KEY FACTORS TO LOOK FOR WHEN LEASING A VEHICLE

You've decided to take the plunge: instead of buying a new car, you're going to lease one. But you're not familiar with the lingo or exactly how the process works. You're worried about making a costly mistake—or two or three.

Relax. Here are some tips from financial planners for what key factors to look for when leasing a vehicle.

Start with the sales price of the vehicle and ignore the advertised monthly payments. In leasing lingo, this is the "capitalized cost"—the price you agree to pay for the car. You can negotiate this price, just as you would if you were buying the car. Some leasing experts even recommend not mentioning you're interested in leasing until after you've negotiated the price. This price should, ideally, be significantly less than the manufacturer's suggested retail price—the MSRP sticker you see on the window. The lower the sales price, the lower the monthly payments.

The final lease price can be reduced by manufacturer rebates, deal incentives and trade-in credits. The price also will be determined by the size of the down payment (which is typically smaller than if you bought it), and the inclusion of some additional fees.

Once you've negotiated a lease price, the other major factor in determining whether the lease is really a good deal is the residual value. This is what the leasing company, not you, estimates the vehicle will be worth at the end of the lease—24, 36 or 48 months from now. If you bought the car, this would be its estimated resale value.

Typically, the residual value is stated as a percentage of the MSRP. Some experts say the best leases start with a residual value of 50 percent of MSRP for a 24-month lease. Naturally, the longer the lease period, the lower the residual value as the vehicle's value declines over time.

The higher the residual value, the lower the payments. That's because what primarily determines the monthly cost of a lease is the vehicle's sales price minus its residual value. You're not “renting” when you lease—you’re paying the cost of the depreciation of the vehicle. Other factors such as fees, mileage and the interest rate figure into the payments, but they’re rarely as critical as these two factors.

When settling on the residual value, be sure it’s a closed-end lease. That means that at the end of the lease, you can either buy the vehicle or walk away from it, regardless of its actual resale value at the time. With an open-end lease, you have to make up any difference should the estimated residual value turn out to be higher than the vehicle’s actual market value at the end of the lease.

Also be sure the lease includes “gap” insurance. Should the car be totaled, this covers any difference between the residual value at the time and the fair market value.

Another factor in determining whether a particular lease is a good deal is a murky term called the “money factor” or “lease factor.” This is the interest rate, though in leasing it’s expressed as a small decimal number. To calculate the equivalent interest rate, multiply the money factor by 2,400, regardless of the length of the lease. A money factor of 0.00208, for example, would equal five percent. The interest charge is rolled into the monthly payment.

Several other potentially expensive fees also can run up the cost of a lease. These include an administrative “acquisition” fee and a disposition fee, which pays for reselling the vehicle at the end of the lease (normally waived if you buy the vehicle at that time or lease a new one).

You’ll be charged an excess mileage fee should you drive more than the allotted miles on the lease. Typically, the break point is around 12,000 to 15,000 miles, but some manufacturers have reduced it to 10,000. Usually you pay a lower per-mile excess fee by paying for extra mileage upfront. At the end of the lease, you also may be charged for “excessive wear and tear”—a judgment you and the leasing company may not agree on. Leasing may mean higher costs for auto insurance and for maintaining the car according to a rigid schedule.

So shop around when leasing, just as you would as if you were buying a car.

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