

Purchase vs. Lease Recommendation

May 24, 2007

I've spent quite a bit of time over the past couple of weeks trying to determine the implications of leasing buses versus purchasing them. In the past, we've purchased buses and utilized 3-4 loans to finance. In discussing the issue with Curt Kleckler, there are certain parameters to look at when discerning whether to lease or purchase. One issue is to determine whether the lease is an operating or capital lease. The terms of a capital lease places the ownership of the bus in the hands of the school district and would count towards our debt limit. An operating lease, on the other hand, has terms that do not place the ownership of the bus in our hands. We pay for the service/operation of the bus/vehicle. An operating lease does not count against our debt limit. In the documentation that Curt sent me, which is attached, there are four criteria to evaluate to determine whether the terms of the lease are "capital" or "operational".

1. The lease transfers ownership to the lessee by the end of the lease term. (The lease we are recommending does not transfer ownership to us. We do not have an option to purchase)
2. The lease contains a bargain purchase option. (The lease we're recommending does not)
3. The term is equal to 75% or more of the estimated economic life of the leased property, and the beginning of the lease term does not fall within the last 25% for the useful economic life of the leased property. (This lease is for new buses which have a life expectancy of around 10 years (50%). The lease is for new buses which are on the front end of the useful life)
4. The present value (PV) of the minimum lease payments at the beginning of the lease term is 90% or more of the fair market value to the lessor less any investment credit retained by the lessor. This requirement cannot be used if the lease's inception is in the last 25% of the useful economic life or the leased asset. The interest rate, used to compute the PV, is the incremental borrowing rate of the lessee unless the implicit rate is available and lower. For the purpose of this test, lease structuring fees or lease administration fees paid by the lessee to the lessor are included as part of the minimum lease payments. (the lease cost of \$12,905 for five years compared to the purchase price of \$72,387 is just under 90%)

A lease agreement meets none of the four criteria set forth above it, it is classified as an operating lease by the lessee. In this scenario, the lease would be an operating lease and not count against our debt limit. In terms of looking at financial impact between leasing and purchasing is negligible. The total cost in almost identical. I believe the issue is the position we would be in at the end of the loan. At the end of five years in the lease, we do not own the buses and would return them. Additionally, we would not have any trade in value available to us. In the purchase scenario, we would have the flexibility to keep the buses for an additional year depending on our financial situation. With the new bus

purchase we might need to extend the life of buses concurrent with the cost of a funding a possible new building. In my opinion, purchasing the buses provides more flexibility at the end of the term with the buses.

<u>Purchase</u>	Qty	Purchase Price	Total Cost	Down Payment	4 year loan payout/yr (4.75%)	Total Loan	Total including down payment	Total minus trade in after 5 years, approximate (\$45,000)
New Buses	3	\$72,387	\$217,161	\$43,432	\$48,790	\$195,161.95	\$238,593.95	\$193,593.95
<u>Lease</u>	Qty	Purchase Price	Total Cost	Down Payment	Annual Lease/year (5 year lease)	Total for 3 buses for five years	Total including down payment	Total cost after five years
New Buses	3	N/A	N/A	N/A	\$12,905	\$193,575	N/A	\$193,575

Recommendation: Agree to lease terms and purchase from Midwest for the following:

Qty.	Vehicle	Purchase Price	Payment
3	2008 International IC/CE 300-77 Passenger bus	\$217,161	Down payment and 4 year loan
1	Extend current lease on activity bus	\$8,000 (new bus)	1 year lease
1	Extend current lease on 24 passenger	\$9,405	1 year lease