Small Business Financing – To Lease Or Not To Lease

By: Matthew H. Sloan
Partner
602.234.7858
mhs@jhc-law.com

In a tough economy, where traditional financing remains elusive for many small businesses, equipment lease financing is a viable, but little understood alternative. However, it is important to enter into a lease for the right reasons and with the right structure. Consider the following to help determine if equipment leasing is right for your business.

Advantages of Leasing. An equipment lease is generally easier to obtain and more flexible than traditional financing. When structured properly, it may provide a small business with certain unique benefits, such as:

- *Expanded credit availability – Lease debt may not need to be shown as a direct liability on a financial statement.*
- *Avoidance of financial restrictions – Most bank financing restricts additional borrowing, where generally equipment lessors do not.*
- *Flexibility of structure – Leases can be structured to accommodate individual cash flow requirements.*
- *Small initial cash outlay – Unlike most loans, equipment leases generally do not require a down payment.*
- *Simplified credit process – Equipment leases are generally easier to obtain, often simply by completing an application.*

Disadvantages of Leasing. Generally equipment leasing can be used most effectively by businesses that are growing and profitable and least effectively by those businesses that are shrinking or suffering losses. Disadvantages to consider are:

- *Overall Cost - An equipment lease may be more expensive than other financing when the tax implications are not considered.*
- *Commitment of Term - Most equipment leases may not be terminated before the original term is completed.*
- *No Equity – Generally, a lessor owns the asset and enjoys all benefits of ownership unless or until a lessee exercises an option to purchase.*
- *Taxes and Maintenance - Most leases require the lessee to pay all property taxes, maintain property damage and casualty insurance and generally maintain the equipment in accordance with the manufacturer's recommended schedules and procedures.*

If the tax benefits of an equipment lease are important to your decision, be sure that you review the general lease terms with your accountant or other tax adviser. The IRS may disallow your treatment if they conclude that you lease is really a conditional purchase.

Equipment leasing is not for every business or for every situation. However, for businesses that utilize equipment that may be obtained through lease financing, it is not just an alternative to a bank loan or credit card debt; it's a deliberate financing strategy.

About the author: Matthew H. Sloan *is a partner with Jennings, Haug & Cunningham. Herepresents clients, including small, medium and large businesses in resolving disputes surrounding contracts, business partnerships, construction issues, credit issues, lease agreements, insurance claims and liability. Matt has been a resident of North Central Phoenix for more than 30 years, and can be contacted at MHS@JHC-Law.com or 602.234.7858.*