



Equipment Leasing Terms

This Glossary of Equipment Leasing Terms will help you understand the "Leasing Language" so when you are ready to acquire equipment you can make an educated decision.

Accelerated Depreciation:

Refers to any one of several methods by which a company, for financial accounting and/or tax purposes, depreciates a fixed asset in such a way that the amount of depreciation taken each year is higher during the earlier years of an asset's life.

Add-On:

A transaction that adds related equipment to an existing lease. Typically, this term is used when the new equipment is financed using the same lease structure (i.e., Fair Market Value, \$1.00 Purchase Option, Fixed Purchase Option, etc.) as was used in the underlying transaction except that the lease term for the add-on is set so that it expires coterminously with the original transaction.

Advance Rental Payments:

The payments made from the lessee to the lessor at the inception of the lease transaction. Typically, first and last months rent.

Application:

The lease application form used to obtain credit information needed to evaluate a prospective lessee's credit worthiness and history.

Application Only:

One page application used to acquire equipment, based solely on your credit score.

Alternative Minimum Tax (AMT):

Introduced by the Tax Reform Act of 1969 as a system for taxing individuals and corporations that in effect prevents taxpayers from otherwise reducing their tax below a certain level.

Amortization:

A breakdown of periodic loan payments into two components; the principle portion and the interest portion.

Annual Percentage Rate (APR):

An expression of the effective interest rate the borrower will pay on a loan, taking into account one-time fees and standardizing the way the rate is expressed. In other words the APR is the total cost of credit to the consumer, expressed as an annual percentage of the amount of credit granted.

Bargain Purchase Option:

A lease provision which allows the lessee, at its option, to purchase the equipment being leased for a price predetermined at the lease inception which is substantially lower than the expected fair market value at the date the option can be exercised.

Big Ticket (Large Ticket):

A market segment, where the equipment financed is over \$5 million.

Broker or Intermediary:

A person or entity who, for compensation, arranges lease transactions between lessees and lessors of an asset. A broker is also referred to as a syndicator. Some banks are actually syndicating leases.

Capital Lease (Finance Lease):

Type of lease classified and accounted for by a lessee as a purchase and by the lessor as a sale or financing, if it meets any one of the following criteria: (1) the lessor transfers ownership to the lessee at the end of the lease term; (2) the lease contains an option to purchase the asset at a bargain price; (3) the lease term is equal to 75 percent or more of the estimated economic life of the property or (4) the present value of minimum lease rental payment is equal to 90 percent or more of the fair market value of the leased asset less related investment tax credits retained by the lessor.

Capped Fair Market Value:

A Fair Market Value Lease with a predetermined ceiling to limit fair market exposure at the end of the lease term.

Captive Leasing Company:

A subsidiary leasing division of a dealer or manufacturer.

Conditional Sales Agreement (CSA):

A contract that provides for installment financing of an asset. The Lessee is treated as the owner of the equipment for tax and accounting purposes. The Lessor has a first priority security interest in the equipment. CSA's are also known as Money over Money, Dollar Buy or Lease Intended as Security transactions.

Contract Financing:

A unique solution we offer vendors and manufacturers who have a client that services investment grade end users.

Coterminous:

A term used when two or more leases of equipment are linked so that both will terminate at the same time.

Covenant:

A clause in a contract, usually required by the lessor, that either requires the lessee to do a certain thing or refrain from doing a certain thing.

Default:

In a lease transaction, when a party breaches certain material lease obligations. After the event of default, the lease company may exercise all its rights and remedies under its lease contract or other agreements to repossess the equipment and seek damages.

Depreciation:

A reasonable allowance for exhaustion, wear and tear, and obsolescence of equipment used by a business. As a periodic item of expense, it allows the owner of the equipment to recover the cost of the equipment over its economic life.

Delivery and Acceptance Certificate:

A document in which a lessee acknowledges that certain specified equipment is acceptable for lease. Usually used in transactions where the parties enter into the lease document well in advance of the equipment's delivery date. It serves to notify the lessor that the equipment has been delivered, inspected and accepted for lease as of a specified date.

Discount Rate:

A certain interest rate that is used to bring a series of future cash flows to their present value in order to state them in today's dollars.

Documentation Fee:

A fee charged for preparing, distributing and storing transaction documents in any finance transaction.

Dollar Buy Out:

The same as a dollar-out lease. Assuming that the lessee is not in default, an option at the end of the lease to buy the leased equipment for \$1.00

Economic Life:

The period of time during which an asset will have economic value and be usable.

Estimated Useful Life:

The period during which an asset is expected to be useful in trade and business.

Equipment Finance Agreement (EFA):

Basically a loan against the equipment, offering you a fixed monthly payment that does not change monthly with the Prime Rate your bank lends against. You will own the equipment and the investor will release the security interest at the end of the finance term.

