Leaseurope

KPMG

European Leasing

A joint Leaseurope and KPMG publication

Acknowledgements

Leaseurope would like to thank all the people who made this publication possible:

Its members for contributing their figures and in particular those associations who contributed an overview of developments in their markets.

Jacqueline Mills, Leaseurope's Senior Adviser, for initiating, coordinating and bringing to a successful end the project on the Leaseurope side.

The KPMG experts for their invaluable insight into local leasing legislation and especially Wolfgang Griesbach, Chair of the KPMG International Asset Finance Taxation Network for coordinating the project on the KPMG side.

Carolina Villamizar for designing a professional, elegant and user-friendly publication.

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Introduction

Welcome to this joint Leaseurope and KPMG publication, a review of the leasing markets as well as the legal, accounting and taxation aspects of the leasing business in 25 different European countries.

What with the strong demand for a comprehensive, easy-to-use reference tool on leasing in Europe, it was a natural step for Leaseurope, the trade association representing the European leasing and automotive rental industry and KPMG, with their highly respected and knowledgeable international network of experts on leasing taxation, to come together to produce a synopsis covering leasing market data at the same time as regulatory aspects of leasing throughout Europe.

The way the publication works is simple. Each national leasing market chapter contains two sections, the first of which is an introduction, provided by Leaseurope, reviewing the size and growth of the market, along with details on the types of assets on lease in the country and other lease contract characteristics. As far as possible, this information is presented in such a way so as to render it comparable from country to country and is based on data collected from Leaseurope's member associations within the context of the federation's 2006 Annual Statistical Enquiry and 2007 Biannual Statistical Enquiry (which reflect the situation of Leaseurope's member associations at 31/12/2006 and 30/6/2007 respectively). These enquiries contain the most recent and extensive information available for the European leasing market at time of publication.

The second part of each country chapter contains a description of the regulatory, fiscal and accounting background of the local leasing market. This information has been provided by members of the KPMG international asset finance taxation network who have leveraged their knowledge of national leasing legislations, direct and indirect taxation regimes as well as local accounting standards to provide a full overview of the regulatory environment in which the local leasing industry evolves. The information provided by KPMG reflects local situations as at end July 2007, unless stated otherwise within a country chapter.

Furthermore, in order to provide a general overview of the European leasing market, overall European leasing statistics are presented at the beginning of the publication, in the same format as the individual country chapters. The preliminary European chapter also contains a glossary of the terms used in the various market descriptions. This is followed by an outline of the international accounting standard for leasing, IAS17, the application of which has been mandatory on a consolidated basis for all listed companies in the EU since the beginning of January 2005.

We hope that you will find this compilation on European leasing interesting and useful. More information on European leasing and the activities of Leaseurope can be found at www.leaseurope.org. KPMG contact details are located within each country chapter.

01
European Leasing Market

European
Leasing Market

Federation Profile*

Leaseurope

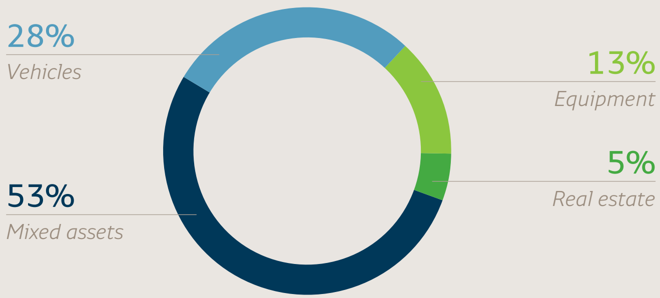
The Voice of Leasing and Automotive Rental in Europe

www.leaseurope.org

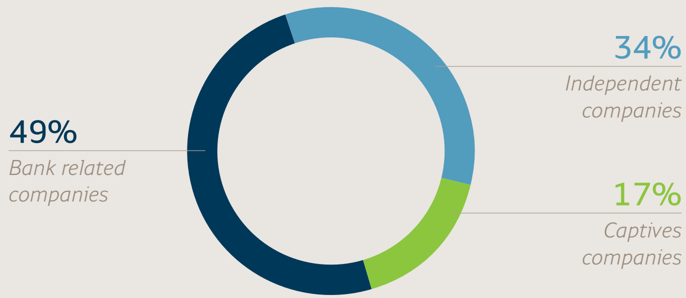
** Unless otherwise stated, the figures shown in this chapter are based on the results of Leaseurope's 2006 Annual Enquiry. 35 member associations active in the leasing (including the long term automotive rental industry) took part in this survey. A list of these members is provided below.*

