

1. FAS 13 (Lessee/Lessor Information Split), **NOT** Fair Value/FAS 159
2. **Operating** Lease (Not meet any of the above criteria)
 - a. Lessor – Own assets, Rent to Lessee (Asset on B/S and Depreciate)
 - b. Lessee - Rent Expense (**No Interest!**)
3. **Issues with Operating Lease**
 - a. Free Rent/Uneven Payment
 - i. Total Lease Payable/Receivable over Lease Term = Revenue/Expense Even for All Years

Cash (Cash per Year)

Rent Receivable (Plug)

Rent Revenue (Amortized Portion)

- b. Initial Direct Costs (FAS 91)
 - i. Fees to Set Up Lease (FF, Appraisal, Document Processing, Registration, Closing)
 - ii. Lessor Pays (Capitalize/Amortize over Life of Lease)
 - c. Lease Bonus
 - i. Lessee pays nonrefundable lease bonus fee to obtain more favorable terms
 - ii. Lessor: Unearned Rent (Amortize over Lease Term)
 - iii. Lessee: Prepaid Rent (Amortize over Lease Term)
 - d. Security Deposits
 - i. Refundable (Liability for Lessor and Receivable for Lessee)
 - e. Leasehold Improvements
 - i. Capitalize and Amortize over Shorter (Lease Term Remaining or UL of Improvement)
 - ii. IF... improvement is in lieu of rent (Expense)
 - f. **Disclosure**
 - i. Payments due in Next Five Years
 - ii. Amount Due in Aggregate
4. **Capitalizing** Lease
 - a. Elements
 - i. Transfer Title
 - ii. BPO
 - iii. Lease Term \geq 75% of UL
 - iv. PVMLP \geq 90% FMV (Reduced by Tax Credit)
 - v. #C/D not executed if within **last** 25% of asset life (sold old assets can be rented out without capitalizing)
 - b. **Lessor**
 - i. **Direct Financing Lease** (Leasing Company/Bank Purchase Asset and Lease to Consumer)
 1. MLP = Rent Payments, BPO, Guaranteed Residual Value, Penalty for Failure to Renew

2. Guaranteed = Add to MLP to arrive at Lease Receivable
3. Unguaranteed – Add to Lease Receivable

Lessor (Bank) Receives Title

Asset to Be Leased (FMV)
Cash

Inception of Lease

Lease Receivable (total payments, gross)
Asset to be Leased (reverse)
Unearned Interest Revenue (plug for interest to be earned)

Amortization

BOY CV
Minus Discount (PMT - Interest)
Boy 2 CV

Disclosure

Current Portion (Discount)
Noncurrent Portion (Residual CV)

Lease Payment

Cash (PMT)
Lease Receivable
Unearned Interest Revenue
Interest Revenue (interest)

Guaranteed Residual (\$\$ Left if Residual Exists)

Cash (If Asset Worth Less)
Residual Value of Equipment
Lease Receivable

- ii. **Sales Type Lease** (MFCR Lease Item, Gross Profit and Int Revenue Earned over Lease Period)
 1. Lease Payment = Sales Price = PVMLP
 2. COGS is Historical Cost/CV – PV of Unguaranteed Residual
 3. Guaranteed Residual = Part of Revenue (Only by LESSEE)
 4. Unguaranteed Residual Excluded from COGS and Sales

SIMILAR JOURNAL ENTRY TO DIRECT FINANCING: Just change Asset (cost) to Sales (PVMLP).

Lease Receivable (Gross) (total MLP)
Sales (PVMLP)
Unearned Interest Revenue (PLUG)

COGS

Inventory

*If Unguaranteed Residual... net these entries

c. **Lessee**

- i. Lease Payment and Reduction of Liability
- ii. Depreciation of Leased Asset
 1. If Title Transfer or BPO (UL = Term)
 2. Or else... Lease Term
- iii. Use LOWEST Interest Rate

Inception

Leased Asset (PV MLP)

Lease Obligation

Payment

Lease Obligation (PLUG)

Interest Expense (CV * IR)

Cash (PMT)

Depreciation Expense

Accumulated Depreciation

d. **Sales-Lease Backs** (Owner Sells Property, Immediately Leases Back)

- i. $\geq 90\%$ or more of FMV

Cash (Selling Price)

Asset (Sold Asset)

Deferred Gain (Plug) Asset Valuation Allowance

Leased Asset (PV of Lease PMTS)

Leased Obligation

Disclosure: Leased Asset - Deferred Gain

EOY

Deferred Gain (Reverse)

Depreciation Expense (Reversed, to Indirectly Increase NI)

- ii. $\leq 10\%$ (Recognize Full Gain)

- iii. $10\% < X < 90\%$

Cash (SP)

Asset (CV)

Deferred Gain (PV of Rental PMTS)

Gain (PLUG)

MISC: Taxes = Expensed as we Go, Real Economic Loss = CV - FV ... Immediate,
Artificial Loss = SP < CV (FV > CV)... Deferred. Capital Lease to Operating Lease =
Sales Lease Back