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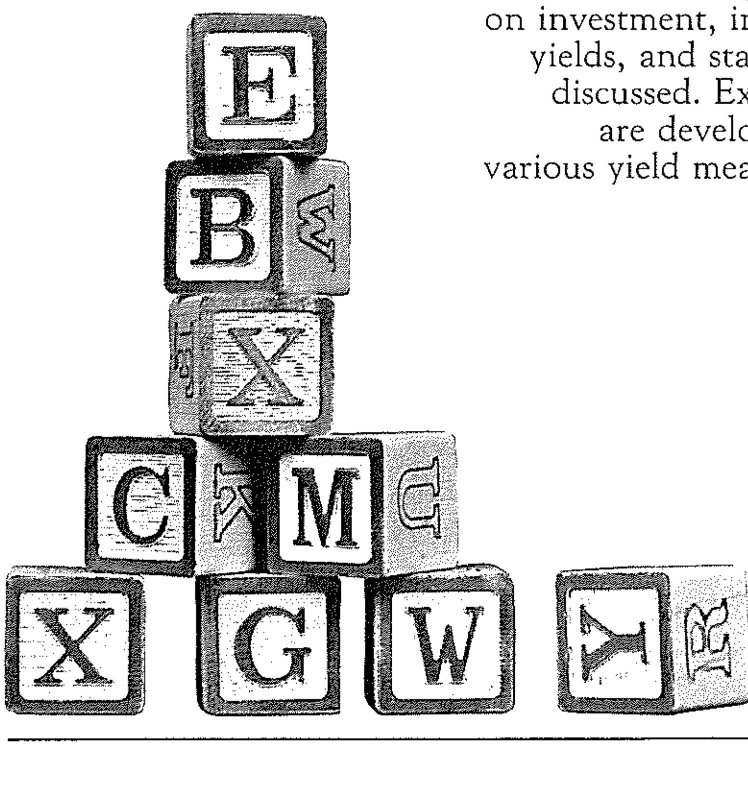
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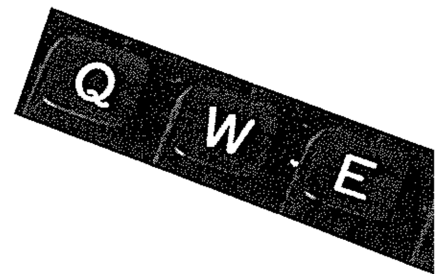
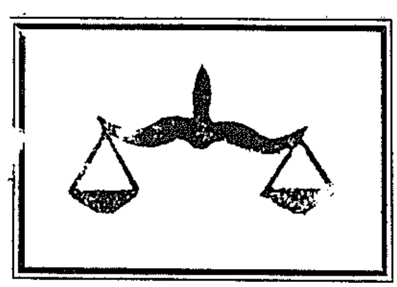
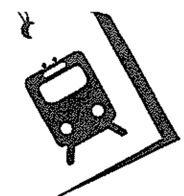
The author describes how computerized modeling can provide management of a leveraged leasing company with a tool to forecast the size of net income for a wide range of marketing strategies, employing a variety of volume levels and transaction types. The article explains how such modeling can be done, starting with tax modeling and its determination of new business volume, and concludes with financial statement modeling and capital structuring.



The article takes the position that the equipment leasing industry has matured to a point where the old marketing formulas no longer apply, and suggests re-evaluation of strategic positions based on an assessment of market needs, competitive forces, technology, and financial objectives.

Because various laws may be applied to a leasing transaction depending upon whether the transaction is viewed as a true lease or simply as a financing, a uniform personal property leasing law has been suggested to clarify the treatment of lease transactions. The article discusses, in a nontechnical manner, these varying laws and reviews some proposals for a uniform code..





Economic Benefits of Lease Financing

The following article is the executive summary of a study by Brimmer & Company, produced under the direction of Andrew F. Brimmer, Ph.D. The study was initiated to determine the economic cost and benefits of guideline leasing in general and its implementation in specific industries. The relationship between leasing, investment and employment was included in the parameters of the study.

Because of the limited amount of statistical data available in this area, much of the basic information used in this analysis was constructed from a variety of sources. While a major amount of information was provided from studies and records of the American Association of Equipment Lessors and other industry sources, data was also provided by the U.S. Department of Commerce, the Federal Reserve Board, a compilation of corporate annual reports, and World Leasing Yearbook.

