

Leasing and Structured Finance Services

Across a wide range of industry sectors, from manufacturing to health care, leasing has become a vital tool for the financing of facilities, machinery, equipment and real estate. To successfully negotiate a lease that meets both fiscal and financial reporting requirements, both domestically and across borders, transaction parties require accurate and supportable determinations of the value and economic life, together with a thorough commercial understanding of the options available in the leasing market.

In recent years the introduction of International Financial Reporting Standards, together with changes in the tax treatment of leases have resulted in many changes in the leasing sector.

German Accounting Guidance

As there is no specific regulation in Commercial Law (HGB) dealing with leases, in practice, most companies use the tax rules as the basis of their accounting. Complex definitions within tax law to distinguish between operating and finance leases are applied both in financial accounting and in the drafting of lease agreements.

Due to unfavorable tax treatment for a lessee, as depreciation generally remains with the lessor, relatively few leased assets are capitalized by lessees.

Within the German accounting treatment, a lease is considered to be a full amortization contract when the following three criteria are met:

- a lease contract is for a basic lease term (fixed contractual lease period)
- during this term the lease is non cancellable
- the present value of lease payments equal or exceed lessor's acquisition or manufacturing costs (including all direct expenses and finance costs)

Leases are classified as partial amortization contracts if the costs of the lessor are not fully covered by the lease payments over the period of the basic lease term.



**American
Appraisal**



International Financial Reporting Standards Guidance

IAS 17 requires all leases to be classified as either operating leases or finance leases.

- Operating leases are treated as fixed assets on the lessor's balance sheet, and not accounted for on the lessee's
- Finance leases are treated as assets on the lessee's balance sheet and as receivables by the lessors

The lease classification process is time consuming and can require some difficult judgments, leading to inconsistent application of IAS17.

Lessees must recognize any profits on asset disposal under sale and leaseback transactions, over the term of the lease.

However, the current discussion between the FASB and the IASB may change the treatment of leases and the related liabilities significantly.

US Financial Accounting Standards Guidance

Under FASB 13, a lease shall be classified as a capital lease by the lessee if the lease meets one or more of the following criteria:

- The lease transfers ownership of the property to the lessee by the end of the lease term
- The lease contains a bargain purchase option

- The lease term is equal to 75% or more of the estimated economic life of the leased property
- The present value of the rents equals or exceeds 90% of the fair value of the leased property

How American Appraisal can assist you

American Appraisal is the leading worldwide independent valuation firm. Our global network enables us to advise global players, leading medium-sized businesses and strongly growing technology companies in a professional way. As a firm we have a wealth of experience, both in Central Europe and internationally, assisting both lessees and lessors to meet their obligations for both domestic and cross-border transactions.

We assist our clients by providing:

- Support in Structuring Leasing Transactions
- Lease inception appraisals
- End of lease appraisals
- Residual value forecasts
- Useful economic life assessments
- Liquidation value appraisals
- Assessment of related lease obligations including balance sheet classification, cost and possible economic enhancements
- Assistance with lease portfolio management, including development of management and tracking systems for analysis, reporting and audit compliance



American Appraisal
Bockenheimer Landstr. 22
60323 Frankfurt am Main / Germany
Tel: +49-69-719184-0 / Fax: +49-69-719184-44
Website: www.american-appraisal.de