

# RVI GROUP

## *Residual Value Insurance for Financial Accounting*

The pioneer in residual value insurance, RVI and its family of companies have been serving the Auto Finance Industry for over 20 years by helping our clients improve the financial performance of their leasing, securitization, and other residual-driven financings.

### **A Layman's Guide to FASB 13 and Finance Lease Accounting**

#### ◆ *What is FASB 13?*

The Financial Accounting Standards Board ("FASB"), Statement 13, classifies leases in one of two ways:

- A lease in which the benefits and risks incident to ownership are transferred to the lessee (a Finance Lease)
- A lease in which the lessor retains these characteristics of ownership (an Operating Lease)

#### ◆ *How does this affect how I account for leases?*

Finance Lease accounting reflects the lease as similar to a loan with the yield component of the lease payments recognized as income, and with the principal portion of the payments reducing the receivable balance. A Finance Lease appears as a financial receivable on the balance sheet, as would a loan.

Operating Lease accounting reflects the lease payment as revenue and the asset's depreciation as an expense, resulting in a straight-line recognition of income.

#### ◆ *Is there a financial benefit to booking Finance Leases vs. Operating Leases?*

Yes. Income is greater in the earlier years of a Finance Lease due to a constant yield being applied to a decreasing balance, thus, earnings are accelerated. In fact, in the first year of finance lease accounting the net income can be almost *three times* that of operating leases.

#### ◆ *How can I book my leases as Finance Leases?*

FASB 13, paragraph 7, states that a lease should be booked as a Finance Lease if it meets one of four criteria:

- Transfer of ownership to lessee occurs by end of lease term;
- Lease contains a bargain purchase option;
- Lease term is equal to 75% or more of economic life of the asset;
- Present value of the lease payments and any guaranteed portion of the residual value exceed 90% of the value of the asset at lease inception; the guarantee must be provided by an independent third party.

The typical retail lease does not meet the first three criteria; **RVI provides a guarantee** so that its clients can meet the fourth criteria, and benefit from finance lease accounting. An RVI insurance policy will provide the *minimum amount of insurance* for each vehicle lease to qualify...a fraction of the residual, at a cost that is just a fraction of the financial benefits you'll gain.

***Maximize the financial performance of your lease portfolio; ask us how.***

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Call Chris Deloge at 203.975.2144 or Valerie Torphy at 203.975.2124 to learn more about RVI's products and services.

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