



## Will leasing equipment or buying it be more tax efficient for your business?

Recent changes to federal tax law and accounting rules could affect whether you decide to lease or buy equipment or other fixed assets. Although there's no universal "right" choice, many businesses that formerly leased assets are now deciding to buy them.

### Pros and cons of leasing

From a cash flow perspective, leasing can be more attractive than buying. And leasing does provide some tax benefits: Lease payments generally are tax deductible as "ordinary and necessary" business expenses. (Annual deduction limits may apply.)

Leasing used to be advantageous from a financial reporting standpoint. But new accounting rules that bring leases to the lessee's balance sheet go into effect in 2020 for calendar-year private companies. So, lease obligations will show up as liabilities, similar to purchased assets that are financed with traditional bank loans.

Leasing also has some potential drawbacks. Over the long run, leasing an asset may cost you more than buying it, and leasing doesn't provide any buildup of equity. What's more, you're generally locked in for the entire lease term. So, you're obligated to keep making lease payments even if you stop using the equipment. If the lease allows you to opt out before the term expires, you may have to pay an early-termination fee.

### Pros and cons of buying

Historically, the primary advantage of buying over leasing has been that you're free to use the assets as you see fit. But an advantage that has now come to the forefront is that Section 179 expensing and first-year bonus depreciation can provide big tax savings in the first year an asset is placed in service.

These two tax breaks were dramatically enhanced by the Tax Cuts and Jobs Act (TCJA) — enough so that you may be convinced to buy assets that your business might have leased in the past. Many businesses will be able to write off the full cost of most equipment in the year it's purchased. Any remainder is eligible for regular depreciation deductions over IRS-prescribed schedules.

The primary downside of buying fixed assets is that you're generally required to pay the full cost upfront or in installments, although the Sec. 179 and bonus depreciation tax benefits are still available for property that's financed. If you finance a purchase through a bank, a down payment of at least 20% of the cost is usually required. This could tie up funds and affect your credit rating. If you decide to finance fixed asset purchases, be aware that the TCJA limits interest expense deductions (for businesses with more than \$25 million in average annual gross receipts) to 30% of adjusted taxable income.

### **Decision time**

When deciding whether to lease or buy a fixed asset, there are a multitude of factors to consider, including tax implications. We can help you determine the approach that best suits your circumstances.