

Municipal Leasing 101

A lease typically refers to an arrangement where one party owns or controls equipment, called the lessor, transfers possession and use of that equipment for a period of time to another party, called the lessee, in exchange for the payment by the lessee to the lessor of periodic rent (i.e., monthly, quarterly, or semi-annually).

A Municipal Lease has a few variations. For example A Municipal Lease or Lease Purchase is essentially an installment purchase contract with no residual and no end-of-lease buyout. A Municipal Lease is renewed annually, and as such, its payments constitute a current expense of the municipality and thereby does not create debt. Because the interest is exempt from federal and state income tax, this financing offers the municipality significant savings compared to conventional leasing.

Not all equipment acquisitions, budgets or equipment finance agreements are the same.

MUNICIPAL LEASE FINANCING HAS DISTINCTIVE ADVANTAGES OVER COMMERCIAL EQUIPMENT LEASING

- The Municipal Lease includes termination for non-appropriation language. The non-appropriation clause, in cases where the lessee is unable to obtain funding for future payment obligations on the lease, enables the lessee to terminate the lease agreement at the end of the current appropriation period without further obligation.
- A municipal lease is referred to as a “Municipal Lease purchase”. During the term of the lease, the municipality generally holds the title to the leased equipment while the lessor holds the security interest. It is a full payout contract to finance the purchase of the equipment rather than a series of rental payments as with traditional commercial leases. The financing is structured so that there is no residual value, or return option to consider.

- A Municipal Lease is also referred to as “tax-exempt” because the interest income on a Municipal Lease is tax exempt to the lessor. The municipality benefits when the lessor passes these savings on to the municipality in the form of a lower interest rate.
- Municipal Lease payments build equity in the future unencumbered ownership of the asset. The lessee has the option of purchasing the equipment outright, at any time, for a predetermined purchase price based on the remaining principal balance outstanding and unpaid.

SUMMARY OF MUNICIPAL LEASING BENEFITS

- Preserves capital
- Up to 100% financing
- Interest rates approach municipal bond rates
- No bond referendum required
- Assets can be financed over their useful life
- Fixed rate
- Simplified documentation
- Generally not subject to public bid requirements

