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to Investing in Greece



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■ FINANCIAL CONTRACTS



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LEASING

Legal Framework – Tax Considerations

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What is meant by “leasing”?

The simple term of “leasing” covers a multitude of different contract types. A common definition of leasing is nevertheless provided by the International Accounting Standards Committee under International Accounting Standard 17 (hereinafter IAS17). Such definition was furthermore adopted by the European Union under the EC Regulation 1725/2003. Thus, under IAS17 leasing is defined as an agreement whereby the lessor conveys to the lessee, in return of series of payments (Rentals), the right to use an asset for an agreed period of time. Title of ownership to the leased asset may or may not be transferred to the lessee at the end of the lease agreement. In financial leasing agreements title of ownership to the asset is agreed to be transferred to the lessee upon maturity of the lease. Leases are classified under IAS17 as either financial or operating leases. A financial leasing is a lease that transfers substantially to the lessee all the risks and incidental rewards to ownership of an asset as opposed to the financial risks assumed by the lessor. Operating leases on the other hand are the leases where the lessor assumes both financial and asset risks. Generally all non financial leases are considered as operating leases.

Is there a legal framework in Greece governing financial leasing agreements?

Law 1665/1986, as amended and in force, (hereinafter the Law) introduced for the first time in Greece the concept of financial leasing. The Law did not provide with specific definition for financial leasing agreements but merely referenced to certain characteristics that a financial leasing agreement should have in order to be considered as such. Thus, according to Article 1 of the Law, financial leasing is mainly defined as a contract between a leasing company or a bank (the lessor) and a company or a professional (the lessee) whereby the first grants to the latter, for a certain period of time, the use of assets upon rental, whilst giving to the lessee the right at the end of the lease term, to either buy the asset or to renew the lease agreement (the Option). The Law only regulated financial leasing transactions.

Why should I choose financial leasing rather than other financial instruments?

Financial leasing is a contemporary and advantageous financial tool for any business seeking financing in order to acquire and use capital assets, securities and/or other property, with the total funding of their value but without any need for direct disbursement of the necessary funds. Thus, in financial leasing transactions the lessee

shall not directly participate in the investment costs and will keep unaltered (even theoretically) its creditworthiness, as well as integer position or even its liquidity funds for making other investments. Generally, financial leasing presents for potential investors the following advantages:

- The ability to finance fixed, capital assets without providing further covenants to the lessor (since the lessor is the owner of the lease asset);
- The improvement of a company's capital structure and its credit rating;
- The opportunity to reduce the overall tax expense (the rentals are tax deductible);
- The exploitation of financial resources deriving from privately-owned financial assets (sale and lease back of commercial buildings);

Is it possible for anyone to receive financing through a financial leasing transaction?

Financial Leasing is a financial tool used by companies and/or freelancers for obtaining and using capital assets for their productive and investing purposes. Pursuant to Article 1 of the Law, notwithstanding the lessee's nationality and/or place of establishment, the asset leased by means of a financial leasing should solely be destined for the lessee's professional use. Thus, any person (legal entity, natural person) may be eligible to contract a financial leasing agreement as long as such persons exercise any kind of profession or business activity and intends to use the leased asset for such purposes. On the contrary, employees, consumers, public servants and/or any other person not conducting a commercial business activity are not entitled, in principal, to financial leasing.

Which are the entities entitled to provide financial leasing?

Pursuant the provisions of Law, as currently in force, leasing contracts may only be concluded by the following entities as lessors:

- leasing sociétés anonymes established with the object of conducting the operations referred to in Article 1 of the Law;
- credit institutions, within the meaning of Article 1(a) of Law 3601/2007, lawfully established and operating in Greece;
- credit institutions, within the foregoing meaning, based in EEA Member States and established in Greece through branches or providing cross-border services in Greece, within the meaning of Articles 13 and 15 of Law 3601/2007;
- credit institutions, within the foregoing meaning, registered in third countries and established in Greece through branches;
- financial institutions, within the meaning of Article 2(11) of Law 3601/2007, based in EEA Member States and established in Greece through branches or providing cross-border services in Greece, under Article 18 of Law 3601/2007; and
- financial institutions registered abroad and established in Greece through branches.

