A SUCCESSFUL SUPERMARKET IN NOVOCHEBOKSARSK

During the Leasing Development Group’s recent seminar in Chuvashia, we learned about a lessee named Trading House #55 from the city of Novocheboksarsk. Director Olga Kosikhina told us how leasing helped her transform her store from a loss-maker into a rising star.

Continued on pg. 24

The overall theme of this edition of the Leasing Courier is lessees. Why have we chosen to devote so much attention to the «consumers» of the leasing industry? Because unlike the savvy experts from the leasing companies, banks and equipment manufacturers, who already thoroughly understand leasing, lessees often have only a vague idea of the specifics of this financial tool. In the hope of educating lessees about leasing, we have decided to launch a new section of the Leasing Courier entitled «Advice for Lessees.» This section will include practical information to help lessees in their business activities.

The Leasing Development Group is also developing a new series of seminars for lessees entitled «Acquiring Fixed Assets Using Leasing» The first of these seminars will be held in Krasnodar this May.

If you would like to suggest any topics that may be of special use or interest to lessees, please contact us at the address listed on the back cover of this journal.
What is the goal of the IFC’s investment projects?

The IFC was created for the purpose of making investments in the private sector. It essentially acts as an investment bank with two objectives: on the one hand, of course, it tries to turn a profit, but on the other, it tries to develop the markets where it operates. The leasing industry is one area that we consider especially important.

We use two basic criteria to assess our investment projects: they must be profitable, and they must contribute to market growth. In countries like Poland and the Czech Republic, where the private sector is already well developed, we are undertaking fewer and fewer projects, since the markets in these countries have begun to function on their own. In Russia, we see our principal task as creating and supporting «model» enterprises that might serve as an example to other companies.

How do IFC investment projects work?

We basically have two kinds of project. Sometimes the IFC buys shares in existing companies or helps found new ones, always capping its involvement at 25%. In other cases, it simply gives loans to client companies. These loans are usually more long-term than those readily available on the market, but they are still commercial in nature, so potential clients should not expect to receive any discounted rates. Furthermore, our loans may not exceed 50% of a client's total assets, so we are never the sole source of funding.

Can you tell us more about the IFC’s criteria for investment projects?

First of all, potential clients must already have a well thought-out plan. A mere desire «to get into leasing» is not enough. The IFC is not a leasing company; it is more like a bank that is interested in financing the process of leasing itself. Therefore, companies should not come to us for help with just one or two deals. We are looking for long-term partners. When we do give loans to leasing companies, we make a number of demands. First of all, the companies must diversify their portfolios so that no single lessee or industry makes up more than 25-30% of their total. Second, the companies must adhere to a strict repayment schedule. Third, certain kinds of business are strictly prohibited, such as any project that involves the manufacture of alcoholic drinks, firearms, military technology or gambling machines. As I mentioned before, projects are expected to be profitable, so companies have to...
consider whether their leases will pay off, where they will make their profits and how much income they will earn on their investments.

Every time the IFC creates a new leasing company, the other players on the market begin to realize that leasing can be a profitable business. At the same time, we try to influence the development of the market itself by pushing for legislative reforms. We also send a signal to potential investors that it is safe and profitable to invest in this particular market — otherwise we wouldn’t be doing it ourselves.

Could you give us some concrete examples of companies that the IFC has created?

We have formed successful leasing companies in more than 60 countries. A prime example is the Korean Development Leasing Company, which has now become the largest leasing company in South Korea.

In Russia, the IFC helped form Deutsche Leasing Vostok, together with Deutsche Leasing, the fourth largest leasing company in Germany. Deutsche Leasing Vostok is the first universal leasing company in Russia with a significant amount of foreign capital. Although the company is still young (it was founded in spring 2000) it has already achieved a certain measure of success for a variety of reasons. The project’s main sponsor, the DL Gruppe, has proven very effective. They have put together a strong team with an appropriate balance of Western and local specialists. DL Vostok has been able to secure funding from some major banks, which is extremely important for a leasing company in Russia, where finance is hard to come by. Finally, the company has been careful to tailor its services to the Russian market. It spent half a year developing the basic structure of its lease agreements, putting together a solid insurance policy, working out agreements with its principal suppliers and selecting its clients. All of these painstaking preparations should soon begin to pay off. The company plans to expand its portfolio dramatically over the next six months.

Karim, how does a company apply for IFC funding?

There is no standard application form. Anyone with a well thought-out plan and a desire to form a new company, or to expand an existing one, can contact the IFC directly. This applies to both foreign companies and local ones. Applicants must tell us about their companies and their proposed projects, either by mail or in person. If a project seems interesting, the IFC will ask the applicant to prepare and submit a detailed business plan for further consideration.

How exactly does the IFC decide which projects to finance?

The review committee usually consists of an investment specialist with considerable experience and a thorough knowledge of both finance.

In addition to leasing companies, the IFC also invests in industrial firms, banks and insurance companies. One example is the well-known yogurt company Campina. This project was developed in two stages. In February 1992, when the Dutch company Campina Melcuni decided to build a yogurt plant in the Stupino district of the Moscow Region, the IFC helped finance the construction. However, before granting the loan, we required that the local farms that were to supply the factory with milk be fully modernized, since a modern yogurt factory can use only the highest-quality milk. Thus, during the second stage of the project we helped modernize and re-equip the local dairy farms. We did not begin working on the construction of the factory until we had already developed the local infrastructure. That took about one year. The construction itself cost about 60 million guilders ($30m). Over the two-year term of the loan, we helped modernize 12 local dairy farms, all of which continue to work with Campina to this day.
and local conditions, and an engineer with the appropriate technical experience. Together they are responsible for making a complete assessment of the technical, financial and economic aspects of the project. They visit the project site itself in order to become familiar with every minute detail, which they later discuss thoroughly with the principal investors. When they return from the site, they present their recommendations to the IFC, which then decides whether to fund the project. If the project gets the green light, the IFC’s legal department begins to draft the necessary documents. Any unresolved questions are discussed with the client company and the other financial institutions involved in the project. Only when every last detail has been thoroughly worked out do we finally present the project to the IFC Board of Directors.

**HOW TO PREPARE AN INVESTMENT PROPOSAL**

All investment proposals submitted to the IFC must include the following information:

1. **A brief description of the project**

2. **The principal investors, management and technical assistance:**
   - The principal investors’ history and types of business (including financial history)
   - Proposed management structure, list of directors and their biographies
   - A description of all technical agreements and other external assistance (management, production, sales, finance, etc.)

3. **Market report**
   - Description of local, regional, national and export markets
   - Expected production volume, cost per unit, marketing plan and projected market share
   - Potential consumers and distribution network
   - Existing suppliers of raw materials
   - Potential competitors and the probability of satisfying consumer demand with analogous products
   - Trade barriers and import restrictions that may affect production and sales
   - Important factors that may influence the market’s potential

4. **Technical foundation, manpower, access to raw materials and environmental issues**
   - A brief description of the production process
   - Specific technical difficulties and need for special know-how or skills
   - Potential equipment suppliers
   - Availability of manpower and infrastructure (transportation, communication, energy, water, etc.)
   - Itemized estimate of operating costs
   - Sources, cost and quality of raw materials and connections to auxiliary industries
   - Import restrictions on essential raw materials
   - Proposed location of enterprise in relation to suppliers, markets, infrastructure and manpower
   - Projected strength of enterprise in comparison to analogous enterprises
   - Potential environmental hazards and possible solutions

5. **Need for investment, project finances and profits:**
   - Estimated cost of project: expenditures on real estate, construction and equipment; volume of turnover capital, including required sum of foreign currency
   - Proposed financial structure of the enterprise, including expected sources of finance and conditions for loans and shareholder capital
   - Type of finance to be requested from the IFC: loans, shares or both (including amount)
   - Expected financial results and return on investment
   - Any important factors that may affect the profitability of the project

6. **Government support and legal framework**
   - Governmental programs for economic development and investment
   - Incentives and support offered by the state
   - How the project can contribute to the country’s economic development
   - Overview of foreign currency regulations

7. **Projected schedule for developing and realizing the project**
Does the IFC control how its loans are used?

Absolutely. After the Board of Director approves a project we begin to allocate the funds according to the procedures stipulated under the agreement. From that point on, the IFC strictly controls how the funds are used. We continue to monitor our investment for the duration of the project, holding regular consultations with management, sending working groups to the site, and requiring quarterly reports on the state of the project with complete information about any factors that could influence its development. The IFC also requires annual financial reports, which we submit to independent auditors.

For additional information, please contact the Central and Eastern Europe Department of the IFC at (095) 755-88-18 in Moscow.

SEMINAR IN SMOLENSK

Eleonora Veitsman  
PR Specialist  
IFC Leasing Development Group

On February 8, 2001, the Leasing Development Group held a seminar in Smolensk entitled «The Principles of Leasing in Russia.» The Smolensk Chamber of Commerce and Industry helped organize the event, which was attended by 74 people representing a variety of interested parties: leasing companies, potential lessees, banks and the regional government. Participants learned about essential elements of leasing and analyzed the legal and financial intricacies of leasing transactions. They also had the opportunity to meet with representatives from the sole active leasing company in the Smolensk region and discuss the possibility of future joint projects.

The seminar concluded with a press conference for local print and television media. The speakers noted that industrial firms in the Smolensk Region desperately need to modernize their facilities. Therefore, leasing, as an effective financial tool for acquiring new equipment, has enormous potential in the region.

At present, the only registered and active leasing company in the Smolensk region is the Smolensk Business Development Center. Two other companies, Askold Bank and Smolenska-grosnab [Smolensk Agricultural Suppliers], a subsidiary of Sberbank, also offer leasing plans in addition to their primary lines of business. In spite of the small number of leasing companies, more and more of the region’s entrepreneurs have begun to understand the advantages of leasing over other forms of finance. As of December 2000, the Smolensk Business Development Center had signed over 120 lease agreements.

