to realize potential capital gains, but this strategy often takes 15 or more years to pay off.

Risk

Typically, real estate owners bear the brunt of risk. Unexpected capital expense surprises like roofs, parking lots, HVAC, and storm damage can be very expensive. Owners are also subject to external influences such as a nearby hospital moving or the neighborhood deteriorating, which can have a material impact on their tenants' businesses as well as their property value.

While a tenant can move to a better building or location at the end of their lease, an owner doesn't have that flexibility.

Additionally, owning the building where your business is located lumps both your real estate risk and your professional risk in the same basket. Many practices prefer to mitigate that risk by leasing their practice space and investing in other real estate.



Flexibility

Leasing allows practices to more purposefully choose a good location, since opportunities to lease are more plentiful than opportunities to buy. Additional revenue from the optimal location, can far outweigh the costs of leasing. Leasing in the right location is always better than buying in the wrong location.

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Owning, rather than leasing, can also make selling your practice much more complicated, especially if you are not diligent in keeping your accounting records separate for the business and building.

Upon sale, most buyers will require a tenant to be in occupancy at that time. It's important to consider if you'll be willing to sign a long-term lease at the time of sale, or if you'll find a replacement tenant to preserve the cash flow.

Opportunity Cost

Owning and managing real estate can take a lot of time and energy, and is often a business in and of itself, which can detract from growing and managing your practice.

Though ownership can result in more control over the physical aspect of the building and maintenance, it comes with more decision-making responsibility and more time spent on real estate rather than practicing medicine.

Often, practitioners find that the highest and best use of their time is practicing medicine and building their business. Leasing allows someone else to run the real estate while they manage their practice and focus on their patients.

"I recently had a personal experience making this decision a few years ago. I own a real estate investment and management company, so it made lots of sense for me to buy the building where my company's offices would be, right?

I thought so, but as I looked for a new home for my growing company that would fit our culture, help us attract and retain talent and provide the flexibility we needed as a growing firm, I came to the realization that what I needed wasn't for sale.

And as I ran the numbers and weighed the pros and cons, it made far more sense to lease the right office in the right location, rather than force ourselves to buy just to build equity. I'm so glad we leased the space we did because it allows me to focus on growing my business."

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Ted has more than 35 years of experience in the real estate industry. Mr. Barr has co-founded 2 real estate acquisition and investment firms focused on acquiring and managing retail, office, medical office, industrial and land investments. He also worked in the Real Estate Advisory group at Deloitte & Touche and has many years of experience consulting and advising medical practices and hospitals on their real estate needs.