The Perfect Storm

Why Successful Lease Financing Companies Have Exited the Marketplace

PREFACE

The concept of The Perfect Storm project was perhaps first discussed in January 2001 during the Industry Future Council meeting. The group spent an unusual amount of time during the meeting focusing on the industry's recent past. One exercise the group completed was to list the leasing companies that had recently exited the business (usually involuntarily). Once the list of names exceeded twenty-five, the focus shifted from whom to why, and the implications for the industry.

The analogy to the book and movie, *The Perfect Storm*, is wonderfully apt since it certainly appeared that a truly massive and unusual event had occurred. Once the investigation and analysis of this project was completed, however, two conclusions became clearer.

First, the number of leasing companies driven out of the market by The Perfect Storm, while significant, was not large relative to the size of the industry. What was unusual was the damage done in a comparatively short period and the industry status of some of the lessors and their management. Second, although sudden and violent when it hit, The Perfect Storm, or at least a development like it, could actually have been foreseen.

All US-based Alta principals participated in the research and analysis for this project, each of whom has extensive leasing industry experience at both the strategic and tactical levels. This experience, in combination with ValueCAP™, Alta's strategic review service, was used extensively in developing, analyzing, and understanding the project information.

It is important to recognize the study for what it is – a post mortem analysis to be used as a learning tool for the industry. In completing the study and analysis, Alta had the benefit of hindsight. The managements of The Perfect Storm's victims were not so fortunate.

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The Equipment Leasing and Finance Foundation is a 501 (c) 3 non-profit organization established by the Equipment Leasing Association of America in 1989.

The Foundation develops and promotes the body of knowledge to enhance recognition and understanding of equipment lease financing. The Foundation's strategic objectives are:

- To maximize the role that equipment leasing plays in the world economy, and;
- To be the prime developer and disseminator of a body of knowledge of the leasing industry.

The Mission

To promote the growth and effectiveness of equipment leasing and finance through programs that:

- Identify, study, and report on critical issues affecting equipment leasing and finance, and
- Develop the body of knowledge of equipment leasing and finance for use by the equipment leasing and finance business, academic, and public policy communities.

All products and services development by the Equipment Leasing and Finance Foundation are FREE! The Foundation relies on your generous support to conduct research to increase the industry's body of knowledge and to provide products to you. Please consider a tax-deductible contribution today.

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Executive Summary

A Perfect Storm has swept the US equipment leasing and finance industry. This confluence of weak strategies, poorly executed plans, and difficult market conditions has caused an unusually large number of companies to exit the industry in a short period of time. Was this Perfect Storm a series of isolated events or an indication of a failing industry? Furthermore, were there any warning signs?

The Equipment Leasing and Finance Foundation commissioned a study to determine why most companies succeed, examine why a few failed in a condensed timeframe, and develop a learning tool for the industry. The study included a broad demographic mix of equipment leasing and finance companies that have recently exited the marketplace. The primary source of information was interviews, supplemented by public data.

The Perfect Storm in the equipment leasing and finance industry may not have the glamour of the movie, but it does have many parallels with it. There were highly questionable decisions and ignored warning signs that combined with disastrous results. In the movie, Captain Tyne's reach exceeded his grasp. The same may be said of many of the lessors in this study.

Although all the companies shared the same ultimate objective of increasing shareholder value, there were various approaches for achieving that objective. The companies also employed a wide variety of tactics to implement their chosen approach. It is interesting to note that most of the companies succumbed to The Perfect Storm at the tactical level.

There were seven major causal themes for why these companies exited the industry. Many of the target companies shared causal themes, or were affected by more than one theme. These causal themes include:

_ external factors
_ flawed business models
_ weak controls
_ inadequate infrastructure
_ rapid growth
_ management issues, and
_ divergence from core competencies.

Although the results of this project are not indicative of a failing industry, the equipment leasing and finance industry has changed. The industry will have to recognize the ramifications of these changes and conduct business accordingly in the future. One of these changes will be a renewed focus on value, for it is a focus on value that will determine the winners and victims of the next Perfect Storm.

Introduction

Several equipment leasing and finance companies have recently disappeared in what James McNair[1] of the Miami Herald described as "a perfect storm of events." Are these isolated failures, the result of avoidable problems, or an indication of a failing industry? More importantly, could this Perfect Storm have been predicted, and were there warning signs?

The answer, just as in the movie[2], is yes – there were warning signs. For example, during the mid 1990s, former ELA Chairman Jim Possehl asked 70 leasing executives attending an Executive Roundtable to indicate their company's growth expectations for the coming year. Did they anticipate their company would grow by less than 10%, 10 to 20%, or more than 20%?

Everyone in the room expected to experience volume growth of more than 20%. Jim next asked how they were going to accomplish this growth in a mature industry? After all, the penetration rate is stagnant and overall industry growth rates are in the 10 – 15% range. Jim had identified, prophetically, it turns out, one of the significant drivers behind many of the recent leasing company failures. Management's belief that aggressive growth rates could be sustained indefinitely led to many of the decisions creating The Perfect Storm.

In this same vein, unrealistic return expectations also were behind many of management's decisions. The US equipment leasing and finance industry is a mature industry, having evolved into a well-established member of the financial services mainstream. With that maturity has come a stabilization of returns.

In its maturity stage, the equipment leasing and finance industry has steadily earned ROE's of 13 – 15%. Consistent, above-market returns are primarily the domain of those companies that add value to their customers, although developing new and unique products has become more challenging.

Foundation Study

The effect of The Perfect Storm has been pervasive. As can be seen in Exhibit One, Companies No Longer in Leasing, numerous and diverse companies have left the industry in the past two years. These companies join the list of other, well-known companies that have disappeared from the scene, such as Itel, OPM, CIS, Greyhound Capital, Atlantic Computer, Bennett Funding, and Nelco. All serve as reminders of the risks and pitfalls that continually face players in a leveraged industry.

Exhibit One

Companies No Longer in Leasing[3]

Company	Reason
Advanta Leasing	Exited leasing business.
American Business Leasing	Ceased operations.
Amresco Inc.	Declared bankruptcy.
Banc One Leasing	Partially exited leasing business.
Bancorp Financial Services	Closed by Humboldt Bancorp.
BankVest Capital	Declared bankruptcy.
Bayview Capital	Exited leasing business.
Capital Associates	Ceased operations.
Centura Leasing	Closed by Bank of Canada.
Comdisco	Declared bankruptcy.
Efinanceworks	Ceased operations.
El Camino Resources	Ceased operations.
Finantra	Exited leasing business.
FINOVA Group	Declared bankruptcy.
Franklin Leasing	Closed by Liberty Bank.
Leasing Solutions, Inc.	Declared bankruptcy.
Liberty Leasing	Ceased operations.
LINC Capital	Declared bankruptcy.
Lyon Credit	Ceased operations.
Merit Leasing	Ceased operations.
Metrolease	Ceased operations.
Metwest Leasing	Ceased operations.
PinnLease, USA	Ceased operations.
Prime Capital	Ceased operations.
Prime Leasing	Ceased operations.
SDI Capital	Declared bankruptcy.
SierraCities.com	Acquired by American Express.
T & W Financial	Declared bankruptcy.
Terminal Marketing	Ceased operations.
The Bancorp Group	Ceased operations.
UniCapital	Declared bankruptcy.
US Capital Leasing	Declared bankruptcy.

The maturity of the equipment leasing and finance industry has precipitated The Perfect Storm; yet, all companies within the industry face the same mature market. Why is it, then, that the vast majority of companies succeeded and only a few failed in a relatively short timeframe?

The Equipment Leasing and Finance Foundation[4], in response to this question, commissioned The Alta Group to:

1. Analyze the industry during the past several years,

2. Determine if there are trends and warning signs to indicate why some successful companies exited the marketplace, and

3. Develop a study to serve as a learning tool for the industry.

The goal of the study is to (i) determine whether these failures were a result of avoidable problems or are an indication of a failing industry, and (ii) identify useful indicators for preventing similar scenarios in the future. The target readership of the study is the equipment lease financing industry, capital markets and funding sources, university academics, and industry analysts.

The study included equipment leasing and finance companies that have recently exited the marketplace, with an emphasis on those companies leaving since early 2000. The target group, although consisting predominantly of public companies, represented a broad demographic mix. Exhibit Two details the composition of the target group.

Exhibit Two

Target Group
(Major Demographics)

Name	Assets[1]	Ownership	Industry	Ticket size
Banc One[2]	5,000	Public	General	ST, MM
BankVest	Not available	Private	General	ST, MM
Comdisco	8,754	Public	IT	MM, LT
El Camino	943	Private	IT	MM, LT
FINOVA	12,089	Public	General	All
SierraCities.com	1,014	Public	General	ST, MM
LSI	747	Public	IT	MM, LT
LINC	513	Public	General	ST, MM
T&W	251	Public	General	ST
UniCapital	4,005	Public	General	All

The group includes companies that offered leases in all ticket sizes. Some of the companies offered the total range of transaction sizes (ST – small ticket, MM –

[1] Last full year of operations, in millions of dollars

[2] Banc One Leasing Corporation only partially left the leasing business. It exited certain segments in order to concentrate on core banking customers.

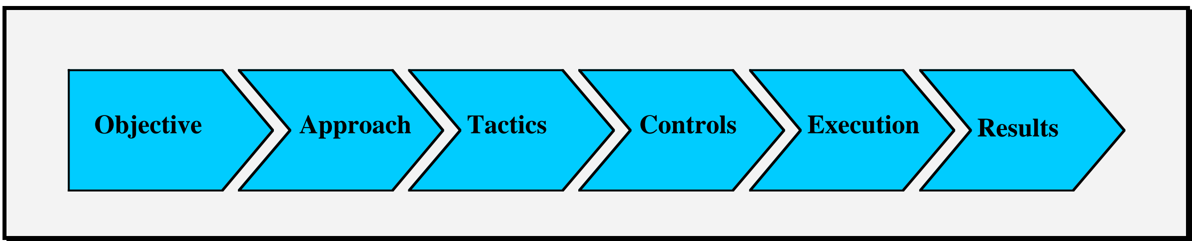
middle market, LT – large ticket), while others specialized in only one or two of these markets.

The majority of the companies studied were equipment generalists, with the balance focusing on the IT segment of the industry. In addition to a mix of entrepreneurial and traditional companies, the size of the target companies covers a broad range.

Analysis and Findings

The starting point in Alta's analysis was to define the critical decision flow of the company, as illustrated below:

Critical Decision Flow



This approach identified specific steps, such as plans, tactics, and execution, in the decision-making process. Each of these critical steps could then be analyzed as to its impact on the eventual demise of the target companies. Included in this process are an analysis of management motivations, any correlation between the tactics, controls, and execution thereof, and the result of those actions.

The study results are heavily dependent on Alta's analysis of diverse information extracted from multiple sources. These sources included targeted company executives, other targeted company stakeholders, industry executives, the ELA *Survey of Industry Activity*, and Alta's internal database, industry experience, and network of contacts. The staff and volunteers at both the Foundation and ELA provided valuable assistance in identifying and locating specific companies and industry executives to interview, and in providing insights and logistical assistance.

The primary source of information, however, was the interviews. Alta conducted confidential interviews with over 30 individuals, using a standard set of questions (see Appendix One for details on the nature of these questions). Alta's experience was utilized to draw additional information from the process and stimulate thoughtful discussions of relevant issues.

Alta gathered financial statement data for as many of the target companies as possible. This data, which primarily was public company data, was used to generate various measures of performance. The primary measures considered are shown in Exhibit Three.

The baseline for the numerical analysis was overall industry performance for the five-year study period of 1996 through 2000. Industry data from the ELA's *Survey of Industry Activity* was used to establish the baseline. Only certain measures had a narrow enough distribution to utilize in drawing what Alta considered meaningful comparisons with target company results.

Exhibit Three

Financial Measures

Leverage
Times Interest Earned
ROA
ROE
Asset Growth Rate
Income Growth Rate
Net Margin
Provision for Credit Losses
Charge-offs to Assets
SG&A to Assets
Other Assets to Total Assets
Residual Write-downs
Year-end Share Price
Average Cost of Funds

The mean, the nominal variance, and average annual variance from the baseline were used to identify those company measurements that either varied significantly from, or closely tracked, the baseline. The correlation coefficients between the baseline and target company trend lines were calculated to determine any correlation, either negative or positive, between the target group and industry norms. Alta also assessed the likelihood of failure or bankruptcy for the target companies based on Altman's Z-score model[5].

Loss provisions, as a percentage of total assets, decreased from 1997 to 1999 and then increased by more than 30-fold in 2000.

