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Real Estate Leasing: A New Chapter on Synthetic and Other Leases Post-Enron

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As a new generation of freshly minted MBAs discuss their career options, the once popular choice of structured finance is rarely heard. "Financial engineering" is no longer the natural outlet for creative minds focused on combining expertise in accounting, engineering, law, and finance. Thanks to Enron, and its many imitators,[1] Armani-clad bankers and Gucci-toed lawyers need no longer meet their corporate cowboy clients and accommodating accountants to fabricate a new "silk purse from a sow's ear." Business ethics, corporate governance, forensic accounting, and investor relations are, for now, the new arenas.

The Enron Debacle, well-chronicled by *Wall Street Journal* scribes Rebecca Smith and John R. Emshwiler in their best-selling *24 Days*,[2] seems the extreme protoype of corporate greed and arrogance, making the 19th century robber barons look like gentlemen. In hindsight, it was a logical, even predictable, extension of the elastic, bonus-driven business ethics of the 1990s, where corporate "gangs" committed street crimes on both Wall Street and Main Street.

The energy companies that pumped their power and stock became Main Street trading companies, manipulating newly freed markets shamelessly with no apparent penalty or remorse.[3] The telecom companies borrowed zillions (or at least billions) to spread cable under and over the sea, then finding neither buyers nor users, traded them with each other like baseball cards. Corporate monarchs became egomaniacal tyrants, convincing themselves, and their appointed director-sycophants, that the success of the enterprise was due entirely to their genius. Mutual wealth via option exercise and insider sales induced them to approve, or overlook, their heroes lavish unprecedented perks, all the while bleeding operating losses and unmanageable debt. The checks and balances of corporate governance, involving outside counsel, outside auditors (also known as "consultants") and audit committees, were paralyzed by inherent conflicts of interest and greed. Enron, followed by Dynegy and Williams Companies, were joined by Qualcomm, Tyco, Global Crossing, Qwest, Worldcom, and countless other manipulators of vague and inscrutable accounting rules.

The gaping holes in accounting for "prepay" and "round-tripping" and contrived sales to seemingly unaffiliated entities were the most glaring examples of form over substance. These obscure deals, struck and barely documented in time to close the books at each quarter's end, reflected accounting aggressiveness at successively new heights. Artificially created earnings targets were miraculously, if mysteriously, met by successive rabbits pulled from the hats of unscrupulous gamesmen. Even rating agencies, bankers, lawyers, and accountants not intimately involved in these baldly circuitous transactions had to be confused by them.

Unshackled stock analysts who asked questions were met with assurances of compliance, and doubters were transferred or ignored.

This smoke-and-mirrors atmosphere calls to mind the old lawyer joke about the "oldest profession" debate among a lawyer, doctor, and engineer. The doctor claimed his was the oldest, because God carved Eve out of Adam's rib, and this was an act of surgery. The engineer replied that God created the world out of chaos, clearly an act of engineering. The lawyer, undaunted, stated confidently, "Aha. Now you have it! Who do you think created the chaos?" Sadly this anecdote must now be rewritten to include bankers, lawyers, and accountants, in the guise of "financial engineers."

Dozens of federal and state investigations have produced unprecedented numbers of indictments, guilty pleas, and settlements of corporate executives and investment bankers. Wall Street's mightiest accomplices, such as Merrill,[4] Citigroup, and J.P. Morgan Chase,[5] agreed to pay massive fines and adopted new rules to prevent themselves from aiding and abetting future financial manipulations. *The New York Times'* photographs of three Merrill bankers in handcuffs[6] sent a curdling chill through a new generation of MBAs who were trained to "think outside the box." In the post-Enron era, the rule is no longer to "think outside the box." The formerly hyperactive financial engineers have been sedated and can't even think about the box, until a consensus builds around its boundaries.

WHY SHOULD ENRON REFORMS AFFECT REAL ESTATE?

