



## **BODY OF KNOWLEDGE**

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Elements of large-ticket lease credit decision making

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Statement of Changes in Equity

Statement of Cash Flows

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- Current ratio
- Debt to equity ratio
- Return on equity ratio
- Net sales to inventory ratio
- Receivables turnover ratio
- Payables turnover ratio
- Net sales to working capital
- Profit on sales
- Inventory turnover
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Importance of understanding financial statements

- Sales process

- Credit process

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- When to obtain

- When relevant to the credit decision

## **LEASE LAW**

Basis for U.S. leasing law

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Legal definition of a lease

Rights associated with a lease

Warranties

- Express warranties

- Implied warranties

Article 2-A of the UCC code

- Requirements to comply

- Effects of meeting requirements

- Exclusion of warranties under Article 2-A

Exclusion of warranties under contract terms

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- After acquired title

- Novation

- “Jointly and severally liable”

- Terminal Rental Adjustment Clause (TRAC)

Bankruptcy

- Types of bankruptcy

- Chapter 7

- Chapter 9

- Chapter 11



Chapter 12

Chapter 13

Payment priorities in bankruptcy

Bankruptcy terminology

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Liquidation

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True lease treatment

Secured transaction treatment

Unsecured transaction treatment

Requirements for registration as a foreign corporations

Definition of "doing business"

Effects of non-registration

On lessor

On lessee

Requirements to meet tax obligations regardless of registration

Sales and use taxes

Property taxes

Income taxes

Venue of tax liability

## **LEASE DOCUMENTATION**

Parties to a contract

Elements of the lease documentation file

Lease documents

Lease contract

Schedules and exhibits

Delivery and Acceptance



- Guarantees
- Corporate resolutions
- Real estate waivers
- Fixture filings
- UCC filings
- Additional collateral agreements
- Purchase order
- Cross default agreement
- Invoice
- Funding/advance funding agreement
- Purchase options
- Other miscellaneous documents

#### Forms of contract

- Standard lease agreement
- Master lease agreement
- Plain language agreement

#### Elements & provisions of a lease contract

- Identification of the parties
- Identification of the vendor/supplier
- Equipment location
- Terms
- Purpose/intent of agreement
- Acceptance of equipment by lessee
- Disclaimer of warranties
- Article 2-A provisions
- Assignment
- Rental commencement and other payments
- Non-cancellation provisions
- Disclaimer of agency
- Lessee/Lessor signatures
- Choice of law/venue
- Security deposits
- Limited amendments, power of attorney
- Provisions for location and use of equipment
- Ownership provisions
- Renewal provisions
- Agreements for insurance, provisions for loss and/or damage
- Insurance requirements
- Responsibility for liens and tax liability regarding equipment
- Lessee indemnification of lessor
- Lessor assignment, waiver of defense clause
- Service charges, late fees, interest
- "Time of essence" provisions



- Default provisions
- Cross default clause
- Remedies to default
- Provisions regarding multiple lessees
- Agreement regarding enforcement expense
- Modifications, changes, severability
  - Attachments, schedules & exhibits

- Equipment lease guarantee
  - Purpose of the guarantee
  - Use in the lease transaction
  - Elements of the equipment lease guarantee
    - Parties to the guarantee
    - Guaranteeable interest
    - The guarantee made by the guarantor
    - Guarantor primarily responsible under the contract
    - Waiver of guarantor's rights

- Delivery & Acceptance
  - Purpose of the Delivery & Acceptance
  - Use of the Delivery & Acceptance
  - Elements of the Delivery & Acceptance
    - Acceptance and representations regarding equipment
    - Instructions to pay vendor
    - Unconditional nature of acceptance

- Corporate resolution
  - Purpose of the Corporate Resolution
  - Use of the Corporate Resolution
    - Resolution to lease
    - Resolution to guarantee lease
  - Elements of the Corporate Resolution
    - Authority of corporation to enter into lease and/or guarantee
    - Identification of authorized signers for the corporation

