



To Buy Or Lease?

Overview

Buying vs leasing is a very common question nowadays. In fact, leasing accounted for over 42% of all new cars last year, and the number is growing at an increasing rate. It is projected that approximately 48% of all new cars will be leased by the end of 2000.

Leasing is the process of "renting" for a specific amount of time. In effect, you are only paying for a portion of the value of the item, not its entire value. While many different types of equipment are available for lease, the most prevalent type of leasing occurs with automobiles, so we will concentrate on this area. Usually, the lease is for a 2-5 year period. You put up an initial security deposit, and usually 1-2 months' advance lease payment. In addition, when it comes to leasing a car, you pay for registration, taxes, and plates. The most prevalent type of lease usually stipulates that you will handle the maintenance and repairs as well. Most car leases have a surcharge for driving more than a certain number of miles over the term of the lease. The majority use a 10,000 to 12,000 mile per annum figure. If you exceed this figure, you may pay 10-30 cents per extra mile on average.

At the end of the lease, you turn the car back in. If there has been any "excessive" wear and tear on the vehicle, it is usually your responsibility to make good on the costs. Depending on whether you have an open-end or closed-end lease, there may be extra charges as well if the car is valued at less than the originally agreed-upon "residual value." In many lease deals, at the end of the term you may buy the car at a "lease buyout price."

As you can see, leasing may or may not be better than buying. Here are a few comparisons:

Benefits to buying

- Car has a residual value to you after a time. You can sell it.
- No restrictions on how many miles per year you can drive it.
- No insurance problems associated with a "premature" termination.
- If a home equity or investment-type loan is used to finance, the interest charges may be deductible on your tax return.
- You can treat the car any way you wish. No turn-in problems with arguing over residual value.

Benefits to leasing

- Usually less up-front money to drive car away.
- Lower monthly payment, but not necessarily lower total costs.
- It is a form of "off-balance sheet" financing, so it may not add to your borrowing maximums for other loan qualifications.
- The higher the cost of the car, and the higher the business use percentage, the greater the tax advantage may be under certain circumstances.
- Some leases may be easier to get than a loan for those with weaker credit.



Two Main Types Of Leases

Closed End Lease

This is the most common type used by consumers. At the end of the lease period, you "walk away" from the car. The so-called "residual value" of the car is determined at the beginning of the lease, so you only pay a fixed amount over a fixed period of time. Tip: Get an option to buy the car at the expiration of your lease.

Open End Lease

Although this type allows for a smaller monthly payment, it does so because you are taking extra risks at the end of the lease-the risk of value decline of the vehicle. For this type of lease, you set the value at the beginning of the term, but, unlike the closed end lease, you pay extra if the car is worth less at the end than the price you set at the beginning. Conversely, if it is worth more, you would get a rebate. This lease type can be a disaster if the residual value of a car model drops due to changes in demand, or manufacturers' defects.

Questions To Ask

Deciding whether to buy or lease depends on a number of issues, some financial, some purely qualitative. Some of the questions you should ask yourself before deciding are:

How many miles do I drive per year?

How long do I want to drive this make/model car?

What kind of monthly payment budget do I have?

What deductible business-use percentage will I qualify for?

How much do I enjoy the feel of a new car?

How good am I at reading contracts?

Assuming you have answered these questions to your satisfaction, the financial comparisons of buying vs leasing are quantifiable, as can be seen from the enclosed comparison that has been prepared for you.

Some Tips

Shop around; leases are very different, and very negotiable.

If the car you are interested in is being offered at super low financing, or with high rebates, odds are it will be cheaper to buy than lease over the long run.

Don't assume the leasing terms for the car you want are set in stone. Items such as excess mileage, excess wear, early termination clause, advance preparation fees, and Gap insurance can be negotiated to some extent.

Seriously review the "early termination" penalties. These are extra charges you may have to pay if you turn in the car early before the lease expires. Many companies will charge you these penalties(which can be very steep) even if it is not your fault-such as a stolen car, or a car that gets totalled.



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Watch for unusual restrictions in the contract such as where you can and cannot drive the car. Some leases don't allow you to drive the vehicle out of the country; some don't allow you to drive it out of the state.

Consider buying Gap insurance especially for the early years. This insurance covers the difference between the car's depreciation value at the time of mishap, and what you still owe on the lease at the time. They are rarely the same in the early years.

Consider having your lawyer review the lease before signing. Remember, this is a contract that is for a relatively large sum, filled with many legal clauses, and it can have a definite impact on your credit rating, among other items.

Definitely review the excess mileage clause. Some leases have very low monthly payments because they only let you drive 5,000 miles per year without penalty charges. Make sure your yearly driving average is within the ballpark of the lease's allowance, or be prepared to pay the extra mileage charges. As a tip, if you negotiate this extra charge before signing the lease, you may be able to greatly lower this extra cost by as much as 50%.

Leasing falls under the Federal Consumer Leasing Act, so be aware of your rights; get a copy of these rights from the lease company.

As you can see, whether leasing or buying is best for you depends on a number of issues, financial facts, and "guesstimates." Hopefully, this analysis will help to shed some light on the issues and options to make it easier for you.