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Buy or Lease?

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The State of Leasing

Corporate America's largest external source of equipment finance is leasing. In 2007 alone, over $220 billion dollars of equipment will be leased in the United States and $550 billion throughout the world. And, worldwide leasing volume continues to grow. U.S. firms lease everything from mowers to motors, computers to cranes and desks to dental chairs. Over 35% of all capital equipment is financed through some form of leasing. Eight out of ten companies -- from mom and pop shops to the Fortune 500 - have turned to leasing to get ahead and stay ahead.

Historical Leasing

Leasing has existed from the time of the earliest known Samarian civilization. Clay tablets from the ancient city of Ur dating to 2010 B.C. detailed the leasing of agricultural tools. Later, ancient Egyptians, Greeks, Romans and Phoenicians all engaged in the leasing of ships. In this country the concept of leasing emerged in the 1700s with the leasing of teams of horses. By the mid-1800s, railroad tycoons, battling to extend their private railroads across the country required tremendous amounts of new capital. Most banks, however, considered railroad financing risky and refused to lend to the emerging transportation industry. Locomotives, cars and other railroad equipment had to be financed using new and creative methods -- the forerunners of the equipment lease.

The lease concept surged again in popularity after World War II as the U.S. economy took off. Quickly expanding companies sought to acquire the equipment they needed without depleting cash and exhausting bank lines of credit. Tax law changes gave companies the ability to expense lease payments, which gave them faster tax write-offs. Leasing, once considered to be aggressive financing used only by those unable to get conventional terms, is now regarded as a stable alternative to wildly-fluctuating interest and inflation rates.

Leasing Today

Today there are approximately 2000 leasing companies in the U.S. The quicker the rate of equipment obsolescence, the higher the likelihood that equipment will be leased. We believe that the hedge against obsolescence is one of the primary reasons companies lease equipment. With technology equipment especially suffering rapid obsolescence, leasing is becoming a "no brainer" for computer and technology systems. Leasing, however, is now common for all business related goods.

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Leasing offers several business advantages over cash purchases. First it frees up capital. Cash purchases not only deplete cash reserves that business may need for operations cash flow; it can have a negative impact on the balance sheet. Leasing also has potential tax advantages that give companies the ability to expense lease payments, which give them faster tax write-offs. When leasing capital goods, a firm preserves their credit lines and no additional collateral is required. Cash purchases on the other hand reduce a firm's cash-asset position. Also, leasing allows easier budgeting and many firms can fiscally function more effectively when they have a fixed monthly payment, an option that leasing allows.

Ordinarily, if equipment is purchased it must be set up as an asset on the balance sheet and depreciated over sixty months. Conventional wisdom holds that the useful life for equipment that is vulnerable to technological obsolescence is rarely over three years. Purchasing Professionals are especially aware of this and want a means by which they can keep their systems on the cutting edge, or if not on the edge, somewhere on the curve. They detest having to constantly battle management for budget items relating to the acquisition of new equipment. They frequently emerge frustrated, delayed and feeling like the process will always be doomed to be inadequate. Management is frequently challenged to realize that technology must he viewed as a commodity or a utility, a constantly renewable resource.

Most companies cannot compete if they are handcuffed to second-rate equipment. Often a strategic plan is developed when management makes an ongoing commitment to fill the needs they know will constantly change and improve.

How do you accomplish this? Enter the Technology Refresh Lease, a one-stop-shop where all needs are met. The user (lessee) asks the lessor for approval of a line of credit for the estimated cost of their purchases for the year. They frequently choose a Master Lease concept whereby only one lease is signed but can be amended as needed with only a purchase order or schedule. The lessee tells the lessor what to buy, from whom and at what amount. More frequently than not, the lessee chooses to include soft costs in the lease including software, training, installation, and service. The term of the equipment schedule, chosen by the lessee, is anywhere from 24-60 months. At the end of the lease, the lessee normally has four options: 1) return the equipment, 2) purchase for Fair Market Value, 3) continue leasing, 4) trade up into new equipment on a new lease.

