LEASING BENEFITS IN GLOBAL ECONOMY

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***Abstract**. Leasing may be considered the most important legal institution that was rarely encountered before World War II and has more recently exploded on a worldwide basis, with everything from autos to farm equipment to airplanes being leased. This chapter examines the tax, financial, and management benefits of leasing and its main sectors application according to the new standard IFRS 16 of the International Accounting Standard Boards (IASB). Tax benefits are one of the main reasons the lessee performs a leasing operation, especially thanks to accelerated depreciation. The financial advantages are those that guarantee a constant income to leasing companies over time established by the contracts. Management benefits, on the other hand, ensure a faster investigation phase than other forms of financing. It also examines the role that leasing plays in these sectors: Instrumental, distinguishing between operational and financial instrumental leasing; Mobile cars where we distinguish passenger cars from commercial or industrial vehicles; Naval and railway, with a strong incidence in the airline sector, by the most recent companies that operate with giants that have been present for longer on the market; Real estate, distinguishing between built and to be built; Commodities 4.0 high-tech and innovative, that have stimulated companies to revive the economy by investing in new technology assets to continue to compete.*
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Introduction. This article seeks to develop a composite picture of the defining features of leases and why leasing is such a widespread and highly successful economic institution. The reasons fall under three general headings. (i) Leasing is an attractive method of financing the acquisition of assets, especially for persons who have limited capital or would like to conserve their capital and cash flows for other purposes. (ii) Leasing is a device for minimizing the risks that either lessees or lessors associate with owning assets; although leasing also creates risks, various lease modifications have been developed to manage these derivative risks. (iii) By dividing the rights to an asset between the lessor and lessee, leasing permits the parties to specialize in different functions and to solve various impediments to contracting that would be difficult to overcome among separate owners. Understanding the economic advantages of leasing is an important first step in considering possible legal reforms for leasing.

Literature review. Analyzing the development of leasing from its origins to the present day, we can see the enormous success that this tool has found in the multiplicity of operators, leading to a continuous recourse by the company to this tool. Now we will try to analyze the main advantages that have allowed leasing to have such wide use.

To get a better exhibition picture, we'll try to group the benefits associated with leasing into three categories:

- Tax,
- Financial,
- Management.

Tax advantages: they are one of the biggest incentives that the lessee has with a leasing operation. The main advantages that banks, companies, and firms have are principally:

- Not to pay full VAT on the property, but only on periodic rents (and on the eventual redemption of the asset), so the outlay of the VAT will be deferred for the entire duration of the contract without affecting the current liquidity;
- To be able to deduct the periodic rents internally, both in terms of capital rate and interest rate, because of the instrumental nature of the leased asset.
- To be able to take advantage of the so-called "accelerated depreciation” accounting technique. Accelerated depreciation is to amortize the cost of a fixed asset in a shorter period of time than is normally practiced, with the aim of reaping tax advantages; that is, the possibility of amortizing the asset in a shorter time frame than that provided by law. In order to take advantage of this benefit, the duration of the lease agreement may not be less than half the depreciation period.

Financial advantages: they allow rental companies to preserve financial strength, ensuring that they make the necessary investments for their production activities, and are:

- The ability to buy goods by delaying the exit time during the entire duration of the contract, so being able to preserve the company's liquidity;
- It does not affect the company's credit capacity.
- Allows the entire financing of the asset, including VAT.

This allows companies to be able, as mentioned above, to make the necessary investments for the business, avoiding, on the one hand, the initial outlay and, on the other hand, taking shelter from the possible obsolescence of the assets leased, being able not to redeem the latter at the end of the contract, thus guaranteeing a greater turnover of the goods.

Finally, we can associate leasing with some "management advantages" that guarantee the user:

- A faster investigation phase than other forms of funding;
- Clauses within the lease agreement are very flexible, even in terms of ancillary performances.

This allows the landlord to enter into an ad hoc contract, thus negotiating better conditions, both in terms of rents, duration, and ancillary benefits, as well as the possibility of choosing the supplier and the terms of the lease agreement.

More specifically, leasing differs:

- From traditional forms of financing (for example, mortgages) to a much shorter investigation phase to much more incisive customization and full investment coverage,
- From the direct purchase of the asset for the fractionation of VAT to the accelerated depreciation
- From the sale in installments for the immediate "non-pass" of the asset, which allows to take advantage of the accounting treatment reserved for leasing.

