



## OPERATING LEASE OR FINANCE LEASE?

Most academies are aware that they are not allowed to borrow without the approval of the DfE. However, not all are aware finances leases are be considered borrowing or how to distinguish between an operating lease and a finance lease.

Nearly all schools will lease various equipment such as photocopiers and ICT equipment. Most leasing companies will offer favourable terms in order to get academies to sign up to lease and it can be difficult to determine whether a lease is either an operating lease or finance lease. This has often led to schools signing themselves up for finance leases with inflated prices far above the value of the asset. Below is some guidance to assist with determining whether a lease represents a finance lease or an operating lease.

### WHAT IS AN OPERATING LEASE?

Operating leases are the only types of leases a school can enter in to. Both hire purchase agreements and finance leases are considered borrowing and require approval from the DfE.

The risks and rewards of owning an asset rest with the lessor and typically the lease will run for less than the life of an asset and the total payments will not cover the total cost of the asset.

The lessor will own the asset, look after the maintenance/repairs and take back the asset after the lease has expired.

### WHAT IS A FINANCE LEASE?

A finance lease is a way to ‘effectively’ purchase an asset by leasing an asset for the majority of its life or having an option to acquire an asset for a negligible amount at the end of the lease term.

During the term of the lease the asset’s ownership will legally sit with the lessor but a finance lease is where the risks and rewards of an asset are judged to have transferred from the lessor to the lessee (the school).

### Questions to ask to ascertain whether the lease is operating or finance

It is worth asking the following questions to help determine whether the lease is an operating or finance lease:

	Answer	Answer
Does the lease transfer ownership of the asset to the lessee (i.e. the school) by the end of the lease term?	Yes - finance lease	No - operating lease
At the end of the lease does the school have the option to purchase the asset at a price which is substantially lower than the market value of the asset at that point?	Yes - finance lease	No - operating lease

Is the lease term for the majority or all of the economic life of the asset?	Yes - finance lease	No - operating lease
At the beginning of the lease do the minimum lease payments amount to nearly the value of the leased asset?	Yes - finance lease	No - operating lease
Are the leased assets of a specialised nature such that only the school can use them without major modifications being made?	Yes - finance lease	No - operating lease
Are you responsible for maintaining and insuring the asset?	Yes - finance lease	No - operating lease

## Top Tips

1. Always specifically ask for an operating lease
2. If the document is titled a Hire or Rental agreement - it may still be a finance lease
3. Make sure that the costs are broken down and that you are aware of your obligations
4. Ensure the term does not exceed the useful life of the asset
5. Confirm what happens at the end of the lease
6. Do not use leasing if you are unable to return the asset. The documentation for an operating lease should include detailed 'Return Conditions'

## RESOURCES

Department for Education resources on 'Effective Buying for your School'

<https://www.gov.uk/guidance/buying-for-schools>



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