

Budget Bricks, Keeping Tax Requirements Level While Maintaining Equipment Refresh Schedule

	Fiscal Years	1	2	3	4	5	6	7	8	9	10	11	12	13	14
\$ 400,000					Lease 4 \$100,000				Lease 8 \$100,000				Lease 12 \$100,000		
\$ 300,000			Lease 3 \$100,000				Lease 7 \$100,000					Lease 11 \$100,000			
\$ 200,000		Lease 2 \$100,000				Lease 6 \$100,000				Lease 10 \$100,000					
\$ 100,000	Lease 1 \$100,000				Lease 5 \$100,000				Lease 9 \$100,000						

Effective Use of Lease Purchase as a Budgeting Tool

GOALS:

- Maintain tax levy at a constant level.
- Optimize equipment replacement schedule to reduce age related maintenance cost.
- Avoid budgetary peaks and valleys.

Too often key equipment replacements for public entities are pushed off for the sake of budgetary limitations. The pushing back of replacements normally results in, greater equipment down time, reduced efficiency of services and increased maintenance costs. Inevitably reality sets in and you have to “bite the bullet.” Finding funds to replace essential equipment in a stressed budget environment can wreak budgetary havoc.

Budgeting more and more for maintenance on older out-of-warranty equipment because you can't afford to purchase new?

Annually convert a portion of your equipment maintenance budget to a lease purchase payment. Use the allocated funding to do a Net Present Value (NPV) lease purchase. A fixed amount in your budget for lease purchase payments will yield constant replenishing funding amount for new equipment.

Assume that a governmental unit has an annual maintenance budget of \$600,000. The equipment being maintained is older, seven to ten years old as an average. Every year for the next four years the governmental unit will reduce the maintenance budget by \$100,000 a year. Annually \$100,000 will be pledged as a lease purchase payment for four years. The NPV of the \$100K lease purchase payment will purchase about \$385,000 of new equipment. For the first year the maintenance budget is reduced to \$500,000 with \$100,000 being transferred to the lease purchase program.

Net Present Value (NPV) of 4 Annual \$100,000 Payments in Advance

Compound Period: Annual
 Nominal Annual Rate: 2.250% estimated

CASH FLOW DATA

	Event	Date	Amount	Number	Period	End Date
1	NPV	2/2/2015	386,989.69	1	\$ Available	at funding
2	Payment	2/2/2015	100,000.00	4	Annual	2/2/2018

In year two the maintenance budget is reduced by another \$100,000 to \$400,000. A new four year NPV lease is entered into and another \$385,000 of new equipment is added. This is repeated in years three and four. The original annual maintenance budget is reduced to \$200,000 a year. In the first four years of the lease purchase program there are four NPV leases that have acquired about \$1,540,000 in new equipment which is under warranty. The average age of equipment has been reduced allowing for greater reliability and a reduction in maintenance costs.

Starting in year five of the program the first NPV lease purchase has been paid off is replaced by a new four year lease purchase with another \$385,000 of new equipment being acquired. The cycle starts again as each annual lease is paid off a new one is entered.

Results: in the space of eight years, with no change in the tax impact to the budget, over \$3,000,000 of new equipment has been purchased with an average age of 4 years. Maintenance costs have been reduced and governmental services improved.

Dennis R. Balodis
DBalodis@HunterdonESC.org
 (908) 439-4280 ext. 4510
 Hunterdon County ESC

