

THESIS ON ECONOMICS H25

**Impact of Lease Capitalization on the
Development of Accounting Standards:
A Theoretical Research**

TOBIAS WIEBELT

TUT
PRESS

TALLINN UNIVERSITY OF TECHNOLOGY
School of Economics and Business Administration
Department of Accounting

**Dissertation was accepted for the defense of the degree of Doctor of
Philosophy in Business Administration on 11th April, 2012**

Supervisor: Professor Lehte Alver, PhD
Department of Accounting, Tallinn University of
Technology, Estonia

Opponents: Associate Professor Ruta Šneidere, PhD,
Faculty of Economics and Management
Department of Accountancy and Auditing
University of Latvia, Republic of Latvia

Jiří Strouhal, PhD
Department of Business Economics,
Faculty of Business Administration,
University of Economics Prague, Czech Republic

Defense of the thesis: May 28, 2012

Declaration:

Hereby I declare that this doctoral thesis, my original investigation and achievement, submitted for the doctoral degree at Tallinn University of Technology has not been submitted for any academic degree

Tobias Wiebelt

Copyright: Tobias Wiebelt, 2012

ISSN 1496-4 782

ISBN 978-9949-23-268-0 (publication)

ISBN 978-9949-23-269-7 (PDF)



European Union
European Social Fund



Investing in your future

Publication of this thesis is granted by the
Doctoral School of Economics and Innovation
created under the auspices of European Social
Fund

MAJANDUS H25

**Liisingu kapitaliseerimise mõju
arvestusstandardite arengule:
teoreetiline käsitus**

TOBIAS WIEBELT

CONTENTS

INTRODUCTION.....	7
Abbreviations	13
List of Tables.....	16
List of Figures	17
1. THE ECONOMIC APPROACH AND THEORETICAL BASIS FOR CAPITALIZATION OF LEASES IN GERMANY	18
1.1. Concept and Purpose of the Economic Approach.....	18
1.2. Historic Development of the Economic Approach	23
1.3. Classification of the Economic Approach within the Judicial Methodology	26
1.3.1. Relationship between the Economic and Legal Perspective	26
1.3.2. Interpretation of the Economic Approach within Jurisprudence	27
1.3.3. Instruments for the Legal Interpretation.....	27
1.3.4. The Limit of Law Interpretation.....	32
1.4. Application of the Economic Approach.....	33
1.5. Classification based on the German Decrees of Leases	39
2. THE PRINCIPLE “SUBSTANCE OVER FORM” AND CAPITALIZATION OF LEASES ACCORDING TO THE INTERNATIONAL GAAP	45
2.1. Definition of “Substance over Form”	45
2.2. Application Scope of the IAS 17.....	47
2.3. Classification of Lease Agreements.....	51
2.3.1. Conceptual Foundations of the IAS 17	51
2.3.2. Capitalization according to the Economic Ownership	52
2.3.3. Classification Criteria (Examples)	56
2.3.4. Classification Criteria (Indicators)	62
2.3.5. Consequences of Changes to the Contract Conditions	63
2.3.6. Special Classification Regulations for Real Estate Lease Agreements	64
2.4. Critical Appreciation of the IAS 17	65
2.5. Criticism of the All or Nothing Approach and Outlook.....	68
2.6. Interim Conclusion.....	69
3. CAPITALIZATION OF LEASES ACCORDING TO THE US GAAP	72
3.1. Conceptual Foundations.....	72
3.2. Classification Criteria According to ASC 840	76
3.3. Interim Conclusion.....	81
4. REFORM PROPOSALS FOR FUTURE LEASE CAPITALIZATION	83
4.1. Characterization of the Reform Efforts Regarding the Lease Capitalization	83
4.2. Financial Components Approach	84
4.2.1. Lease Capitalization: Conceptual Basis	84
4.2.2. Capitalization of Lease Agreements by the Lessee	86
4.2.3. Capitalization of Lease Agreements by the Lessor	96
4.2.4. Evaluation of the Information Transmission	101

4.3. Whole Asset Approach	101
4.3.1. Capitalization of Leases	101
4.3.2. Critical Evaluation.....	103
4.4. Critical Comparison of the Discussed Concepts	104
4.5. Status of the Reform Proposals	108
4.5.1. Time Schedule of the Reform Project	108
4.5.2. Analysis and Assessment of the Topical Discussion Paper	112
4.5.3. Characterization of the Decision Relevance.....	115
4.5.4. Interim Summary and Outlook.....	118
4.6. Conversion of the Right of Use Concept in Capitalization Leases According to the IFRS by the ED/2010/9 “Leases”	121
4.6.1. Introduction	121
4.6.2. The Standard Draft “Leases”	122
4.6.3. Capitalization by the Lessee	124
4.6.4. Capitalization by the Lessor	126
4.7. Effects on Selected Subject Areas.....	132
4.7.1. Sale and Leaseback Transactions	132
4.7.2. Multi-level Lease Agreements	133
4.7.3. Evaluation of the Standard Draft.....	134
4.8. Interim Conclusions	135
5. CONCLUSION	137
REFERENCES.....	145
Appendix 1. Fiscal Classification of Fully Amortized Contracts (Movables) .	163
Appendix 2. Fiscal Classification of Fully Amortized Contracts (Immovable – Buildings).....	164
Appendix 3. Fiscal Classification of Fully Amortized Contracts (Immovable – Land)	165
Appendix 4. Fiscal Classification of Partially Amortized Businesses with Movables	166
Appendix 5. Fiscal Classification of Partially Amortized Businesses of Immovable.....	167
Appendix 6. Elulookirjeldus	168
Appendix 7. Curriculum Vitae	171
KOKKUVÕTE.....	174
ABSTRACT	179

INTRODUCTION

Leasing of assets is one of the world's oldest business activities. It can be traced back thousands of years and it has evolved substantially over the last century. Many ancient civilizations used leasing as a financing tool, including the Greeks, Romans, Egyptians and Phoenicians. In the early Medieval Ages, various types of agricultural, industrial and even military equipment were leased (e.g. in England, Norway and Wales). In the modern times, the industry has grown from being a manufacturer-selling technique into a specialized financial service with the formation of the first independent leasing company in the United States in 1952. The industry extended to Europe and Japan in the 1960s and has been spreading throughout emerging markets and developing countries since the mid-1970s. By 1994, leasing had been established in over 80 countries. More recently, we have seen the significant growth of independent financing companies of all sizes from the very large ones operating in several countries, to an endless number of small and medium-sized businesses specializing in the financing of the acquisition of particular types of equipment and vehicles. Leasing companies are pioneering joint venturing, out-sourcing, partnering other services out or creating alliances for financing risk sharing and their innovative products and services are a driver of change in financial services.

Nowadays, the largest external source of financing the acquisitions of equipment is, beside banks and credit unions, leasing. It is the fastest growing form of business investment. In 2012 alone between \$550 and \$600 billion dollars of equipment will be leased throughout the world. Overall, worldwide leasing volume continues to grow. Over 35% of all capital equipment is financed by some form of leasing. Eight out of ten companies have turned to leasing to get ahead and stay ahead.

Leasing, as a financing instrument, is an integral part of the entire business life today both in the commercial and private sectors. The understanding that the advantage of investment goods lies primarily with their use and not with their legal ownership is becoming more and more widespread within enterprises. Beneficial ownership in connection with lease agreements can be interpreted as an undercover purchase, combined with a loan financing by the lessor. Therefore, it is not surprising that the role of leasing increases due to the increasingly cautious attitude of banks. Leasing companies saw continuous growth even during economically difficult times, and in some areas, these increases are significantly higher than the overall economic growth. Leasing leads to enormous balance sheet changes. It has a direct effect on the invested capital and on the subsequent depreciations. In addition, it affects the capital structure and thence the debt to equity ratio of an enterprise. To avoid negative rating assessments, lessees usually have a special interest in designing the lease contract in such a way that only the rent has to be reported in the balance sheet.

In this case the leased item and especially the relevant lease obligation would not appear in the balance sheet and borrowed capital and the debt to equity ratio would not be affected. Therefore, the central question regarding leasing businesses is the financial allocation of the leased items. Who has to capitalize what?

The example of leasing – the importance of which is increasing constantly, shows clearly how complicated the correct classification of assets is, despite the help derived from viewing it from an economic approach. Should the leased item be recognized in the lessor's or lessee's balance sheet? Are the classification rules internationally comparable? What are the differences and similarities of the German Handelsgesetzbuch (HGB – Commercial Code), the US Generally Accepted Accounting Principles (US GAAP) and the International GAAP (IASs/IFRSs)?

A trend towards the internationalization of financial reporting is taking place which should help to improve and harmonize the transfer of information (Bay, Bruns, 2000, pp. 716–717). In particular, with the support of the European Union, the International Financial Reporting Standards (IFRSs) as a worldwide system of financial reporting, together with the US GAAP and the German Commercial Code have been established. The passage of the EU Regulation from July 19, 2002 stipulated that all business entities with an orientation towards the capital market must apply the IASs/IFRSs in their annual financial reports, starting from January 1, 2005. The obligatory application harmonizes financial reports with regards to capital market orientation within the EU. Enterprises with securities on stock exchanges outside the EU, which used other internationally accepted reporting standards (e.g. the US GAAP), were granted an extension until January 1, 2007. Since then they have been obligated to use the International GAAP.

Besides the harmonization of financial reporting within the EU, a project of the International Accounting Standards Board (IASB) and the US Financial Accounting Standards Board (FASB) for the convergence of IASs/IFRSs and US GAAP is ongoing. The convergence project was decided on September 18, 2002 and its objectives are the harmonization of the two reporting systems and the coordination of future work programs of the two standard setters. On February 27, 2006 the IASB and the FASB set up a concrete timetable for the convergence of the International GAAP and the US GAAP. Several individual projects were agreed on in the process, during which specific financial reporting problems will be dealt with. In the course of the development of the convergence project the financial reporting of lease agreements was added to the common agenda of IASB and FASB in July 2006.

The German enactments (“Leasingerlasse”) with regard to lease attempted to solve the problem by applying clear and unambiguous classification rules. However, the fixed quantitative limits (e.g. narrow lower deviation of the limited value) allow the purposeful setup of a lease agreement (Knobbe-Keug, 1993, p. 77; Sabel, 2006, p. 32; Bordewin *et al*, 2003, p. 39). Nevertheless, the International GAAP does not demand fixed limited values for economic reasons; thus there is significant room for interpretation.

The currently valid financial reporting regulations for lease agreements according to the International GAAP and the US GAAP have an identical basic concept – the so-called risk and reward approach. For the purpose of financial reporting, all lease agreements have to be classified in accordance with the respective financial reporting standards IAS 17 (Leases) and FASB ASC 840 (Leases Operating and Capital – Accounting Standards Codification 840), and based on the rewards and risks for each leasing partner – either as a finance/capital lease respectively, or as an operating lease. The financial reporting obligation of the leased item depends on the type of lease contract. Both reporting systems follow the all or nothing approach, according to which in cases of a finance/capital lease the leased item and the resulting obligations have to be reported by the lessee, while in cases of operating leases the lessee does not have to capitalize it in the balance sheet. The reporting neutrality of certain lease agreements and the sensibilities of classifying the lease are the main points of criticism of the current reporting regulations in relevant literature (Fülbier *et al.*, 2005, pp. 275–277).

This criticism is one of the reasons why IASB and FASB strive for a fundamental reform as part of the common leasing project, which is based on the so called G4+1 working group. One core objective is the cancellation of the classification of leases into two in the current financial reporting and replacement by a system of equal treatment of all lease agreements. A preliminary result of the discussion so far, the two international standard setters published a paper on March 19, 2009. It contains the conceptual basis for a possible future financial reporting system for lease agreements. The possible change of paradigm regarding the financial reporting of lease agreements is of great significance for investors, especially since leasing is being used very widely nowadays.

On August 17, 2010 IASB and FASB presented the Exposure Draft ED/2010/9 “Leases”, which proposes a fundamental shift in the way leases have been capitalized until now. More than 700 opinions resulted in a hot debate, similar by the publication of the discussion paper in March 2009. The boards adopted a large part of the original version of the discussion papers in the ED/2010/9, despite some strong dissenting voices. It remains to be seen how the result of the convergence project, which has been in progress since 2006, will turn out.

The main motivation behind the proposed fundamental revision of IAS 17, SFAS 13 and ASC 840 respectively is the reduction of the so-called off-balance-sheet accounting, which in the view of the standard setters leads to a distortion of the financial information. Thus, the boards suggest the complete annulment of the current categorization into finance/capital leases and operating leases on the basis of an opportunity-risk approach. In conformity with the discussion paper the capitalization of lease contracts in the ED/2010/9 is based on the right of use approach. The proposal is that the lessee should capitalize all lease agreements at all times. A right-of-use asset in the amount of the cash value of the future installments and at the same time a liability in the same amount will be capitalized. While the discussion paper focuses primarily on the capitalization by the lessee, the ED/2010/9 suggests also concrete changes for the capitalization by the lessor. In contrast to the lessee, the lessor will continue to have two capitalization methods with new naming available – the “performance obligation” and “de-recognition”. The two methods differ primarily with regard to the question, whether the lease contract is treated similar by a sale or not at the time of its conclusion. The distinction of two types of lease contracts in the IAS 17 on the side of the lessee, which was criticized earlier on, re-appears again in the standard draft in a similar form on the side of the lessor: on the basis of the opportunity-risk approach, he chooses one of the two capitalization methods. Although in accordance with the ED/2010/9 all lease contracts are treated the same for lessees, the proposed changes will result in the loss of the (fundamental) mirror-inverted capitalization by the leasing parties. This is a distinct contradiction to the efforts of the equal treatment of lease contracts, which seeks to provide more transparency and comparability. However, the currently ongoing discussion shows that still no complete agreement has been achieved within the boards with regard to the illustration of a lease agreement on the side of the lessor.

The paper presented here first of all deals with the fundamental proposals for changes concerning the capitalization of leases and with the criticisms of the ED/2010/9 that have been published so far. In addition, the research clarifies that the currently proposed capitalizing for lessors shows the structural weaknesses of the standard draft and problems in its practical implementation. These problems greatly impair the advantages regarding the reduction of the off-balance sheet accounting.

The desired changes proposed in the standard draft in its present form lead to the danger of unnecessary puffing of the balance sheet and to the inclusion of contradictory profits and losses.

The objective of the dissertation is to analyze the decision usefulness for the financial reporting of business entities by following the International GAAP, the

US GAAP and HGB regarding lease agreements, and the significance of the economic approach (“substance over form”). In this context the need for reforms of the currently valid reporting system of lease agreements has to be examined and the current status of the IASB/FASB lease project will be recognized. The current conceptual bases of reporting lease payments in accordance with the International GAAP, the US GAAP and HGB and the concepts discussed as alternatives will be the focus of this research. Based on the various conceptual approaches, concrete steps for reforms will be discussed. Since the application-oriented concretization of the financial reporting of lease contracts will not be analyzed for individual cases, some special features will not be discussed in the complete way, e.g. leasing companies.

The fundamental question will essentially be answered in three stages. At the first stage a benchmark for the evaluation of the currently valid regulations of lease agreements is developed. Special attention will be paid to the analysis of the significance of the economic approach (“substance over form”). The second stage will research the currently valid reporting regulations of lease agreements according to the HGB, the International GAAP and the US GAAP. This will document the need for reforms of the current reporting system of lease agreements. The third stage will recognize the current status of the IASB/FASB leasing projects. In addition, concrete suggestions for the ongoing reform process will be developed.

In Chapters 1, 2, and 3 the currently valid regulations regarding the financial reporting of leases in according to HGB, the International GAAP and the US GAAP are analyzed in the context of their significance regarding the economic approach (“substance over form”) and the related decision usefulness of making decisions by the reporting addressee. Due to the conceptual character of the given research, which is based on the risk and reward approach, the conceptual basis of the current financial reporting of leases has to be looked at. On this basis the financial reporting of the lessor and lessee in connection with the fundamental concept is discussed. The explanations will lead to the analysis of the decision usefulness of the currently valid lease reporting system. In the process, the question whether the currently valid regulations of the financial reporting of leases assure the transmission of decision useful information, or whether reforms are indeed necessary, will be answered. The analysis of the currently valid leases reporting system is the starting point for the discussion of the current IASB/FASB Leasing project in Chapter 4. In this context, first of all, the basis for the current project of the financial components approach and the whole asset approach is presented and evaluated. The decision usefulness of the provided information will serve as the evaluation benchmark. Subsequently, the further development of these financial reporting systems as part of the IASB/FASB lease project and the current intermediate result of the reform project will be appreciated. Research will have to be done on whether the

concepts for the future lease reporting system in the discussion paper will facilitate a better decision useful transmission of information. In addition, suggestions for the increase of the decision usefulness for the future financial reporting of leases are developed.

Acknowledgements

The Author is grateful to Supervisor Professor Lehte Alver for her support, thoughtful comments and useful suggestions. Thanks also to all reviewers, assistants and students who helped me during the studies. Your valuable comments and thoughts were detailed, helpful and very instructive! Finally, special thanks are also extended to my family and friends.

Abbreviations

Abs	(Absatz) – Paragraph
AO	(Abgabenordnung) – General Fiscal Law
Art.	Article / Paragraph
BB	Betriebs-Berater (journal)
Bd	(Band) - Volume of a Book
BewG	(Bewertungsgesetz) – Valuation Tax Act
BFH Court	(Bundesfinanzhof) – Federal Tax Court / Federal Fiscal
BGB	(Bürgerliches Gesetzbuch) – German Civil Code
BStBl	(Bundessteuerblatt) – Federal Tax Gazette
BuW	Betrieb und Wirtschaft (journal)
DB	Der Betrieb (journal)
DP	Discussion Paper
DStR	Deutsches Steuerrecht (journal)
ED	Exposure Draft
ESTG	(Einkommenssteuergesetz) – German Income Tax Law
F	Framework
FASB	Financial Accounting Standards Board
FLF	Finanzierung, Leasing, Factoring (journal)
Fn	Footnote, footer
FR	Finanz Rundschau (journal)
GAAP	Generally Accepted Accounting Principles

GG	(Grundgesetz) – German Basic Law
GMZ	(Grundmietzeit) – Fixed Lease Term
GoB	Generally Accepted German Accounting Principles
HGB	Handelsgesetzbuch (German Commercial Code)
IAS	International Accounting Standard(s)
IASB	International Accounting Standards Board
IFRIC	International Financial Reporting Interpretations Committee
IFRS	International Financial Reporting Standard(s)
IWP	Institut für Wirtschaftsprüfung (journal)
JbFSt	Jahrbuch für Fachanwälte für Steuerrecht (journal)
KoR	Kapitalmarktorientierte Rechnungslegung (journal)
NJW	Neue Juristische Wochenschrift (Zeitschrift)
MLT	Minimum Lease Term
PIR	Praxis der Internationalen Rechnungslegung (journal)
RAO	(Reichsabgabenordnung) – General Fiscal Law
RFH	(Reichs Finanzhof) – Reichs Finance Court
RIW	Recht der Internationalen Wirtschaft (journal)
RWZ	Zeitschrift für Recht und Rechnungswesen (journal)
SFAS	Statement of Financial Accounting Standards
SIC	Standing Interpretations Committee
StbjB	Steuerberater-Jahrbuch (journal)
SL	Service Life

StuB	Steuern und Bilanzen (journal)
StuW	Steuer und Wirtschaft (journal)
SULB	(Saarländische Universitäts- und Landesbibliothek) (library)
TA	(Teilamortisation) – Partial Amortization
US GAAP	United States Generally Accepted Accounting Principles
UuLB	(Universitäts- und Landesbibliothek) – University Library
VA	(Vollamortisation) – Full Amortization
WiSt	Wirtschaftswissenschaftliches Studium (journal)
WM	Wertpapiermitteilungen (journal)
WPg	Die Wirtschaftsprüfung (journal)
ZfgK	Zeitschrift für das gesamte Kreditwesen (journal)

List of Tables

Table 1 List of the German Decrees of Leases by the Federal Ministry of Finance

Table 2 Some Short Definitions/explanations of the Term “Capital Lease”

Table 3 Overview of the Most Important Changes of the ED/2010/9 in Comparison to DP/2009/1

Table 4 Overview of Capitalization by the Lessee

Table 5 Overview of Capitalization by the Lessor According to the Performance-obligation Approach

Table 6 Calculations for Expected Series of Payments

Table 7 Overview of Capitalization by the Lessor According to the De-recognition Approach

List of Figures

Figure 1 Different Meanings of the Term “Economic”

Figure 2 The Position of the Economic Theory of Taxation

Figure 3 The Tasks of the Economic Theory of Taxation

Figure 4 Borderline between the Interpretation of a Matter and a Creation of Law

Figure 5 Areas in Finding of Justice

Figure 6 The Relationship between Economic Ownership and Ownership according to Civil Law

Figure 7 IAS/IFRS Standards that have to be applied to Lease Agreements

Figure 8 Application Scope of the IAS 17

Figure 9 Classification of Lease Contracts according to the IAS 17.10 and 17.11

Figure 10 All or Nothing Approach according to the IAS 17

Figure 11 Chronology of the IASB/FASB Lease Project

1. THE ECONOMIC APPROACH AND THEORETICAL BASIS FOR CAPITALIZATION OF LEASES IN GERMANY

1.1. Concept and Purpose of the Economic Approach

Interpretation of the meaning of “economic approach”. An analysis of the words “to observe” and “approach” shows that these can be understood either as a visual examination or as a kind of an evaluation. To identify the term “approach” specifically and demonstrate the way the observation takes place, a descriptive adjective is needed. When referring to an economic approach, it is obviously “an evaluation, consideration, or examination of an object, with a special emphasis on the economic approach”. However, the term “economic” is not defined precisely. In its general linguistic usage the term “economic” is often used with different intentions and thus carries different meanings (Urbas, 1987, pp. 12–16). Often the terms “economical” or “profitable” are used as synonyms for “economic”, in which case it refers to the “efficiency” or “profitability” of a certain matter (see Figure 1). In such cases the quality of a certain matter is emphasized and highlighted. Additionally, a more specific definition of the term “economic” exists. “Economic” refers also to the industrial field of the economy or to the financial economy.

The necessity of the economic approach. One must not make the mistake of confusing the economic approach with the business perspective, although they are very similar (Beisse, 1981a, p. 3; Böcking, 1994, pp. 19–21). Since this would result in a limitation of the economic approach, it is not permitted (Oldenburger, 2000, p. 78). Besides the business aspects, the economic approach includes other aspects as well, such aspects that are close to the economy and could thus be referred to as economic (Urbas, 1987, p. 39; Beisse, 1981a, p. 4). However, the business perspective fundamentally is part of the economic approach, and therefore is an important, if not the most important, part of the economic approach (Urbas, 1987, pp. 38–40; Beisse, 1981a, p. 4; Beisse, 1981b, p. 136; Groh, 1980, p. 126).

The importance of the economic approach in legal studies is derived from the fact that problems can often be solved only through interdisciplinary cooperation, which means that an adequate solution can only be found by several scientific fields together (Lehmann, 1979, p. 2; Tipke *et al.*, 2002, § 5.65). This is especially true with regard to tax legislation. Without knowledge of other, “alien” scientific fields, it is very difficult to make correct legal decisions and apply the law (Lehmann, 1979, p. 4; Eibelshäuser, 2002, p. 1427; Tipke *et al.*, 2002, § 5.68; Beisse, 1984, p. 9). For example, taxation is not purely a legal problem. The state needs money to finance and execute its tasks. In this context it is the task of the economic approach to provide support regarding the

application of tax legislation (Eibelshäuser, 2002, pp. 1427–1428; Urbas, 1987, p. 204). In order to create fair taxation, economic insights are needed, which in



Figure 1. Different meanings of the term “Economic”

Source: Urbas, 1987, p. 18

turn are gained through the economic approach (Beisse, 1981a, p. 3). Tax legislation mostly uses definitions which are derived from civil law. To guarantee a fair tax system, these definitions have to be interpreted with the help of the economic approach (Eibelshäuser, 2002, p. 1429; Larenz, 1979, pp. 298–307; Tipke *et al.*, 2002, § 5.68–70; Schmidt-Liebig, 1986, p. 129). Consequently, in tax legislation the evaluation of circumstances and proper interpretation of the law are important (Moxter, 1999, p. 40; Beisse, 1988, p. 41). For both, the application of the economic approach is necessary since legal knowledge alone is not enough to evaluate and pass judgment (Urbas, 1987, pp. 42–48; Tipke *et al.*, 2002, § 5.65).

