The Benefits of Leasing

Leasing converts a large capital of expenditure into small monthly payments. Hence the company has the profit-making equipment immediately and keeps their cash reserve available.

Rather than investing the precious cash reserves in depreciating assets, the company can use them to help increase profits.

Lease Rental is 100% Tax Deductable

The main reason that the majority of companies lease rather than purchase equipment is that they use leasing as a method of reducing their tax bills. This is because lease rental is 100% tax deductible, meaning that all payments you make for your equipment are written off against your tax bill. For any profit making business, this means a substantial saving in real cost of acquiring equipment by lease rental. This could save you between 20-40% of your lease payments, depending on the rate of tax you pay.

Payments on qualifying leases are written off as direct operating expenses, rather than a debt or outstanding liability, thus reducing short term taxable income. Any capital allowances are passed on to you, you can offset your rentals against taxable profits and you can also reclaim the VAT on your monthly payments.

This status as a rental as opposed to a liability on a companies balance sheet is something the banks like to see, which is why an operating lease can be attractive. For this reason, leasing is often referred to as 'off balance sheet' financing – a tremendous advantage to both large and small businesses.

Ownership at the end of the lease

Lease rental is just that, a rental agreement. Title of the goods remains with the Lessor (ie BOSEF), which means the equipment does not show on the companies balance sheet, therefore not needing to be depreciated over a fixed period.

The leasing company are the third party involved within the lease agreement, therefore they buy the equipment from the funder and then sell it on to the customer. This means that the customer can take full advantage of all the benefits of leasing but still own it at the end. (Tax loop hole).

The disadvantage of buying equipment outright

The disadvantage to buying equipment out-right, is that the capital invested becomes a depreciating asset. This is an asset and the value decreases over time.

Tax Advantages of Leasing – Example Figures

Most clients use a lease to acquire their system. This is a highly tax advantageous means of purchase because every payment receives 100% tax relief.

Outright Purchase - £5,000.00

Lease - £26.76 plus VAT per week (paid by monthly direct debits £115.98)

60 Payments (5 years) £6,958.56.

Maximum tax relief £2,783.42

Cost after tax relief £4,175.14

**** A Saving of £824.86 against the cash purchase price ****

As you can see by the example above the lease can have considerable advantages so long as you are in profit. *The amount of tax relief depends on your tax band (22%/40%).*

The tax relief can actually reduce the overall cost and you do not have to endanger your liquid cash flow purchasing new equipment when you can invest in stock and increase your profits.

At the end of your lease

During the lease period (normally 3-5 years) you are renting the system and for that reason you are gaining your 100% tax relief. At the end of the period therefore the equipment is not your property, which means in theory you should return it to the supplier, however in practise no one does this.

The lease company sell the customer the equipment for one further monthly payment, which of course is still 100% tax deductable.

Which Way to Go?

Unless the customer has the cash in the budget with nothing else to spend it on most clients will prefer the lease option.

* Capital allowances can be claimed against equipment bought outright at a value of 25% of the written down value of the goods, depreciating year on year.

Some questions and answers:

Why Lease? Leasing is probably the most popular method of financing a new equipment today. Virtually any item of equipment can be leased from a barbers chair or coffee machine to a complete shop refit ie from £1000.00 to several hundred thousand pounds.

Should I pay cash or lease? You may be able to afford the equipment outright, but before you make this decision you must consider the following;

- All leasing payments are rental payments and as such are an allowable business expense, therefore if a business is making profits they reduce the profits by the amount of rentals you pay each year which in turn reduces your tax bill.

- Lease payments are normally the same throughout the least contract. This means that increases in interest rates do not affect you and enables you to budget your cash flow more effectively.

- Leasing enables you to save your cash for other purchases such as new stock, staff training, advertising, new business opportunities and unexpected happenings.

Do my payments increase if inflation or interest rates rise? No, your monthly payment is fixed at the start of the lease and so is unaffected by interest rate rises. As inflation rises, because your payments are fixed the cost of the equipment reduces in real terms.

How do I make my payments? All payments are made by direct debit on the same date each month or quarter. Quarterly invoice payments are available on occasion although an extra charge of 2% is made by the banks for this facility.

Should I go to my Bank? Using your bank for all your business funding is not a good practise. If you use all your overdraft facilities you leave yourself in a vulnerable position to react to any unexpected needs of short term borrowing. Your bank may change the interest rate mid-way through a loan or reduce your overdraft facilities, which can dramatically affect the cash flow of your business. Sometimes bank will limit the amount they will lend you without further security such as taking a charge on your home. It is not financially prudent to have all your eggs in one basket.

Who Leases? Nearly every market sector large or small benefits from leasing, from new start business to large established companies.

How does a lease work? A lease agreement is a contract between you the customer and a leasing company. This enables you to use equipment over a period of time on payment of rentals to the leasing company. With a typical lease agreement, you make a series of regular payments (usually on a monthly basis), thus helping cash flow, as opposed to a large capital outlay for the equipment.

Have the best equipment. You normally only pay a small deposit with a lease agreement, this enables you to choose the best equipment available with only a small initial cash outlay. This enables you to have the best equipment available with the latest technology and start to enjoy the extra profits this generates before your next lease payment is due.

For any other questions on leasing call Cambs Compressor Engineering today and we will be pleased to assist you.

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