

**ELA's Recent Decision to Censor  
Norvergence Report  
at ELA Conference:<sup>1</sup>  
  
and Other Troubling Implications  
Upon the Leasing Industry  
resulting from  
the Norvergence Scandal**

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I received a cordial email on 2/1/05 from Ms. Jade Friedensohn, Event Producer for the Equipment Leasing Association/ Information Management Network, March 10, 2005 Conference: "Thank you for contacting me, Rhonda. I think we are all eager to hear your findings."

Ms. Friedensohn refers both to my submission of an abstract and to my study of the ongoing questions and impact of the Norvergence fraud case. Ms. Friedensohn sent this email and an attached letter inviting me to "join us as a distinguished speaker." This invitation was prompted by my CV, which documents many other papers I have given at prestigious academic venues throughout the world, and by what she told me was the "wide interest in the Norvergence case" among ELA members. Ms. Friedensohn's invitation was also signed by the President of

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<sup>1</sup> The 285 page report, "**THE ROLE OF LEASING COMPANIES IN THE NORVERGENCE FRAUD,**" by yours truly was prepared for the EQUIPMENT LEASING ASSOCIATION: The Fourth Annual Investors' Conference on Equipment Leasing Finance and Securitization, March 10, 2005, Marriott Marquis, New York City, for the **SESSION: COMMON METHODS TO PREVENT FRAUD AND MITIGATE INVESTOR CONCERNS ABOUT TRANSACTIONS "GOING BAD" OR BANKRUPTCY IN THE NORVERGENCE FRAUD.** Despite the last minute banning of my presentation, the report was distributed in the conference CD-ROM earlier in that morning of March 10<sup>th</sup> during registration, before the compliant, upon information and belief, by CIT. Here is the link to my full report [http://www.asrlab.org/temp/ELA\\_Report.pdf](http://www.asrlab.org/temp/ELA_Report.pdf) for those who are interested.

Equipment Leasing Association (ELA), Michael Fleming, and by Scott Brody, Managing Director, Information Management Network). Ms. Friedensohn said that people she spoke to felt an academic would provide yet another perspective among the panel on the topic of fraud, in general, and its specific focus on Norvergence.

In light of Ms. Friedensohn's letters, one can imagine how shocking it was to arrive at the March 10<sup>th</sup> ELA conference registration table just prior to my 1:45 PM talk, and be informed that I was banned from speaking due to a "last minute complaint"? I was told that Mr. Fleming had decided to censor the presentation of my findings. I asked to speak to him for clarification and to lodge a protest. I appreciated Mr. Fleming's courtesy in granting my request to discuss his action (to his credit, for about 30 minutes, at the registration table).

I was unaware, during this discussion, that at 12:53 PM that day, a threatening letter from Mark Melodia, CIT's lawyer in the Norvergence civil case, had been faxed to my office. (CIT most likely hired criminal as well as civil attorneys for its continued involvement in the Norvergence debacle. As reported in the press and in their SEC 10K filing, grand jury subpoenas were issued by the US Attorney's Office in the Southern District earlier in the same week of the conference).

In their letter to me, CIT ominously advised that I should "consult with my attorney" before proceeding with my speech; that my report was "defamatory to CIT" and "at the leading conference for the leasing industry will certainly have a negative impact on CIT."

Mr. Fleming never revealed to me who had complained about my report.<sup>1</sup> In hindsight, I can assume CIT wanted to make sure I would not speak at the conference; beyond their letter, they complained (also threateningly?) directly to ELA; thus causing the last-minute, ham-fisted banning of my talk.

The Norvergence scandal has placed the Equipment Leasing Association and the entire industry on the public stage. How ELA handles the fall-out (a natural consequence of business failure, large losses and scandal, all reflected in my report) will be judged both in the context of the Norvergence debacle and in ELA's larger dealings and practices.

Mr. Fleming's last-minute decision on behalf of ELA's membership to ban my talk, after a formal invitation was sent and commitment was made, because of one member's complaint, has, beyond the particular Norvergence scandal, placed the very credibility of ELA's practices at stake.

