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### **Doctors of Dentistry Facing Lease Vs. Own Decision Need to Take Long-Range Outlook**

Fledgling entrepreneurs -- be they owners of doctors of dentistry, machine shops, local restaurants, clothing stores, real estate agencies or other small businesses -- face the question of whether to lease or own the property housing their business.

According to national commercial real estate experts, there is no "right" or "wrong" answer. A variety of factors pertinent to the individual business and the owner's objectives, as well as local market factors, must be taken into account before an informed decision can be made.

Whether or not your dental practice will grow -- and grow substantially in the future -- is one of the principal factors influencing the lease versus own decision. If the practice is expected to grow dramatically over the next three to five years, owning is probably not a good option. A dental practitioner is better off leasing in that situation.

By leasing, the entrepreneur avoids the prospect of either purchasing a building that's too large, with the expectation of growing into it, or one that only accommodates current space needs, which will be too small in a few years.

The next issue to consider is the availability of flexible lease terms. Landlords in many markets today offer a long-term lease of seven to 10 years with a clause allowing the business to exit the lease after five years with six months notice. In this case the tenant would pay the unamortized cost of getting out.

I emphasize that obtaining this kind of lease flexibility for small entrepreneurs is a more prudent option than owning real estate.

Small business owners initially should try to avoid tying up valuable capital in real estate assets. Leases tend to lower fixed costs because there is no required down payment or amortization of loan principal. Lowering fixed costs reduces overall business risks.

Leasing real estate offers a business the option to still occupy and control a property, but utilize capital in other ways.

From the perspective of purchasing a business property, a dentist in business a few years with few plans to grow the business significantly might consider an outright purchase. If a business owner knows he can manage the company effectively in the same building for 10 years or longer without requiring additional space, then he should take a hard look at the cost differences between leasing and owning.

In this case, owning appears to be a viable option. But even with ownership there are pitfalls. If you purchase the property and 10 years in the future the business gets into financial difficulties, you as the owner do not have the flexibility a lease would offer. If you file for bankruptcy and you are a tenant, it is most likely you can tear up the lease and claim you need to move to a lower cost building in order to get back on your feet. An owner simply does not have that flexibility.

Another problem with ownership, is it carries a potential opportunity cost. Owning real estate through either equity or mortgage loan financing ties up capital that might otherwise be invested in the business, for expansion or renovation. Such operations investment might produce greater returns than the real estate investment, creating an opportunity cost that accompanies real estate ownership."

If the entrepreneur opts for a lease over ownership, certain criteria must be followed in order to secure the best possible lease. For example, leases should provide the tenant with an acceptable level of control over the asset. These control issues include assignability,

reasonable condemnation and taking provisions, and purchase options. Lease escalation clauses should be manageable in order to lessen downside risk.

If a dental practitioner opts for purchase, when to make that purchase is paramount to getting the best price. Analyzing current market conditions and available sales information provides the buyer with valuable insight.

Lease vs. own analysis is definitely a situation-by-situation equation. There are many factors to consider and the decision should be made in conjunction with a qualified real estate professional who has proven experience in that particular market.

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### **Bio**

Carl Pautlitz is the President and COO of Sheeran Sotheby's International Realty, the leading real estate company for luxury properties in Southeastern Virginia. Carl's education includes a BS degree in corporate finance from Arizona State University and an MBA from The College of William & Mary. His credentials include the CCIM designation for commercial real estate and he was selected to the Virginia Leadership Academy for Virginia Association of Realtors. He serves on the Richmond Commercial Board of Governors, the President of Williamsburg MLS board, and VAR's International Council. His background includes working as a financial investment manager for IBM in San Jose, CA and the European finance manager for Brocade Communications. He uses his corporate finance and analytical skills to assist business owners and investors in all real estate investment decisions.

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