It is clear that most of the target companies, although seeking to increase shareholder wealth, failed to even *maintain* value. Such a conclusion leads to an asking of the question, "Why?"

The data analysis, as a whole, did not yield a treasure trove of useful information. This lack of utility primarily is a function of the broadness of the public data, inconsistencies in presentation of the information, the short timeframe being considered (both in terms of years and the life of some companies), and certain aberrations in the baseline data. Data correlation also must be evaluated in the context of the data being compared.

The loss provision data of FINOVA, for example, tracked the baseline data quite closely. As it turned out, however, significant credit losses were the trigger for FINOVA's demise. The loss provisions from the financial statements, as a percentage of total assets, decreased from 1997 to 1999 (.8%, .5%, and .2%, respectively), and then increased by more than 30-fold in 2000. Charge-offs, also as a percentage of total assets, averaged .5% from 1997 to 1999, jumping to 5.3% in 2000.

In this respect, the reported financial statement measures did not reflect the economic realities of the company's situation. This disconnect occurred because:

1. The procedures and controls relating to credit risk, nonaccrual, and write-offs were circumvented through the use of "approved management exceptions", and

2. What appear to be inadequacies in the functioning of the control and governance features relating to the reserve for doubtful accounts, credit concentrations, and overall credit quality.

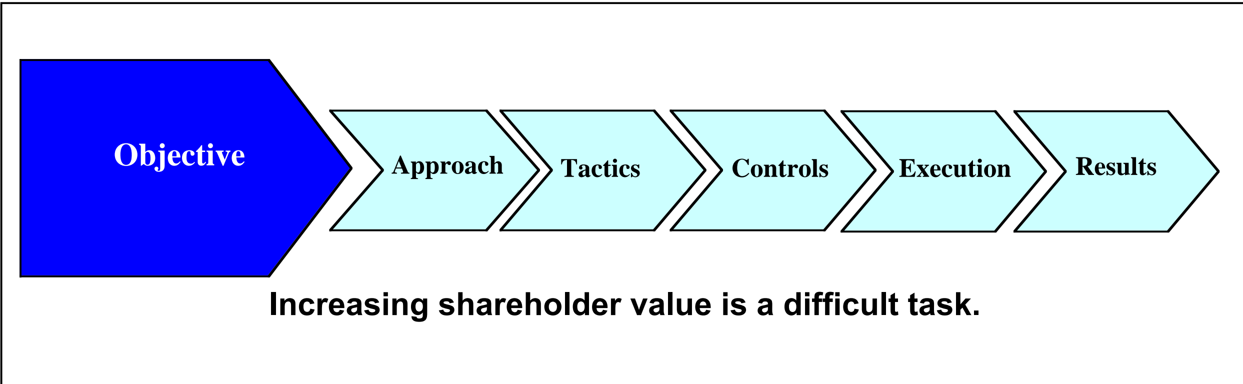
There were several interesting relationships noted for individual companies. For instance, when there was correlation between the data, there usually was significant magnitude in the variances between the data lines.

This result suggests the importance of not only looking at company trend lines and percentage changes, but also at the absolute variance between the company and industry data. (Although comparisons were made between the group and baseline data, they were suspect due to the inconsistency of data

between companies, and the extreme variances encountered in the final year of company operations.)

The likelihood of bankruptcy, based on Altman's Z-score, was determined to be high for three of the four companies for which applicable data was available. The analysis was based on the two years prior to the declaration of bankruptcy. Key factors noted included negative working capital (inadequate cash from operations), significant declines in retained earnings (mounting or continuing losses), an inability to raise additional equity (liquidity crisis/flight to quality), and debt maximization (high leverage).

It should be noted that, while the Altman model indicates the possibility of bankruptcy, the unclassified nature of the balance sheets and the low availability of data make these conclusions difficult to rely on.



Increasing shareholder value is a difficult task.

The equipment leasing and finance market, as it has matured, has become more commodity-like and much more competitive. These two factors have conspired to compress margins. As a result, increasing, or even maintaining, shareholder value has become more difficult. Companies throughout the industry have struggled with this problem.

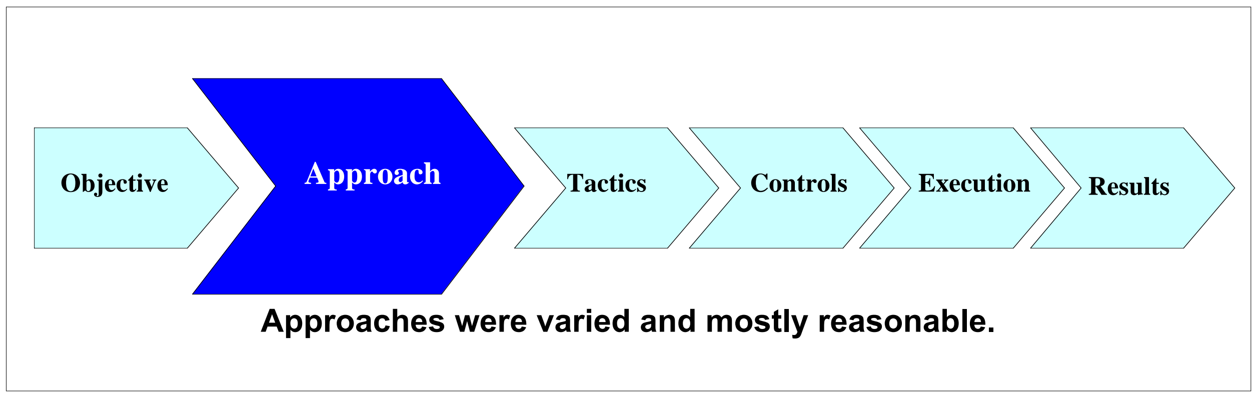
Not surprisingly then, the common objective of the target companies was to increase shareholder value. (Shareholder value, in this context, is used in its broadest sense, i.e., value to the owners, public or private.) This objective does have several sub strata, however, some of which may run counter to each other.

One reason for management to increase shareholder value, for example, is that it better positions the company to issue equity and take advantage of the capital markets (i.e., by enriching, or presenting the possibility of enriching, current and future stakeholders). Another motivation for increasing shareholder value is management self-interest, particularly if management compensation is tied to share price[6].

Management held stock ownership positions in many of the target companies. Management ownership in Comdisco, for instance, was both significant and widespread. Comdisco embarked on a strategy to transform itself into a sector that commanded higher price/earnings multiples. Since higher multiples create direct pecuniary consequences for management, it is possible that management self-interest played a role in the direction this company was taken.

The overall good of the shareholders is sometimes suborned by managements' self-interests when compensation is based on share price. Contrarily, management may be unwilling to take measured risks or innovate without proper motivation to do so. In Comdisco's case, compensation practices had a positive effect by forcing the company to consider many different business opportunities. Unfortunately, it was unable to successfully execute the plan for achieving its goal.

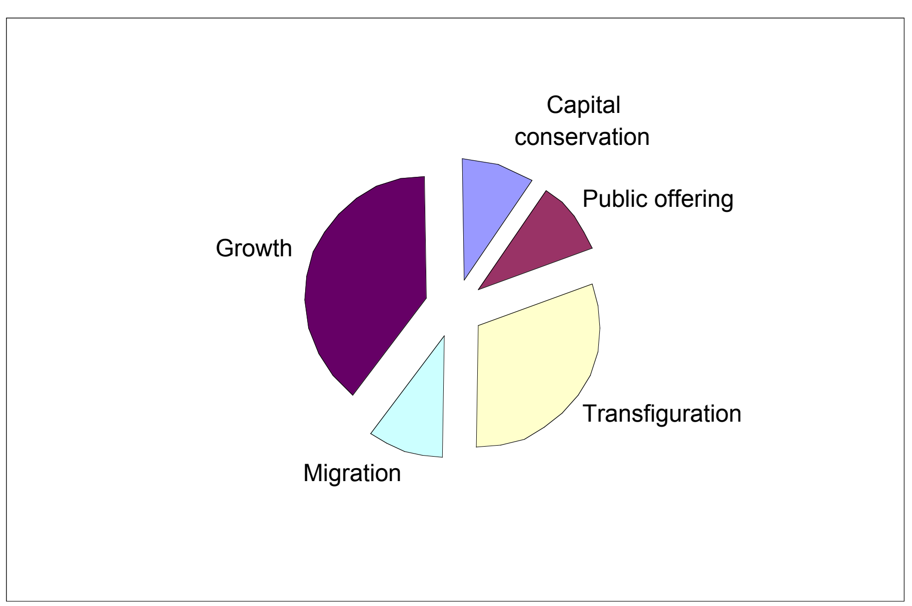
Both sides of this argument present compelling reasons for ascribing to one above the other. Perhaps the disconnect occurs in the timing of management rewards; that is, short term versus long term. In this study, it appears that the stock-based compensation of management had a material and adverse affect on several of the companies.

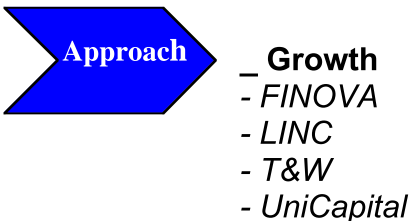


Although all the companies shared the same ultimate objective, there were various approaches for achieving that objective. Some companies stayed with one approach, while others used more than one. Exhibit Four illustrates the breakdown of the primary company approaches.

Exhibit Four

Common Approaches



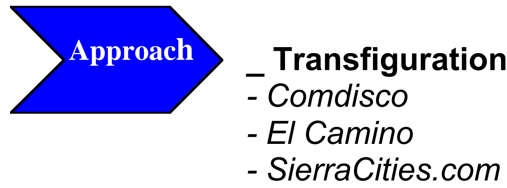


_ Growth
- *FINOVA*
- *LINC*
- *T&W*
- *UniCapital*

Some companies chose growth as the vehicle for increasing shareholder value. LSI sought growth both in the number of its vendor relationships and in the international market, while FINOVA and LINC chose to grow internally and through acquisitions. SierraCities.com and UniCapital, on the other hand, relied on acquisitions for their growth.

T&W focused on rapid organic growth and, by using funds raised through its IPO, portfolio acquisitions. As one T&W interviewee put it, "Imagine suddenly finding yourself with millions and millions of dollars to plow back in the business, and couple that with the 'grow or die' mantra of the rapid industry consolidation that was taking place in the late 1990s. They went on a buying spree…"

Growth as an approach is not at issue here. How these companies tried to achieve growth did create problems, however.



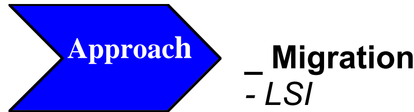
_ Transfiguration
- *Comdisco*
- *El Camino*
- *SierraCities.com*

Other companies chose the transfiguration approach, in which they attempted to transform themselves into something outside of their core competencies. These companies offered a non-leasing image to investors and analysts. Specifically, Comdisco, SierraCities.com, and El Camino decided to transfigure themselves as technology companies because technology price/earnings multiples were much higher than those of leasing companies. One former

"The old-line business of leasing was not sexy nor high profile enough for Wall Street."

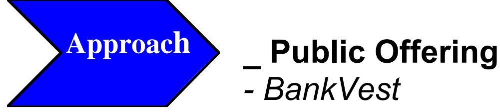
executive commented that, "The old-line business of leasing was not sexy nor high profile enough for Wall Street."

Comdisco and El Camino decided to use their equipment knowledge and technology expertise as a springboard into technology. El Camino focused on technical services, while Comdisco invested heavily in its Prism acquisition, in what were viewed as opportunistic responses to market factors. These companies set themselves up for failure by trying to become something they were not.



The migration approach involved staying within the company's core competencies. LSI decided to stay within its leasing competency, but followed a migration path into a different market. This migration consisted of shifting from leasing "infrastructure" equipment such as telecommunications equipment and mid-range computers, to leasing desktop technology. Although this approach was sound, LSI did not properly prepare for the migration.