Urbas emphasizes: “The point is not to award economic insights in tax legislation solely to decisiveness, but to assure that economic insights will be considered in the form of a criterion in the administration of justice” (Urbas, 1987, p. 50). Both the legislative and judiciary must know and consider the legal and economic consequences of their actions. Otherwise we could talk about a “monocular” observation model” (*Ibid*, 1987, pp. 48–52).

The task and objective of the economic approach. Since most legal problems cannot be seen as one-dimensional but must be seen as multi-dimensional, the jurisdiction can fulfill its tasks only on an interdisciplinary basis. This means that the “fundamental dependence of legal decisions on insights from other scientific fields has to be accepted” (Lehmann, 1979, p. 2). The economic approach should help one to understand, evaluate and interpret the terms and circumstances used in the laws and standards. These laws and standards have been developed mostly by civil law and in case of need, developed further (Eibelshäuser, 2002, p. 1429; Larenz, 1979, pp. 298–307; Tipke *et al.*, 2002, § 5.68–70; Schmidt-Liebig, 1986, p. 129). The fundamental task is the compilation, evaluation and interpretation of the economic meaning and purpose of laws (Beisse, 1981a, pp. 1–2; Oldenburger, 2000, p. 20; Reifner, 2005, p. 493).

The task of the economic approach with regard to tax legislation is to gain insights from the field of business economics useable for tax legislation and thus act like a bridge between the jurisprudence and economic sciences (Groh, 1989, p. 227; Urbas, 1987, p. 52). This bridge or link represents the so called economic theory of taxation. Figure 2 illustrates its role as a “mediator” between business economics and tax legislation (Urbas, 1987, pp. 56–58).

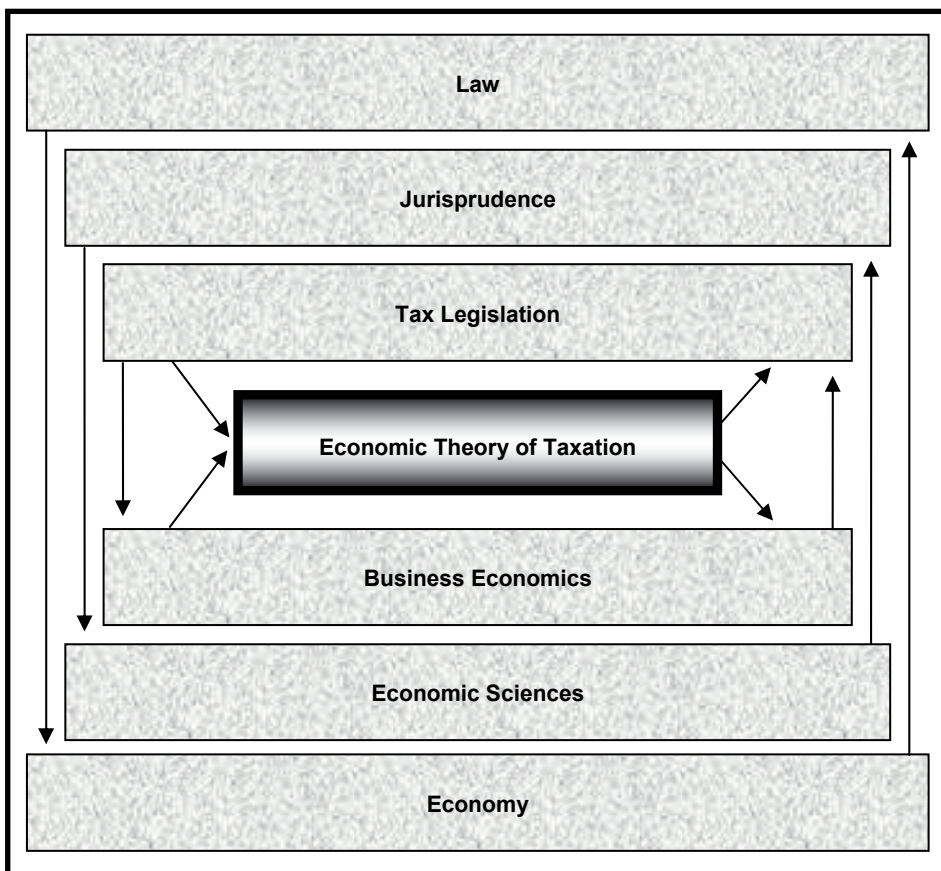


Figure 2. The position of the economic theory of taxation

Source: Urbas, 1987, p. 56

One of the tasks of the economic theory of taxation is to make the insights of the adjacent sciences – economic sciences and jurisprudence – usable to each other (Eibelshäuser, 2002, p. 1427; Urbas, 1987, p. 58). “Tax laws have the primary goal of compiling comparable economic processes regardless of their legal and technical appearance. With their factual description they want to identify the economic and real processes and conditions, and consequently create the fundamental condition of equal taxation.” (Eibelshäuser, 2002, p. 1430; Schmidt-Liebig, 1986, p. 130). As Figure 3 shows, the tasks of the economic tax theory can be split into two areas, namely the tax impact theory and the tax formation theory. The tax impact theory describes the implementation of laws in economically relevant factors, which means that the effects of taxation and tax laws are quantified. “To influence the formation and application of tax legislation norms” (Urbas, 1987, p. 59), by transforming economic conditions into laws is the task of the tax formation theory (*Ibid*, pp. 58–64).

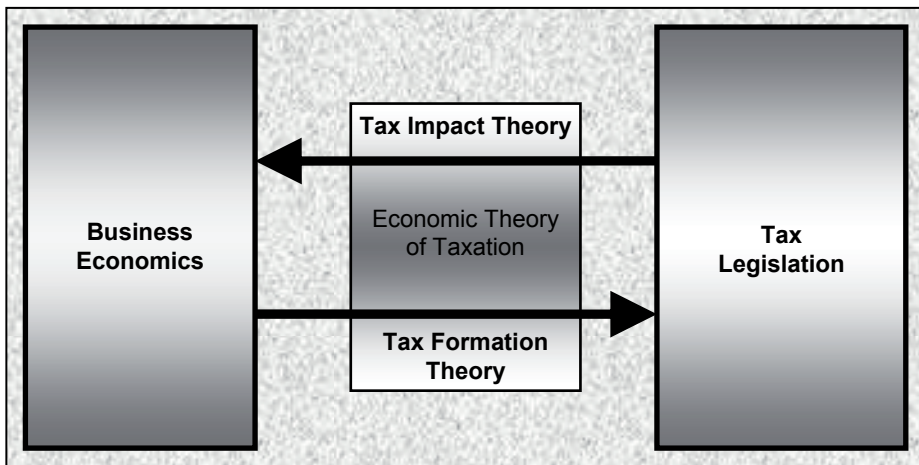


Figure 3. The Tasks of the Economic Theory of Taxation

Source: Urbas, 1987, p. 60

It fulfills this task by analyzing and researching quantitative models to find out which effects changes of laws will have on taxation. The result of these models and research will enable the economic theory of taxation to make recommendations and to answer open questions (Urbas, 1987, pp. 60–61). The purpose of the economic approach, namely the proper application of laws by including economic insights, corresponds with the task of the tax formation theory to help with the creation of norms (Eibelshäuser, 2002, p. 1429; Urbas, 1987, p. 64). “Therefore the economic theory of taxation and the economic approach are inseparably connected with each other.” (Urbas, 1987, p. 64)

The economic approach application is intended to help change and improve those tax norms, which do not concur with the economic principles (Eibelshäuser, 2002, p. 1429; Urbas, 1987, p. 65). In this case it is referred to as the “creation of norms” by the economic approach, because certain tax laws and their interpretations are economically shaped (Urbas, 1987, p. 65). The point is to identify the person who has the economic benefit from a certain asset – to whom the asset is capitalized. The purpose of the economic approach therefore is to act as a fundamental “corrective of tax legislation”, which not only helps with the creation of laws and norms and influences them economically, but also serves as an important tool in the interpretation and application of the law (*Ibid*, 1987, p. 66).

1.2. Historic Development of the Economic Approach

Formation and boom years of the economic approach. The economic approach was first mentioned in the Roman Empire (Urbas, 1987, p. 115; Friedländer, 1956, p. 1049; Becker, 1930, p. 48, p. 79). In the German law, especially in §§ 278–279 HGB of 1861, the first provisions in reference to the economic approach appear, some of which have been literally adapted into the laws of today (Eibelschäuser, 2002, p. 1428). § 278 HGB (from 1861) dealt with the interpretation of merchandising businesses and emphasized and paid attention to the “truly intended” and the “will of the contenders” (Urbas, 1987, p. 116). § 279 HGB (from 1861) has been literally adapted to contemporary § 346 HGB and values objective intention more than subjective will (*Ibid*, 1987, pp. 116–117; Hedemann, 1929, p. 5). Courts have accepted and integrated more and more frequently the practices and more of commerce into their assessments of circumstances and decisions. Consequently, courts have accepted them into the administration of justice (Urbas, 1987, p. 117; Hedemann, 1929, p. 6). However, the authors of the RAO of 1919 understood already then, “that the fundamental principle did not contain what was not already predetermined by the administration of justice, but independently from the expression of the law, has been accepted authoritatively by the practice of law” (Werndl, 1983, p. 49). The codification of the economic approach intended to clarify its significance and necessity and its important role as an interpretation rule (Werndl, 1983, p. 50). Until 1919 tax legislation was mostly administered as part of the civil law. Both the Prussian Administrative Appeals Tribunal and the Supreme Court of the German Reich dealt with tax matters exclusively based on civil law (Ball, 1924, p. 32, p. 71; Mayer, 2003, p. 13). However, in 1919 Enno Becker succeeded with the standardization of the economic approach, which resulted in the separation of tax legislation from the civil law (Beisse, 1981a, p. 4; Groh, 1989, pp. 229–230). This standardization in § 4 RAO reads like this:

“When tax legislation is interpreted, its purpose, its economic significance, and the development of the circumstances have to be taken into consideration.”

With this general fiscal law, a new era for the administration of justice with regard to taxes began (Cordes, 1971, p. 27). These new rules meant that judges no longer had to follow just strictly the “letter of the law”, but could deliver more flexible judgments and decisions guided more by the economic reality (Urbas, 1987, p. 126; Tipke *et al.*, 2002, § 5.66). Based on this, the theory of the economic approach gradually evolved (Cordes, 1971, p. 47). This codification of the economic approach is considered a victory of the jurisprudence of interest over the jurisprudence of definitions (Mayer, 2003, p. 13; Eibelschäuser, 2002, p. 1430; Groh, 1989, p. 227). The jurisprudence of interests assesses the purpose and the intentions of the law higher than the positivistic application of the law

that strictly follows the letter of the law, which is typical for the jurisprudence of definition (Tipke *et al.*, 2002, § 5.48). Preference is given to the teleological interpretation method (Mayer, 2003, p. 13). The separation of tax legislation from the civil law and its independent standing happened mostly due to Becker. The economic approach had finally been accepted as the basis for interpretation and became a part of the administration of justice in the RFH (Urbas, 1987, pp. 129–130; Ebert, 1955, p. 32).

The crisis of the economic approach. Beginning from the middle of the 1950s, criticism, which had been there from the very beginning at least latently, of the independence of tax legislation developed (Beisse, 1981a, p. 4). Critics deplored the isolation of tax legislation and demanded that tax laws should be merged with other legal fields (Urbas, 1987, p. 142; Beisse, 1981a, p. 5). The main point of criticism was the economic approach, which was then applied less and less as a result of the criticism. Under the cover of the economic approach, judgments were pronounced more and more frequently resulting in unacceptable and erroneous results on the basis of an over-emphasis of the economic purpose and interpretation of the law. Thus, criticism was justified (Ebert, 1955, p. 34; Urbas, 1987, pp. 130–133, p. 153; Hedemann, 1929, pp. 130). The criticism led to a stronger “unifying effect within the legal system” and in the interest of legal certainty the economic approach was pushed to the back. More emphasis was placed on the strict interpretation of terms in accordance with civil law definitions (Beisse, 1981a, pp. 5–6; Tipke *et al.*, 2002, § 5.29). This new and low appreciation of the economic approach, which reached its lowest at the beginning of the 1960s, was manifested in numerous judgments and commentaries. Consequently, the dominating role of the civil law in relation to the tax law became very obvious (“Primate of Civil Law”) (Grimm, 1978, pp. 283–286; Oldenburger, 2000, p. 20; Tipke *et al.*, 2002, § 5.67). The civil-legal perspective had replaced the economic approach and prevailed again (Urbas, 1987, pp. 142–148).

Renewal of the economic approach. With the decision of November 11, 1964, however, the Federal Constitutional Court reaffirmed the independence of the tax legislation and the significance of the economic approach, which in certain cases has to be preferred to the civil law viewpoint (Beisse, 1981a, pp. 5–6). As a consequence of the decisions made in 1964 and 1969, the economic approach was again considered and applied more frequently. The reason for this lies to a large extent with the further development of the judicial methodology (Urbas, 1987, pp. 149–151; Beisse, 1981a, p. 5).

On January 1, 1977, the General Fiscal Law (AO 1977) came into force. It replaced the General Fiscal Law of the Reich, which had been in effect until then and did not contain any specific rules regarding the economic approach anymore since the committee considered them as expendable (Eibelshäuser, 2002, p.

1428; Groh, 1989, p. 230). “The reason for the reform was the intention to harmonize the rules with the administrative procedures act, to find a reasonable balance between the opposing principles of equality of taxation and the legal certainty, and to improve the systematic of the law”. From this point onward the legislative approach did not see a reason anymore for the legal entrenchment of the economic approach since it was now generally accepted as an interpretation in the tax law (Mayer, 2003, p. 15). Therefore no substantial changes appeared through the omission of the codification of the economic approach (Beisse, 1981a, p. 11).

In the HGB the economic approach is not explicitly codified, but derived from the principle of integrity (§ 246, Art. 1 HGB) and firmly anchored as a rule of interpretation (Tipke *et al.*, 2002, § 5.65). The codification was no longer necessary, because the economic interpretation of circumstances is now generally accepted, which was not the case before (Eibelshäuser, 2002, p. 1428). However, new rules were included in the §§ 39–42 AO, which are considered as special cases of an economic approach (Mayer, 2003, p. 15; Tipke *et al.*, 2002, § 5.84–113). “The fact that the economic approach is widely considered identical with the tax law is to a large extent due to the fact that until 1977 an instruction regarding the interpretation was specifically regulated, while such regulations outside the tax law were and are absent” (Eibelshäuser, 2002, p. 1428).

Conclusions to economic approach. During the last century enormous changes in the administration of justice regarding taxation took place. At the beginning the laws were interpreted rather positivistically and strictly based on the wording of the law, but later on the economic intention during the legal formation was taken into consideration to an increasingly greater extent. Then the gradual separation of the tax legislation from the civil law followed, and the jurisprudence of interest won over the jurisprudence of definition (Urbas, 1987, p. 152; Eibelshäuser, 2002, p. 1430; Beisse, 1981a, pp. 3–4; Tipke, 1986, p. 5; Moxter, 2000, pp. 2147–2149).

In the year 1919, the economic approach was codified by Enno Becker in § 4 AO (Eibelshäuser, 2002, p. 1428; Beisse, 1981a, pp. 4–5). Gradually, the use of the economic approach and the orientation to economic conditions became more and more accepted in practice. However, the excessive application of the economic approach and the violation of interpretational limits led to strong criticism after a few years, and a dispute over methods followed (Urbas, 1987, p. 153). This was followed by a renaissance of the civic-legal perspective and a re-orientation to the civil law, which provided more legal certainty than the too flexible economic approach, which in many people’s view was a borderline in its interpretation (Beisse, 1981a, p. 4). But at the end of the 1960s the trend changed once again. The economic approach was integrated again into the

methodology and considered more in the administration of justice (Urbas, 1987, pp. 150–153; Tipke *et al.*, 2002, § 5.68). But the AO (General Fiscal Law) of 1977 did not contain any explicit regulations because the committee considered it dispensable and did not see a reason for a legal inclusion of the economic approach since it had already been generally accepted as a fiscal interpretation rule (Mayer, 2003, p. 15; Eibelshäuser, 2002, p. 1428; Beisse, 1981a, p. 11; Groh, 1989, p. 230). According to the commercial law, the principle of the economic approach, together with the principles of objectivity and of timeliness, is part of the basic framework principles which apply to the financial reporting tasks (Moxter, 2003, p. 15).

The use of the economic approach brought curses as well as blessings. On the one hand it “served as support for any argument”, and on the other hand, it appeared to “make explanations dispensable and rebuttals hopeless” (Urbas, 1987, preface). However, it was already clear that some legal problems would only be solved with the help of the economic approach (Urbas, 1987, p. 117; Beisse, 1981a, p. 5). “A flexible interpretation, which can be adapted to economic facts, is desirable. But it also opens – as the past has shown – the possibility of conflicts with regards to the overstepping of interpretational limits, and thus can result in the unacceptable creation of justice by a judge” (Urbas, 1987, p. 154). From the historical view it is clear that problems with the economic approach are closely connected with the relationship a judge has with the law (Beisse, 1981a, p. 5).

1.3. Classification of the Economic Approach within the Judicial Methodology

1.3.1. Relationship between the Economic and Legal Perspective

Urbas understands the legal perspective as the “assessment, consideration or research that is focused on the item/thing, with special attention given to the legal aspect, or from a legal perspective” (Urbas, 1987, p. 34). Special attention given to the legal aspect is identified by the user’s knowledge of all applicable legal rules and laws, and by paying attention to them and using them correctly (*Ibid*, 1987, p. 35). Further important aspects of the economic approach are embodied by the investigation of, implementation of and compliance with what is legally desired or the purpose of the law respectively, which will result in legal peace. An appropriate definition of the economic approach does not exist within tax legislation since a legal perspective can only be applied in other, non-legal fields (Böcking, 1994, pp. 22–24; Rittner, 1975, p. 17, p. 47). Thus, while a legal perspective can exist for example in the economy, in the medical or technical fields, it cannot exist within the law/justice itself. The same applies to the economic approach (Urbas, 1987, p. 36).

Therefore the relationship between the economic and legal perspectives is interpreted very differently. Some authors emphasize the legally shaped understanding of the economic approach and the close link of both perspectives (Urbas, 1987, p. 37; Beisse, 1981a, p. 2; Beisse, 1972, p. 94; Moxter, 1989, pp. 240–241; Beisse, 1984, p. 12), while other authors consider them as opposites (Urbas, 1987, pp. 36–37; Böcking, 1994, pp. 25–26; Behr, 2002, p. 35).

1.3.2. Interpretation of the Economic Approach within Jurisprudence

From the legal viewpoint the economic approach is understood as a way of observation to identify the economic implications, meaning and purpose of the law (Kühn, 1968, p. 787; Barske, 1976, p. 2943; Beisse, 1984, p. 12). Often the economic scope and the economic presentation of facts were also discussed (Urbas, 1987, pp. 19–20).

“However, legal actions – in the same way as economic actions – are part of certain holistic actions and therefore the application of the law is influenced by criteria from other action categories. Regarding tax legislation this is especially true for the influence from economic action criteria” (*Ibid*, 1987, p. 30). Therefore the economic approach gives special consideration to the economic action category. Stüdemann defines the economic approach as the evaluation of the application of tax legislation with a special consideration to the satisfaction of the needs that are focused on it (Stüdemann, 1984, p. 548).

For the definition of the economic approach according to Beisse it is especially the interpretation of the terms used in the law and the identification of what is economically desired that matters (Beisse, 1984, p. 12; Schmidt-Liebig, 1986, p. 131). The economic reality and the so called meaning and purpose of legal norms must be understood and developed further (Beisse, 1981a, p. 1; Eibelshäuser, 2002, p. 1429). The economic approach therefore is a form of applying the teleological method of finding justice (Beisse, 1980, p. 637, p. 643; Moxter, 1989, p. 232; 1983, p. 1613; Schmidt-Liebig, 1986, p. 143). From the legal viewpoint, an economic approach should examine the economic significance and facts, that which is actually desired (Böcking, 1997, p. 97; Schmidt-Liebig, 1986, pp. 131–132), examine, expose and interpret a process, and in so doing improve the content of information (Böcking, 1997, p. 100; Moxter, 1989, p. 232).

1.3.3. Instruments for the Legal Interpretation

Preliminary Remark. Since the economic approach poses a fundamental question of interpretation, it must first of all be clarified how laws are interpreted generally. Due to the separation of power, the judge is in a position to apply a

law created by lawmakers and not by the judge himself. Furthermore, laws are abstract and general norms. This means they are valid for an indefinite number of cases and do not specifically determine what is true in one particular case. Therefore the interpretation of the law by a judge is necessary. It must be determined whether a certain case fits into an existing norm or not, and what the consequences will be. Thus, the purpose of the interpretation is the clarification of the meaning and purpose, which is contained in the norm text of the law (Larenz, 1969, p. 292; Moxter, 1989, p. 232; Beisse, 1981a, p. 1). This specification by the judiciary is necessary, because uncertain and abstract terms are used in the legal text (Beisse, 1981a, p. 3; Tipke *et al.*, 2002, § 5.68–70). “Only through its application does the abstract law become concrete (or more concrete) law” (Tipke, 1981, p. 42). In a legal system that is primarily shaped by codifications, the text of the norm – the wording – is the first and most fundamental mean for interpretation. However, the actual norm text is not the same as the extracted legal norm and meaning. Additional aspects of interpretation have to be taken into consideration.

The basic formula of a legal proposition consists of facts and legal consequences (Tipke *et al.*, 2002, § 5.44). “The application of such consequences demands an examination, whether concrete circumstances in life fit with the abstract legal facts of the legal proposition. If the concrete circumstances can be subsumed under the legal facts, then the legal consequences in accordance with the norm will apply” (Tipke, 1981, p. 87; Urbas, 1987, p. 157). This “If (facts) then (legal consequence)” principle can in some cases result in the interpretation of the law that contradicts its own legal text (Urbas, 1987, p. 159; Larenz, 1979, p. 307; Beisse, 1981a, p. 7; Tipke *et al.*, 2002, § 5.52; Reifner, 2005, p. 491). The criterion “literal sense” has even been adapted by the BFH (Tipke, 1979, p. 86; Beisse, 1981a, p. 7). This emphasises once again the importance and necessity of the interpretation of laws. It also shows that good laws always have the need for interpretation (Urbas, 1987, p. 158).

Laws are created for a purpose and are a means to determine the purpose of the law (Tipke, 1981, p. 90; Urbas, 1987, p. 159). An objective of the interpretation of laws is to determine and clarify the purpose and meaning of laws and consequently enable their correct application and the predictability of fiscal laws (Beisse, 1981a, p. 7; Böcking, 1994, p. 26; Tipke *et al.*, 2002, § 5.50; Moxter, 1989, p. 232). The meaning of the terms used in laws is subject to change in the course of time, therefore it is never conclusive and the same forever. It changes with time (Tipke, 1981, p. 93; Urbas, 1987, pp. 159–160). Legal requirements change with time and new legal questions arise. Therefore laws have to be adapted, developed and modified further. If flexible limits between the application and the creation of laws exist, their interpretation must not be overly delayed (Urbas, 1987, p. 161).

A distinction is made between subjective and objective theories in the search for the meaning and purpose of laws. The subjective theory is focused on the purpose, which was predominant at the time when the law was created. The subjective theory tries to provide a certain stability and legal certainty. The objective theory however, searches for an independent and objective purpose of the law, and tries to integrate the changes of time into modified or new laws, e.g. through continued legal education (Urbas, 1987, pp. 159–163; Tipke, 1981, p. 93; Larenz, 1975, p. 303). According to the current opinion, the objective meaning of the law is decisive, because the economic approach should consider in its interpretation of the law the development of circumstances, and not the historical will of the lawmakers (Beisse, 1981a, p. 2). Engisch and Beisse call these insights the “Relativity of Legal Terms” (Engisch, 1977, p. 157, pp. 244–248; Beisse, 1981a, p. 2; Schmidt-Liebig, 1986, p. 130 and p. 143).

