

[Medical Equipment Acquisition and Leasing](#)

There are a wide range of options that healthcare providers can utilize to acquire much-needed equipment. This article summarizes these choices and offers advantages and disadvantages to each option.

Options for equipment acquisition:

1. Cash Payments

This option assumes that there is enough cash available.

Advantages:

- * It's simple and quick.
- * Everybody accepts cash
- * Cash purchases minimizes paperwork and may help reduce purchase price.

Disadvantages

- * It's generally not a good use of funds because it ties up much needed capital that can be utilized in other profitable ways.

In today's investment market, you can often obtain a yield on your money in excess of the interest charged for financing the equipment purchase. The only rationale for paying cash for the purchase is if your funds are in a low-paying account whose yield is less than the interest on a loan or lease. In that case, taking the funds from a low-yield account in order to avoid paying 9% or 10% is a sound financial decision. Of course, having significant funds in a 3% account is not wise cash management.

2. Financed Purchase

In this method of purchase, a lender provides funds for the purchase and generally obtains some form of lien or other encumbrance on the equipment until the funds have been repaid.

Advantages

- * It does not deplete cash flow. Usually a 10% to 20% down payment of the total purchase price is required. In many cases, the income generated by the equipment can exceed the payments.)
- * Funds not expended for a cash purchase can possibly earn a higher-income yield than the interest rate of the loan.

Disadvantages

- * Interest rates may be high.
- * The down payment may be high.
- * The equipment is encumbered by a third party unless the funds are borrowed from a source other than a financial institution such as a pension fund.

3. Leasing

A lease offers an alternative to traditional financing. With a lease, the equipment is owned by the leasing company. The practice makes payments to the leasing company in exchange for being able to use the equipment (i.e., essentially rental payments). Leases can be closed-ended, in which case the leasing entity retains the equipment at the end of the lease term. There are also open-ended leases, where at the end of the lease term a predetermined amount is paid to the leasing entity, and the practice attains ownership of the equipment.

As a general rule, the higher the residual value (balance owed) at the end of the lease, the lower the monthly payments.

Advantages

- * Generally little or no down payment is required.
- * Leases are often supported by the equipment manufacturer, which can lower the interest rate or the residual payment (the amount required to attain ownership of the equipment at the end of the lease term).
- * Leasing can give you the ability to obtain more purchasing power from a given amount of available cash.
- * Sometimes equipment becomes obsolete in a relatively brief period of time. A closed-ended lease may allow you to use the equipment during its useful life and return it to the leasing entity at the end of the lease term. This arrangement could result in lower total expenditures than an outright purchase would have required.

Disadvantage

* In general, more interest is paid than in any other form of acquisition.

Other Leasing Considerations

1. Trade: An equipment manufacturer may have a lease program that makes it easy for the lessee to upgrade. The program can make sense for the lessee if the lessor grants significant credit for the older equipment. This can alter the calculation of the best option for acquisition.

2. Supported Leases or Financing: An equipment manufacturer may support the interest rate of a lease or financing plan. They may lower lease payments by increasing the residual value of a closed-ended lease. Again, these special offers may significantly alter the assessment of the best acquisition option.

3. Purchase Price: No matter what financing option you choose, do not ignore the purchase price. Negotiate your best price before you evaluate financing. Do not fall into the trap that automobile dealers have used for years. You should always start with the purchase price and then move to the terms (whether lease or purchase).

4. Beware of the lease that's not a lease. The Internal Revenue Service may consider an open-ended lease with a purchase option to be a purchase contract rather than a lease. The impact of this is that the lease payments may not be deducted as expenses. Instead, the equipment will be capitalized and depreciated. Have your professional financial advisor evaluate the financing contract to assess your level of risk.

5. Each Transaction Is Unique: Each piece of equipment you are considering for acquisition must be evaluated in the context of the following:

- a. Purchase price
- b. Projected useful life of the item
- c. Your current cash position and monthly cash flow
- d. Your current and projected future tax position
- e. Financing incentives offered by the vendor
- f. Careful evaluation of the lease or financing contract to ensure that it meets the requirements for the method you plan to use to report the equipment in your tax filings
- g. Any other considerations required by your expert financial and tax advisors

Discussion

In today's financial and tax environment, many of the factors that favored one type of financing over another have disappeared. What remain are the purchase price and financing terms, whether the transaction is called a lease or a purchase. Keep in mind that today's market may not be as good as it was in the past. In the final analysis, you may find that purchasing is cheaper than the interest cost on a lease.

For equipment that you anticipate retaining at the end of the lease or financing term, you must evaluate several factors. The purchase price, down payment, monthly payments, and total payments are key. These factors can be impacted by incentives from the vendor, but ultimately the same evaluation needs to be done.

If you are just starting out, your current cash position may dictate that you finance the equipment. Remember to get advice from a professional lease broker to help you sort out the details of the equipment lease.

About the Author

Kent Harlan has been a CPA since 1984 and is the owner of Ozarks Capital Funding, a firm offering financing in the areas of accounts receivable factoring, [equipment leasing](#), and [financing for healthcare providers](#).

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