What is "tax-exempt" municipal leasing?

(A non-technical/non-legal definition)

Or perhaps you've heard of municipal leasing's "first financial cousin," the tax-exempt municipal bond. Both are very low cost methods of financing the acquisition of essential-use equipment, vehicles, hardware and software exclusively for state, county and municipal governments, special districts and authorities ("municipal" leasing is an umbrella term applicable to all of the aforementioned entities.) There are however some very significant differences between leases and bonds, that we'll cover below.

Let's start with the "tax-exempt" piece first as it is sometimes misunderstood. The I.R.S. created tax-exempt municipal leasing (and bonds) as vehicles to provide state, county & municipal entities--also referred to as state and political subdivisions, with access to the lowest cost of funds. The I.R.S. accomplished this by allowing banks and investors to deduct the interest earnings and carrying costs on these transactions from *their* federal income taxes--thereby lowering the funding source's "cost of doing business" and allowing them to lend at considerably more aggressive rates than would otherwise be possible. Hence the "tax exempt" nomenclature that we use to distinguish this unique type of borrowing. It is the funding source that is "exempt" from their federal (and sometimes state and local) taxes. This I.R.S. tax exemption should not be confused with sales (or other) taxes which most, but not all governments are exempt from on their typical purchases.

What are the critical difference between municipal leases and municipal bonds?

Both are types of multi-year borrowings. Both reflect the very attractive interest rates characteristic of their tax-exempt pricing as described above. But there are some BIG DIFFERENCES *to you*, the borrower.

Bonds are based on an unconditional pledge of the "full faith and credit" of the municipal entity, including a pledge to levy property taxes on every tax-payer in the jurisdiction, as necessary to cover the bond debt, if necessary. This is why most bonds require public consent in the form of complicated, time-consuming and expensive voter referendums. In direct contrast to bonds, our municipal leases ARE subject to the annual appropriation of funds in all jurisdictions that require it--meaning that if funds are not available to make the payments for any legal reason, in any budget year, the government entity would have the legal prerogative to terminate the lease after the current budget period *without legal penalty* and to return the equipment/vehicles to us (the Lessor). This is one reason why a municipal lease, unlike a bond, does not generally create balance sheet debt on the books of the Lessee (municipal entity).

While the very low interest rates on tax exempt municipal leases compares favorably with bonds, municipal lease issuance expenses are just a small fraction of the those involved in the documentation and legal compliance required for bonds--making bonds a much more expensive option for all but the largest (multi-million dollar and up) transactions.

For more information on municipal leasing:
http://www.LeaseExperts.com/MUNICIPAL_LEASING.htm
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