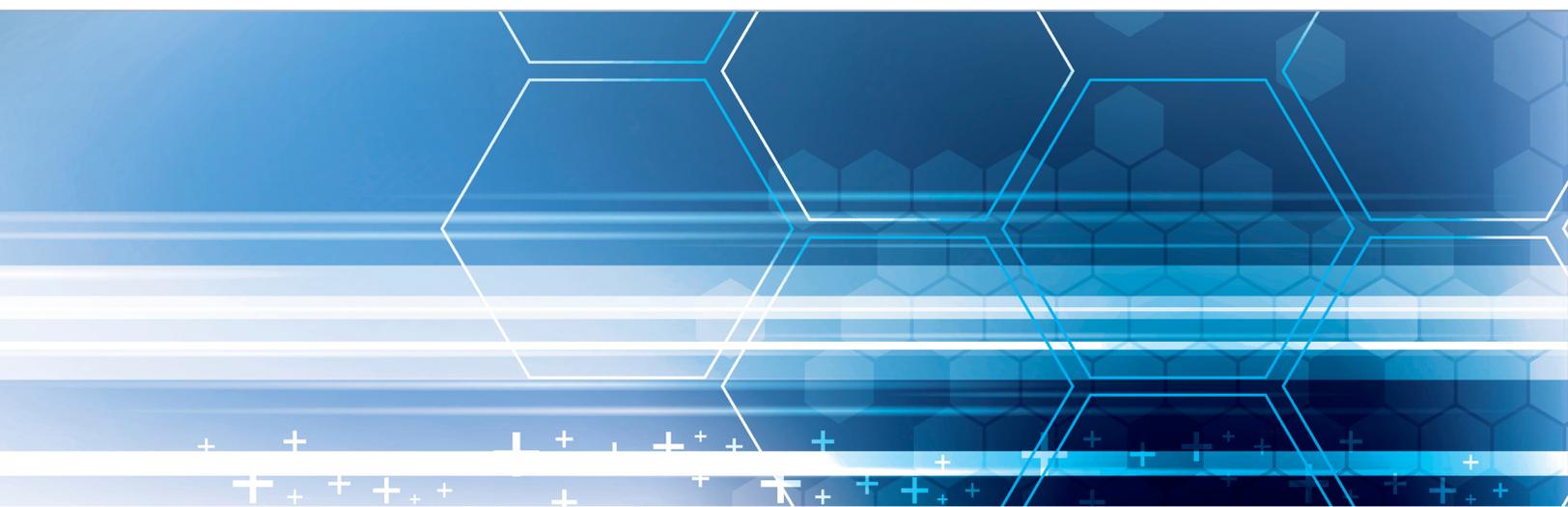


Lease Purchase



A Lease Purchases

A lease purchase is an agreement entered into by the school district to acquire a capital item without paying the full purchase cost all at once. When considering a lease purchase it is important to understand the distinction between a lease purchase agreement and a simple lease/rental contract because of the potential adverse financial impact that could occur to the district if the payments are treated incorrectly in the district's accounting system.

Distinction between lease purchase and lease/rental:

Lease Purchase:

- Agreement between the school board and a financing entity (trustee).
- Financing entity (trustee) retains title to the property until the district completes the lease purchase payments.
- All cash for the capital item is acquired, managed, and expended by the financing entity (trustee). The only entries on the district's books reflects the annual principal, interest, and fees. District does not receive or receipt cash associated with a Section 177.088, RSMo, lease purchase into the district's accounts.
- Principal and interest is paid from the Capital Projects Fund.

Lease/Rental:

- District **will NOT take title** to property.
- If district buys the item at the end of the rental and takes or assumes title to real property, the full amount expended for the real property will be deducted from the state aid payment in the year following the transfer of title to the district (per Section 177.088.11, RSMo).
- Lease/rental amount is paid from the General (Incidental) Fund.
- Included in current operating costs.

A school district has two lease purchase provisions available: Sections 177.082 and 177.088, RSMo.