### Three factual issues affecting ELA's internal and external credibility

- 1) In the context of academic and conference protocols, the radical action of censorship of research findings was made. Mr. Fleming censored my talk against all academic and conference norms, without even reviewing my report, and without enough information

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<sup>1</sup> Here is the link to my full report [http://www.asrlab.org/temp/ELA\\_Report.pdf](http://www.asrlab.org/temp/ELA_Report.pdf)

to weigh the facts fairly from all parties before making a judgment and then taking action.

- 2) Mr. Fleming took the side of a single member, CIT, at the expense of other members who would have benefited from my anecdotal survey at the meeting, and who were indeed interested in learning the facts about what went wrong in the Norvergence case. Not everyone took the Norvergence deal, yet because of it, all leasing companies are paying the price of exposure to a possible government crack-down as well as a tainted reputation. Leasing company members who participated in the Norvergence deal are motivated to hide what they did wrong. It's fair to assume these leasing companies do not want peers, competitors and investors to know what actually went on. By favoring CIT with a cover-up, other members miss vital information and lessons learned, and, since the industry does not acknowledge its error, it signals the government and public to a need for intervention with new government regulations. Mr. Fleming's action on the part of CIT can bring the thought readily to all members that, in ELA's regular practice, through Mr. Fleming, one powerful member can exact control over what other members are permitted to hear.
  
- 3) ELA and its Foundation conducts industry research reports, and funds and publishes papers. From Mr. Fleming's willingness to ban the presentation of my findings, members and the public now can fairly question whether other similar forms of censorship take place in ELA's research products, resulting in skewed and biased conclusions, rendering the data invalid.

Now, I will set aside my feelings of personal and professional offence and, what gives the appearance of questionable managerial and ethical judgment in the matter of censoring my presentation.

I here address three matters: First, my view of the absurd industry-wide defense claiming the innocence of the leasing companies involved in the Norvergence scheme. I will discuss (and include) the revelatory text in a Norvergence and leasing companies "program partnership" contract only recently found through litigation discovery. This document provides, for everyone, except Norvergence and leasing companies employees directly involved who already knew, a window for seeing what leasing companies negotiated and agreed to in advance of any lessees. Secondly, I will discuss the exposures and consequences of facts, and accounting and insurance questions, I believe the leasing companies now face. The third matter, involves my recommendations that possibly may assist ELA and its members in avoiding future Norvergence scandals.

## Industry-Wide Accountability Needed: Despite Universal Claims of the Innocence

It is truly difficult, if not impossible, for me and dozens of others whom I interviewed in the equipment leasing field to accept that leasing companies (including Fortune 500 companies) were innocent victims who had been outwitted by two fast-talking Norvergence sharpies. I also find it hard to believe that the ELA and all its members are so omniscient and righteous that outsiders can have nothing to add to your industry dialogue.

During my conversation with Mr. Fleming at the registration table, he expressed several contradictions -- one being a plea that leasing companies were both naïve and invulnerable -- as he explained that this investor's conference was not the "correct forum" for my talk and that an accounting conference might be more "appropriate" if my report happens to vet out [again].

Mr. Fleming made 4 specific statements that merit comment:

- 1) "I know all of these leasing companies and can guarantee that no one did anything wrong."
- 2) "Leasing companies did not consider and did not know, and did not have to know the Norvergence equipment values."
- 3) "Fair Market Values are what the market will bear."
- 4) "It would have been impossible (and "impractical") for the leasing companies to know the Norvergence equipment's value."

Concerning Mr. Fleming's first statement, "I know all of these leasing companies and can guarantee that no one did anything wrong," I'm sure, in retrospect, he did not mean it literally. A blanket denial of wrongdoing on the part of any and all parties and employees (amounting to thousands from accounting to sales, in all approximately 40 leasing companies, large and small, involved) is more an emotional and paternal response than a reasoned one, akin to a father saying to a teacher or the police, "my boy did nothing wrong."

However, with all due respect to Mr. Fleming, I want to point out that this psychological denial expressed from the top of your industry is not indicative of credit or praise of members who passed on the Norvergence deal, versus other members who did participate and were in error-- as the facts of scandal, large losses, black eyes in the press and troubling SEC disclosures prove.