- Total number of member associations *(end 2007)*: 48
- Total number of individual leasing companies in Europe reported in the 2006 Leaseurope Annual Enquiry: 1 650
- Leaseurope represents on average 92 % of the European leasing industry in terms of new leasing volumes
- Profile of European leasing firms:

Percentage of European leasing companies leasing the following



Percentage of European leasing companies according to shareholder type



European Leasing Market[1]

2006

New leasing volumes
€ 297 510 Mil

Outstandings
€ 630 701 Mil

Total growth[2]

2005 / 2006
+ 6,90 %

Penetration rate[3]

New leasing volumes
19,02 %

Equipment [Including Automotive] Leasing

Total new equipment [including automotive] leasing business

2006
€ 250 595 Mil

Growth

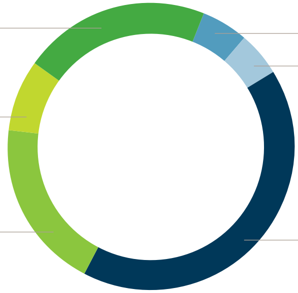
2005 / 2006
+ 7,20 %

1. The following figures are those of the 35 leasing and long term automotive rental members that took part in Leaseurope's 2006 Annual Enquiry.
2. Calculated based on a constant sample of members reporting in both the 2005 and 2006 Annual Enquiries.
3. The contribution made by leasing to the European economy can be expressed as a penetration rate. This is calculated by taking new leasing business as a proportion of all investment in all countries for which data is available. Investment figures are Gross Fixed Capital Formation minus investment in dwellings taken from Eurostat. If real estate leasing is excluded from the calculation, the penetration measure reaches 28.4% for equipment including automotive assets.

Equipment [including automotive] leasing
continued →

Share of new volumes in 2006

By asset type



19%
Road transport vehicles

21%
Machinery & industrial equipment

8%
Computers & business machines

5%
Other

5%
Ships, aircrafts, railway, rolling stock

41%
Motorcars

	> Growth
€ 101 682 Mil	+ 2,73%
€ 11 382 Mil	-
€ 15 595 Mil	+ 8,78%
€ 47 829 Mil	+ 17,54%
€ 20 760 Mil	+ 3,23%
€ 52 897 Mil	+ 16,25%

