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Choosing The Right Lease: The Devil's In The Details

By Claude Solnik

Leasing is rapidly replacing purchasing as the procurement norm. Steven Orenstein, senior vice president of Manhattan-based Sterling National Bank and its leasing division, Sterling Bank Leasing, explained the popularity of leasing: "Our clients and potential customers are hesitant to commit to acquiring new technology." Orenstein also cited a credit crunch and uncertainty over the economy.

More than $200 billion is spent annually on all equipment leasing, Orenstein said. Companies lease computers, faxes, phone systems, photocopiers, local area networks, laptops, flat screens and office furniture as technology turns around quickly in a temporary world.

While it may be a way for businesses to tap the latest office technology as it becomes available, experts agree all leases are not equal.

Companies need to decide how long, under what terms and even how to finance leases, and also must consider the potential tax and financial consequences.

The wrong lease can result in additional payments for use - such as exceeding the page-count limit for copiers - or repair costs that could otherwise have been avoided.

Art Colman, general manager of copier dealer Specialty Business Solutions in Deer Park, said firms should make sure payments remain flat, rather than escalating after a year.

He also said companies should be careful they're doing business with dealers that will be around for the duration of the lease.

"Some dealers take money up front and go out of business, leaving you with machines that have no service," Colman said. "You want to make sure they'll be around to service whatever you get."

Another item to consider is financing. Marc Hamroff, managing partner at Garden City-based law firm Moritt Hock Hamroff & Horowitz, said companies should investigate financing options from manufacturers, banks and financiers.

Captive finance companies from IBM, Dell and Apple may offer good rates, but Orenstein cautions customers to consider other sources to "keep them honest."

One factor affecting the cost of a lease is its length. Hamroff said companies often end up with leases too long-term for their needs, since longer terms translate to lower payments. But if your lease is too long, you may end up stuck with outdated equipment. A three-year lease is often better than a five- or six-year term for a copier, he and Colman agreed.

"If they go out too long, the technology is likely to be antiquated or break down more often," Hamroff said.

Firms may be better off leasing phone systems or furniture for longer terms, since they're larger, costly to replace and the technologies don't change so rapidly.

There are additional points to consider. Companies should seek leases that let them upgrade without penalties, so they can shift to new technology. Companies also need to make sure maintenance contracts and warranties are comprehensive or risk charges for replacing parts due to wear and tear.

Finally, there are tax implications of leasing. Firms can benefit by deducting lease payments on taxes if they have a true lease rather than an installment plan.

Hamroff said leases are distinguished from installment plans by comparing payments to acquisition price and considering useful equipment life and fair market value at the end of the lease. "The concept of a true lease is one of the most litigated issues in the courts," he said.

Orenstein said firms can write off monthly payments on true leases as operating expenses similar to rent, insurance, payroll and supplies.

In contrast, firms may sign finance agreements - known as capital leases - for fixtures, file cabinets, window treatments, furniture, phone systems or carpeting, but these are not true leases.

"In those situations, there is no residual value at the end of the term," Orenstein said.

At the end of those agreements, customers typically have the right to buy, for modest amounts, prohibiting them from writing off monthly payments.

But in those transactions, firms still could write off interest and take depreciation on taxes, Orenstein said.