- Fixture Filings
  - Purpose of a Fixture Filing
  - Use of the Fixture Filing
  - Form used for Fixture Filings
  - Filing requirements
  - Protections offered from a fixture filing
    - Issues not protected

- Real Estate Waivers
  - Purpose of the Real Estate Waiver
  - Use of the Real Estate Waiver
  - Form of the Real Estate Waiver
    - Landlord Waiver





#### Lender's Waiver

Filing requirements for a Real Estate Waiver

Elements of the Real Estate Waiver

Identification of the parties

Legal description of the property

Statement of consideration

Intent and agreement on the nature of the "fixture" covered by the Real Estate Waiver

Waiver of certain rights by Landlord/Lender

Permission to reclaim "fixture" upon default by Lessee

Signature acknowledged by a Notary Public

#### UCC Filings

Purpose of UCC filings in the lease transaction

Form of the UCC filing

UCC-1

UCC-2

UCC-3

Filing requirements

Filing location

Timeliness

Fees

#### Additional Collateral Agreements

Parties to the agreement

Purpose of an additional collateral agreement

Use of the additional collateral agreement

Form for the agreement

Requirement to perfect interest

Real Estate as Additional Collateral

Forms of security

Deed of Trust

Mortgage

Assignment of interest

Requirements for filing, perfecting interest

Anti-Deficiency laws

#### Invoice

Parties to the invoice

Purpose of the invoice

Content of the invoice

Use of the invoice

Form of the invoice

#### Purchase Order

Parties to the purchase order

Purpose of the purchase order

Content of the purchase order



Representations required by vendor

Disclaimers and conditions set by lessor

Use of the purchase order

Form of the purchase order

Funding/advance funding agreement

Parties to the agreement

Purpose of the agreement

Use of the agreement

Contents of the agreement

Potential dangers of use

Purchase/renewal options

Parties to the option

Types of options

Purchase option

Call option

Put option

Renewal option

Use of the option

Form of the option

Potential effects of the option in the determination of the nature of the agreement

True lease treatment

Treatment as secured transaction

Lessor liability issues

Potential liabilities of lessor

As owner of the equipment

As financier of equipment

Liability protections for lessor

Contractual provisions

Insurance

Business practices

The issue of Agency

Equipment in inventory/repossessed equipment

Lessor's status in sale or lease

Sale to end-user

Wholesale disposal

Lessor liabilities

Possible lessor protections

Contractual

Insurance

## **COLLECTIONS**

Purpose of collections

Characteristics of a good collector



Signs of delinquency in a lease

Typical reasons for delinquency

- Overlooked due date

- Lease terms misunderstood

- Equipment problems

- Payment priorities

- Seasonal slow downs

- Catastrophic occurrences

- Internal accounting issues

- Personal financial difficulties

- Chronic slow pay

- Failing business

- Fraud

  - Types of fraud

  - Warning signs of fraud

  - Fraud prevention techniques

- Bankruptcy

Progression of a delinquency and lessor actions

- Initial contact

- Second and subsequent contacts

- Formal collections

- Repossession of equipment

  - Voluntary return by lessee

  - Ex Parte

  - Replevin action

  - Claim and delivery

- Litigation

  - Venue issues

  - Obtaining a judgment

    - Registration of foreign judgment

  - Action for fraud

  - Litigation in bankruptcy

    - Fraud action

- Course of action on a stated "no-pay"

  - Written records

    - Importance

    - Use

      - Court evidence

      - History of account

      - Management tool

- Possible collection remedies

  - Partial payments

  - Extensions



- Changes in due dates
- Recovery agreements
- Forbearance program
- Modifications
- Transfer and assumption
- Other reasonable remedies
- Alternative ways to make lessee contact
- Types of repossession
  - Voluntary return by lessee
  - Court orders and enforced repossession
  - Self-help repossession
    - Potential dangers to lessor
- Commercially reasonable sale
  - Elements of a commercially reasonable sale
    - Notice
    - Timing issues
    - Advertisement
    - Who may purchase at sale
    - Application of sale proceeds
    - Lessor rights to recover deficiency

