



# THIS SMART FINANCIAL MOVE PUTS MONEY IN YOUR POCKET AND THE NEWEST EQUIPMENT TO WORK

**EQUIPMENT-AS-A-SERVICE CAN HELP YOUR BUSINESS PAY AS YOU GO FOR MACHINERY YOU NEED NOW WHILE AVOIDING ONEROUS UPFRONT CAPITAL EXPENDITURES AND PROVIDING GREATER PREDICTABILITY.**

BY NELSON ABELHA

In the world of heavy equipment, ownership can be costly and burdensome. Aside from the initial purchase price of equipment, there is also the financial responsibility of maintenance, repair, and eventual depreciation.

This is where Fair Market Value (FMV) leases can offer significant cost advantages and flexibility. With an FMV lease, organizations can receive the full benefits of using the equipment while only paying for a portion of the machine's value over the lease term.

## FMV LEASES FREE UP CAPITAL

An FMV lease is a type of operating lease that allows businesses to use equipment for a specified period while making regular payments. This structure is particularly beneficial for companies that need access to heavy equipment but don't want to invest large amounts of capital up front.

At the end of the lease term, the business has the option to return the equipment, extend the lease, or purchase the equipment at its fair market value. Additionally – and as mentioned previously – one of the biggest advantages of an FMV lease is that it allows businesses to use equipment without having to pay the full cost of ownership. This is especially valuable in the construction sector, where equipment is essential but not always needed long-term. Rather than tying up capital in equipment purchases, companies can allocate those funds toward other critical operational areas.

With an FMV lease, businesses only pay for the use of the equipment during the lease term and are not responsible for the total value of the machine, as they would be with an outright equipment purchase. The result is a more efficient use of financial resources, allowing companies to access the equipment they need while keeping their capital free for other investments.

## THE ADVANTAGES OF THE EQUIPMENT-AS-A-SERVICE MODEL

The concept of "equipment-as-a-service" has gained popularity in recent years, and FMV leases are a prime example of this model in action. With equipment-as-a-service, businesses essentially rent the functionality of the machine rather than owning it outright. This approach offers several advantages.

Equipment-as-a-service allows businesses to control costs more effectively by only paying for the use of the machine rather than bearing the total cost of ownership, maintenance, and repairs. Companies can use the equipment for as long as needed and then return it at the end of the lease term, avoiding the long-term commitment and costs associated with ownership.

With an FMV lease, businesses can easily upgrade to newer models at the end of the lease term, ensuring they always have access to cutting-edge technology and the best tools for the job. This regular access to newer equipment can lead to improved efficiency, reduced downtime, and, ultimately, a stronger bottom line.

The ability to turn variable costs into fixed costs has a direct impact on a company's cash flow and financial forecasting. When costs are predictable, it's easier for businesses to allocate funds toward other essential areas such as labour, materials, and project development. This is especially important in an industry such as construction, where cash flow can be inconsistent due to the seasonal nature of the work and dependencies on supply chains and project timelines.

By returning equipment at the end of the lease and opting for newer models, businesses can also avoid the pitfalls of owning outdated equipment, which can become costly to maintain and less efficient over time.

## A LOOK AT THE EQUIPMENT-AS-A SERVICE MODEL IN ACTION

ABC Construction needed a fleet of excavators for a two-year project. Instead of purchasing the machines outright, ABC opted for an FMV lease.

By choosing to lease rather than purchase, ABC Construction effectively shielded itself from potential financial losses tied to the resale of depreciated equipment at the project's end. This savvy decision relieved the company from the obligation of paying the total value of the machines up front and eliminated burdensome maintenance costs.

Opting for a Fair Market Value (FMV) lease allowed ABC Construction to streamline its expenses into a single manageable monthly payment. This not only ensured consistent monthly costs covering the equipment but also included essential maintenance, repairs, and soft costs like installation. Such an approach not only simplifies budgeting but also enhances operational efficiency, making it a wise choice for any construction firm.

This strategic shift stabilized ABC Construction's cash flow, providing the funds needed for critical areas like hiring skilled labor and procuring materials. As a result, the company boosted profitability and increased its capacity to take on more projects without the fear of unexpected financial burdens.