Although virtually all of the region’s enterprises need new equipment, only certain industries have really begun to make active use of leasing: namely, those that use relatively inexpensive technology and have a high rate of capital turnover. The Smolensk Business Development Center’s leasing portfolio breaks down as follows: retail equipment, 36%; food-processing equipment, 13%; real estate, 13%; petrol stations, 13%; vehicles, 7%; and printing equipment, 3%.
The Smolensk regional government has begun to promote leasing in earnest, as it recognizes the importance of leasing to the region's social and economic development. It allocated one million rubles to the Smolensk Regional Fund for the Support of Small Entrepreneurship for the creation of a business incubator in 1999, and half of these funds will be used to finance leases. In August 1999, the region also received 1.5 million rubles for leasing projects from the Federal Fund for the Support of Small Entrepreneurship.

The region allocated 4.8 million rubles to its business development fund in December 2000, with 2.35 million rubles specifically earmarked for the region's bakeries to help them lease new equipment. However, due to tax shortfalls, only 200,000 rubles have actually been transferred to the fund so far.

The Smolensk Region's business development program for 2001-2002 will continue to promote leasing as a valuable tool for supporting small enterprise.

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**A SEMINAR FOR THE ICE CREAM PRODUCERS’ UNION**

*Aleksei Trepykhalin*
*Training Manager*
*IFC Leasing Development Group*

On March 1, 2001, the IFC Leasing Development Group held a seminar entitled «An Overview of Leasing in Russia» at the All-Russian Exhibition Center in Moscow. Organizational support was provided by the Union of Russian Ice Cream Producers and the Region InvestConsult Center, a joint project of the Council for the Study of Productivity (part of the Russian Ministry of Economic Development and Trade) and the Russian Academy of Sciences. The seminar was held concurrently with the Eighth International Exposition of Ice Cream and the Frozen Foods Industry.

The IFC seminar attracted a great deal of attention at the exposition, since the frozen food industry is in desperate need of new equipment, and leasing represents one of the most realistic solutions. The seminar addressed the following topics:

- The concept of leasing and its advantages
- An overview of the Russian leasing market
- A survey of Russian leasing legislation
- How to choose a leasing company and build an effective partnership
- The essential clauses of a lease agreement
- Essential accounting and tax regulations for leasing transactions
- Leasing as an effective means of acquiring new equipment

Several leasing companies attended the seminar, including RG Lizing, Rosagrolizing, Prodshlizing, KNK Lizing and the Moscow Leasing Company. These companies were able to meet with expo participants and establish contacts with potential lessees.
SEMINAR IN SARATOV

On March 22, the IFC Leasing Development Group held a seminar on «The Principles of Leasing» in the city of Saratov. Organizational support was provided by the Saratov regional government, the state enterprise Saratov Special Programs Management and the Directorate for Investment and Leasing.

Yury Mikhailovich Sapronov, director of Saratov Special Programs Management, opened the seminar with a detailed discussion of the potential for leasing in Saratov and an account of the regional government’s initiatives to create favorable conditions for leasing in the region. Several of the region’s ministries are currently working on a «Leasing Development Program,» which will include concrete measures for the support of leasing projects and the dissemination of information about leasing among potential lessees in the region. The program will also include pilot projects such as an equipment yard for regional construction companies. By inviting the IFC to hold its «Principles of Leasing» seminar in Saratov, the regional government has taken an important first step towards developing the local leasing industry. It is no surprise that the administration of Saratov has taken such an interest in leasing: the region’s factories are in urgent need of new equipment, while its small and medium-sized businesses cannot achieve their full potential due to a shortage of financing. Under these circumstances, leasing is one of the most effective means of helping manufacturers acquire new equipment, modernize their production facilities, raise productivity, become more competitive and create new jobs. And the more the leasing industry grows, the more the regional government will earn in tax revenue.

Despite the huge demand for leasing services, the only licensed leasing company currently active in Saratov is the Volga [Povolzhsky] Leasing Center. Several local banks also have leasing licenses. An extensive publicity campaign is still required to make potential lessees and suppliers in the region realize the benefits of leasing.

The IFC seminar addressed the following topics:

- The concept of leasing and its advantages
- An overview of the Russian leasing market
- A survey of Russian leasing legislation
- The stages of a lease
- How to choose a leasing company and build an effective partnership
- The essential clauses of a lease agreement
- Essential accounting and tax regulations for leasing transactions
- Lease payments
- Implementing a lease agreement
- Guarantees on leases
- Leasing as an effective means of acquiring new equipment

Seminar participants were able to ask questions and receive detailed consultations from the IFC’s panel of experts. Local media provided thorough coverage of the event. The seminar raised considerable interest not only within the commercial sector, but also among regional academics. The IFC Leasing Development Group has already been invited to hold a second seminar on leasing in Saratov.
NEW SEMINAR FOR LESSEES

Veronika Shtelmakh
Economist
IFC Leasing Development Group

The Leasing Development Group is preparing a series of seminars on «Leasing as a Means of Acquiring New Equipment.» The seminars are intended for lessees of all levels of experience, from novices to experts. The first of the seminars will be held in late May 2001 in Krasnodar.

Over the last few years the IFC Leasing Development Group has held seminars on «The Principles of Leasing» in 19 regions throughout Russia. These seminars, which shed light on the financial and legal aspects of leasing, were intended for a diverse audience, including lessors, lessees, attorneys, economists, financial analysts, scholars and students.

However, we began to notice from the very beginning that most of those attending seminars in the regions were lessees. This is not surprising, since, according to the Registration Chamber of the Ministry of Justice, 75% of Russia’s registered leasing companies are concentrated west of the Urals, while only 15.6% are situated in the Ural Mountains and a mere 8.4% in Siberia. Therefore, whenever we held seminars in the provinces, no more than four or five leasing companies sent representatives, while the overwhelming majority of the participants were either potential or active lessees. That is why we have decided to organize a new series of seminars that will cater specifically to lessees and their particular interests.

The seminars on «Leasing as a Means of Acquiring New Equipment» are designed for company directors and financial specialists. Participants do not have to be experts on leasing: anyone with a basic understanding of how leases work will be welcome to attend. The seminars promise to be useful to both experienced lessees and those that are only beginning to contemplate their first lease. They will help lessees make contact with leasing companies and structure more effective leases.

During the seminars, participants will learn about the history of leasing in Russia and the important features of the Russian leasing market. They will learn how best to plan and structure their leases and how to handle the various tax and accounting problems that arise over the course of a lease. Some time will also be spent analyzing difficult legal problems. The IFC’s attorneys will explain issues such as the essential clauses of a lease agreement and the forms of guarantees that leasing companies typically require of lessees.

A lot of attention will be devoted to business planning and financial analysis. Participants will learn how to write business plans for leasing companies and how to make important financial decisions, such as whether to purchase an asset outright with working capital, take out a bank loan or enter into a lease. The IFC’s experts will analyze the main features of lease payments and use concrete examples to show how they affect a lessee’s cash flow.

Most topics will be accompanied by practical exercises. At the end of the seminar, participants will be invited to take part in an educational game, in which they will be divided into teams and asked to critique some sample business plans and find the weak points in the accompanying financial documents - in short, to play the role of a lessor.

We hope that our seminars will help Russian businesses and leasing companies build constructive partnerships.

Package of the documents given in the leasing company

1. Company charter and other legal documents
2. Financial documents
3. Business Plan with attachments
4. Collateral & guarantees for the leasing agreement
5. Draft equipment purchase contract
6. Other documents as requested

A slide from the IFC’s seminar on «Leasing as a Means of Acquiring New Equipment»
In our discussions with numerous Russian leasing companies, we have discovered a very interesting fact: it turns out that when Russian lessors first meet with potential lessees, they often have to dispel certain myths about leasing that have gained currency among Russian businessmen.

Some Common Misconceptions among New Lessees:
• Leasing is an effective tool for any enterprise
• The application process for a lease is much simpler than for a bank loan
• Leasing companies make quick decisions about whether or not to sign a lease
• Leases do not require additional guarantees
• Lessees do not have to be in solid financial shape in order to take out a lease

We hope that this article will help clarify these misconceptions, prepare lessees for their first meeting with a leasing company and facilitate the negotiating process.

When is leasing profitable?
We would like to begin by dispelling one of the most dangerous myths about leasing: that it is always effective. There are cases where leasing makes less sense than other sources of financing. There are several reasons why this can occur. First of all, lease agreements, like loan agreements, come in many different forms, and their specific terms can vary considerably from case to case. The terms offered by a commercial leasing company are probably not going to be as attractive in comparison to a subsidized government loan. Second, one of the main economic benefits of leasing is that it allows a company to reduce its profit tax. If a company is not earning any profits, this advantage is lost, and leasing will probably turn out to be a relatively expensive form of finance. Therefore, companies should consider leasing as only one of several possible ways to finance the acquisition of new assets. They should make all of the necessary calculations and compare their options while they are still developing their business plans.

Choosing a Leasing Company
Once a company has decided to take out a lease, the next step is to choose a suit-
able leasing company. Some of the questions that potential lessees often ask at this stage include:

1. Where can I find information about existing leasing companies?
   You can obtain information about leasing companies from several sources. It is quite likely that the bank you are currently using has its own leasing subsidiary or preferred leasing company. Your local Chamber of Commerce probably has data on leasing companies that do business in your area. And of course, you can always refer to the IFC Leasing Development Group's Directory of Russian Leasing Companies; the third edition, which came out in October 2000, can be found on our web site.