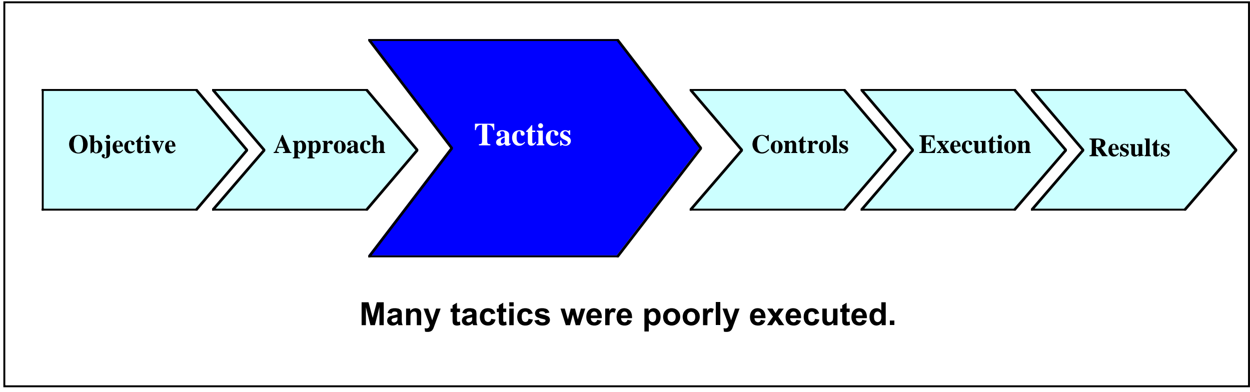
Banc One purposefully left all leasing markets that were not supportive of building relationships with bank customers. This action was taken as a means to better employ its capital and improve the parent bank's ROA. Capital should always be put to its best use, and, in this regard, Banc One's approach was sensible.



The route BankVest chose to follow to increase shareholder value was to bring the company to a critical mass and level of profitability sufficient to go public. This approach was intended to provide an IPO exit strategy for the investors. Positioning a company for an IPO is not unusual. BankVest, however, failed to properly execute and control its approach.

The common objective of increasing shareholder value appears sound, at least on the surface. The results of the study, however, support the hypotheses that shareholder wealth should be a direct outgrowth of the lessor's value to the marketplace.

That is to say, an increase in shareholder wealth is the natural, although not only, result of establishing value to the marketplace. There are cases, for instance, in which companies have increased shareholder wealth without establishing value to the market. Long-term success, however, is more likely if the emphasis is on creating value to the customer. This emphasis was absent in many of the target companies' approaches.



Subject to our observations regarding the ordering of value creation, most of the approaches taken by the target companies were reasonable in concept. This combination of laudable objective and reasonableness of approach placed most of the target companies on the track to success, at least up until this point.

As might be expected, the companies employed a wide variety of tactics to implement their chosen approach. Some of these tactics were common to several of the companies, although not all of them created value. Tactics utilized by the study companies included:

_ **Relying on gain-on-sale accounting**

LINC, BankVest, SierraCities.com, T&W, and UniCapital all relied on gain-on-sale accounting to drive their earnings. Although acceptable under GAAP, total reliance on gain-on-sale accounting represents a flawed business model. This model is unsustainable, as it forces a company into a cycle of ever-increasing volume expectations. Due to the flight to quality in the capital markets, particularly after the Asian financial and Russian debt crises of 1998, these companies were forced to rely on bank lines.

Because of the reliance on this flawed business model, they faced dramatic increases in borrowing costs and the slashing of margins and returns. The

fallout from this tactic hastened the departure of these companies from the industry.

_ Using the roll-up model

SierraCities.com and UniCapital also used the roll-up as a business model. Although perceived as a success in other industries such as funeral homes, waste management, and food services, the roll-up did not create additional value in the equipment leasing context.

As applied to the equipment leasing and finance industry, the roll-up model did not achieve the expected synergistic results. There were difficulties in assimilation, integration, and achieving scalability. All the roll-up concept did for leasing was to create additional competitors that, at worst, were not even marketplace rational.

"Nothing made a compelling case that the roll-up model would ultimately succeed."

As Tad Briddell, the UniCapital turnaround specialist said after three months of analysis, "Nothing made a compelling case that the roll-up model would ultimately succeed."[7] This tactic represented a flawed business model that, in combination with other causal themes, resulted in the departure of these two companies from the industry.

_ Shifting core competencies

El Camino put major emphasis on technical services, which was a shift in core competencies. Comdisco and SierraCities.com also shifted core competencies by entering related technology businesses. Additionally, Comdisco further emphasized the technology side of the business through its venture capital unit. This tactic, in each of these companies, appears reasonable given the circumstances. The execution of the tactic, however, was flawed.

El Camino did not have the management expertise to make this shift work. Although its management team had been in place doing leasing for many years, it had limited relational experience in technical services. The failure to

Comdisco provided Prism with cash totaling $478 million for expansion and operating costs.

recognize the need for, and bring in, experienced management in its target field was fatal to El Camino.

There were several flaws in Comdisco's execution of this tactic. Top management at Comdisco also had very little technology business experience. Furthermore, its funding strategies did not change to reflect the new business emphasis. Comdisco changed the nature of its business, yet continued to fund itself as a leasing company.

According to one executive, "Essentially, its form was a technology business, but its substance was still a leasing company. It took on very different risks on the asset side but did not change the right-hand side of the balance sheet."

Comdisco's decision to dedicate so much of its resources to this new competency also looms large, as the Prism acquisition/development and emphasis on the ventures group created a huge drain on liquidity. (From February 1999 through September, 2000, Comdisco provided Prism with cash totaling $478 million for expansion and operating costs.) Management, essentially, bet the franchise on two ventures outside its core competencies.

An argument also could be made that FINOVA had a shift in core competencies. FINOVA recently expanded its operations to include a broad number of business units (18), some of which were outside its core strengths. FINOVA's shift was unsuccessful also because it did not have the management breadth and depth to make this move work.

_ Relaxing and/or ignoring credit controls

Nothing can be said to justify this tactic as being reasonable, yet it was utilized by several of the companies. BankVest employed relaxed credit parameters as a market tactic. This approach was a conscious decision, as opposed to a breakdown in control and governance. In several other instances, credit quality deteriorated as a result of lack of control due to high growth, but this was not a tactic.

At FINOVA, some business units stayed within the given parameters, while others were more lax. This laxness was more prevalent at units that were

looking to grow assets, and, therefore, stretched the credit underwriting criteria.

In some of these units the company charge-off policy was not always followed. Furthermore, business unit management determined the collateral value or recoverability of problem accounts. Accounts also accrued income until charged-off, allowing business unit managers to control income earned and amounts charged off, thereby masking current credit problems.

LSI failed to adhere to concentration parameters, entering into several very large enterprise transactions (some as high as $100 million). FINOVA also found itself with concentration issues, as evidenced by the $70 million write-off of one account in its Distibution & Channel group during April, 2000.

_ Relaxing and/or ignoring residual controls

LSI, in addition to its credit concentration, also had asset concentration issues. In some cases, both the credit and residual concentrations were in one transaction. There also was a relaxation of residual controls at T&W.

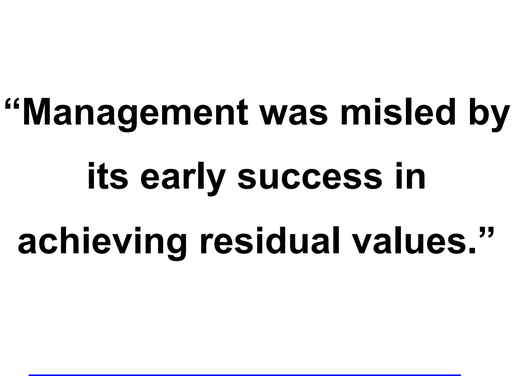
_ Shifting market focus

This tactic was utilized by many of the target companies and includes several variations. Some of these variations include moving from a small-ticket to a mid-market focus, and vice versa, changing from a market specialist to a market generalist, focusing on specialty markets, and shifting between equipment markets.

LSI initiated several shifts in its market focus. For instance it placed strong reliance on its Dell Computer vendor program, including large enterprise transactions, and expanded into the Canadian and European markets. It also changed its equipment focus, moving from leasing "infrastructure" equipment, such as telecommunications equipment and mid-range computers, to leasing desk-top technology.

…as evidenced by the $70 million write-off of one account in its Distibution & Channel group during April, 2000.

While appearing reasonable in concept, several of these steps were either flawed or not properly executed. The shift to desktop leasing, for instance, was accomplished using residual concepts that did not apply to this market. Management applied "infrastructure" equipment residual values to the new equipment category based on the false assumption that off-lease equipment in the desktop market would seldom be returned. This was a mistake.



As one of the interviewees remarked: "Management was misled by its early success in achieving residual values. It failed to take into consideration the differences between reasonable residual expectations for infrastructure equipment such as telecommunications equipment and mid-range computers, and desk-top equipment such as PCs and laptops. Management believed that the same end-of-lease return characteristics would apply, when in fact, they did not."

Management also failed to fully develop the necessary back-end functions of the business cycle, such as equipment tracking and remarketing. In spite of the reliance on high residuals, the company did not have in-house remarketing and residual expertise.

UniCapital shifted resources into a specialty market – aircraft – in which it had little expertise. Top management relied on its Aircraft Segment to carry the company when gain on sale accounting was no longer available. The aircraft group was given more leeway in credit decisions because it was believed the segment could recover any shortfalls from residual proceeds. The emphasis within the company changed to aircraft in 1999, with disastrous results, as the aircraft segment performed poorly in 1999.

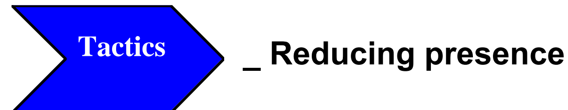
LINC moved away from being a market specialist. As a specialist, its core businesses were analytical equipment leasing, asset-backed leasing in the IT and telecommunications industries, and wholesale programs. LINC's tactic was to become more of a generalist in the vendor program market through acquisitions of smaller lessors specializing in vendor programs.

Although bearing some risk, this move apparently was sound. Again, it was lack of execution that caused the tactic to fail. Proper due diligence was not performed on some of LINC's acquisitions, and delinquencies increased – slowly at first, then rapidly. Management initially believed the increase in

delinquencies was due to the length of time needed to consolidate disparate billing and IT systems. Many of the acquired vendor relationships, however, were bringing high-risk business.

As one executive remarked, “We never did get all the lessors’ systems integrated into LINC’s. We were managing multiple billing systems and multiple processes, and our delinquency levels suffered as a result.”

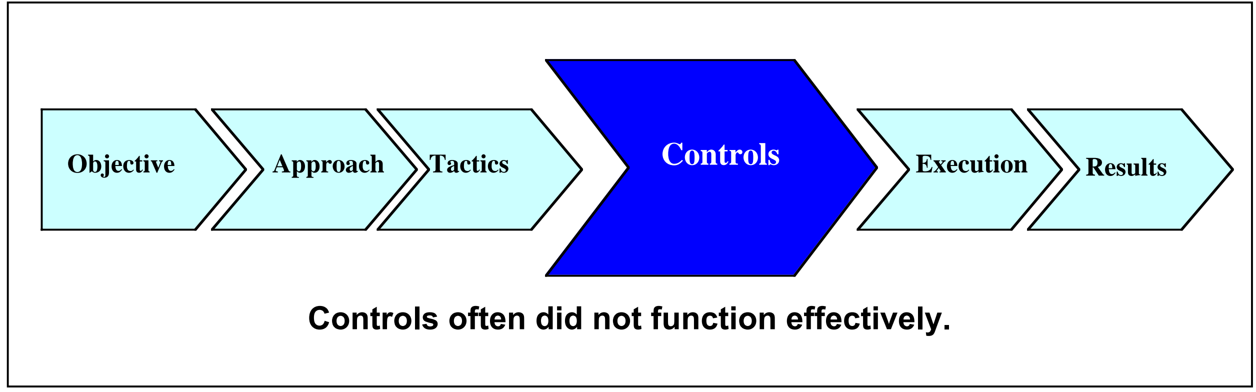
One of BankVest’s tactics was to aggressively attack the middle market vendor sector. Execution in this case was flawed as management’s expertise was in small ticket leasing. BankVest approached the middle market sector using small ticket parameters such as credit assessment and pricing assumptions.

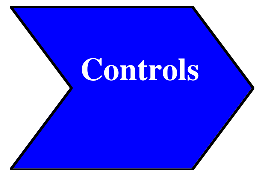


_ Reducing presence

The tactic Banc One used in its approach to maximizing shareholder value was to sell its vendor portfolios and reduce non-relationship staff. This tactic was sound in the context of what Banc One was trying to accomplish. Furthermore, its execution was good.

James Dimon, Chairman and Chief Executive Officer, recently said “Our efforts to reduce costs, manage credit exposure and invest in key businesses are paying off.”[8] However, according to an insider, the bank may have “lost an opportunity to sell the leasing organization or complete an orderly sale of its portfolios by not involving leasing company management.”





Control and governance covers a wide range, from the Board of Directors to the company's policies and procedures. It also can be applied at every step of the decision process. Based on Alta's review, it appears that the controls and governance in several of the target companies were not functioning effectively, or were not in place. These shortfalls occurred at several levels within the organization.