The task of judges regarding the interpretation of laws is to consider both theories and decide case by case whether legal certainty or further legal education should be given priority. “Thus, it can be stated that the meaning of the law, which is to be identified through the interpretation, consists of several elements. On the one hand we have the objective element of “the will of the law”, which serves the interests of further legal education, while on the other hand we have the subjective element of the “will of the lawmakers”, which serves the interests of legal certainty” (Urbas, 1987, p. 164; Cornelius, 1968, p. 145). In the context of the economic approach both of these elements are often referred to (Cornelius, 1968, pp. 139–140).

A legally regulated interpretation of the law does not exist. However, in § 20, Art. 3 GG, a close linking with the wording of the law is requested, and in § 133 BGB refers to the actual will of the law, which has to be considered in the interpretation (Larenz, 1975, p. 341; Urbas, 1987, pp. 165–166; Schmidt-Liebig, 1986, pp. 130–131). Therefore everyone who applies norm texts and laws has to find out the actual will of the law and execute it accordingly (Urbas, 1987, p. 166; Beisse, 1984, p. 4).

Methods of Interpretation. To interpret laws properly and/or determine their meaning and purpose, the interpretation should be multi-dimensional, which means the methods should complement each other. Savigny talks of four and Häberle of five equal interpretation methods, for which, however, there is no fixed sequence as to how they are used (Moxter, 1989, p. 240; Urbas, 1987, pp. 168–176). The different interpretation methods are factually linked with each other and therefore should always be applied together (Tipke *et al.*, 2002, § 5.51; Groh, 1989, p. 230). “Those, who think that the interpreter can choose from among the methods, should think about this” (Larenz, 1975, p. 315). The interpretation methods, which complement and support each other, are the following: Grammatical Interpretation, Historical Interpretation, Systematic

Interpretation, and the Teleological Interpretation. Häberle still adds the Legally Comparing Interpretation, which however, is not part of the canon of interpretation methods (Urbas, 1987, pp. 165–168).

Grammatical Interpretation Method. The grammatical interpretation method deals with the wording of a legal text. Not only must the general use of words, be considered with regard to this method, but also the use of special terminology. It can be assumed that lawmakers succeeded in choosing the words, which express most precisely the original intention (Urbas, 1987, p. 169; Tipke, 1981, p. 91; Larenz, 1979, pp. 307–309). However, if some terms in the legal text leave some leeway, the limits of which are not defined clearly, then these terms have to be interpreted. The grammatical interpretation plays a special role in the criminal law. It is constitutionally not permitted to expand the application scope of a norm beyond its actual literal sense at the expense of the offender (prohibition to justify and toughen punishment analogy – prohibition of analogy (Beisse, 1981a, p. 9; Tipke, 1979, p. 36, p. 94)). Often the grammatical interpretation of legal texts is not enough by itself to determine the meaning and purpose of laws clearly.

Historical Interpretation Method. The historical interpretation method attempts to explain the legal text by considering its history of origin. The meaning and purpose of the norm that needs to be interpreted should be as close as possible to the original intentions of the lawmakers (Schmidt-Liebig, 1986, p. 131; Eibelshäuser, 2002, p. 1428; Larenz, 1975, p. 319). The expectation is to understand the original intention of the law. However, it is necessary to agree with Larenz that this method serves only as a support and must be applied with caution, because the search for a unified will of the lawmakers is hard to portray (Larenz, 1975, pp. 315–316). After all, many members from various fractions and parties participate in the law making process, and unfortunately often only very few experts among them actually understand the laws. In general it can be stated that the significance of the historical interpretation decreases as a norm becomes older and more distant from the time of its creation (Urbas, 1987, pp. 171–173; Larenz, 1975, pp. 311–319).

Systematic Interpretation Method. The systematic interpretation is based on the idea that the legal order as a whole has to be without contradictions, and therefore no specific norm can be in contradiction with another one. From this perspective the systematic interpretation method is actually not really an interpretation method, but rather a construction of principles. If one specific legal regulation is seen as part of a system and in the context, the underlying purpose can often be identified through inference because fundamentally a harmonious and logically balanced legal system in itself is assumed (Eibelshäuser, 2002, p. 1429). The systematic interpretation argues on the basis of the position of a norm in the law and the connected norms, quasi in the

context with other legal texts (Tipke *et al.*, 2002, § 5.58). An additional aspect is attributed to the systematic interpretation method, namely that a legal norm in accordance with the systematic interpretation must be used according to the regulation that it is connected with law (Larenz, 1975, pp. 311–312; Eibelshäuser, 2002, p. 1429). Eibelshäuser emphasizes: “Insofar, the whole law, to which the norm belongs, that has to be interpreted or other laws, connected through their content, is used to identify the meaning” (Eibelshäuser, 2002, p. 1429). It is often argued against the systematic interpretation that it is not the essential step to draw the implication from a known but to recognize the systematic as something that is only possible through other interpretation methods.

Teleological Interpretation Method. In the interpretation of norms and laws regarding the accounting law and the tax accounting jurisdiction, economic aspects are evaluated and interpreted by the use of the economic approach (Böcking, 1997, p. 85; Döllerer, 1980, p. 202). On the basis of its meaning and purpose a norm that is observed has to be interpreted and evaluated in such a way that the facts will be economically presented in the correct way. Thus, the meaning and purpose of a norm can only be identified through a process of factual and logical evaluation. The economic approach is receding to the jurisprudence of interests, a teleological (purpose-oriented) interpretation method and therefore shapes the finding of justice as well as the application of the law (Lorenz, 2002, p. 22; Urbas, 1987, p. 190; Beisse, 1981a, p. 2; Döllerer, 1980, p. 195.; Eibelshäuser, 2002, p. 1426; Schneider, 1983, p. 143.; Böcking, 1997, p. 87). It is also a legal perspective because for reasons of legal certainty formal legal aspects cannot be waived (Moxter, 1999, p. 8). Since it is a legal perspective, it is therefore independent from economic-scientific theories (Beisse, 1984, p. 11; Eibelshäuser, 2002, p. 1427; Moxter, 2000, p. 2146).

The teleological interpretation is often seen as the central part of interpretation methods and in cases of doubt it might therefore dip the scale (Beisse, 1981a, p. 1–3). It requests to examine the law as to which meaning and purpose should be achieved with a certain norm (Oldenburger, 2000, p. 78; Urbas, 1987, p. 190; Moxter, 1989, p. 241). In doing so, it does not refer to the will of the lawmaker as a subjective interpretation, but the objective purpose expressed in the norm. This purpose might have changed with older norms in the course of time (Beisse, 1981b, p. 135). The objective meaning of legal norms conforms to the changing and real actuality and the value judgments in a society (Beisse, 1981a, p. 2; Larenz, 1975, p. 139). Therefore it depends on the purpose and the meaning of accounting as to what extent the formal and legal aspects can be repressed. However, this must be in conformity with the required objectification of the balance sheets (Lorenz, 2002, p. 1). If the law does not define the information obligations sufficiently, they must be developed by the administration of justice with the help of the economic approach, which is derived from the general

methodology of legal sciences (Beisse, 1981a, p. 7; Lorenz, 2002, p. 26). Whether the meaning and purpose of a norm can be discovered through the economic approach and whether it is the appropriate tool, will eventually be decided by the “value of the result” (Beisse, 1981b, p. 139).

1.3.4. The Limit of Law Interpretation

When interpreting laws and norms, it is important to recognize that there are limits. These limits will be transgressed as soon as the literal sense of the legal text or norm is unduly expanded and not interpreted in its narrow sense (see Figure 4). In such case we do not refer any longer to an interpretation but consider it as creation of law (Larenz, 1975, pp. 309–310; Urbas, 1987, p. 179). However, it is problematic to draw an exact line or define exactly from which point the sense of the word is unduly interpreted (Urbas, 1987, pp. 176–177).

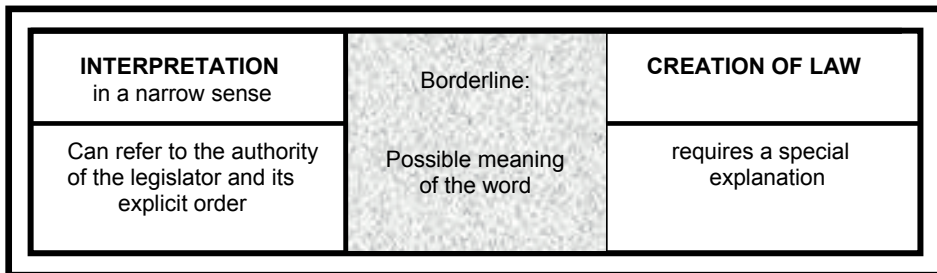


Figure 4. Borderline between the Interpretation of a Matter and a Creation of Law
Source: Urbas, 1987, p. 179

The judge can make an independent and autonomous decision, where the possible literal sense of a word is overstepped. Although the possible literal sense of the word cannot be defined exactly, but with the help of interpretational components it can be ascertained (Tipke *et al.*, 2002, § 5.52–53; Urbas, 1987, p. 183). In cases where the interpretation has gone beyond the legal text and/or the literal sense of the word, a specific justification must be given. In this regard, the economic approach has been seen as such in many BFH-judgments (Canaris, 1964, p. 20; Urbas, 1987, p. 179, p. 183). The creation of law itself can be divided into two areas. Generally, “filling gaps in the law” or the “development of the law” lies within the authority of a judge as part of finding justice. However, the expansion of laws is always prohibited (Urbas, 1987, pp. 180–181; Beisse, 1981a, p. 7; Tipke *et al.*, 2002, § 5.71–79; Schneider, 1983, p. 145). Filling in a gap – in contrast to recognizing a gap – beyond the interpretation is already considered as an amendment of the law. This means that “everything beyond the interpretation in the broader sense constitutes a prohibited creation of law, because it intrudes into area free from law” (Urbas, 1987, pp. 181–182). Figure 5 illustrates the distinction between interpretation in the broader sense and the creation of law.

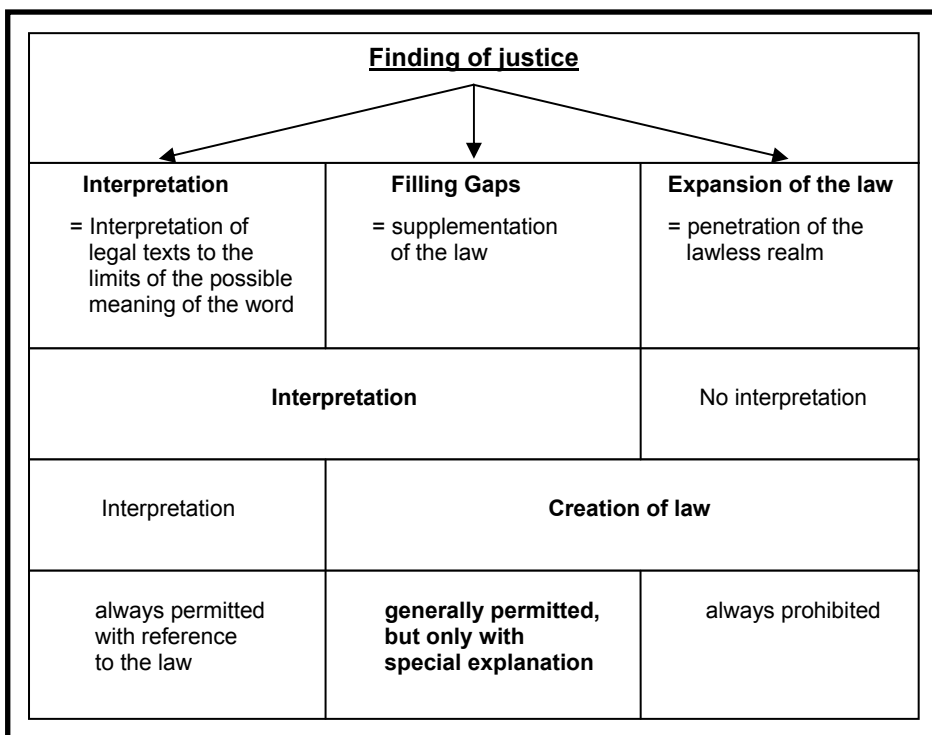


Figure 5. Areas in Finding of Justice

Source: Urbas, 1987, p. 182

That area of finding justice where a special justification and explanation is needed, namely the area where interpretation and creation of new laws overlap, has until now often been explained and decided with the economic approach (Beisse, 1981a, p. 8). With that, a certain problem comes because it is not the task of the economic approach to justify and legalize improper finding of justice by overstepping the border towards the unauthorized creation of law, and then argue and justify this with the economic approach. This has happened in the past on various occasions (Urbas, 1987, pp. 182–185). This shows again that the interpretation of laws with the help of the economic approach also has to observe “interpretation limits as to the possible literal sense of the word” (Urbas, 1987, p. 185; Beisse, 1981a, p. 8).

1.4. Application of the Economic Approach

Economic Ownership and Ownership by Civil Law. To make distinction between economic ownership and ownership by civil law, it is necessary first to clarify the meaning of the term “ownership”, and then the relationship that exists with the “economic ownership” (Urbas, 1987, p. 216; Werndl, 1983, p. 13; Moxter, 1989, p. 237). According to § 903 BGB, the owner of an object/thing

can decide freely and exclude others from interfering, as long as the law or the rights of third parties are not affected by it. “Contrary to “economic ownership” and to the ownership guarantee according to Article 14 GG (German Basic Law), which refers to asset rights or commodities, the definition of ownership in the BGB refers only to physical objects/things” (Urbas, 1987, p. 217).

Ownership, in contrast to other material controlling rights, constitutes a total and unlimited rule of law. The two un-codified elements of ownership are therefore the rule of law of objects and the right of exclusion, which are also identified as positive and negative right to property. Which of these two elements is the more important one is disputed even among experts. For example, supporters of the right to the rule of law over objects consider the disposal over the benefits of a commodity as the decisive criterion. Others consider the right of exclusion, due to the negative obligation, as more important (Moxter, 1989, p. 237; Urbas, 1987, pp. 216–221).

Now, if the owner transfers the right of use for a certain time period to another person, then the right of use superimposes his own right to property, although the legal ownership still remains with the owner. Contrary to the owner, who has the legal and factual right of disposal over the object and can use, utilize and consume it, the rights of the material beneficiary are limited. The status of ownership does not change, only the rights to property of the owner are restricted for a certain time period. In this case we are talking about the transfer of a restricted material right to the rule of law. In the case of an assignment, such as security, beneficial use, title retention, trust ownership, or in the case of leasing, the economic owner has a restricted material claim power and can therefore use the item, contrary to the legal owner, and gain economic benefit from it (Kusssmaul, 1987, pp. 4–12, p. 160; Urbas, 1987, pp. 222–224).

The term of economic ownership is not clearly defined in the German law (Mellwig *et al.*, 1996, pp. 2345; Werndl, 1983, pp. 28–30; Sabel, 2006, p. 29). The term is often criticized also because it is in itself a contradictory catchphrase. However, current opinions do not see the need for a change or transliteration of the term because it has become established and its characterization is generally considered appropriate (Urbas, 1987, pp. 224–228; Werndl, 1983, p. 2).

Economic Ownership as Attribution Rule in Commercial Law. According to the §§ 238 HGB, every merchant has to, for the purpose of providing information and as an assessment for payments, declare in his balance sheets and balance his personal claims and debts (Bitz *et al.*, 2003, p. 120), his money in cash, and all other assets in his ownership, which are in accordance with the GoB partly codified and partly un-codified (Sabel, 2006, p. 29; Kusssmaul, 1987, p. 29; Oldenburger, 2000, p. 79; Riedel-Stegner, 2006, p. 18). The term

“ownership” is not defined here for the reason that ownership according to civil law alone is not decisive. The fiscal classification of assets and the evaluation of economic ownership are specifically dealt with in § 39 AO. This regulation is considered as an expression of the economic approach (Mayer, 2003, p. 8). According to § 39 Abs. 1 AO, commodities are classified to ownership according to civil law as a matter of principle. However, if a third party exercises the rule of law over the asset, then – in accordance with § 39 Abs. 2 AO – it has to be attributed to this third party (Urbas, 1987, p. 228 and p. 238; Sabel, 2006, pp. 29–30; Eibelshäuser, 2002, p. 1431; Beisse, 1984, p. 12). The current opinion assumes that economic ownership in commercial law and in fiscal law are in line, and therefore § 39 AO for the commercial and legal classification of assets (Moxter, 1999, p. 39; Urbas, 1987, p. 238). Due to the principle of decisiveness the classification according to commercial law is compulsory with regard to the tax balance sheet (Knobbe-Keug, 1993, p. 76; Urbas, 1987, p. 238; Oldenburger, 2000, p. 111). Consequently, it is clearly the economic ownership and not the ownership according to civil law which matters. It is the actually exercised control over the asset, which decides its classification. However, the overall condition of circumstances is always taken into consideration as well (Urbas, 1987, pp. 230–231; Eibelshäuser, 2002, p. 1431; Sabel, 2006, p. 30). As soon as the legal owner ceases to have influence on his property, the asset is classified by the economic owner (Mayer, 2003, p. 153). The question as to whether an asset has to be included in the balance sheet can be answered only on the basis of economic criteria and with the help of the economic approach (Urbas, 1987, p. 232; Eibelshäuser, 2002, p. 1431; Mayer, 2003, p. 153). Urbas has emphasized: “Thus, the question of “ownership” becomes irrelevant. It may have some role regarding formal matters, but not in the context of the logic of the law” (Urbas, 1987, p. 231).

According to the basic thought of the economic approach the decisive criterion is who benefits from the economic asset and who uses the asset in which way (Mayer, 2003, p. 153). An additional criterion must be considered when the economic approach is applied: not only opportunities and risks, but also the authority to decide must be transferred¹ (Sabel, 2006, p. 31; Mellwig *et al.*, 1996, p. 2347). “If the opportunity to use asset and the legal ownership of an asset belong to two different subjects, the question of allocation of the economic ownership can be decided with the help of the commercial law and by using the evaluation process of risk-opportunity approach” (Sabel, 2006, p. 31).

For capitalization of property assets according to commercial law, the economic, not the legal relationship, is relevant in the balance sheet (Urbas, 1987, p. 240; Beisse, 1981a, p. 6; Oldenburger, 2000, p. 22; Döllerer, 1971, p. 536). Nevertheless, in every case both individual and case-specific research studies

¹ This is in line with the position of the IAS 17.

have to be made in order to clarify who must capitalize the economic asset. Therefore, ownership according to civil law and economic ownership have to be kept separate with regard to the capitalization (Oldenburger, 2000, p. 19). In the case of leasing one of the problems is that a decision has to be made in advance regarding who will have to report the leased item in the balance sheet (Urbas, 1987, pp. 233–234, p. 240).

Examples. To illustrate the aforementioned problematic situations in application of the economic approach the following cases are analyzed. In the so called Tomberger-case the question was, whether an in-phase receipt of dividends, with existing majority shares and exerting influence on the use of profit, was permissible (Blaum *et al.*, 2000, p. 1233). The Advocate General, Tesauero of the High Senate disagreed with this thesis. Following the civil law and/or a purely formal legal observation, he saw a violation of the basic principle of the appropriate realization of profits on the day of the financial report, and a violation of the basic principle of the proper periodical allocation (Böcking, 1997, p. 92; Eibelshäuser, 2002, p. 1431). This explanation was criticized by the German Government as too restrictive and formalistic. Whether the capitalization requirement applies to an asset depends first of all on, at least from an economic viewpoint, whether the object is part of the economic assets of an enterprise. The deciding criterion is not who has the economic ownership but to whom the economic ownership is classified and whether the item is identified as an asset (*Ibid*, p. 93). “Insofar the economic perspective has priority over the decisiveness of the civil law” (Böcking, 1994, p. 5).

The example 2 is connected with the usage of the economic approach or it is so called “pharmacist-case”. A pharmacist rented an apartment for €2000 per month, and then sublet the apartment to a medical doctor for only €1000 (Böcking 1997, p. 96). From the sublease he had to expect a monthly loss of €1000. Formally and legally an accrual for the expected loss could have been set up (*Ibid*, p. 97). However, from the economic viewpoint the whole setup of circumstances and the economic intention are considered (Moxter, 1993, p. 2484). In doing so, the location advantage has to be contrasted by the impending losses from the sublease. In the opinion of Moxter, such an accrual for the expected losses would constitute a “gross distortion of meaningful contents in the balance sheet” (Moxter, 1993, p. 2482) and therefore has to be rejected (Böcking, 1997, p. 99). The High Senate of the BFH decided in this case that an accrual for impending losses could not be explained sufficiently. From an economic viewpoint, the advantages and disadvantages of this business have to be seen as one unit. From the economic viewpoint, the equivalence of the payments is assumed (Urbas, 1987, pp. 96–102).

It is obvious that fundamentally the overall economic observation is taken into account and not only the assessment of individual contracts and facts, or the title

of these contracts (Kümpel *et al.*, 2006, p. 3, p. 10; Sabel, 2006, p. 55, p. 57; Weiss, 2006, p. 55; Esser, 2005, p. 429). Also in cases of interconnected businesses the intentions have to be identified. A narrow legalistic view would not do justice to the facts and would untie the “contract package” (Esser, 2005, p. 497 and 507). A legal splitting of economic facts, which are in an economic interdependence and serve a common purpose, is therefore not permitted. From an economic viewpoint, one contract would not be concluded without the other (Reifner, 2005, pp. 496–497, p. 500). The decision of the BFH of February 9, 2006 can be considered a confirmation of the previous statement (treatment regarding the value added tax of the sale and lease back procedure), in which it was stated unambiguously that in the presented sale and lease back case the provision of the authority to dispose was lacking. No leasing object was delivered and therefore no substance, value and profits were transferred. Furthermore, the “overall circumstances” had to be considered and the contracts had to be considered as a “legal and economic unit”, and “on the basis of the interests of both parties they would not have been concluded without the other” (Bünnig, 2006, pp. 1668–1671; Reifner, 2005, p. 497).

Interim summary. The economic approach is especially significant in the fiscal classification of assets. A reason for using of economic approach for the classification of assets is based on the idea that taxes should be distributed equally and fairly, based on the individual productivity, and should not be tied to the possession of such assets only (Eibelshäuser, 2002, p. 1430; Tipke *et al.*, 2002, p. 74, p. 133; Moxter, 1983, p. 300). Therefore, the one who benefits from the economic ownership will pay the taxes. Taxation must therefore be focused on the economic ownership and not on the narrow legalistic ownership because according to tax legislation only the one who receives the economic benefit from the asset should be taxed, not the one whom the asset legally belongs to (Mayer, 2003, p. 18; Seeliger, 1962, p. 1; Urbas, 1987, pp. 278–284; Sabel, 2006, pp. 29–32). The author of the dissertation agrees with Mayer and Böcking, who have noted that from this perspective the decisiveness principle meets the limits where commercial-legal principles of proper bookkeeping oppose the purpose of the fiscal capitalization. This is particularly true with the principle of caution, which is responsible for the different forms of ownership in commercial and tax laws (Mayer, 2003, p. 64; Böcking, 1997, p. 87). Classification of assets in relation to commercial law corresponds with the classification of economic assets in accordance with § 39 AO, whereby unlawfully acquired control, e.g. theft, constitutes an exception (Mayer, 2003, p. 153).

