

**Dipl. Kaufmann Klaus Feinen**

**Sprecher der Geschäftsführung**

**Deutsche Immobilien Leasing GmbH**

## **ERES annual meeting**

**Alicante, Spain**

### **abstract**

- ☞ Service and taxation - The drivers of real estate leasing in Germany
  - ☞ An alternative financing model
  - ☞ Services define the industry
  - ☞ Services through structuring
  - ☞ Globalisation and tax motivated structures
- ☞ European perspective: Impact of the Euro
- ☞ Different legal frameworks and tax harmonisation in the Monetary Union

**SERVICE AND TAXATION –THE DRIVERS OF REAL ESTATE LEASING IN GERMANY**

According to statistics from Leaseurope, the joint body of the leading European leasing associations, Germany has been leading the field of real estate leasing for many years, with total real estate valued at 35.5 billion €. Looking at new business, however, Italy was able to enter into contracts valued at 5.57 billion € in 1999, after an impressive increase of 90% compared with the previous year, leaving Germany slightly behind for that year with 5.43 billion €.

Changes in some programs designed to encourage investment in the new (Eastern) federal states, relative weakness in the building sector in the old (Western) federal states and significant tax changes introduced in the Tax Reform Act of 1999 have most recently led to some commentators voicing a rather cautious opinion of the future of the real estate leasing industry. However, those involved in the market have good reason for optimism when looking at both its historical development and strengths.

By way of contrast, the German success story is significantly more complex and wide-ranging. That story has been shaped by a mixture of many qualitative and quantitative advantages. The continuing adaptation to the individual needs of customers and to changes in the market have shown themselves to be major strengths for the successful development of the industry. Creativity and flexibility are not merely words. Instead, they are a hallmark of real estate leasing in Germany. In over 30 years, a highly specialised sector of the economy has developed in Germany, offering leasing models not only suitable for classical real estate types including office, retail, industrial buildings (warehouses, plants), but also for “facilities”, such as power plants, water and sewage treatment facilities and wind power stations etc.

For the purpose of clarification, one thing should be made clear: “Immobilienleasing” - the German word for real estate leasing derived from English - is in Germany always regarded as equivalent to financing. Real estate leasing has an off-balance sheet character despite the fixed purchase option. This balance sheet neutrality forms the basis of its identity, in Germany and certainly also in other countries.

What is behind this financing product and the impressive figures? What can foreign companies operating at an international level expect from German real estate leasing companies? These questions and the drivers behind the real estate leasing market are addressed below in more detail.

### **An alternative financing model**

When the idea of leasing came to Europe from the USA in the 1960s, some of the industry pioneers recognised quickly that real estate being used for commercial purposes is in some cases something inherently suitable for leasing. It was the recognition that, given the right location and usefulness to

third parties, the real estate had a different lending value from that reflected through lending against mortgage, resulting in a 60 % loan-to-value ratio. The value of the equity in the company as a “scarce commodity” had already been recognised at that time and, encouraged by a favourable tax environment, that was the birth of a financing instrument which today is widespread in all sectors of the economy as well as in the public sector.

### **100 % Financing**

Beside the objective of providing 100% financing for a specific property, the first contractual forms in Germany concentrated on the amortisation of the acquisition and construction costs in a relatively short lease term, ie the creation of tax deferral effects. Lease payments include high amortisation instalments and can therefore lead to accelerated write-off effects, as are still seen today in France and Italy.

As a prerequisite for achieving these effects, the attribution of the economic ownership to the lessor soon came into the spotlight of the courts. After a decision of the German Supreme Fiscal Court and the reaction of the tax authorities to this decision, tax-oriented structures quickly began to lose their importance at the beginning of the 1970s. The tax authorities provided in several decrees, the so-called “Leasingerlasse” that an amortisation of the asset by means of the lease payments cannot be faster than in the case of conventional credit financing.

The Decrees on Real Estate Leasing stipulate that the purchase option price at the end of the lease term must be at least equal to the net book value, calculated according to straight-line depreciation. The industry developed non-full payout contracts as a reaction to this, which to this day continue to determine the market.