Equipment Schedule:

A document that describes in detail the equipment being leased; to include the commencement date, lease terms, repayment schedule and location of the equipment.

Fair Market Purchase Option:

An option to purchase leased property at the end of the lease term at its then fair market value.

Fair Market Value (FMV):

The price for which property can be sold in an "arms length" transaction. The parties must be informed, unrelated and willing, each of which is acting rationally and in its own best interest based on the assumption that the equipment or other capital asset is in a known or required condition.

Fair Market Value Lease:

A lease which includes an option for the lessee to either renew the lease at a Fair Market Value renewal or purchase the equipment for its Fair Market Value at the end of the lease term. Though often referred to as Tax Leases, not all Fair Market Value Leases qualify as Tax Leases.

FASB (The Financial Accounting Standards Board):

Sets accounting rules in the United States, subject to certain oversight by federal governmental agencies.

FASB 13:

Financial Accounting Standards No. 13 of the Financial Accounting Standards Board, which establishes standards for lessees' and lessors' accounting and reporting for leases. FASB 13 includes the characterization of a lease as an operating lease or capital lease for the lessee's purposes. A company's assets, liabilities and net income will differ depending on how it chooses to structure its leases. The provisions of FASB 13 derive from the view that a lease that transfers substantially all of the benefits and risks of ownership should be accounted for as the acquisition of an asset and the incurrence of an obligation by the lessee (capital lease) and as a sale or financing by the lessor. Other leases should be accounted for as the rental of property (operating leases).

Finance Lease (Capital Lease):

The same as a Full Payout Lease. A lease used to finance the purchase of equipment, not a true lease. The lessee is responsible for the total cost of the equipment including maintenance, taxes and insurance. Finance Leases are generally considered to be capital leases from an accounting stand point and non-tax leases from a tax stand point.

First Amendment Lease:

Provides you a purchase option at one or more defined points in time with the requirement that you renew or continue the lease if the purchase option is not exercised. The 'option rule' is usually either a fixed price intended to approximate the fair market value or is defined as fair market value by appraisal and subject to a minimum price to insure that the lessors residual position will be covered if the purchase option is exercised. If the purchase option is not exercised then the lease is automatically renewed for a fixed term (typically 12-24 months) at a fixed rental intended to approximate fair rental value, which will further reduce the lessors end of term residual position. You are not permitted to return the equipment on the option exercise date. If the lease is automatically renewed, then at the expiration of that initial renewal term, you will typically have the right to return the equipment without penalty, renew or purchase at fair market value.

Fixed Priced Purchase Option:

An option given to the lessee to purchase leased equipment from the lessor on the option date for a certain price. Both the date and price must be determined at the inception of the lease. A fixed price purchase option could equal as little as 10-15 percent of the original cost of the equipment.

GAAP:

Generally Accepted Accounting Principles.

Guaranteed Residual Value:

An arrangement in which, for example, a manufacturer guarantees that a lessor will receive not less than a certain amount for specified equipment when it is disposed of at the end of the lease term.

Guarantor:

One who guarantees a debt or lease obligation of another person or entity.

Hell-or-High-Water Clause:

A lease provision that commits a lessee to pay the rent unconditionally. The lessee waives any right that exists or may arise to withhold any rent from the lessor or any assignee of the lessor for any reason what so ever, including any setoff, counterclaim, recoupment, or defense.

Large Corporations:

Corporations with Annual Revenues of \$500+ Million.

Lease Agreement (Lease):

A contract in which an equipment owner, the lessor, transfers the equipment's use, subject to the specified terms and conditions, to another, the lessee, for a prescribed period of time and rental rate.

Lease Line:

A pre-approved amount of debt or funds that a lessor will allow to a lessee.

Lease Purchase:

Full payout, net leases structured with a term equal to the equipment's estimated useful life. Because many Lease Purchases included a Bargain Purchase Option for the lessee to purchase the equipment for one dollar at the expiration of the lease, these leases are often referred to as dollar buyout or 'buck-out leases'. Lease Purchases are generally considered to be Capital Leases from an accounting perspective due to their bargain purchase option and length of lease term.

Lease Payment (Lease Rate):

The periodic payment made during the lease term. Usually paid each month, but may be paid quarterly, to the lessor.

Lease Schedule:

A schedule to a Master Lease agreement describing the leased equipment, rentals and other terms applicable to the equipment.

Lease Term:

The fixed term of the lease in months.

Lease Underwriting:

The process in which a lease broker arranges a lease transaction for the account of third parties, a prospective lessor and a prospective lessee. Typically, on a best efforts basis.

Lessee:

The user of the equipment that is the subject of a lease agreement.

Lessor:

The company that buys the equipment then rents it back to you.

Leveraged Lease:

A lease in which a portion, generally 60-80%, of equipment acquisition cost is borrowed from a bank or other lending institution, with the lessor paying the balance. The debt is commonly on a non-recourse basis, and the rental payments are usually sufficient to cover the loan debt service.