Section 177.082 Lease Purchases (Provision One):

The lease purchase authorization in Section 177.082, RSMo, provides for lease purchases for apparatus, equipment (including school buses), and furnishings, directly with a vendor. This authorization does not provide for the purchase of buildings (including mobile classroom units) or land.

Section 177.088 Lease Purchases (Provision Two):

The lease purchase authorization in Section 177.088, RSMo, requires a district to enter into an agreement with a financing entity (trustee). This statutory authority is the only means a district has to enter into a lease purchase agreement for buildings (including mobile classroom units) or land.

Fund Transfer Options For Lease Purchase Payments

If a district has Section 177.088 RSMo, lease purchases entered into prior to January 1, 1997 (“grandfathered” lease purchases), the transfer authority is as follows:

A district in compliance with Section 163.031.6, RSMo, may use the Lease Purchase prior to 01/01/1997 transfer to transfer amounts from the General (Incidental) Fund to the Capital Projects Fund necessary to cover current year obligations for lease-purchase obligations entered into prior to January 1, 1997.

If a district has Section 177.088, RSMo, lease purchases entered into after January 1, 1997, and if the district is in compliance with Section 163.031.6, RSMo, the district may use the \$162,326 or 7% x SAT x WADA transfer to transfer amounts from the General (Incidental) Fund to the Capital Projects Fund necessary to cover current year obligations for lease-purchase obligations entered into after to January 1, 1997.

When a district enters into a lease purchase with a financing entity (trustee) to acquire a new building, the financing entity (trustee) will actually build and own the building for the term of the lease purchase agreement. All construction expenditures will be made by the financing entity (trustee). The school district ***will not pay any construction costs***. The local board of education may review and approve all appropriate construction invoices/bills prior to the financing entity (trustee) paying such invoices/bills. This reduces the possibility of doubling or inflating expenditures for the school district. ***Construction expenditures will not be reflected in the school district’s accounting records.***

The method of accounting for Section 177.088, RSMo, lease purchase costs are the same regardless of the district’s basis of accounting (cash or modified accrual). There has been some discussion suggesting that a different method should be used to account for a capital lease purchase for real property depending on the cash or accrual designation. While this distinction may be important for purposes of preparing audit financial statements, in actual practice, state law does not differentiate between the cash basis or modified accrual basis of accounting regarding the purchase of real property through a Section 177.088, RSMo, lease purchase agreement.

The provision authorized in Section 177.088.3, RSMo, to lease from a financing entity (trustee) those buildings, equipment, furnishings, etc., acquired or constructed infers the district is receiving the asset from the financing entity (trustee). There does not appear to be a statutory allowance for the district to simply borrow money from the financing entity (trustee) (i.e., receipt money into the district for use in construction) and then proceed to expend those funds to construct a facility for the financing entity (trustee) regardless of the district’s basis of accounting. The statutory inference is that the financing entity (trustee) constructs and owns the facility. This concept is emphasized in Section 177.088.6, RSMo, which references debt obligations secured by a mortgage pledge or deed of trust stating, “...such bonds, notes and other obligations issued shall not be the debt of the educational institution and the educational institution shall not be liable thereon ... shall not constitute an indebtedness of the educational institution within the meaning of any constitutional or statutory debt limitation or restriction.”

To summarize, regardless of possible governmental requirements relating to reporting of capital lease purchase obligations on the district’s independent audit financial statements, the actual journal transactions completed by the district are the same regardless of whether the district is on cash or modified accrual basis of accounting. The process of booking fair market value of the asset and the net present value of the lease purchase payments become, for all practical purposes, an audit function which should be discussed with the district’s auditor. Remember, the only expenditures recorded on the school district’s books for a lease purchase contract for construction of a building are the annual lease purchase principal, interest, and fees paid to the financing entity (trustee). Principal expenditures are recorded in the Capital Projects Fund, Function Code 5131 - Principal on Lease Purchase Agreements or if capitalized to 4051 - Facilities Acquisition and Construction, Expenditure Object Code 6613 - Principal Lease Purchase Agreements or if capitalized 6521- Buildings. Interest costs are recorded in the Capital Projects Fund, Function Code 5231, Expenditure Object Code 6623. Appropriate fees should be recorded in Function Code 5331, Expenditure Object Code 6633.

