
Appendix 6b. Topical Summary—Financial Leases

Reference:
1993 SNA Rev. 1, Chapter 17
Cross-Cutting and Other Special
Issues

A6b.1 *A financial lease is a contract between lessor and lessee whereby the lessor puts a good at the disposal of the lessee and the lessee pays rentals, such that the lessee has most or all of the risks and benefits of ownership.* This is an example of where economic ownership differs from legal ownership. The rationale is that while legal title remains with the lessor, the lessee has most or all of the risks and benefits of ownership, and so there is a change in economic ownership of the good. The arrangement is treated as a transaction in goods financed by a loan, which is repaid in full or in most part by the rentals. Financial leases are also called finance leases or capital leases. For further details of the definition, see paragraphs 5.55-5.56.

A6b.2 Financial leases are distinguished from operating (or operational) leases, (see paragraphs 10.140-10.143), in which neither legal nor economic ownership changes, and the rentals are recorded as services. In terms of underlying economic processes, although both operating and financial leases have similar forms, the essence of a financial lease is seen as being a loan, while the operating lease is seen as providing a service. That is, the operating lease provider has a stock of assets, which it wants to provide to other

entities, and provides varying degrees of backup support. In contrast, the financial lease provider is usually a financier, and operates a lot like a lender except that the lessor has the additional collateral of legal ownership of the assets. Accounting standards also recognize this distinction.

A6b.3 As a result of this treatment, a cross-border financial lease will give rise the following entries in different accounts:

- A loan liability of the lessee and a loan asset of the lessor is recorded to the value of the goods acquired. The outstanding amount is shown in the **international investment position** (see paragraph 7.56).
- The creation of the loan and the subsequent repayments of the loan (including, at maturity, the return of the good or its purchase) are recorded under loan transactions in the **financial account**.
- The equipment subject to the lease is regarded as being purchased by the lessee, so there is a change of economic ownership of **goods** from the lessor to lessee. If cross-border, this change of ownership is shown in the goods and services account (see paragraph 10.17(f)). If the good is returned to the lessor at the maturity of the contract, there is a change of economic ownership of **goods** from the lessee to lessor,

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- which is also recorded in the goods and services account.
- Any explicit fees and FISIM is attributed on the loan if the lender
 - **Interest** is accrued on the loan (see paragraph 11.49).
- is a financial intermediary and included in **financial services** (see paragraphs 10.113-10.130).

Box A6b.1 Numerical Example of Financial Lease

A piece of imported equipment worth 1000 is provided under a financial lease from a nonresident financial intermediary. The lease begins on January 1, an annual payment of 140 is made on December 31 each year for ten years, at which time the lessee purchases the equipment at an agreed price. The contract is based on an interest rate of 7 percent per annum, while the reference rate of interest is 5 percent per annum.

For the economy of the lessee, the following entries are made in the first two and final years:

Year 1

	Credit	Debit
<i>Current Account:</i>		
Goods		1,000
Services-Financial services (FISIM)		20
Primary Income-Investment income		50
<i>Financial Account:</i>		
Other investment-Loans	1000	70
Other investment-Currency and deposits	140	

Accrued interest is 70, of which 20 is FISIM and 50 is pure interest. The value of the loan debt is 930 at the end of year 1 ($1000 + 20 + 50 - 140$)

Year 2

	Credit	Debit
<i>Current Account:</i>		
Services-Financial services (FISIM)		18.6
Primary Income-Investment income		46.5
<i>Financial Account:</i>		
Other investment-Loans		74.9
Other investment-Currency and deposits	140	

Accrued interest is 65.1, of which 18.6 is FISIM and 46.5 is pure interest. The value of the loan debt is 855.1 at the end of year 1 ($930 + 18.6 + 46.5 - 140$)

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Year 10

	Credit	Debit
<i>Current Account:</i>		
Goods	32.8	
Services-Financial services (FISIM)		3.2
Primary Income-Investment income		8.1
<i>Financial Account:</i>		
Other investment-Loans		161.55
Other investment-Currency and deposits	140	

Accrued interest is 11.3, of which 3.2 is FISIM and 8.1 is pure interest. The residual value of the good purchased is 32.8, which is recorded as a goods transaction if the good is returned to the lessor (as in the example) rather than the lessee purchasing it.