### **Trade tax advantage**

But, real estate leasing in Germany continues to enjoy the advantage in the treatment of lease payments for trade tax (Gewerbesteuer) purposes. In the case of conventional credit financing, 50% of the interest expenses have normally to be added to the tax base upon which the trade tax is calculated. As a result 50% of the interest expense cannot be deducted. In the case of exclusive management of own properties, it is possible to apply for a so-called “extended trade tax deduction” under § 9 (1) 2 of the Trade Tax Act allowing a complete deduction of the interest expense. This provision has been used by the leasing industry for the greater part of its transactions. The resulting concrete advantage for specific investment projects depends on the local levy rates for trade tax applicable, but normally means that lease financing is not more expensive than comparable conventional financing. However, real estate leasing offers much more!

## **Services define the industry**

Real estate leasing in Germany is a classical service industry, offering comprehensive technical and commercial services related to real estate.

An initial necessity has thereby been made into a virtue. A 100% financing includes, of course, a higher risk for the lender than a conventional financing, where the lender's collateral position is buttressed by an equity investment in the property. The risk of default on credit granted or a leasing transaction can be reduced by assessing the credit rating of the lender / lessee, but never be influenced in a lasting manner. That is different where a leased asset is concerned. Starting with the recognition that at the point of construction or purchase of the real estate, a decisive reduction in the risk profile of the investment can be achieved, leasing companies have built up their own appraisal departments as well as know-how for planning and carrying out real estate projects to the point at which they are ready for occupancy.

## **Valuation and construction management**

The lessee has to secure that the lessor has an all-encompassing knowledge of and experience in the building sector. While many larger companies have their own departments for planning and building the necessary company facilities at a low price, most small companies often only need to expand once in a longer period of time. In this process they are depending on foreign consultants. One major disadvantage results from the facts that they are only doing business with the building companies once. By choosing the leasing alternative this handicap can be avoided.. Well-established lessors use subsidiaries qualified as building managers, to conduct the building process.

Frequently doing business with the building industry lessors are able to detect and eliminate risks and chance occurrences. They are able to conduct the building programs, secure deadlines, reduce costs, optimise procedures and make sure the leased asset can be sold at the end. Their deep insight in the market gives a highly qualified staff the knowledge not only of prices and conditions but also of new technologies, materials and procedures to reduce the costs for energy. The lessee profits by these cost reductions the lessors achieves with lower leasing rents. Needless to say that the lessee is involved in all changes of plans and cost reducing measures. He is able to influence the building process at his delight at all times.

It is the aim of facility management to keep the leased asset functioning at all times according to changing municipal legal conditions. Facility management contains the technical, infrastructural and commercial aspect that a good lessor all can cover.

Technical facility management contains all measures that appear necessary to comply with the municipal provisions for the object. Especially for the municipalities this has proven to be quite a source for savings e.g. to reduce energy costs. Space management tries to increase the productivity of space. By doing a stock taking of available space it is possible to arrange the usage of space in a more effective way in order to save space. The commercial facility management contains the accountancy, cost management and contract management. In the field of municipal leasing this also contains the classical administration services such as the consulting of lessees.

### **Commercial services in the building process**

By the conclusion of the lease contract the lessee assigns the function of conducting the building process to the lessor. Besides the technical responsibilities the lessor takes over numerous commercial functions for the lessee e.g.:

- conclusion of real estate, purchase and building lease contracts as well as their implementation together with the
- conclusion of necessary insurances and applying for necessary authorizations
- examination of the property related taxes and charges,
- the annual supply of data for budget and accounting
- advice in selection and negotiation of the best refinancing package.

### **Refinancing**

Although all leasing companies are subsidiaries of one or more large banks, it is no secret that the majority of the refinancing is dealt with outside of their respective parent companies. A stable real estate market over many years in Germany and competition between commercial and mortgage banks have ensured that leasing companies have always been able to find interesting sources of refinancing.

In an increasingly liquid refinancing market, the leasing companies have been able to refinance the leasing arrangements almost entirely by bank loans on a non-recourse basis. The lender is secured by

an assignment of the lease payments, together with a land charge / mortgage in the real estate being financed.

### **Services through structuring**

The more the actual refinancing function has returned to the banks, the more the leasing companies have differentiated themselves from their competitors through forming accounting and tax-orientated structures.

### **National and international accounting**

As stated above, the off-balance sheet effect gave the leasing product its identity early on. It is seen in both in the accounting and tax treatment. In Germany, there is a close link between commercial and tax accounting. By virtue of the principle of authority (Maßgeblichkeitsprinzip) commercial accounts must be consistent with the tax accounts. The lack of explicit commercial law provisions led to an adoption of the tax rules into the German Commercial Code (Handelsgesetzbuch / HGB) and – as a result of this – to a reversal of the principle of authority.