Real estate leasing and financing transactions have long used special purpose entities, or SPEs,[7] as owners of real estate leased to public and private entities in synthetic leases, credit-tenant leases (CTLs), and sale-leasebacks. SPEs had, of course, been used in many legitimate, fully-disclosed financial transactions of real estate and other assets for the purpose of insulating lenders and investors from unwanted liabilities and risks. Since SPEs could hold and operate assets, which would otherwise clutter a reporting company's balance sheet, and reflect liabilities, expenses, and losses, they were ripe for abuse. Enron and its followers used indirectly controlled SPEs—some aptly named "Raptors"—to "buy" declining or worthless assets from consolidated subsidiaries and affiliates, thereby concealing or deferring losses and fabricating income. Sometimes, the SPE would own and "sell" an unwanted barge in Liberia to a friendly banker who was verbally assured of short-term repurchase at a profit. Financing was, in each case, readily obtained based on direct or indirect guarantees from the company—still surprisingly rated as investment-grade.[8]

Regardless of whether or not synthetic or other leases involving SPEs were properly classified as operating leases under GAAP[9] and disclosed by public companies, their structure and economic viability have become ensnared—perhaps unfairly—in the Enron fallout. Undoubtedly, bankers were able to accumulate their books of synthetic lease business by offering their public company clients lower rents than conventional leases, and lower expense charges than direct ownership. So long as real estate residual values could be preserved, the low interest-only rent with no depreciation was enticing,[10] and the rent expense without depreciation was consistent with real estate economics. When synthetic leases were extended to include special-purpose property with integral equipment and other unique or isolated real estate with declining residual value and no provision was made for amortization or anticipated future write-downs,[11] however, some distortion was inevitable. It was not the banker's issue, because, in a synthetic lease, repayment of the "unamortized lease investment balance" was supported by the lessee's 85 percent[12] residual value guarantee (RVG), a first-dollar layer of loss protection. Thus, the banker-lessor could look almost entirely to the lessee's credit and not the underlying real estate.

THE ACCOUNTING REACTION

Eager to assure the Securities and Exchange Commission, legislators, and its various other constituencies that the accounting profession, now down 25 percent to the Big 4 after the demise of Andersen, was capable of policing itself, the Financial Accounting Standards Board embarked on the long overdue task of rewriting the rules involving the use of SPEs. The end result, FIN 45[13] and 46,[14] became part of the "Enron Effect" and cast a dark pall over the world of real estate leasing. Previous articles[15] have summarized the text and basic rules, and their perceived impact on synthetic and other operating leases. Without repeating or attempting to interpret all of their many clauses and caveats, this article suggests that the world of synthetic leasing has, indeed, survived in a slightly different form, and for the most part, without diluting the legitimate intent of accounting reforms.

The Variable-Interest Entity

A major impact of FIN 46 is its requirement that primary beneficiaries of Variable-Interest Entities (VIEs)—the successor in spirit to SPEs—consolidate leased assets on their balance sheets. Each synthetic lessor that held its client's real estate in an SPE would become a VIE, and the mere presence of the lessee's residual value guarantee (RVG) or purchase option, would make the lessee the primary beneficiary. This would require the lessee to consolidate the lessor and deprive it of most of the financial benefits of the synthetic lease structure. In order to avoid classification as a VIE, and the ensuing determination of which interest-holder among lenders, investors, and lessee was the primary beneficiary, the lessor would have to show that it had sufficient equity to absorb reasonably expected losses of the enterprise.[16] The rules created a rebuttable presumption though not a safe harbor—that 10 percent was the *minimum* amount of equity required.[17]

If, however, a lessor could not escape VIE treatment, the presence of the RVG and the lessee's fixed-price purchase option at the Unamortized Lease Investment Balance (ULIB) would make the lessee the "primary beneficiary" of the VIE, and require consolidation of the lessor and its real estate by the lessee. One immediate question is whether the RVG—the linchpin of the synthetic lease—could still be available as a *first-loss* cushion to absorb a decline in real estate values without negating the "equity at risk" requirement. If the VIE test required that the minimum 10 percent equity must be sufficient to absorb reasonably expected losses, and those losses invariably involved a decline in the fair market value of the leased property, how could the lessee provide a first-loss RVG to protect the equity? Although no answer has yet been formally announced by either FASB or the Big 4 accountants—probably because their focus has been on other means of avoiding consolidation—it seems likely the RVG will continue unabated as a first-loss guarantee without requiring consolidation by an otherwise sufficiently capitalized lessor.[18] By analogy to prior rules, the FASB had adopted a seemingly strict analysis in EITF 96-21 requiring that the then minimum 3 percent equity required by EITF 90-15 remain "at risk" for the life of the lease. Yet, this "equity" was then permitted to be cushioned by the first-loss RVG. If the intent of the new rules is to identify the parties bearing the most risk or receiving most of the reward, the finger remains firmly pointed at the lessee, both by virtue of its first-loss RVG and purchase option at Unamortized Lease Investment Balance.