In principle, since many of ELA members correctly passed on the Norvergence deal, to their credit, while other members in bad judgment purchased 200 million dollars of Norvergence leases, it would seem important not to penalize the more judicious members by unequivocally backing those who failed, managers and shareholders alike, and who scorched the entire industry. If those who went terribly wrong are not held accountable by the industry, "Norvergence" will happen again.

New Documents indicate Leasing Companies' "Leasing Programs" with Norvergence were "Partnerships"

Mr. Fleming's statements 2 and 3 indicate his belief that leasing companies did not consider, know, need to know, and that it was not possible or practical to know Norvergence equipment values. His statement 4 defines "fair value" as the amount that someone will pay or the amount the market will bear.

If the Norvergence equipment cost and value were irrelevant, as Mr. Fleming and your industry have publicly claimed, why, in contradiction to this "fact," were the submission and receipt of Norvergence equipment invoices and spec sheets for two basic types of equipment, determined by leasing companies to be used as the key information (in addition to the Delivery and Acceptance paper), that *triggered leasing companies payment to Norvergence?*

Such specific terms, as what Norvergence, as vendor, would be required to supply to leasing companies, and when leasing companies would make payments was carefully detailed (and obviously, negotiated) in "vendor lease agreements." Also called "leasing program partnership" contracts, these agreements for mutual commitments and disclosures (including information about the equipment), upon information and belief, had been negotiated and signed between leasing companies and Norvergence, well before any small business signed a Norvergence lease. See "Commerce Commercial Leasing Vendor Lease: A Commercial Leasing Program Proposed Exclusively For Norvergence" attached with this document."

Among the references to equipment clearly stated and agreed upon by leasing companies in these leasing company/vendor contracts are: requirement that Norvergence (the vendor) provide:

Mentions of Equipment in the Commerce Commercial Leasing Vendor Lease:  
A Commercial Leasing Program "Partnership" Between CCL and Norvergence

1. "New and unused" equipment
2. Leasing Company would limit "funding the equipment cost up to 100% of full purchase price...plus 20% allowable soft costs"
3. "Vendor agrees to assign any reps or warranties for the equipment purchased by vendor that are provided by manufacturer"
4. Vendor supplies "a full and complete description of the equipment" as part of the "prospective" renter/customer "credit review"
5. Leasing company requires "each equipment invoice must have an equipment cost equal to or greater than \$5,000 and the minimum monthly payment...must be \$50.00 or more"
6. A "fixed amount purchase option" where Norvergence can repurchase equipment from leasing companies for a set amount.

A clause titled “Equipment specifications” states: “With respect to the equipment, each lease transaction will not become final until, among other things, assignee (leasing company), verifies the equipment specifications including, but not limited to: Model number, serial number, number of units, and installation costs; and approves the final equipment.”

How, in the light of these contracts between leasing companies and Norvergence, and their usual terms, can Mr. Fleming possibly indicate that leasing companies did not consider, know, need to know Norvergence equipment values and that it was impossible and impractical to know Norvergence equipment values? As an industry outsider, with no on-staff residual or valuations experts typically found at the big leasing companies, I easily acquired a professional appraisal using the very same spec sheets Norvergence provided the leasing companies within one week. CCL charged Norvergence a \$5,000 fee “to cover program set-up costs which includes, but is not limited to vendor qualification, credit and documentation legal review” before doing anything else beyond their initial deal memo. Reimbursement of the \$5,000 would not be made “until 1 million dollars in lease volume is booked.” CCL could just as easily charged \$10,000 and used the extra \$5,000 to get a top-notch appraisal in less than one week.

No one from leasing companies called the Adtran manufacturer of Norvergence equipment, according to the product manager. Residual experts and telecommunication appraisers would have been able to inform leasing companies quickly and easily the value of the two Norvergence products. I hope ELA and members conclude from this appraisal (included in my ELA conference report) and from the expectations stated in the leasing company/ Norvergence contract, that it was indeed possible for leasing companies to have obtained or required Norvergence to obtain and provide, arm’s-length fair values of the Norvergence equipment, expediently and cheaply.

