

How to Budget and Negotiate Equipment Leasing Contracts for the Lowest Total Cost of Financing



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Budget early and use real-time market intelligence by using Blue Sky's proprietary lease payment calculator that makes decision-making easier

Blue Sky's proprietary lease payment calculator uses real-time market intelligence to efficiently provide budgetary guidance for equipment financing options. The rates are updated monthly as a reflection of the hundreds of millions of dollars of equipment Blue Sky negotiates financing for on behalf of our clients.

Blue Sky's online equipment finance calculator allows you to quickly adjust the financing structure, term, equipment type, credit profile and amount financed to get budgetary and planning estimates. If you want to take advantage of Blue Sky's market leverage and save money on your equipment financing contracts, all you have to do is enter the information and press the "Apply Now" button to immediately gain access to Blue Sky's leverage, real-time market intelligence and expertise for negotiating below market rates, terms and conditions that will save money on your equipment lease contracts.

There is often confusion about the differences between an operating lease and a finance lease. Fair Market Value leases can be structured as either an operating lease or a finance lease depending on the present value of the payments as well as end-of-term options in the contract. It is important to understand that "\$1 out" is just a term that references that you're solving for ownership of the assets at the end of the financing for a fixed dollar value. Here's some useful terminology to help with using the payment calculator.

Important terms when reviewing lease rate factor

Base rate index adjustments

It is imperative that if your proposal includes base rate adjustments you understand how they affect your payment.

Terms and conditions (T&Cs)

The lease rate factor is only a small portion of the total cost of the contract. Because there are so many T&Cs in the leasing contracts, most people and most companies – even most sophisticated lessees with a lot of experience – don't understand them. That is where a financial expert can come in handy. You may calculate interim rent risk but underestimate the risk that this interim language has into significant cost leakage.

Equipment return provisions

These riders may feel like a non-issue at the time of signing, but over the term of your contract they will loom larger. Over-hours usage, return fees, damage repair fees: all those items add up. People don't think about this. They get a dealer quote, and it looks like less per month than they get elsewhere so they sign. But when they get to the end-of-term, and they realize they have hidden costs that they didn't expect.

What is the difference between an operating lease and a finance lease under the new lease accounting rules ASC842?

Operating lease - An operating lease is a contract that allows you to use the asset without owning the asset during the term of the financing. Operating leases will save you from paying the full purchase and sales tax upon equipment delivery while giving you the equipment you need to meet your business requirements. You then return, extend or purchase the equipment at the end of term.

Note: although you don't own the equipment, you are still completely responsible for the equipment's condition if you return it! It is imperative to completely understand all the equipment return rider provisions for the operating leases to avoid significant unexpected expenses at end of term.

5 Criteria that a contract MUST meet to qualify for an operating lease

1. No bargain purchase option
2. No transfer of ownership
3. Net present value of payments must not exceed 89.9%
4. The term of the contract must not exceed the asset's economic useful life
5. Asset cannot be "Special Purpose," for example, it must have a secondary market for resale

Finance lease - A finance lease is any financing that does not meet ALL five of the above listed criteria for an operating lease. All of these are criteria form an accurate picture of what you will pay in the total cost of an equipment financing. Accuracy is the key here. Each data entry point should be considered to get the best estimate.

Instructions for Using the Blue Sky Lease Payment Calculator

Enter Amount of Equipment Financing

use the text field below to type in the amount or use the slider below the text field

\$

200000

Lease Type

☐ Fair Market Value

☒ \$1 Out

Your Company's Credit Profile

☒ Investment Grade

☐ Non Investment Grade

☐ High Yield

\$6,105.40

for 36 months

\$4,550.00

for 48 months

\$3,728.00

for 60 months

Calculated rates are estimates. Final rates are subject to submitting detailed equipment quotes along with a completed credit application or submission of a complete credit package for underwriting review and approval.

To quickly secure a fully approved rate

Apply Now

1. Enter the Amount of Equipment Financing

Enter the total hard cost and soft cost (excluding sales tax) to be financed. After entering the dollar value, you can use the blue radio button slider below the \$ sign to adjust the amount financed and see the direct correlation to the monthly payments.