   According to the most recent data from the Ministry of Justice's Registration Chamber, there are now some 1,500 leasing companies registered in Russia. However, many of these companies only obtained their licenses for the sake of one or two major deals, after which they never signed another lease. The Leasing Development Group estimates that only some 30% of Russia's licensed leasing companies - that is, around 500 - are currently active. Most of them (around 70%) are concentrated in European Russia (west of the Urals), and another 15% in the Urals region and Western Siberia.

2. Should I choose a local leasing company or one from another region?
   When choosing between a local leasing company and one from another region, one should always factor in the cost of travel and long-distance telephone calls. On the one hand, working with a local leasing company means lower overhead. On the other, if the project is a large one, local leasing companies might not have sufficient financial resources to see the deal through. Furthermore, local leasing companies and the larger firms from Moscow and St. Petersburg are likely to offer very different terms.

3. How do I know if a leasing company is reliable?
   When considering a potential leasing company, one should always check whether it has a leasing license and when that license is due to expire. It could happen, for example, that the company's license is due to expire within one year, while your project is going to last for a three-year period. After the lessor's license expires, the lease agreement will remain in effect, but the parties will no longer be able to claim any of the tax benefits allowed for leasing transactions. Therefore, as the date of expiration approaches, lessees should make sure that the leasing company has extended its license or applied for a new one.

   Lessees should also be sure to note whether a leasing company is open or secretive. Legitimate and successful leasing companies do not hide information about themselves and should always be glad to name their key partners and important clients. If a leasing company does not give you straight answers, you should hear alarm bells ringing.

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1 See Leasing Courier #7 (2000), «Questions and Answers», for a more detailed discussion of this problem.
How to Lay the Foundation for an Effective Partnership

We suggest that you clarify the following questions during your first meeting with a leasing company:

• How long will it take to reach a decision?
• What sort of guarantees will be required?
• What kind of documentation will the leasing company require? (a complete list)

A mutual understanding on these points will put your relationship with the leasing company on a solid footing and eliminate the risk of false expectations during the application process.

The Lessee’s Application

As a first step, many leasing companies ask their potential lessees to fill out a lease application. In Insert #1 below you will find some sample questions from a typical application form. Even if the leasing company does not require any application, it is to the lessee’s advantage to prepare a written outline of the project in preparation for the first meeting with a leasing company. This will make the lessee appear more trustworthy in the eyes of the leasing company. Leasing companies tend to appreciate clients who know from the outset exactly what kind of equipment they want, who manufactures the equipment and how much it costs.

On the basis of the lease application, the leasing company’s experts will make a preliminary estimate of the lease payments and payment schedule. The lessee is then expected to incorporate this estimate into the financial section of his business plan.

Documentation Required by Leasing Companies

In Insert #2 we show the documentation typically required for leases. Leasing companies usually require potential lessees to submit the following documents when applying for a lease: company charter and other legal papers, financial documents, business plan with supplements, and documentation of possible guarantees.

In some cases, leasing companies might require a smaller number of documents. For example, Baltlizing usually asks its potential clients to submit 20 supporting documents, but in the case of automobile leases it requires only six: the application form, company charter, balance sheet, bank statement, confirmation of signing authority and a copy of bank signatures.

Guarantees

It is easy to explain how the «myth» arose that leasing does not require guarantees. In the West, this «myth» is actually a reality: the leased asset itself serves as a sufficient guarantee, and additional collateral is usually not required. In Russia, however, this arrangement is still impossible for a number of reasons, including the prohibitive costs of finance and the absence of any reliable mechanism for repossessing a leased asset.

Business Plans

Writing a business plan for a leasing company is no different from writing a business plan for any other financial institution. We have already noted that lessees should provide detailed forecasts of their potential sales and possible developments in their markets. The business plan’s overall financial data will be based on these forecasts, so any error in the calculations may lead to serious problems, even insolvency, further down the road. It goes without saying that all of the financial data that the lessee reports in the business plan should accurately reflect the state of the balance sheet, as leasing companies will check this information in much the same way as a bank would before issuing a loan.
According to A.P. Mokin, director of Kreditimpleks Leasing Company, one of the most common misconceptions among potential lessees is that they do not have to be in good financial shape in order to take out a lease, since the leased assets themselves (motor vehicles, in the case of Kreditimpleks) already serve as sufficient guarantees. One has to realize that leasing is essentially a form of lending, so leasing companies will always prefer to work with lessees whose current revenue easily exceeds the size of future lease payments.

The leasing company’s decision will be based in large part upon the documentation that the lessee has submitted.

**Some Useful Advice**

While we are on the topic of creating a positive working relationship with a leasing company, we should add a few words of advice about maintaining that relationship throughout the duration of a lease. We suggest that lessees maintain regular contact with their leasing companies. Regular contact is essential for building trust, which plays an important role in long-term business relationships. Useful forms of contact include regular updates on the financial status of your projects (supported by financial documents), information about your company’s activities and how the leased asset is being used, regular phone calls, etc.

Whenever a lessee finds himself in financial difficulties, he should let his lessor know immediately. It is better for the lessor to hear about such problems directly from the lessee than from some third party. This way the lessor will be more willing to work out a mutually acceptable resolution.

Keeping up regular contact with a leasing company makes it easier for a lessee to resolve such issues as restructuring the lease, obtaining payment deferrals and signing new deals.

Good luck!

The author would like to thank I.M. Chuvilova, head of the credit analysis department at RG Lizing, as well as the directors of Kreditimpleks, Baltlizing and other Russian leasing companies for their assistance in preparing this article.

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**THE LEASE AGREEMENT: A LESSEE’S PERSPECTIVE**

*Olga Shishlyannikova, Attorney*

*IFC Leasing Development Group*

A lease agreement entails a complex set of legal rights and obligations on the part of both the lessor and the lessee. People often forget this and think only in terms of the lessor’s rights and the lessee’s obligations — an unbalanced point of view that is often reflected in the terms of the lease agreement. As a rule, lease agreements tend to favor the lessor. We believe that this is inappropriate. In this article, we shall look at the provisions of a standard lease agreement from the point of view the lessee’s interests.
Agreeing on the Terms of the Sales Agreement

One of the differences between a lease agreement and a regular rent agreement is that with leasing, the lessor purchases the asset on behalf of a particular lessee. The lessee, who is not a direct party to the sales agreement, must be given some form of control over the terms of this agreement.

The most convenient way of achieving this, from the lessee’s point of view, would be to require the lessor to obtain the lessee’s written approval of the sales agreement before it is signed. But leasing companies rarely agree to such arrangements, arguing that they must protect the confidentiality of their agreements with suppliers. In such cases, the lessee should make sure the lease agreement itself stipulates the essential terms of the sales agreement, such as those regulating the characteristics of the leased asset, the delivery of components and spare parts, delivery times and places, receipt of the leased asset, procedures for making complaints regarding quality or quantity, mandatory technical training for the lessee’s personnel, maintenance procedures, etc. In practice, lessees often make these demands at the outset, when submitting their lease applications.

If the vendor refuses to include any of these important terms in the sales agreement, the lease agreement should require the lessor to obtain the lessee’s consent before agreeing to any other conditions. The lease agreement should also give the lessee the right to annul the lease if the lessor fails to obtain his consent before signing the sales agreement.

It is also critical that the lessee be informed of the terms of the sales agreement at all times. This is particularly important in cases where the leasing company has chosen the asset and the vendor, and the lessee has limited knowledge of the terms of delivery, since Article 670, Clause 1 of the Russian Civil Code gives lessees the right to make direct claims against the vendor for any violation of the terms of the sales agreement. Since the lessee effectively has the rights and obligations of a buyer, he must therefore be informed of the provisions of the sales agreement.

As we noted above, the most convenient arrangement would be to attach a copy of the sales agreement as part of the lease agreement. If the leasing company refuses to do so, the lessee should require it, under the terms of the lease agreement, to reveal all essential provisions of the sales agreement within a specified period. The lessee should also make sure that the leasing company is legally liable for failing to provide this information, e.g., by stipulating fines or penalties for each day it is late.

Formal Acceptance of the Leased Asset

According to Article 668, Clause 1 of the Russian Civil Code, the vendor usually delivers the leased asset directly to the lessee. Therefore, one of the first responsibilities that the lessee faces is to formally accept the leased asset. He should therefore pay careful attention to the provisions of the lease agreement that deal with the procedures for formal acceptance. On the whole, receiving a leased asset is no different from receiving goods under a sales agreement. However, we would like to point out two important aspects that sometimes give rise to questions: the actual procedures for accepting the leased asset and the time frame for filling out the appropriate paperwork.

Financial leasing is a trilateral affair, involving vendor, lessor and lessee. Since the transfer and formal acceptance of the leased asset affects all three parties, they should draw up the paperwork together. Unfortunately, geography often makes this difficult, as the parties are not

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1 Except the obligation to pay for the asset and the right to annul the sales agreement without the leasing company’s consent.

2 Penalties and fines can be expressed either as a fixed sum or as a percentage of the total contract value, the cost of the leased asset, etc.

3 Current legislation gives the parties considerable freedom to determine the procedures for transferring and receiving the leased asset.
situated in the same region. Therefore, when considering whether to have all three parties sign the transfer documents, one has to consider both the positive effects (e.g., the ability to resolve certain problems during the process of transferring the asset) and the negative effects (e.g., added time and expense).

If the parties agree to draft and sign the transfer documents together, the lease agreement should stipulate not only who will take part, but also the consequences for failing to turn up at the designated time and place. Thus, the lease agreement might give the lessee the right to draw up the formal acceptance documents unilaterally if the other parties fail to appear. Alternatively, the date of acceptance might simply be postponed.\(^4\) In any case, it would make sense to stipulate the lessor's liability for failing to appear.