FASB 13 carefully defined “Fair Value”: EITF 00-21 even goes further requiring “Vendor Specific Objective Evidence” of Equipment Fair Value

Concerning Mr. Fleming’s statement 4 and his definition of fair value. In the FASB, Statement 13, rules for accounting, the definition is clear and contradicts his own notion that fair value is essentially what any fool is willing to pay. Considered of importance, FASB uses their definition of “Fair Value” 69 times throughout Statement 13. See <http://www.fasb.org/pdf/fas13.pdf>, page 5.

*5.c. Fair value of the leased property.* The price for which the property could be sold in an arm's-length transaction between unrelated parties.

This definition becomes more specific with regard to whether a lessor is or is not a manufacturer or dealer.

- i. *When the lessor is a manufacturer or dealer*, the fair value of the property at the inception of the lease (as defined in paragraph 5(b)) will ordinarily be its normal selling price, reflecting any volume or trade discounts that may be applicable.
- ii. *When the lessor is not a manufacturer or dealer*, the fair value of the property at the inception of the lease will ordinarily be its cost, reflecting any volume or trade discounts that may be applicable.

Related to this issue of the definition and leasing companies' duty to know fair market valuation in the Norvergence leases is FASB's EITF 00-21 requirement for unbundling of services and equipment in a lease. As in the false revenue reporting fraud case with Xerox, Norvergence leases were based on their willful conflation of services as equipment, booking both, upon information and belief, as if equipment cost and profits on their balance sheets were first year earnings. This accounting fraud allowed profits to be taken years before the actual delivery of services, exactly what Xerox had done in their scandal.

The fact of Norvergence having completed two leases--one for services and one for equipment--and sold only the "equipment lease," offers no reprieve from the EITF 00-21 requirement of rigorously seeking the fair value to determine and allocate what services as distinct from equipment in a lease.

On page one, EITF 00-21 specifically cites (emphases mine), "In applying this Issue, separate contracts with the same entity or **related parties** that are entered into at or near the same time are presumed to have been negotiated as a package and should, therefore, be evaluated as a single arrangement in considering whether other are one or more units of accounting." See quotation below from [http://www.iasplus.com/resource/00-21\\_draft.pdf](http://www.iasplus.com/resource/00-21_draft.pdf). Note: final version of EITF 00-21 is same as this draft version for 16.

**16. Contractually stated prices for individual products and/or services in an arrangement with multiple deliverables should *not* be presumed to be representative of fair value. The best evidence of fair value is the price of a deliverable when it is regularly sold on a standalone basis. Fair value evidence often consists of entity-specific or vendor-specific objective evidence (VSOE) of fair value.**

As discussed in paragraph 10 of SOP 97-2, VSOE of fair value is limited to

- (a) the price charged for a deliverable when it is sold separately or
- (b) for a deliverable not yet being sold separately, the price established by management having the relevant authority (it must be probable that the price, once established, will not change before the separate introduction of the deliverable into the marketplace).

The use of VSOE of fair value is preferable in all circumstances in which it is available. Third-party evidence of fair value (for example, prices of the vendor's or any competitor's largely interchangeable products or services) is acceptable if VSOE of fair value is not available.

In order to ensure compliance to the unbundling rules, EITF-00-21 requires what it calls "VSOE" (Vendor Specific Objective Evidence) to determine the fair market value of multiple deliverables, including services and equipment. If leasing companies are required to supply these valuations, they cannot afterwards feign ignorance that services were included or that they inadvertently had been misallocated as equipment.

New Scrutiny into Leasing Companies' Common Business Practices: Can Vendors and Leasing Companies really have "Partnership Programs" and *still be* "unrelated Parties" in the same Portfolio?

A more complex discussion and exposure for leasing companies involves the question of whether or not leasing companies are actually *related parties* in relation to Norvergence. As related parties, as cited above, leasing companies doubtless must apply EITF 00-21 rules for unbundling services and equipment.