Traditional guideline leasing constitutes a major source of capital for American industry. This method of financing has helped to expand the availability of funds—and to reduce the cost of credit—to many segments of American business which would otherwise find it difficult to obtain the equipment and facilities needed to expand the supply of goods and services on which the welfare of the American public depends.

These general conclusions are derived from a comprehensive assessment of the role which lease financing plays in capital formation in the United States. The study is based on a newly collected body of statistical and other information which made it possible to describe the pattern and magnitude of lease financing in American industry in recent years. It was also possible to estimate the number of additional jobs which leasing helps to create through the financing of new investment in plant and equipment.

Brimmer & Company is a diversified economic and financial consulting firm, established in 1976 by Andrew F. Brimmer, a former member of the Board of Governors of the Federal Reserve System. The firm conducts research on financial developments affecting financial institutions, trends in economic activity and interest rates in money and capital markets. It has produced a number of studies on employment, technology, economic growth and industry structure and competition.

Economic Incentives for Lease Financing

The acquisition of capital equipment through leasing has expanded substantially in recent years. This was primarily a reflection of the increased appreciation of the economic benefits provided by this source of financing. The tax incentives introduced in the 1950s and 1960s—designed to encourage investment spending—gave a strong boost to leasing. The reason is straightforward: If a firm needing equipment faces a tax situation which precludes its taking advantage of accelerated depreciation or the investment tax credit, it can lease the equipment from another company which can use the tax benefits. The availability of tax benefits to the leasing company enables the latter to charge rents below the cost to the user of purchasing the equipment. Thus, leasing lowers the cost of capital to many businesses while providing tax benefits to lessors who bear the risk of ownership.

Beyond tax incentives, however, a number of other economic factors make leasing an attractive financial instrument for many companies. These include the high cost of tying up cash in equipment purchases that might be better employed in other uses (such as the provision for working capital) or to acquire short-term financial assets. Moreover, compared with the use of bank loans to purchase equipment, leasing requires a smaller down payment, and it typically involves fewer restrictions. Many lease arrangements also include maintenance and repair services.

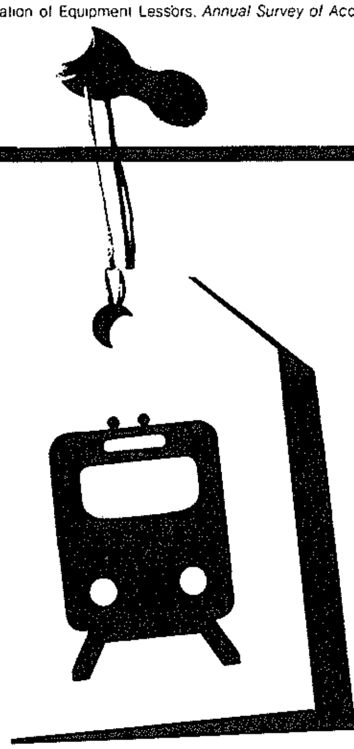
Table 1

FINANCING BUSINESS INVESTMENT, 1980-1983
(amounts in billions of dollars)

Category	1980	1981	1982	1983 F
Business Fixed Investment	309.2	346.1	347.6	327.9
Structures	110.6	129.7	141.4	130.2
Producers Durable Equipment	198.6	216.4	206.2	197.7
Selected Sources of Funds				
Equipment Leasing	43.5	55.5	57.6	61.2
Corporate Equities	12.9	−11.5	1.7	8.5
Corporate Bonds	32.9	35.6	42.0	42.4
Commercial Mortgages	20.7	−1.1	−0.8	6.9
Commercial Bank Loans	29.3	42.8	38.7	−7.4
Sources of Funds as a Percent of Business Fixed Investment				
Equipment Leasing	14.1	16.1	16.6	18.7
Corporate Equities	4.2	−3.3	0.5	2.6
Corporate Bonds	10.6	10.3	12.1	12.9
Commercial Mortgages	6.7	−0.3	−0.2	2.1
Commercial Bank Loans	9.5	12.4	11.1	−2.2

F = Forecast

Source. Compiled and calculated by Brimmer & Company Data on business fixed investment from U S Department of Commerce. Bureau of Economic Analysis Data on sources of funds from the Board of Governors of the Federal Reserve System Data on equipment leasing calculated by Brimmer & Company. based on the American Association of Equipment Lessors. *Annual Survey of Accounting and Business Practices* 1980, 1981 1982



Costs of Leasing: Public Policy Perspective

The benefits of leasing (particularly the tax savings) accrue primarily to the lessor and lessee, the principal parties to the transaction. The counterpart of these private tax savings is the loss of tax revenue by the federal government. This loss of tax revenue is roughly equivalent to expenditures of federal funds, and they are computed and accounted for as "tax expenditures." For instance, in fiscal year 1982, total tax expenditures were calculated at $253.5 billion. Of this amount, $198.4 billion were benefits to individuals, and the remaining $55.1 billion (21.8% of the total) were benefits to corporations.