The common objective of increasing shareholder value appears sound and most of the approaches taken by the target companies were reasonable in concept, subject to our observations regarding the ordering of value creation. The control and governance function appeared to be effective up to this point, although more could have been done to control and monitor the pace of growth in many of the companies.

Most of the breakdowns in control occurred at the tactical level. For example, total reliance on gain-on-sale accounting was not a sound tactic and should have been questioned more vigorously at half the companies. Although many companies today still use gain-on-sale accounting, it is only a component of their overall funding strategy.

More emphasis could have been placed on management expertise and experience as companies shifted core competencies and markets. Presumably, this oversight would have to come from outside of the management team. As was mentioned, the failure to recognize the need for, and bring in, experienced management in its target field was fatal to El Camino.

Management breadth and depth also was a factor at FINOVA. UniCapital's shift of resources into the aircraft market falls in this same category. Based on the experience of these companies, it would seem that tactics and strategies could have been questioned more aggressively. This would especially be true for Comdisco's financial commitment to Prism and its technology venture businesses.

Control and governance features did not appear to be functioning effectively at FINOVA, at least as they related to credit parameters. In the case of LSI, large residual concentrations at high dollar amounts were allowed, and back-end functions, such as equipment tracking and remarketing, were not fully developed. The rapid decline and large write-offs at LSI also indicate the possible lack of adequate financial and/or audit controls.

Many of the breakdowns in control and governance, however, appear to be the result of rapid growth. These breakdowns typically occurred at an operational level, although this does not relieve other control and governance checks of responsibility.

More emphasis could have been placed on management expertise and experience.

Rapid growth at both T&W and LINC resulted in a breakdown of business controls. One comment related to T&W indicated, "Their systems were a shambles. They were trying to keep track of multiple portfolios across multiple platforms with an overburdened staff. It wasn't hard to see disaster coming."

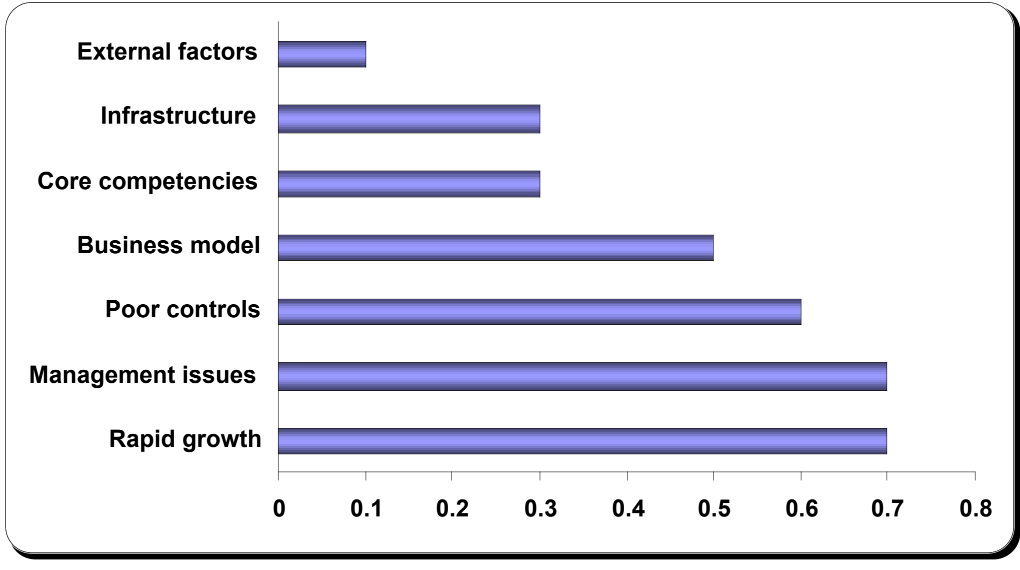
Causal Themes

Alta applied its ValueCAP™ methodology of assessing strategic strengths to identify specific problems and, unfortunately, posthumous solutions. It was discovered that most of the companies succumbed to The Perfect Storm through their choice of tactics, the execution of those tactics, or a combination of the two. For example, in some cases, once desired growth was achieved, the infrastructure was inadequate to handle the additional volume. In others, the cost of funding skyrocketed when gain-on-sale accounting fell out of favor.

The major causal themes of why these companies exited the industry are contained in Exhibit Five. The horizontal bars represent the frequency with which each theme occurred. Rapid growth, for instance, was a contributing factor for exiting the industry in 70% of the companies studied.

Exhibit Five

Major Causal Themes



The following discussion analyzes the causal themes that were instrumental in causing the target companies to exit the equipment leasing and finance market. It is interesting to note that, in most cases, it was a combination of these themes, and not a single theme, that created the problems for the target companies. In this regard, Alta has identified the primary causal theme for each company.

Theme 1 – External Factors

- *Banc One Leasing*

The external factors that impacted several of the target companies did not, by themselves, cause companies to exit the industry. Their impact was felt most when combined with other casual themes. The external factors identified in the study include:

1. The decline in telecommunication and information technology spending
2. The decline in demand for technology services
3. Higher cost of debt as a result of the Asian financial and Russian debt crises
4. A loss of key vendor relationships
5. A change in lessee behavior, specifically, lessees becoming more astute in handling end-of-lease matters and return options
6. The utilization of growth strategies by the competition
7. A decline in residual values
8. The tightening of liquidity markets.

Theme 2 – Inadequate Infrastructure

- LINC
- LSI
-T&W

Most of the companies studied had adequate infrastructure in place to handle their current levels of business. Some did not. LSI, for instance, did not have the internal capabilities for residual realization and remarketing necessary to support its chosen approach. Others did not have the infrastructure to support their chosen tactics.

When growth became a strategic imperative, many experienced growth beyond the company's capabilities. These capabilities include the infrastructure to perform such basic functions as billing and collection, and end-of-term activities. In some cases, the accounting information was not adequate to allow management to perform its oversight and control function.

Rapid growth also outstripped management's ability to control not only the ongoing growth, but also the basic functions associated with past growth. In these cases, management generally failed to address the entire leasing

process, focusing, instead, only on the front-end functions of sales and marketing.

Theme 3 – Stray from Core Competency

- *Comdisco*
- *El Camino*
- *SierraCities.com*

The old saw of 'sticking to one's knitting' became even more relevant during the course of the study. *Eight* of the lessors studied entered new markets, market segments, and even industries within the several years before their exit. Some of these new markets were similar to their traditional ones, and required the same core competencies. Many, however, were not similar, nor was there much similarity in the required core competencies.

In this latter category, some of the differences were subtle and easy to miss, even in hindsight. For example, LSI migrated from leasing one type of IT equipment to another type. In the first instance, which was infrastructure equipment, the lessees seldom returned the equipment as it came off lease. The second type of equipment, on the other hand, was often returned. LSI did not adjust its residual value strategy to reflect this difference, with disastrous results.

Eight of the lessors entered new markets, market segments, and even industries.

Theme 4 – Flawed Business Model

- *BankVest*
- *LSI*
- *LINC*
- *T&W*
- *UniCapital*

Although several companies followed the same flawed business model, there actually is more than one flawed model involved in The Perfect Storm. One of these is the concept of the 'roll-up'. The other is the use of gain-on-sale accounting. *Half* the target companies utilized gain-on-sale accounting.

Theme 5 – Poor Controls

- *BankVest*
- *Comdisco*
- *El Camino*
- *FINOVA*
- *LSI*
- *T&W*

Alta examined the theme of weak controls from an oversight control and corporate governance perspective, as well as internal control mechanisms such as accounting and risk management policies and procedures. The focus of this examination was on three facets of control:

1. The Board of Directors (primary)
2. The external auditors (secondary)
3. The lenders (tertiary)

Alta views these controls as being at different levels. The Board of Directors is the primary control point for the company while the external auditors provide an overall, secondary check of the company. The lenders, who have no fiduciary obligation to monitor the health of the company, only their own self-interests, serve in a tertiary, or back up, role.

The results of Alta's interviews and analyses indicated a potential failure on the part of several Boards of Directors to exercise their fiduciary duty of control and governance. Interviewees also raised questions as to how the problems that were developing in some of the companies could be missed by the external auditors.

Alta addressed this latter question with members of the auditing profession. Several of the auditing executives interviewed agreed that the auditors could have made a combination of mistakes. The more important issue, however, is that the role and responsibilities of the outside auditor are often misunderstood. As one audit executive stated, "There is a clear gap between the presumed and actual responsibilities of the auditor." Some of the presumed (and inaccurate) responsibilities of the external auditors include the roles of equipment appraisers, judges of portfolio credit quality, and adjudicators of management's strategic plan.[9]

The lenders to an equipment leasing and finance company represent a tertiary, but non-fiduciary, form of control. Alta spoke with several lenders to some of the victims of The Perfect Storm. The main theme, or self-accusation, arising from these discussions was that lenders at times did not truly understand the leasing businesses to which they were lending. As one

lender put it, "Lenders to lessors often have a lack of appreciation for the magnitude of the distinctions between leasing and lending."

Another theme that emerged more than once was that the capital structure of some lessors became a major control problem. One banker, who experienced this issue first hand, said: "One of the challenges as a lender is to insure that there is an alignment of interests between all of the lender constituencies and the management of the lessor."

Theme 6 – Management Issues

- *Comdisco*
- *El Camino*
- *FINOVA*
- *LSI*
- *SierraCities.com*
- *T&W*
- *UniCapital*

The inadequacy of senior management played a significant role in several of the target company failures. This fact is viewed as somewhat surprising, given the focus the industry has provided over the last decade to the principle of employee development, empowerment, and training.

Shortcomings in senior management were found in several areas and at different levels. Management problems were encountered at both the strategic and operational levels. Specific areas of weakness include lack of leasing-related experience, too much reliance on too few executives, lack of relational, executive business experience, and a lack of managerial support at lower levels.

These management issues were, in many cases, ones of circumstance. Management simply did not have the skills and leadership ability to contend with the rapid changes. As one executive remarked, "For the most part, I think these were good people trying to do the right thing. It is just that their reach exceeded their grasp."

Theme 7 – Rapid Growth

- BankVest
- FINOVA
- LSI
- LINC
- SierraCities.com
- T&W
UniCapital

Seven of the ten lessors in the study experienced rapid to very rapid growth during the several years preceding their exit from the industry. Growth, for purposes of this study, means the volume of new business generation. Rapid growth refers to growth in excess of 25% per annum.

In some cases, growth was a central point in the lessor's strategy. In others, growth was a byproduct of the lessor's move into new markets or industries. In yet others, growth was a management tactic to address declining margins. Whatever the reason for the rapid growth, its existence often contributed materially to the company's exit from the industry by exacerbating other issues.

As can be seen from the preceding discussion, many of the target companies shared causal themes for exiting the equipment lease and finance market. Some may view this commonality as a source of concern, in that more than one company has fallen victim to its themes. In many respects, however, this commonality may be viewed as a positive sign, for it clearly points to areas of risk and concern that have affected many companies. As the saying goes, 'forewarned is forearmed'.

Lessons Learned

Exhibit Six contains a summation of the study findings, presented in the form of Alta's critical decision flow model. (Individual company analyses are located in Appendix Three.) Based on this process, and the causal leasing environment themes that were identified, Alta suggests the following as lessons to be learned from the fallout of The Perfect Storm.

- The equipment leasing and financing market has become more commodity-like and much more competitive. Margin compression is an unpleasant fact. *Eight* out of the ten companies involved in The Perfect Storm became victims because of failed strategies to improve their income performance. Return expectations that were materially higher than industry norms were often the germ of these failed strategies.

- Rapid growth is often a sign of future problems. Of the ten companies studied, *seven* experienced significant problems because of growth levels that exceeded management's ability to control it.

  This is not to say that growth, or even rapid growth, is bad, in and of itself. It must, however, be carefully monitored and potential trouble spots identified. Areas to monitor include deterioration of asset quality, unusual employee turnover, operational stress, and changing margins. Each of these problem areas contains additional signals that must be watched.

- Problems associated with oversight controls and corporate governance were contributors to the failures of *nine* out of the ten companies studied. While most of these problems were related to ineffective boards of directors, the role of the external auditors cannot be dismissed as a contributing factor. The Board of Directors should include individuals with financial services experience.

- The interruption of continued access to the capital markets with reasonable terms and conditions was a major factor in the failure of at least *seven* out of the ten lessors studied. The ability to properly manage access to the capital markets is one of the most critical required core competencies in the equipment leasing and finance market.

  In many of these cases, existing lenders' inability to understand the lessor's business plan and/or the loss of trust interrupted access to the capital markets. Two conclusions are clear:

  1. Lenders to the leasing industry must thoroughly understand their borrower's business and any material changes that may impact it.