By contract term

9%
Up to and including 2 years

73%
2-5 years

12%
5-10 years

5%
Longer than 10 years

By client type

3%
Agriculture, forestry & fishing

29%
Manufactoring, industry & construction

44%
Services

4%
Public sector

16%
Consumers

5%
Other

Real Estate Leasing

Total new real estate leasing business

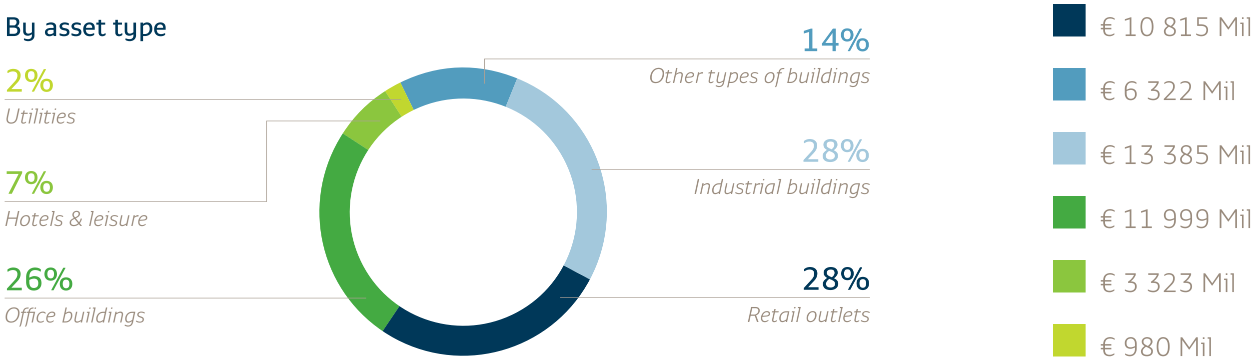
2006
€ 46 824 Mil

Growth

2005 / 2006
+ 5,60 %

Share of new volumes in 2006

By asset type



By contract term

European Leasing

The simple term "lease" covers a myriad of different contact types throughout Europe, the common feature of which is that the finance provider, or lessor, retains the ownership of the leased asset throughout the life of the contract. With a multitude of definitions existing in local GAAP and fiscal legislations, the only common definition of a lease that can be given is that provided by IAS17, the international accounting standard for leases, where a lease is defined as *an agreement whereby the lessor conveys to the lessee, in return for a payment or series of payments, the right to use an asset for an agreed period of time*.

In Europe, Leasing is used to finance a vast range of assets, including cars, trucks, yellow goods, industrial machinery and equipment, IT and other office equipment, software, planes, trains, ships and real estate to name a few.

The benefits of using lease finance include the possibility to finance 100% of the purchase price of an asset without having to offer any additional guarantees or being able to use equipment or other assets without having to worry about considerations linked to being an owner such as the disposal of the asset when it is no longer used. A lease can also be accompanied by an array of services, including insurance and maintenance of the asset. Depending on local fiscal treatment, leasing can also be beneficial from a tax point of view. In certain cases, particularly for smaller companies with high growth potential but little history, leasing may be the only source of funds available to help them finance their development. Generally speaking, lessors can provide finance in circumstances when traditional bank loans would not be granted as lessors have greater security due to the ownership of the asset.

In Europe, the use of leasing is becoming increasingly popular as illustrated by the level of average leasing penetration (which measures the share of European investment financed by leasing) which grew from 11.9% in 2000 to 19% in 2006[1]. Equipment lease finance in particular is an important source of funding, with leasing financing on average around 28% of equipment investment in Europe during 2006[2].

1. Leasing penetration is calculated as new leasing volumes provided by Leaseurope members in the 2006 Leaseurope Annual Statistical Enquiry divided by gross fixed capital formation less investment in private dwellings taken from Eurostat.
2. Calculated as new equipment leasing volumes divided by gross fixed capital investment in all asset types excluding real property from Eurostat.

Glossary

New business/new volumes

New business is total lease production for the year excluding VAT and finance charges.

Outstandings

Initial value of assets minus depreciation to date or, if unavailable, amount of capital still due on contacts.

Asset categories

Machinery and industrial equipment
Includes all types of machinery/equipment be they for commercial, industrial or agricultural use. Harvesters, tractors and earth movers, as well as other “wheeled” assets that are not registered (i.e. do not have a licence plate) are included under this section and not under “Road Transport Vehicles”.

Computers and business machines
Includes all IT equipment and other business machines such as photocopiers, etc.

Road transport vehicles
Includes all registered commercial vehicles, regardless of their weight. This section therefore includes both light commercial vehicles (typically vans) as well as other, heavier commercial vehicles (e.g. trucks, trailers, busses).

Motorcars
Includes new and used cars, be they for private or business use. Motor cycles as well as caravans are included here too.

Leasing companies according to shareholder structure

In the profile of leasing firms active on a market, a bank-related leasing company either has a banking licence in its own right or is part of a banking group. A captive company is a leasing company related to a manufacturer.

Notes

Figures shown in this publication relate to leasing in its widest sense, including products know locally as hire purchase, finance leases and operating leases. Long term rental is considered as leasing (and will often qualify as operating leasing). It should be noted that there is no international or European definition of leasing, apart from that given in IAS17, the international accounting standard for leases. Local definitions of leasing products may vary according to the local legal, taxation or accounting framework as shown in this publication.

Please note that where percentage figures are used in new volume breakdowns, totals may not add up to 100% due to rounding.

Figures are provided by member associations in local currency and converted into euros using the yearly average exchange rate taken from Eurostat.

Growth rates are calculated based on the new leasing volume figures provided by associations in Leaseurope's 2005 and 2006 Annual Statistical Enquiries.

It should be noted that real estate leasing growth rates tend to be more volatile than those for equipment leasing. This is due to the fact that the market for real estate leasing may be heavily influenced by low volume, high value transactions.

