Leasing

Lessor - Owner
Lessee - User of the Asset

View points

Lessee

(a) **Borrowed**

Total Cost	xx
→ Interest (after Tax)	
→ Principal (No Tax)	
Less:	(xx)
→ Tax Shield on Dep^n	
→ Salvage Value	
CFAT	xx

(b) **If Leased**

Total Cost	xx
→ Lease Rentals	
Less:	(xx)
→ Tax Shield on Lease Rentals	
	xx

Lessor

Lease

Total Incomes:	xx
→ Lease Rent Recd (after Tax)	
→ Dep^n Shield	
→ Salvage Value	
Less:	
Initial Invest	(xx)
NPV	xx

Lease - Issues

1. Whether to Buy or Lease?
2. How much Lease Rental to charge?
3. N P V of the asset

Note : If advance Pj comes, Yr 0 there will be no tax benefit.

: Which discounting rate to take?

→ Disc Rate Given — Take that

→ COC is given — ——

→ Both are Given — Rate of Interest (1 - t) on BORROWING

→ **EAI case**

It means Installments are same, but principal & interest varies yr - yr

S_1 : Calculate EAI ie $\frac{\text{Invst}}{1 + \sum DF (1-n)}$

S_2 : Draw the Table

Yr(A)	EAI (B)	Loan(C) (Beg)	Interest(D)	Princi (E)	Loan(F) (end)	Int(1 - t) (G)
	S_1	Invst	= C × rate	= B - D	= C - E	= D(1 - t)
	S_1			Cos Instal = P + I	deduct only Principal	Cos Interest gets Tax benefit
	S_1					
	S_1					

→ Salvage & CG Issues

Note that Salvage Value means Sale Value
Calculate WDV of the Machinery at the Salvage Value date. If Sal Value > WDV = profit
Sal Value < WDV = Loss

If Loss, profit reduces, Hence can get tax benefit on it.

eg:

WDV on 31/3/2012	- 8,00,000
Salvage Value	- 7,00,000
tax	= 10%
Disc fact	= 12% assume 0.012 @ yr_5

∴ P.V of Salvage + Tax Savings on Loss
⇒ (7,00,000 × 0.012) + (Loss × rate of tax × disc factor)
+ 1,00,000 × 10% × 0.012

Ignore Common Costs ie Costs that has to be incurred if opted Borrowing or Leasing option