If leasing companies are *unrelated* third parties, as has been the present assumption, FASB 13, also seems to require assignees of leases, the leasing companies, to maintain the same accounting method used by the original lessor, Norvergence. This being true, the unambiguous need for unbundling compliance and proper Vendor Specific Objective Evidence must be similarly applied by leasing companies' accounting. See FASB 13, page 13 (emphasis mine):

#### **Participation by Third Parties**

20. The sale or **assignment of a lease** or of property subject to a lease **that was accounted for as a sales-type lease or direct financing lease shall not negate the original accounting treatment accorded the lease.**

However, the view that leasing companies are, in fact, *related parties* appears to be a possible perspective based upon the material facts and timing and the vendor/leasing company partnership contracts.

FASB 13, 5. c. definition of "*Related parties in leasing transactions*" on page 5, includes "...an investor (including a natural person) and its investees, provided that the parent company, owner company, or **investor has the ability to exercise significant influence over operating and financial policies of the related party.**"

5.c. cites specific examples of “significant influence” which includes “extensions of credit.” (As typical in these “partnerships,” CCL and other leasing companies set a volume limit for booked leases, say, \$400,000 per month and 5 million total for the first year. The leasing companies would then “monitor portfolio performance throughout the year to determine volume objectives after the first year.” If Norvergence failed to reach the contracted lease volumes, funding could be completely cut off by leasing companies in these “program partnerships.”

An accounting professor at a major business school wrote to me in response to my questions about the possible status of leasing companies’ involvement with Norvergence as a related party. He suggests, off-the-record, two possible views from an accounting perspective:<sup>2</sup>

The close connection between Norvergence and CIT (and other real lessors) prior to the inception of the leases (e.g., CIT evaluating the credit of the potential lessees) means either:

- a) Norvergence is not a substantive entity but rather simply a conduit for the lessors to obtain "leases" that basically aren't, suggesting that the lessors should "look through" Norvergence in their accounting, *or*
- b) CIT (and the other real lessors) are complicit in Norvergence's (rather than their own) accounting fraud.

If Norvergence did not invest 3% of total capital invested by the leasing companies, it may be concluded that since Norvergence had no “substantive” equity (according to FASB, their standard requires at least a 3% investment in order to qualify as a "substantive" investor), this arrangement between leasing companies and Norvergence was, in fact, a Special Purpose Entity (SPE) for the benefit of leasing companies.<sup>3</sup>

In the Norvergence case, the SPE would be, what’s called a layered SILO with each of the leasing companies having no cross collateralization would, individually consolidate their accounting with Norvergence. “The holder in due course” defense against the linkage of leasing

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<sup>2</sup> Almost every leading leasing experts I interviewed is afraid to criticize the leasing industry openly ; either they fear they will lose business and be “black-balled,” or they are unable to weigh-in due to conflict of interest. I believe this muzzling of counter viewpoints creates a dangerous situation where everyone is told what they want to hear and that it places an extra burden upon the ELA to be open, to transcend and even solicit views contrary to the “party line,” in order to ensure safety for its members. I will address this point again in my conclusion.

<sup>3</sup> Please see white paper discussion on this topic of consolidation and the 3% rule:  
[http://library.lp.findlaw.com/articles/file/00037/002060/title/Subject/topic/Banking%20%20Finance%20Law\\_Lending%20%20Secured%20Transactions/filename/bankingfinancelaw\\_1\\_19](http://library.lp.findlaw.com/articles/file/00037/002060/title/Subject/topic/Banking%20%20Finance%20Law_Lending%20%20Secured%20Transactions/filename/bankingfinancelaw_1_19)

companies to Norvergence's misdeeds, in this case of consolidation, is no longer a lifeboat for leasing companies.

Can Leasing Companies book an "Equipment Lease" as Assignees, Holders in Due Course, and a "Net Receivable:" when the Original Lessor never funded the lease, and it was never properly allocated , as services *and* equipment according to EITF 00-21?

Normally, vendors send leases to the leasing company on behalf of the lessee, and the leasing company then puts the lease in its own name and funds the lease. Assignments occur when this lessor, who originally funded a lease, sells it to a third party, or other leasing company.