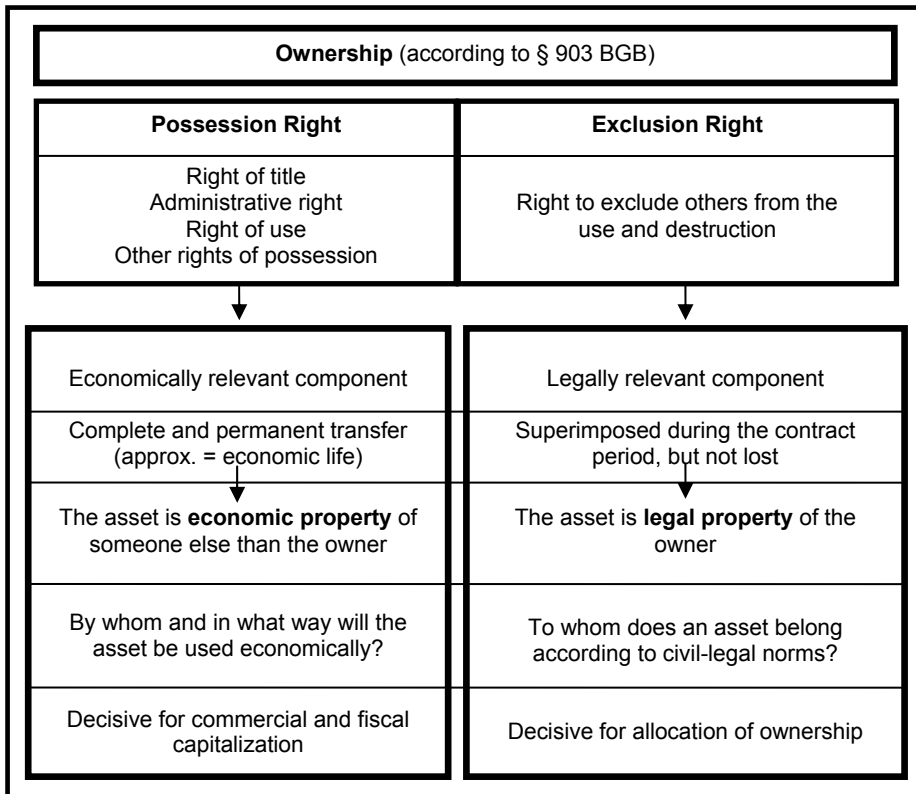


Figure 6. The Relationship between Economic Ownership and Ownership according to Civil Law

Source: Urbas, 1987, p. 246

Characteristics of ownership are the possession right and the right of exclusion (see Figure 6). The possession right constitutes the economically relevant component and the right of exclusion constitutes the legally relevant component (Bordewin *et al*, 2003, p. 29). For the possession right the criterion of possible future benefits applies. For the right of exclusion the obligation of injunction from the other legal associates is decisive. The author of the dissertation agrees with Urbas, who has noted that commercial law is already much more attached to the economic area than the tax law, and therefore it is much more permeated and controlled by the economic approach (Urbas, 1987, p. 237). The economic approach is especially used with the classification of economic assets. The point is that laws and “norms are not interpreted as isolated structures of terms, but should be seen in the context of the reality to which they relate” (Werndl, 1983, p. 49; Eibelshäuser, 2002, p. 1429).

Since the current opinion assumes agreement of the economic ownership in commercial law and tax law for capitalization of assets in terms of commercial law, the § 39 AO is decisive as well (Moxter, 1999, p. 39). Due to the principle

of decisiveness, which is anchored in § 5 EStG (German Income Tax Law), the classification of assets in terms of commercial law is binding for the tax balance sheet (Oldenburger, 2000, p. 111). Based on the decisiveness principle in both the commercial law and tax law, the person economically acting, the one who receives the economic benefit from the object/asset, has to be identified, and not the legal owner (Urbas, 1987, pp. 238–245).

1.5. Classification based on the German Decrees of Leases

Classification Criteria of the BFH. As it has been stated earlier according to § 238 HGB a merchant has to report his/her assets and debts completely in the balance sheet. The question as to whether an asset has to be reported in the balance sheet has to be decided not only on the basis of legal but also economic criteria, especially with the help of the economic approach – while at the same time the overall circumstances have to be considered. Following the basic concept of the economic approach: the decisive matter is who receives the essential opportunities and carries the risks of further development of the economic asset. In other words, who will be the economic owner? How does this apply to leasing agreements?

The German Commercial Law does not have specific and independent capitalization regulations for lease contracts. Capitalization of leased assets in terms of commercial law follows mostly the regulations which have been developed by the financial administration and by the BFH (Sabel, 2006, p. 9, p. 28, p. 53, Bordewin *et al.*, 2003, p. 25). The BFH has, starting with the fundamental judgment of January 26, 1970, established in four decrees detailed criteria regarding the classification of leased assets. These decrees are still valid and accepted today and were intended to cover the “quantitative substantiation of the applicable risk-rewards approach” (Sabel, 2006, p. 53) for a wide scope of possible cases, guarantee practicability, provide legal certainty and thus enable lease agreements where the legal consequences were not assessable beforehand (Bordewin *et al.*, 2003, pp. 30–32 and p. 38; Hastedt *et al.*, 1998, p. 34). To provide the desired legal certainty, a quantitative limit for lease agreements was established. This intended to enable the correct classification of economic property (Mellwig, 1998, p. 16; Sabel, 2006, p. 32 and p. 45; Riedel-Stegner, 2006, p. 42). However, these concrete quantitative limits also permit an intentional narrow lower deviation, which enables the often desired capitalization by the lessor or non-capitalization by the lessee (Sabel, 2006, p. 2, p. 49 and p. 53). Nevertheless, these quantitative limits guarantee “an objective classification of leased assets, which would be very difficult in individual cases by using qualitative criteria” (Sabel, 2006, p. 32; Küting *et al.*, 1998, p. 1468).

If the leased asset is capitalized by the lessor, the lease agreement is treated as a classical lease agreement. The capitalization and depreciation of the leased asset

has to follow the general and fundamental rules. However, for the part of the lease agreement that has not yet been processed, the principle of non-capitalization of pending businesses has to be applied (Sabel, 2006, p. 39 and p. 53; Brakensiek, 2001, p. 258; Kussmaul, 1987, p. 103; Küting *et al.*, 1999, p. 363). In this case, neither the obligation of paying rental installments nor the right to the future use has to be reported in the balance sheet. However, lease agreements have to be disclosed in accordance with § 285 No. 3 HGB as “other financial obligations” in the notes.

If the leased asset is capitalized by the lessee, the leasing agreement is treated as a **hire purchase** (Sabel, 2006, pp. 1–4, 14 and 49; Moxter, 1999, p. 41; Bordewin *et al.*, 2003, p. 38). In such a (rather rare) case the lessor recognizes the receivable in the balance sheet in the amount of the agreed lease installments. The amortization rate of the lease installment has to be discounted and deducted as neutral from the capitalized receivable, which stands in contrast to the interest, and cost portion of the lease installment (Sabel, 2006, p. 40, 49, and 53).

The four decrees of leases (see Table 1) can be classified between fully and partially amortized movables and immovables (Riedel-Stegner, 2006, p. 42).

Table 1. List of the German Decrees of Leases by the Federal Ministry of Finance

Decrees	Date of issue	Reference	Citation
VA-Decree Movables	19.04.1971	IV B/2-S 2170-31/71	BStBl: I 1971, p. 264 BB: 1971, p. 506
VA-Decree Immovables	21.03.1972	F/IV B/2-S 2170-11/72	BB: 1972, p. 433
TA-Decree Movables	22.12.1975	IV B/2-S 2170-161/75	BB: 1976, p. 72
TA-Decree Immovables	23.12.1991	IV B/2-S 2170-115/91	BStBl: I 1992, p. 13

Source: Kratzer *et al.*, 1997, p. 57

A full amortization constitutes acceptance of all costs by the lessee by way of the lease installments. The decrees provide examples of cases where the lessor capitalizes leased items. For lease agreements which are not covered directly by the decrees, the general principles of economic ownership have to be applied with regard to the capitalization. At the same time the criteria developed in the decrees must not be neglected.

Lease Agreements with Full Amortization. Agreements belong to the category of lease agreements with full amortization if during the irredeemable basic rental period all accrued costs of the lessor are covered by the lease installments of the lessee.

In the cases of fully amortized lease agreements for movables the leased asset is classified by the legal owner as a matter of principle. However, in exceptional cases the capitalization by the lessee can be justified. This usually applies in accordance with decrees of leases when the irredeemable basic rental period is shorter than 40% or longer than 90% of the economic life (of the leased asset). Under normal circumstances, the lessor will recognize the leased asset in his/her balance sheet if the irredeemable basic rental period is between 40% and 90% of the normal economic life (Sabel, 2006, p. 34, Bordewin *et al.*, 2003, p. 38, Riedel-Stegner, 2006, p. 44).

If the basic rental period is below the **40%-limit**, fiscal authorities assume a covered up hire purchase, because it is highly unlikely for a lessee to accept responsibility for the full depreciation of the leased asset while using less than 40% of its normal economic life (Sabel, 2006, p. 34; Bordewin *et al.*, 2003, p. 38; Riedel-Stegner, 2006, p. 44). In cases where the **90%-limit** is exceeded, it is assumed that the leased asset practically will be without value after the basic rental period is over, and therefore the economic ownership of the leased asset was transferred to the lessee. In such a case the lessor is permanently exempt from profits and substance (Sabel, 2006, p. 34; Bordewin *et al.*, 2003, p. 39; Hastedt *et al.*, p. 39, Döllner, 1971, p. 537). If a lease agreement does not specify **only options**, the classification likewise follows the 40–90%-limits (Riedel-Stegner, 2006, p. 45; Bordewin *et al.*, 2003, p. 40).

If, for example, a lease agreement contains a **purchase option**, which is considered favorable, the lessee is, in the case the option is exercised, entitled to a possible increase in value, which he will likely make use of due to economic circumstances. Therefore the leased asset will usually be classified by the lessee, when the agreement includes the purchase option and when the economic circumstances are considered favorable. However, if the price of the purchase option corresponds with the expected market price, then, by observing the 40–90%-limits, the leased asset has to be reported in the balance sheet of the lessor (Sabel, 2006, pp. 34–35; Riedel-Stegner, 2006, p. 45; Bordewin *et al.*, 2003, p. 41; Weiss, 2006, p. 41).

An agreed **option to extend the rental period** could also lead to the decision that the leased asset will be capitalized by the lessee. This would apply if economic needs lead to the exercise of the option, or if the exercise of the option appears reasonably certain from the economic perspective. This could be, for example, the case when the subsequent rent is considerably lower than the former one and only constitutes an appreciation fee (Sabel, 2006, p. 35; Bordewin *et al.*, 2003, p. 43; Riedel-Stegner, 2006, pp. 45–46; Weiss, 2006, p. 42).

If a leased asset is specifically built for the lessee and if only the lessee can take advantage of meaningful economic use of it, it is referred to as a **special leasing**. A subsequent usage by the lessor is unlikely in such cases. The lessee controls all rewards and risks from the leased asset. The 40-90%-limits do not play any role in such cases (Sabel, 2006, p. 35; Bordewin *et al.*, 2003, p. 47; Riedel-Stegner, 2006, pp. 46–47).

If, after the basic rental period is over, the lessee is entitled to any **proceeds from the sale** at the market value or at the book value, the leased asset has to be classified by the lessee as well (see appendix 1). Consequently, the classification of the leased asset depends, contrary to IAS/IFRS, mostly on the distribution of rewards, arising from the leased asset after the basic rental period is over (Hastedt *et al.*, p. 40; Sabel, 2006, p. 34; Riedel-Stegner, 2006, p. 51).

In cases of fully amortized lease agreements for immovable assets, attention has to be paid to the fact that a distinction is made between the land, on the one hand, and the building on the other hand, even if only one lease agreement has been concluded (see appendices 2 and 3). Land can be used without time limits and is therefore always capitalized by the lessor. The classification by the lessee is only applied if it is a special leasing, of a favorable purchasing option or a rent extension has been agreed in the contract, or if the basic rental period is outside the 40-90%-limits (Sabel, 2006, p. 35; Bordewin *et al.*, 2003, p. 53).

Lease Agreements with Partial Amortization. Lease agreements with partial amortization for movables can be distinguished in three different contract types, whereby also with these contracts the 40–90% limits have to be observed. In addition it has to be clarified by whom the economic value can be capitalized after the basic rental period expires (see appendix 4). “With all three types of contracts the economic ownership lies with the lessor, if the lessee accepts the whole amortization risk, while the lessor participates considerably in the recognition of the value” (Riedel-Stegner, 2006, pp. 48–49; Leippe, 2002, p. 107).

In the first case we are dealing with lease agreements that include a so-called right to offer (for sale). The lessor has the right to sell the leased asset to the lessee after the expiry of the basic rental period at a price that has been fixed in the contract. Since the lessor might benefit from an increase in the value, but the lessee only has the risk of a possible decrease in value, the leased asset is consistently capitalized by the lessor. This illustrates again that in accordance with the decrees of leases only the distribution of rewards regarding the leased asset after the expiry of the basic rental period is taking place (Sabel, 2006, p. 33 and pp. 36–37; Weiss, 2006, p. 45; Riedel-Stegner, 2006, p. 48; Bordewin *et al.*, 2003, p. 51; Hock *et al.*, 1993, p. 215).

In the second case we are dealing with the agreement concerning the possible distribution of (higher than expected) additional proceeds. After the expiry of the basic rental period the lessor sells the leased asset to a third party. If the return on the sale is lower than the difference between the book value and the return on the sale, the lessee has to compensate the difference. However, if the return on the sale is higher, the additional proceeds will be shared. In this case the leased asset is capitalized by the lessor, if he receives at least 25% of the additional proceeds. This applies, if he (the lessor) has sufficient opportunities for profits through the leased asset (Riedel-Stegner, 2006, pp. 49–50; Sabel, 2006, p. 37; Bordewin *et al.*, 2003, p. 51; Weiss, 2006, p. 45).

In the third case we are dealing with irredeemable rental contracts with decree of sales proceeds of a final payment made by the lessee. The lessee can terminate the agreement after 40% of the normal economic life at the earliest. In this case the lessee has to make a final payment to the lessor. The payment is calculated from the difference between the already performed rental installments and the total costs of the lessor not covered by the performed payments. However, 90% of the return of the sale of the leased asset will be allowed for the final payment. In this case, too, the lessee carries all the risks. The lessor has the reward from the return of the sale and thus, the asset has to be capitalized by the lessor (Riedel-Stegner, 2006, pp. 50–51; Sabel, 2006, pp. 37–38; Bordewin *et al.*, 2003, p. 52).

In addition so called non-decree conform lease agreements exist, which are not directly affected by the decrees. Agreements with double options and special automobile lease agreements belong to this category. Nonetheless a factual overall appreciation with the help of the general principles of economic ownership and/or the general criteria of the decrees of leases should be made (Sabel, 2006, p. 33; Riedel-Stegner, 2006, p. 51; Mellwig, 2000, p. 72; Bordewin *et al.*, 2003, p. 52).

In summary, it can be stated “that capitalization by the lessee will only apply, if he carries almost all of the risks and rewards from an appreciation in value of the leased asset” (Sabel, 2006, p. 38).

In the case of partially amortized lease agreements a distinction is made between land and building. The land is capitalized in principle by the economic owner of the building, who in the case of option free agreements is usually the lessor. To become the economic owner, the lessee has to take over the essential rewards and risks. This applies to special lease agreements and favorable purchase and rent extension options when more than 90% of the normal operational economic life time has been made use of (Sabel, 2006, p. 38). Since these options are considered favorable, a so called economic use of coercion exists (see appendix 5).

Critical Evaluation of the German Decrees of Leases. The four decrees of leases classify lease agreements for movables and immoveable items, and with full and partial depreciation. These capitalization regulations, according to the economic approach, are oriented towards the economic overall recognition of the circumstances of the economic authority to dispose, and towards the GoB in terms of commercial law (Knobbe-Keug, 1993, p. 81; Moxter, 1989, p. 241; Sabel, 2006, p. 10, p. 53). The decrees of leases contain six guiding principles, which emphasize the circumstances of the overall economic recognition of individual cases. In principle, the leased asset is capitalized by the lessor, in contrast to the International GAAP. If, however, the economic utilization potential is used by someone other than the legal owner, then the economic asset has to be capitalized to this someone else through an evaluation process (Sabel, 2006, p. 53). Hereby the capitalization depends only, in contrast to the IAS 17, on the distribution of rewards after the expiry of the basic rental period (Küting *et al.*, 1998, p. 1470; Riedel-Stegner, 2006, p. 52). Since the German Commercial Law does not have explicit capitalization criteria (Findeisen, 1997, p. 838; Riedel-Stegner, 2006, p. 39), the decrees of leases include detailed capitalization criteria. They are meant to provide predictable legal certainty. The intention was to provide legal certainty through quantitative limits that do not allow room for choices (Sabel, 2006, p. 32; Mellwig, 1998, p. 16; Riedel-Stegner, 2006, p. 40 and p. 133). These fixed quantitative limits (Riedel-Stegner, 2006, p. 88, p. 133; Mellwig, 1998, p. 8) enable, however, a narrow lower deviation of the limit and consequently the purposeful creation of lease agreements (Knobbe-Keug, 1993, p. 77.; Sabel, 2006, p. 32; Bordewin *et al.*, 2003, p. 39). “Nevertheless, they provide objectives for capitalization of leased assets, which would be difficult to achieve with the evaluation of individual cases and with quantitative criteria” (Sabel, 2006, p. 32; Küting *et al.*, 1998, p. 1468).

2. THE PRINCIPLE “SUBSTANCE OVER FORM” AND CAPITALIZATION OF LEASES ACCORDING TO THE INTERNATIONAL GAAP

The requirement that annual financial statements should give a true and fair view has been emphasized in the paragraph 46 of the IASB *Framework for the Preparation and Presentation of Financial Statements*: “Financial statements are frequently described as showing a true and fair view of, or as presenting fairly, the financial position, performance and changes in financial position of an entity”. According to the Fourth EC Directive on Company Law (or Fourth Directive) and the Seventh EC Directive on Company Law (or Seventh Directive), the annual and consolidated financial accounts² (statements) must show a true and fair view. Article 2 paragraph 3 of the Fourth Directive provide as follows: “The annual accounts shall give a true and fair view of the company’s assets, liabilities, financial position and profit or loss”. At least in theory, the true and fair view criterion ensures that statements are not only correct but also are useful indicators of a company’s financial health³. The fulfillment of this criterion requires a concern for **substance over form** and the application of professional judgment. It is necessary to emphasize that the degree to which accountants and auditors search for ‘fairness’ as opposed to correctness or legality has differed substantially internationally⁴. In an attempt to ‘present fairly’, accountants have come to the view that it is necessary to try to account for the **economic** substance of events rather than for the **legal** form.

2.1. Definition of “Substance over Form”

Substance is the material or essential part of something, as distinguished from *form*, which is the observance of a legal or technical manner or order. **Economic substance** refers to the economic benefits and economic losses or any kind of economic implications related to the event whereas, **legal form** refers to the legal status of the event. Arguably the greatest issue facing accountants today is that concerning the clash between economic substance and legal form in corporate financial reporting. (Lee, T. A., 2006, p. 232) Most time we do not need to apply this concept as the economic and legal aspects of the transactions

² “Accounts” is British term for “financial statements”.

³ The Honorable Mrs. Justice Arden emphasizes that true and fair view is a dynamic concept (Arden, 1993, pp. 151–152) and ‘true and fair view’ cannot be defined and that synonyms cannot be found for it. However one can identify a number of features of the true and fair view. (Arden, 1997, p. 676)

⁴ Cook has emphasized that much of the existing debate on the significance of the true and fair view requirement in Europe has been polarized between those who believe there can be only one interpretation across all member states and those who believe that the principle takes on a different content in each member state. (Cook, A., 1997, p. 703)

are concentrated at one place i.e. both of these aspects are not segregated among two different parties. But if to take into account that in some transactions these two aspects get segregated it is necessary to emphasize that substance over form is critical for reliable financial reporting. The key point of the concept is that a transaction should not be recorded in such a manner as to hide the true intent of the transaction. Substance over form concept seeks to emphasize the **economic approach** (economic view).

“Economic substance” should not be confused with “possession” or “use”. There are many examples in which the possession of the asset is with the party other than the owner and still we do not apply this concept. Economic substance is not about possession and/or use; it is about the risks and rewards. Through this concept we check whether the risks and rewards are with the party and then accordingly decide what will be the accounting treatment.

The doctrine of ‘substance over form’ is found in many attempts to construct a conceptual framework of accounting and financial reporting. Many interpretations have been made of the phrase but it is perhaps most readily understood as the belief that financial statements should, when there is conflict, be based on economic (or commercial) reality rather than legal form. (Lewis, R., Pendrill, D., 2004, p. 206) This involves the famous ‘duck test’⁵.

Where the economic substance of a transaction is inconsistent with its legal form, *substance over form* requires that the accounting represents the economic substance (or impact) of the transaction. (Deegan, C., Unerman, J., 2006, p. 182) Debates about economic substance versus legal form arise because many accounting rules are devised by the International GAAP while some are contained in company legislation. The accountant is required to assess the ‘economic reality’ of the reporting entity. However, the legal form of a transaction may yield a conflicting view.

Accounting for schemes following merely the letter of the law resulted in certain assets or liabilities being hidden from the reader of the financial statements. The ICAEW was the first to issue an official document on the issue. Technical Release (TR) 603, ‘Off Balance Sheet Financing and Window Dressing’, published in 1985, urged accountants to consider the economic substance of a transaction rather than the mere letter of the law. In early 1986, UK standard setters were even discussing adopting substance over form as a fifth accounting concept (along with going concern, accruals, consistency and prudence concepts) (Hopwood, A., Vieten, H., 1999, p. 357).

IASB view. According to the International GAAP the priority of economic substance over legal form is one of the basic accounting principles. It is an important basis for many standards. The IASC has not issued a standard on accounting for substance over form and therefore guidance must be sought from

⁵ If something looks like a duck and quacks like duck, then it is a duck.

the *Framework for the Preparation and Presentation of Financial Statements*. The Framework establishes a general requirement to account for transactions in accordance with their substance, rather than only their legal form. The Framework says that you should keep the substance over form principle in mind when assessing whether an item meets the definition of an asset, liability or equity: the underlying substance and economic reality of the item should be examined and not merely its legal form.

International GAAP versus US GAAP. The substance over form principle, although logical and useful, is not universally accepted. Problems may arise simply because a transaction is extremely complex, which makes it quite difficult to ascertain what the substance of the transaction is – even for a law abiding accountant. Stolowy and Lebas have noted that to make an oversimplification, the substance over form principle is accepted and used mainly in the North American zone of influence (Stolowy, H., Lebas, M. J., 2006, p.161). In the USA, in spite of the existence of a conceptual framework containing the broad principles for accounting and financial reporting, the emphasis has been for accounting standards to prescribe detailed and complex rules to be followed when preparing financial statements. This difference in emphasis has led to the IASB approach to standard setting being characterized as ‘principle based’ and the US FASB approach as ‘rules based’. Consequently, substance over form is the distinguishing factor between the International GAAP and the US GAAP.

2.2. Application Scope of the IAS 17

Elliott and Elliott have emphasized that the IAS 17 Leases was the first formal imposition of the principle of accounting for substance over legal form, aiming to ensure that the legal characteristics of a financial agreement did not obscure its commercial impact (Elliott, B., Elliott, J. 2002, p. 315). Capitalization of lease agreements according to the International GAAP is decided by the economic approach (Weinstock, 2000, p. 219). Accordingly, the evaluation of actual circumstances is based purely on the economic effects (economic substance over legal form) and not on the legal form (IAS 17.10, Haller, 1994, p. 260; Pellens, 2001, p. 169). A later transfer of ownership is therefore irrelevant (Hirsch, 1998, p. 101; Mellwig, 1998, p. 3; Feinen, 2002, p. 94; Weinstock, 2000, p. 221.). This principle of “substance over form” is anchored in the IAS F. 35.

In principle, the leased asset is capitalized by the contract party, who receives substantially all rewards and carries most of the risks during the basic rental period. Rewards can be, for example, expectation of profitable operation over the asset’s economic life and of gain from appreciation in value or realization of a residual value. Possible risks can arise from possibilities of losses from idle capacity or technological obsolescence and of variations in return because of

changing economic conditions. Therefore the asset must be capitalized by the lessee if all essential risks and rewards are transferred to him. In the IAS 17 the quantitative criteria are provided which indicate the obligation to capitalize, but they are not exact in their quantification and/or concretization. Thus, the capitalization allows choices and a scope for description, which will be discussed in more detail hereafter.