One question that often arises is the appropriate time frame for signing the formal acceptance documents after the leased asset has been delivered. Current legislation does not provide any useful guidelines, so it is up to the parties to reach an acceptable agreement. The model lease agreement for a fully depreciable leased asset\(^5\) stipulates that the transfer papers must be signed within 30 days of delivery. In our opinion, this time frame cannot be applied universally. For some types of assets, the period is unjustifiably long; for others, such as high-tech equipment, the period does not give the lessee enough time to evaluate the quality of the asset.

The schedule for signing the delivery record for the leased asset should be determined on a case-by-case basis, depending on the specific characteristics of the leased asset and the parties' abilities to visit the delivery site. One should also bear in mind that delivery can take a considerable amount of time if the leased asset needs to be assembled or installed. The leasing company and the vendor will not wish to prolong the overall delivery period substantially, but it might not be feasible to speed up the assembly and installation; therefore, the lessee and the leasing company might want to agree on separate periods for the physical delivery of the leased asset and its final readiness (after assembly, installation, etc.).

As we noted above, all three parties have a vested interest in the proper delivery of the leased asset. But the legal relationships between the parties are defined under two separate agreements. The parties must therefore make sure that these two agreements, the lease agreement and the sales agreement, contain the same provisions for transferring and delivering the leased asset.

**Insuring the Leased Asset**

Lease agreements very often stipulate that one of the parties must insure the leased asset. We devoted an article to this subject in a previous issue of the Leasing Courier.\(^6\) Here we shall only discuss the process of negotiating the terms.

According to current legislation, the leased asset may be insured by either the lessor or the lessee. But no matter who assumes this responsibility under the lease agreement, the lessee must remember that insuring the leased asset is as much in his own interests as in the lessor's. Article 669 of the Russian Civil Code stipulates that the lessee normally assumes liability for accidental damage or destruction. Therefore, insuring the leased asset protects the lessee from possible losses.\(^7\)

Once you have decided to insure a leased asset, you must clarify the following points:

- Which party will take out the insurance policy? In deciding this issue, one should consider each party's ability to pay insurance premiums and to include these premiums in their production costs.
- Which party will be the beneficiary? This should depend on which party will be responsible for restoring the asset if it is damaged.

\[^4\] The transfer cannot be postponed indefinitely, however, so the parties should agree on a final date, after which the lessee has the right to effect transfer unilaterally.


\[^6\] See LC#5 (1999), pp. 27–28.

\[^7\] Insurance is particularly important in the case of automobile leasing.
• Which insurance company will the parties use? Very often, the party that assumes responsibility for insuring the leased asset also chooses the insurance company. At the same time, he must obtain the other party's written approval of his choice. In practice, this arrangement often leads to conflicts and misunderstandings. In our opinion, it would make more sense for the parties to indicate the name of the insurer within the lease agreement itself.

• What are the terms for notifying the other party once the insurance policy has been signed? Since both parties have a vested interest in insuring the leased asset, the lease agreement should require the insured to provide the other party with a copy of his insurance policy.

• The lease agreement may contain other important provisions, such as responsibility for future insurance payments, consequences of payment delinquency, etc.).

Having a Valid Leasing License

One of the most important advantages of leasing is that it allows both the lessor and the lessee to claim certain tax benefits. However, the tax authorities will not be able to grant these benefits unless the lessor has a valid leasing license. Since leases tend to be fairly long-term, while licenses are only issued for a limited period, there is a high probability that the leasing company's license will expire at some time over the course of the lease.

Imagine, for instance, that a lease agreement was signed on February 1, 1999. The leasing company obtained its leasing license on May 1, 1997, valid through May 1, 2001. The lease agreement was signed for a three-year term, expiring on January 31, 2002. Thus, the leasing company's license does not cover the entire term of the lease. In order for both parties to be able to claim their tax benefits between May 1, 2001, and January 31, 2002, the leasing company will have to extend its license on time.

In order to make sure that he will not lose his tax benefits, the lessee might want to require the lessor to extend his leasing license by a certain date (for example, no later than 30 days before his current license expires). The lease agreement should stipulate the consequences for the leasing company if it fails to obtain a new license on time.

In the next issue, we will look at more standard provisions that demand the lessee’s special attention.

Since the founding of the Leasing Development Group, we have been asked to help with local investment projects or provide information about other organizations that support private enterprise in Russia. We have therefore decided to start publishing information in the Leasing Courier about Western aid organizations. In this issue, we present the Eurasia Foundation:

THE EURASIA FOUNDATION
PRIVATE ENTERPRISE DEVELOPMENT

Alan Moseley
Outreach Coordinator, Eurasia Foundation

Private enterprise serves as the primary engine of economic growth throughout the world. While the percentage of private businesses in the economies of NIS countries has grown significantly over the past decade, this transition is not yet complete. New and aspiring entrepreneurs still need support and assistance in establishing and operating their businesses. The Eurasia Foundation’s private enterprise development program supports projects that meet these needs, specifically by improving business practices, increasing access to capital,
and reducing legal and regulatory barriers to business development. Given the great potential of small and medium-sized enterprises to spur economic growth, the Eurasia Foundation places priority on projects targeting this sector of the economy.

**Improved Business Practices**

Establishing and running a successful business takes more than just a good idea - it requires leaders with management, marketing, finance, planning, accounting, and other critical skills. The Eurasia Foundation seeks to meet the demand for such skills by supporting the creation and development of high-quality, sustainable business training and education programs that provide students, entrepreneurs, and business leaders with the skills they need to transform their ideas into successful enterprises. In addition to building skills, the Foundation promotes ethical practices in business and sound corporate governance.

**Increased Access to Capital**

Entrepreneurs also need access to capital to establish and develop their businesses. In Russia, the acute shortage of capital is one of the biggest obstacles to the development of private enterprise. To increase the amount of capital that is available, the Eurasia Foundation supports the creation and expansion of financially sustainable credit mechanisms aimed at micro, small and medium businesses, both through existing banking systems and through innovative mechanisms, such as micro-lending programs, equity funds, credit unions, and savings and credit associations.

**Reduced Legal and Regulatory Barriers to Business Development**

Given the potential of central and local governmental policies to directly impact private sector development, the Eurasia Foundation supports projects aimed at creating a more favorable legal and regulatory environment for the growth of private enterprise. Projects aimed at reducing regulatory barriers, improving protection of economic rights, or developing more efficient mechanisms for resolving disputes fall into this category. The Foundation also promotes tax policies that enhance growth in the small business sector and regulations that enable credit mechanisms to

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**The Eurasia Foundation**

The Eurasia Foundation was incorporated in 1993 with the goal of aiding the development of democratic and market institutions in the Commonwealth of Independent States. In working toward this goal, the Eurasia Foundation recognizes that the spread of democratic values and market principles depends on well-functioning governments, social organizations and commercial structures. Therefore, the Foundation seeks to develop local organizations that help local citizens become active participants in the political and economic life of their countries. At the same time, the Foundation tries to build solid partnerships between these organizations and their counterparts in other democratic countries.

The Eurasia Foundation currently operates through a network of offices located in Almaty, Baku, Washington, Vladivostok, Yerevan, Kiev, Moscow, Saratov, Tashkent and Tbilisi, as well as through representative offices in Ashgabat, Bishkek, Gyumri, Dushanbe, Kishinev, Minsk and Yuzhno-Sakhalinsk. Through its network of offices, the Eurasia Foundation currently awards approximately 1,000 grants worth over $20 million on an annual basis. Field offices are responsible for awarding grants directly to NIS organizations. Averaging $20,000, these grants presently account for approximately 80% of the total grant dollars awarded by the Foundation.
emerge and prosper. Finally, the Foundation helps to build the capacity of business and professional associations to advocate for sound public policies.

Grantmaking criteria

The Foundation first considers the following three criteria in its review of grant proposals:

1. **Fit with Foundation Goals and Priorities.** How does the proposed effort support the Foundation’s strategic goals and regional priorities?

2. **Project Demand and Local Support.** In what way does the initiative respond to demands and needs that exist locally? What degree of local support and commitment does the initiative have?

3. **Sustainability.** To what extent is the effort locally sustainable, both financially and operationally? Will the initiative result in sustainable and positive changes that continue over time?

If the proposal satisfactorily meets the above criteria, the Foundation then applies the following considerations:

1. **Implementation Plan.** Is the strategy for achieving the goals of the initiative well developed and realistic? What barriers or risks might impede achievement of the stated goals? What steps will be taken to mitigate these risks? What external conditions are necessary for the project to succeed?

2. **Cost-Effectiveness.** To what extent is the proposed effort cost-effective? Is this the most cost-effective approach to achieve the project goals?

3. **Qualifications.** To what extent do participating individuals and organizations have the experience and qualifications needed to implement the project successfully and to manage grant funds?

4. **Outcomes.** What significant changes will the initiative produce among its beneficiaries? Has a realistic plan been developed to measure and report on these effects? What steps will be taken to incorporate these results into future decision-making?

5. **Leveraging.** To what extent does the effort leverage other resources, including contributions from other donors, project revenue, and grantee in-kind contributions?

6. **Synergy.** To what extent does the proposal complement or build upon other initiatives in the region, including those supported by the Eurasia Foundation?

For more information, please contact the Eurasia Foundation in Moscow at (095) 956-12-35.
The Tomsk Leasing Development Project was founded in September 2000 with a grant from the Moscow office of the Eurasia Foundation. The project is run by the Tomsk Regional Center for Resource Development. Its goal is to improve access for small and medium-sized enterprises to investment capital by fostering the growth of the local leasing industry.

Among its most important activities, the Leasing Development Project holds regular training seminars on the principles of leasing. The Center held its first seminar, «Leasing: A Financial Tool for Businesses», in September 2000. These seminars familiarize local businessmen with the concept of leasing and help them understand some of the legal and financial issues involved. Representatives from local insurance companies gave additional presentations on insurance aspects of leasing transactions.

