Finance leasing option essay

Business

At first glance, the leasing option may seem equally enticing as the borrow-purchase plan for this equipment, but after the first year the value of choosing the borrow-purchase plan becomes more and more clear. Though the plans again come close to the same cost in the fourth year, the savings in the second year and especially in the third year make the borrow-purchase option the best choice by far. In the first year, the after tax cost of leasing is one dollar cheaper than the cost of borrow-purchase plan.

However, in the second year the leasing cost is $243 more and $372 more in the third year. In the final year, the costs begin to level out again with the leasing option being only $77 more expensive than the borrow-purchase plan. So, except for in the first year, the borrow-purchase plan is considerably more cost effective than the leasing.

In the course of the years, the borrow-purchase plan has a total cost of $691 less than the leasing option. The only way the leasing plan would make sense if the interest rate on loan was variable and expected to go higher or if the corporation was already leveraged to a point that an additional loan could affect its overall financial rating. Given that these issues are not in evidence, with all things being equal, the leasing option is a bad choice. By choosing the borrow-purchase option, the company can save almost a tenth of the total purchase price over the course of four years. Additionally, the tax savings generated by the borrow-purchase plan are significantly more beneficial than the leasing option. With the leasing option, the business may take the tax shield benefit, but loses the ability to claim depreciation.

The tax credit allowed in depreciation also helps make the decision. In four years time, the tax benefits for the borrow-purchase option are the determining factor in making it the more affordable option. Again, if tax laws were less favorable, this might not be the case.

Another option the company would have to consider would be financial incentives for paying the loan off early. If the company could afford to pay the loan earlier, it could save on interest payments and make the borrow-purchase option that much more attractive.