At the conclusion of the 24-month project, ABC simply returned the equipment, having only paid for its use throughout the lease. This method allowed them to expand its equipment fleet for the larger short-term project and return the machinery once it was no longer needed. Ultimately, this strategy put them in a prime position to upgrade to the latest models, ensuring the company always has access to cutting-edge technology for future projects.

By leasing rather than purchasing, ABC Construction avoided the costs associated with making payments on the full value of the machine, in maintaining that equipment and taking a loss on the eventual sale of this depreciated equipment at the end of its useful life. By opting for an FMV lease, ABC Construction was able to bundle all these variable costs into its monthly lease payment. Over the course of the lease term, the company enjoyed fixed monthly costs that covered not just the equipment, but also all associated maintenance, repairs, and soft costs such as installation.

This shift allowed ABC Construction to stabilize its cash flow, ensuring it had sufficient funds available for other important areas such as hiring skilled labor and purchasing materials. As a result, the company saw increased profitability and was able to take on more projects without having to worry about unexpected expenses.

At the end of the 24-month project, ABC simply returned the equipment, having only paid for the use of the machines during the lease term. ABC Construction was able to expand its equipment fleet to accommodate this larger short-term project, then return the equipment at the end of the lease, when it was no longer needed. Ultimately, they were able to upgrade to the latest models when their next project required more advanced technology.

For a \$700,000 unit, the payment is **\$21,869.38** per month.

ABC Construction was also provided an alternative — a 36-month capital lease:  
For the same \$700,000 unit, the payment is **\$21,639.08** per month.

However, since the project is only 24 months in duration, with a 36-month capital lease, ABC Construction would be obligated to make an additional 12 months of payments for a machine it no longer required.

**That is an additional carrying cost of \$259,668.96.**

#### A SMART, FLEXIBLE SOLUTION FOR EQUIPMENT NEEDS

FMV leases provide businesses with the flexibility and financial efficiency needed to stay competitive in the construction sector. By allowing companies to receive the full benefit of equipment without paying for its total value, and by offering the option of regular equipment upgrades, FMV leases are effectively turning equipment into a service that businesses can rely on.

An FMV lease provides more than just access to equipment — it offers financial predictability. By converting variable costs such as repairs, maintenance, and soft costs into fixed payments, construction companies can better manage cash flow, reduce financial risks, and make more informed business decisions. For greater financial stability in an unpredictable industry, an FMV lease is a valuable tool that is worthy of consideration.



THE CONCEPT OF "EQUIPMENT-AS-A-SERVICE" HAS GAINED POPULARITY IN RECENT YEARS, AND FMV LEASES ARE A PRIME EXAMPLE OF THIS MODEL IN ACTION.

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## CONSTRUCTION BUSINESS



# 5 WAYS TO LEAN INTO CREATIVE FINANCING TO GIVE YOUR BUSINESS A NEW LEASE ON LIFE IN UNCERTAIN TIMES

BY NELSON ABELHA

Life in the construction sector hasn't been easy lately, given the challenging economy and uncertainties at every turn. Unfortunately, it looks like we'll all need to continue to keep our seat belts tightly fastened for the foreseeable future. In a recent economic update, Ken Wattret, vice president of global economics at S&P Global Market Intelligence, says: "The path forward will likely remain bumpy, given numerous US-related uncertainties, including the risk of a hard landing, the timing and magnitude of policy rate cuts, and the outcome of elections in November and their policy implications."

For those in the construction industry, the path to persevere and grow isn't as clear-cut as in the past. Adaptability is crucial, and this adaptability should also apply to construction equipment financing.

Full Market Value (FMV) leases, which can often be viewed as rigid or conventional, can be customized to meet unique business demands. This ushers in newfound flexibility to help companies adapt and adopt new approaches.

The industry is employing FMV leases in creative ways, empowering companies to navigate significant obstacles and capitalize on new opportunities.

Below are five use cases highlighting the flexibility and potential of FMV leases as creative financing strategies for the construction sector.

## 1 – CROSSING BORDERS TO SECURE THE RIGHT EQUIPMENT

One area where creative financing approaches can come to the rescue is in the instance of cross-border equipment financing. This may come into play when the equipment needed for your project doesn't happen to exist in the country you currently operate within. Sometimes, a client may require a piece of equipment built overseas or that exists presently overseas.