Discrepancies between Leaseurope's figures and those used by KPMG in their introductory paragraphs may relate to a different scope of the leasing product or currency issues.

Leaseurope members taking part in the 2006 Annual Statistical Enquiry*

Austria: Verband Österreichischer Leasing-Gesellschaften
Bosnia & Herzegovina: Association of Leasing Companies in Bosnia and Herzegovina
Belgium: Association Belge des Entreprises de Leasing and RENTA
Bulgaria: Bulgarian Leasing Association
Switzerland: Schweizerischer Leasingverband
Serbia & Montenegro: Association of Leasing Companies in Serbia-Montenegro
Czech Republic: Czech Leasing and Finance Association
Germany: Bundesverband Deutscher Leasing-Unternehmen
Denmark: Finans og Leasing
Estonia: Estonian Leasing Association
Spain: Asociacion Española de Leasing and Association Espanola de Renting
Finland: Federation of Finnish Financial Services
France: Association française des Sociétés Financières and Fédération Nationale des Loueurs de Véhicules
Greece: Greek Car Rental Companies Association
Hungary: Hungarian Leasing Association
Italy: Associazione Italiana Leasing - ASSILEA
Latvia: Leasing and Factoring Committee of the Latvian Association of Commerical Banks
Lithuania: Lithuanian Leasing Association
Luxemburg: Fédération Luxembourgoise des Loueurs de Véhicules
Netherlands: Nederlandse Vereniging van Leasemaatschappijen and Verenigine van Nederlandse Autoleasemaatschappijen
Norway: Finansieringsselskapenes Forening
Poland: Association of Leasing Companies in Poland
Portugal: Associacao Portuguesa de Leasing e Factoring
Romania: Romanian Leasing Association and Romanian Leasing and Non Banking Financial Services Association
Russian: Russian Association of Leasing Companies - Rosleasing
Sweden: Associations of Finance companies - AFINA regrouping the Finansbolagens Förening and the Svenska Bankföreningen
Slovenia: Slovenian Leasing Association
Slovakia: Association of Leasing Companies of the Slovak Republic
Ukraine: Ukrainian Association of Lessors
United Kingdom: Finance and Leasing Association

* For the purpose of this publication, short term automotive rental associations and their figures have not been shown. A full list of Leaseurope members can be found on the federation's website at www.leaseurope.org.

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02
IAS 17

IAS 17

Legal, Accounting and Taxation Treatment of Leasing

The relevant International Financial Reporting Standard (IFRS) for leasing is International Accounting Standard number 17 (IAS 17) – Leases. This chapter summarizes the accounting requirements for leases under IAS 17 and other relevant standards.

Types of Transactions covered by IAS 17

Under IAS 17, a lease is defined as an agreement whereby the lessor conveys to the lessee in return for a payment or series of payments the right to use an asset for an agreed period of time. Title to the asset may or may not transfer to the lessee at the end of the lease.

There is no distinction between hire and operating leases; any transaction which involves the hire of a specific asset falls within the definition of a lease. It therefore includes the short-term charter hire of assets such as ships and aircraft. Leases of land and buildings are also included.

IFRS contains two other pieces of guidance - issued by the International Financial Reporting Interpretations Committee (IFRIC) and its predecessor, the Standing Interpretations Committee (SIC), on what types of transactions fall within IAS 17:

- IFRIC Interpretation 4 - Determining whether an Arrangement contains a Lease. This gives guidance as to when a transaction, that is not legally a lease, contains elements that meet the definition of a lease and so should be accounted for under IAS 17. An example of such a transaction is a service contract that also conveys the right to use an asset to the purchaser of those services. Determining whether an arrangement is, or contains, a lease is based on an assessment as to whether:

  1. Fulfillment of the arrangement is dependent on the use of a specific asset (or assets).
  2. The arrangement conveys a right to use the asset. This depends on whether the purchaser of the services has the right to control the use of the underlying asset.

- SIC-27 - Evaluating the Substance of Transactions Involving the Legal Form of a Lease. This gives guidance as to when a transaction, that is legally a lease, does not in substance involve a lease and so falls outside IAS 17. Examples include certain lease in lease out structures and certain sale and finance leaseback transactions. Accounting entries for such a lease outside IAS 17 are determined by IAS 39, rather than IAS 17, and are outside the scope of this chapter.