## **FINANCIAL & TAX ACCOUNTING FOR LEASES**

### Definitions

- Fair market value
- Fair rental value
- Bargain purchase option
- Bargain renewal option
- Economic life
- Estimated residual value
- Unguaranteed residual value
- Lease Term
- Non-cancelable lease
- Minimum lease payments receivable
- Lessor's implicit rate
  - Calculation of lessor's implicit rate
- Lessee's incremental borrowing rate
- Initial direct costs (IDC)
- Contingent rentals
- Accrual basis accounting
- Cash basis accounting
- Aging the receivables/payables
- Non-performing account
- Reserves



Amortization

Cash flow

Appreciation

Depreciation

    Depreciation methods

        Straight line

        Double declining balance

        150% declining balance

        Sum of the years

        MACRS

    Book Depreciation

    Tax Depreciation

        Part year conventions

Inventory valuation methods

    LIFO

    FIFO

    Average Cost

Liquidate

Negative cash flow

Working capital

Capitalized cost

Compensating balance

Tax accounting methods

Book accounting methods

Sales and use taxes

    Lessor liability

    Reporting requirements

    Payment options

    Liability on residual sale

    Liability on assignment or lease by lessor

Personal Property Taxes

    Assessment process

    Lessor liability for personal property taxes

Historic view of FASB 13

Provisions of FASB 13

Historic view of IRS Revenue Ruling 54-540 and Revenue Procedure 75-21

Provisions of Revenue Ruling 55-540

Provisions of Revenue Procedure 75-21

Book accounting for a capital lease

    Determination of accounting treatment through FASB 13 rules

        Calculation of "90%" rule

            Lessor's treatment using lessor's implicit rate

            Lessee's treatment using incremental borrowing rate



Entering the capital lease on the lessor's balance sheet

Entering the payments received from the lessee on a capital lease on the lessor's balance sheet and operating statement

Entering the capital lease on the lessee's balance sheet

Entering the payments paid by the lessee on the lessee's balance sheet and operating statement

Tax accounting for a non-tax (capital) lease

Determination of tax treatment through Revenue Ruling 55-540 and, as applicable, Revenue Procedure 75-21

Entering the non-tax lease on the tax books of the lessor

Entering the payments received from the lessee on the tax books of the lessor

Entering the non-tax lease on the tax books of the lessee

Entering the payments paid by the lessee on the tax books of the lessee

Book accounting for an operating lease

Determination of accounting treatment through FASB 13 rules

Calculation of "90%" rule

Lessor's treatment using lessor's implicit rate

Lessee's treatment using incremental borrowing rate

Entering the operating lease on the lessor's balance sheet

Entering the payments received on an operating lease on the lessor's balance sheet and operating statement

Entering the operating lease on the lessee's balance sheet

Entering the payments paid by the lessee on the lessee's balance sheet and operating statement

Tax accounting for a tax (operating) lease

Determination of tax treatment through Revenue Ruling 55-540 and, as applicable, Revenue Procedure 75-21

Entering the tax lease on the tax books of the lessor

Entering the payments received from the lessee on the tax books of the lessor

Entering the tax lease on the tax books of the lessee

Entering the payments paid by the lessee on the tax books of the lessee

Reasons for differences in treatment of a lease between book and tax

Accounting treatment

Different rules between tax and book

Accounting methods

Accrual vs. Cash

Difference in book accounting treatment between lessee and lessor

Lessor's implicit rate vs. lessee's incremental borrowing rate

## **SOURCES OF FINANCING FOR A LEASING COMPANY**

Sources Include

Bank and/or Financial Institution

Finance Company

Private Loans

Other Lease Companies

Pension Funds

Insurance Companies

Common Funding Methods



Internal Funding

Brokerage

Discounting

Definition of "discounting"

Elements of the discount transaction

Mathematical calculations for the discount transaction

Timing adjustments

Economics of the discount transaction

Effects of discounts, holdbacks, or other reserves

Lease Packaging

Lease package defined

Elements of a lease package

Who determines the content

Who determines the structure

The package "narrative"

The package "request"