2. Enter the Lease Type

- *Fair market value (FMV)*

One of the benefits of an FMV lease is you only pay for what you use. Based on the asset type and the term of the financing, the lessor takes the residual value risk in the asset, and you only pay for a portion of the original equipment cost. At the end of the financing, you will have the option to return, extend or purchase the assets at their current FMV.

- *\$1 Out Lease*

A finance lease that provides a path to equipment ownership, \$1 out lease financing allows you to use an asset and gives the lessee a chance to purchase the equipment at the end of the lease at a bargain purchase price, typically one dollar for the bill of sale. \$1 out leases may have a higher lease payment because you are fully amortizing the complete cost of the asset in addition to a financing expense. One of the benefits of the \$1 out lease is your company will get the tax shield for the depreciation expense. extend or purchase the assets at their current FMV.

3. Enter Your Company's Credit Profile

There are several factors that decide your company's overall credit profile. Unless you have specific reference points to an S&P or Moody's rating, you can instantly get feedback from Blue Sky's Lease Payment Calculator on multiple credit profile options and decide which profile you prefer to use for budgeting.

Your 3 Credit Profile Options

- *Investment grade*

This category is the highest level of credit rating and indicates a low risk of default, a high rate of on-time payment and optimal key financial ratios such as (but not limited to) profitability and debt service coverage ratio. Investment grade criteria are equivalent to a Standard & Poor's rating ranging from AAA to BBB-.

- *Non-investment grade*

It is common NOT to have an investment grade credit rating. Non-investment grade credits still qualify for aggressive rates for both FMV leases and \$1 out leases. The company may be recovering from recent economic hardships, be highly leveraged or just have a couple of key ratios that don't meet the investment grade ratings requirements. Non-investment grade ratings are anything below BBB- to a B credit rating.

- *High yield*

Companies with high-yield credit profiles are typically below the single B rating and considered riskier because there is a greater probability that the borrower may default on their debt obligations. Many startup companies that don't have operating performance and/or highly leveraged companies that have not consistently produced EBITDA or net profits fall into this category. Companies with high yield credit profiles may have limited access to traditional bank loans requiring access to independent and specialty lenders. High yield can also be assigned to companies that are associated with business sectors that are more susceptible to economic downturns.

Maybe you're not sure exactly where your credit profile is for budgeting purposes. Credit profiles don't always fall perfectly into any one of these three categories. In that case you can estimate and split the difference between two of the credit profile categories.

TRY OUT THE CALCULATOR >>

Other considerations when budgeting and negotiating

There are other considerations you should have in mind when thinking about budgeting and what is required to get a best and final term sheet proposal that is fully underwriting-approved and ready to finance your equipment.

Criteria for consideration for underwriting, credit approval and lease documentation.

Small ticket applications, generally those financings that are less than \$200,000, require far less financial due diligence. If your company is public, the credit review, underwriting and pricing can be quickly calculated based on the financial data that is in public domain.

If the company is private, there are 2 options to pursue financing:

1. *Complete a credit application, or*
2. *Submit a complete credit package that generally consists of 3 years audited or reviewed financial statements.*

For private companies that only have internally prepared financial statements, it can take a few days for underwriting to obtain a full credit review. For transactions of less than \$200,000, the fastest, most efficient path is to submit a completed credit application and a short-form lease. Blue Sky's Lease Calculator provides quick and easy access to an online Equipment Financing Application which you can send directly to Blue Sky to leverage our extensive network of funding sources to get the lowest total cost of your next financing.

For the private companies that have over \$200,000 in annual spend, or public companies that may have multiple transactions over a 12-month period, please use the "Request a Consultation" on the **Blue Sky website** to schedule time with a leasing advisor. In supporting more than \$2.5 billion in lease originations, Blue Sky has developed unique, direct access to funding sources to get priority response on credit approvals and below market rates.



You can do all of this on your own or you can press the easy button and make one call to have a professional take care of this for you for no added cost. IRONPROS has teamed up with Blue Sky Capital Strategies to supply low-cost, high flexibility financing to give your business the competitive edge.

For over 25 years, Blue Sky Capital Strategies has been using proprietary processes with real-time market intelligence for sourcing the most competitive financing options. It is easy and efficient to get started now!