Research methodology. Before introducing the next chapter with the analysis of the new accounting rules of IFRS 16, it is necessary to describe the scope of IFRS 16 and leasing sector applications, with a market analysis and a forecast of their future development in relation to the new accounting.

On the date of the first application of IFRS 16 (January 1, 2019), it is necessary to identify all leasing contracts based on the new definition introduced by IFRS 16. The new accounting standard is applied to contracts that are or contain a lease under IAS 17 and IFRIC 4;

As provided for by IAS 17, the new accounting standard excludes from its scope all leasing transactions attributable to the cases listed in the following areas:

a) leasing for exploration or extraction of minerals, oil, natural gas, and similar non-regenerative resources (IFRS 6);
b) licensing agreements for goods such as films, video recordings, shows, manuscripts, patents, and copyrights (IAS 38);
c) valuations of properties owned by tenants that are accounted for as real estate investments (IAS 40);
d) valuations of real estate investments granted by lessors by operating leases (IAS 40);
e) valuations of organic assets used by the lessor through financial leasing (IAS 41);
f) valuations of organic assets granted by the lessor through operating leases (IAS 41), as these cases are regulated by different specific IAS.

With the introduction of the new IFRS 16 accounting standard, the balance sheets drawn up in accordance with international principles will provide a more faithful representation of leases.

Looking at the leasing sectors, the increase in the number of contracts was driven by the instrumental sector, followed by registrations in the car sector. Even brighter, on a much smaller scale, is the volume performance of the aeronaval sector.

The performance of the real estate sector fell slightly compared to the previous year, although, as we shall see, there was still a recovery in the leasing sector on properties to be built.

Table 1: **Leasing and rental numbers**

TYPE OF LEASING	Numbers	VALUE	Var % Num	VAR % valuee
Leased vehicles	119.319	4.719.115	0.8	25.7
NLT vehicles	250.042	4.622.815	15.8	12.9
Leased NLT vehicles	35.604	1.097.702	-13.7	2.7
NLT Comm. vehicles	40.404	746.995	-11.7	-13.9
Industrial vehicles	22.313	*2.184.193*	5.7	7.8
TOTAL CARS	**467.682**	**13.370.820**	**5.7**	**13.2**
Financial instrumental	93.446	7.337.054	-2.5	15.5
Operative instrumental	118.177	1.568.303	51.3%	34.8
TOTAL INSTRUMENTAL	**211.623**	**8.905.357**	**21.7%**	**18.5**
AERONAVAL RAILWAY	**354**	**521.829**	**-0.8**	**59.3**
Real estate built	3336	2.139.889	-2.8%	-6.9
Real estate to be built	869	1.601.852	5.6	6.1
REAL ESTATE	**4295**	**3.741.741**	**-1.2**	**-1.8**
ENERGY	**107**	**88.228**	**-11.6**	**-27.8**
TOTAL	**683.971**	**26.627.975**	**10.1**	**12.9**

***Source*: Tibuzzi, Pontecorvi, Toscano (2018).**
To lease: Leasing and rental numbers

Looking at the medium-term dynamics of the lease, as mentioned, the largest increases have been in the car and instrumental sectors.
It is these two segments that hold the highest share of the contract (over 80%) both in terms of number and value. Car leasing in 2017 reached almost two million new units, consolidating the fourth year of growth for the sector. The results demonstrate *(Figure 1).*

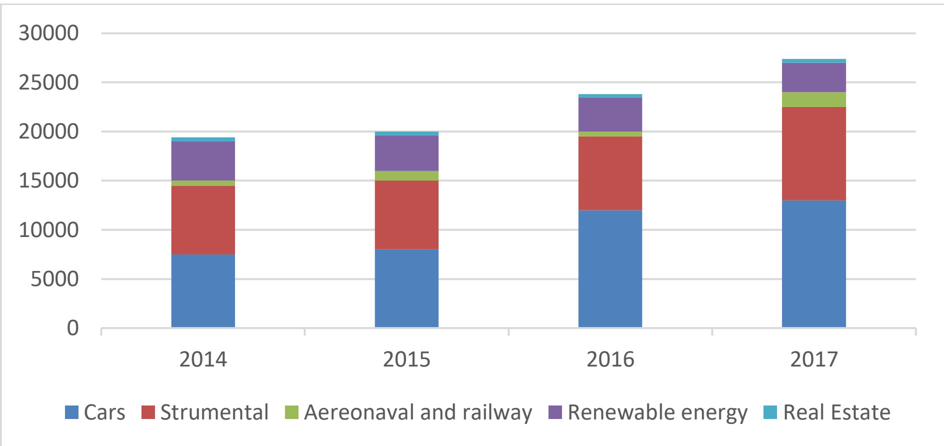

Figure 1: **Leasing sectors**
Source: Tibuzzi, Pontecorvi, Toscano (2018). To lease: Leasing and rental numbers