Financial data analysis as part of the lease package

Tailoring the package to the requirements of the funder

Equity and Debt

Sale of company interest

Common stock

Preferred stock

Issues of company control

Shareholder issues

Securities law compliance

Cost of funds

Private Investors

Transactional sales

Portfolio Sales

Determination of price and terms

Possible effects on remaining portfolio

Marketing considerations

Public Debt Offering

Corporate bonds

Other debt instruments

Securities law compliance

Limited partnerships/trusts

Asset Securitization

Nature of the securitization transaction

Asset backed financing

Structure of the securitization transaction

Pay through structure

Pass through structure



#### Parties to a securitization and their respective roles

- Lessee
- Lessor
- Attorney
- Outside auditors
- Rating agencies
- Outside servicer
- Appraiser
- Investment Bankers
- Trustee
- Investor
  - Institutional
  - Individual

#### Lessor motivations and benefits in a securitization

Potential lessor problems in a securitization

Servicing obligations

Tax considerations

- Sale vs. loan treatment of the transaction

- Book treatment

- Tax treatment

- Personal property tax considerations

- Sales and use tax considerations

Recourse vs. non-recourse structure/UNL

Credit enhancements

Economics of the securitization to the lessor

- Cost of funds

- Transactional costs

Securitization strategies for the lessor

- Short term benefits and detriments

- Long term benefits and detriments

Securities law compliance and liability

## **LEASE PRICING**

Time use of money concept

Cash flow diagrams

Structuring of a payment

- Principal plus interest

- Amortizing payment

Basic elements of a lease transaction

- Term

- Number of payments/Number of advance payments

- Equipment cost

- Indirect costs





- Lease payment
- Residual value
- Security Deposit
- Lessor's yield
- Other fees/costs

#### Understanding the transaction

- Application of the cash flow diagram to the lease transaction

#### Mathematical computation for a lease transaction

- Solving for any unknown element in the transaction
- Determining the rate factor for a lease transaction
- Computing unusual payment structures
  - Skip payments
  - Step payments
  - Hi-low payments
  - Seasonal payments

#### Definitions of terms

- Internal rate of return
- Stream rate
- Basis points
- Points

## **MARKETING\***

Potential market for leasing in today's economy

Development of a marketing plan

Elements of a marketing plan

- Choosing business type
- Choosing industry type
- Choosing equipment type
- Choosing a geographic area
- Defining the customer
- Identifying sources of funds
- Identifying available programs
- Limitations
- Product availability
- Marketing strategies

## **SALES\***

Definition of sales effort

Purpose of sales within the lease organization

Elements of the sales process

- Introduction
- Body



Close

Overcoming objections

Pre-emptive principle

Using questions to determine the real objection

Closing the deal

Closing techniques

The sales proposal

Defining the contents of the sales proposal

The salesman's main tool – knowledge

Financial statements

Credit requirements and criteria

Credit reporting and credit report data

Tax returns

Business structure and operation

Lease pricing

Lease structuring

## **LEASE VS. BUY DECISION MAKING\***

Selling the lease vs. buy decision

Knowledge of customer

Motivations

Concerns

Intended use of equipment

Personality

Company decision making process

Financial situation/Tax situation

Knowledge of Product (leasing)