Seminar participants are able to meet with representatives from a variety of leasing companies, learn about each company’s policies and ask questions about leasing deals. Not only does this allow the participants to make useful business contacts, it also gives them the opportunity to learn more about leasing directly from leasing company specialists.

In addition to the seminars, the Leasing Development Project also holds individual consultations about leasing and other aspects of running a business. The Project acts as a link between potential lessees and leasing companies. Local businessmen usually prefer to consult with the Center before approaching any leasing companies. The Center employs highly qualified specialists (economists, accountants and lawyers) who can explain the advantages of leasing, provide excellent legal advice and help lessees choose the most suitable leasing company.

Since its creation, the Center has published a series of articles in the local press about leasing and the Leasing Development Project. For example, several articles about leasing were published in the local business journal «Nashe Delo.» The Center has also established a web site (http://leasing.stkm.ru) that gives additional information about leasing in the Tomsk region.

Over the last few months, the Center’s specialists have been gathering and analyzing data about the local leasing industry. It has compiled and circulated a directory of leasing companies that are active in the region. The Center has drafted a report about the state of the region’s leasing industry and problems that hinder its growth, and has also put forward a set of proposals on how to solve these problems.

The Center plans to continue its program of seminars, round tables and consultations on leasing. In April 2001, it will launch a new series of seminars for the local timber industry with support from the Tomsk regional government. The Center also plans to hold a joint seminar with the IFC Leasing Development Group. This April, the Center will publish a textbook for lessees that will include materials from past seminars.
LEASING LICENSES

As of March 19, 2001, the new licensing agency for leasing companies is the Russian Ministry of Trade and Economic Development. The Ministry receives applications on Tuesdays and Thursdays from 10:00-16:00 by appointment only. To make an appointment, call the Ministry's Moscow office at (095) 209-8423, 209-8943 or 209-8504.

Applications are also accepted by mail. Send documents to the Russian Ministry of Trade and Economic Development [Ministerstvo ekonomicheskogo razvitii i torgovli RF], 125818, GSP, A-47, ul. Tverskaya-Yamskaya 1-3.

The Ministry of Trade and Economic Development will not consider applications that were submitted to the Ministry of Justice's State Registration Chamber. If you have already filed an application with the State Registration Chamber, you will have to resubmit your documents to the Ministry of Trade and Economic Development.

LEASING IN CHUVASHIA

The Chuvashia Small Business Leasing Company and Chuvashkreditprom Bank have agreed to work together to finance leasing projects in the region. The two companies signed an agreement in the city of Cheboksary on March 5, 2001. The IFC helped organize a press conference devoted to this important agreement.

The agreement represents an important step in the development of the region's economy. This kind of cooperation will help spur growth in the region's leasing industry, which will benefit local enterprises and suppliers in addition to Chuvashkreditprom Bank and its leasing partner. Leasing will enable local firms to obtain new equipment and machinery with relatively small amounts of capital. Local equipment manufacturers will be able to use leasing as a valuable sales tool. The leasing company will be able to expand its portfolio, while the bank will be able to increase its turnover without subjecting itself to the high risks associated with ordinary loans.

The Chuvashia Small Business Leasing Company was incorporated in June 1998 with financial support from the Chuvashia Foundation for the Support of Small Enterprise. Over the last three years, the company has earned a reputation among regional enterprises as a reliable and effective supplier of modern equipment. The company initiated talks with the commercial bank Chuvashkreditprom in the interest of expanding its leasing portfolio. The two institutions reached a long-term agreement to finance leasing projects in the region. According to the agreement, the leasing company will select promising projects and conduct a preliminary analysis. The bank will then decide, on the basis of the leasing company's evaluation, whether or not to finance a given project. The bank and the leasing company are expected to sign a credit agreement for 500,000 rubles in the near future. The leasing company plans to use this loan to lease new equipment to Telefonstroy Manufacturing and Construction Company.

1 For more information about the Chuvashia Small Business Leasing Company, see Leasing Courier #9–10 (2000).
Telefonstroy is a major cable television provider in Chuvashia. It specializes in manufacturing and installing telecommunications networks and electricity grids. A projected one million-ruble lease will enable Telefonstroy to acquire much-needed cable-laying equipment. In the future, the Chuvashia Small Business Leasing Company plans to lease three kinds of equipment to Telefonstroy: receivers for satellite television, cable-laying equipment and home-viewing equipment. This means that television viewers in Chuvashia will finally have access to a wide variety of quality programming. We will provide more information about Telefonstroy in a subsequent issue of the Leasing Courier.

The deal with Telefonstroy is only the first in a series of planned projects, as the agreement between Chuvashia Small Business Leasing Company and Chuvashkreditprom Bank allows both parties to expand their clientele substantially. Future leasing projects include motor vehicles for Mekhovshchik, a regional furrier, and cash registers for Municipal Trading House #55.

In the hope that leasing will help spur economic growth in the region, the government of Chuvashia is doing everything it can to support the local leasing industry. Several government officials gave speeches at the press conference, including representatives from the regional Ministries of Finance, Economics, Industry, Agriculture, Business Development, Trade and Rural Crafts. The speakers noted that most enterprises in the region badly need new equipment, and that leasing, as a financial tool, would bring much-needed capital to the region’s manufacturing sector. If the region succeeds in developing its leasing market, it will become much more attractive for both domestic and foreign investors.

State Duma Deputy Anatoly Aksakov, who helped draft the recent bill of amendments to the Federal Law on Leasing, also took part in the press conference. He explained how the legislative branch was working to improve the Law on Leasing and bring it into line with other Russian laws and international agreements. Deputy Aksakov emphasized that “stimulating the leasing industry in the regions helps domestic producers modernize and expand their facilities and develop more competitive products, which in turn helps Russia integrate with the world economy.”

The IFC Leasing Development Group considers the latest agreement between Chuvashkreditprom Bank and the Chuvashia Small Business Leasing Company a positive continuation of work that was actually begun in 2000. The Group held a seminar on «The Principles of Leasing» in the city of Cheboksary last December with support from the government of Chuvashia.

The Canadian Business Association Visits Russia’s Northwest Region

The Canadian Business Association sent a trade delegation to the city of St. Petersburg in late March 2001. This is the second time of late that a Canadian business delegation has visited the region. The visit included meetings with Russian businessmen and local officials, as well as a presentation on financial leasing by the IFC Leasing Development Group and a round-table discussion on the investment climate of the Northwest Region.

The IFC Leasing Development Group’s presentation on «Leasing in Russia» featured a speech by Project Manager James Gorham. Mr. Gorham noted that Russia’s leasing industry remains underdeveloped. Although the industry has grown in absolute terms over the last five years, it still comprises no more than 1.5% of total investment in Russia. To date, more than 2,000 companies have received Russian leasing licenses, but only some 500 of these firms are actively engaged in leasing. In the city of St. Petersburg, 66 companies have received leasing licenses, of which nine are currently active. Interestingly, Russia’s oldest leasing company, Baltic Leasing, was founded in St. Petersburg ten years ago. Today, the city’s leasing
companies are supplying a wide range of equipment using financial leasing, including manufacturing, construction, medical, shipbuilding and food-processing equipment, motor vehicles, etc. Leases vary from two- to five-year terms, with contract values ranging from $10,000 to $500,000.

Last year saw the creation of the St. Petersburg Association of Leasing Companies, whose goal is to improve the local investment climate through consulting and legislative activities. The non-profit organization includes St. Petersburg's major leasing companies, banks and insurance companies.

The St. Petersburg city government has already implemented a variety of regulations to stimulate the local leasing industry. It has amended the city's Law on State Support for Investment in St. Petersburg and the Law on Tax Benefits to create a more favorable tax climate for leasing as a form of investment. The government of the Leningrad Region is currently drafting a new Law on Leasing that would improve the existing legal framework for leasing and, at the same time, introduce new tax benefits and state guarantees for leasing transactions.

In summarizing the Canadian delegation's visit to the region, Linda MacDonald, the Canadian Consul-General in St. Petersburg, noted that the local investment climate has improved considerably in recent years. However, the region still needs to «promote» itself, she said, adding that a number of Canadian firms are beginning to take a serious look at St. Petersburg as a possible place to invest. Canada's Chisholm, a major exporter of meat and dairy products, has already invested $4 million in a refrigerated warehouse on Valdai. According to Consul-General MacDonald, «this kind of cooperation benefits both Russia and Canada.»

Natalya Ivanovna Kichko
Director
Tomsk Leasing Development Project

STATE DUMA WORKING GROUP FOR IMPROVING LEASING LEGISLATION

As our readers may recall, the State Duma held a session on October 3, 2000, devoted to the development of leasing in Russia, during which it decided to create a working group to improve Russia's legislation on leasing. The group is composed of State Duma deputies and representatives of the relevant ministries, as well as leasing company directors and prominent academics. State Duma Deputy Anatoly Aksakov was selected to chair the group.

Since its creation, the working group has come up with a variety of proposals for improving current legislation and has also drafted several new leasing laws that are currently being debated in the Duma. Some of the group's most notable achievements include:

• A bill of amendments to the Federal Law on Leasing. The group submitted the bill to the State Duma in April of this year. The bill brings the Law on Leasing in accordance with the Russian Civil Code and other laws, as well as introducing several new leasing regulations.

• An analysis of the Russian Civil Code's chapter on profit tax, including the bill of amendments proposed by the State Duma in March of this year, as well as a set of recommendations on tax policy that could spur the growth of leasing in Russia. The group's recommendations include retaining accelerated depreciation for leased assets, preserving the right to record a leased asset on either the lessor's or the lessee's balance sheet, and making it easier for leasing companies to include interest payments in their production costs.