In 2017, there was also a real "boom" in dealer registration cars: these types of cars, used at zero km and therefore offered on cheaper terms than new cars, have in fact powered the private market, partially offsetting the decline of the sector of new cars. The results demonstrate *(Figure 2):*

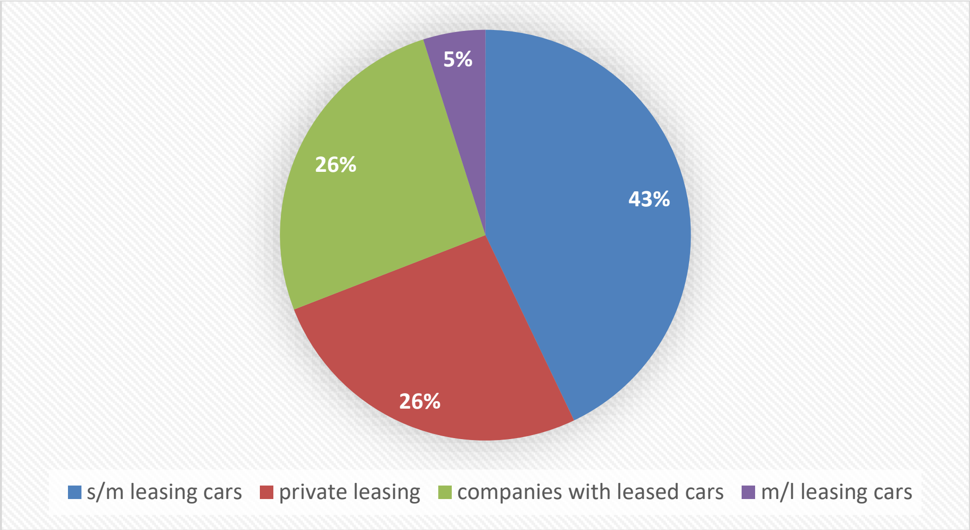

Figure 2: **Types of cars leasing**

Source: Tibuzzi, Pontecorvi, Toscano (2018). To lease: Leasing and rental numbers

In the future, car leasing, following the introduction of IFRS 16, all rental contracts will be interpreted in the light of which they grant a right of use on rented goods in exchange for future payments (c.d. liabilities pertaining to the rental agreement); in fact, the IASB, also following the comments received on the complexity of application that would have encountered certain types of operators, provided some exemptions to the application of the new accounting standard as well as some practical expedients. IFRS 16 will not be applied to leases with a term of the contract not exceeding 12 months and whose contract-subject asset has a small unit value.

Research methodology. It is easy to infer that the main impact will be on long-term rental vehicles, as they respond, in most cases, to the dictates of IFRS 16 (non-modest goods with rental durations of more than 12 months), while other goods often rented (mainly PCs and other low-value equipment) are excluded. On the accounting level, the first consequence will be the recognition of the rights of use and a liability related to the leasing contract on the lessee's balance sheet.

Depreciation of usage rights and interest on the corresponding liabilities should also appear in the lessee's profit and loss account. This means that, instead of in the form of a rental canon as under IAS 17, in accordance with IFRS 16, the cost of a leasing contract will be underlined through a stable depreciation and a decreasing interest rate in the financial plan. Another consequence is that the new standard will improve the EBITDA indicator by accounting for depreciation and interest instead of current overheads.

On the balance sheet, the impact will be on the inclusion in the asset value of vehicles with a higher financial debt than stated by previous IAS 17.

A practical example can elucidate what has just been said.