Conceptual Foundations. The capitalization of lease agreements is regulated in principle by the IAS 17, whereby in the IAS 17.2 it is stipulated that all illustration rules and disclosure requirements in the IAS 17 have to be applied to **all** lease agreements. As shown in Figure 7 numerous other standards have to be observed as well in this context.

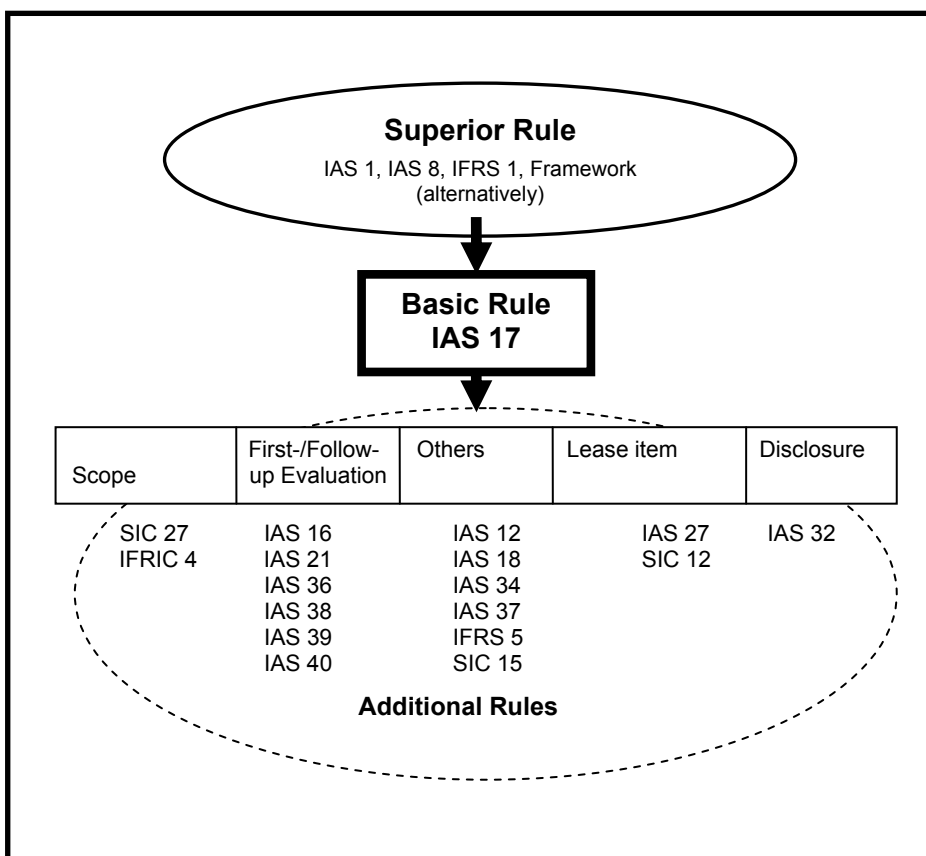


Figure 7. IAS/IFRS Standards that have to be applied to Lease Agreements

Source: Kümpel *et al.*, 2006, p. 2

The scope of the IAS 17 encompasses all agreements for the transfer of the legal right of use regarding an asset against payment or series of payments for an agreed period of time, and is closely connected with the definition of lease

contained in the IAS 17.4: “A lease is 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”. Sabel, as well as Hastedt and Mellwig have noted that the term “lease” does not only describe lease agreements in a narrow sense, but all transfers of the right of use with a limited duration, even if they are not explicitly named as “lease” (Sabel, 2006, p. 55; Hastedt, Mellwig, 1998, p. 13) But it is necessary to emphasize that in exceptional cases it is possible that agreements have to be capitalized according to the IAS 17, although no right of use according to the civil law has been agreed on. This applies, for example, to “cover up lease agreements”, when only an acceptance contract is concluded. Furthermore, a financial service in return for the right of use is not absolutely necessary because the service in return can also be part of a barter business. It is obvious that always the overall economic observation is the deciding criterion, not only the evaluation of individual contracts and conditions, or the naming of these contracts (Kümpel, Becker, 2006, p. 3; Sabel, 2006, p. 55 and p. 57; Weiss, 2006, p. 55; Esser, 2005, p. 429). The decisive criterion for the evaluation and classification of a lease agreement and/or for answering the question, whether the requirements of the IAS 17 have to be applied, lies with the economic substance of the agreement. The agreements therefore have to be examined, “whether from the perspective of the economic approach an actual transfer of legal rights of use of assets has taken place although the legal construction does not suggest so” (Kümpel, Becker, 2006, p. 3).

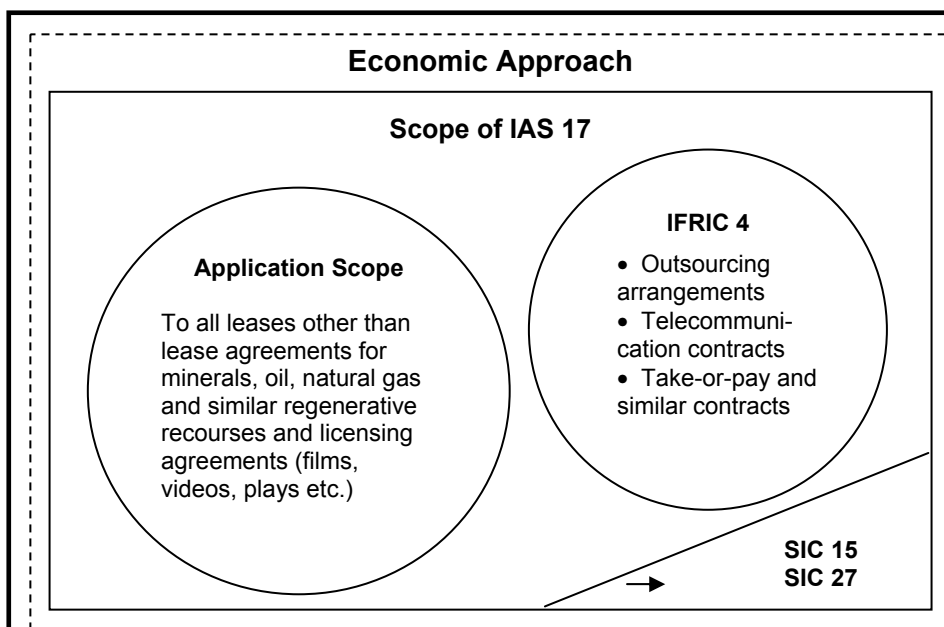


Figure 8 Application Scope of the IAS 17

Source: compiled by author

Consequently, the interpretation of the SIC 27 and the IFRIC 4 requires the examination of contracts, which could be covered by leasing regulations, even though they were not explicitly named as leasing agreements. The enormous significance and role of the economic approach (substance over form) according to the International GAAP could not be highlighted more. The scope of the IAS 17 is illustrated in Figure 8.

Expansion of the Scope of the IAS 17 by IFRIC 4. IFRIC 4 was passed in December 2004 and thus, the scope of the IAS 17 was expanded to ensure that indirect legal rights of use and rights of use that are limited in time, will be included in lease agreements according to the IAS 17.4. However, it is often very complicated to recognize an indirect legal right of use because the shape and diversity of contracts are becoming more complex and difficult (Zülch, Willms, 2005, pp. 315–316). To help clarify this matter, the definition of the term “lease” in the IAS 17.4 was concretized and expanded by the IFRIC 4. According to the IFRIC 4.6 determining whether an arrangement is, or contains, a lease shall be based on the substance of the arrangement and requires an assessment of whether:

- fulfillment of the arrangement is dependent on the use of a specific asset or assets (the asset); and
- the arrangement conveys a right to use the asset.

In accordance with IFRIC 4, the assessment of whether an arrangement contains, a lease is to be made at the inception of the arrangement. A reassessment is permitted only if any of the following conditions is met (IFRIC 4.10):

- a) There is a change in the contractual terms, unless the change only renews or extends the arrangement.
- b) A renewal option is exercised or an extension is agreed to by the parties to the arrangement, unless the term of the renewal or extension had initially been included in the lease term in accordance with the IAS 17.4.
- c) There is a change in the determination of whether fulfillment is dependent on a specified asset.
- d) There is a substantial change to the asset, for example a substantial physical change to property, plant or equipment.

Furthermore, the IAS 17.3 was concretized and amended with the IFRIC 4 in such a way that now all contracts with several components are part of the scope of the IAS 17. These are contracts with not only the legal right of use, but they include other services, such as maintenance and service work, which are agreed in addition. However, if the contract does not include the legal right of use, but only certain service components, then the contract would not be declared as

leasing according to the IAS 17.3 and therefore not be covered by the scope of the IAS 17.

Limitation of the scope through the SIC 27. As has been mentioned before, several contracts exist which are not officially declared as lease agreements, although they belong within the scope of the IAS 17. And alternatively, there are contracts with agreements similar and close to lease agreements, the legal structure of which assumes a lease and yet these contracts are not part of the scope of the IAS 17. On the basis of the overall economic observation, each factual situation and each contractual agreement has to be examined as to whether it really is covered by the scope of the IAS 17, and whether it fulfills the lease definitions of the IAS 17.4, respectively, and whether a transfer of the legal rights of use with regards to an asset has indeed taken place.

Examples include the so called US leasing transactions, which are also referred to as cross border leases (CBL) or lease and leaseback agreements, respectively (Bühner, Sheldon, 2001, pp. 315–318; Bordewin, Tonner, 2003, pp. 143–144). The main purpose of these transactions is of a fiscal nature; namely to gain a cash value advantage through tax moratorium effects. US transactions contain various contracts, which are concluded as part of an overall plan and can only be understood in their entirety. It is the fundamental intention of these transactions to use different tax laws in two or more countries and save taxes in the process. The different fiscal regulations in two or more countries create the fiction of two fiscal owners of one and the same item. Both, following the laws of their respective countries, (fiscally) amortize this same item. Both the lessee and the lessor can write off the leased item from their taxes with this construction. Since the US side can capitalize the amortization without any actual acquisition costs, it can be stated that this model is purely for tax saving purposes. The US partner will then share part of the saved taxes with the lessee (Kümpel, Becker, 2006, pp. 9–13). Kümpel and Becker have emphasized that “to grasp the economic content of these transactions, the contract conglomerate has to be seen as a whole. The principle of individual evaluation is given up in favor of the economic approach”. (Kümpel, Becker, 2006, p. 10) Due to the indications of the SIC 27, US leasing transactions are not anymore part of the scope of the IAS 17. Other exceptions and perimeters from the scope are found in the IAS 17.2, where it is stated unambiguously that, for example, agreements concerning the discovery of natural resources or lease agreements concerning investment properties are covered by other scopes than the IAS 17.

2.3. Classification of Lease Agreements

2.3.1. Conceptual Foundations of the IAS 17

The concept of the IAS 17 concerning the capitalization of lease agreements is based on the fundamental idea that assets have a certain economic benefit. The

future economic benefit embodied in an asset is the potential to contribute, directly or indirectly, to the flow of cash and cash equivalents to the entity. This economic benefit, defined in IASB Framework para. 53, can be transferred with the help of the lease agreement to the lessee, without transferring the legal ownership of the asset in any way. Consequently, the ownership according to the civil law is totally irrelevant regarding the capitalization of assets. Only the economic ownership matters. Consequently, on the basis of the economic approach (substance over form), factual circumstances are evaluated only according to their economic content (Riedel-Stegner, 2006, p. 53 and p. 100; Esser, 2005, p. 430; Preißler, 2002, p. 2394).

Based on the principle of substance over form, which has a high standing within International GAAP, the central question is who must capitalize the leased asset. According to IASB Framework para. 49a the asset is a resource controlled by the entity as a result of past events and from which future economic benefits are expected to flow to the entity. Following the IAS 38.13 in conjunction with the IAS 8.11 (a) an entity controls an asset if the entity has power to obtain the future economic benefits flowing from the underlying resource and restrict the access of others to those benefits. An explanation of how to identify an economic owner cannot be found in the framework. Instead, in the IASB Framework para. 57a (indirect) reference to the IAS 17 exists, which has fundamental significance that goes beyond leasing agreements.

In determining the existence of an asset, the right of ownership is not essential; thus for example, property held on a lease is an asset if the entity controls the benefits which are expected to flow from the property. Although the capacity of an entity to control benefits is usually the result of legal rights, an item may nonetheless satisfy the definition of an asset even when there is no legal control.

2.3.2. Capitalization according to the Economic Ownership

The fundamental concept of the framework serves as the main requirement for the IAS 17 concerning the capitalization of lease agreements, according to which assets have to be capitalized by the one, who as the economic owner, has the authority of disposal over the asset, and who controls the essential rewards and risks. This fundamental approach is also referred to as the risk and reward approach. Some of the rewards in connection with the asset are, for example, the expectation of profitable operation over the asset's economic life and of gain from appreciation in value or realization of a residual value. Risks can arise from possibilities of losses from idle capacity or technological obsolescence and of variations in return because of changing economic conditions. These examples highlight that the terms in the IAS 17, referring to "rewards" and risks" represent what is identified as the future economic benefit in the framework.

The IAS 17 distinguishes two kinds of lease agreements, namely the **finance lease** and the **operating lease**. A finance lease is 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 (IAS 17.4). An operating lease is a lease other than a finance lease (IAS 17.4). The classification as a finance lease or operating lease has to be decided at the inception of the lease. However, if the contract parties had already agreed earlier on the essential content of the contract (e.g. amount of the rental installment, duration of the agreement, etc.), this earlier point in time is applied. The inception of the lease is the earlier of the date from which the lessee is entitled to exercise its right to use the leased asset (IAS 17.4). The commencement of the lease term does not play any role in this (Kümpel, Becker, 2006, pp. 21–22).

The criterion of distinction is whether the lessor or the lessee should capitalize the leased asset. It is a finance lease according to the IAS 17.4, if substantially all risks and rewards, namely the future economic benefits, are transferred to the lessee. In accordance with the economic approach this is a case of hire purchase, and therefore the asset has to be capitalized by the lessee. If the criteria for a finance lease according to the IAS 17.4 do not exist, the lease agreement is automatically classified as an operating lease. The definition of operating lease agreements is a “negative distinction” (Kümpel, Becker, 2006, p. 17; Sabel, 2006, p. 56; Weinstock, 2000, p. 94), since all lease agreements that do not fulfill the definition criteria of a finance lease will automatically be considered operating leases (Sabel, 2006, p. 56). If a lease agreement belongs to the category of operating leases, the lessor will capitalize it; it can be compared to a rental contract (Weiss, 2006, p. 57; Sabel, 2006, p. 56; Kümpel, Becker, 2006, p. 17).

It should be noted that the special terms used in Germany do not provide the conclusive information regarding the classification of the economic ownership, whereas according to the International GAAP only such cases where the economic ownership is transferred to the lessee will be considered finance leases (Hastedt, Mellwig, 1998, p. 14; Sabel, 2006, pp. 56–57; Kümpel, Becker, 2006, p. 17). To assure that lease agreements will be classified correctly, examples and indicators are listed in the IAS 17.10 and the IAS 17.11 (see Figure 9), with the help of which the identification of finance leases will be made easier. The IAS 17.10 provides examples which will usually result in the classification of a lease agreement as a finance lease:

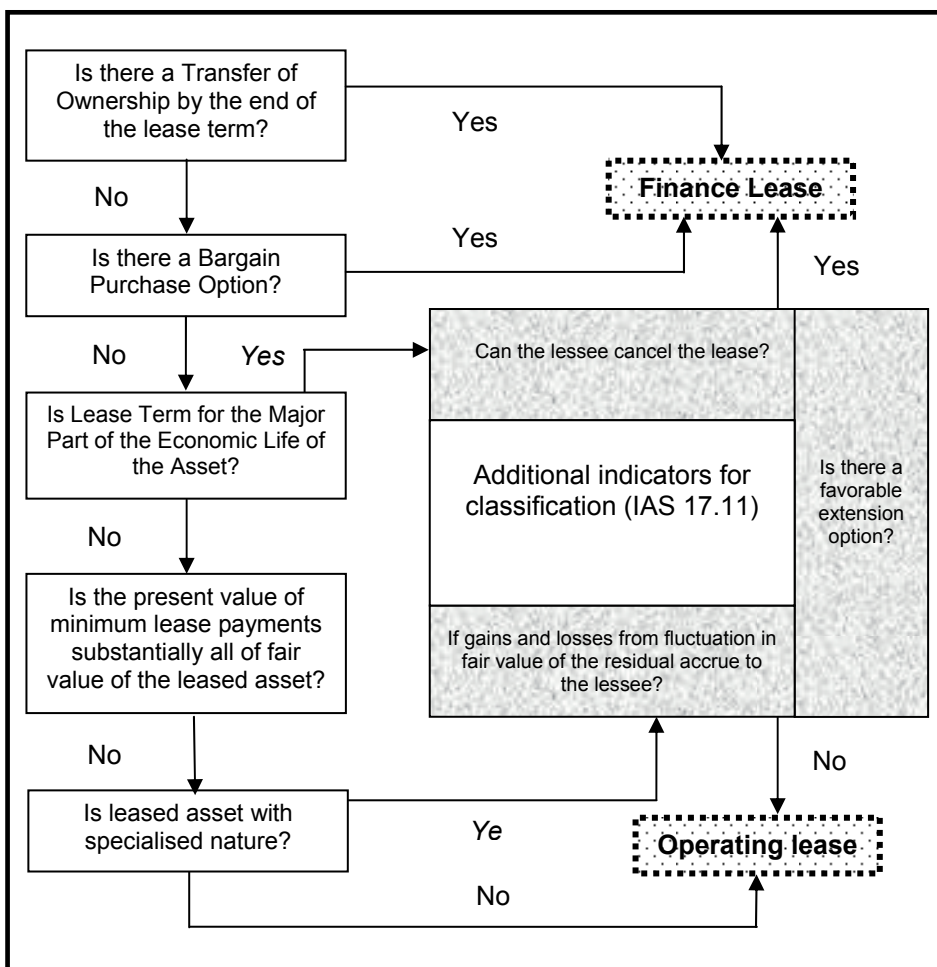


Figure 9. Classification of Lease Contracts according to the IAS 17.10 and 17.11

Source: compiled by the author

- automatic transfer of ownership – the lease transfers ownership of the asset to the lessee by the end of the lease term (IAS 17.10a);
- bargain purchase option – the lessee has the option to purchase the asset at a price that is expected to be sufficiently lower than the fair value at the date the option becomes exercisable for it to be reasonable certain, at the inception of the lease, that the option will be exercised (IAS 17.10b);
- economic life test – the lease term is for the major part of the economic life of the asset even if title is not transferred (IAS 17.10c);
- recovery of investment test – 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 (IAS 17.10d);

- special lease – the leased assets are of such a specialized nature that only the lessee can use them without major modifications (IAS 17.10e).

In addition to the examples in the IAS 17.11 further indicators are mentioned, pointing to the classification as a finance lease:

- losses in the case of cancellation – if the lessee can cancel the lease, the lessor's losses associated with the cancellation are borne by the lessee (IAS 17.11a);
- gains or losses from fluctuations of residual value – gains or losses from the fluctuation in the fair value of the residual accrue to the lessee (for example, in the form of a rent rebate equaling most of the sales proceeds at the end of the lease) (IAS 17.11b);
- favorable rent extension option – the lessee has the ability to continue the lease for a secondary period at a rent that is substantially lower than market rent (IAS 17.11c).

These criteria are, in contrast to the German leasing decrees, of a qualitative and not quantitative nature. This means that they neither have quantitative limits nor a definitive character. Küting *et al.* explain the existence of this open classification by the application of a holistic economic approach in the IAS 17 and the resulting flexible and case oriented interpretation of the rules (Küting, Hellen, Brakensiek, 1998, p. 1468; Küting, Hellen, Koch, 2006, p. 651). The application of a holistic economic approach is intended to secure the classification of lease agreements case by case, and to avoid automatism (Esser, 2005, p. 431; Sabel, 2006, p. 61; Weinstock, 2000, p. 98). That results in a certain degree of discretion and remains room for interpretation (Kümpel, Becker, 2006, p. 19; Sabel, 2006, p. 61; Küting, Hellen, Koch, 2006, p. 651; Vater, 2002, p. 2096).

Although the conceptual differentiation between examples and indicators and the varying strict formulations in the IAS 17.10 and the IAS 17.11 are unclear, it can be assumed that clues in comparison with the examples offer weaker evidence for the classification of contracts (Sabel, 2006, p. 59; Mellwig, 1998, p. 6; Vater, 2002, p. 2095; Lüdenbach, Freiberg, 2006, p. 259; Pellens, Fülber, Gassen, 2006, p. 595). Despite the help that is offered by the examples and indicators, it is not permitted to assume that an “automatism of classification” of the criteria exists – which is in contrast to the German decrees of leases (Kümpel, Becker, 2006, p. 19; Mellwig, 1998, p. 4; Esser, 2005, p. 432; Leippe, 2002, p. 123; Alvarez, Wotschofsky, Miethig, 2001, p. 936). They only help with the identification and do not necessarily result in the classification as a finance lease (Sabel, 2006, p. 59; Weinstock, 2000, p. 99). If, on the basis of the economic approach, not all essential rewards and risks are transferred to the lessee, the lease agreement has to be classified as an operating lease. Consequently, the

converse case is also possible, namely the classification as a finance lease, although the above mentioned examples and indicators actually exist (Sabel, 2006, p. 59; Weinstock, 2000, pp. 98–99). In this context it is important always to consider the overall economic observation and to appreciate the concrete case. This will assure the correct classification and capitalization of leases.

2.3.3. Classification Criteria (Examples)

Transfer of Ownership Test. If an automatic transfer of ownership after the basic rental period is part of the lease agreement, it is essentially a finance lease. This automatic transfer of ownership does not have to be part of the lease agreement; it can be part of another, additional contract. But from a holistic and economic overall observation, these two contracts would have to be evaluated together, because one would not have been concluded without the other. An agreement, where the legal ownership is transferred after the basic rental period automatically, namely after payment of all rental installments, is considered a rent purchase contract in Germany. This is actually a purchase contract, whereby the installment payments can be compared with the lease installments (Sabel, 2006, p. 60; Mellwig, 2000, p. 75).

Following the control approach of the IAS/IFRS (Oldenburger, 2000, pp. 116–118; Behr, 2002, p. 34; Sabel, 2006, p. 154) the classification as a finance lease and the resulting capitalization by the lessee can hardly be disputed (Kümpel *et al.*, 2006, p. 23) because the lessee has permanent control over the asset, and thus he also has the economic right to the future benefit of the asset. Furthermore, he/she can prevent the legal owner from using the future benefit (Alvarez *et al.*, 2001, p. 936). The transfer of rewards and risks to the lessee does not have to be controlled at the beginning of the lease agreement; it is independent of time. The important criterion concerning the capitalization of the leased asset is the authority over the utilization potential, which in the case of a finance lease is transferred to the lessee, not only the transfer of rewards and risks (Kümpel *et al.*, 2006, p. 23).

Bargain Purchase Option Test. A finance lease has to be assumed if the lease agreement includes a purchase option which entitles the lessee to purchase the leased item at a very favorable price after the expiry of the basic rental period – which means at a sufficiently lower price than the probable fair value. However, the purchase option can also refer to other items, not only to the leased assets. In this case we talk about an indirect purchase option, which however, is treated identical by a direct purchase option of the economic approach (Kümpel *et al.*, 2006, p. 23).

Since it concerns a “favorable” purchase option, a certain economic dictate on the part of the lessee to exercise the option is assumed with sufficient certainty. In this case the terms “favorable” or “sufficiently lower” purchase price does not

have quantitative limits – as it was the case in the German decrees of leases – because the evaluation is done case by case and with the help of a coherent and economic overall perspective, and not by applying rigid limits (Sabel, 2006, p. 61; Küting *et al.*, 1998, p. 1468; Lüdenbach *et al.*, 2006, p. 261; Riedel-Stegner, 2006, p. 102).

Reasonable certainty can be assumed if an economic dictate regarding the exercise of the option exists, and if the price is far below the actual value. If the favorable purchase option is compared with the automatic transfer of ownership, striking similarities of the two evaluation tools can be noticed (Kümpel *et al.*, 2006, pp. 23-24). “While in the case of the contractually agreed transfer of ownership a legal dictate of purchasing the leased item exists, the purchase option derived from the concept of substance over form is based on the economic dictate” (Kümpel *et al.*, 2006, p. 24; Mellwig, 1998, p. 4).