2. Lessors must thoroughly define and explain their business to lenders.[10]

- The emergence of strategic initiatives that are inconsistent with the lessor's core competencies is often a sign of future problems. In at least *six* of the cases studied, the lessor had initiated major business strategies that had little or nothing to do with its core business.

Lessors must thoroughly define and explain their business to lenders.

This issue overlaps with several other findings of the study. The Board of Directors, for instance, could have modified these strategies, or even prevented them from being implemented. The same can be said for strong and experienced management. External feedback, through either the Board of Directors or third parties, is a critical component of developing and implementing a sound and viable strategy.

- Strong marketing, sales, and new business volume performance are not enough. Companies must be able to manage the complete business cycle within competitive standards. At least 50% of the companies involved in The Perfect Storm became victims because substantive portions of their business cycle were inadequately managed.

- The strength and adequacy of senior management was a factor in 60% of the cases studied. These factors ranged from management experience that was not relational to the environment of the lessor, to situations where too much reliance was placed on too few executive managers, to situations where executive managers did not have, or did not require, sufficient support from second line managers.

  As the latest Foundation *Industry Future Council Report*[11] stated:

  > "To compete effectively, firms will require more focused and consistent leadership. ….Leasing companies, must, for example, find more managers with longer-term, strategic outlooks – who are more strategic than tactical, more tactical than operational and transactional."

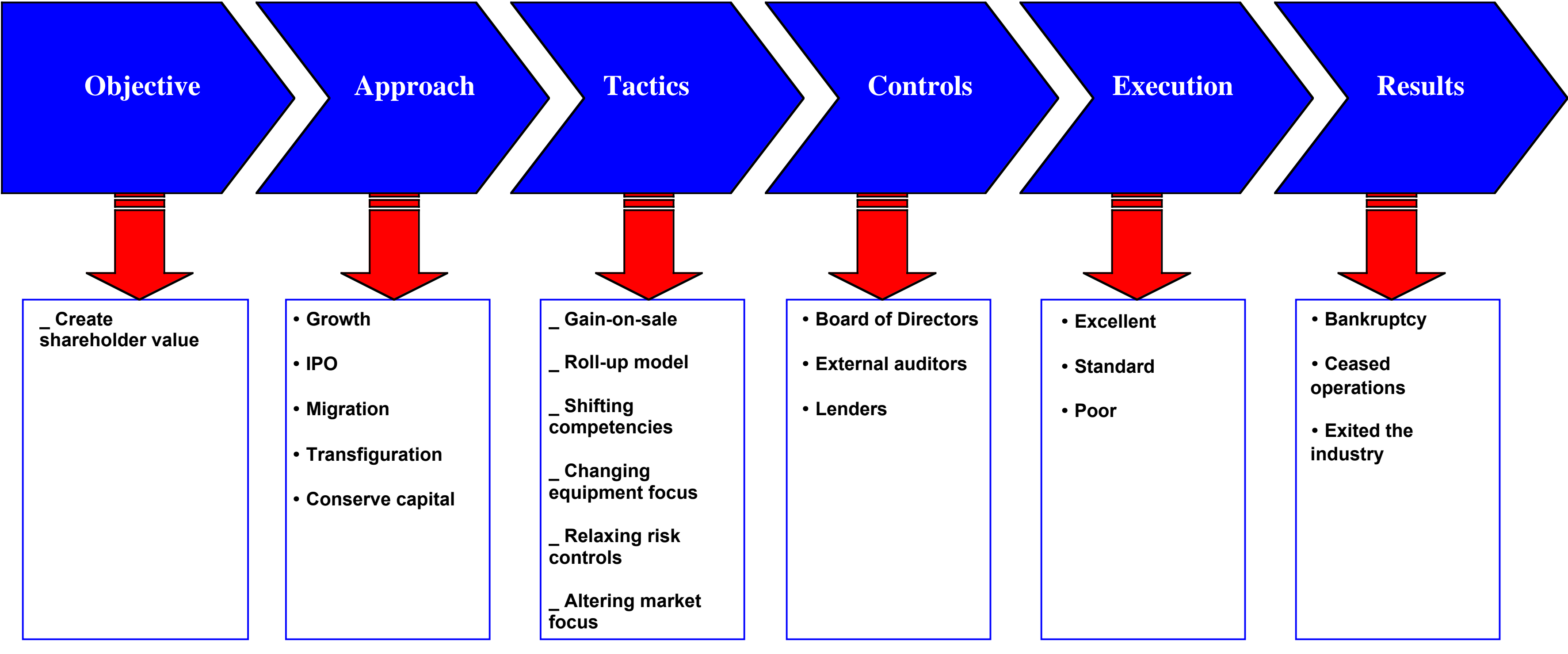
- Management of the target companies usually understood the serious nature of their company's problems on a timely basis and took definitive action to try to correct the problems. The definitive action, however, often

was unsuccessful. The problems, at least within the contexts studied, had become too big and serious for management to control.

This inability to correct the problems on a timely basis reflects the realities of operating in a leveraged environment. Leverage works to the company's advantage when things go well, but it magnifies and accelerates problems when they do not. As a result, much like a supertanker whose course has been set, these companies found themselves unable to turn quickly enough to avoid The Perfect Storm.

Exhibit Six

Summary of Findings



Conclusion

The captain of the Andrea Gail, was looking for the “big catch.” In doing so, he took his boat and crew into waters outside his experience. Although there were more fish there, he increased the risks in a business already fraught with risk. Furthermore, he ignored the warning signs of impending trouble, thinking he could work his way through what turned out to be a dire situation.

The Perfect Storm in the equipment leasing and finance industry has many parallels with that of the movie. Many of these lessors, looking for the “big catch”, entered businesses outside their core competencies. Others created additional risks beyond those systemic to the industry. And, many ignored the warning signs when they came, hoping to work their way through the situation.

The combination of these factors with a cold front of inadequate infrastructure, a hurricane of external events, and a Great Lakes gale of poor controls brought the seas crashing down upon them. In the end, Captain Tyne’s reach, like many of those in this study, exceeded his grasp.

This project, however, indicates that the identified failures were a result of avoidable problems, and are not prophetic of a failing industry. Furthermore, there are useful indicators such as deterioration of asset quality and changing margins that may be used to prevent similar scenarios in the future.

The equipment leasing and finance industry has changed. Growth has slowed and ROEs have stabilized. It is clear that nonstandard returns can only be achieved with difficulty and additional risk. Will those in the industry learn from The Perfect Storm by recognizing the ramifications of these changes? Will they conduct business accordingly in the future?

Past theories of consolidation and size must now give way to a new, proactive theory of the industry – the value imperative. A company does not have to be large to prosper, let alone survive, under the value imperative. Size is no longer the determining factor. A focus on value, or lack thereof, will determine the winners and victims of the future.

Value is the key to continued financial health and viability. Equipment leasing and finance companies of the future must:

Create **value** to survive.
Add **value** to keep customers.
Prove **value** to attract capital.

Industry maturity has created a spread in margins between those that use commodity pricing and those that add value to their products. Accepted wisdom is that only those lessors that create, add, and prove value will achieve desirable yields. The rest will continue to exit the marketplace, Perfect Storm or not.

Appendix One
Interview Questions

1. The company's business model.
    a. Description and parameters
    b. Drivers
    c. Tactics
    d. Divergences

2. The nature and timing of business changes.
    a. Strategic direction
    b. Key personnel
    c. Cost structure
    d. Funding
    e. Information systems
    f. Risk assessment parameters
    g. Asset management parameters
    h. Markets
    i. Products
    j. Core competencies

3. The effect of external factors.
    a. Customer demand
    b. Legislative actions
    c. Regulatory changes
    d. Competitive landscape
    e. Capital markets
    f. Technological changes

4. The role of oversight and control.
    a. Management
    b. Board of Directors
    c. External auditors
    d. Management and executive committees

Appendix Two
2001 Foundation Board of Trustees

Chairman
Thomas C. Wajnert
Fairview Advisors

Vice Chair
Steven F. Groth
Financial Federal Corporation

Treasurer
Deborah J. Monosson
Boston Financial & Equity Corporation

Secretary
Edward A. Groobert
Dykema & Gossett PLLC

Executive Director
Lisa Levine
Equipment Leasing Association

President
Michael Fleming
Equipment Leasing Association

John H. Beville
Suntrust Leasing Corp.

David H. Frankel
Citibank

Paul S. Gass
Help & Profit Company Inc.

Larry Hartman
American Express Business Finance

James M. Johnson, Ph.D.
Northern Illinois University

Robert J. Knapp
Siemens Financial Services, Inc.

Michael A. Leichtling, Esq.
Jenkens & Gilchrist Parker Chapin LLP

Salvatore Maglietta
CitiCapital

Donal R. Ratigan

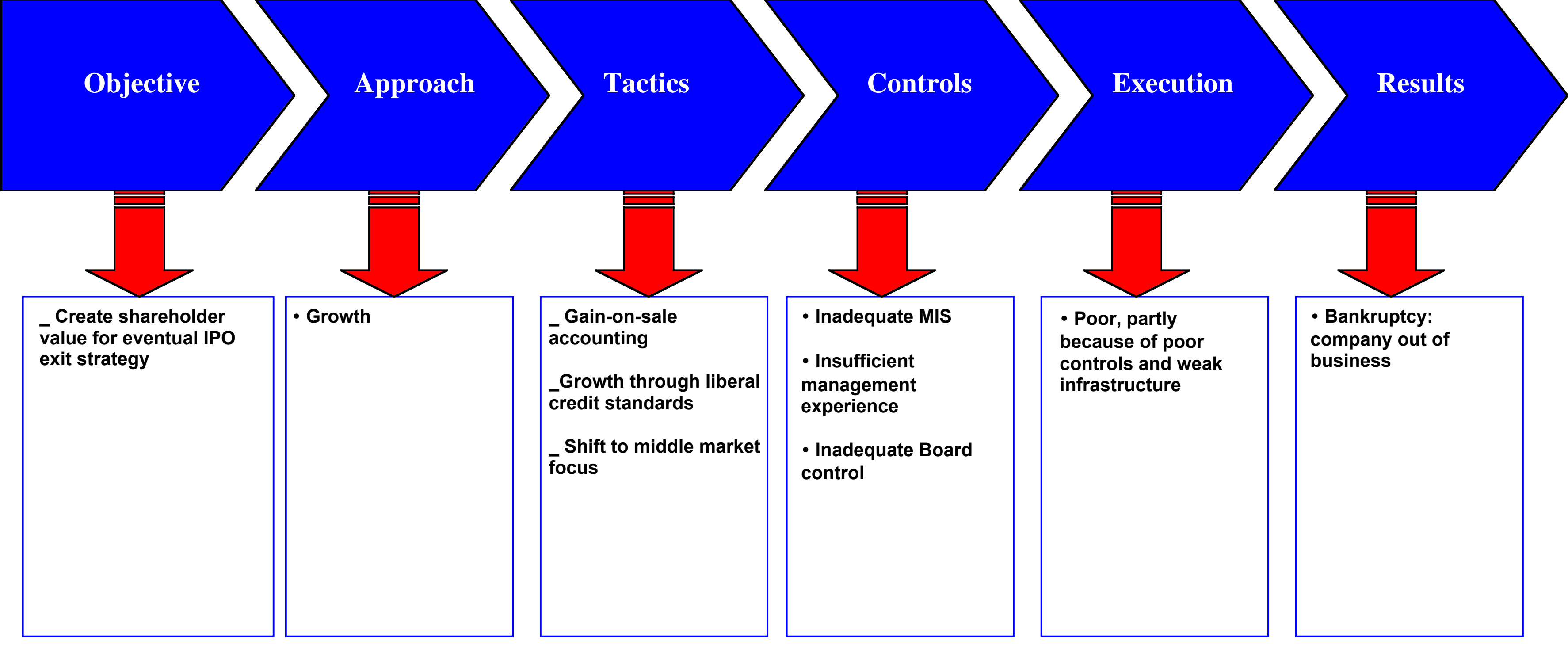
James S. Schallheim, Ph.D.
University Of Utah