Norvergence's plan, in concert with leasing companies, added an extra step where Norvergence, the vendor, would first put leases in *their* name, make no investment, and then quickly "assign" them to leasing companies, who would then send Norvergence monies that funds the leases for the first time. In between the time when a "Norvergence" lease was signed by the lessee until this lease was "assigned" to the leasing companies, no money changed hands. It was an administrative trick between two partners; Norvergence never had the actual risk of a lessor holding a lease with cash invested, and leasing companies, the other partner, gains advantage when assigned the lease as "holder in due course."

As "holders in due course," and with the appearance of a third party arrangement and assignee, leasing companies' investments in Norvergence were legally removed from any responsibility of the "original lessor" Norvergence.

Leasing companies have strategically positioned themselves to have legal authority to continue collecting the full lease amount from lessees, come "hell or high water," as this clause is called. Despite the close dealings from the beginning between Norvergence and leasing companies; any failure to disclose material facts to its lessees or any default on services by Norvergence, a start-up telecommunications company with no business or credit history, would not be leasing companies' problem or liability.

The contractual manipulation, where the leases are first in Norvergence's name (with Norvergence not having to put up cash to have leases in its name), magically laundered the "equipment leases" (a fiction that was really mostly services with little equipment ) into "net receivables." Leasing companies' conversion of equipment leases into net receivables on the books makes the original, and fraudulent, conflation of services and equipment evaporate, as if it never existed.

Leasing companies' investment into "Norvergence leases" created a Norvergence portfolio of their own invention. There was no investment in the leases by Norvergence. With \$200 and \$1550 equipment, Norvergence was able to finance its services in equipment leases ranging from \$10,000 to \$340,000.

Pieces of equipment worth \$200 and \$1550 were the only real basis for these leases that leasing companies were funding. Norvergence was receiving as much as \$200,000 + for each lease for a grand total of \$200 million + of these 11,000 lease transactions. Norvergence could get away

with this because leasing companies did not look between the lines? This does not jibe with the words in the CCL/ Norvergence partnership agreement.

Before the final paragraph, “If this proposal meets your approval...countersign,” a “General Information” section above cites (emphasis mine): CCL “shall not be required to enter into the proposed **vendor lease program partnership until the completion of all due diligence inquires**, receipt of approvals from all requisite parties, **the execution and receipt of all necessary documentation and the credit approval of Norvergence, Inc. by CCL.**”

Obviously, at least on paper, leasing companies believe, at minimum, in giving the appearance of having done due diligence regarding equipment. In CCL’s words this verification includes, as quoted earlier: “With respect to the equipment, each lease transaction will not become final until, among other things, assignee (leasing company), verifies the equipment specifications including, but not limited to: Model number, serial number, number of units, and installation costs; and approves the final equipment.”

Leasing companies chose to or neglected to do due diligence. They were program partners with Norvergence , upon information and belief, right from the beginning. I do not condone but I can understand many ways this could happen, both legally and illegally. What I can not understand is the denial by ELA that due diligence should have been done by your members who participated in the Norvergence scheme, including the valuation of the equipment.

#### Leasing Companies pursuit of legal action against Norvergence Lessees has resulted in Investigations into Insurance Fraud

Leasing companies that claim to not know or care about equipment values or if the leases bundled services and equipment, likely booked the Norvergence leases as “net receivables.” What is striking, however, is that despite this accounting position, when it comes to insurance, these same leasing companies no longer view these same leases as net receivables with unknown equipment values. Suddenly “equipment” has a value that they claim to know and they represent this value to insurance companies, naming themselves as the payees upon loss of the equipment.

Leasing companies dared to represent “equipment values” to insurers who believed they were insuring equipment, and they charged customers premiums, not based upon the actual replacement value, but based on the total amount leasing companies paid to Norvergence. In the case of Norvergence, this means in reality insuring services ranging from \$10,000-\$340,000 with equipment underlying the lease worth only \$200 or \$1550.

In my earlier report prepared for the ELA Conference, that Mr. Fleming prevented me from presenting, CIT has a particularly troubling inconsistency in the charging of premiums to lessees. Not only were customers cheated by paying hundreds of dollars in insurance for equipment only worth \$200 or \$1550, CIT claims in writing that the premiums paid by lessees is only a “reimbursement.” The rate provided by their insurers proved this to be untrue.