Co-operation with international customers and the legally granted possibility for German companies to draw up consolidated financial statements according to international accounting principles which came into effect in 1998 have for some time led to lease contracts taking into account IAS and US GAAP standards as well as the national principles. As far as the central point of the attribution of the economic ownership is concerned, the leasing companies take advantage of their own resources in providing appraisals and, through their profound knowledge of the refinancing market, in the placement of residual risks.

In these times of shareholder value and in the competition for investors' capital, leasing models offer an interesting and - particularly for quoted companies - sought after addition to the financing spectrum. Real estate leasing has a positive impact on the key ratios as Return on Assets Employed, Return on Equity, etc. and ratings by credit rating agencies, which take into consideration that a lessee can unconditionally use the property on a longterm basis while longterm risks and chances of ownership can be optimized through end-of-lease-term options.

### **IAS and US-GAAP**

IAS and US-GAAP have a high density of formal criteria though US-GAAP is more complex than IAS. In contrast to the German commercial law IAS and US-GAAP comprise extensive and detailed regulations with respect to the accounting of leasing. According to this the economic ownership of the leased asset is the prerequisite for its capitalisation. The disclosure of the leased asset in the balance

sheet of the lessee has to be shown if all risks and rewards incident to ownership of an asset are transferred to the lessee. Title may or may not eventually be transferred. Leases which meet these requirements are classified as finance or capital lease - all other leases are classified as operating lease. In Germany most of the real estate leasing transactions are operating lease assuming a highly qualified consulting staff is involved. In this case the off-balance character of leasing is guaranteed. The differentiation between finance and operate lease is made from an economic viewpoint. The strict rule is "substance over form".

According to **IAS 17 revised** there are numerous criteria which characterize a finance lease:

- the lease transfers ownership of the asset to the lessee by the end of the lease term;
- 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;
- the lease term is for the major part of the economic life of the asset even if title is not transferred;
- 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 lease asset; and
- the leased assets are of a specialised nature such that only the lessee can use them without major modifications being made.

Indicators of situations which individually or in combination could also lead to a lease being classified as a finance lease are:

- if the lessee can cancel the lease, the lessor's losses associated with the cancellation are borne by the lessee;
- 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 equalling most of the sales proceeds at the end of the lease); and
- the lessee has the ability to continue the lease for a secondary period at a rent which is substantially lower than market rent.

These example and indicators classify a finance lease. The disclosure of the leased asset has to be shown in the balance sheet of the lessee. So, to keep the off-balance character of leasing these indicators have to be ruled out.

Additionally, there are certain disclosure requirements for finance leases, e.g.:

a reconciliation between the total gross investment in the lease at the balance sheet date, and the present value of minimum lease payments receivable at the balance sheet date. In addition, an enterprise should disclose the total gross investment in the lease and the present value of minimum lease payments receivable at the balance sheet date, for different periods.

These disclosure requirements are harmful for the off-balance character of leasing. So LEASEUROPE has stated some criteria it thinks are better suitable to ensure a fair treatment of leasing.

According to SFAS 13 the leased asset has to be disclosed in the balance of the lessee if the lease meets one or more of the following criteria:

- transfer of ownership test: the lease transfers ownership of the property to the lessee at the end of the lease term;
- bargain purchase option test: the lease contains a bargain purchase option for a price which is sufficiently lower than the expected fair value of the property at the date the option becomes exercisable that exercise of the option appears, at the inception of the lease, to be reasonably assured;
- economic life test: the lease term is equal to 75 percent or more of the estimated economic life of the lease property;
- recovery of investment test: the present value at the beginning of the lease term of the minimum lease payments equals or exceeds 90 percent of the excess of the fair value.

#### **G 4 + 1**

The ASB and G 4 + 1 believe that standard-setters should aim to replace the present distinction between finance leases and operationing leases with a single method of accounting that applies the same principles to all leases and is consistent with the concepts behind the development of modern accounting standards, e.g. a lessee should recognise an asset, which is the right to use the leased property for the lease term, and a liability, which is the obligation to pay for its use. The asset and liability should initially be recognised when the item that is the subject of the lease is delivered or otherwise made available to the lessee. At the beginning of the lease term, the asset and liability should be recorded at their fair value, which is generally measure as the present value of the payments the lease requires, and any other liabilities incurred.