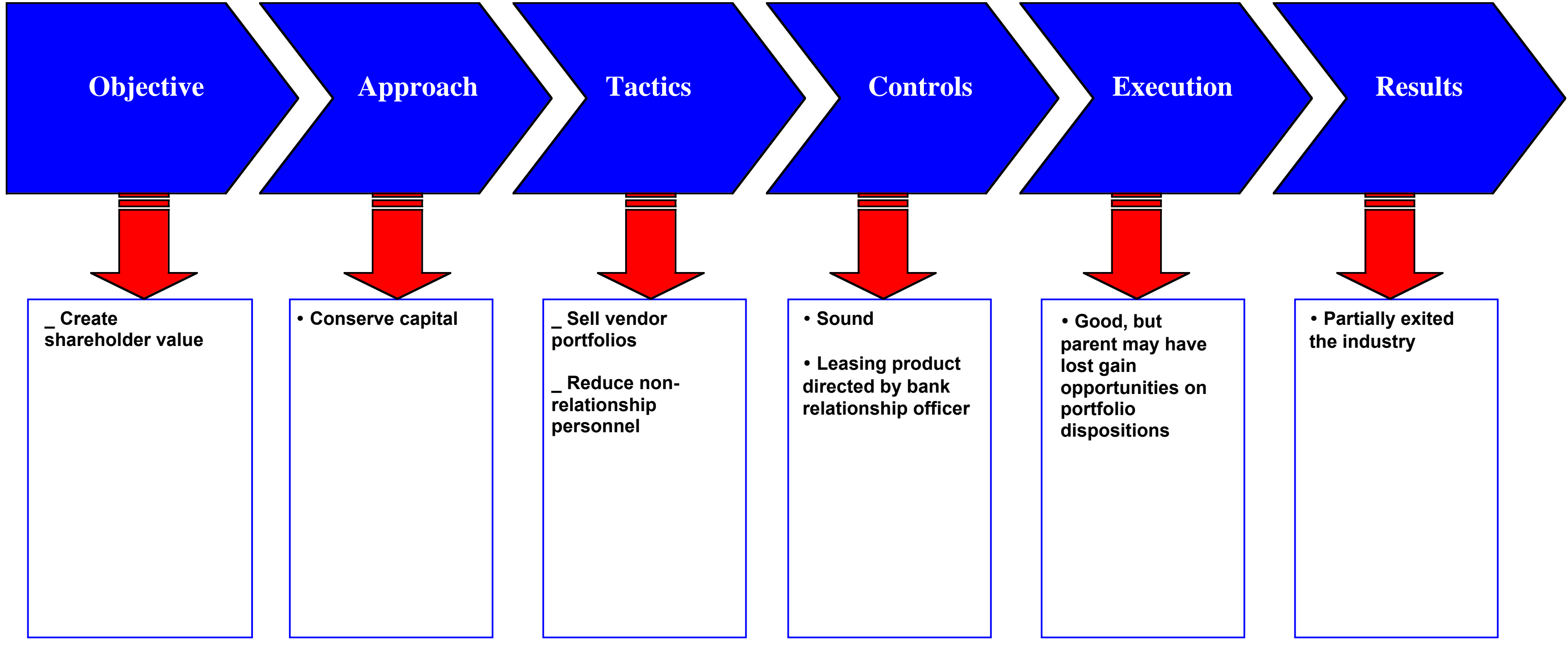
Louis J. Vigliotti
LENDX, Inc.

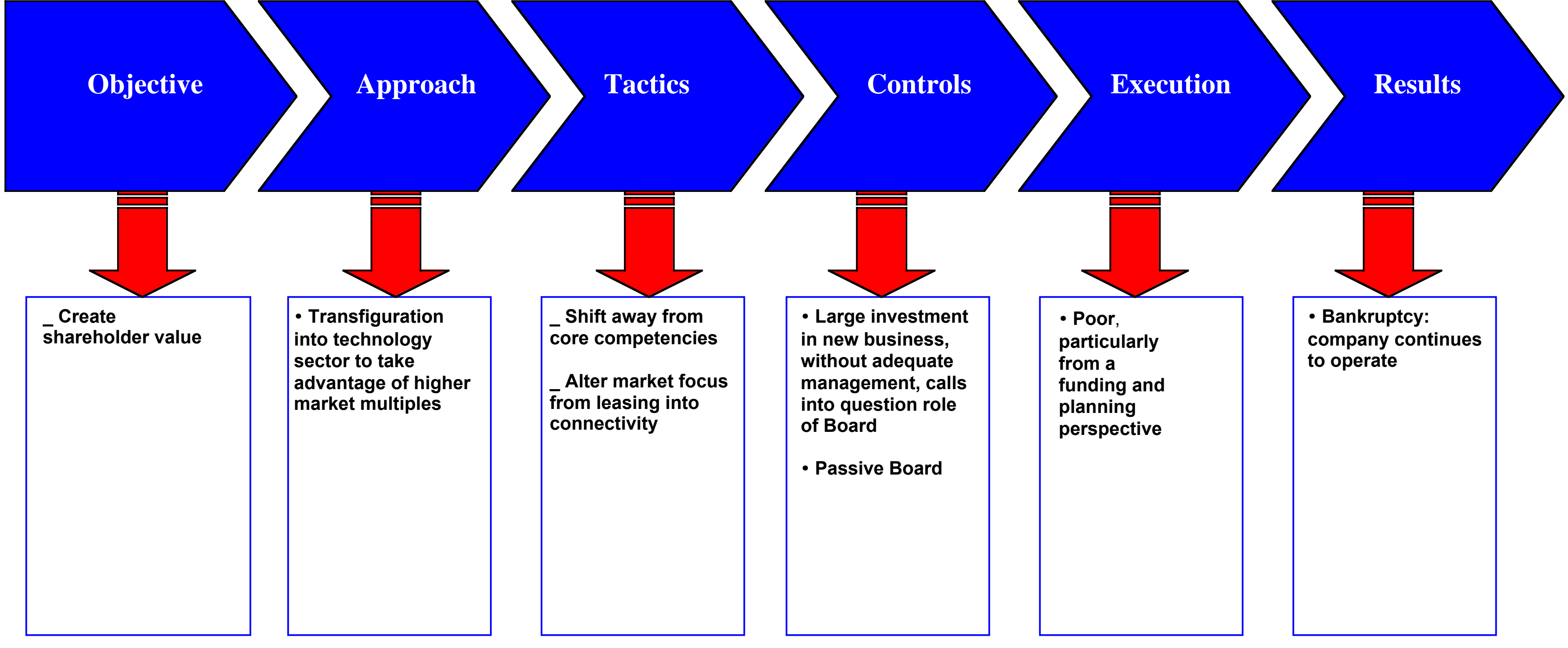
David S. Wiener
GE Capital Markets Services, Inc.

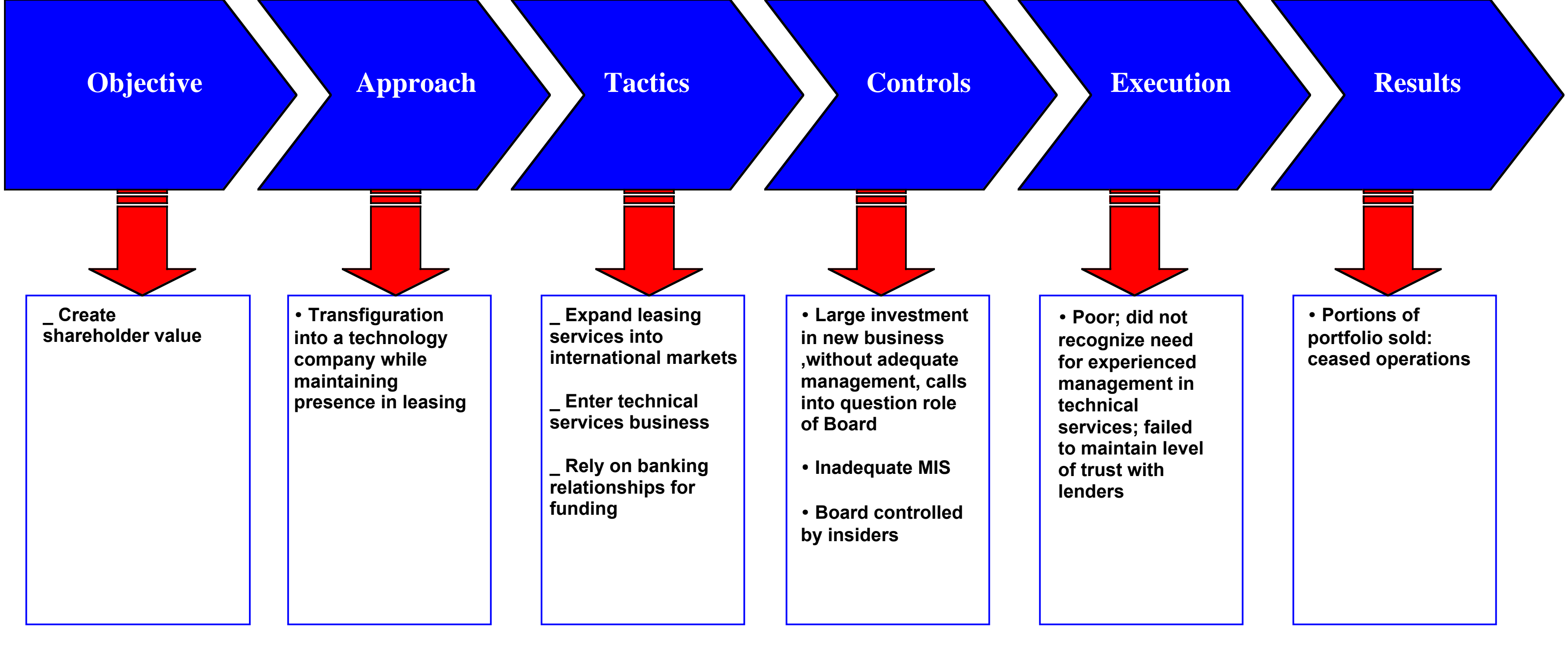
Robert Young
Moody's Investors Service

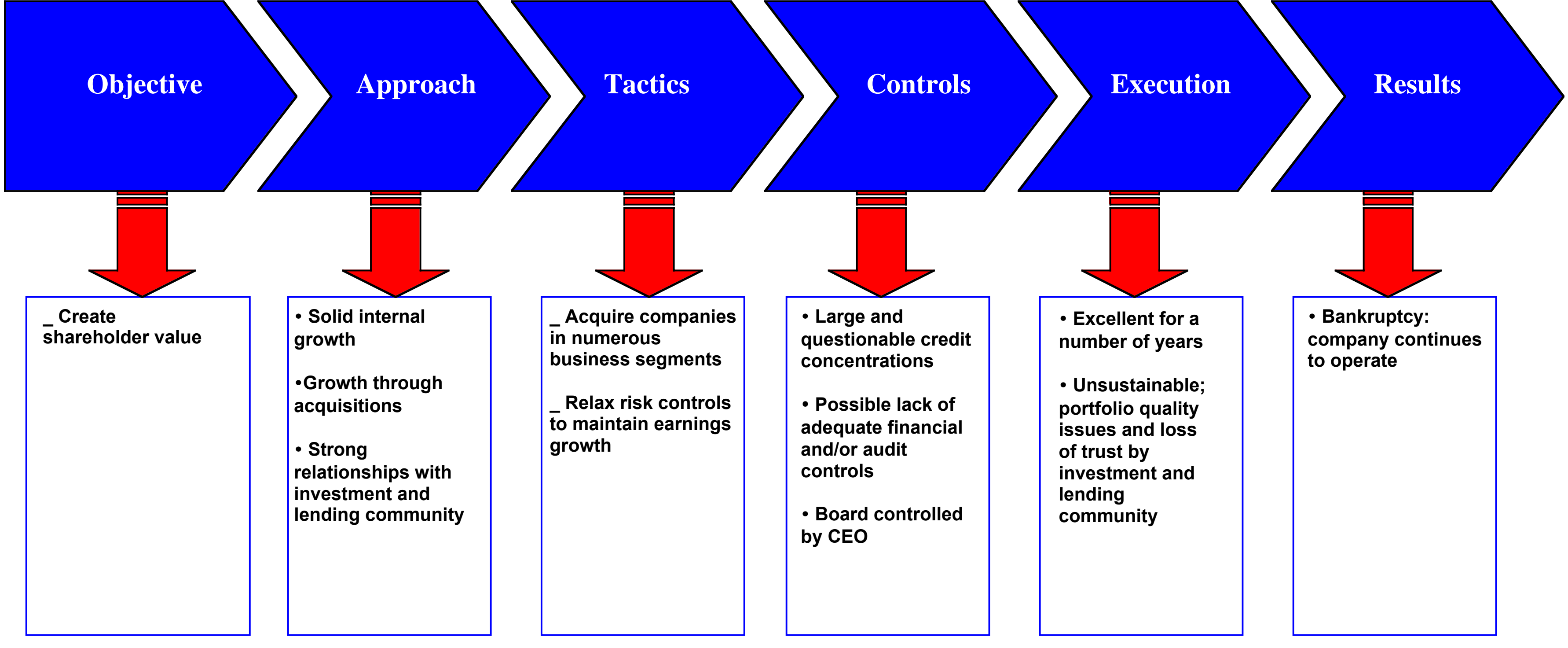
Appendix Three
Individual Company Analysis