Table 2: **Effects on contracts long-term car rental**

The company A has a contrats with the following features:		
Value of leased assets	K € 100	
Financial debt	K € 120	
Contract duration	5 years old	
Annual rental rate		
Equity share	K € 20	
Interest rate	K € 4	
Vehicle depreciations	5 years old	
The income effects resulting from the application of the new principle, compared to IAS 17 will be as follows:		
	IAS17	IFRS16
Rental costs	K € 24	-
Ebitda Impact	K € 24	-
Depreciation		K € 20
Financial charges		K € 4
Impact on net profit	K € 24	K € 24
From the patrimonial point of view, next year, we will have:		
	IAS17	IFRS16
Vehicles	-	K € 80
Active Impact	-	K € 80
Financial liabilities	-	(K € 80)
Passive Impact	-	(K € 80)

Source: S. Ladogana (2018). IFRS 16: effects on contracts long-term car rental. Budget&Income,

In subsequent years, the impact on net profit will be reduced by the portion of interest, while depreciation will be constant for the expected duration. On the balance sheet side, the value of assets will continue to decline as a result of depreciation, and the value of liabilities will decrease as a result of capital repayments. Moving on to instrumental leasing instead, this sector is the one that has recorded the strongest growth, with significant growth compared to 2016.

The government of Italy, for example, has helped to increase this phenomenon, where the total value of the different types of capital goods leased increased for most goods by more than 20% over the previous year. This phenomenon is mainly linked to the effects of incentives related to "Superammortamento" and "Piano Industria 4.0 (the Piano Industriale 4.0 is an opportunity for all companies that want to seize the opportunities related to the fourth industrial revolution).

Through this plan, innovative goods companies have been stimulated to boost the economy by investing in new technological goods to continue to compete. "Piano Industria 4.0" and the main actions activated by the government through Superammoramento and Iper-ammortamento (it is used to support and incentivize companies that invest in new capital goods, material and intangible goods, software, and IT systems that are functional to the technological and digital transformation of production processes)

Moving on to the air and rail sector, the figures collected in 2017 show another positive year for the aeronaval and rail leasing sectors: the amount of the total contracted increased by 59.3% compared to the previous year. Positive signs of growth also exist for the aviation industry. Nautical leasing (that is, recreational and commercial nautical), as seen, represents the dominant part of the aeronaval and rail sectors.

The results demonstrate *(Figure 3):*

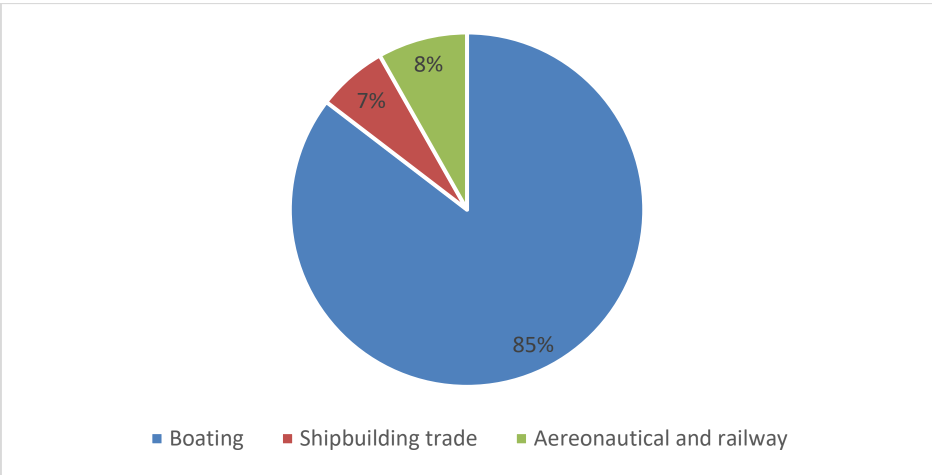

Figure 3: **Aeronautical and railway leasing**

Source: Tibuzzi, Pontecorvi, Toscano (2018). To lease: Leasing and rental numbers

Concluding with real estate leasing, however, the negative trend of the "built" sub-sector was offset by positive values for leasing investments in the "to be built" sector. This dynamic between the two sub-sectors, which has been repeated for three years, has allowed the leasing sector to increase the weight of the total real estate contract. The results demonstrate *(Figure 4).*