The establishment of leasing companies in order to conduct leasing activities in Greece is subject to authorization by the Bank of Greece, which is responsible to supervise

and control such companies, define the conditions of authorization and set solvency, liquidity and risk concentration ratios.

Shall I contact directly the leasing company?

First of all, usually the lessee enters into negotiations with the supplier (i.e. seller of the asset to be leased), during which the lessee chooses the asset suitable for its activity and agrees with the supplier the purchase price of the asset. The lessee then refers to the leasing company in order to finance the purchase of the asset. The leasing company carefully examines the financial good standing of the lessee and his ability to pay the leasing rentals. If the leasing company agrees to finance the purchase, a financial leasing agreement is then executed between the lessor and the lessee. Subsequently, the leasing company (lessor) settles to the supplier the purchase price of the asset and mandates the latter to deliver the asset to the lessee.

Can I lease any kind of asset for my business through financial leasing?

Pursuant to the provisions of the Law, a Financial Leasing agreement may concern, subject to the exceptions herein below mentioned, any kind of movable and/or immovable asset the use of which may be granted to the lessee by the lessor. Such assets may be, including but not limited, as referred hereinunder:

- Movable assets: machinery, industrial equipment (for commercial, industrial or agricultural use), harvesters, tractors, earth movers, other “wheeled” assets that are not registered, computers and business machines, IT equipment and other business machines, road transport vehicles, motorcars etc;
- Airplanes, helicopters;
- Real estate’s (i.e. professional buildings, agricultural plots, apartments, offices etc.);

Services, boats and/or any kind of floating crafts cannot, pursuant to Article 1 par. 2 and 3 of the Law, constitute the object of a financial leasing agreement. Furthermore, professional buildings are also excluded for sale and lease back transactions [as opposed to direct leasing transactions] where the lessee is a freelancer [as opposed to a legal entity].

Are there different kinds of financial leasing agreements?

Although there are different kinds of financial leasing agreements (i.e. mixed leasing, leveraged leasing, construction leasing, lease down, vendor leasing etc.) in the majority of cases financial leasing is encountered, either as a:

(a) “Direct leasing” transaction: whereby the lessee enters into negotiations with the supplier of the asset and agrees with the latter all matters relating to the purchase of the asset (specifications, pricing, delivery dates etc.). The leasing company executes a financial leasing agreement with the lessee and settles the purchase price of the asset. The supplier then delivers the asset to the lessee. Usually the lessor, since it did not participate in the negotiations for the purchase of the asset, conveys to the lessee all rights a buyer usually has against the seller (supplier) of such asset under a contract of sale. The lessee undertakes to keep the asset appropriate for use, to enter into an

insurance agreement for such asset and in general to bear all the obligations deriving from it. The lessee bears in other words all the risks of the asset;
or (b) as a “sale and lease back” transaction: whereby the potential lessee prior to the execution of the leasing agreement is the owner of the asset to be leased. Thus, the lessee sells the asset to the leasing company, receives the agreed purchase price for the transfer of property and subsequently executes the leasing agreement whereby the lessor leases back to the lessee the use of the asset. Such transaction offers to the lessee liquidity, as opposed to the use of a specific asset as under direct leasing transactions.

Can I “sell and lease back” any kind of asset?

Pursuant to the Law, as amended and currently in force, any asset could in fact become the object of a sale and lease back transaction. In practice however, sale and lease back transactions are mainly encountered in real estate (commercial buildings) transactions.

Is there a minimum term for a leasing transaction?

The Law provides minimum term requirements for leasing transactions depending on the asset leased. Thus the minimum lease term for equipment is three (3) years, for aircrafts five (5) and for real estate ten (10) years.