BankVest Capital
Summary of Findings
Objective
Approach
Tactics
Controls
Execution
Results
_ Create shareholder value for eventual IPO exit strategy
• Growth
_ Gain-on-sale accounting
_Growth through liberal credit standards
_ Shift to middle market focus
• Inadequate MIS
• Insufficient management experience
• Inadequate Board control
• Poor, partly because of poor controls and weak infrastructure
• Bankruptcy: company out of business

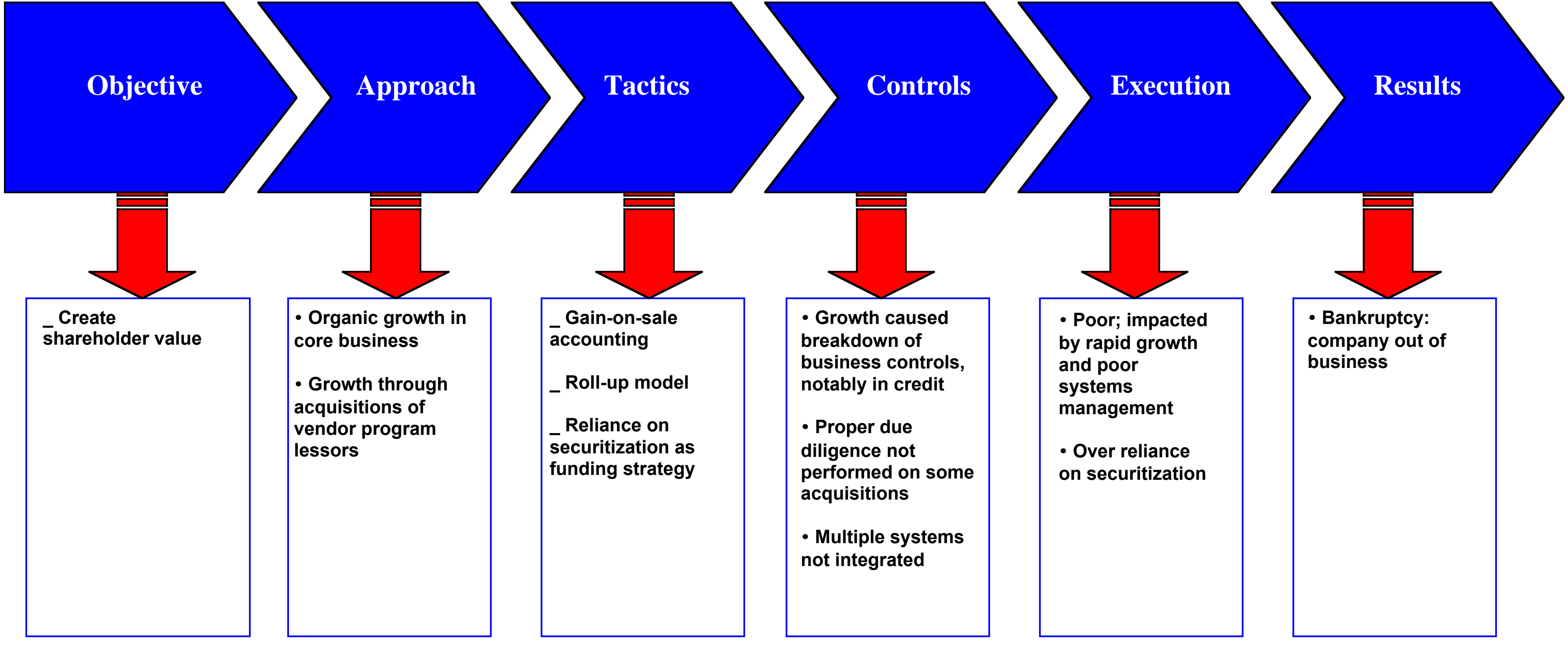

Banc One Leasing
Summary of Findings
Objective
Approach
Tactics
Controls
Execution
Results
_ Create shareholder value
• Conserve capital
_ Sell vendor portfolios
_ Reduce non-relationship personnel
• Sound
• Leasing product directed by bank relationship officer
• Good, but parent may have lost gain opportunities on portfolio dispositions
• Partially exited the industry

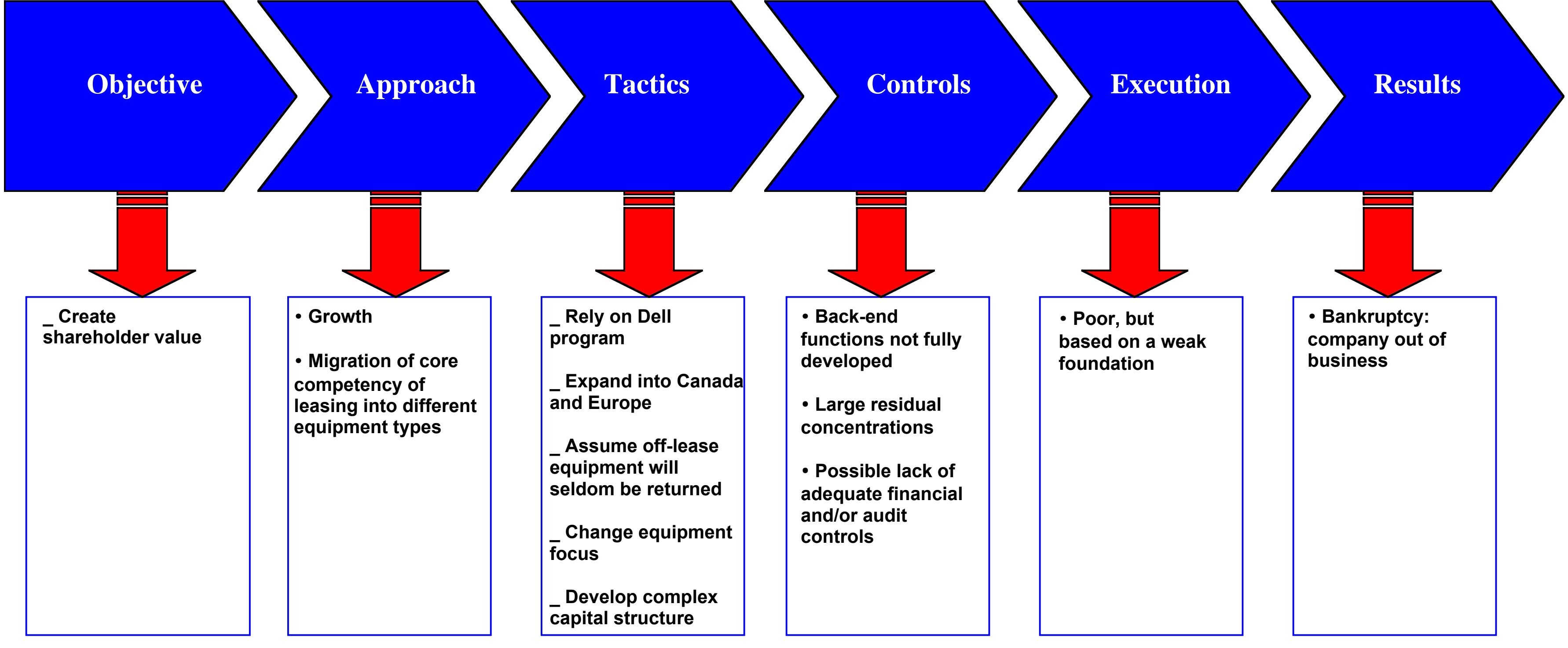

Comdisco
Summary of Findings
Objective
Approach
Tactics
Controls
Execution
Results
_ Create shareholder value
• Transfiguration into technology sector to take advantage of higher market multiples
_ Shift away from core competencies
_ Alter market focus from leasing into connectivity
• Large investment in new business, without adequate management, calls into question role of Board
• Passive Board
• Poor, particularly from a funding and planning perspective
• Bankruptcy: company continues to operate

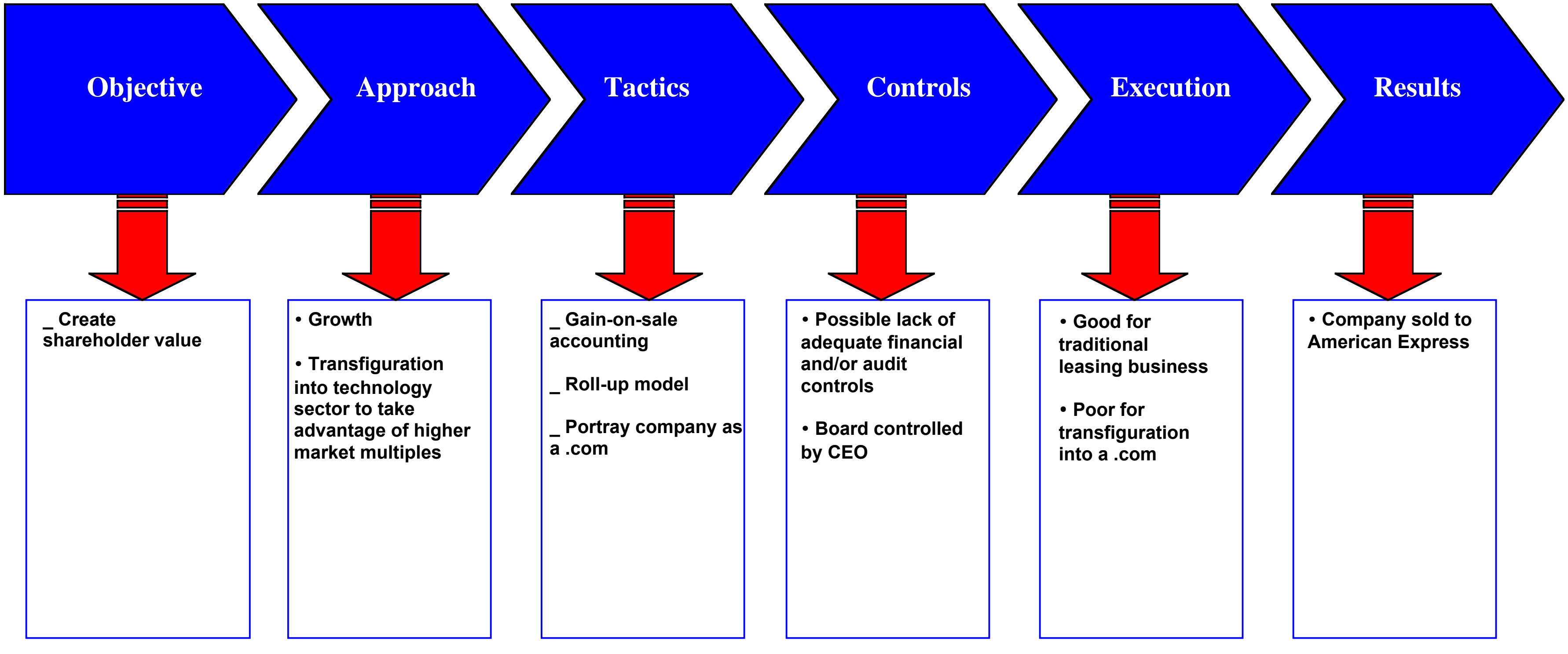

El Camino Resources
Summary of Findings
Objective
Approach
Tactics
Controls
Execution
Results
_ Create shareholder value
• Transfiguration into a technology company while maintaining presence in leasing
_ Expand leasing services into international markets
_ Enter technical services business
_ Rely on banking relationships for funding
• Large investment in new business ,without adequate management, calls into question role of Board
• Inadequate MIS
• Board controlled by insiders
• Poor; did not recognize need for experienced management in technical services; failed to maintain level of trust with lenders
• Portions of portfolio sold: ceased operations