Recently, a construction company based in Canada needed to purchase a machine from a dealer in the United Kingdom. The complexities of cross-border transactions can be challenging, especially when it comes to securing the necessary funds. Creative leasing approaches were of benefit here, not only to fund the down payment and ensure the transaction could move forward but also to fully fund the deal before the machine was even shipped to Canada. This approach minimized the financial risk for the company. It streamlined the entire transaction process, making it possible for them to acquire the equipment they needed without delay while enabling them to continuously focus on their day-to-day operations.

## 2 – MAKING FLEXIBLE PAYMENT STRUCTURES ALIGN WITH CASH FLOW

Cash flow management is critical for construction companies, especially when dealing with large equipment purchases. However, as anyone in the industry knows, cash flow can and often does fluctuate, particularly in the initial months of a contract.

Creative financing approaches can take a debt load off in these scenarios. Look for unique finance structures, such as deferred and skip payments, that align with your revenue streams. By deferring payments or allowing skips in the early months, companies can focus on completing their projects without the added pressure of immediate, substantial payments.

Alternatively, if your business performs seasonal work, such as fewer highway paving projects in the winter months or snow removal in the winter months with less usage in the summer months, payment months can align with months with the highest incoming receivables, making payments much more manageable.

## 3 – FINANCING SPARE PARTS TO PREVENT DOWNTIME

Unplanned machine downtime can be incredibly costly, so it's crucial to have spare parts on hand, particularly because replacement parts can be in short supply. Over the past few years, the industry has experienced lengthy lead times for replacement parts.

To help maintain operational efficiency, creative financing approaches can offer needed resources specifically for spare parts purchased along with the machine orders. This proactive approach allows companies to stock essential components to keep their operations running smoothly, by avoiding crucial part shortages and lengthy downtimes.

## 4 – INTERIM FINANCING FOR FACTORY-ORDERED MACHINES

Long lead times are often required for factory-ordered machines, and manufacturers typically demand a down payment before commencing the build process. For many companies, this presents a significant cash flow challenge, particularly when a machine can take upwards of nine months or longer to build. Creative financing strategies can address this issue by financing the interim payments. This allows organizations to avoid substantial out-of-pocket expenses before the machine is built and operational, providing the financial flexibility needed to begin paying for the equipment once it is put into operation. In this way, companies can achieve a positive return on their equipment investments immediately.

## 5 – FIRST AMENDMENT LEASES: FLEXIBILITY FOR THE LONG TERM

Creative financing can offer the best of both worlds – a structure that begins with an operating lease, complete with a residual, but with the ability to extend and transition into a full payout term. This innovative approach gives organizations the flexibility to adjust their financing as their needs evolve, giving them more flexibility regarding their assets. Initially, a company can benefit from the lower payments and flexibility of an operating lease. Later, if desired, a company can amend the lease to fully amortize the equipment, retaining it for the long term, giving them more flexibility regarding their assets.

## FAIR MARKET VALUE LEASES: THE CREATIVE FINANCING OPTION THAT GIVES YOU OPTIONS

FMV leases can be more than just a standard financing option, they can be incredibly flexible and adaptable; lease terms can be adjusted to address specific needs and an organization's financial scenario, which is especially crucial when the business outlook and/or cash flow may be unpredictable.

As the use cases above illustrate, they can be a powerful tool to help your business grow, adapt, and thrive. Whether you're dealing with cross-border transactions, managing cash flow, or planning for future equipment needs, creative financing approaches can help you access needed resources.

As César Pelli, the famous Argentine-American architect who designed some of the world's tallest buildings and other major urban landmarks, noted, "Construction is a matter of optimism; it's a matter of facing the future with confidence." Creative financing gives the construction sector greater capacity and confidence to navigate today's business and economic challenges.



The industry is employing FMV leases in creative ways, empowering companies to navigate significant obstacles and capitalize on new opportunities.

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# WHICH LEASE TYPE IS MORE FLEXIBLE? DEBUNKING MYTHS & MISCONCEPTIONS

## UNDERSTANDING THE TRUE NATURE OF FAIR MARKET VALUE (FMV) AND CAPITAL LEASING AGREEMENTS CAN HELP COMPANIES MAKE MORE INFORMED DECISIONS ALIGNED WITH THEIR OPERATIONAL NEEDS AND STRATEGIC GOALS.

BY NELSON ABELHA

Construction companies often need to make decisions about how to finance their heavy equipment. There are two main options: operating leases, also known as Fair Market Value (FMV) leases, and capital leases, also known as finance leases.