Lease classification

Under IAS 17, leases are classified as either finance leases or operating leases. The classification affects how lessors disclose the leases in their balance sheets and how they recognize income.

For lessees, the classification affects whether or not the lease is even included in the balance sheet as well as how the lease expenses are recognized.

Under IAS 17, a finance lease is a lease that transfers substantially all the risks and rewards incidental to ownership of an asset. Title may or may not eventually be transferred. In other words, the key risks being assumed by the lessor are financing risks rather than risks associated with the asset being financed. All other leases are operating leases.

IAS 17 states that the lease classification depends on the substance of the transaction rather than the form of the contract and on an assessment as to the extent to which risks and rewards incidental to ownership of a leased asset lie with the lessor or the lessee. The classification is therefore judgmental rather than based on detailed rules.

IAS 17 does, however, give various examples and indicators to assist with this classification. It gives the following examples of situations which would normally lead to a lease being classified as a finance lease:

1. The lease transfers ownership of the asset to the lessee by the end of the lease term.

2. The lessee has the option to purchase the asset at a price which is expected to be sufficiently lower than the fair value at the date the option becomes exercisable such that, at the inception of the lease, it is reasonably certain that the option will be exercised.

3. The lease term is for the major part of the economic life of the asset even if title is not transferred.

4. At the inception of the lease the present value of the minimum lease payments amounts to at least substantially all of the fair value of the leased asset.

5. The leased assets are of a specialized nature such that only the lessee can use them without major modifications being made.

The following points should be noted which reinforce the judgmental nature of lease classification under IAS 17:

- The above are described as examples rather than being a definitive list of all situations that should be considered; there may be other situations that give rise to a lease being classified as a finance lease that are not listed.
- The wording uses the word 'normally' and this implies that there could be exceptions.

IAS 17 also gives the following indicators of situations, which individually or in combination could lead to a lease being classified as a finance lease:

1. If the lessee can cancel the lease, but the lessor's losses associated with the cancellation are born by the lessee.

2. Gains or losses from the fluctuation in the fair value of the residual fall to the lessee (for example in the form of a rent rebate equaling most of the sales proceeds at the end of the lease).

3. The lessee has the ability to continue the lease for a secondary period at a rent that is substantially lower than market rent.

Under IAS 17, where a lease contains both land and buildings, the land element and the building element should be classified separately. This is likely to lead to most leases of land being classified as operating leases and more buildings being classified as finance leases than would be the case if the lease was classified as a whole.

The lease classification should be carried out at the inception date of the lease. This is the earlier of the date of the lease agreement and the date of commitment by the parties to the principal provisions of the lease. The classification is not subsequently changed if there are subsequent changes in estimates (for example, changes in the residual value estimate) or changes in circumstances (for example, default by the lessee). However, if at any time the lessee and the lessor agree to change the provisions of the lease, other than by renewing the lease, the revised agreement is regarded as a new agreement and the classification needs to be reconsidered.

Key terms used by IAS 17

Minimum lease payments are the payments over the lease term that the lessee is or can be required to make, excluding contingent rent, costs for services and taxes to be paid by and reimbursed to the lessor, together with: (a) for a lessee, any amounts guaranteed by the lessee or by a party related to the lessee; or (b) for a lessor, any residual value guaranteed to the lessor by: (i) the lessee; (ii) a party related to the lessee; or (iii) a third party unrelated to the lessor that is financially capable of discharging the obligations under the guarantee.

If the lessee has an option to purchase the asset at a price that is expected to be sufficiently lower than fair value at the date the option becomes exercisable such that it to be reasonably certain, at the inception of the lease, that the option will be exercised, the option price should be included in the minimum lease payments.

As noted above, minimum lease payments exclude the following:

- Contingent rent – This is defined as that portion of the lease payments that is not fixed in amount but is based on the future amount of a factor that changes other than with the passage of time (e.g. percentage of future sales, amount of future use, future price indices, future market rates of interest).
- Costs for services – For example maintenance costs and expenses borne by the lessor such as road fund tax for a leased vehicle.
- Taxes to be paid by and reimbursed to the lessor – For example VAT.