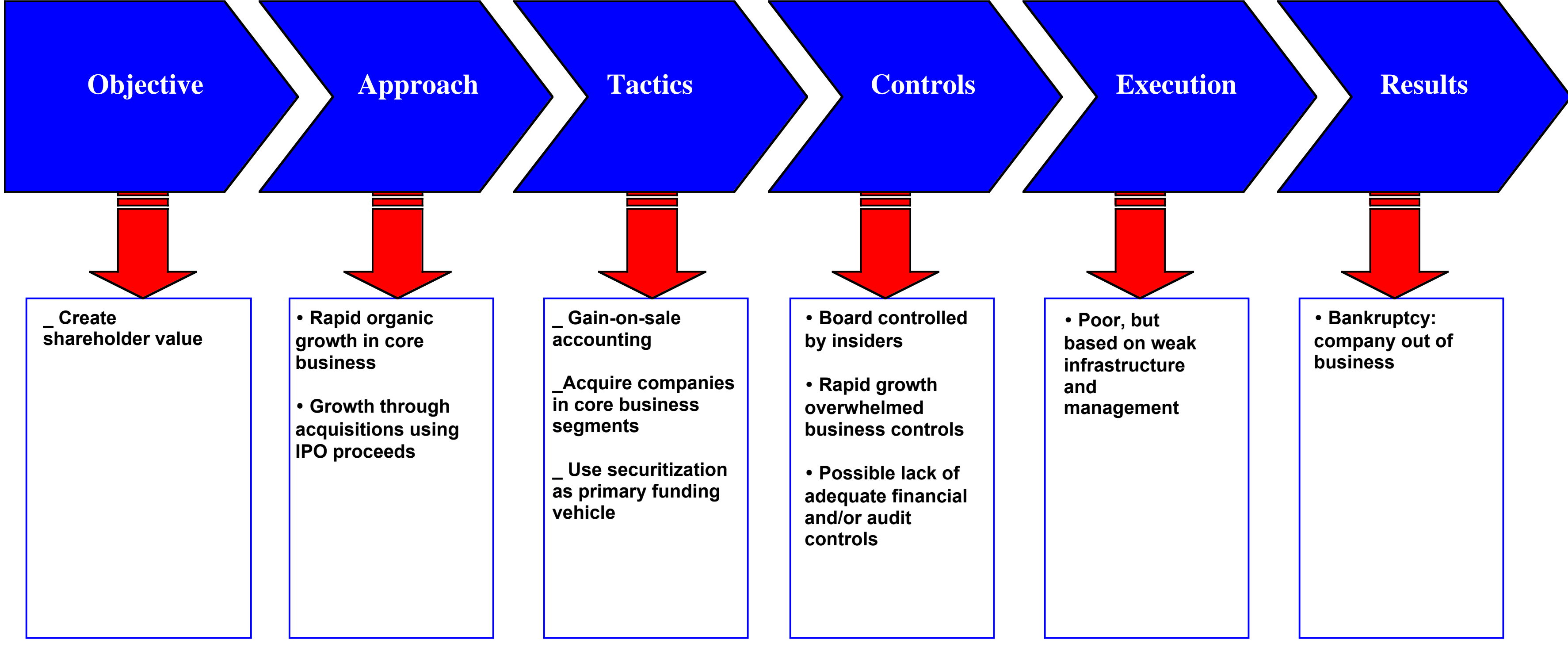

FINOVA
Summary of Findings
Objective
Approach
Tactics
Controls
Execution
Results
_ Create shareholder value
• Solid internal growth
•Growth through acquisitions
• Strong relationships with investment and lending community
_ Acquire companies in numerous business segments
_ Relax risk controls to maintain earnings growth
• Large and questionable credit concentrations
• Possible lack of adequate financial and/or audit controls
• Board controlled by CEO
• Excellent for a number of years
• Unsustainable; portfolio quality issues and loss of trust by investment and lending community
• Bankruptcy: company continues to operate

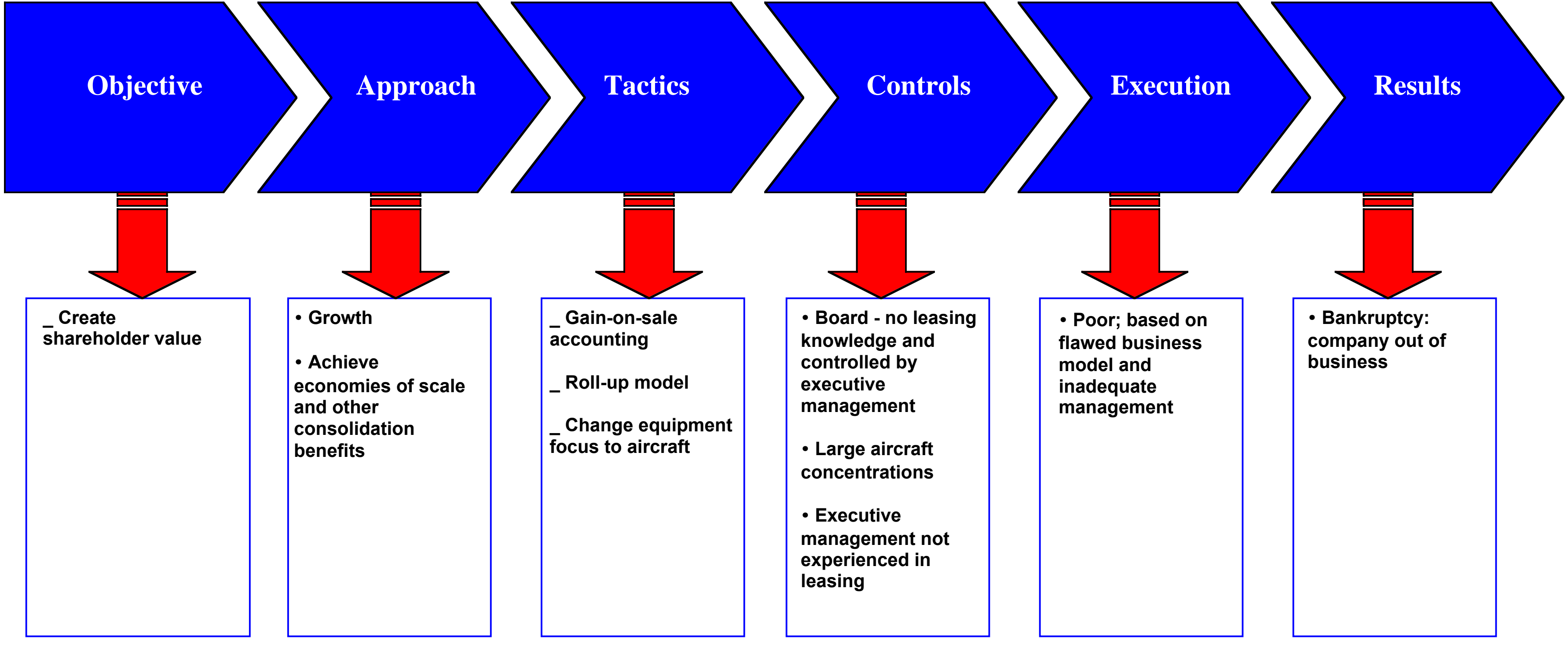
LINC Capital
Summary of Findings




LSI
Summary of Findings
Objective
Approach
Tactics
Controls
Execution
Results
_ Create shareholder value
• Growth
• Migration of core competency of leasing into different equipment types
_ Rely on Dell program
_ Expand into Canada and Europe
_ Assume off-lease equipment will seldom be returned
_ Change equipment focus
_ Develop complex capital structure
• Back-end functions not fully developed
• Large residual concentrations
• Possible lack of adequate financial and/or audit controls
• Poor, but based on a weak foundation
• Bankruptcy: company out of business


SierraCities.com
Summary of Findings
Objective
Approach
Tactics
Controls
Execution
Results
_ Create shareholder value
• Growth
• Transfiguration into technology sector to take advantage of higher market multiples
_ Gain-on-sale accounting
_ Roll-up model
_ Portray company as a .com
• Possible lack of adequate financial and/or audit controls
• Board controlled by CEO
• Good for traditional leasing business
• Poor for transfiguration into a .com
• Company sold to American Express


T&W Financial
Summary of Findings
Objective
Approach
Tactics
Controls
Execution
Results
_ Create shareholder value
• Rapid organic growth in core business
• Growth through acquisitions using IPO proceeds
_ Gain-on-sale accounting
_Acquire companies in core business segments
_ Use securitization as primary funding vehicle
• Board controlled by insiders
• Rapid growth overwhelmed business controls
• Possible lack of adequate financial and/or audit controls
• Poor, but based on weak infrastructure and management
• Bankruptcy: company out of business


UniCapital
Summary of Findings
Objective
Approach
Tactics
Controls
Execution
Results
_ Create shareholder value
• Growth
• Achieve economies of scale and other consolidation benefits
_ Gain-on-sale accounting
_ Roll-up model
_ Change equipment focus to aircraft
• Board - no leasing knowledge and controlled by executive management
• Large aircraft concentrations
• Executive management not experienced in leasing
• Poor; based on flawed business model and inadequate management
• Bankruptcy: company out of business

Equipment Leasing and Finance Foundation

The Resources You Need!

The Equipment Leasing and Finance Foundation is a nonprofit organization whose mission is to promote the growth and effectiveness of equipment leasing and finance companies through programs that identify, study and report on critical issues affecting equipment leasing and finance. The Foundation works to develop the body of knowledge of equipment leasing and finance for use by the industry, academic, and policy communities. The Foundation provides the following FREE resources to you:

- Research Grant Program

The Foundation awards grants funds to academics to study topics of interest to the equipment leasing and finance industry. Proposals are accepted three times each year. Average grant is $10,000.

- Authorship Honorariums

The *Journal of Equipment Lease Financing*, the official Journal of the Foundation, is published twice annually. Authorship honorariums are available to academics and industry professionals that contribute in-depth articles on topics of interest to those working in and/or researching this industry.

- Academic Internships

The Foundation works closely with university students and industry leaders to place students in academic internships within the lease financing industry.

- Industry Reports and Analysis

Annually, the Equipment Leasing and Finance Foundation produces numerous reports and research papers on trends, industry analysis, forecasting and the state of the industry. These Research reports and studies are available to you FREE of charge.

- Website Resources

The websites of both the Equipment Leasing and Finance Foundation and the Equipment Leasing Association (ELA) contain myriad research, statistical material, and industry related information for your use and exploration. Site addresses: www.leasefoundation.org and www.elaonline.com.

- Case Studies and Teaching Modules

  The Foundation has worked with industry and academic leaders to develop cutting edge classroom teaching material including real-life case studies and teaching modules available to academics through the Foundation website.

All of this and so much more is available through the Equipment Leasing and Finance Foundation—and its ALL FREE. Why? Because the Foundation's mission is to enhance the body of knowledge within the equipment lease financing industry. We are happy to provide this information to all academics and professionals interested in the industry.

We would also appreciate receiving your tax-deductible contribution to help support the Foundation ongoing efforts. To make a contribution visit the website www.leasefoundation.org, or call Lisa Levine, Foundation Executive Director at 703-527-8655.

Endnotes

[1] McNair, J., March 22, 2001, '*UniCapital Post-Mortem*', Miami Herald

[2] The movie, The Perfect Storm, is a Warner Brothers release based on Sebastian Junger's book of the same name (Junger, S., *The Perfect Storm*, W.W. Norton, 1997).

[3] Menkin, K., *The List*, Leasing News, www.leasingnews.org

[4] The Equipment Leasing and Finance Foundation is a nonprofit association. It is dedicated to increasing the awareness of the equipment lease finance industry and being the premier disseminator of the equipment lease financing body of knowledge. The Foundation was created in 1989 by the Equipment Leasing Association to conduct research in the industry. See Appendix Two for a listing of the 2001 Foundation's Board of Trustees.

[5] Edward I. Altman originally studied publicly traded manufacturing companies that filed bankruptcy between 1946 and 1965, and found five ratios that most effectively measured financial health. These ratios were multiplied by coefficients and the products added together to form a Z Score. This Z Score was used to determine the likelihood of failure or bankruptcy.

Altman followed up with a later study that showed the original model correctly classified 86% of the 218 companies that filed for bankruptcy between 1970 and 1982. He later refined his original model and developed a four-variable, or general, Z-score model. This general model is broader than the original model and may be applied to private and service companies as well as publicly traded manufacturing companies. Data from Altman's most recently completed study indicate that the general model Z-score can be effectively used as a predictor of possible bankruptcy.

[6] Professor Michael C. Jensen, a noted expert on a wide range of economic, finance and business-related topics, has addressed the issue of management self-interest and compensation in articles such as '*Performance Pay and Top Management Incentives*,' and '*Value Maximization, Stakeholder Theory, and the Corporate Objective Function*.'

[7] McNair, J., March 22, 2001, '*UniCapital Post-Mortem*', Miami Herald

[8] *Bank One Corporation Press Release*, Chicago, October 16, 2001

[9] Most of the major public accounting firms publish information concerning corporate compliance programs that deal with this subject in more detail. In part, they often address the pronouncements dealing with the subject.

[10] *A Guide for Effective Funding and Capital Market Presentations*, produced by the Equipment Leasing Association, provides guidance to lessors in this regard.

[11] *The 2001 Industry Future Council Report*, Equipment Leasing and Finance Foundation, 2001.