Master Lease:

A lease agreement designed to permit future equipment not contemplated when the lease is executed to be added to the lease later. The document is set up in two parts. The main body contains the general, or boiler plate provisions, such as the maintenance and indemnification provisions. An annex, or schedule, contains the type of items that usually vary with a transaction, such as rental rates and options.

Middle Market:

A market segment usually represented by financing amounts of \$500,000 to \$30 million.

Middle Market Companies:

Companies with annual revenues of \$25 Million to \$500 Million.

Modified Accelerated Cost Recovery System (MACRS):

The Tax Reform Act of 1986, established a modified accelerated cost recovery system, called MACRS. It is a tax depreciation system that allows a business to recover the cost of income producing equipment over a specific recovery period. The Tax Act established an accelerated system of allowing a business to take deductions faster than in equal amounts over a period of years usually 3, 5, 7, 10, 15 or 20 years.

Municipal Lease:

A lease designed to meet the special needs of state and local governments. The lease contains a non-appropriation clause which states that the only condition under which the entity may be released from its payment obligation, the lease, is when the legislature of funding authority fails to appropriate funds. Since the lessee is a municipality or an organization supporting the government, it is exempt from paying federal income taxes. Thus, the IRS doesn't charge the lessor income taxes on this type of lease.

Municipality:

A general-purpose district typically governed by a mayor, city council or municipal council. Cities, Towns, Townships & Villages...

Net Lease:

A lease agreement in which the lessee is responsible for paying all costs. Such as maintenance, certain taxes, and insurance, related to using the lease equipment, in addition to the rental payments. Typically, Finance Leases are Net Leases.

Off Balance Sheet Financing:

Financing that does not appear on the balance sheets of a lessee as a liability or asset, due to the application of FASB 13, rather the cost of the lease is treated as an expense.

Operating Lease (True Lease):

A lease which is treated as a True Lease, as opposed to a loan for accounting purposes. As defined within FASB 13, an operating lease meet all of the following criteria: (1) lease term is less than 75% of estimated economic life of the equipment, (2) Present value of lease payments is less than 90% of the equipments fair market value, (3) lease cannot contain a bargain purchase option, (4) ownership is retained by the lessor during and after the lease term. The operating lease is accounted for by the lessee without showing the asset or liability on his balance sheet. The lease payments are accounted for by the lessee as an operating expense.

Pre-Funding:

Some vendors require they be paid at least 50% of the invoice cost before proving the equipment to the lessee.

Primary Lease Term:

The same as base lease term.

Progress Payments:

Payments that may be required by an equipment manufacturer or builder during the construction period toward the purchase price. Typically required for costly equipment with a long construction

period, the payments are designed to lessen the manufactures or builders need to tie up their own working capital during construction.

Purchase Option:

The right to buy agreed upon equipment at the times and the amounts specified in the option. Usually these options are only exercisable at the end of the primary lease term, although they sometimes can be exercised during the primary lease term or at the end of any renewal term.

PUT Option:

A right that a lessor may have to sell specified leased equipment to the lessee at a fixed price at the end of the initial lease term.

Renewal Option:

An option to a lessee to renew the lease term for a specified rental time and period.

Residual Value:

The value of the leased equipment at the end of the lease term.

Sale Lease-Back:

An arrangement in which an equipment buyer buys equipment for the purpose of leasing it back to the seller.

Skip Payment Lease:

A lease that contains a payment stream requiring the lessee to make payments only during certain periods of the year. Great for seasonal construction companies.

Step Up/Down Payments:

Lease payments that change during the lease term, usually from lower payments in the beginning of the lease to higher payments during the later part of the lease.

Tax Exempt Entity:

Generally, any local, state or federal government that is exempt from paying sales tax.

Tax Lease (Operating or True Lease):

An arrangement that qualifies for lease treatment for federal income tax purposes. Under a true lease, the lessee may deduct rental payments and the lessor may claim the tax benefits accruing to an equipment owner.

TRAC Lease:

A lease of motor vehicles or trailers that contains what is referred to as a Terminal Rental Adjustment Clause (TRAC). The clause permits or requires the rent amount be adjusted based on the proceeds the lessor receives from the sale of the leased equipment. TRAC Leases qualify as true leases.

Uniform Commercial Code (UCC):

A standardized program and method of administering, legalizing and recording lien instruments for equipment leases.

Upgrade:

To trade in leased equipment for a newer, more advanced piece during the lease term.

Use Tax:

Several states charge a 'use tax' in lieu of a sales tax when equipment is leased.

Useful Life:

Typically the economic usable life of an asset.

Vendor:

The seller of property. Usually the manufacturer or distributor of equipment.

Vendor Program:

A program in which an equipment lessor provides a lease financing service to customers of an equipment manufacturer.

Venture Leases:

A lease finance solution for start-up businesses backed by a venture capital company.