

Non-Appropriation Risk for State, County, and Local Leases Within the Equipment Leasing and Finance Industry

May 2011

Industry Background:

The Equipment Leasing & Finance Foundation publishes research for and about the \$521 billion equipment finance market. Leases to municipalities (City, County, and State) have become an important product within the financial services sector. These transactions range in size from the very small to multi-million energy management transactions. Equipment types are from computers to phone systems, school buses, etc. Generally the transactions favored by industry players are sometimes called “human welfare” assets, which include fire trucks, 911 systems, police cars, medical equipment, systems for universities and communities, and many other daily use items for the communities.

The Study Background:

History suggests tax-exempt entities using non-appropriation clauses to cancel leases is insignificant relative to existing tax-exempt lease portfolios. However the changing financial conditions create a challenge today which is to evaluate the likelihood of tax-exempt entities to exercise this clause in 2011 and years to come. For example, over the longer term, shifting budget demographics will adversely impact state finances. Nearly a third of states’ budgets go to cover Medicaid, and those costs will expand as the recently passed health care law takes effect. An additional share goes to the post-retirement healthcare costs and other retirement costs of public sector retirees. These burdens will increase over time, creating perceived if not real risk in state debt.

For most of the past decade, local government was a growth business. Avid consumption and the real estate boom spurred an abundance of sales- and property-tax receipts; with dollars flowing in, governments got used to spending more and borrowing more. Then, in the recession, tax revenues dried up, while demands for services kept rising. For the last few years, both cities and states have faced severe, recurring budget gaps. Most of the forecasted financial challenges for the municipal market focus on the Bond market. The leasing market is impacted by the same general issues but there are few data sources on the potential for any substantial increase in non-appropriation.

The Problem Statement:

The data and general information on the non-appropriation risk in these municipal leases is not well founded providing many in risk management to avoid these transactions. The risk that a municipality will decide to non-appropriate the necessary funds to continue a multi-year lease transaction is of major concern given the current forecasts for municipal bond defaults. The key driver in this concern is the legal requirement in most entities to only obligate funds for one year for any obligation without the voters’ approval. This non-appropriation event creates a risk especially in the current revenue declines, overall budget requirements, and pension liabilities. The Foundation would like a comprehensive study of the history, benefits, pros and cons of non-appropriate leases, as it relates to the potential risk to the municipal leasing sector.

Issues to be addressed in the Study:

- What do government officials believe would cause them to non-appropriate?

- What is the non-appropriation experience with existing portfolios?
- What are the repercussions for a municipality using non-appropriation?
- Who tracks the data on the annual statistics on non-appropriation?
- What have been the historical losses on non-appropriation assets?
- Do the municipalities have alternatives to exercising non-appropriation?
- How important is tax-exempt leasing to the overall capital equipment acquisition for the municipality?
- Do municipal managers expect to increase or reduce the use of non-appropriation leases?
- Do municipal managers understand the repercussions for exercising the non-appropriation clause?
- Why have municipal managers increased the use of tax-exempt leasing over the past ten years?

Note to Researcher:

The Foundation recommends that the researcher perform a thorough review of available Foundation (<http://www.store.leasefoundation.org/>) and ELFA literature (http://www.elfaonline.org/cvweb_elfa/cgi-bin/memberdll.dll/OpenPage?WRP=productsearche.htm&WLN=LeftNav_Products.htm) and industry statistics, and other public venues such as newspapers and websites, prior to making any decision regarding conducting a survey of industry members. The Foundation can recommend the most relevant research available. We request that any recommended surveys be limited to information that is not otherwise readily available.

About the Equipment Leasing & Finance Foundation

The Foundation strives to be the “Eye on the Future” through development of future focused research, studies and articles regarding the equipment financing industry. Since its formation, the Foundation has commissioned and endowed over \$1.3 million for research projects. This has significantly increased the body of knowledge available to equipment finance organizations and those that work with these financing organizations. There is no other organization seeking to independently study key issues facing the industry with a view on where it could be in 3,5, or 10 years.

The Foundation is a sister organization to the Equipment Leasing and Finance Association (ELFA), the trade association representing companies in the \$521 billion equipment finance sector, which includes financial services companies and manufacturers engaged in financing capital goods. ELFA members are the primary users of research developed by the Foundation. ELFA’s 600 member companies include Fortune 100 financial services companies, captive manufacturer finance subsidiaries as well as small and mid-sized independents and service providers engaged in financing commercial equipment and software. In 2011, ELFA is celebrating 50 years of “Equipping Business for Success.” For more information, please visit www.elfaonline.org.

Foundation Budget: \$516,000 for fiscal year ending December 31.

IRS Classification – 501 (c) (3)

Staff – 2

Website: www.Leasefoundation.org

Required Deliverables

It is the expectation of the Foundation that the final study will be delivered in no more than four months from contract date.

Specific include:

1. All deliverables should be written for the lay reader.
2. Monthly progress reports submitted via email to Executive Director.
3. Each Foundation project is assigned a Steering Committee comprised of industry experts, to serve as a resource and reviewers of the findings and draft reports.
4. Research Study Paper- Final study provided in Microsoft Word and PDF version. Charts and graphs will be provided in PDF and Excel, to include the source data. All graphics must be provided in high-resolution and low-resolution quality. Study Page Count Variable: 30-150 pages.
5. Article - Journal of Equipment Lease Financing article – approximately 2,000 words. Author guidelines may be found at <http://www.leasefoundation.org/JELF/>
6. An abstract (approximately 250 words) of project results must be submitted at the conclusion of the original or amended project funding period. The abstract will be used to report the study to a general audience. The abstract must be written for the lay reader.
7. Upon request by the Foundation, be available to present findings live and/or via web seminars.

For more information on the grant process, application and grant guidelines visit:

<http://www.leasefoundation.org/Grants/about.htm>

Timeline and Contract Terms

Proposal due June 30, 2011.

Proposal selection occurs within 30 days of due date.

First Draft report expected no later than October 1, 2011.

Final report and all deliverables expected by November 1, 2011.

Selection Criteria

1. Experience in similar assignments
2. Resources/capacity to perform the required work
3. Experience with associations
4. Qualifications of the individuals who will perform the work
5. Knowledge of the equipment finance industry
6. Quality of the proposed study design
7. Price
8. References
9. Intangibles

Response Details

Submit your electronic response to Kelli Nienaber, Executive Director, at knienaber@leasefoundation.org.

Information Required

1. Researcher (or Firm's) history and background
2. Experience/knowledge with lease finance research
3. Experience with non profit associations
4. Overview of the study design
5. Credentials and qualifications of staff to be assigned the project
6. References/client list, with written permission to contact

7. Description of similar studies performed by the researcher
8. If appropriate, description of how staff time and other costs are billed

Staff Contact:

Kelli Jones Nienaber, Executive Director, Equipment Leasing & Finance Foundation, 1825 K Street, NW, Suite 900, Washington, DC 20006; phone 202-238-3400, knienaber@leasefoundation.org
Website: <http://www.LeaseFoundation.org>