The Residual Value Guaranty Under FIN 45

Another potential obstacle to achieving the benefits of synthetics seems to have had little adverse impact. FIN 45 had introduced a new requirement that the lessee book a liability for the fair value of its RVG. With virtually no precedent or guidance, lessees' accountants were left to ponder the net present values of potentially negative cash flows pursuant to prior FASB standards.[19] One approach was to use the somewhat analogous premium charged for residual value insurance (RVI) and adjust for the fact that, unlike the RVG, RVI is not a first-loss risk. RVI is also usually for a smaller risk position—15 percent to 30 percent—rather the typical 85 percent RVG. What seems to have evolved, however, is an analysis, based on an appraisal, of estimated future fair market value (EFFMV) upon expiration of the lease. If, as expected, EFFMV is at or above the trigger of the RVG, it would result in the use of offsetting entries with no net effect.

By extrapolation from the RVI premiums, a lessee might value its RVG in a synthetic lease at 4 percent of the 85 percent amount guaranteed. That amount would be booked on the balance sheet as a liability and credited to prepaid rent. The prepaid rent is amortized over the term of the lease, increasing rent expense, but an offsetting credit to income is taken as the liability burns off. This neutral effect is, of course, unavailable if the value of the asset declines, as it well may in the case of special-purpose property or depreciating equipment, property improved beyond its locational value, or a substantial down cycle in commercial real estate. The added rent expense continues but the liability may become real, and remain until expiration of the lease.

The likely—and beneficial—result of FIN 45 is to limit the use of non-amortizing synthetic leases to well-located real estate whose collateral values are likely to be sustainable over the five-to-ten year of the lease. Special-purpose properties and equipment are better suited economically to either direct ownership or amortizing leases, with rent schedules that conform to their depreciated values. This achieves one of the primary objectives of FIN 45 and 46 by eliminating the understatement of expense on income statements for depreciating assets leased in non-amortizing, perpetually renewed, synthetic leases.

The Primary Beneficiary of a VIE Under FIN 46

As previously noted, a lessor could be classified as a VIE if its equity were deemed insufficient, and if so, the typical synthetic lessee's RVG and purchase option would render

the lessee the primary beneficiary. Having resolved the seemingly difficult task of applying FIN 45 to RVGs without killing the synthetic, the major bank leasing companies, their corporate clients, and their Big 4 auditors sought to address the constraints of the VIE under FIN 46. Yet, how could they avoid VIE status with 10 percent or more equity and its potential increase in lease pricing—a first-loss RVG that might be viewed as impairing true "equity at risk" characterization and other uncertainties?

The first Exposure Draft on Consolidation of Special Purpose Entities attempted to distinguish SPEs from SOEs, or Substantive Operating Entities. As terminology evolved, SPEs became VIEs, with some distinctions, and SOEs gave way to Voting Interest Entities (VOEs). The primary feature of a VOE was its independence from the lessee, attributed to either or both voting control and/or some degree of independent capitalization and the resulting ability to absorb expected losses without additional support from other variable interests. Although the accountants have had difficulty devising a bright-line test on what was a VOE and what was not a VIE, it is clear that single-asset lessors are VIEs. Conversely, multi-asset leasing companies owned or controlled by big, well-capitalized financial institutions may or may not be VIEs, but they seem to possess the financial independence of VOEs.

The result of a FIN 46 determination that a lessor is a VIE and that the lessee is the primary beneficiary is that the lessee must consolidate the assets of the lessor. If the lessor has other assets that are not leased to the same lessee, the analysis can become more complicated. For example, what if a newly formed independent leasing company (ILC) synthetic-leased a $100 million corporate headquarters property to Mega Corporation (MC) and has five smaller pieces of property and equipment leased to other companies with a total cost of $90 million. The headquarters property is ILC's single largest and most important asset but ILC has independent credit lines from banks enabling it to seek and close new acquisitions and leases. Under the emerging consensus, MC might be required to consolidate all of the assets of ILC, even though the other assets are leased to unrelated parties.