The group plans to continue its work as these important bills make their way through parliament and new leasing regulations are introduced.
HOW LEASING COMPANIES CAN MINIMIZE RISK BY CONDUCTING A THOROUGH ANALYSIS OF POTENTIAL LESSEES:
Analyzing a Lessee’s Current Finances and Projected Cash Flow

Elena Degtiareva
Financial Analyst
IFC Leasing Development Group

In this article, we continue our discussion of how leasing companies can minimize their risks, which began in Issues 9–10 (May–August 2000). In previous articles we looked at ways of minimizing risks associated with the leased asset itself and at strategies for building a solid lease portfolio. Now we turn to methods of evaluating a potential lessee.

The Main Components of a Financial Analysis

Evaluating a potential lessee is one of the first steps in deciding whether or not to invest in a particular project. The process of evaluating a lessee can essentially be divided into two components:
- An analysis of the lessee’s current financial condition (the past)
- An analysis of the project’s potential (the future)

Depending on the amount of funds involved and other factors, leasing companies may require potential lessees to submit detailed business plans, demonstrating the feasibility of their projects, or they may simply ask for essential financial data. In either case, the leasing company must conduct its own, independent analysis of the lessee and his proposal, using the lessee’s own documents for comparison only.

Analyzing a Lessee’s Financial Condition

Analyzing the lessee’s financial condition means evaluating how the company has performed to date. It includes analyzing the lessee’s profitability, liquidity, financial stability, management of working capital, etc. All of these factors must be studied as a whole and individ-
ually in order to get a clear picture of the company’s financial trends and outlook. This analysis should not be limited to a simple calculation based on standard indicators. The leasing company should integrate all of the available data and try to understand how it has evolved over time. We shall write in more detail about the methods of analyzing and interpreting quantitative data later. First, we shall explain why it is necessary to evaluate a potential lessee’s current finances.

The Main Goals of a Financial Analysis

Analyzing a potential lessee’s current finances enables the leasing company:

• To uncover negative trends in the lessee’s business activities
• To verify financial data supplied by the lessee
• To predict the lessee’s future cash flow

The most important reason for analyzing the lessee’s financial condition is to determine whether the company will be able to meet its lease payments and whether there is a serious risk of default. Negative financial indicators may serve as sufficient grounds for rejecting a potential lessee, in which case the leasing company does not need to make any further calculations. The importance of evaluating the lessee’s past and present finances cannot be overstated, as the success of the proposed project will largely depend on the lessee’s financial stability. This is especially true if the leased asset constitutes an essential and inseparable part of the lessee’s enterprise. Furthermore, the financial analysis will enable the leasing company to judge whether the lessee’s projections of future cash flows are realistic. The leasing company should compare the lessee’s current sales figures, transitional and regular expenses, and relationships with suppliers and customers (consistency of deliveries and payments) with the figures that the lessee has forecast in his business plan. If there are any large discrepancies between the lessee’s current performance and forecasts, they must be explained and justify them thoroughly. Acceptable forms of proof may include signed agreements with new suppliers and distributors, market research, etc. The lessee’s quantitative indicators, such as turnover, current expenses, working capital, etc., can be used to verify not only the starting figures reported in his business plan, but also forecasts about future cash flow. If the proposed project is not an independent commercial unit, but is inextricably linked to the lessee’s operations, the leasing company must be sure to evaluate the lessee’s current cash flow as an indicator of the project’s future solvency. This is especially true if the project is small in comparison with the lessee’s total operations. In such cases, income generated through the project will not be the lessee’s only source of revenue from which to make the lease payments. However, if the lessee is already operating at a loss, he may use the income generated by the leasing project to fund his other activities.

Of course there are cases where it is not really necessary to analyze the potential lessee’s current finances. This is true, for example, when the project involves the creation of a new and independent company, or when the amount of investment and expected turnover far exceed the enterprise’s current assets and turnover. In such cases, the lessee will obviously not be able to provide sufficient guarantees on the lease, and some additional form of collateral, such as a bank guarantee, will be required. This means that rather than evaluating the lessee, the leasing company will have to analyze the guarantor.

The Main Sources of Information for a Financial Analysis

The financial analysis of a potential lessee should be based on accounting documents, credit history, bank statements, tax reports, etc. As everyone knows, a Russian company’s accounts do not necessarily correspond to reality. Therefore, one must be very careful about drawing important conclusions based on formal indicators. However, by analyzing a company’s accounts over the past several years (leasing companies usually require accounting records from the last three years) and comparing the data from different periods, you can trace the basic
development of the company's business. By comparing important indicators, you can deduce the original data, and by substituting real market values, you can correct many of the figures. In other words, a leasing company can get a fairly accurate picture of a potential lessee's finances by scrutinizing the accounts and comparing them to external data.

Evaluating the Feasibility of a Project

The second important component in evaluating a potential lessee is analyzing the project's feasibility. The method for carrying out this analysis will depend on the nature of the project (i.e., whether it involves creating new production facilities, expanding existing facilities, modernization, etc.). In any case, the evaluation should be based on the project's predicted cash flow. Leasing companies should keep the following principles in mind when predicting the future cash flow of a potential leasing project:

- Make an accurate calculation of all previous revenue and expenses associated with the project
- Consider fluctuations in payments over time
- Plan through the end of the lease term and break the forecast down into payment periods in accordance with the lease payment schedule
- Make sure that the currency used in the calculations corresponds to the expected currency of the lease payments.

A project is considered viable if it is:
- Financially solvent
- Profitable
- Not susceptible to high risks

Important Aspects of Evaluating a Project

1. Analyzing the project's solvency. How liquid is the project? In other words, will it be able to meet all of its financial liabilities (payments) at every stage of its development?
2. Analyzing the project's feasibility. Will the project provide a sufficient return on investment?
3. Analyzing the project's risks.

In future editions of the Leasing Courier we will continue to look at how analyzing a potential lessee can help a leasing company minimize its risks. In the next issue we will take a closer look at the financial data that a leasing company should use in its calculations.

A SUCCESSFUL SUPERMARKET IN NOVOCHEBOKSARSK, CHUVAShIA

Continued from pg. 1

first heard about leasing five years ago,» began Ms. Kosikhina. «At that time I was working for another store, very similar to Trading House #55. Our business was just scraping by, and we really needed extra capital in order to expand. The newspapers had been publishing articles about leasing, so I asked the owner what he thought about taking out a lease on some new equipment. He was very skeptical about it and said that he couldn't see any possible advantage to leasing. In those days, it's true, leasing companies were offering very unattractive terms. In the end, the owner decided to take out a bank loan, which, as far as I know, he is still paying off to this day.»

Two years ago, Olga Kosikhina became the director of Municipal Trading House #55. When she first arrived, the store was a run-down affair with annual profits of 8,000 rubles. Working capital was totalling only 90,000 rubles, and the store urgently needed new equipment and major renovations. Olga Kosikhina looked through her folder of newspaper clippings and found an advertisement for the Chuvashia Small Business Leasing Company.

Without a moment's hesitation, she made an appointment with the company's director, Oleg Nikolayev. First they talked about the concept of leasing in general, as Olga Kosikhina had only a
vague understanding of it. They then worked out two separate leasing plans and signed an agreement. «The plans were very convenient,» explained Olga Kosikhina. «Leasing was the only way for us to acquire new equipment under the circumstances. Investment loans would have been almost impossible to find, and even if we had been so lucky, we would never have been able to handle the interest payments.»

The new partners began by re-equipping the store’s cafeteria. They wanted to complete the work before the summer tourist season began, as the store was situated in a densely populated area next to a summer resort. If the cafeteria could be ready in time for the summer tourists, it was expected to turn a profit very quickly. Olga Kosikhina used the store’s working capital to renovate the cafeteria, and the Chuvashia Small Business Leasing Company provided an icebox, mixer, grill, tables and chairs under the first leasing plan. The equipment, which was all foreign-made, cost a total of 130,000 rubles. The lease agreement was signed in May 2000, and just 30 days later the cafeteria was already open for business. It was an immediate success. The grill, for example, turned out to be the only one in the city, and customers even started ordering food to go. «We were afraid to buy a large grill,» explained Olga Kosikhina. «We didn’t know how things would turn out, so we just bought a small, 8-chicken grill. Well, that was a mistake, but at least now we know that we can buy a bigger one next time.» Two months later, the Chuvashia Small Business Leasing Company provided Trading House #55 with some stands and a counter worth another 40,000 rubles. The store began to offer its customers a wide selection of beverages, snacks and pastries. The leasing company also provided an Italian slicer, which raised the store’s quality of service.

The lease was originally signed for a one-year term, but Trading House #55 managed to complete its lease payments by January 2001, and by March it had acquired full ownership of the equipment. Except for one short delay in January, when Trading House #55 was forced to replace its accountant, the store made all of its lease payments on time. Olga Kosikhina plans to work with the leasing company in the future, so she was very careful to fulfill all of the terms of their agreement. Over the last year, the store has managed to increase its working capital to 300,000 rubles and take on seven new employees.

Ms. Kosikhina’s predecessors had considered the store’s spaciousness a disadvantage. The premises are indeed quite large, with a total area of 2,037 square meters. The shop itself measures 576 square meters. But Olga Kosikhina sees this as an opportunity. The grocery store is absolutely essential to its densely populated, residential neighborhood, so there will never be a shortage of customers. The trick is to make the store as convenient as possible for them.