Payments may be required in advance of the actual construction for costs associated with contractor or architect fees. The district may make these up front expenditures with the financing entity (trustee) reimbursing the district by check payment. The reimbursement, if received during the same fiscal year, would be recorded as a credit against the expenditure account, thereby reversing the initial expenditure transaction already on the books.

General Journal entries to record the yearly lease purchase payment on a capitalized lease purchase:

General Journal entries to record the receipt of various revenues (if a district sets a levy in the Capital Projects Fund):

| <u>Date</u> | <u>Capital Projects Fund Entry</u> | <u>A/C No.</u> | <u>Debit</u> | <u>Credit</u> |
|-------------|---|----------------|--------------|---------------|
| 7/1/xx | Cash in Banks | 1111 | \$60,000 | |
| | Taxes, Current Ad Valorem | 5111 | | \$36,000 |
| | Taxes, Delinquent Ad Valorem | 5112 | | \$13,000 |
| | State Assessed Railroad and Utility Taxes | 5221 | | \$11,000 |

General Journal entries to record the yearly principal and interest payments on a capitalized lease purchase for a building project:

| <u>Date</u> | <u>Capital Projects Fund Entry</u> | <u>A/C No.</u> | <u>Debit</u> | <u>Credit</u> |
|-------------|---|----------------|--------------|---------------|
| 7/1/xx | Expenditures - Building Acquisition, Construction, and Improvement - Principal | 4051 - 6521 | \$43,000 | |
| | Interest - Lease Purchase Agreements | 5231 - 6623 | \$12,500 | |
| | Cash in Banks | 1111 | | \$55,500 |

General Journal entries to record the yearly principal and interest payments on a capitalized lease purchase for equipment:

| <u>Date</u> | <u>Capital Projects Fund Entry</u> | <u>A/C No.</u> | <u>Debit</u> | <u>Credit</u> |
|-------------|--------------------------------------|----------------|--------------|---------------|
| 7/1/xx | Equipment | *xxxx - 6541 | \$43,000 | |
| | Interest - Lease Purchase Agreements | 5231 - 6623 | \$12,500 | |
| | Cash in Banks | 1111 | | \$55,500 |

*Use appropriate function code.

General Journal entries to record the yearly lease purchase payment on a non-capitalized lease purchase:

| <u>Date</u> | <u>Capital Projects Fund Entry</u> | <u>A/C No.</u> | <u>Debit</u> | <u>Credit</u> |
|-------------|---------------------------------------|----------------|--------------|---------------|
| 7/1/xx | Principal - Lease Purchase Agreements | 5131 - 6613 | \$43,000 | |
| | Interest - Lease Purchase Agreements | 5231 - 6623 | \$12,500 | |
| | Cash in Banks | 1111 | | \$55,500 |

General Journal entries to record the yearly lease purchase payment on buses:

| <u>Date</u> | <u>Capital Projects Fund Entry</u> | <u>A/C No.</u> | <u>Debit</u> | <u>Credit</u> |
|-------------|--|----------------|--------------|---------------|
| 7/1/xx | District Operated Pupil Transportation Service/Pupil Transportation Vehicles - Buses | 2552 - 6552 | \$43,000 | |
| | Interest - Lease Purchase Agreements | 5231 - 6623 | \$12,500 | |
| | Cash in Banks | 1111 | | \$55,500 |

Section 177.088 Lease Purchases Refinancing

The financing entity (trustee) is technically the entity refinancing the lease purchase thus there are ***no entries that will appear on the district's books for the refinancing.*** Part IV of the ASBR will contain the information regarding the refinancing of the lease purchase.