Although both leasing options have their advantages, there's a common misconception that capital leases offer greater flexibility. However, a closer look shows that FMV leases may actually be a better choice to provide the quintessential operational versatility that construction companies need.

Let's take a closer look at each leasing type to debunk the myth of capital lease flexibility and highlight how and why FMV leases can provide optimal flexibility, making this lease type a far superior choice.

### UNDERSTANDING CAPITAL LEASES

Capital leases essentially give the lessee (borrower) ownership of the equipment. The lease term typically covers most of the equipment's useful life. At the end of the lease term, the lessee has the option to purchase the equipment for a nominal fee, usually \$10 or \$1. This type of lease is recorded as an asset and a liability on the company's balance sheet, reflecting the equipment's value and the obligation to make future lease payments.

#### Advantages of Capital Leases

1. **Ownership benefits** The lessee eventually owns the equipment, which can be advantageous if the machinery has a long operational life and is essential to the company's core activities.
2. **Depreciation** Although I'm not an accountant, nor do I play one on TV, the company can benefit from tax advantages related to the equipment's depreciation.
3. **No usage restriction** There is no limitation on how many hours a construction company can operate the machinery throughout the lease term. Since the equipment cannot be returned, there are also no concerns about its condition at the end of the lease term. This is beneficial if the equipment is heavily used and may not be in a suitable condition for return. At first blush, capital leases may seem to offer quite a bit in the way of flexibility, but there's more to this story. Despite these advantages, capital leases may not be as flexible as they appear.

#### The Illusion of Flexibility in Capital Leases

The perception of flexibility with capital leases often comes from the aspect of ownership. However, this ownership can limit flexibility in several ways:

1. **Long-term commitment** Capital leases require a long-term commitment to the equipment. This can be a significant drawback if a company's needs change or technological advancements render the leased equipment obsolete. In an industry where machinery and technology evolve rapidly, being tied to older equipment can be a disadvantage.
2. **Balance sheet impact** Since capital leases are recorded as assets and liabilities, they increase a company's debt-to-equity ratio – a key financial statement metric. This can affect the company's financial health, potentially making it more challenging to secure additional financing or impacting borrowing costs, which can restrain growth.
3. **Maintenance and disposal** Ownership means the lessee is responsible for all maintenance and disposal costs. These costs can be substantial for heavily used construction equipment. Additionally, the company must manage the logistics of selling or disposing of the equipment at the end of its useful life, adding another layer of complexity. This often means the company must employ its own team of technicians.

### THE TRUE FLEXIBILITY OF FMV LEASES

Alternatively, FMV leases offer a different kind of flexibility that can be aligned with the dynamic needs of construction companies. Under an FMV lease, the lessee pays for the use of the equipment for a specified period, with the option to purchase the equipment at its fair market value at the end of the lease term. Alternatively, the lessee can choose to return the equipment or renew the lease, and in some cases, this can be on a month-to-month basis.

#### Advantages of FMV Leases

1. **Lower monthly payments** FMV leases typically have lower monthly payments compared to capital leases. This is because the lessee is not paying for the full cost of the equipment, just for its use during the lease term. Lower payments improve cash flow, allowing the company to allocate financial resources to other critical areas.
2. **Upgrade options** At the end of the lease term, companies can return the equipment and lease newer models. This is particularly beneficial in the construction industry, where technology and equipment quickly become outdated. The ability to upgrade ensures the company always has access to the latest and most efficient machinery.
3. **Maintenance and repairs** Many FMV leases include maintenance and repair services. This reduces downtime and transfers the burden of maintenance costs away from the company while helping ensure the equipment remains in optimal condition throughout the lease term.
4. **Flexibility at lease end** FMV leases provide multiple options at the end of the lease term: The lessee can return the equipment, purchase it at fair market value, or extend the lease. This flexibility allows construction companies to adjust their equipment needs based on business conditions and project requirements.

### DEBUNKING THE MYTH

Many people mistakenly believe that capital leases offer more flexibility due to the traditional association of ownership with control. However, in the fast-paced construction industry, where adaptability and financial agility are crucial, Fair Market Value (FMV) leases often provide superior flexibility. They enable companies to keep up with technological advancements, manage cash flow more effectively, and avoid the pitfalls associated with long-term ownership commitments.

