



## Leasing from an Accounting Perspective

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Financial reporting is strictly defined by rules of the Financial Accounting Standards Board (FASB). All leases are classified as either a capital (finance) or operating lease (off balance sheet) for financial reporting purposes. FASB seeks to determine if the risks and benefits of ownership are transferred from:

- The lease transfers ownership of the property to the lessee
- The lease contains a bargain purchase option
- The lease term is equal to 75% or more of the estimated economic life of leased property
- The present value of the minimum lease payments equals or exceeds 90% of the original value of the leased property

All leases that fail to meet **all** of these four criteria are classified and accounted as operating leases.

#### Operating Lease

The lease is accounted for as a pure rental. The equipment is neither shown as a liability nor an asset on the lessee's business balance sheet.

#### Capital (Finance) Lease

The lease is treated the same way as a purchase. The equipment is shown as an asset and a liability on the lessee's business balance sheet.

### Summary of Financial Statement Effects: Lessee

	Capital Lease	Operating Lease
<b>Total Assets</b>	Higher	Lower
<b>Total Liabilities</b>	Higher	Lower
<b>Total Lease Related Expenses</b>	Initially Higher	Initially Lower
<b>Net Income</b>	Initially Lower	Initially Higher
<b>Cash Flow from Operations</b>	Higher	Lower
<b>Cash Flow from Financing Activities</b>	Lower	Higher
<b>Leverage Ratio: Debt/Equity</b>	Higher	Lower
<b>Return on Assets</b>	Lower	Higher

*\*Please consult you tax advisor regarding any tax or accounting questions .*