



Purchasing or Leasing Healthcare Real Estate

KEY DETERMINING FACTORS

One of the most common questions healthcare providers ask regarding their practice's real estate is *"Should I purchase or lease my office space?"* Many providers are quick to assume that since they own their home, they should also own their office space. While that logic is sound and often times own-

ing is the top option by far, there are scenarios where owning your office space may not be in your best interest. The simple answer to the question, "Is it better to own or lease?" is — *It depends.* Unfortunately, there is no easy, one-size-fits-all answer on ownership vs leasing. Instead, there are many factors that come into play and need to be fully vetted when contemplating this decision.

Analyzing considerations like the season of your practice and future growth needs, available financing, cash flow and your practice's financial position, tax implications, and market availability, all play roles in determining whether to lease or purchase. The following considerations are important to evaluate and will help guide your decision on this topic.



LEASING YOUR OFFICE SPACE

FLEXIBILITY: When you lease a property, you typically have more flexibility to relocate your office space as you will likely be signing a 5, 7 or 10-year term. At the end of that initial term, you can easily walk away from the space, relocate to another property, or decide to sign on for another term. You don't need to prepare the property to sell, list and show the property, or walk through a sale transaction to get out. You simply walk away at the end of the term or you renew the lease.

CONCESSIONS: Another great benefit of leasing comes in the way of the concessions that landlords will offer blue chip tenants, like healthcare practices. When you are properly represented and have the appropriate posture and negotiation strategy, many landlords will become more aggressive and stretch further to make a deal with a healthcare provider than with other traditional tenants.

Some examples of these concessions are tenant improvement allowances where the landlord will provide money to help build out the space in the property, or a free build out period to complete the construction so the tenant is not paying rent before they occupy the space. It's also possible to achieve free rent once the practice opens.

With expert representation, a healthcare

tenant can often times create leverage to demand concessions that reach into the six-figure range, totaling \$100,000, \$150,000, even \$200,000 and more in build out allowances from the landlord, along with 6-12 months of free build out time and additional free rent upon opening. These concessions are huge benefitting factors to leasing verses owning, as it means less money from the tenant on the frontend to get the office up and running, and less money and interest paid to a lender.

AVAILABILITY: An important factor to consider when determining whether to lease or purchase is market availability. If you are in a high-growth, dense urban or downtown area, there may be very few options to purchase. In most markets, lease options outweigh purchase options by 10 to 1, and in more populated markets, the disparity is even greater. It's important for healthcare providers to not get 'set' on only one scenario. The best strategy is to look at the entire market or area, both purchasing and leasing, to find out what property options are available. In these decisions, it is best to keep the needs of the practice as the main priority, as the practice is what drives revenue.

It's also imperative to look at an all-encompassing apples-to-apples comparison that takes into account the principle paydown, monthly figures, concessions and costs, tax implications and the equity position after 10 years, 15 years and 20



years. Those are the figures that will ensure the decision is informed and factual.

PURCHASING YOUR OFFICE SPACE

ADDITIONAL ASSET: If you have enough money for a down payment along with the ability to secure financing, and there are good purchase opportunities available in the area you are looking, then ownership may be the best option for your practice. It's very common at the end of a doctor's career that the value of the building and property are worth as much or even more than the practice itself.

ADDITIONAL ANNUITY: Healthcare providers also have the option of selling their practice but retaining their property and leasing it back to the buying party. This creates an annuity and becomes retirement cash-flow, often with a building that is fully paid off.

HEALTHCARE-SPECIFIC FINANCING: If you are considering a purchase, it is wise to speak with a healthcare-specific lender who has loan products geared towards healthcare real estate. These lenders typically understand the cycle of build outs, the unique nature of healthcare offices, the strength and cashflow of healthcare practices, and they in turn

package their loans in a more beneficial way than a general lender might.

PRINCIPLE PAYDOWN: Another distinct benefit of ownership is principle paydown and equity that is built up. If you are leasing, you get nothing at the end of the lease term except another renewal document. At the end of 10-15 years of ownership, you will likely see a balance sheet on the property that can be in the hundreds of thousands and even millions of dollars to your benefit. If you pay off the building after 15 or 20 years, then your property costs are limited to upkeep, taxes and your operating expenses. That is a huge benefit of ownership.

TAX BENEFITS: Both purchasing and leasing have tax benefits and considerations that you will want to fully understand through the advice and counsel of a good CPA and Agent. Two of the most impactful tax benefits that result from commercial real estate ownership are depreciation and mortgage interest deduction, both of which are motivating factors of purchasing.

ADDITIONAL CONSIDERATIONS

It's also helpful to look at the season your practice is in. Are you an associate right now, looking at a start-up? If so, it might make more sense to lease



for the first 7-10 years to really determine where your target market is located, how much space you'll need in the short and long term, what your parking needs look like and more.

Do you own a practice that's been leasing for 10 years or more and you are now trying to determine whether purchasing is right for you? If so, running a detailed lease vs purchase analysis and then discussing it with your Agent and CPA would provide you meaningful insight.

Should a healthcare provider who is looking to retire in the next three to five years consider purchasing a building or should they simply remain in a leased space? Again, it depends... On the surface, it might not make sense to invest \$150 to \$200 per square foot into finishing out a new space, plus the cost of the building and land, if a practice sale is likely within a few years. However, if the new lease to the buyer of the practice creates cashflow, it could be an excellent invest-

ment and one that substantially increases the value of the practice. Again, every scenario and market are different and unique. That is why you need to have a good team of advisors around you and be confident you are evaluating all of your options.

IN CONCLUSION

It's easy to see how this may be the most common question regarding healthcare office space; however, it's not a question that has a definitive answer for everyone. You need to dive into your situation and scenario deeper with the help of a good healthcare tenant Agent or Broker. There are many considerations and implications to consider and having all the information in a comparative analysis puts you in the driver's seat to make the most beneficial decision for your practice.

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