This concept gives the lessee the ultimate in choices and flexibility. If properly structured the lessee can expense the payments over the life of the lease, which will coincide with the useful life of the equipment. Management and Purchasing Professionals are poised to take advantage of whatever option allows them to stay efficient, compliant and competitive.

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An Unregulated Industry

Many consumers assume, sometimes at their peril, that leasing companies are regulated like banks but indeed the industry is not regulated by any governmental body. Because of this lack of regulation, leasing is an industry where caveat emptor is the ruling philosophy. Many industry practices, fees and a host of end-of-lease surprises may be technically legal but push the limits of business ethics. These practices are not limited to small, obscure leasing firms; they are conducted by many throughout the leasing industry - even the best known, highly respected national firms. Often unsuspecting lessees -- even sophisticated buyers -- are caught in these costly traps.

Frequently, the lion's share of a leasing company's profits is derived from fees that the lessee does not anticipate. Some of the more common revenue enhancers for the leasing company are late charges assessed with no grace period, interim rent, automatic renewals, early termination fees, unreasonable return fees and conditions, capricious Fair Market Value determinations and forced insurance fees.

Obviously, the choice of a leasing company must go well beyond the quoted price per month -- reputation and a history of ethical business practices are paramount. Finding and working with principled leasing firms is critical to your firm realizing the benefits that leasing offers. A reference from other lessees is one of the best ways to start your research. One must also examine their lease agreement in detail and get written answers to questions regarding fees and practices. In order to avoid the many traps that may exist in a lease contract, many lessees have consulted with independent specialists in the industry.

A local firm, Independent Lease Review, Inc. **(Mary A. Redmond)**, specializes in reviewing lease agreements for clients across the country, including many major law firms. For further information visit www.IndependentLeaseReview.com.

The Certified Lease Professional certification (CLP) was developed by UAEL, a leasing trade association, to raise the professional status of leasing professionals. It is a recognized credential throughout the industry, with members of the general public and with governmental agencies. The CLP designation sets the standard for professionalism in the leasing industry. This designation recognizes individuals within the industry who have demonstrated their competency, through continued education, testing and conduct. Pertinent information relating to the requirements established to achieve the CLP status can be found at www.clpfoundation.org. Currently, of the 200 Lease Professionals in the country who have undergone the process of further education and testing to achieve the CLP certificate, three are employed at Clune & Co.

Technological Adaptations

Many leasing firms offer state of the art services for on-line applications, timely (if not nearly instantaneous) credit decisions, electronic banking and many web services. A process that took

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two days in the not too distant past can frequently take fifteen minutes. Clients of Clune can now

take advantage of our paperless process. Clune's philosophy is that our level of service must be akin to the ease of using a corporate credit card.

Future of Leasing

The Federal Accounting Standards Board (FASB) is widely expected to change the rules governing leasing to conform to international standards. The desire is to make lease transactions transparent on the balance sheet. The effect of this is unknown but expected to have the biggest impact on large ticket transactions.

Additionally there is a trend in manufacturing to try and capture customer financing through captive, wholly owned leasing companies or through partnerships that private label the relationship. Even though this may be good for the lessor, it is advisable to consult with an independent lessor for a competitive quote.

Investigating and trusting your service suppliers is critical to a successful and on-going business relationship. Leasing is no different. Research your supplier of choice and learn their business practices. With a reputable, trustworthy leasing firm handling your leasing needs, your company will realize financial flexibility and benefit from a financial business partner. Leasing as a form of financing offers many advantages to firms of all sizes. With your firm's specific business goals in mind, it is incumbent upon Purchasing Professionals to investigate the value of a lease finance plan.

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Mary A. Redmond, The FearLess Negotiator, works with business professionals who want to become stronger negotiators. After attending one of her workshops or coaching sessions, clients feel more confident in stressful business situation whether they need to close bigger and more complex sales, secure the perfect new job, ask for that well-deserved raise or improve communication with their colleagues, bosses or families.