Moreover, CIT 's premiums, in a random sample of customers, indicate that the premiums were not based on their stated "insured amount." One would naturally predict that CIT's higher insured amounts would generate the highest premium charges. The almost total lack of correlation between insured amounts and premium charges, found in CIT's case, indicates to me two possibilities: one, they had some sort of valuation system for the equipment that departs from what they declare is the "insured value" and is not transparent, or they bought the policy from their insurance company and payed the simple rate. They then do some brand of their own risk-analysis, as if they were themselves an insurance company, and then charge lessees premiums according to this formula.

The answers to CIT's insurance mystery has not been forthcoming from them. How insurance is done by leasing companies-- the dangers of acting as an insurance company, and not making proper and honest disclosures to lessees-- should be placed, based upon the aforementioned CIT situation, as an important ELA emerging issue for its members.

### Conclusion

I have two suggestions:

#### *I. Acknowledge Wrong-Doing*

Defending unethical companies against the interests of other more ethical members is unfair to both members and the industry as a whole. It engenders public and governmental distrust of the industry itself and provokes investigations and consequential regulations. Failing to acknowledge the difference between the correct action of some members and incorrect action of others gives the appearance that ELA and members neither know nor care about the distinction between practice that is correct and incorrect.

The credibility of your organization and the entire leasing industry is at stake. ELA's support of negative behavior, along with the objective results of giant losses, as well as the public relations nightmare when leasing companies insist that small Mom and Pop businesses pay up to \$340,000 over five years for leased equipment worth only \$200-\$1550.

The longer leasing companies keep this attempt to collect on Norvergence leases in the courts, the more scrutiny will be launched from various government quarters. Leasing companies' insistence upon being paid by lessees continues to be the issue that keeps the Norvergence's case and the complicity of leasing companies in the eyes of the public, the regulators, and most recently, the criminal prosecutors. (The cliché "attempting to win the battle loses the war," come to mind). Case in point: CIT's US Attorney subpoenas in a Criminal Grand Jury investigation. The stakes have risen from a focus on Norvergence's fraud exclusively to recent scrutiny of leasing companies.

The issues for ELA briefs were in civil court; now the inquires have expanded into criminal court and focus on one leasing company member, CIT, upon information and belief, issues that surpass the purview of Norvergence. The Norvergence case brings questions that naturally lead to apply these questions to dealings throughout the entire equipment leasing industry.

Leasing companies bought equipment leases from a service provider that was, in fact, mostly service contracts. Leasing companies accepted and funded leases for equipment with invoices and spec sheets, technical descriptions they claim to have known nothing about. If leasing companies had checked the equipment values, such as the manufacturer's SRP, as is their usual practice, these Norvergence leases, and the great losses and victimization of 11,000 small businesses never would have happened.

Small businesses signed up for services that stopped and no longer exist. The Norvergence case, when judged within the context of the leasing companies' specific knowledge, industry experience and involvement with Norvergence, reeks of hubris when leasing companies try to equate small businesses with their own culpability. The leasing companies' perspective of being able to contractually receive, review and compare Norvergence equipment and hundreds of Norvergence leases with their invoices and spec sheets, in advance of any commitment, is a distinct advantage that individual lessees did not share. Leasing companies easily could have required Norvergence to provide outside appraiser reports on their two products before any deal to commit millions of dollars was finalized.

Could anything other than "willful blindness" allow such lack of internal controls that let purchases of equipment leases "slip by" the same day that invoices for the same equipment, *with identical names and spec sheets*, were booked into leasing company records, as ranging from 10X to 100X ( \$10,000 to \$200,000)—a difference of tens of thousands of dollars? And for equipment leasing companies then to turn around and book these same blatant inconsistencies again, this time for acquiring insurance and naming themselves as payees? Is this the behavior, on the part of a limited number of its members, that ELA backs and is willing to stake its reputation on?

## II. *Encourage Lessees Role in ELA Membership*

Listening to objective voices un-invested in mutual reassurance would reveal information that ELA would not normally hear from your leasing company, investor and vendor membership. Lessees, functioning like miners' canaries, would warn you in advance of problems and dangers. This would enable a proactive response rather than a reactive one provoked by negative issues in the press or in court records. ELA would also have the high ground of being way out front of issues and able to hear all sides in order to make a proper evaluation.

