Why spend your capital when you can lease?

Cap Ex vs. Loan vs. Lease - a comparison of three options

When companies decide they need a new facility they can choose to either own or lease. If they choose to own they need to further decide if they want to make a capital expenditure for the entire cost of the facility or finance a majority of it through a loan, typically from a banking institution. The following is a comparison of these three scenarios:

	Capital Expenditure	**Bank Loan (with smaller Capital Expenditure)**	**Lease**
Initial Capital Outlay	Entire cost paid up-front	Typically a large down payment and bank fees are paid up front.	Minimal to no upfront payment required
Inflation/Interest Rate Risk	100% of the cost is paid up-front in "current" dollars.	Most bank loans are floating rate, so the Borrower accepts inflation/interest rate risk or may enter into an onerous hedging contract, if available.	Lease rates are fixed and typically a majority of the lease payments are on the back-end of the lease –paid in "future" less expensive dollars.
Effect on Bank Lines and Liquidity	100% of the cost is paid up-front in cash thereby reducing the firm's liquidity and increasing the likelihood that existing bank line covenants may be violated.	Reduces the amount of bank credit lines available. The reduction in liquidity is certainly less than CapEx, but financing significantly increases dependence on bank(s).	No impact to bank lines. A lease often helps with future bank negotiations by diversifying capital sources and reducing the risk for the bank.
Option to Renew/Extend	N/A – facility is acquired up-front, and Owner has no optionality.	N/A – facility is acquired up-front, and Owner has no optionality.	Tenant generally has multiple options to renew/extend its lease thereby gaining long term control of the facility.
Option to Buy	N/A – facility is acquired up-front, and Owner has no optionality.	N/A – facility is acquired up-front, and Owner has no optionality.	Lease usually include rights of first offer to acquire the facility and may even include an option to buy.
Capital Outlay upon Expansion or Renovation	100% of the cost is paid at time of expansion or renovation.	If additional bank borrowing is available typically a large down payment and additional bank fees will be required.	Most Landlords will roll 100% of these costs into a new lease.
Collateral	N/A	Banks often use blanket liens to tie up all company assets.	Usually the facility itself is all that is needed to secure a lease transaction.
Tax Impact	Depreciate over IRS useful life which is often longer than the actual useful life of the facility.	Depreciate over IRS useful life which is often longer than the actual useful life of the facility. Interest expense deducted as incurred.	May be a fully deductible operating expense subject to meeting the IRS "true lease" tests. You control the timing of deductions based on payment amounts and term and through design of the lease with BRI.

Risk of Obsolescence	Firm accepts all risk of facility obsolescence.	Due to bank lines usually being fully collateralized, the borrower accepts all risk of facility obsolescence.	The Landlord accepts all risk of obsolescence.
Reuse Risk at Move-Out (Note: Over time firms often change their plans relating to occupying and/or keeping a facility.)	The firm accepts all reuse risk at the time of sale or releasing of the facility.	Due to bank lines usually being fully collateralized, the borrower accepts all reuse risk upon sale or releasing of the facility.	The Landlord accepts all reuse risk upon sale or releasing of the facility.