These benefits to business enterprises represent a direct reflection of the express intent of Congress to provide benefits and incentives—through the tax code—for companies to undertake certain types of economic activity. The most important of these specific objectives is the stimulation of investment in new plant and equipment. The tax benefits derived from leasing have been a major source of support for this new investment.

For instance, in fiscal year 1982, tax benefits associated with all lease financing are estimated at $6.7 billion. This figure represented 31.4% of total tax benefits generated by capital expenditures. The leasing-related benefits were divided into those associated with traditional guideline leasing ($4.0 billion) and safe harbor leasing ($2.7 billion). Thus, despite the large but transitory impact of safe harbor leasing, the traditionally used guideline leasing accounted for 60% of the tax benefits derived from leasing. Consequently, lease financing clearly has an important—and growing—role in the promotion of new capital investment. Its share of tax benefits appears to be an accurate reflection of the contributions this type of financing makes to total investment expenditures.

Lease Financing of Business Investment

Lease financing has expanded to the point where it is the most important single source of funds to support business expenditures for capital equipment. For example, as shown in Table 1, in 1982, spending on business fixed investment amounted to $347.6 billion. This total was divided into outlays for structures ($141.4 billion) and producers durable equipment ($206.2 billion). In the same year, equipment leasing is estimated at $57.6 billion. At this level, lease financing was equal to 16.6% of total business fixed investment. It also represented 27.9% of outlays for producers durable equipment.

Moreover, during the last few years, leasing has risen faster than total capital expenditures. Lease financing as a proportion of the latter climbed from 14.1% in 1980, to 16.1% in 1981, and to 16.6% last year. During 1983, the fraction is projected to rise further to 18.7%.

These estimates suggest that leasing is a more important source of funds to meet business capital requirements than either new equity issues, corporate bonds, commercial bank loans, or commercial mortgages. Leasing is at least five times as important as new equities or commercial mortgages and nearly one and a half times as important as corporate bonds and commercial bank loans.

Lease Financing: Industry Profile

While leasing finances about one-sixth of business fixed investment across American industry taken as a whole, the proportion is much higher for a number of important types of equipment. The broad pattern and extent of reliance on leasing can be seen in Table 2, which shows capital expenditures and lease financing of selected types of equipment in 1982.

Table 2

CAPITAL EXPENDITURES AND LEASE FINANCING OF SELECTED TYPES OF EQUIPMENT, 1982
(amounts in billions of dollars)

Category	Capital Expenditures	Lease Financing Amount	Lease Financing percent of capital expenditure
Computers	34.0	5.0	14.7
Railroads - Class I	2.0	0.7	35.0
Motor Vehicles	30.1	9.3	30.9
Aircraft[1]	4.0	1.8	45.0
Shipping[2]	3.1	0.7	22.6
Agricultural Equipment[3]	13.3	0.7	5.3
Equipment and Facilities: State and Local Governments[4]	14.6	2.0	13.7

[1] Capital leases plus tax benefit transfers
[2] Capital expenditures consist of the value of newly produced nonmilitary vessels
[3] Farm gross capital expenditures ($12 6 billion) plus new leases of equipment ($0 7 billion) 1981
[4] Estimated outlays for equipment ($12 6 billion) plus new leases ($2 0 billion). 1981