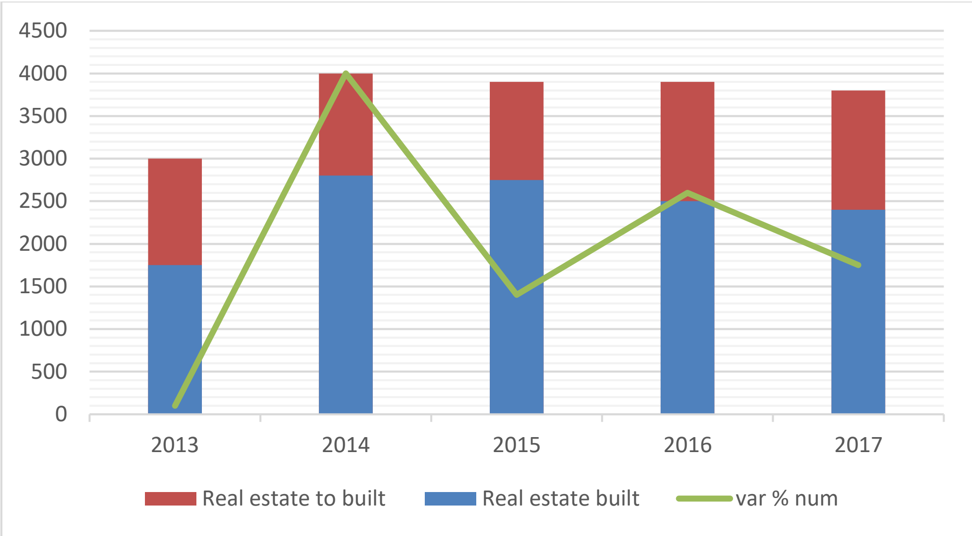

Figure 4: **Real estate leasing**
Source: Tibuzzi, Pontecorvi, Toscano (2018). To lease: Leasing and rental numbers

Although industrial real estate has a higher value than commercial real estate, there has been an increase in the weight of office, hotel, and shopping center real estate, to the detriment of residential and public sector real estate, which represents a minimal share of the portfolio offered by leasing. The results demonstrate *(Figure 5):*

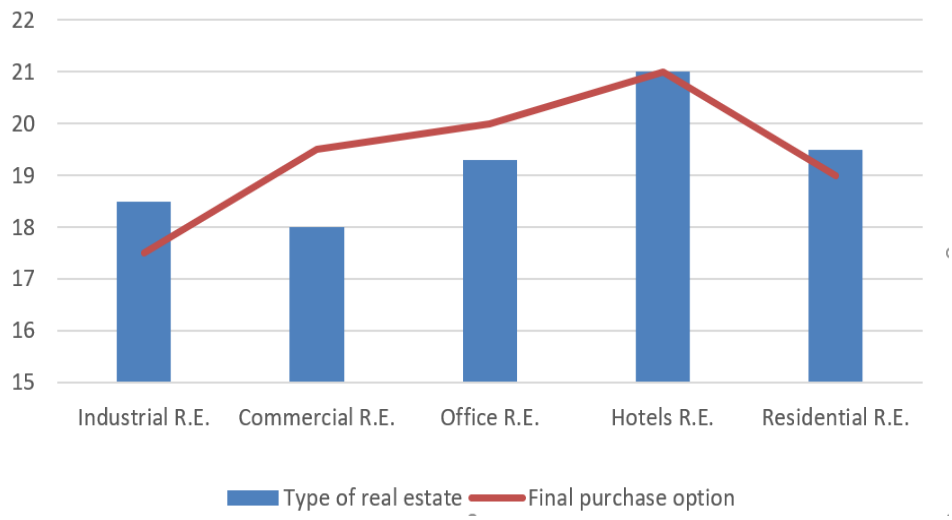

Figure 5: **Types of real estate**
Source: Tibuzzi, Pontecorvi, Toscano (2018). To lease: Leasing and rental numbers

Discussion and conclusions. For the application of the new IFRS 16 standard, companies in the sectors mentioned before should plan and carry out these activities to take advantage of leasing:

- definition of the project, its phases, and its organizational framework;

- planning for the implementation of the project and its timing;
- identifying the types of contracts potentially impacted by the new international standard, appreciating their accounting effects, and choosing the transition methodology to be adopted;
- analysis of the effects on the reporting system, the balance sheet, key performance indicators, and financial covenants;
- development of the analysis of the different scenarios that lie ahead, assessing the opportunity to renegotiate existing contracts, and identifying the critical elements when entering into new contracts.

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