

Finding The Magic Money Tree

Realities and details in leasing gear

By Doug Kocsis

Suppose we all had a money tree. What a splendid garden it would be, carefully tending our trees, pruning each branch.

Spring brings that first sign of new life; we'll call it loose change. That makes a person feel good – there's hope for vast rewards. Summer – ah summer – shows us the bold green color of our hard-earned bounty.

Then, glorious autumn. With each dollar in full maturity dropping on the yard, our treasured money tree is giving us the pleasure of literally raking in the dough. (And I don't want to talk about winter!)

Of course, there is no money tree. Rather, we all deal with a little thing called REALITY when it comes to

commerce. Yet even in this less-exciting version of the universe, there are ways of making your financial gardens grow and bloom

IN PLAIN ENGLISH

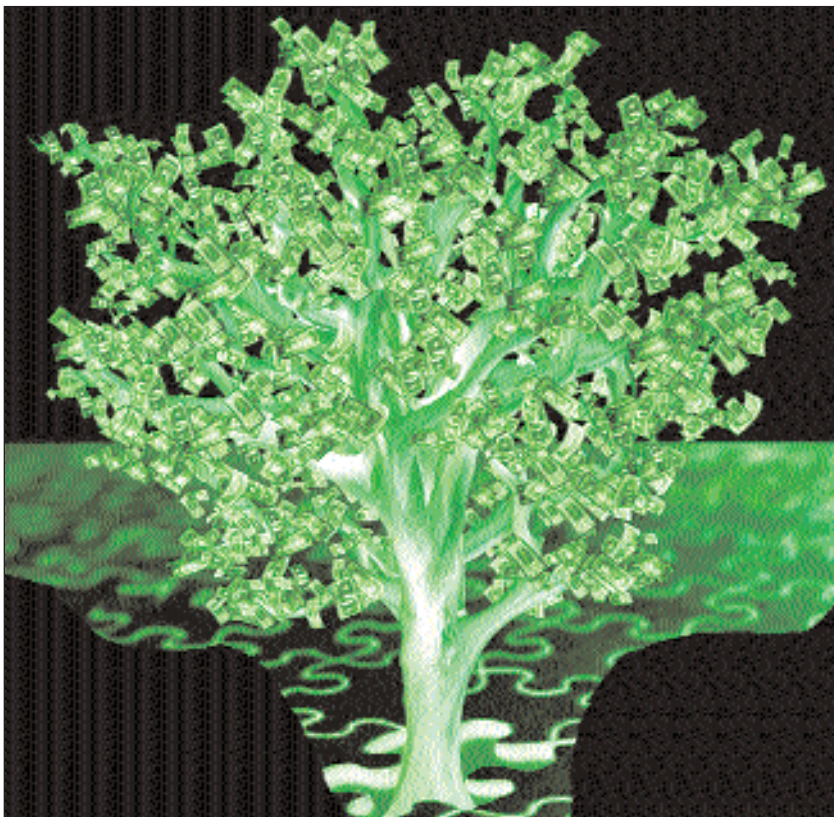
Leasing equipment, rather than buying, can present the potential for positive progress. In my discussions with vendors and customers, I find some who are all for leasing, while others can't see how it fits into their plans. How about a look at "Leasing 101" to get a better understanding?

The best place to start is with a definition in plain English. An equipment lease is simply a contract between a lessor (the company providing the lease) and a lessee (the end user). The lessor rents products to the lessee for a mutually agreed-upon period of time and specific rate of pay. The two parties also agree to a purchase option for the equipment, or it is returned at the completion of the agreement.

In the U.S., there are two basic types of equipment leases offered for general business equipment. (The IRS defines other types of leases, but in the majority of cases, we're talking about the "big two.")

One option is the Capital Lease, very similar to an installment bank loan, and, like loans, they are treated as purchases. At the end of the term, the lessee (that's you!) takes an ownership position. The assets of a Capital Lease appear on your balance sheet, with the equipment included on the depreciation schedule rather than treating it as a line item expense.

Recent tax code incentives, such as the 50 percent depreciation bonus, plays very well come tax payment time. And note that a Capital Lease is an interest-bearing note, so the interest on the lease can be classified as an expense.



Bottom Line

On the other hand, there is the True Lease. Let's say that you and your accountant (because you should be talking with your accountant!) have agreed it's better to treat your lease as a rental agreement.

A True Lease can be carried off your balance sheet and listed as a line item deduction. Note, however, that these payments are NOT interest bearing! The payments are 100 percent written off against pre-tax dollars, minimizing your taxable income.

