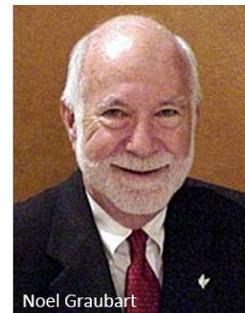


## Pay Rent Or Own Your Business Property

By Noel Graubart

This is a question that many business owners should be asking as part of their long range business plan and exit arrangements for the future.

Owning the business property is not going to be wise for all business owners. Many companies are in the process of expansion and the use of capital as well as the flexibility lost can be a hindrance rather than an advantage. If the space needs may change substantially in the near future, they may be better off having the flexibility of easily moving to larger space until the business has matured regarding its space needs.



However, let's take as an example a small business that is leasing 2,000 square feet in a showroom/warehouse building. They are distributing tools to construction trades and have been in business for about 20 years. The company is profitable and the owner/operator has enjoyed a very good income giving them time to travel, put their kids through college, buy a nice home, contribute to their favorite charities and generally enjoy a good reputation in the community. The owner is about 55 years of age and in good health. Thoughts about eventual retirement are starting to enter into the family conversations.

Although they may have put money aside for retirement, one of their biggest potential assets may have been overlooked. Wouldn't it be nice to eventually sell the business and retire? The new owner would buy the business and continue to pay rent to the present landlord. However, there may be a better plan. If the family personally owned the business property, then they could sell the business and continue to have family income from the rent that the business would pay to them since a lease would be part of the sale transaction.

Sounds great, so let's think about how this can be done.

Assume the following:

Business property is 2,000 square feet	
<b>Annual Rent is \$22 a square foot</b>	<b>\$44,000</b>
<b>Annual Common Area Maintenance is \$8.00</b>	<b>\$16,000</b>
<b>Annual Empty Cost of Renting</b>	<b>\$60,000</b>

Let's look at buying the building now being used or a similar building

Should be able to build or buy for \$175 a square foot	\$350,000
Equity of 20%	\$ 70,000
Loan	\$280,000
<b>Annual Payments on 20 year loan @ 5%</b>	<b>\$23,000</b>
<b>Annual Common Area Maintenance \$8.00</b>	<b>\$16,000</b>
<b>Annual Empty Cost of Owning</b>	<b>\$39,000</b>

**Difference between Empty Cost of Renting vs Owning      \$21,000**

So, doesn't it make sense to invest \$70,000 in a building which will save the business \$21,000 a year? First of all, they will get their money back in about 3.5 years. Beyond that, they will have a revenue stream that continues even after they sell the business at a later date. The new buyer will sign a lease that will pay the family \$44,000 a year so after paying the mortgage they will have free cash flow of \$21,000. In addition, if they own the building they will earn equity with each monthly payment as the loan is reduced. Additionally, they can also deduct the Interest on the loan as an expense, and a given amount of Depreciation Expense may also be allowed.

The family met and what do you think they decided to do?♦

~ Noel Graubart is a Silver Fox Advisor