Lessee information and data has been critical in my research. One specific example I briefly discussed with with Mr. Fleming at the registration table:

### Important Information from Norvergence Lessees about State Property Tax Refunds Due to Lessees from Leasing Companies

The personal property tax issue is one problem and fall-out from the Norvergence debacle that your membership would benefit from by becoming informed.

States like Virginia and Texas used the Leasing companies' inflated and false equipment valuations received from the Leasing companies to collect personal property tax. When made aware by lessees of the bloated valuation, counties will refund taxes to the leasing companies who paid out the tax on behalf of lessees.

Since Leasing Companies' internal bookkeeping systems are set up to *collect these property taxes and not to refund them*, lessees have been cheated, inadvertently or on purpose. When Counties refund taxes to lessees, Leasing Companies so far have not refunded these monies as Counties have instructed them to do.

It's obviously illegal to hold refunds of taxes improperly collected in order to cover other indebtedness. Mention of this negligence in refunding tax monies and improper collection sounds bad, and looks worse when documents back up the lessee's claim in black and white. Documents prove that Counties have refunded taxes and directed the Leasing Companies to pay the lessee, and all the Leasing Companies did, so far, is cash the check.

One lessee informed me about this property tax refund problem.

In 2003, I reimbursed DeLage Landen for more than \$500 to cover my property taxes based on its \$13,706 value. The tax rate is 4.57%. The \$13,760 was depreciated by 20% and I was forced to pay the tax (plus additional costs) on 4.57% of \$10,965 or \$501. Additional charges brought the amount up to \$576.

In September of 2004 I complained to the my County's taxing authorities that the equipment valuation was much too high and that the equipment was falsely described as being capable of providing telecommunications services. The County agreed my Matrix Soho was nothing but a computer router and changed the depreciation schedule on my equipment. This resulted in a reduced depreciated value (at 50%) and my tax was re-computed to be \$188 less. The County sent a refund to De Lage Landen for that amount (which was never returned to me) and reduced the tax for 2004 in a similar matter.

Three specific ideas for implementing a greater role of lessee voices in the ELA are:

1) ***“Lessee Hot Line” placed on the ELA website***

Where ELA can log and track lessee complaints and collect data. ELA would then begin monitoring and responding to emergent problems. As in the case of the Norvergence State Property Tax situation, ELA would thus provide a great service to members by alerting them to watch out for requests to refund tax monies, which is not

reflected in their normal bookkeeping. ELA's warning, based upon a valid and verifiable lessee complaint, protects itself and its member if, for example, a member does not comply. ELA can show that it took a proper public stance.

2) ***Openly include Lessees and Outside Academics in Conferences and Allow their Presentation of Findings Despite Individual Member Fears or Anger***

Mr. Fleming promised that he would review my report in our discussion at the registration table. (Please see link for final version

[http://www.asrlab.org/temp/ELA\\_Report.pdf](http://www.asrlab.org/temp/ELA_Report.pdf) ).

Outside research findings would communicate ELA promotes transparency and will give a voice to all parties involved in leasing, including lessees and outside academics studying leasing.

3) ***Fund Research Done by Outside Academics and Lessees***

In addition to funding research by leasing insiders, whose livelihoods depend upon Leasing Industry dollars-- and are therefore predisposed to censor themselves so as not to offend--also fund the research of people like lessees and outside academics, who have nothing to lose when speaking out and no conflict of interest.

Leasing is an industry where accountants in the big four accounting firms, prominent leasing attorneys, or other leasing experts, have at one time represented all the Leasing Companies, are forever constrained in any critical commentary or analysis due to a permanent conflict of interest.

ELA members fight in court to ensure what appears to be, in the court of public opinion if not (yet) proven in civil court, unjust payment; this only serves to keep this dark chapter in equipment leasing a viable target for passions and the ongoing, serious pursuit of corporate crime. As Nero was told: "Rome is burning." Each step ELA takes will be watched by the public, the government and the courts and will affect the multi-billion dollar Equipment Leasing empire in a trend either towards its collapse or its glory.