While capital leases have their own benefits, they do not necessarily provide greater flexibility. For numerous construction companies, FMV leases present a more versatile and financially prudent option. Understanding the true nature of these leasing agreements can help companies make more informed decisions aligned with their operational needs and strategic goals. The real flexibility lies in the ability to adapt to changing circumstances – something that FMV leases facilitate far better than capital leases.

## The True Flexibility of FMV Leases

Pay for the equipment over specified period then purchase, return, or renew the lease.

### PROS:

- Lower Monthly Payments
- Upgrade Equipment as Needed
- Maintenance & Repairs Included
- Flexibility at End of Lease

## Limitations of Capital Leases

Similar to a loan, company owns equipment and buys out lease at end of term.

### CONS:

- Higher Monthly Payments
- Long-term Commitment
- Responsible for Maintenance & Disposal
- Risk of Equipment Obsolescence
- Affects Company's Debt-to-Equity Ratio

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## CONSTRUCTION BUSINESS



# OPTIMIZE YOUR EQUIPMENT COST PER HOUR

## THE DOLLARS AND SENSE OF FAIR MARKET VALUE LEASES

BY NELSON ABELHA

Leasing provides an affordable way to update and upgrade business equipment, preserving cash for other needs. The choice between Fair Market Value (FMV) and capital leases can significantly impact operational efficiency and financial health. To make the best choice, it's crucial to understand leasing option advantages, particularly in terms of cost per hour.

### THE DIFFERENCE BETWEEN FMV LEASES AND CAPITAL LEASES

FMV leases are operating leases and the prevalent choice in the market today. With FMV leases, the lessee can use the equipment for a specific period, paying relatively lower monthly installments. At the end of the lease term, the lessee has the flexibility to return the equipment, purchase it at its fair market value, or extend the lease. This empowers businesses to align equipment usage with evolving needs, making FMV leases a practical and versatile option.

Capital leases, also known as finance leases, are more akin to a loan. The lessee essentially finances the equipment purchase, typically with higher monthly payments, and owns the equipment at the end of the lease term. With this type of lease, there are higher monthly payments when compared to an FMV lease, but at the end of the lease term, the lessee purchases the equipment for \$1. This is like an equipment loan and is ideal if you plan to keep the equipment for a long time, or when equipment obsolescence isn't a concern.

### COST PER HOUR ANALYSIS

Cost per hour is a crucial metric that measures the total cost of owning and operating equipment; it's calculated by dividing the total payments for the initial lease term by the number of hours the equipment is used.

FMV leases can provide several cost per hour advantages:

#### Lower monthly payments

Since FMV leases do not require the lessee to pay the full equipment cost over the lease term, the monthly financial burden is significantly reduced compared to capital leases. Lower payments mean better cash flow, allowing businesses to allocate funds to other critical areas, such as labour, materials, and project development.

#### Maintenance and repair costs

FMV leases often include maintenance and repair services as part of the lease agreement. This can equate to substantial savings in equipment operation cost per hour. With maintenance covered, businesses can dodge unexpected repair costs, reduce downtime, and ensure equipment is always in optimal working condition. In contrast, with a capital lease, the lessee is typically responsible for maintenance and repairs, which can be unpredictable and costly.

#### Technological advancements

Heavy construction equipment technology is constantly evolving. With an FMV lease, companies can upgrade to newer, more efficient models at the end of the lease term without the financial burden of owning outdated equipment. This ensures ongoing access to the latest technology, for greater productivity and reduced operational costs. Capital leases could lock companies into long-term ownership of equipment that may become obsolete, leading to higher costs due to less efficiency.

#### Flexibility and scalability

FMV leases offer greater flexibility compared to capital leases. Projects vary in scope and duration, and it's critical to adjust equipment needs accordingly. With FMV leases, companies can scale equipment fleets up or down based on project requirements without long-term ownership commitment. This ensures equipment costs align with actual usage, optimizing cost per hour.

**Tax advantages**

FMV leases can offer tax benefits not available with capital leases. Lease payments under an FMV lease are often fully deductible as business expenses, reducing taxable income which can provide significant tax savings, lowering overall equipment operation cost per hour. Capital leases typically allow for depreciation deductions, which may not be as advantageous depending on a company's tax scenario.

FMV leases offer several advantages over capital leases for heavy construction equipment, especially in cost per hour, making FMV leases an appealing option for construction companies seeking to improve their operations and financial well-being.