A Big 4 consensus seems to have emerged to avoid this anomaly, however, and defer determinations of VIE status. Even Big 4 accountants and their colleagues at the FASB recognize the incongruity of requiring several different lessees of leasing companies to consolidate all of their lessor's assets. While other remedies could be devised, they have concluded that when no single lessor accounts for 50 percent or more of a lessor's portfolio, no lessee need consolidate its lessor's assets. Thus, once ILC's business has diversified a bit more, as it would if it closed another $15 million lease with a sixth lessee, no single lessee would account for more than 50 percent of its assets and MC would not be required to consolidate ILC regardless of whether ILC was classified as a VIE. Thus, MC would receive operating lease treatment despite its having provided an RVG and received a purchase option at the Unamortized Lease Investment Balance, despite the fact that it seems quite clearly to be a primary beneficiary. Presumably, under this approach, it would not matter how ILC funded its leases or whether it had adequate equity or other layers of available capital to absorb expected, or unexpected, losses.

The second condition seems to address the risk aspect of the issue, though not necessarily the FIN 46 capital adequacy and primary beneficiary tests. Previous accounting releases, such as EITF 96-21, had instructed that if a lessor funded several separate leases but effectively insulated each from the other by using 100 percent non-recourse, secured debt, that lessor could be viewed as a multi-tiered SPE, and subject to the requirements of EITF 90-15, which then required a minimum equity of 3 percent in most synthetic leases. In a similar concept, if multi-asset leasing companies were to create separate, insulated "silos" for each leased asset, they would be using the silos and each silo would be separately subject to the primary beneficiary test of FIN 46. A multi-asset lessor could avoid having a leased asset treated as a "silo," however, by ensuring that at least 5 percent of each asset is funded by equity or recourse debt. In theory, this minimum equity or recourse debt provision affords some assurance of capital adequacy and financial independence, though it may seem to set a double standard by contrast to the 10 percent minimum equity at risk threshold required of other VIEs.

As in the threshold determination of sufficient "at risk," the same question arises as to whether this same 5 percent equity or recourse debt that avoids silo treatment can be effectively cushioned and protected by the traditional first-loss RVG, or whether the RVG must now be restructured to come *behind* the lessor's risk capital. The answer at present seems to be that the RVG can be invoked to cover the first dollar of loss to the lessor, and that the "silo" definition essentially ignores the economic reality that the RVG protects the lessor from any loss. This approach can be justified by the analogy to an amortizing lease such as a conventional long-term net lease or credit-tenant-lease, or CTL, in which all or most of the acquisition cost is recouped through a long-term committed rent stream. Arguably, there are some

basic differences. The synthetic lessee exercises a greater degree of control through its fixed-price purchase option and its ability to deal with shorter-term leases. By contrast, the CTL lessor has some residual upside, since purchase and renewal options are generally related to future fair market values. Moreover, a lessee in a CTL or other "true lease" takes the lessee's long-term credit risk, and must rely on the value of the real property if the lessee should file for bankruptcy and the lease is rejected, while the synthetic lessor retains a liquidated claim for accelerated rents up to the Unamortized Lease Investment Balance, for whatever it may be worth.[20]

ACCOUNTING REFORMS IN PRACTICE: CHANGE WITHOUT REVOLUTION

Fair or not, the playing field is not level. FIN 46 does make life easier for multi-asset (usually bank-owned) leasing companies than small independent lessors, since they can meet the 50 percent and silo tests. Theoretically, large multi-asset leasing companies are not controlled by their lessees, although they are probably just as anxious to please their clients as a small leasing company. In reality, even with the cushion of the RVG, independent non-bank leasing companies not functioning as lenders are more likely to act independently in negotiating rents and renewal and purchase options if they have 10 percent or more equity at risk subject to the lessee's credit and the property's residual value to protect against a credit decline.

Nonetheless, the evolution of these standards is not inconsistent with the fundamental intention of producing balance-sheet classifications that are meaningful. Synthetic leases have never produced anything close to the dangerous level of financial distortions that were generated by the "Enron Outlaws." Properly disclosed—and ensuring full disclosure is now a clear condition of both the accountants and bankers in the post-Enron era—synthetic leases do not hide assets or liabilities, nor do they fabricate or inflate earnings as the phony barge sales, "prepays," and cable "roundtripping."

The most vulnerable piece of the synthetic structure was the omission of amortization from the rents, which a true lessor would charge the lessee to recoup its economic depreciation cost.