Determining the expected value of the leased item is problematic due to the use of unspecific terms and provides room for discretion during the necessary evaluation process (Kümpel *et al.*, 2006, p. 25; Sabel, 2006, p. 61; Mellwig, 1998, p. 5). Furthermore, it appears complicated to evaluate whether the agreed purchase price is considerably below the expected fair value of the leased item at the time of the actual purchase already at the time of the contract conclusion, (Engel-Ciric, 2003, p. 395; Mellwig *et al.*, 1996, p. 2345; Weinstock, 2000, p. 101). In the IAS 17.4 the amount is given as the fair value, for which an asset could be exchanged, or a liability settled between knowledgeable, willing parties in an arm’s length transaction. This definition is also found in other IAS standards, whereby no other concrete instructions are given for the determination of the value. To close the remaining gaps, the option is offered in the IAS 8.11a – the requirements in IFRSs dealing with similar and related issues. Since lease agreements usually deal with tangible assets, it is natural to refer to the regulations in the IAS 16.31 for the revaluation model and as an addition to the explanations in the IAS 40.33 concerning the measurement of investment property on the basis of the fair value (Kümpel *et al.*, 2006, p. 25; Tanski, 2005, p. 93). After recognition as an asset, an item of property, plant and equipment whose fair value can be measured reliably shall be carried at a revalued amount.

According to the economic approach, there is always a need for a holistic, economic and individual evaluation of all aspects of the evaluated circumstances to assure the correct classification (Kümpel *et al.*, 2006, p. 40; Engel-Ciric, 2003, p. 397; Sabel, 2006, p. 63). Insisting only on the determination of the fair value will not be enough. If, for example, facilities are built and/or installed on leased land, and if the utilization period of these facilities is longer than the leased land, an economic dictate to exercise the purchase option might exist (Mellwig, 2000, p. 96; Kümpel *et al.*, 2006, p. 32). However, for the assumption of this economic dictate, it is not enough to only talk about a meaningful

alternative; there must not be another meaningful economic alternative to the exercise of the purchase option.

Economic Life Test. If the lease term is for the major part of the economic life the leased asset, in accordance with the IAS 17.10 (c) a finance lease can be assumed. An asset can provide usefulness only for a limited time period (the so called economic utility period or the economic life), and therefore, in the case of the transfer of the predominant part of the economic life, all essential rewards and risks are transferred to the lessee. Consequently, after the expiry of the lease term and after using most of the utility potential, the leased item does not have any significant value for the lessor anymore (Mellwig, 2000, p. 76; Sabel, 2006, pp. 62–63). In the decision of classification and capitalization to either the lessor or the lessee, **the lease term** (or agreed period of time) and the **economic life** play a significant role.

According to the IAS 17.4 **the lease term** is defined as the non-cancellable period for which the lessee has contracted to lease the asset together with any further terms for which the lessee has the option to continue to lease the asset, with or without further payment, when at the inception of the lease it is reasonably certain that the lessee will exercise the option. A non-cancellable lease is a lease that is cancellable only upon the occurrence of some remote contingency; with permission of the lessor, if the lessee enters into a new lease for the same or an equivalent asset with the same lessor or upon payment by the lessee of such an additional amount that, at inception of the lease, continuation of the lease is reasonably certain. If the cancellation of the contract becomes very unlikely due to the cancellation conditions in the contract, it will not affect the lease term of the leasing agreement. Concerning exceptional and special cancellation rights it has to be evaluated, whether they have been concretized and whether such a cancellation will realistically occur.

Furthermore, the leasing partners could agree to cancel the lease agreement or let it expire and then conclude a new one shortly after that for a corresponding or similar leased item. In this case, from the economic approach viewpoint, the continuation of the lease agreement according to the regulations in the IAS 17.3 would be assumed and the existing or cancelled contract respectively would be still considered as non-cancelled and continues to be valid (in a modified form). However, if the leased asset is altered (e.g. through renovation) to such a degree that it is equivalent to a new asset, then a new lease agreement could be considered reasonable from an economic perspective. If a lease agreement contains an option for extension, it has to be checked and evaluated at the beginning of the agreement, whether the option can be considered as reasonably certain. Similarly, as with the favorable purchase option, it will be examined whether the economic dictate for an agreement extension exists (e.g. rental payments far below the market value, contract fines in case of non-action

concerning the option, favorable purchase option after the contract extension, etc.). If the exercise of the option brings advantages to such an extent that the non-action would be meaningless from an economic viewpoint and could not be comprehended rationally, the exercise of the option can be assumed and therefore a finance lease can be assumed as well. This again makes clear the importance of a holistic and economic approach with consideration for the individual case when a leased asset has to be classified.

According to the IAS 17.4 **the economic life** is determined either (a) as the period over which an asset is expected to be economically usable by one or more users; or (b) the number of production or similar units expected to be obtained from the asset by one or more users. Thus, the economic life of an asset is independent from the capitalizing enterprise and is different from the various and individual economic lives from individual enterprises (useful life) (Sabel, 2006, p. 62; Kümpel *et al.*, 2006, p. 38). In the cases of already used leased assets the IAS 17.10 (c) stipulates that the lease term is for the major part of the economic life of the asset even if title is not transferred. From the perspective of the economic approach this could lead to different results in the assessment of economically identical facts.

Example. A 10-year-old machine has a remaining economic life of three more years. This machine can either be bought at €30,000 or it can be leased for a period of three years at €833.33 per month. The two cases are different only regarding the classification of the legal ownership (in the case of a purchase, the legal ownership is transferred to the buyer; in the case of a lease, the lessor would remain the legal owner).

However, from an economic perspective the economic ownership is transferred in both cases to the buyer or lessee, respectively, because all essential rewards and risks are transferred to him. Therefore, from the viewpoint of substance over form the remaining economic life has a greater significance for the classification of the asset than the economic life (Kümpel *et al.*, 2006, pp. 38–40). The exact meaning of the term “major part of the economic life” is, due to its imprecise formulation, controversial even in practice and in relevant literature (Sabel, 2006, pp. 62–63; Kümpel *et al.*, 2006, pp. 39–40; Alvarez, Wotschofsky, Miethig, 2001, p. 935). The scope of the value, discussed in the German professional literature, spans from “more than 50% to 75% and as far as up to 90%” of the economic life. This leaves considerable room for discretion and interpretation (Helmschrott, 2000a, pp. 426–429; Alvarez *et al.*, 2001, p. 937; Vater, 2002, p. 2094; Esser, 2005, p. 432). Here we need to remember again that the IASB has refrained from suggesting or deciding limits on purpose, in order not to restrict the holistic economic approach that focuses on the individual case (Kümpel *et al.*, 2006, p. 40; Sabel, 2006, p. 63).

Recovery of Investment Test. If the recovery of an investment test reveals that the present value of the minimum lease payments amounts to at least substantially all of the fair value of the leased asset, then a transfer of the economic ownership to the lessee is assumed in accordance with the IAS 17.10d, and thus a finance lease is assumed. The meaning of the term “at least substantially of the fair value” is not clear, due to its vague formulation in the literature and practice (Alvarez *et al.*, 2001, pp. 938–939). The scope of the limits discussed in the literature starts from “more than 90%” to 95% and goes as far as 99% of the fair value of the leased item. Thus, a significant scope of discretion exists. If in the comparable US GAAP regulation (SFAS 13.7d) as a clue is used, “more than 90%” limit, or even better the 95% limit would appear as the appropriate lower limit (Sabel, 2006, p. 64; Findeisen, 2002, p. 64; Mellwig, 1998, p. 9). However, we need to be reminded again that the IASB has waived the naming and fixing of exact limits on purpose, in order not to restrict the holistic and economic approach that deals with each case individually (Kümpel *et al.*, 2006, p. 40; Sabel, 2006, p. 63; Engel-Ciric, 2003, p. 397).

To calculate the present value of the minimum lease payments, both parties need to know the fair value of the leased asset, the contractually agreed number and amount of the rental installments, the dates of the payment and the corresponding contract period (including optional time periods if exercising these options appears reasonably certain), and, of course, they need to know the applicable discounting interest rate (Kümpel *et al.*, 2006, p. 42; Sabel, 2006, pp. 64–65). The fair value is the amount that independent contract partners who are experts and willing to conclude a contract would agree on for the transfer of ownership. Minimum lease payments according to the IAS 17.4 are the payments over the lease term that the lessee is or can be required to make, excluding contingent lease, costs for services and taxes paid by and reimbursed to the lessor. Contingent lease payments, such as payments for services and taxes that do not fulfill the definition of minimum lease payments, are not considered a part of the minimum lease payments due to their volatility and uncertainty. Thus, according to the economic approach, they cannot be included in the recovery of investment test (Kümpel *et al.*, 2006, pp. 43–46; Sabel, 2006, pp. 64–65; Mellwig, 2001, p. 304). The same explanation applies to why clauses regarding the index, guaranteed value or interest adjustments are part of the contingent lease payments (Kümpel, *et al.*, 2006, pp. 44–46). The situation is different with leased items, which have not yet been manufactured and thus their final investment amount cannot be decided exactly. Agreements, which due to their insufficient determinability have been declared as contingent lease payments, must be declared as minimum lease payments and be deemed to have taken place at the inception of the lease treated as if they had existed already at the beginning of the lease agreement in accordance with the IAS 17.5. It has to be noted that both the minimum lease payments and the applicable discounting rate are defined differently (according to the IAS 17) by the lessor and the

lessee, and thus the recovery of investment test can lead to different results at the two contract parties.

The duration period of the lease agreement (discounting period) normally corresponds with the basic rental period, plus an optional extension, whereby the basic rental period according to the IAS 17.4 is the earlier of the date of lease agreement and the date of commitment by the parties to the principal provision of the lease.

To allow a comparison of the present value of the minimum lease payments with the fair value, both parties have to determine a discounting rate at which the minimum payments have to be discounted. The current opinion according to the IAS 17.36 in conjunction with the IAS 17.4 (net investment in the lease) is to apply the interest rate implicit in the lease, although this is not clearly obvious from the IAS 17.7 – IAS 17.19. The interest rate applied in the lease agreement is defined in the IAS 17.4 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. Since determining the interest rate is very difficult for the lessee due to a lack of information, and since estimations are not permitted, the lessee can use the lessee's incremental borrowing rate of interest. Incremental borrowing rate (IAS 17.4) of interest is the rate of interest would have to pay on a similar lease or, if that is not determinable, the rate that, at the inception of the lease, the lessee would incur to borrow over a similar term and with a similar security, the funds necessary to purchase the asset.

If it turns out that the calculated net present value of the minimum lease payments is approximately the same as the fair value of the leased item, the transfer of the economic ownership and consequently a finance lease, has to be assumed. In this case the investment risk of the lessor will be (almost) completely transferred to the lessee. Only a risk of credit worthiness remains with the lessor, and this underpins the assumption of a finance lease. In this concrete case it must also be checked whether the basics of the IAS 17 are observed, i.e. whether all essential risks and rewards are transferred to the lessee. If this is not the case, the classification of the leased asset to the lessee would not be correct (Sabel, 2006, pp. 66–67; Kümpel *et al.*, 2006, pp. 59–62; Weiss, 2006, pp. 59–60). “Therefore it can be argued that even the recovery of investment test does not necessarily lead to an automatism but must be evaluated together with the results of other criteria” (Sabel, 2006, p. 67; Kümpel *et al.*, 2006, p. 61).

Special Lease. The example in the IAS 17.10e describes the case of a special lease, which means that the leased assets have a specialized nature that only the

lessee can use them without major modification. Because the leased asset cannot be used by the third persons it can be assumed that after the expiry of the basic rental period no further rewards exist and no profits can be earned by the lessor. Therefore it can also be assumed that the lessor wants to have all investment costs amortized during the basic rental period, including the interest. In this case the rewards are transferred to the lessee, and thus, the classification as a finance lease can be justified (Alvarez *et al.*, 2001, p. 939). If the essential rewards and risks were not transferred to the lessee, a classification as a special lease, and consequently as finance lease, would not be justified. What is decisive for the assessment and capitalization of the leased asset is therefore the holistic and economic approach, which considers the individual case, and the regulations agreed in the contract (Sabel, 2006, p. 57, pp. 73–74; Kümpel *et al.*, 2006, pp. 64–65; Weiss, 2006, p. 60; Lüdenbach *et al.*, 2006, pp. 262–264; Kirsch, 2003, p. 500; Riedel-Stegner, 2006, pp. 115–117).

2.3.4. Classification Criteria (Indicators)

Losses in Cases of Cancellation. In addition to the examples in the IAS 17.10 further indicators are listed in the IAS 17.11, which either alone or in combination might point to the classification as a finance lease. If the lessee has a right of cancellation (IAS 17.11a), and in connection with it, the obligation to cover all possible costs of the lessor, then such an economic dictate is considered an indicator for a finance lease because in this case the lessee fully carries the investment risks. In a similar way as with the recovery of the investment test, the IAS 17.11a only focuses on the risks and not on the rewards connected with the leased asset, and thus it has to be assessed critically. If it should, for example, turn out that the essential rewards remain with the lessor, then the capitalization of the leased asset by the lessee would not be justifiable.⁶ The differentiation in the IAS 17.10 and the IAS 17.11 between the examples and the indicators is not explained in the standard or in the interpretations. In the literature, however, it is assumed that the indicators are a weaker form of the classification assessment than the given examples. Therefore, regarding all the given examples and indicators, a flexible, holistic and economic overall appreciation of the circumstances with attention paid to the individual case, is target aimed, not an automatism (Mellwig, 1998, p. 6; Sabel, 2006, p. 74; Kümpel *et al.*, 2006, pp. 65–67; Weiss, 2006, p. 60; Pellens *et al.*, 2006, p. 595; Vater, 2002, p. 2096).

Gains or Losses on Fluctuations in the Residual Value. If a lessee assumes responsibility for the gains and losses on fluctuations in the residual value for the remaining time, then this is also an indicator for the classification of a finance lease. According to the IAS 17.8 a contract for a finance lease has to be declared in this case, if substantially all the risks and rewards in connection with the

⁶See IAS 17.8.

ownership are transferred to the lessee. The same applies if the lessee holds substantially all the risks and rewards at the end of the lease agreement, for example, if a residual value guarantee of the lessee is agreed in the contract. If however, the contract is made in such a way that the lessor is entitled to some relevant remaining rewards and remaining risks (or to a certain part of them) at the end of the basic rental period, then the assessment and classification of these rewards and risks has to be carried out with the help of the economic approach. Should the economic and holistic assessment of the circumstances reveal that the essential rewards and risks were not transferred to the lessee an operating lease has to be assumed. This economic assessment can also lead to a significant leeway of discretion and interpretation, since no quantitative limits for the assessment of the rewards and risks are stipulated in IAS/IFRS. Moreover it should be highlighted “that it is not a formal transfer of the rewards and risks to the lessee that matters, but the economic transfer. This is probably the reason why the IAS 17.11b does not demand the allocation of gains or losses to the lessee if a finance lease is assumed” (Kümpel *et al.*, 2006, p. 70). The transfer of gains or losses, which arise through fluctuations of the fair value, can be the decisive criterion according to the IAS 17.11b for the classification of the leased asset to the lessee.

Favorable Rent Extension Option. Similarly to the bargain purchase option according to the IAS 17.10b, the favorable rent extension option has to be checked, whether the lease agreement provides for the lessee the opportunity to extend the lease agreement at a substantially lower than market rent. Based on this option, which can be compared with the German decrees of leases, the certain extension of the contract can be assumed by the exercise of the option, due to economic dictates. The classification as a finance lease with sufficient certainty that the essential rewards and risks are transferred to the lessee is asserted. Again, there is a need to emphasize that such examples and indicators by themselves cannot give conclusive information regarding their classification; they only serve as clues for the classification of leasing agreements. In any case, a flexible, holistic and economic overall assessment that considers the individual case is reasonable and target aimed, and thus, should be applied (Kümpel *et al.*, 2006, pp. 72–73; Sabel, 2006, p. 76; Weiss, 2006, p. 61; Küting *et al.*, 2006, p. 651).

2.3.5. Consequences of Changes to the Contract Conditions

According to the principles of the IAS 17.13 the lease classification has to be decided at the beginning of the leasing agreement. However, if the contract conditions are changed, the following three facts have to be considered. The first case concerns subsequent changes in the provisions of the lease. Although in the IAS and also in the praxis different opinions exist regarding the delimitation of these indicators, according the current opinion the following

cases fall into this category: subsequently agreed purchase options, residual value guarantees, extending or shortening the duration period, and subsequently agreed changes to the lease installments (IAS 17.10).

The second case concerns the economic renewal of the lease. If seen in retrospect, the leasing agreement would have been classified differently on the basis of the newly applied contract conditions. If this actually is true from the substance over form perspective, such a leasing agreement has to be classified a new – by including all new insights (Kümpel *et al.*, 2006, p. 76).

The third case concerns changes of assessments or framework and market conditions (changes in estimates or changes in circumstances). If it becomes clear – with the help of the economic approach – that the stated amounts at the first assessment – such as the credit worthiness of the lessee or the economic, legal, or technical framework conditions – have changed, then there is no need for a new classification of the leasing agreement according to the IAS 17.13.

2.3.6. Special Classification Regulations for Real Estate Lease Agreements

If the lease contract concerns both land building element, an entity assesses the classification of each element as a finance or an operation lease separately (IAS 17.15A). In determining whether the land element is an operating or finance lease, an important consideration is that land normally has an indefinite economic life. The minimum lease payments are allocated between the land and the building elements in proportion to the relative fair values. If the lease payment cannot be allocated reliably between two elements, the entire lease is classified as a finance lease. This allocation is also referred to as the new allocation rule, because already before the revision of the IAS 17 by the improvements project an allocation key was used. But if both elements do not fulfill the criteria of a finance lease then entire lease is classified as an operating lease (IAS 17.16).

According to the IAS 17.17, if the share of the land is immaterial in relation to the whole value of the leased asset, then the leased asset has to remain as one unit and not be divided. The unified classification of the leased asset is then based on the assessment of the economic life of the building. The IASB leaves out quantitative limits on purpose and leaves the assessment to the economic overall evaluation. In principle it is not permitted to replace qualitative criteria of the IAS 17.10c and the IAS 17.10d, by referring to the opening clause of the IAS 8.12, by using the quantitative limits from the US GAAP (Sabel, 2006, p. 98; Schimmelschmidt *et al.*, 2004, p. 5).

If a leased asset is purchased and capitalized by a lessee as investment property, the special regulation of the IAS 40 has to be observed. According to this standard the lessee can capitalize the leased asset in his balance sheet (right of choice) as a financial lease, although it had been classified as an operating lease. Furthermore, according to the IAS 17.19 a lease agreement can be capitalized as a finance lease, even if the investment property due to later events can no longer be classified as financial investment. Corresponding examples are found in the IAS 17.19a and the IAS 17.19b.

If it concerns large scale and very cost intensive lease contracts, e.g. with airplanes and ships, often a new leased item is specially manufactured. This unit, which is created for tax reasons, serves only one client (the lessee) and probably has restricted decision making. Therefore it must be checked, whether the lessee controls this special purpose entity and whether this is a parent subsidiary construction according to the IAS 27. If this is the case, the lessee has to include this special purpose entity in his balance sheet (Kümpel *et al.*, 2006, pp. 88–89). Therefore, to assure the desired off balance sheet effect (exclusion of the leased asset in the balance sheet of the lessee) at the lessee, neither the economic ownership can be transferred nor must an obligation of consolidation due to the parent subsidiary relationship exist. According to the SIC 12.8 the examination of the formal criteria of the IAS 27.13 requires a holistic and economic way of looking at it, with attention given to the individual case. The SIC 12.10 provides four indicators for the examination of these criteria, which are meant to help with the assessment and serve as a clue as to whether an obligation for consolidation exists. Here, the so called risk and reward approach is applied. It has to be clarified, whether the lessee holds the majority of the rewards and risks in the special purpose entity, “and/or whether the residual claims and/or risks, that are specific for an owner, can be attributed to the lessee” (Kümpel *et al.*, 2006, p. 89).

2.4. Critical Appreciation of the IAS 17

The regulations of the IAS 17 provide references with regard to the classification of lease contracts or the capitalization of leased assets, respectively, which follows primarily, similar to the HGB, the risk and reward approach (Esser, 2005, pp. 431–433; Vater, 2002, p. 2100; Sabel, 2006, p. 157). This approach seeks to identify the economic owner of the leased asset by classification of the essential rewards and risks. Unlike in the German Commercial Law, there is no need to refute the assumption that the legal owner is also the economic owner at the same time (Sabel, 2006, p. 97; Mellwig, 1998, p. 7; Kümpel *et al.*, 2006, p. 93).

The legal ownership is therefore irrelevant for the classification of the leased asset. The only aspect that matters is the capitalization of the asset to the economic owner, or the transfer of the essential rewards and risks respectively,

regarding the leased asset (general rule of the IAS 17.8). In other words, what matters is the economic content of the lease contract (IAS 17.21). This shows that the substance over form approach according to IAS/IFRS is rated higher and much more distinct than the economic approach of the HGB (Sabel, 2006, p. 97).

The division into examples and indicators highlights the difference in their importance, although they are closely connected with each other. Both, mentioning the examples, which are relevant for the classification, and the inclusion of the indicators in the IAS 17, serve mainly as tools for the capitalization of leased assets and should not lead to an automatism under any circumstances. Especially the overall appreciation in the IAS 17 of a holistic, flexible, and economic overall assessment, with consideration given to the individual case, cannot be replaced in the process of capitalization a (leased) asset (Sabel, 2006, p. 57 and pp. 97–98; Kümpel *et al.*, 2006, pp. 93–95; Vater, 2002, p. 2096; Schimmelschmidt *et al.*, 2004, p. 12).

This highlights also the intentional guideline of qualitative and not quantitative limits. The qualitative formulation is intended to provide certain flexibility so that the overall economic perspective is not limited through some randomly selected and misleading values (Riedel-Stegner, 2006, pp. 99–100; Mellwig, 1998, p. 1). Consequently, there is no regulative gap in accordance with IAS 8.12. For this reason it is not permitted, although in the praxis it often happens, to refer to quantitative limits of comparable standards (e.g. those of the US GAAP). Although the guidelines for qualitative limits result in significant room for description and legal uncertainty, the IASB accepts this, also for the sake of the required overall assessment (substance over form).

Due to the wide variety of choices and due to the subjective evaluations in the balance sheets, lease contracts could be classified differently – something that should definitely not happen, since it would result in legal uncertainty. “Therefore the criteria in the IAS 17 are impractical for the classification” (Sabel, 2006, p. 100). However, attention must be paid to the fact that the use of the limits according to the US GAAP would trigger an automatism with regards to the contract classification, and that is exactly what the IAS 17 does not want (Sabel, 2006, pp. 98–100; Vater, 2002, p. 2095).

A general problem of the quantitative limits is the intentional marginally lower deviation of the limits, the misleading result of which is that they are no longer classified as finance leases since the limits would trigger an automatism with regard to the contract classification. This problem could actually be eliminated if IAS/IFRS introduced nonbinding limits as indicators, whereby these indicators would only serve as a tool, while the economic approach would still remain obligatory (Vater, 2002, p. 2096).

Determining the economic owner without quantitative limits can turn out to be complicated and subjective for several reasons. The huge number of possibilities in the setting up of contracts, including the many layers of regulations, makes the determination of the economic owner a lot more difficult (Esser, 2005, p. 431; Weinstock, 2000, p. 185). Furthermore, many variables have to be estimated and incomplete information has to be dealt with, and thus, significant variety of choices is created in the process. This uncertainty results in an actual right of choice regarding the capitalization, because subjective estimates can be included in the classification and thus, those who prepare the balance sheet can decide by themselves, how and where to classify the leased asset (Vater, 2002, p. 2099; Kümpel *et al.*, 2006, p. 207). In the extreme cases such a subjective classification of leased assets the “double capitalization” or in a so-called “double non-capitalization” situation can result. This phenomenon can occur, if, for example, the fair value of the same leased asset is evaluated differently by the lessor and the lessee, or if the valuation takes place at different moments and therefore produces different results. This illustrates the lack of legal certainty of the IAS 17 and its factual inapplicability.