These provisions do not take into consideration the international divergence in lease accounting rules. Rendering an account would be impeded. The disclosure of leasing contract can not be isolated. A joint european solution has to be found.

#### **Globalisation and tax motivated structures**



Leasing of moveable assets is looking increasingly towards cross-border structures from the point of view of tax arbitrage. However, these ideas do not appear to be directly transferable to the real estate leasing industry because of the lack of mobility of the underlying assets. This has, however, not stopped the industry from adopting cross-border leases into its product range.

From as early as the beginning of the 1990s, structures were developed in which the right of taxation of the ongoing rental income stayed with Germany, but capital gains were tax-free. This tax loophole, however, was closed in the Tax Avoidance Act (Steuermissbrauchs- und -bereinigungsgesetz) of 1994.

### **“White” income and “double dip”**

However the leasing industry reacted and used the idea of generating so-called “white” income from cross-border leases. From the point of view of one of the countries involved, the lease arrangement can qualify as a “lease”, the other country involved may see this as a “financing transaction”. This differing interpretation and the use of the appropriate double tax treaty result in achieving the objective of the lease arrangement not being taxed.

While there appears to be low inhibition level within the leasing industry as far as the use of conflicting classification is concerned, which leads to a “double dip”, the industry has been cautious in case of “white” income. This is not least a result of the recent developments in the field of German tax treaty.

In the past, the classical tax treaties were primarily to avoid international double taxation, but stopping a reduction in the tax paid has moved more and more into the spotlight. “Subject-to-tax clauses” which stipulate that treaty benefits are only available if the income has actually been taxed in the country of residence have had a large part to play in this. In addition to this, “Fall-back clauses” may be used with the effect that the right of taxation falls back to the country of residence if the country in which the income arose does not make use of its right of taxation.

### **Summary**

So, it can be seen that service and taxation are the drivers behind real estate leasing in Germany. The companies have recognised that in the end, given the changing legal and tax environment, it will be the services offered which will allow them to distinguish themselves from other financial products and which will define their strengths. The market leaders are recognised for their wide-ranging specialist knowledge and their success over many years in finding solutions for problems faced by top national and international companies

### **European Perspective: Impact of the Euro**

On January 1, 1999, European monetary union was launched by introducing the euro as the single currency in 11 of 15 member states of the European Union. This was the beginning of the third step of the European Monetary Union. The treaty establishing the European Community assigns the primary objective of maintaining price stability in euro land to the European System of Central Banks (ESCB). There is no longer an independent foreign exchange market on which the in euro quoted currencies can be dealt. There are only original euro notations compared to third currencies.

The euro is present on all major financial markets worldwide. Although not yet embodied in the physical form of new banknotes and coins, there is no doubt that the new currency is set to play an important role, both in the euro area and beyond. What does this mean for an European leasing-company? Is there a unified leasing-market or will a unified leasing-market arise in the near future?

Before discussing these questions, let me give you a brief overview of the leasing-business in different European states. The historical development shows the meaning of leasing as a well established investment measure. Apart from a weak economic development in 1992 the leasing business is characterized by continuous growth rates in equipment leasing as well as in real estate leasing. The survey includes the four leading European economies: Germany, France, the United Kingdom and Italy. These four are comparable, measured by gross national product and population. The survey also deals with the situation in Spain, Portugal, Ireland, the Netherlands, Belgium, Luxembourg, Greece, Sweden, Denmark und Austria. Furthermore, figures from East European countries are represented in the survey. These countries are Bulgaria, the Czech Republic, Hungary, Poland, Russia, Slovakia, Slovenia, Latvia, Estonia and Uzbekistan.

1999 was a positive year with a turnover of more than 136 billion euro. This is an increase of 19 per cent.

### **Different legal frameworks and tax harmonisation within the Monetary Union**

In the sixties the leasing idea was born in the United States of America. The idea was taken over by European banking institutions and major companies which completed their service business. The question if either the lessor or the lessee has to balance the leased asset was left to common legal principles.

trans-  
parency:  
*Historic  
trend*

In most European states, independent leasing regulations have been developed which in most cases result from a development of the legal systems through legislation and practice and only in a few nations through a government supervision concerning the leasing business. For this reason leasing business is often called a „national source for financial operations.“ The European harmonization progress has not been able to eliminate the national differences, so that a unified leasing market has not arised.

