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To Own or Not Own Your Restaurant Real Estate

By Dennis Monroe

That's the question that's been debated for years especially during periods of high interest rates when capital is expensive. Yes, restaurant operators should work on growing operations rather than tying up capital in real estate. However, those of us with years of experience in the industry believe, when possible, owning the real estate can be the preferred approach.

Also, let me put on my lawyer and tax advisor hat: In most cases, the real estate should be owned in a separate entity from the operating company. This provides greater flexibility for financing, ownership changes, succession and liability management. Here are seven reasons why ownership of restaurant real estate is so important:

1. Overall control

Control is perhaps the strongest argument for ownership. If you identify a great location and can afford to acquire it, ownership provides flexibility that a lease simply cannot match. Markets change, concepts evolve and consumer preferences shift. When you own the property, you have options. You can change concepts, redevelop the site, lease it to another operator or sell the property altogether.

While leases should carefully be negotiated with termination rights, performance-based exit clauses, and limitations on personal guarantees, it is still a long-term obligation over which you may have limited control. Ownership allows flexibility and the ability to better manage uncertainty over the life of the business.

2. Capturing the value you create

A successful restaurant drives traffic, improves the reputation of a location and often increases the value of the surrounding property. When operators lease their sites, much of that value accrues to the property owner rather than the restaurateur. By owning the real estate, you capture both sides of the equation: the value of the operating business and the appreciation of the underlying property. The combination of a strong concept and a desirable location can create significant long-term wealth.

3. Building long-term equity

Every rent payment made under a lease is an expense. While it provides the right to occupy the property, it generally does not create equity.

When you own the real estate, a portion of every mortgage payment contributes to building ownership value and debt is reduced while equity grows. Many successful restaurant operators have found the wealth generated from real estate ownership ultimately exceeded the profits generated from operations alone.

4. Protection against rising occupancy costs

One of the biggest challenges restaurant operators face is increasing occupancy costs. Lease renewals often come with higher rents, additional charges and landlord demands that can impact profitability. A location that once generated strong returns can become much less attractive when rent escalates beyond sustainable levels.

Owning the property provides greater certainty. While financing costs and property taxes may change, ownership generally protects operators from rent increases and gives them more control over a major expense category.

5. Financing and strategic flexibility

Real estate ownership creates additional opportunities for financing and growth. Properties can serve as collateral for loans, support refinancing transactions, or provide access to expansion capital. Also, ownership allows operators to structure sale-leaseback transactions if they decide unlocking capital becomes advantageous at a later stage.

Having ownership of the real estate gives business owners more strategic options than simply being tenants.

6. Long-term wealth creation and exit value

At some point, every restaurant owner thinks about their exit strategy. A restaurant operation may experience fluctuations in value based on market conditions, competition or consumer trends. Well-located real estate, however, often retains value and may continue appreciating over time, and can be sold, refinanced, transferred to family members, or retained as an income-producing investment after selling the restaurant business.

For many operators, the real estate ultimately becomes one of the most valuable components of their overall wealth.

7. Tax advantages

Even for those not classified as real estate dealers, properties held as an investment for more than one year should qualify for long-term capital gains treatment upon sale. This can provide a large tax advantage, particularly when compared to higher ordinary income tax rates.

Also, investors may benefit from tax strategies which can accelerate depreciation deductions and add larger tax savings, as well as create usable tax losses that offset other income, subject to tax rules and limitations. When properly structured and managed, these benefits can enhance the after-tax return on the real estate.

There is no single answer for every restaurant concept, but, in my experience, when ownership is financially feasible and the location is right, owning restaurant real estate provides control, flexibility, equity growth and long-term wealth creation that can be difficult to achieve through leasing alone.

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