## TWO SCENARIOS: FMV AND CAPITAL LEASE OPTIONS

	FMV LEASE	CAPITAL LEASE
XYZ Construction Company is evaluating leasing options for a \$705,000 articulated dump truck (ADT).	XYZ opts for an FMV lease with a monthly payment of \$18,437.19 over two years. Maintenance and repairs are included in the lease. At the end of the term, XYZ can return the equipment and lease a new model.	Alternatively, XYZ could choose a capital lease with a monthly payment of \$31,177.70 over two years, and be responsible for all maintenance and repair costs, estimated at \$15,000 annually.
Top-Line Cost Analysis	<ul style="list-style-type: none"> <li>Total lease payments: \$18,437.19 x 24 months = \$442,492.56</li> <li>Maintenance and repair costs: \$0 (included)</li> <li>Total cost: \$442,492.56</li> </ul>	<ul style="list-style-type: none"> <li>Total lease payments: \$31,177.70 x 24 months = \$748,264.80</li> <li>Maintenance and repair costs: \$15,000 x 2 years = \$30,000</li> <li>Total cost: \$778,264.80</li> </ul>
Cost Per Hour Breakdown (if XYZ uses the excavator for 1,500 hours per year):	\$442,492.56 / (1,500 hours x 2 years) = \$147.50 cost per hour	\$778,264.80 / (1,500 hours x 2 years) = \$259.42 cost per hour

In this scenario, the FMV lease provides a significantly lower cost per hour – a savings of \$111.92 per hour – which would cover the costs of more than two unionized machine operators.

*"The choice between Fair Market Value (FMV) and capital leases can significantly impact operational efficiency and financial health."*

— NELSON ABELHA, Regional Vice President, First Financial Canadian Leasing

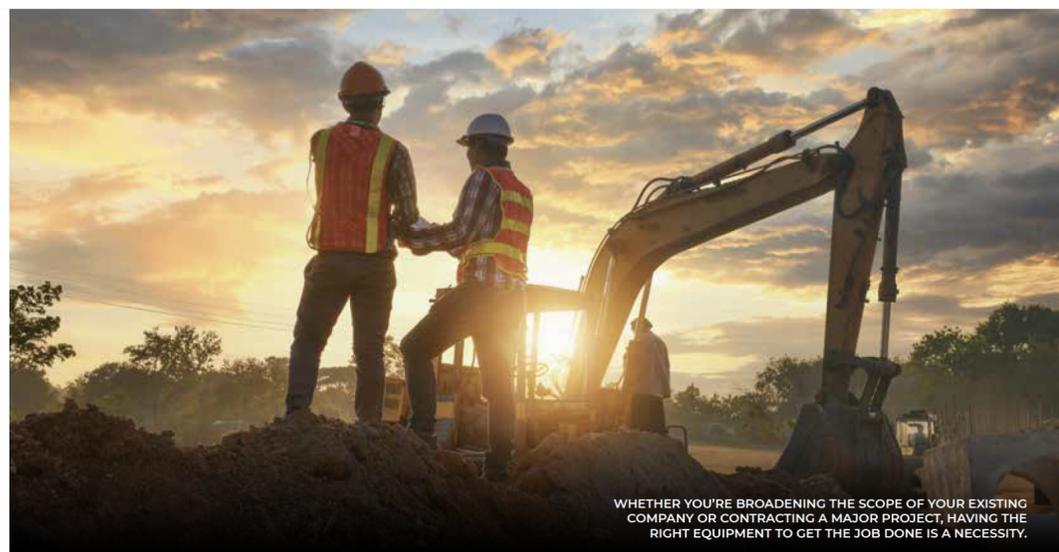
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### CONSTRUCTION BUSINESS



## REFACTOR YOUR CONSTRUCTION EQUIPMENT ACQUISITION PLAN IN AN ERA OF ECONOMIC UNCERTAINTY AND CONSTRAINED LENDING

BY NELSON ABELHA



WHETHER YOU'RE BROADENING THE SCOPE OF YOUR EXISTING COMPANY OR CONTRACTING A MAJOR PROJECT, HAVING THE RIGHT EQUIPMENT TO GET THE JOB DONE IS A NECESSITY.

## Refactor Your Construction Equipment Acquisition Plan in an Era of Economic Uncertainty and Constrained Lending

By Nelson Abelha

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