Please take a look at the transparency: You can see the new business volumes of four European states. Compared to last year the situation has not changed substantially with the exception of Italy. Only the Italian real estate leasing industry enjoyed an increase of more than 70% in 1999.

With respect to the Eastern European countries there is an increase in leasing agreements in the Czech Republic (+13%), Poland (+48%) and Slovenia (+15%). Altogether, in the Eastern European states, there is a decline in leasing activity of 5 %.

Several systems can be distinguished depending on the degree of regulation. A lessor who is active in an unregulated market needs neither a bank admission nor a leasing license. A leasing license is required in regulated markets. Strongly regulated markets even require an admission as credit institution, ie bank.

First of all, in countries with a strongly regulated leasing market the admission is required before starting the activities. The lessor as a credit institution is subject to the bank supervision. The bank admission is needed before starting the operations at first time, not however if a bank, which is established in the domestic market goes abroad. A European guideline passed in 1989 laid down that a lessor who is accepted in one EU-country does not need a second admission in any other country of the European Union.

The foreign activities of credit institutions are supervised by the bank of the lessor’s country of origin. An exception are the captives whose purpose is to promote the lessor’s sales. They are free of any duty to ask for a bank admission because they refinance themselves with the help of their parent companies.

Therefore, especially the captives are gaining by the opening of the European markets. Nevertheless, a tendency is observable to get the refinancing with the help of the capital markets. This is the reason why the captives are trying to get the admission to do banking.

trans-  
parency:  
the east  
country:  
situation

---

parency  
*degree*  
*of re-*  
*gulation*

France represents an example for regulated market. For the foundation of a leasing company within France, a bank admission is needed. If a German leasing company plans to enter the French market, for example, the obligation to apply for a bank admission lapses if the company is organized as credit institution in Germany. Due to the fact that this is not the case in Germany - leasing companies are free as other service business companies - it is necessary to establish a specific credit institute compared with the one in France. This is in particular the case if a credit-bail deal, which is legally regulated, is strived for.

In countries with less regulated leasing markets a leasing license is sufficient. There is, for example in Belgium and Italy a special regulation concerning the taking up of the lessor's business operations. In Belgium, to get the leasing license, the lessor has to fulfil some particular special regulations. However, a bank admission before starting operations is not necessary.

In countries with totally unregulated leasing markets neither a bank admission nor a leasing license is needed. This is the case in Germany as well as in the United Kingdom. Leasing companies of these countries which are not in possession of a bank admission, have to apply for such an admission if they want to become active in those countries where an admission is necessary. In the following, some of these frameworks in leasing activities will be shown through some chosen European-Union-members.

## **Germany**

Germany is one of the countries with an unregulated leasing market. There are no special tax statutes applicable to leasing. Neither a bank admission nor a leasing license is necessary. The main issue of the tax related considerations is the question, who has to balance the leasing object in its balance sheet. If the lessor is the economic owner, it has to balance and depreciate the asset. The economic ownership is directed according to the leasing directives. The leasing directives are some special German guidelines, enacted by the government to state more precisely the term of „economic ownership.“ These regulations were established in 1970, 1971, 1975 and 1991.

trans-  
parency:  
Germany

The provisions of commercial law concerning the question of how to balance the leased asset are following tax related rules. So, the commercial law is focused on the economic ownership, as well.

Provided that leasing contracts are conforming tax related leasing directives, the activation of the leasing object has to take place in the lessor's balance sheet, activated on acquisition costs respectively production costs. A part for that is an unique extra payment: the inheritable right for erecting and maintaining a building at the real estate leasing. Rental payment affects the operating result. The

economic ownership is the deciding factor in the balance sheet classification. This is a difference compared with Anglo-Saxon liabilities to render an account.

## **France**

Leasing companies in France need a bank admission or an admission as a credit institution in order to start operations. Leasing companies are subjected to the French bank supervision. They must conform to certain obligations, for example minimum capital. The Code Civil gives an definition of "location simple". There is a definition, concerning the leasing business, in a law about leasing companies. The law about leasing companies contains a common definition of credit-bail, this is a lease with call option in favour of the lessee, to delimit it from other bank businesses.

trans-  
parency:  
France

The lessor acquires movable and non-movable economic goods to lease them to third parties. The contract contains an option to purchase the goods which is entitled to the lessee. The lessee can buy the goods to a price which was negotiated before the beginning of the contract, at the latest after the leasing contract term has passed. The existence of an option to purchase the goods is seen as a fundamental part of a credit-bail-agreement. The lessor remains the owner in terms of civil law during the leasing contract term. The lessee is obliged to use the leasing object in a commercial manner.