Rates, yields, time use of money

Financial statement impacts of leasing

Tax impacts of leasing

Convenience considerations

Other implication of using leasing

Options for acquisition/use of equipment by lessee

Elements of the lease vs. buy decision

Equipment considerations

Budget and decision making

Conveniences

Financial statement impacts

Tax consequences

Cash flow issues

Costs



## **LEASE COMPANY MANAGEMENT\***

Structure/organization of a lease company

Key management

    Role of key management

Management Issues

    Administration

        Organizational structure

        Human resource issues

        Efficiency

    Financial Management

        Budgeting

        Cash flow

        Financial Statements

        Profitability

        Cost of Capital

        Reserves

        Managing Cash flows

    Credit Decision Making

        Impact on debt/financing

        Establishing company policy and criteria

        Impact on marketing efforts

        Impact on portfolio composition and performance

        Impact on profitability

        Timing issues

        Lessor servicing

        Third-party contract servicing

        Personal property tax issues

        Sales tax reporting

        Internal systems and reporting issues

## **PORTFOLIO MANAGEMENT\***

Issues related to portfolio management

    Portfolio quality

    Residual realization

    Financial statement integrity

    Maintenance of financial relationships

    Competition

    Insurance issues

    Personal property tax exposure

    Marketing and sales efforts and requirements

    Quality of accounting data

    Recourse exposure



- Delinquencies
- Concentrations
- Asset management and disposition
- Profitability
- Projections for the future
- Analysis of the lease portfolio
  - Weighted averages
    - Computing weighted averages
  - Determining the portfolio yield
    - Weighted average yield
  - Determining the portfolio term
    - Weighted average term
    - Ramifications of portfolio term on portfolio management and lease company management issues
  - Analysis of portfolio aging
  - Residual valuations
    - Tracking actual residual realizations
  - Loss reserves
    - Methods for determining loss reserves
  - Portfolio concentrations
    - Types of concentrations
    - How concentrations may occur
    - How concentrations may be avoided

## **GOVERNMENT LEASING\***

### Definition of "government"

- Municipal
- Federal
- Quasi-Federal
- Prime Contractors
- Indian tribes and nations
- Not-for-profit entities
- Public and private activities

### Municipal government lease documentation

- Form of lease agreement
- Bank qualification letter
- Legal opinion
- Proof of authority
- U.S. form 8038G or 8038GC
- UCC-1
- Statement of essential use
- Acceptance certificate
- Insurance documentation
- Delivery and Acceptance



- Other miscellaneous documentation
- Federal Government lease documentation
  - Purchase order
    - Addendum to purchase order
  - Inspection, receiving & acceptance report/certificate
  - Vendor documentation
- Special terms and conditions in government leases
  - Non-appropriations clause
  - Non-Substitution clause
  - Termination at the convenience of the government
  - Base closure clause
  - Contract termination clause
- Benefits of government leasing
  - Tax benefits
    - Municipal
    - Indian tribes and nations
    - Federal Government

## **INSURANCE FOR LEASING COMPANIES\***

- Definition of Insurance
- Understanding Insurance Contracts
  - Legal Purpose
  - Legal Capacity of the Parties to a Contract
  - Genuine Assent
- Types of Insurance
  - Business Owner Policy (BOP)
  - Key Man Insurance
  - Fleet Insurance
  - Garage Liability
  - Residual Value Insurance
- Rating Agencies
- Functions of Insurance
  - Spread of Risk
  - Basis of Credit System
  - Eliminates Worry and Encourages Entrepreneurship
  - Loss Prevention and Loss Reduction
  - Source of Employment and Investment Capital
- Risk Assessment
  - Retention of Risk



## **AGRICULTURE LEASING\***

Agricultural Entities

- Company Structures

- Types of Entities

Types of Equipment that can be leased

Forms of Agriculture

- Growing crops

- Dairy production

- Forestry

- Animal husbandry

- Viticulture

- Ornamental crops (horticulture)

- Raising of fish and shellfish

- Raising of fowl

Areas of commerce within Agriculture

- Growing

- Distribution

- Marketing

- Processing

Special types of Agricultural finance

Public Programs available to US farmers

Agricultural insurance

- Programs

- Types

Special Agricultural lease pricing

- Payments

- Periodicity

- Seasonality

Equipment

Transaction Structures

Lending to Agricultural Businesses

## **ADVANCED PRICING AND STRUCTURING\***

Definitions of true leases

- IRS rulings & procedures

Issues affecting lease pricing

- Tax Depreciation

- Term

- Residuals

- Lessor's yield

- MACRS

- Lessor's tax rate



- Sinking fund rate
- Tax lease pricing methods
- Purchase Option considerations
  - Appraisal definitions
    - Fair Market Value
    - Orderly Liquidation Value
    - Forced Liquidation Value
  - Stipulated Loss Value
  - Bargain Purchase Option