

Dealing with Equipment, Vehicle and Building Leases

Many leases of equipment and vehicles are true leases, but some (for some bins for example), are actually finance contracts. When recording them in ABA, a decision will need to be made about which of these two categories they fall into.

True leases (generally called operating leases) require a scheduled payment in exchange for the use of the leased item. There is no conveyance of ownership at the end of the lease, nor does the lessee have an option to purchase the asset at a bargain price at the end of the lease. In recording this kind of lease, there will be no capture of equity in the asset as none will have accumulated. These leases will then be recorded in the Equipment Leases section at the bottom of the Machinery page. The annual lease amounts shown will then be transferred by ABA to the expense section at the bottom of the Crops production page, and will be included in projected operating expenses for the farm. The timing of the payments is dealt with on the Cash Out 2 worksheet.

Leases that are actually finance contracts (generally called capital leases) have a conveyance of the asset, or the option to purchase the asset at a low price at the end of the lease, and are used with the intention of taking ownership at the end of the lease contract. Because of these features, these leases result in an accumulation of equity, which can only be captured in a financial statement if the item is shown as an asset, and the financing arrangement being shown as a debt. If a lease is a capital lease, it is suggested that the asset be listed on the Machinery page at its market value and treated as an owned asset. The asset would then be depreciated over the asset's economic life. The lease would be set up as a loan on the Term Liability worksheet, and the Principal Outstanding column equal to the present value amount of the lease payments plus any final buy out amount, according to the terms of the lease agreement. The payment amount and frequency would be as per the lease agreement. Some of the other account parameters might need to be estimated, as the information might not be readily available.

The accountants this was discussed with indicated that it should not be assumed all arrangement called leases are true leases. We want to represent the farm's financial position as accurately as possible. In many cases, leases are, in reality debt. Not showing them as such, if they are truly debt, can misrepresent a farmer's true financial situation.