This issue is, for the most part, rectified by the new conditions of FIN 45 that would first impose a new liability for the fair value of the RVG, and then, deny the lessee of a truly depreciating asset the reduction of liability income credit to offset the prepaid rent charge. The end result is to place leases of such properties on a similar, if not quite equal, footing as lessees of depreciating properties under true leases. This will tend to limit synthetic leases to more generic, newer properties which are believed to retain their residual values and funnel other properties into more traditional longer-term leases in which lessors can amortize some or most of their costs and are paid a fair return on equity for their residual risks.

ALTERNATIVE LEASE STRUCTURES

Where does this apparent acceptance of the synthetic lease, at least in non-VIE lessors and multi-asset lessors, leave alternative lease structures? Many issues and sub-issues remain to be documented, and lessors will be asked for both closing certificate representations and continuing undertakings to ensure their status and the lessee's continuing freedom from consolidation. Lenders will want to be fully secured, and equity investors or recourse lenders to leasing companies will be more cautious than ever about which credits are included in their lease portfolios. Banks, already constrained from direct real estate ownership,[21] may become more concerned about their leasing portfolios cluttering their consolidated balance sheets and distorting their return on asset ratios. Industries with less certain credit profiles, and higher leverage, will find it difficult to find a multi-asset leasing company and will be forced to obtain more costly, secured lease or direct financing. Properties with less certain residual values will also migrate into amortizing lease structures.

Public companies that shoved all their corporate real estate into synthetics may now choose to renew some leases and replace others. They may seek alternative structures with less sensitive structuring issues. Sale-leasebacks for special-purpose and older depreciated properties may now be much more attractive, once it becomes clear that they will have to absorb either amortization in a rent stream or depreciation. Hybrid lease financing structures for both new and existing real estate will be devised and adjusted, and just as the lines have been drawn on synthetic leases, they will be drawn for other forms of leases with credit features.[22]

A lease is, after all, a means of financing the use of real estate. There is nothing un-American, un-transparent, deceptive, or un-economic about a lease structure in which the rent charged is related to the lessor's cost, risk, and reward. A financially weak lessee should pay more rent than a rock-solid, investment-grade lessee because the lessor will have to risk more equity and pay more to finance any lease for a weak lessee. A short or medium-term lease involves

more residual value and refinancing risk than a long-term lease that can amortize a sizable amount of the lessor's investment and debt and should have a higher rent. The synthetic lease structure properly reduces rent in exchange for the risk mitigation of the RVG and the short-term nature of both the credit and residual exposure. Other leasing structures can combine credit and residual factors to achieve an equally fair balance of risk and reward to both parties.

CONCLUSION

The Enron Debacle is a long-overdue wake-up call to regulators, investors, auditors, financial executives, attorneys, and bankers of all types. It is significant, however, that the gross distortions of balance sheets and income statements were not triggered by phony or fabricated real estate leasing or financing transactions. Nor was this massive deception aggravated by synthetic leases, despite their size and apparent anomalies.[23] The mission of those who are structuring and passing upon corporate and real estate transactions is to report the economic effects fairly and accurately and rely on a newly rekindled "smell" test of economic substance. Any financing transaction—real estate, corporate, or other—that defies logic and has no economic justification other than misleading investors and analysts should be rejected.

The understandable reaction to Enron is to fear and avoid all "thinking outside the box." This has the dangerous side effect of anesthetizing all analytic thinking. Robotic conformity to a limited number of established structures and large, multi-asset leasing companies can ultimately produce its own set of distortions. The acquisition, development, and financing of real estate depends on the availability of lease-financing and free access to the capital markets. New real estate lease-financing structures—whether for synthetic or "true" leases—should not be summarily rejected because they appear to have different features or form. Nor should the spectrum of permitted leasing companies be limited to those owned or funded by large financial institutions.

If lease classification and consolidation were based solely on the distinction between a 'true' lease and a financing, that line has become even more blurred taan before by the predominance as lessors of financial institutions more accustomed to credit than real estate analysis. Yet, any lease is, in essence, a means of financing the use of the leased asset for a portion of its useful life. Ultimately, whether a synthetic or other form of lease is an operating lease not required to be consolidated by its lessee will require a full understanding and analysis-historically an exercise avoided by accountants—of the economic substance of the transaction and the relationship between the parties.