Leasing contracts which are concluded with individuals are strictly separated from credit-bail contracts. Only credit bail companies are governed by strict regulations. Leasing contracts which are concluded with individuals and transactions without a purchase option are not governed by regulations.

French accounting does not know the idea of economic ownership. French accounting is attached only to civil law. The lessor has to balance the leasing object in its balance sheet with its production costs. In the lessee's balance sheet, there is no reference to the leasing contract. The leasing contract remains off-balance. The rental payments are captured as expenditures in the profit-and-loss-account. The lessee has to give detailed information in the appendix, for example the total amount of all rental payments which have to be paid in the future.

## **Italy**

Due to the lack of specific provisions leasing contracts are finalized in accordance with the general rules of the Civil Code. A leasing contract is seen as a normal contract, which is concluded following the principles of contractual liberty between the lessor and the lessee. Finance leasing has been dealt

trans-  
parency:  
Italy

with in specific legislation, in particular by tax law. The legal formula which most closely resembles the leasing contract, is the one concerning the renting or hiring of fixed or movable assets. Finance leasing is taken to mean those operations of renting of fixed or movable assets, acquired or built by the proprietor following the choices and indications of the lessee. He takes all the risks involved and has the option of becoming the proprietor of such rented assets on expiry of the contract, upon payment of a predetermined sum.

Leasing companies must be registered in an official album under the control of the Ministry of the Treasury and must present a list of the directors, general managers and shareholders. A minimum capital is required (L 1 billion). All transactions above L20 million must be reported to the Italian Exchange office. The Bank of Italy indirectly controls finance and leasing activities and future capital ratios are expected.

If the leasing object is not leased, the lessor has to balance the leasing objects as immaterial assets within its fixed assets. The object is to balance as material asset if the object is leased to a lessee. The lessee has to balance neither the leasing object nor a leasing liability. Under special circumstances the leasing contract remains off-balance.

The rental payments are captured as expenditures in the profit-and-loss-account. The lessee has to show financial liabilities in the appendix.

## **United Kingdom**

Leasing companies in the U.K. neither need a leasing license nor a bank admission or registration. Nevertheless, the banking act guidelines have to be observed if a new company is founded. U.K.'s legal system is quite different from the Continent's legal systems because of its primary legal source „Case Law“. After using the „Case Law“ - the codified legal system takes a secondary role.

trans-  
parency:  
United  
Kingdon

It is the law's task to complete the Case Law and to do necessary corrections from time to time. The Statue Law is laid down through judicial decisions. Commonly leasing is defined as a transfer of an object's possession in which the transferer keeps the ownership. The accounting standards are following the principles of economic ownership and differentiating finance and operating leases. In a finance lease the economic ownership of the leased asset is assigned to the lessee. In that case, the registration in capital assets is justified. Leasing contracts which are not classified as finance lease are operating leases. The lessor has to balance the leased object in its capital assets.

## Belgium

Generally, Belgium's leasing companies are not seen as credit institution, a bank admission is not needed before starting operations. Nevertheless, an equipment-leasing company which plans to do activities in location financing, is committed to applying a leasing license before starting its operations. The Ministry of Economic Affairs has to confer the license.

trans-  
parency:  
Belgium

The Code Civil does not give an explicit definition of leasing contract. It does give a definition of what is considered an equipment-leasing company, though, in order to delimit its activities from those of other leasing companies. This definition is the location financing. It describes a full-amortization-contract. The rent payments cover the lessor's expenditures over the term of the leasing contract.

If the location financing applies, the lessee has to report the leasing object in its balance sheet. Other leasing contracts must not be reported in the lessee's balance sheet. In this case, it's the lessor's task to report the object which is reduced according to the plan of depreciation.

### Winners and losers through the monetary union

In order to explain why the majority of the lessors are gaining substantially from the monetary union, it seems necessary to discuss the euro's launching influences in an economic manner, first.

The advantages of the launching of the euro are mainly observable in the microeconomic sector. There are some more direct and some more indirect savings in transaction- and information costs. Direct savings concern the exchange costs deriving from the difference between buying- and selling rate. The European Commission has assessed these exchange costs, in a 1990 survey, at 2.5 per cent of the value in exchange.

trans-  
parency:  
euro-  
launch.  
advant.