As has been stated already, lease contracts are classified into finance leases (hire purchase) and operating leases (tenancy agreement). Due to this distinction, the residual value guarantees or options, often found in lease agreements, are not properly presented in the balance sheets” (Sabel, 2006, p. 100). This is so because also in the case of a finance lease it can be agreed in principle that the leased asset will be returned to the lessor after the expiry of the basic rental period (legal owner), and thus, the lessor has a guaranteed receivable to the residual value. Nevertheless, the balance sheet of the lessor does not include a residual value, which can lead to a violation of the principle of differentiation (Sabel, 2006, p. 101; Vater, 2002, p. 2099). In a finance lease the residual value is treated like a lease payment. The lessee includes the contractually agreed residual value guarantee fully in his liabilities.

On the other hand, the lessor capitalizes this guaranteed residual value as the liability. This has to be considered a violation of the basic values and principles of the IAS/IFRS (Sabel, 2006, p. 87, p. 100). But the situation regarding to an operating lease is different. The lessee does not treat the residual value as lease payments, at least not as long as the lessee is not threatened by a likely burden (Sabel, 2006, p. 100).

Some criticism is due, for example, in the case of a purchase option, where the exercise of the option is already assumed if it is considered as “favorable”. “The freedom of choice offered by the option is not taken into consideration. Options that are not considered favorable will not be included in the balance sheet, although they normally have a certain value” (Sabel, 2006, pp. 100–101).

2.5. Criticism of the All or Nothing Approach and Outlook

As has been shown in the previous subchapters, the IAS 17 has significant weaknesses and ambiguities, which have been recognized and criticized by the IASB itself. Enormous problems arise in practice, due to the lack of information on the all or nothing approach. According to the all or nothing approach (see Figure 10), an asset or a leased asset will be capitalized by one of the two leasing partners; a partial capitalization is not possible (Sabel, 2006, p. 101; Waßmer *et al.*, 2000, p. 2025; Brakensiek, 2001, p. 205). Due to the distinct off balance sheet efforts of enterprises, and due to the possibilities regarding the structure of lease contracts and the interpretation concerning the parameters, today one finds almost only lease contracts that are classified as operating leases, which means they are capitalized by the lessor (Sabel, 2006, p. 101; Kümpel *et al.*, 2006, p. 208; Schimmelschmidt *et al.*, 2004, p. 1). In such a case the lessee enjoys all the advantages of the leased asset and has the legal right of use to the leased item. But he does not have to recognize it in the balance sheet, and consequently his balance sheet analysis appears better than in the case of a hire purchase (Sabel, 2006, pp. 1–3). “Since in practice the capitalization of operating leases is often made good for later in the balance sheet analysis (Brakensiek, 2001, p. 206), the question arises whether their non-disclosure fulfills the stock market information obligation of the IAS/IFRS balance sheet” (Sabel, 2006, p. 101).

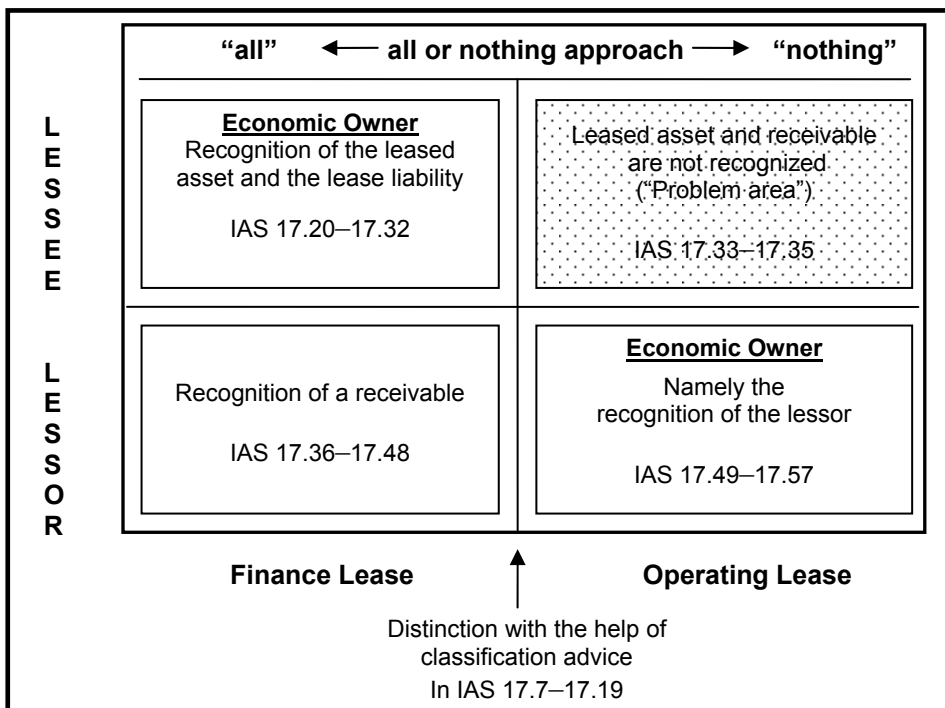


Figure 10. All or nothing approach according to the IAS 17

Source: Fülbier *et al.*, 2005, p. 277

In 2002 the IASB initiated a long-term research project, based on the awareness of the problems of the all or nothing approach, with the task of developing a new concept for the capitalization of leases, and/or to develop a new IAS/IFRS leasing, respectively. Besides the all or nothing approach, two additional approaches were discussed and evaluated. One of these is the so-called financial components approach. This approach, favored by many, suggests a completely new basic concept for leases. “This approach, at its core, includes the concept that leased assets will no longer be classified as tangible assets to the economic owner (Kümpel *et al.*, 2006, p. 209). In this case the lessee capitalizes only the legal right of use of the leased item and the corresponding lease liabilities, both at the present value of the minimum lease payments. Consequently, all lease agreements would be classified as finance leases, whereby however, instead of the leased asset an intangible asset, with obligatory amortization, would be capitalized. The financial components approach is mainly oriented towards the basic idea of the McGregor-papers and at the so called Tweedie-outline (Brakensiek, 2001, p. 211). As a second possible concept the whole asset approach is currently discussed as well. This approach suggests the continuation of the capitalization of assets, instead of legal rights of use; however, the lessee has to capitalize the leased asset at its fair value at all times. This would mostly constitute a finance lease, with the difference that the temporal duration period does not play any role with regards to the attributed value (Fülbier *et al.*, 2005, p. 281).

In summary it can be stated that new concepts are at work because the current IAS 17 contains too many problems and uncertainties. The proposal under discussion so far will probably not result in enormous improvements since, in essence, no new information is available (Kümpel *et al.*, 2006, p. 211). In addition, it is also clear that leasing as a financing alternative will not lose its attractiveness, whatever the intended modifications might be.

2.6. Interim Conclusion

The economic approach according to the German commercial law as a type of application of the teleological method of finding justice has experienced, contrary to the substance over form, profound theoretical discussion over many years. Nevertheless, the economic approach in accordance with commercial law and the concept of substance over form have many similarities in their contents. Both reject the capitalization purely according to civil law and refer to the economic significance and the factual economic conditions – the actual intention of a process. In both systems of capitalization the economic approach and the substance over form are valued highly. However, according to the HGB and the IAS 17 they are understood and applied in different ways. These differences apply especially when it comes to the identification of the economic owner. According to the German Commercial Law, only the remaining rewards after

expiry of the basic rental period matter. In contrast, according to the IAS 17 the rewards and risks during the basic rental period are considered for the classification.

The lease capitalization according to the HGB regarding the classification of the leased asset follows fiscal regulations; the fundamental reference normative for determining the economic owner is the § 39 of the AO. The leasing decrees contain quantitative limits, the result of which is that quantitative classification criteria are applied in the determination of the economic owner and whether it is an operating or finance lease. These partially arbitrarily set limits guarantee legal certainty and planning, and thus, there is no room for interpretation. However, they allow for a narrow intentional lower deviation, which allows the capitalization to be done by the lessor and a non-capitalization by the lessee (the so-called off balance sheet financing).

According to the IAS 17 the economic owner is identified with the help of the so called risk and reward approach. In this case the classification of the leased asset follows qualitative criteria respectively. These, however, allow significant room for discretion and interpretation, either for an operating or finance lease. Regarding the IAS 17 there is no need to disprove the fundamental assumption that the legal owner is also the economic owner at the same time. According to the IAS 17 the ownership by civil law is not relevant for the capitalization of the leased asset. The only issue is the capitalization of the asset to the economic owner or the transfer of the essential rewards and risks during the basic rental period, namely the actual economic content of the lease contract. The IAS 17 provides examples and indicators as tools for the identification of the economic owner, but they do not have definite character and are meant only to serve as clues. The uncertainty of the qualitative criteria constitutes an actual right of choice with regards to capitalization, because subjective assessments and classifications can be applied. The leasing partners can decide themselves, how and where to classify the leased asset. Because the current IAS 17 and especially all or nothing approach applied in it have considerable shortcomings and weaknesses, a new concept has been a work in progress for some years. According to the all or nothing approach, which is still in use today, a leased asset is either completely or not at all capitalized with one of the leasing contract partners. The new, but not yet applied, approach suggests that leased assets are no longer classified as tangible fixed assets to the economic owner, but instead will be amortized as the intangible legal right of use. These suggestions under discussion, however, will probably not result in enormous improvements, because no fundamentally new information is available. In addition, it is clear that leasing as a finance alternative will not lose its attractiveness due the planned modifications. It has to be seen whether such a concept will actually provide new and better information, especially if one considers the strong leasing lobby.

In conclusion, it can be stated that the economic approach regarding the two systems of capitalization plays a very important role and always tries to portray the actual economic situation of an enterprise and interpret laws according to their actual meaning and purpose. However, it is interpreted differently in the two systems. Perhaps a combination of the quantitative and qualitative criteria would make sense, in order to combine the respective advantages and thus improve the communication of information; this is even more so against the background of the depiction of lease agreements and the harmonization of international accounting.

3. CAPITALIZATION OF LEASES ACCORDING TO THE US GAAP

3.1. Conceptual Foundations

The term “GAAP” is an abbreviation for **Generally Accepted Accounting Principles (GAAP)**. Generally Accepted Accounting Principles refer to the standard framework of guidelines for financial accounting used in any given jurisdiction; generally known as **accounting standards**. GAAP includes the standards, conventions, and rules accountants follow in recording and summarizing, and in the preparation of financial statements. In the United States, Generally Accepted Accounting Principles are accounting rules used to prepare, present, and report financial statements for a wide variety of entities, including publicly traded and privately held companies, non-profit organizations, and governments⁷.

The term “GAAP” confined to the United States is commonly abbreviated as **US GAAP** or **U.S. GAAP** or simply **GAAP**. Similar to many other countries practicing under the common law system, the United States government does not directly set accounting standards, in the belief that the private sector has better knowledge and resources. The US GAAP is not written in law, although the U.S. Securities and Exchange Commission (SEC) requires that it be followed in financial reporting by publicly traded companies.

The various rules and pronouncements come from the Financial Accounting Standards Board (FASB) which is the highest authority in establishing generally accepted accounting principles for public and private companies, as well as non-profit entities.

The rules and procedures for reporting under GAAP are complex and have been developed over a long period of time. The US GAAP is composed of a mixture of over 2,000 documents that have developed over the last 60 years or so. As might be expected, the documents that comprise GAAP vary in format, completeness, and structure. In some cases, these documents are inconsistent and difficult to interpret. As a result, sometimes financial statement preparers are not sure whether they have the right GAAP; determining what is authoritative and what is not have been difficult. In response to these concerns, on June 3, 2009 the FASB approved the Financial Accounting Standards Board **Accounting Standards Codification** (or more simply “the Codification”) and issued FASB 168 (the Hierarchy of Generally Accepted Accounting Principles – A Replacement of FASB Statement No. 162) (*ASC 105–10*). The Codification is organized into eight main topics and approximately ninety subtopics. The

⁷ The concept of such a set of written principles originates in the USA, although the abbreviation is used in reference to other countries also.

Codification is not intended to change the existing US GAAP, but rather integrates the existing accounting standards by multiple standard-setters within the current GAAP hierarchy. The Codification is now the single official source of authoritative nongovernmental US GAAP, superseding the existing FASB, AICPA, EITF, and related literature. Furthermore the US GAAP will no longer be issued in the form of an “accounting standard”, but rather as an update to the applicable “topic” or “subtopic” within the Codification. To provide easy access to the Codification, the FASB also developed the Financial Accounting Standards Board Codification Research System (CRS). CRS is an online, real-time database that provides easy access to the Codification. If the Codification does not cover a certain type of transaction or event, other accounting literature should be considered, such as FASB concept statements, the International Financial Reporting Standards, and other professional literature.

There exist several differences between the US GAAP and the International GAAP now used by a majority of countries around the world. For instance, according to the International GAAP LIFO (Last in First out) and extraordinary items are prohibited. Note that by prohibiting extraordinary items, the International GAAP also differs in how EPS is reported on the Income Statement. This and many other differences affect the way investors, analysts, creditors, government agencies, and businesses analyze financial statements. The same is true in leasing matters. The overall accounting for leases under the US GAAP and the International GAAP is similar. Both focus on classifying leases as either capital/finance or operating and both separately discuss lessee and lessor accounting. Both require the party that bears substantially all the risks and rewards of ownership of the leased property to recognize a leased asset and the corresponding liability and specify the criteria (US GAAP) or indicators (International GAAP) to make this determination. However, to enable a comparison of the US GAAP capitalization/noncapitalization of leases with the IFRS capitalization/noncapitalization, some of the relevant differences between the two accounting standards should be identified.

Accounting for leases in the United States has been regulated by the Financial Accounting Standard No 13 Accounting for Leases (SFAS 13) issued in 1976, which became effective as of January 1, 1977. In fact, SFAS 13 was the most complex accounting standard issued up to its time. It has been amended several times, for instance by SFAS 22, SFAS 23, SFAS 27, SFAS 28, SFAS 29, SFAS 98, and SFAS 121. In addition, numerous interpretations and technical bulletins have been issued giving additional guidance. Previously labeled as section L10 in the FASB Current Text, the new FASB Codification uses section *ASC 840* for the entire lease accounting rules and guidelines. So the fundamental rules regarding the capitalization of lease agreements are constituted in the section **Accounting Standards Codification 840**, also known as **FASB ASC 840** or simply **ASC 840**.

Much of the terminology for lease accounting in the International GAAP and the US GAAP is the same. One difference is that finance leases are referred to as **capital leases** in the US GAAP. In special literature *capitalization* means “recording of a cost as a fixed asset”. So the original form of the term “capital lease” should be **capitalized** lease:

capitalized lease → capital(ized) lease → capital lease.

There are some differences in short definitions/explanations of capital lease in specialized dictionaries published in the United States (Table 2).

Table 2. Some Short Definitions/explanations of the Term “Capital Lease”

Definition/explanation	Source
One in which the lessee obtains significant property rights.	Siegel, J. G., <i>et al.</i> (2010). Dictionary of Accounting Terms. Fifth edition. New York: BARRON'S.
A lease that is treated like a purchase of an asset even if it is called a lease.	Mooney, K. (2008). The Essential Accounting Dictionary. Naperville: Sphinx Publishing.
A lease that “in substance” is a purchase and financing arrangement.	http://www.accountingcoach.com/terms/C/capital-lease.html
A lease in which the ownership of the leased asset is transferred to the lessee at the end of the base period.	Wanjialin, G. (2004). An International Dictionary of Accounting & Taxation. Lincoln: iUniverse.
A lease in which the lessor only finances the lease, and all other rights of ownership transfer to the lessee, resulting in the recording of the asset as the lessee's property in its general ledger.	http://www.accountingtools.com/definition-capital-lease
A lease obligation that has to be capitalized on the balance sheet.	http://www.ventureline.com/accounting-glossary/C/capital-lease-definition/
Long term lease of capital equipment that for accounting purposes is treated as a borrowing of funds and a balance sheet asset to be amortized.	Fitch, T. P. (1990). Dictionary of Banking Terms. New York: BARRON'S.
A long-term lease in which the lessee must record the leased item as an asset on his/her balance sheet and record the present value of the lease payments as debt.	Farlex Financial Dictionary. © 2011 Farlex, Inc. All Rights Reserved
A long-term lease contract, structured in conventional or leveraged form, where the LESSEE accepts most/all of the RISKS and benefits of the leased property.	http://finance-dictionary.com/definition/c/capital-lease/
A lease in which the lessee obtains some ownership rights over the asset involved in the transaction, resulting in the recording of the asset as company property in its general ledger.	http://www.finance-lib.com/financial-term-capital-lease.html
Fixed-term (and usually non-cancelable) lease that is similar to a loan agreement for purchase of a capital asset on installments.	http://www.financialtermsdictionary.com/terms/11099-capital-lease.html

A lease that is treated as though the lessee had borrowed money and bought the leased assets.	http://www.qfinance.com/dictionary/capital-lease
A lease that transfers substantially all of the benefits and risk incident to the ownership of property.	Oldham, G. E. (1993). Dictionary of Business and Finance Terms. New York: Barnes & Nobles Books.
The lease shown in a firm's balance sheet as an asset and corresponding liability.	Rosenberg, J. M. (1986). The Investor's Dictionary. New York: John Wiley & Sons.
A lease considered to have the economic characteristics of asset ownership.	http://www.investopedia.com/terms/c/capitallease.asp#axzz1p5vpTSgf
A lease that in an economically substantial way transfers nearly all of the risk and rewards inherent in the leased property to the lessee.	http://invest.yourdictionary.com/capital-lease
The long-term lease of a capital asset.	Scott, D. L. (2003b). Wall Street Words: An A to Z Guide to Investment Terms for Today's Investor. New York: Houghton Mifflin Harcourt. Scott, D. L. (2003a). The American Heritage Dictionary of Business Terms. New York: Houghton Mifflin Harcourt.
The long-term lease of a capital asset.	http://business.yourdictionary.com/capital-lease
Lease that must be reflected on a company's balance sheet as an asset and corresponding liability.	Friedman, J. P. (2007). Dictionary of Business Terms. Fourth edition. BARRON'S.
Fixed-term (and usually non-cancelable) lease that is similar to a loan agreement for purchase of a capital asset on installments.	http://www.businessdictionary.com/definition/capital-lease.html
Lease that has the economic characteristic of asset ownership.	http://definitions.uslegal.com/c/capital-lease-gaming-law/
Lease of business equipment which represents ownership and is reflected on the company's balance sheet as an asset.	Murray, J. Capital Lease.

Source: compiled by the author

The abovementioned short definitions/explanations of capital leases could be classified by using the following criteria:

Definitions which pay attention to the type of transaction, emphasizing that the capital lease is a **purchase and financing agreement**: "...is a purchase and financing arrangement" (<http://www.accountingcoach.com/terms/C/capital-lease.html>), "...that is similar to a loan agreement for purchase ..." (<http://www.financialtermsdictionary.com/terms/11099-capital-lease.html>). Some dictionaries emphasize the capitalization (reflection in the balance sheet) of capital lease: "... recording of the asset as the lessee's property in its general ledger" (<http://www.accountingtools.com/definition-capital-lease>), "...the lease shown of a firm's balance sheet as an asset and corresponding liability" (Rosenberg, J. M. 1986), "...lease that must be reflected on a company's balance sheet as an asset and corresponding liability (Friedman, J. P. 2007). Some dictionaries emphasize the importance of similarity to (economic) ownership:

“... significant property rights...” (Siegel, *et al* 2010), “... some ownership rights over the asset ...” (<http://www.finance-lib.com>), “... the economic characteristics of asset ownership ...” (<http://www.investopedia.com/terms/c/capitallease.asp#axzz1p5vpTSgf>). The finance, investment and business dictionaries, but not so many accounting dictionaries, stress the economic substance of the capital lease: “... LESSEE accepts most/all of the RISKS and benefits of the leased property” (<http://finance-dictionary.com/definition/c/capital-lease/>), “... a lease that transfers substantially all of the benefits and risk incident to the ownership of property” (Oldham, G. E. 1993), “... A lease that in an economically substantial way transfers nearly all of the risk and rewards inherent in the leased property to the lessee” (<http://invest.yourdictionary.com/capital-lease>).

3.2. Classification Criteria According to ASC 840

The classification of lease agreements has to be made by the two contract parties, independently of each other, on the basis of the information available.

The accounting profession recognizes leases as either an operating lease or a capital lease. Capital leases are lease agreements where essentially all benefits and risks in connection with the leased asset are transferred to the lessee. Since the differentiation follows an **economic approach** (substance over form), the transfer of the legal ownership is not necessary. Contrary to the contract classification according to the IFRS, the classification criteria laid down for the lessor and the lessee are not identical in the US GAAP. To distinguish the two, the FASB provided criteria for when a lease should be capitalized (ASC 840-10-25 Recognition):

Transfer of ownership. The lessor transfers ownership of the property to the lessee at the end of the lease term. This criterion is met in situations in which the lease agreement provides for the transfer of title at or shortly after the end of the lease term in exchange for the payment of a nominal fee. If the transfer of the legal ownership at the end of the lease term is reasonably certain, the leased asset must be depreciated during the remaining economic life.

Bargain purchase option. The lease contains a bargain purchase option. This is an option that allows the lessee, upon termination of the lease, to purchase the leased asset at a price significantly lower than the expected fair value of the asset. Exercise of the option must appear reasonably assured at the inception of the lease. If this criterion is met, the depreciation period is the economic life of the asset.

Lease term (economic life test). The lease term is equal to 75 per cent or more of the estimated economic life of the leased property. If this criterion is satisfied, the depreciation is realized during the lease term, under consideration of the

expected residual value. However, if the beginning of the lease term falls within the last 25 percent of the total estimated economic life of the leased property, including earlier years of use, this criterion shall not be used for purposes of classifying the lease. It is necessary to emphasize that determining the estimated economic life can pose problems, especially if the leased asset is a specialized item or has been used for a significant period of time.

Minimum lease payments (fair market test). At the beginning of the lease term the present value of the minimum lease payments, excluding that portion of the payments representing executor costs such as insurance, maintenance, and taxes to be paid by the lessor, including any profit thereon, is equal to or greater than 90 percent of the excess of the fair value of the leased property to the lessor at lease inception over any related investment tax credit retained by the lessor and expected to be realized by the lessor. If the beginning of the lease term falls within the last 25 percent of the total estimated economic life of the leased property, including earlier years of use, this criterion shall not be used for purposes of classifying the lease. The lessee shall compute the present value of the minimum lease payments using his incremental borrowing rate⁸, unless it is practicable for him to learn the implicit rate computed by the lessor⁹ and the implicit rate computed by the lessor is less than the lessee's incremental borrowing rate. If both conditions are met, the lessee shall use the implicit rate. Lease payments that depend on a factor directly related to the future use of the leased property, such as machine hours of use or sales volume during the lease term, are contingent rentals and, accordingly, are excluded from minimum lease payments in their entirety. However, lease payments that depend on an existing index or rate, such as the consumer price index or the prime interest rate, shall be included in minimum lease payments based on the index or rate existing at lease inception; any increases or decreases in lease payments that result from subsequent changes in the index or rate are contingent rentals and thus affect the determination of income as accruable.

If this criterion is satisfied, the depreciation period is the life of the lease.

The four criteria correspond – with exceptions with the quantitative limits – with the listed examples for situations in the IAS 17.10 (a) – 17.10 (d), which according to the International GAAP normally lead to the classification of a lease into a finance lease. Regarding the **interpretation of the criteria** no

⁸ Incremental borrowing rate is defined as the rate that, at the inception of the lease, the lessee would have incurred to borrow the funds necessary to buy the leased asset on a secured loan with repayment terms similar to the payment schedule called for in the lease. (FASB Statement No. 13, para. 5 (1))

⁹ The interest rate implicit in the lease is the discount rate that, when applied to the minimum lease payments and any unguaranteed residual value accruing to the lessor, causes the aggregate present value to be equal to the fair value of the leased property to the lessor. Ibid., para. 5 (k).

fundamental differences to the IAS 17 exist. The classification of leases in accordance with the US GAAP is basically – analogous to the corresponding IFRS regulations – focused on the economic ownership of the leased asset (risk and reward approach). The classification resulting from capitalization according to the US GAAP also follows the all or nothing approach. Contrary to the International GAAP, if one of the criteria is fulfilled, the lease contract has to be classified as a capital lease by the lessee. The actual transfer of all essential rewards and risks in connection with the leased item does not have to be checked especially. If none of the criteria is fulfilled, it is always an operating lease for the lessee. The difference from the classification according to the IAS 17 lies in the automatism with regards to the contract classification and in stipulating quantitative limits.