NOTES

1. Enron traders turned investment bankers are reported to have created a separate profit center to teach other companies how to manipulate markets and manufacture profits.
2. R. Smith and J. M. Emshwiler, *24 Days* (Harper Business 2003).
3. After issuing blanket denials of complicity in California's blackout-producing energy crisis, which cost the state's residents billions, Enron traders bragged about their ability to clog energy traffic by bogus trades at artificially manipulated prices. Enron's then chief, Jeffrey Skilling, subsequently blamed California's lax regulators for being unprepared to handle deregulation, as if it was Enron's inherent right to profiteer by deception.
4. *See*, *The New York Times*, September 18, 2003, at A1.
5. J.P. Morgan Chase and Citigroup agreed to pay $305 million to settle a wide variety of SEC and other federal agency charges relating to $8.3 billion of fraudulent loans disguised as income-producing sales to Enrou and Dynegy, its crosstown Houston co-trader. See, *The Wall Street Journal*, July 29, 2003, at A1.
6. *See*, *The New York Times*, September 18, 2003, at C5.
7. SPEs can be grantor trusts, limited liability partnerships, limited liability companies, or any other legal entity having a clearly defined charter limiting its activities and ability to incur liability. Institutional investors and lenders in real estate historically preferred to use SPEs in order to limit their contingent liabilities for environmental risks and uninsured losses.
8. Despite their intimate knowledge of many of these deceptive transactions, it remains unclear whether Enron's major banks actually understood the domino effect of unraveling them, and the inevitable ratings downgrade and liquidity crunch. Their role in leading syndications for these financings would suggest, however, that they did not fully appreciate the entire picture, or perhaps thought it would all be remedied over the short term.
9. FAS 13 sets forth the criteria for operating lease treatment.
10. Synthetic lease volume was reported to approach $150 billion by the end of 2001.
11. FAS 121 requires the write-down of, and charge to earnings for, assets whose fair market value has declined from that carried on the balance sheet.
12. This amount may vary. Depending on the amount permitted to be included as "rent" in the net present value calculation know as the 90 percent test of FAS 13, Para. 7.
13. FASB Interpretation No. 45, *Guarantor's Accounting and Disclosure Requirements for Guarantees, Including Indirect Guarantees of Indebtedness of Others* (November 2002).
14. FASB Interpretation No, 46, *Consolidation of Variable Interest Entities: an Interpretation of ARB No. 51* (January 2003). Note, however, thath as this article went to press, the FASB releasred and extensive revision of the FIN 46, effective December 2003. Several provisions, most notably a new exception from VIE treatment for any lessor entity qualifying as a "business," could affect the views expressed herein.
15. *See, e.g.,* Gil Sandler, "Synthetic Leases After FIN 46: As FASB Issues New Accounting Rules, the Future Remains Unclear," *Real Estate Finance*, June 2003, at 2; Gil Sandler, "Synthetic and Other Off-Balance-Sheet Leases: Prospective Accounting Reforms," *Real Estate Finance*, December 2002, at 14.
16. Para. 5a of Fin 46 defines a VIE in terms of sufficient "equity investment at risk to permit the entity to finance its activities without additional subordinated financial support from other parties"—presumably lenders aud the lessee.
17. FIN 46, paras. 9-10, and Appendix C, paras. 21-24.
18. Assuming that the lessor has sufficient equity—presumably 10 percent in most cases—that equity would still be considered "at risk," thereby avoiding VIE classification.
19. *See*, FASB Statement of Financial Accounting Concepts No. 7 (February 2000).
20. The synthetic lease, unlike the standard true lease, accords the lessor the right to accelerate the entire ULIB in the event of default, and, and further recites that, in the event of bankruptcy, the lease will be regarded as a financing and not subject to rejection or disaffirmance.
21. Generally, banks are restricted from direct ownership of real estate except real estate owned (REO) by reason of foreclosure, or for direct bank occupancy. Reg. Y permits loans to bank holding company subsidiaries holding and leasing real estate, but not necessarily to affiliates.
22. By way of disclosure, the author's firm, RealVest Capital Corporation, is actively engaged in leasing transactions involving true and synthetic leases, and has structured long-term "hybrid" leases and sale-leasebacks combining elements of both credit and real estate residual values.
23. Some critics of the synthetic lease focused on the omission of controlled real estate from corporate balance sheets, but this effect has, for the most part, been neutralized by the rating agencies' reformation of balance sheets. The synthetic's different tax and accounting treatment may also be viewed as unusual, but accounting and tax standards are different in many areas, because they have different objectives. So long as transactions have economic substance and liabilities and expense are properly accrued and disclosed, different tax and accounting treatment should be essentially irrelevant.