The discount rate to use in present valuing the minimum lease payments would generally be the interest rate implicit in the lease. This is defined as the discount rate that, at the inception of the lease, causes the aggregate present value of (a) the minimum lease payments and (b) the unguaranteed residual value to be equal to the sum of (i) the fair value of the leased asset and (ii) any initial direct costs of the lessor.

Initial direct costs are directly attributable incremental costs incurred in negotiating and arranging the lease.

Lessor accounting

Having decided upon a lease's classification, it is next necessary to consider the accounting treatment required for that lease. The following sets out the accounting by lessors under IAS 17.

Finance leases

Lessors should recognize assets held under a finance lease in their balance sheets as receivables at an amount equal to the net investment in the lease. Income is recognized so as to give a constant periodic rate of return on the lessor's net investment in the lease.

The net investment in the lease is the gross investment in the lease discounted at the interest rate implicit in the lease.

The gross investment in the lease is the aggregate of: (a) the minimum lease payments receivable by the lessor under a finance lease, and (b) any unguaranteed residual value accruing to the lessor.

Given the definition of interest rate implicit in the lease, the result is that the amount initially recognized equals the fair value of the asset plus any initial direct costs. The income is allocated in proportion to the average net investment in the lease.

Operating leases

In the case of a finance lease, the transaction is in substance the provision of finance and income is recognized in a similar manner to interest.

In the case of an operating lease, the lessor is essentially taking asset risk and so this is reflected in the accounting by treating the leased asset as a fixed asset. The accounting for that asset is the same as for any other fixed asset – generally this would mean depreciating the asset on a straight-line basis. The earnings from that asset (i.e. rentals) are generally recognized on a straight-line basis, unless another systematic basis is more representative of the time pattern in which use benefit derived from the leased asset is diminished.

Lessee accounting

Finance leases

Where an asset's use has been obtained under a finance lease, it should be capitalized, i.e. the lease should be recorded in the balance sheet as a fixed asset and as an obligation to pay future rentals. It should be capitalized at the lease commencement – i.e. the date from which the lessee is entitled to exercise its right to use the leased asset. Note that this is when the lessee is entitled to use the asset which may be earlier than when the asset actually comes into use.

Initially the value of this asset and liability should be the fair value of the asset or, if lower, the present value of the minimum lease payments. This present value should be calculated using the interest rate implicit in the lease.

The asset is then depreciated in the same way as for any other fixed asset over the shorter of the term of the lease and the asset's useful life. One should depreciate down to the residual value at the end of the depreciation period (if the lessee receives this benefit). The lease term, for this purpose, includes any secondary periods if exercise of those secondary periods is reasonably certain.

The finance charges on the liability should be allocated to accounting periods so as to give a constant periodic rate of charge on the remaining liability.

Operating leases

Operating leases are not capitalized by lessees, i.e. they are 'off-balance sheet'. The rentals should generally be charged on a straight-line basis over the lease term unless another systematic basis is more representative of the time pattern of the user's benefit, even if the payments are not made on such a basis. The only amounts on the lessee's balance sheet will simply be any rentals accrued or prepaid at the balance sheet date.

Examples of where one would recognize rentals as they arise rather than on a straight line basis would be where:

- The rentals vary with usage.
- The rentals vary in line with an inflation index or market rates.

The majority of property leases are likely to be operating leases. Sometimes in order to sell the deal to the lessee, a rental holiday, reverse premium or other incentive is offered. Under an interpretation - SIC-15 Operating Leases - Incentives, the benefit should be recognized over the lease term.

A payment may be made on entering into or acquiring a leasehold that is accounted for as an operating lease. This payment should be treated as prepaid lease payments and be amortized over the lease term in accordance with the pattern of benefits provided (normally straight line).

Future changes

The International Accounting Standards Board (IASB) and the US equivalent – the Financial Accounting Standards Board (FASB) - are currently carrying out a joint project to develop a new lease accounting standard. This project will take several years but the likely outcome is that, instead of the current distinction between a finance lease and an operating lease, all leases will be capitalized by lessees at amounts reflecting the fair value of the lease commitments.

International financial reporting standards contact

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The following pages are an extract of the publication entitled European Leasing. Individual country chapters detailed in the full publication have not been shown here. For further information, please contact: **Jacqueline Mills** j.mills@leaseurope.org

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