

**Overview of Lease Financing Options**  
**Prepared by Linda J. Camp**

Key Element	Lease Purchase	Operating Lease
Legal Status	Conditioned sale; Lessee owns equipment at the end of the lease period. Title of equipment is transferred to the Lessee.	True lease; Lessor retains ownership of the equipment throughout the leasing period; title is not transferred to the Lessee; Lessee pays for use of the equipment.
Description	Lessor provides cash to fund equipment up front; Lessee repays Lessor over a period of several years, generally making either monthly or quarterly payments composed of principal and interest.	Lessor purchases equipment from agreed upon vendor; Lessee pays for use of the equipment, making monthly payments over the lease period. Monthly payment is based on cost of equipment plus fee for "use" of the money.
Financing Structure	Similar to a mortgage; current interest rate is applied to the total amount borrowed (principal); interest portion of regular payment declines over lease period, while principal increases.  Certain entities, such as local governments, qualify for tax-exempt lease financing under the Internal Revenue Service Code. Lessor can offer a lower interest rate because IRS allows some special deductions due to status of Lessee.	Similar to "rent," where equal monthly payments are made during lease period. Finance charge is calculated by applying a "rate factor" to the total amount borrowed. Rate factor is based on length of lease term, type of equipment, current T-bill rates, credit worthiness of Lessee, among other things.
Accounting Status	Equipment financed is treated as an asset for accounting purposes for Lessee; items appear on Lessee's fixed asset inventory.	Equipment financed is treated as an asset for accounting purposes for Lessor; monthly payments are treated as an operating expense for Lessee.
Lease Period	Should generally match the expected useful life of the equipment being acquired.	Should generally match the expected useful life of the equipment being acquired.

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Key Element	Lease/Purchase	Operating Lease
Sources of Financing	Banks, Equipment Leasing Companies (generally specialize in this type of lease), some equipment companies	Historically, provided by Equipment Leasing Companies who specialize in operating leases; equipment companies are now offering operating leases. Very few banks offer operating leases because of the need to dispose of equipment at the end of the term.
Benefits	<ul style="list-style-type: none"> <li>• Spread cost of equipment over the useful life of the equipment</li> <li>• Get the use of money over a longer period and thus may be able to gain benefits by investing cash</li> <li>• May help organization to better plan for replacement of equipment because of fixed lease period, and predictable payments</li> <li>• May help organization to achieve other benefits by having access to more or better equipment</li> <li>• May help organization standardize software and hardware</li> </ul>	<ul style="list-style-type: none"> <li>• Same as lease/purchase, plus</li> <li>• Some of responsibilities for disposing of equipment at end of lease period are shifted to Lessor</li> <li>• Do not have to maintain items on fixed asset inventory</li> </ul>
Issues	<ul style="list-style-type: none"> <li>• Lessee has responsibility for disposing of equipment at the end of the useful life cycle</li> <li>• Works best when part of an overall strategic management plan for the equipment</li> <li>• Cost/value tradeoffs</li> </ul>	<ul style="list-style-type: none"> <li>• Sound planning is required because equipment will need to be replaced at the end of the lease period</li> <li>• Lessee needs to make sure all equipment is returned at the end of the lease period or will be expected to pay for items</li> <li>• Works best when there is central management of lease and equipment</li> <li>• Cost/value tradeoffs</li> </ul>