Renovating the cafeteria turned out to be a good test of the company’s ability to use a leasing plan effectively. Now that she has some experience, Olga Kosikhina plans to use leasing to modernize the rest of her store. «First we’re going to lease some new shop equipment. We need some new stands, some refrigerated shelves and a new meat cutter to replace our antique ax. We’re also investing a lot into renovating our building. Since it was first opened 18 years ago, the shop has never undergone major renovations. We have a dark interior, dark tiles and a crumbling facade. We want to make the place more cheerful.» After the renovations are complete, the store will be able to expand its selection of goods. By acquiring the new equipment under lease, the store will still have plenty of working capital left over. Most important, it will be able to achieve all of its goals (renovation, modernization and expansion) at once, without having to close down the shop in the meantime.
As we concluded our interview with Olga Kosikhina, we asked her whether it was hard to be a female entrepreneur in Russia. After all, she has already managed to accomplish a great deal, and it looks as though she is far from finished. «Anyone who is willing to work hard can achieve,» she said. «It doesn’t matter if you’re a man or a woman. When I was working for the other store, the owner simply couldn’t understand the advantages of leasing, and he probably never will. One has to be willing to take on responsibilities and, at the same time, to make realistic plans for the future. At Trading House #55, we have had our ups and downs, but we have never stopped moving forward.»

Viktoria Struts
PR Specialist
IFC Leasing Development Group

PRESS DIGEST

RECENT EVENTS IN THE RUSSIAN LEASING INDUSTRY

A vanguard Bank is planning to invest in the Russian gold mining industry. Avangard, which has traditionally specialized in gold mining, is prepared to invest up to $25 million in Russian gold mines this year. The bank has already signed several leases, worth a total of $2-3 million, for terms of three to four years. It plans to sign more deals later this year. The bank’s specialists are currently considering several investment projects in Kamchatka, Irkutsk, Magadan and Yakutiya.

Noble Metals Market News
February 1, 2001

T he government of Smolensk has approved various measures to support local agriculture in the year 2001. Local farmers will receive 21.9 million rubles in emergency relief. Ten million rubles will go towards repaying interest-free loans received in 2000 for fuel purchases, while the remaining 11.9 million rubles will be used to repay tied credit granted in 1995. The Republic of Belarus will repay its natural gas debts by leasing 1.5 billion rubles worth of farming equipment to the region. State-owned Rosselkhoz Bank [Russian Agricultural Bank], whose charter capital is expected to reach 2 billion by the end of the year, will help finance the region’s farmers. Rosselkhoz Bank will also lead an initiative to create a network of farmers’ credit unions, develop agricultural insurance and provide loans to private farmers. The region also plans to stimulate agricultural leasing with the help of the State Leasing Fund. Last year, 30-40% of the region’s new equipment was acquired under lease. The federal government has promised to invest 3 billion rubles in 2001 to help farmers lease new equipment.

Rabochy put (Smolensk),
February 8, 2001

T he government of the Moscow Region has finalized its plans to lease pedigree livestock and agricultural machinery to regional farmers. The region is prepared to invest 39 million rubles at 3% APR in agricultural machinery and poultry farm equipment. The lease terms will range from 2 - 5 years, depending on the value of the leased assets. Lessees will be required to make 20% down payments on any equipment valued at less than 50,000 rubles, 10% on equipment worth more than 50,000, and 20% on livestock. Lessees will also be required to insure all leased assets.

RIA Novosti
February 13, 2001

S tate-owned Rosselkhoz Bank plans to establish a leasing subsidiary, Rosagro Leasing, with 500,000 rubles in charter capital, announced the bank’s public relations man-
The Okulovsky Bumazhnik Company of Novgorod has launched a new paper recycling line capable of processing up to 35 tons of paper per day. The company is leasing the $200,000 equipment through Rosmark-SI of St. Petersburg. The new machinery will enable the company to reduce its production costs considerably.

The municipal government of Yakutsk has taken out a lease on 20 new ambulances. Sixteen of these vehicles will be equipped with cardiographs, tonometers and specialized stretchers. The remaining four will contain drug-administering equipment, laryngoscopes and other high-tech equipment.

According to Vyacheslav Sokolov, deputy director of the Center for Investment Market Research, the total volume of investment in Russia should rise by 17-20% this year. Mr. Sokolov announced these figures at a round-table discussion on leasing at the Executive Committee of the CIS. Mr. Sokolov explained that in developed economies, leasing accounts for some 30% of total investment, while in Russia it comprises no more than 1-1.5%. He added that leasing is an essential driving force behind investment in the West. Therefore, he explained, it is imperative that the governments of the CIS countries take active measures to support their local leasing industries. State guarantees would dramatically increase the number of leasing projects in the CIS and attract more foreign lessors, he said.

Russia’s Atlant-Soyuz Aviation has announced its intention to lease ten new Il-96-300-T’s and four new Tu-203S’s. According to Atlant-Soyuz’s general director, Stanislav Leychenko, the company has already signed an agreement with Ilyushin Finance Leasing Company. The contract is valued at around $450 million. «The aircraft will be manufactured at the Voronezh and Ulyanovsk Aviation Plants and equipped with Russian PS-90A engines and Russian electronics,» said Mr. Leychenko.

«This is the largest order for Russian-made aircraft in the last ten years. You might say it’s the ‘deal of the century.’» The first planes will be delivered within 22 months.

The Liksi Sugar Factory, located in the Voronezh region, is in the process of assembling its new German production line, valued at $1.5 million. The factory will switch over to new production methods this April. The restructuring should enable the factory to boost its output, improve the quality of its sugar, and reduce its production costs and energy bills. The new equipment was acquired under a three-year lease.

Pulkovo Aviation, Rossiya Travel, the Gorbunov Aviation Plant (Kazan) and the International Bank of St. Petersburg signed a protocol on March 11 to form a new aviation consortium. The consortium unites several companies that have a vested interest in reviving the Russian aviation industry. The airlines hope to expand their services by acquiring new, Russian-made aircraft that comply with international standards. For the International Bank of St. Petersburg, joining the consortium was a natural and logical step, since Pulkovo and Rossiya are two of its most important clients. The bank, which already has considerable experience with such industrial groups, will finance the consortium’s investment projects, including leasing plans.

Ever since they signed a partnership agreement in 1999, the republics of Karelia and Belarus have steadily increased their
economic, scientific and cultural ties. Belarus's Belrusavto continues to lease equipment to Karelian logging companies. The Onezhsky Tractor Plant now uses up to 10 million rubles worth of Belorussian components monthly. Onezhsky recently tested a new tractor engine from the Minsk Motor Plant and has already signed a preliminary agreement for a shipment of the engines.

Severny Courier (Petrozavodsk)
March 16, 2001

St. Petersburg's Silovye Mashiny Group has signed a partnership agreement with Rosbank and Vneshtorg Bank. Silovye Mashiny includes some of the largest manufacturers of power-generating equipment in the CIS: The Leningrad Metal Factory, Elektrosila, The Turbine Blade Factory and Energomashexport. The agreement calls for improvements to the companies' international and domestic payment systems, funding for modernizing their facilities and expanding their sales networks, financing for their current export and import operations, and increased coordination on joint investment projects. The signatories will be able to invest available capital in the Russian power-generating equipment industry through newly opened credit lines and syndicated loans. Rosbank has signed a five-year deal to help the manufacturers modernize their plants. In particular, the bank will evaluate their investment projects, monitor their use of funds, act as a guarantor, set up a leasing program for the plants' power-generating equipment, attract investors and form an investment consortium for joint ventures. Working with Vneshtorg Bank will give the industrial group access to the bank's broad network of foreign and domestic subsidiaries, as well as the services of the leasing company Evrolizing GmBX. Vneshtorg Bank will also be able to provide the group with bank guarantees on international tenders and export contracts.

Rosbalt Information Agency
March 20, 2001

The Leningrad region will receive 130 million rubles for equipment leases this year. The regional government has already received 20 million rubles, and an additional 110 million will come from the federal treasury in 2001. According to the regional government's press service, the region has leased 1,080 pieces of equipment since its leasing program was founded seven years ago. The program favors agricultural producers that provide a good return on its investment. First in line this year are the region's dairy suppliers; they will receive new milk tankers this year. The demand for tankers has grown, as the region's dairy production has surged to 20 tons of milk per day. Last year, the leasing program helped farmers in the remote areas of Podporozhe, Tikhvin, Slantsy, and Lodeyiopol. The region plans to secure these leases by requiring the lessees to make payments in kind.

Vesti (St. Petersburg)
March 27, 2001

Altay Agropromsnab was declared the most successful supplier of agricultural equipment, spare parts and raw materials at an interregional seminar devoted to preparing for this year's sowing season. Vladimir Yesionov, deputy director of Rosagrosnab, made this announcement during his speech to the assembly. Last year, farmers in the Altay region received 406 million rubles worth of new equipment and raw materials, almost 40% through dealership agreements at discounted prices. The farmers were able to lease 130 new grain harvesters, 173 tractors, 41 fodder harvesters, 60 harvester attachments and other equipment worth a total of 249 million rubles. The government of Altay has earmarked an additional 150 million rubles this year to finance leases in the region.

Altayskaya Pravda (Barnaul)
March 27, 2001

The capital growth rate among St. Petersburg's banks last year suggests that the local banking sector is sufficiently liquid. Since 1998, the total volume of registered charter capital among St. Petersburg's banks has grown 5.2 times to 2.86 billion rubles (as of January 1, 2001). Further evidence of the banks' good financial health is the fact that 80% of them are currently profitable. Many of the banks have expanded to include new kinds of services. Most important, considering the high demand for new equipment in the region, the banks have begun to expand their leasing programs. Inkas Bank has opened a third leasing subsidiary to handle the growing demand for leasing services.

Delovoy Peterburg (St. Petersburg)
March 29, 2001
Atlantic-Soyuz Aviation and Ilyushin Finance Leasing Company have signed an agreement to equip II’s 92-ton-capacity aircraft with Russian-made engines and electronics instead of American imports. The new planes will cost half as much as the current 96-T series and only one-third as much as Western equivalents. The planes will be assembled at the Voronezh and Ulyanovsk aviation plants.