Like any other tax break, there are rules, so don't get misled into thinking that a pre-set buyout, for example, 10 percent, is going to qualify you for this program. If this lease is treated as a purchase in any way, then it's not a True Lease. As a result, my advice is not to tango with the IRS. Or get anywhere near them, for that matter. (See *July/August 2000 issue of Live Sound for more information on these rules.*)

It's always been my position that large-ticket items typically leased by live sound professionals should be capitalized. After all, ownership is usually the long-term plan of action, isn't it?

And remember this very important rule: when capitalizing a lease, be sure to have – in writing – the exact purchase option whether it be \$1, \$1000 or 10 percent. I've heard so many horror stories about end-of-lease disasters. In fact, some really well-run businesses won't touch leasing because of this very thing.

EASIEST METHOD

Most leasing companies offer "application-only" financing arrangements, probably the easiest method of making purchases. You don't have to experience that sinking feeling of inferiority associated with being "short-chaired" by a bank. (Reference the film *It's A Wonderful Life*.) A mid- to upper-level five-figure loan can be attained by providing basic company information on the application.

A few basic qualifiers:

- **Time in business.** Two years (or more) typically opens the door.
- **Bank and trade references.** The lessor looks for an average of at least \$1,000 in your business bank account. Don't list vendors you're not paying on time – it doesn't make sense.
- **Personal credit of all owners.** Ah yes, the sensitive issue of personal credit. In today's wacky economy, it's wise to tend to your creditors. In my view, this is the single most valuable asset to your businesses.

A few other factors, more minor in nature, are involved, such as Dun & Bradstreet reports and knowing the age of the equipment to be leased if it's used. But for the most part, this is all that's required to be in the running

for an application-only lease.

When faced with a purchase larger than the parameters of the application-only lease, the financing of the equipment must be viewed similarly to approaching a bank. Most lessors request a full financial package, consisting of business and personal taxes as well as financial statements.

Also, many lessors are cash-flow lenders. If your statements verify adequate cash-flow coverage along with a reasonable net worth in accordance with the amount of money you're applying for, you'll likely qualify.

A little trick to beef up net worth when it's not obvious on your financial statement is to have a reputable appraisal firm draw up a current inventory with the street value of your unencumbered assets. This shows the lender that you care about their equity position, while also demonstrating that your company is liquid. It's helped some of my customers get large-ticket leases even though their statements didn't merit the approval.

When dealing with leases at this level, expect a discount in rates and more flexibility in terms. Rates can drop simply because you're proving to the lender that you're minimizing their risk. Terms can be flexible for the same reason.

Finally, select the right leasing company to work with. It largely comes down to comfort and fit, in addition, of course, to the lease being fair and well presented. It's like going to the barbershop. If you're not sure about the steadiness of Floyd's hands, you're not comfy in the chair, right?

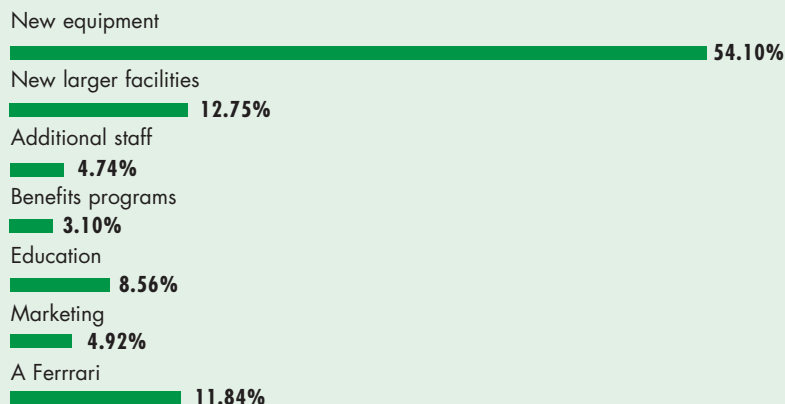
Feel out the lessor, see if there's any real care as to whether you make out well with this investment. After all, they're being paid to handle your investment, and this directly affects your livelihood.

No deal is ever perfect, so get a sense that the leasing company is going to be there for you after the deal is booked. You shouldn't feel left out in the cold. And keep dreaming about money trees! ■

Doug Kocsis is head of DK Capital, Inc., a financial services company well versed in working with the needs of small businesses. He can be reached at doug@dkcapitalinc.com.

LIVE SOUND – ProSoundWeb POLL

If I had a larger budget, I would first invest on:



Polling period: 1/10/04 - 1/24/04. To participate in LSI/PSW polls, go to www.prosoundweb.com.