Can I repay the financial leasing and buy the asset before maturity of the leasing contract?

Yes. Usually repayment of the financial leasing and transfer of property of the leased asset to the lessee may happen before maturity of the lease agreement as long as the lessor agrees to such repayment. Before any such repayment the lessee should nevertheless examine all tax implications relating to it.

Am I allowed to sublease a leased asset?

Yes. The lessee may request from the lessor to grant him the right to sublease the asset. Sublease of the asset is more often encountered in real estate transactions (e.g. hotels and/or real estate companies leasing premises and then subleasing such premises to third parties) and in “passenger car” transactions (e.g. car rental companies). Usually the leasing company requires that the sublease rentals are assigned from the lessee to the lessor in order for such rentals to be directly collected from the leasing company. The Lessor thus adjusts the amount of the leasing rentals to the amounts collected from sublease rentals (back to back).

When is a financial leasing agreement dissolved?

A financial leasing agreement is usually dissolved upon:

- maturity of the lease term; The lessor transfers title of ownership of the asset to the lessee if all rentals are paid;
- purchase of the asset before maturity of the agreement;
- destruction of the asset;
- termination of the agreement; Usually the lessor terminates the leasing agreement if the lessee is in breach of the contract;

- bankruptcy of the lessee; The financial leasing agreement is automatically terminated (pursuant to Article 4 par. 3 of the Law).

What happens with the leased asset if the leasing company is declared bankrupt?

As opposed to the lessee's bankruptcy, the leasing agreement is not automatically terminated upon bankruptcy of the lessor. Claims that the lessor had against the lessee (in relation to the payment of the rentals etc.) are transferred to the bankruptcy property and the rentals should be paid to the trustee in bankruptcy. The trustee in bankruptcy, upon maturity of the lease agreement and settlement of the totality of the rentals is obliged to transfer title of ownership of the asset to the lessee.

Are there any fiscal advantages in financing my business through financial leasing?

As above mentioned the institution of financial leasing was inaugurated in order to assist local economy and to facilitate the accomplishment of investments. Thus, the Law provided leasing transactions with different tax exemptions. Pursuant to Article 6 of the Law a complete and objective exemption of tax, duties, contributions, rights due to the state and/or to state companies and in general due to any third party was established. Furthermore, as opposed to borrowers with loan agreements that are only allowed to deduct from their gross income the interest of installments paid to the bank, lessees with financial leasing agreements are entitled to deduct from their gross income the totality of the amount of the rentals paid to the lessor (interest and capital). The amount of the rentals is considered as an operating expense of the lessee.

Furthermore, according to Article 6 par. 1 of the Law, notwithstanding VAT and/or income tax, the following are exempt of any other tax, duties, contributions, rights etc:

- The contracts by which the leasing company acquires any movable assets which will then be leased through a financial leasing agreement. (Transfer of property of a real estate is subject to property transfer tax except in cases of sale and lease back of commercial buildings and transfer of property from an offshore company);
- The financial leasing agreement itself;
- The assignment agreements or other agreements relating to or in connection with a financial leasing agreement;
- The Public notary's fees etc;
- The transfer of property of the asset to the lessee at maturity of the lease agreement (even if such asset is a real estate) are exempt from property transfer tax and from surplus value tax.

Is there any special accounting treatment involved in a financial leasing transaction?

(a) Lessor's accounting. Under IAS 17 finance leasing lessors shall record 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 recorded so as to give a constant periodic rate of return on the lessors net investment in the lease.

(b) Lessee's accounting. The lease should be recorded in the balance sheet of the lessee as a fixed asset and as an obligation regarding the payment of 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). Initially the value of the asset and liability should be calculated as the fair value of the asset or if lower, as the present value of the minimum lease payments. The value of the asset is then depreciated in the same way as for any other fixed asset over the shorter of (i) the term of the lease and/or (ii) the asset's useful life.

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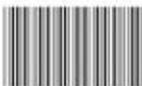
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