Kommuna (Voronezh)  
March 29, 2001

Two of Russia’s large, state-owned banks, Vneshekonom Bank (VEB) and the Russian Development Bank (RBR) have announced their intention to create leasing subsidiaries. Another state-owned bank, Rosselkhoz, already opened a leasing subsidiary this February. The combined turnover of Russian leasing companies reached 17.5 billion rubles last year. More than half of this sum was invested in high-tech and manufacturing equipment. It is no surprise that state-owned banks are taking an interest in leasing, since several of them, such as VEB, work with high-tech firms in the military-industrial complex and the automobile industry. The chairman of VEB, A. Kostin, announced that his bank intends to create a universal leasing company with $10 million in charter capital. The company will likely be called Vneshekonom Leasing. Rosselkhozbank is planning to launch a new investment program this April with funding of up to 900 million rubles. The winning contractor was the Tyumen Agricultural Leasing Company.

Tyumenskiye Izvestiya (Tyumen)  
March 30, 2001

Minister Ilya Klebanov pointed out that Russian airlines, which currently have no choice but to use obsolete technology, will suffer next year when the European Union begins to enforce a ban on outdated aircraft. Even if Russia’s aviation companies tried to modernize their planes, they would not be able to bring more than 25% of them into compliance with the new European regulations. This is why the government has decided to finance leases for new Tu-204 and Tu-214 aircraft, as well as Il-96s. Tupolev is expected to come out with a new model, the Tu-334, in 2003. Mr. Klebanov added that the Ministry of Finance, Rosaviakosmos and the Ministry of Trade and Economic Development will decide in the near future how much the federal government will be able to spend on subsidized loans for Russian aviation purchases. The loans will be issued for periods of 10-12 years at 13-14% APR in dollar terms. The government will also act as guarantor on around 85% of the loans.

RIA Novosti  
March 29, 2001

The Agriculture Department of the Tyumen region has held an auction for agricultural leases to be financed by the regional government. The government awarded the contracts on the basis of several criteria: delivery terms, equipment quality, cost-effectiveness and service. The winners were the Tyumen Agricultural Equipment Supplier (Tyumenoblagropsnab) and the Tyumen Agricultural Leasing Company.

Tyumenskiye Izvestiya (Tyumen)  
March 30, 2001

The Hungarian government has decided to lease used American F-16 fighter planes to replace its aging Mig-29s. Hungary’s Minister of Defense, Szabo Janos, announced that the country would lease and renovate twenty-four F-16s over the next ten years at a cost of around $560 million. The first planes will be put into action by the year 2004. Last year, a Russo-German joint venture offered to renovate Hungary’s Mig-29s, and a preliminary agreement was reached with the Hungarian government.
but Hungary was forced to scrap the plan due to strong opposition from NATO, especially the United States.  

*Sinhua Information Agency  
February 10, 2001*

**Cyprus Airlines** has announced its intention to replace its fleet over the next two years. The company will buy two new aircraft and lease an additional two from Europe’s Airbus consortium, as well as leasing four new planes from Boeing for its subsidiary, Euro Cypria. Two new Airbus A-319-200s are scheduled to arrive in Cyprus early next year, followed by two A-330-200s and four Boeing 737-800s under lease in the year 2003. Cyprus Airlines currently has four Airbus A-310-200s, which it plans to lease out over the next two years on profitable terms.  

*ITAR-TASS,  
February 20, 2001*

**Ukrainian president Leonid Kuchma** has signed a decree on Further Measures for the Development of Agricultural Leasing in Ukraine. The decree aims to promote structural reform in Ukrainian agriculture, to create economical- ly viable farms and to stimulate competition in the agricultural equipment market. The government has been given one month to establish a national leasing company, Ukragroleasing, confirm its charter and define its principal goals. The cabinet must also compile a list of state property that will serve as the leasing company’s collateral. The government has been asked to simplify the procedures for leasing agricultural equipment under federal programs.  

*UNIAN Information Agency (Kiev)  
February 23, 2001*

**Georgia’s bus lines** will use new Swedish Tetra buses for their intercity services. The Spanish firm Oriega Brothers will lease six new buses to the Georgian companies for their long-distance routes. The specific terms of the leases will be decided later, after the buses have begun to generate profits. The agreement will help Georgia modernize its bus fleet, improve the quality of its bus service and increase customer safety.  

*PRIME NEWS Information Agency (Tbilisi)  
March 9, 2001*

The press digest was prepared by Viktoria Struts

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**QUESTIONS & ANSWERS**

**IF a trucking company has trouble meeting its lease payments, can it sublease its trucks to another trucking company? If so, how?**

According to our interpretation of Russian law, there are two ways for a lessee to transfer his rights and obligations under a lease agreement to a third party: subleasing and lease transfer.  

In either case, the lessee must first obtain the lessor’s permission before transferring the leased asset.  

Subleases are fully subject to Russian leasing laws unless otherwise stipulated by current legislation. One such exception is Article 615 of the Russian Civil Code, which stipulates that a sublease may not exceed the term of the primary lease agreement.  

If you are planning to sublease a motor vehicle, you need to give special thought to the matter of vehicle registration. According to the GIB-DD’s Procedures for Registering a Leased Motor Vehicle (05/24/00), a subleased vehicle must be registered in the name of either the lessor or the lessee. This means that the registered party will have to grant the sublessee power of attorney over the leased vehicle.  

Remember that if the lessee does sublease a vehicle to a third party, he still remains fully liable to the lessor under the terms of the primary lease agreement.  

If the lessee actually transfers his lease to a third party, that party acquires all the rights and...
What are the accounting procedures for a leaseback agreement?

Because the lessee takes on the function and status of a vendor under a leaseback agreement, he must record the sale of the leased asset to the leasing company in his accounting records. As a rule, the assets leased under leaseback agreements have already been used by the lessee. Selling such assets at any price other than their residual value will give the lessee either a positive or a negative balance.

The sale should be recorded under account 47 «Sale or Transfer of Fixed Assets»:

- D51 K62 (300): Payment for Property
- D62 K47 (300): Sale of Property
- D47 K01 (540): Deduction for Original Value of Property
- D02 K47 (360): Deduction for Wear and Tear
- D47 K68 (50): Deduction for VAT
- D47 K80 (70): Total

In all other ways, the lessee should record the leaseback agreement exactly as he would an ordinary lease. The property transfer, current operations and termination of the agreement are all recorded in the same way.

As for the leasing company, the bookkeeping procedures for a leaseback agreement are identical to those for an ordinary lease, including the purchase of the leased asset.

Under the new Tax Code, will small enterprises still be able to claim the VAT exemptions stipulated under Article 9 of the Federal Law on State Support for Small Enterprise?

According to Article 9, Clause 1, Part 2 of Federal Law 88-FZ on State Support for Small Enterprise (06/14/95), if any change in Russian tax law increases the tax burden for small enterprises, these enterprises may continue to observe the regulations that were in place at the time of their incorporation for four years (from the time of incorporation). Neither the Tax Code nor any other tax law has abrogated this right. Since the «tax break» in question (the VAT exemption) stipulated under the Law on Value-added Tax (Article 5, Clause 1, Subclause “Ya”) nearly always raises the actual costs of leasing, one cannot say that annulling the exemption will raise the tax burden. Consequently, there is no legal basis in such cases for applying Article 9 of the Law on State Support for Small Enterprise.

Nevertheless, in certain cases disallowing the VAT exemption may increase the tax burden for some small enterprises. These enterprises have every right to claim protection under Article 9 of the Federal Law on State Support for Small Enterprise. That is, enterprises that were incorporated before Chapter 21 of the new Tax Code went into effect would have the right to claim the VAT exemption stipulated under the Law on Value-added Tax until the fourth anniversary of their incorporation.

In short, small enterprises may continue to claim the VAT exemption in accordance with the Federal Law on State Support for Small Enterprise only if abolishing this exemption has increased their overall tax burden.

Elena Degtiareva
Financial Analyst
IFC Leasing Development Group

1 According to Article 11, Clause 1 of Federal Law 148–FZ on the Single Imputed Income Tax for Certain Types of Business, Article 9 of the Law on State Support for Small Enterprise does not apply to certain enterprises that pay imputed income tax.

2 See the January–February 2001 issue of the Leasing Courier (#13).
ducted under account 83 «Income for Future Periods» (assuming that the leased asset is recorded on the lessor’s balance sheet)?

The difference that the lessor records under account 83 should correspond to account 46 «Sale of Goods, Labor or Service.»

This is based on Clause 5 of Accounting Standard (PBU) 9/99 «Entities’ Income», confirmed by the Ministry of Finance’s Order of May 6, 1999 (12/30/99 edition). According to this regulation, lessors should record lease payments as income from ordinary business activities.

According to the Accounting Plan for the Commercial Activities of Enterprises and its accompanying Instruction (confirmed by USSR Ministry of Finance Order 56 of 11/01/91, 02/17/97 edition), this revenue should be credited to account 46 «Sale of Goods.»

However, we should add that according to Clause 6 of Ministry of Finance Order #15 of 02/17/97 on Accounting Procedures for Leasing Transactions, the difference recorded under account 83 «Income for Future Periods» should be deducted in accordance with the amount of profit from lease payments credited to account 80 «Profits and Losses.»

Since both of these regulations were passed by the same agency, the more recent one (Accounting Standard 9/99 «Entities’ Income») takes precedence.

Therefore, the difference recorded under account 83 should be recorded as follows:

D83 K46: Deduction for the difference between the value of the lease agreement and the value of the leased asset included in the lease payment
D46 K80: Total