

TO LEASE OR NOT TO LEASE

ADVANTAGES OF LEASING

- Leasing a vehicle is similar to renting a home. A person pays for the use of the home or vehicle. They do not build any equity. Those that favor leasing say that it makes sense to lease items that decrease in value and purchase items that increase in value. Most vehicles depreciate as they get older.
- Most leases do not require large down payments. A person may get into a lease for little money up front.
- Monthly payments are frequently smaller when leasing a vehicle. Payments are based on "use" of the vehicle by the lessee.
- The difference between a lower lease payment and a higher purchase payment can be put into a savings account or invested.
- Most leases are 24 - 60 months long. A person could drive a new vehicle every 2 - 5 years.
- At the end of the lease, the lessee is not stuck with a used vehicle.
- Leasing offers minor tax advantages to individuals. Sales tax is paid monthly as part of the lease payment and is based on the lease payment amount, versus sales tax, which is paid up front on the full purchase price on a purchased vehicle.

DISADVANTAGES OF LEASING

- Payments are made to use a vehicle that the lessee does not own.
- Leasing a car may require a better credit rating than purchasing.
- The value of lower lease payments diminishes the longer a person leases a car. It may be better to purchase a car if it is going to be kept for five or more years.
- Lease contracts frequently include penalties for each mile driven over the contract amount.
- The lessee is frequently responsible for "excessive wear and tear" at the end of a lease. The lessor may be the one who determines "excessive wear and tear". Examples could be bald tires, lost trim, cracked glass or worn seats.
- Early termination of a lease may result in a substantial penalty.
- End of lease "disposal fees" or other similar fees may be charged to the lessee.

BEFORE SIGNING THE LEASE

Make sure that you have received in writing everything that you negotiated before you sign the lease contract. Read and understand all the terms of the lease before signing the contract.

LEASE PAYMENT CALCULATION

There are basic components that determine the monthly payment amount.

1. Term or length of the lease. Usually 24 - 60 months.
2. **Gross capitalized cost.** The agreed upon value of the vehicle and any items you pay over the lease term, such as, service contracts, insurance, outstanding prior credit or lease balance and acquisition fee.
3. **Capitalized cost reduction.** The amount of any net trade-in, rebate, noncash or cash you pay that reduces the gross capitalized cost.
4. **Adjusted capitalized cost.** The gross capitalized cost less the capitalized cost reduction. The amount used in calculating the base monthly payment.
5. **Residual value.** The value of the vehicle at the end of the lease used in calculating the base monthly payment.
6. **The money factor.** A number used to calculate the rent charge. The dealer will know the money factor, which will be a decimal number.

The importance of these factors is clear when you see how a monthly payment is calculated. Here is an example of a lease payment calculation.

1. Gross capitalized cost	\$22,700
Less capitalized cost reduction	- <u>\$2,700</u>
Adjusted capitalized cost	\$20,000
2. Adjusted capitalized cost	\$20,000
Less residual value	- <u>\$8,000</u>
Total	\$12,000
Divide by number of months leased	<u>48</u>
Base monthly depreciation	= \$250
3. Adjusted capitalized cost	\$20,000
Add the residual value	+ <u>\$8,000</u>
Total	\$28,000
Multiply by the money factor	x <u>0.004</u>
Monthly rent charge	= \$112
4. Base monthly depreciaton	\$250
Add monthly rent charge	+ <u>\$112</u>
Base monthly lease payment	= \$362*

*Note: Monthly sales/use taxes will be added to the base monthly lease payments.

Multiplying the money factor by 24 approximates the interest rate: $0.004 \times 24 = .096 = 9.6\%$.

DOLLARS AND CENTS

Pay special attention to the agreed upon value of the vehicle you are going to lease. A person can negotiate to arrive at the agreed upon value, capitalized cost, terms and rates of a lease just as they can negotiate the purchase price, terms and rates when they purchase a vehicle.

Don't focus only on the monthly payment amount when negotiating. One lessor's monthly payment may be lower than another lessor's because of several factors. One lease payment may be \$199 per month but require a large down payment. Why pay a high down payment amount on a vehicle that is being rented?

Cash payment, trade-in equity or manufacturer's rebates may be applied to reduce the gross capitalized cost or may be applied toward the up-front costs, such as the first month's payment or the security deposit.

END OF LEASE EXPENSES

Find out who will perform the end of lease inspection. What are the charges for "excessive wear and tear". Be sure you understand the penalties for terminating the lease early because they can be severe. Be careful not to under-estimate the number of miles that you will put on the vehicle. The excess mileage charge can add up. Sometimes a lease contains a "disposal fee". The lessor may charge you more than a monthly payment amount simply for the privilege of returning the vehicle.

OTHER EXPENSES IF YOU CHOOSE TO LEASE

Whether a person purchases a vehicle or leases a vehicle, he will incur expenses other than just the monthly payments. Vehicles will need to be insured and maintained. What insurance is required? Does the contract include life or disability insurance? What is the cost and do you really want or need it?

Is a maintenance contract included and if so, will you be charged extra for it? Also, do you really want or need a maintenance contract on a lease vehicle? Consumers should look at both short-term and long-term costs of leasing.

GAP PROTECTION CONSIDERATION

Regular automobile insurance normally covers a vehicle if it is stolen or damaged in an accident. Such insurance will normally reimburse you for the vehicle's present market value. This amount may be substantially less than what is still owed on the lease. GAP protection covers the difference. You may be able to have GAP protection included in the lease contract or you may want to purchase it separately.

FURTHER INFORMATION

The Auto Industry Division Internet homepage, located at www.mv.state.co.us/dlr/dealer.html has information available for consumers and dealers.