Indirect savings result from the improvement of the companies' accountancy, the diminished storing of foreign exchanges and the quicker administration of cross-border bank transfers. The savings to this are estimated at 3.9 to 6.1 billion euro per year.

In summary, one can say that the introduction of the euro will quantitatively bring the savings of transaction costs of 0.3 to 0.4 per cent of the Union's yearly gross domestic product.

Winners of the described savings of direct and indirect transaction costs are clearly companies which are not only operating in their national markets but also abroad. Provided that leasing companies have followed the development in time, they should gain from the monetary union.

Disadvantages occur above all in the macroeconomic sector. For example, the exchange rate is no longer an instrument which helps to absorb economic shocks among different countries. There is also a danger of increasing unemployment because of regional wage adjustment. Lessors are hardly affected by this development. If the introduction of the euro can strengthen the economic growth, lessors can only profit through the strengthened demand for goods and services. Due to increased competition there will be more chances than risks for profitable lessors.

trans-  
parency:  
euro-  
launch.  
disadva.

The unified monetary union makes it possible to compare performances. This is not only the case in view of lessor's offers. It is also possible to create savings for lessors in the acquisition phase especially for equipment leasing companies. These opportunities also arise for real estate leasing companies. For example, a construction management company, which is a subsidiary of the real estate leasing company, gets a better market transparency. Thus, it is easier to compare price- and performance offers.

trans-  
parency:  
special  
advant. :  
lessors

An increasing competition is likely to occur in countries with hardly developed leasing markets. In less developed leasing markets a low leasing quota is observable. The increasing competition through foreign leasing companies will deteriorate the profits of the local leasing companies. Leasing companies which are future-oriented are founding subsidiaries in several European countries at the moment.

There are much more refinancing opportunities than before. Today, credit terms are easier to compare and there are more possibilities to do business with people who are ready to invest. The European Monetary Union has increased the quantity of floor space required. Regarding the location, the reorganization of European companies will heavily influence supply and demand.

This is one of the main reasons why customers profit from leasing companies' services. Leasing companies are capable of using refinancing instruments from other countries, which may be unknown in the domestic market because of the former currency risks. Nowadays, for example, Italy and Spain use long-term capital-market-loans to finance leasing objects, which has shown to be favourable. This was not possible in the past.



A problem for leasing companies as well as for other companies, however, is the introduction of the monetary union without a unified framework. Politicians want the monetary union to accelerate the institutionalization. Apart from the Monetary Union, there is no unified domestic market. The local character of leasing business is characterized by law of supervision, national law-system and national laws of taxation. For the leasing industry there are massive structural differences.

In Germany, the Netherlands and the United Kingdom, e.g. everybody is free to do the leasing business. In France, Spain and Portugal, leasing companies must be organized as credit institutions. While the German leasing market is open for anybody, the German leasing companies which go abroad, as e.g. to France, have to organize as a credit institution before starting business. Different tax systems, however, are still remaining after the introduction of the euro which has a great impact on cross-border leasing activities. Both, the European leasing industry and the European committees have to work together in order to reach a joint solution.

Regarding the leasing companies the introduction of the euro will separate the "wheat from the chaff". They all will profit from the microeconomical advantages. Because of the reasons mentioned before this is also the case in respect of the macroeconomical situation for those who are fit for the future. The leasing companies are looking forward to meet the challenge. Their customers gain through the cross-border presence of leasing companies all over Europe. The customers' cross-border activities can be supported and new customers can be attracted. This is the case in the home market of the leasing companies as well as in the lessors' foreign markets. The next step for the European committees and for the European leasing industry is to create a unified leasing market.

In the future it will not be sufficient to only be represented in all European markets, but also to be located in the right premise in the right place. The experience of an international leasing company is very helpful in this process. The problems which derive from the differences in legal systems and in ways of communication and mentality can be resolved by experienced leasing companies. This is particularly the case when working together with foreign planners, authorities and building / construction companies. Real estate management which is only focused on the national markets is not sufficient. If necessary one day, lessees should select a lessor capable of accompanying the lessee abroad.

Dipl. Kaufmann Klaus Feinen  
Sprecher der Geschäftsführung  
Deutsche Immobilien Leasing GmbH  
Königsallee 106

40215 Düsseldorf, Germany

Tel.: +49-(0)211-9946-101

Fax: +49-(0)211-9946-430