Source Estimates by Brimmer & Company

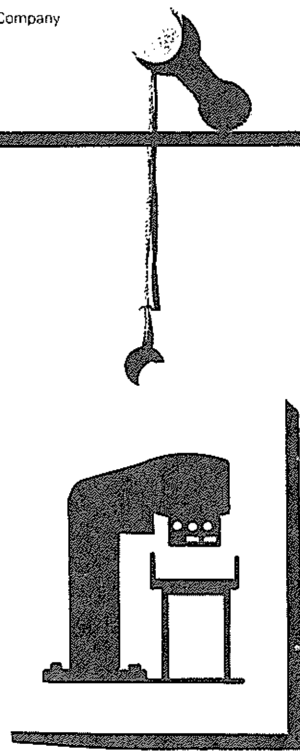


Table 3

LEASING AND EMPLOYMENT, 1981

Industry	New Jobs per $1.0 Billion of Investment Spending	Value of Leases on New Equipment (billions of dollars)	Increase in Employment (number)
Computers	43,170	4.1	176,997
Office Machinery and Equipment	41,080	3.1	127,348
Transportation Equipment	20,542	15.0[1]	308,127[1]
Construction Machinery and Equipment	25,170	1.6	40,272
Production Machinery and Equipment	26,410	6.9	182,229
Nonproduction Machinery and Equipment	27,890	3.5	97,615
Agricultural Equipment	24,720	2.9	71,688
Medical Equipment	33,430	2.0	66,860
Other Equipment	30,302	3.0	90,906
Total	27,602	42.1	1,162,042

[1] Includes aircraft, trucks, business automobile fleets (10 or more) and shipbuilding, based on estimates by Brimmer & Company

Sources: Value of new leases estimated by Brimmer & Company. Basic data from the *Annual Survey of Accounting and Business Practices*, American Association of Equipment Lessors, 1982. Increases in employment calculated by Brimmer & Company

Capital expenditures for aircraft are the most heavily dependent on lease financing. In 1982, such expenditures came to $4.0 billion, and leasing provided $1.8 billion (45.0%) of this amount. Second in line were railroads, where $700 million in leasing accounted for 35.0% of capital outlays. Close behind were motor vehicles. Businesses spent $30.1 billion for this type of equipment, and $9.3 billion (30.9%) was provided by leasing. In the case of shipping, nearly one-quarter (22.6%) of the value of newly produced nonmilitary vehicles was covered by leasing.

Capital outlays for computers amounted to $34.0 billion in 1982. Leasing supplied $5.0 billion (14.7%) of the required financing. Spending on agricultural equipment came to $13.3 billion. However, lease financing has not made much headway in this sector, and it accounted for only 5.3% of total capital expenditures.

While not directly comparable to traditional guideline leasing transactions, lease-purchase financing of equipment and facilities by state and local governments has been increasing. In 1982, this type of financing amounted to $2.0 billion and represented 13.7% of the estimated $14.6 billion in outlays for equipment acquired by these jurisdictions. The volume of lease-purchasing of equipment and facilities by state and local governments has nearly tripled over the last three years. This rapid growth has been stimulated by the seriously adverse economic and fiscal problems faced by states and municipalities.

Leasing, Investment, and Employment

Leasing makes a major contribution to the creation of new jobs in the American economy. This contribution arises primarily through the support of business spending on new plant and equipment. Such outlays stimulate the demand for capital goods and for a variety of related products and services. As output rises to meet these demands, labor requirements increase, and new jobs are created.

The impact of lease financing on new job creation is illustrated by the statistics in Table 3. The first column of figures indicates how much additional labor (input) is required to bring forth a specified amount of production (output). For the present analysis, it was assumed that an additional expenditure of $1.0 billion was made on new equipment in selected industries. For example, a rise of $1.0 billion in outlays for computer and equipment increases total employment by 43,170 persons over what the level otherwise would have been. (This gain consists of 17,050 jobs in the computer industry plus 26,120 jobs generated in related supplier industries.) Summary estimates of added employment per $1.0 billion of new investment spending are also shown for other industries.

The second column in Table 3 shows the value of leases on new equipment in 1981. These amounts, when multiplied by the number of extra jobs in the first column, provide an estimate of the increase in total employment generated by the volume of lease financing of the types of equipment indicated.

For example, lease financing of computers and equipment is estimated to have stimulated the creation of about 177,000 new jobs in 1981. Among the eight types of equipment shown, the number of new jobs ranged from just over 40,000 in construction machinery and equipment to more than 308,000 in transportation equipment. In the aggregate, it is estimated that the $42.1 billion of equipment leasing shown in Table 3 stimulated the creation of more than 1,000,000 new jobs in 1981.

Concluding Observations

The results of this study lead to several important conclusions: Traditional guideline leasing does derive a part of its appeal to investors from the federal income tax benefits associated with the capital expenditures financed under this type of arrangement. However, those benefits are an integral part of the series of tax incentives which the federal government has provided to help achieve a variety of worthwhile public purposes. And among the latter, the stimulation of investment and the creation of new jobs have been given the highest priority on the agenda of national economic policy.