For the lessee the classification process is then concluded. From the viewpoint of the lessor, however, the regulations of the *ASC 840-30 Capital Leases* have to be fulfilled cumulatively, in order to classify the lease agreement as a capital lease:

- collectibility of minimum lease payments is reasonably predictable;
- no important uncertainties surround the amount of unreimbursable costs yet to be incurred by the lessor under the lease.

If at least one criteria of *ASC 840-10-25 Recognition* and both criteria of *ASC 840-30 Capital Leases* for the lessor are fulfilled, the lessor is obliged to classify the lease agreement as capital lease.

As it was emphasized before, capital leases are regarded as essentially equivalent to a sale by the lessor, and a purchase by the lessee (even though the title remains with the lessor). Therefore, the lessee is placed in a position similar to that of an owner and the leased asset must be capitalized and shown in the lessee's balance sheet as a fixed asset with a corresponding non-current liability (lease payable). The capitalization generally follows the same way as in the case of a finance lease according to the IAS 17, following the capitalization model of a purchase that is financed by a loan. In accordance with SFAS 13.10 the leased asset and liability are capitalized (recorded) at the beginning of the lease term at the discounted value of the minimum lease payments plus the present value of any bargain purchase option. If the total present value of the payments and bargain purchase option exceeds the fair value of the leased asset, the asset must be shown at its fair market value. Thus, the performance neutral treatment of the assumed purchasing cost is assured (Brakensiek, 2001, p. 199).

In a capital lease transaction, the lessee is using the lease as a **source of financing**. The lessor finances the transaction through the leased asset, and the lessee makes rent payments, which actually are installment payments. Therefore, over the life of the property rented, the rental payments to the lessor constitute a

payment of principal plus interest. According to SFAS 13.12 during the lease term, each minimum lease payment shall be allocated as a reduction of principal (debiting the liability) and as interest (debiting interest expense), so to use a constant periodic rate of interest on the remaining balance of the obligation. The capitalization regulations for capital leases in accordance with the US GAAP are therefore basically in conformity with the guidelines for finance leases according to the IAS 17.

The lessor capitalizes the leased asset in accordance with SFAS 13.19 (a) the leased property shall be included with a near property, plant, and equipment in the balance sheet. The rent shall be reported as income over the lease term generally in a straight line basis in accordance with SFAS 13.19 (b), as long as another systematic and rational basis is more representative. Initial direct costs according to SFAS 13.19 (c) shall be deferred and allocated over the lease term in proportion to the recognition of rental income. The accounting of operating leases according to SFAS 13.19 corresponds with the International GAAP.

From the perspective of the lessor, three sub-categories of capital leases have to be distinguished, namely sales type leases, direct financing leases and leveraged leases.

The **sales type lease** – seen from an economic view point – is a sale which includes the financing of the purchasing price as part of the lease agreement. The manufacturer or the dealer acts as a lessor. They (often) do so in order to promote their sales. The lessor records the lease in the same way as a sale of the property: sales, cost of goods sold, lease receivable, unearned income are recognized by the lessor. A sales type lease gives rise to a manufacturer's or dealer's profit or loss on the assumed sale of the item in the year of the lease as well as interest revenue over the life of the lease. The asset leased is an item of inventory to the lessor.

The **direct financing lease** is purely a financing business, similar to contracts with banks and leasing agencies. In a direct financing lease, the lessor is not a manufacturer or dealer in the item; the lessor purchases the property only for the purpose of leasing it. Capitalization of a direct financing lease is generally done in an analogous way to the sales type lease. However, since the contract parties have only concluded a financing deal, no sales profit or sales loss can result from it. Lease receivable and unearned income are recognized by the lessor. It is necessary to emphasize that direct financing lease does not meet any of the leveraged lease criteria.

A **leveraged lease** combines two transactions into one: 1) the lessor borrows money and purchases the leased property; 2) the lessor leases the property to the lessee. A leveraged lease involves at least three parties: a long-term creditor

(lender) in addition to the lessor and lessee. The creditor, usually a bank or insurance company, puts up a percentage of the cash required to purchase the asset, generally more than half. (Friedman, J. P. 2007) Thus, the lessor uses a **combination of its own funds and borrowed money** in order to purchase the asset that is then leased to another party. Through the long-term financing by the creditor a significant leverage effect for the lessor occurs. The lessor's net investment declines during early periods and rises during later periods. The lessor recognizes the following rentals receivable, unearned and deferred income, the residual value of leased property, investment tax credit, if applicable. But the lessor does not get a manufacturer's or dealer's profit. Fitch emphasizes that a leveraged lease is a true lease for tax purposes, because the lessor, as owner of the asset is entitled to all of the tax benefits of ownership, including accelerated depreciation write-offs, deduction of interest payments on the bank loan, and the investment credit, if any, for purchase of the asset (Fitch, T. P. 2006).

All lease agreements, which do not meet the criteria mentioned above, must be classified as operating leases (negative distinction). According to *ASC 840-20 Leases* lease is classified as an operating lease by the lessor if it is not classified as one of the following:

- sales type lease
- direct financing lease
- leveraged lease.

Regarding the lease agreements which have been declared as operating leases, the economic ownership of the leased asset remains with the lessor. The leased property continues to be reported as an asset in the lessor's balance sheet and is depreciated by the lessor. The lessor recognizes rent revenue.

If a lease agreement does not meet any of the criteria of a capital lease and therefore is classified as operating lease (negative distinction), neither the leased asset nor the lease liability is capitalized by the lessee. Rather – similarly to the IAS 17 – only the lease expenses are recorded. In principle all lease installments have to be allocated on a straight line basis over the whole lease term in accordance with the US GAAP. Only if another systematic and rational basis is more representative of the time pattern in which benefit is derived from the leased asset, that basis shall be used. The lessee shows nothing about the operating lease on the balance sheet. In contrast to the International GAAP, at the inception of a guarantee, the guarantor shall recognize in its balance sheet a liability for that guarantee in accordance with FIN 45.9 (b) the liability recognized at the inception of the guarantee should be an estimate of the guarantee's fair value. According to FIN 45.11 (d) if a residual value guarantee were provided by a lessee-guarantor when entering into an operating lease, the

offsetting entry would be recorded as prepaid rent, which would be accounted for under the US GAAP.

3.3. Interim Conclusion

The overall accounting for leases under the US GAAP and the International GAAP is similar, although the US GAAP has more specific application guidance than the International GAAP. Reflecting on the explanations so far it can be stated that the capitalization of leases according to the US GAAP is based in accordance with the International GAAP on the risk and reward approach. For capitalization purposes the contract parties have to differentiate between capital/finance leases and operating leases, based on the distribution of the rewards and risks in connection with the leased asset. In the case of a capital lease agreement the lessee becomes the economic owner, and according to *ASC 840-10-10 Objectives* the capital lease should be accounted for as the acquisition of an asset and the incurrence of an obligation by the lessee and as a sale or financing by the lessor. In contrast to the International GAAP regulation however, a criteria catalogue is used, which leads to automatic contract classifications. The capitalization is tied to the classification and follows the analogy of the IAS 17 and also the all or nothing approach, whereby the lessee has to capitalize the leased asset and the resulting obligations in cases of a capital lease. In the case of a capital lease agreement the lessee becomes the economic owner, and according to *ASC 840-10-10 Objectives* it should be accounted for as the acquisition of an asset and the incurrence of an obligation by the lessee and as a sale or financing by the lessor. In the case of an operating lease the economic ownership remains with the lessor, who therefore has to include the leased item in his balance sheet, while it does not influence the balance sheet of the lessee. In contrast to the lessor, the lessee does not capitalize in cases of operating leases. The classification as a capital lease agreement or operating lease agreement according to *ASC 840-10-25 Recognition* is generally decided at the beginning of the lease agreement, which corresponds in essence with the classification according to the International GAAP.

It has to be stated that the decision relevance on the basis of the currently valid regulations for the capitalization of leases is very limited. The all or nothing approach leads to an incomplete information transfer because in the case of an operating lease neither assets nor obligations resulting from the lease contract on the side of the lessee are capitalized. The additional reporting cannot avoid that investors still lack information about future payments. In addition, leaving out conditional lease payments and the exclusive consideration of favorable purchase options and/or extension options prevent the availability of complete information.

From the perspective of the economic approach (substance over form) the capitalization that is independent from the legal ownership can be endorsed, as long as the presented facts correspond with the constellations of the capitalization of capital leases. However, such a sharp classification of actual contracts is often not possible and therefore, as a result of the all or nothing approach there is the danger that economically comparable facts will be capitalized in different ways.

The classification as a capital lease agreement or operating lease agreement according to *ASC 840-10-25 Recognition* is generally decided at the beginning of the lease agreement, which corresponds in essence with the classification according to the International GAAP. Since the classification according to the IAS 17 follows only qualitative orientation guidelines that are part of the overall assessment of the economic conditions, the contract classification is factually a right of choice. Contrary to the regulations in the IAS 17, the classification in accordance with the US GAAP does not apply the rewards and risks, connected with the leased asset, as a superior principle. The classification of a lease in accordance with the US GAAP follows without exception the standardized criteria. The quantitative classification criteria in *ASC 840-10-25 Recognition* reduce the leeway for depictions, but they enable the bypass of limits by constructing the contracts in appropriate ways. The comparability is significantly reduced through the contrasting method of capitalization (all or nothing approach) that results from the contract classification at the lessee. The flawed additional reporting about the depiction leeway and the contract classification reduce especially the comprehensibility of the information provided.

From the viewpoint of reliability it appears that the current regulations regarding the capitalization of leases according to the International GAAP and the US GAAP need to be improved. Especially the neutrality of the information provision is threatened by the depiction leeway regarding the classification, because the capitalization – based on the contract classification – according to the all or nothing approach can result in a biased report by the lessee, who seeks to avoid capitalization. The lack of additional explanations about the use of the depiction leeway and the contract classification result in a flawed verifiability of the information that is provided by the accounting, and thus the information does not fulfill the purpose of minimum objectivity.

The analysis shows that the current regulations for the capitalization of leases according to the International GAAP and the US GAAP have big deficiencies – especially on the side of the lessee – regarding the decision usefulness and the reliability. On this basis the following chapter will research, whether the current reform efforts of the two standard setters – IASB and FASB can contribute to the improvement of the decision usefulness of the information that is transmitted through the capitalization of leases.

4. REFORM PROPOSALS FOR FUTURE LEASE CAPITALIZATION

4.1. Characterization of the Reform Efforts Regarding the Lease Capitalization

Discussions about the capitalization of leases on the basis of the all or nothing approach are not new even in the international accounting community (Brakensiek, 2001, p. 205). Again and again the complexity of the regulations and the (nevertheless) existing differences in regards to capitalization, as well as the incorrect classifications of lease contracts of leasing partners, have been criticized.

The current status quo of the capitalization of leases is generally considered unsatisfactory, and in the recent past this has led to two reform proposals, which are part of the internationalization process. The reform proposals go hand in hand and are oriented on the potential implementation of the IFRS capitalization. A search for a more practicable and complete solution regarding the capitalization of lease specific facts is going on. For that purpose the so called G4+1 working group was initiated in 1995. The working group included high level representatives from the national standard setters from Australia, Great Britain, Canada, New Zealand and the USA – together with representatives from the IASC as observers.

The declared objective of this cooperation has been the development of worldwide unified concepts to selected questions concerning the accounting and the promotion of their application (Street *et al.*, 1998, pp. 132–133; Blanchet *et al.*, 1999, p. 7). Since none of the participating standard setters had delegated the competence to develop and pass (new) accounting standards to the G4+1 group, the published position papers had no formal binding force for the standard setting participants (Lewicki, 2001, pp. 9–10). The position papers were mostly intended to serve as a discussion basis and for the development of the actual accounting standards (Küting *et al.*, 2000, p. 1720). The task for the G4+1 working group therefore was the coordination of the work of the respective standard setter (Mellwig, 1998, p. 12). In the process of the restructuring of the IASB and the agreed intensified cooperation with the national standard setters, the G4+1 working group was dissolved in 2001.

During its existence the G4+1 working group published two position papers among other things. The position paper published in 1996 carries the title “Accounting for Leases: A New Approach”. It encompasses the conceptual foundations for a redevelopment of the capitalization of leases (McGregor, 1996, p. 17; Weinstock, 1996, pp. 794–798). Referring to its main author, the paper is usually called the “McGregor-Paper”. The McGregor-Paper – in the opinion of the authors – should serve as a basis for discussions among the participating

standard setters for the revision of capitalization of leases, which was planned at that time (McGregor, 1996, p. 4 and p. 25). Although the proposals of the McGregor-Paper were not taken up by the standard setters, the G4+1 working group developed the basic concepts of a revised approach to the capitalization of leases further and developed another position paper which was published in 2000 by the then IASC under the title “G4+1 Position Paper: Leases – Implementation of a New Approach”. The concretizations and detailed regulations for the capitalization of leases within the basic concepts were developed under the aegis of the British Accounting Standards Board (ASB); therefore the second position paper is often referred to as the “Tweedie-Paper”, named after the then ASB chairman David Tweedie. From 2001 until June 2011 Sir David Tweedie was chairman of the IASB, which underlines the importance of the position paper for the current project for the capitalization of leases (Nailor *et al.*, 2000).

The position papers of the G4+1 working group were revived again in connection with convergence efforts between the IASB and the FASB. Besides these two proposals that build on each other and the basic concept of which is the so called financial components approach (Fülbier *et al.*, 2005, p. 278; Monson, 2001, p. 277), the so called whole asset approach that is discussed in the US literature is the starting base for the joint lease project (since 2006) of the two standard setters. Before discussing the current standard of this project – with the decision usefulness as background – the following sections will deal first with the two discussion papers of the G4+1 working group, namely the financial components approach, and then with the whole asset approach, which serve as the basis for the project. Subsequently, a critical comparison of the decision usefulness regarding the information, transmitted by these two models, and the currently valid regulations of capitalization leases follows.

4.2. Financial Components Approach

4.2.1. Lease Capitalization: Conceptual Basis

The conceptual and basic idea of the financial components approach of the G4+1 working group represents a departure from the essential principles of the former (and current) capitalization of leases according to the International GAAP and the US GAAP. The G4+1 working group argues against the need for a reform of the current capitalization of leases especially based on the fact that assets and liabilities resulting from operating leases are not capitalized in the balance sheets of the lessee (McGregor, 1996, p.1). The problem of this balance sheet neutrality is intensified by the differences regarding the characterization and setup of the contract classification. The result of this can be that economically identical lease agreements are capitalized in completely different ways (McGregor, 1996, p.10). The financial components approach, which is presented in the two position papers by the G4+1 working group, suggests that lease agreements should not be

capitalized anymore as tangible assets on the basis of the risk and reward approach, namely on the basis of the distribution and identification of the economic owner. Instead, the capitalization of the legal right of use at the side of the lessee is suggested as a principle. It follows that the lessee, who controls the economic resource, should capitalize the leased asset and, as a consequence, recognize also a liability. However, the idea to capitalize legal rights of use was not invented by the G4+1 working group. These proposals go back into the 1960ies and discussions – independently from lease agreements – about the capitalization of legal rights of use by lessees. However, these discussions did not have any significant influence on the development of accounting standards regarding leases (Myers, 1962, p. 34–67; Dieter 1979, p.19). Due to the proposed unified approach regarding all lease agreements there is no need for the current classification between finance leases and operating leases. The position papers therefore constitute a turning away from the all or nothing approach” (Nailor *et al.*, 2000).

The proposed obligation to capitalize all assets and liabilities, resulting from a lease agreement, is derived by the G4+1 working group from the framework concepts and the definition and approach criteria that were developed by the standard setters for assets and liabilities (McGregor 1996, p. 15 and pp. 27–31). The working group states in the two position papers the opinion that the legal right for use of the lessee and the receivable from the agreed lease installments on the side of the lessor fulfills the definition criteria of a property asset (McGregor, 1996, pp. 15–16). The obligation of the lessee to pay the lease installments fulfills the definition of a liability (McGregor, 1996, p. 16), as argued by the working group. Furthermore, from the viewpoint of the working group all irredeemable lease agreements fulfill the additionally required criteria regarding the accounting capability of assets and liabilities. Thus, the capitalization of all assets and liabilities, resulting from the lease agreement, is recommended by following the two-step approach concept in the framework. The criterion of the economic ownership, used until now, appears to be dispensable (McGregor, 1996, p. 17).

From the viewpoint of the working group, the point in time of the transfer of the leased asset is the main issue for the lessee to recognize the leased asset because the lessee receives control over the leased asset at that point in time and thus, the criterion for control regarding the asset definition is fulfilled.

The G4+1 working group defines all contracts as lease agreements, wherein the lessee received the right to use a certain asset during an agreed period of time. In return, the lessee is obliged to make specified payments (IASB 2000, 2.3). The legal ownership, however, remains with the lessor during the whole lease term. The reform proposals do not suggest independent capitalization regulations for lease agreements with special leased assets. Therefore the currently valid

capitalization scope would need to be expanded to include licenses and similar intangible rights (McGregor, 1996, p. 18).

According to the financial components approach, all irredeemable lease agreements result in the recognition of an asset and a liability in the balance sheet of the lessee. The McGregor-Paper suggests a limitation of the capitalization of these legal rights of use which result from lease agreements with a duration time of at least one year (McGregor, 1996, p. 18). However, since lease agreements with a shorter duration period can result in significant legal rights of use, the Tweedie-Paper has rightly cancelled this point (IASB, 2000, 2.54). An exception – specific for leases – is therefore explicitly not provided anymore (Nailor *et al.*, 2000). According to the proposal of the G4+1 working group all lease agreements – independent of the contract formation – will result in the recognition of an asset and liability in the balance sheets of the lessee – something that is in contrast with International GAAP and US GAAP. Leases in accordance with the financial components approach will thus lose its off balance sheet character. The contract regulations will only influence the stated amount of the legal right of use and the lease liabilities. Furthermore, and if applicable, the options granted to the lessee and the guarantees given by the lessee, shall be recognized as independent assets and liabilities. Capitalization on the basis of the reform proposals is therefore based on the assumption that legal rights of use have been purchased (Nailor *et al.*, 2000).

The lessor, in contrast, has to close out the transferred share of the legal right of use regarding the leased item against a lease receivable, which will result basically in a symmetrical balance for the lessor and the lessee (McGregor, 1996, p. 24). The residual value of the leased item usually remains with the lessor, namely the remaining legal right of use and the exploitation right, and these will continue to be capitalized by the lessor. Thus, the two contract parties capitalize the respective share of the utility potential of the leased asset, which they can control. This way of capitalization according to the financial components approach is similar in principle to the current capitalization of lease agreements according to finance leases and operating leases respectively, and will be discussed in more detail in the following section. It should be noted that the two position papers of the G4+1 working group, besides the above mentioned basic concept, contain the main outline of the suggested capitalization and not so much the technical details.

4.2.2. Capitalization of Lease Agreements by the Lessee

Characterization of the Intended Lease Capitalization. The central right that is transferred in the lease agreement is the temporary right of use of the leased asset. In return the lessee has the obligation to pay the agreed lease installments to the lessor. If a lease agreement has been concluded in this sense, then the

lessee – in accordance with the proposals of the G4+1 working group – has the central right of use and the resulting obligation to capitalize the leased item (Helmschrott, 2000b, pp. 28–29).

In contrast to the capitalization regulations for finance leases and operating leases, the lessee following the financial components approach does not capitalize the leased asset but his right of use of the leased asset. Following the viewpoint of the working group, leasing businesses should therefore in capitalization follow the concept of purchasing the right of use (IASB 2000, 3.8). Consequently, those elements in the contract, which go beyond the right of use and are not part of a purchasing process, have to be dealt with separately. This applies for example to service components such as the performance of maintenance and service by the lessor, which are paid regularly together with the actual and agreed lease payments. However, by their very nature, they are not completed yet at the time of transferring the leased asset. According to the view of the working group, these separate service agreements are pending businesses, which do not need to be capitalized until they fulfill the definition and recognition criteria of assets and liabilities. Therefore, according to the financial components approach, the lease payments which are agreed on between the contract parties, have to be classified analogous to the currently valid capitalization of finance leases and operating leases into payments for service performances (if any) by the lessor, and into payments for the right of use, which is decisive for the capitalization approach (IASB, 2000, 2.41).

This classification, which will allow room for discretion due to the initial uncertainty regarding the services that will have to be performed by the lessor, shall be applied in the view of the reform proposal for all lease agreements and therefore also to the current operating leases, which are non-obligatory now. From the assumption of the purchase of the right of use, a first evaluation of the right of use and the corresponding liability in the amount of the fair value of the transferred right of use is derived (IASB, 2000, 3.13–3.15). Since there is normally no demand for temporary and limited rights of use, the fair value of transferred rights of use cannot be directly determined in the market. Therefore the discounted minimum lease payments are used as reference, since they – in the view of the G4+1 working group – correspond with the fair value of the rights of use. Therefore both the right of use and the liability are set at the present value of the minimum lease payments, which, according to the financial components approach are the central evaluation criteria and exclusively encompass the unavoidable payments by the lessee. For the purpose of capitalization, the earliest possible termination of the lease agreement by the lessee has to be assumed at all times. The above mentioned minimum lease payments are based on a fundamentally different concept in comparison with the currently valid regulations because the current lease standards encompass the minimum lease payments of the economically likely payments of the lessee.

This different understanding of terms results, for example, in the situation that the exercise of agreed “favorable” extension options cannot be expected any longer by the lessee and thus, the expected payments during the optional time periods are no longer part of the minimum lease payments. Due to the changed definitions the current evaluation of some lease agreements that are classified as finance leases and/or operating leases and thus are capitalized by the lessee, will – according to the proposals of the G4+1 working group – lead to fewer capitalization approaches (IASB, 2000, 3.25).

For the discounting of the minimum lease payments the incremental borrowing rate of the lessee for an outside financing – comparable in duration and collateralization – has to be applied. The interest rate, applied in the lease agreement, considers the various risks of the lease payments and of the residual value; therefore – in the view of the working group – it can only be used alternatively if the lessor carries only a relatively small residual value risk (IASB, 2000, 6.12, 6.5). The purchase of the right of use of a leased asset that is acquired as part of a lease agreement is limited as a matter of principle to the term of the contract. The right to dispose and the right of use after the contract period remain with the lessor. According to the view of the working group, the obligation of the lessee to return the leased asset at the end of the contract term is not an obligation because the benefit from the leased asset after the contract period was never transferred to the lessee (in the first place), and thus, the return of the leased asset does not constitute a loss or benefit. Therefore the obligation – independent from any explicit agreement regarding the return – does not have to be presented by the lessee (IASB, 2000, 3.20).

In the following periods the asset has to be amortized by the lessee analogous to the utility process during the expected utility period. In addition, unscheduled depreciations – if applicable – have to be applied in accordance with the general evaluation regulations. The obligation, resulting from the lease agreement, has to be reduced – by considering the effective interest rate method and the performance of lease payments by the included amortization rate. According to the financial components approach the following evaluation corresponds therefore with the valid capitalization regulations for finance leases in accordance with IAS 17 and operating leases in accordance with SFAS 13 (Nailor *et al.*, 2000).

In the position papers of the G4+1 working group it is not explicitly clarified, to which part in the lessee’s balance sheet the capitalized asset has to be reported (IASB, 2000, 1.12, 9.6). The right of use constitutes an intangible asset, and therefore the classification to intangible assets seems to be a possibility. However, from the view and opinion of the economic approach (substance over form) the balance sheet part, to which the leased asset itself would belong, is preferred. A tangible asset that is leased by the lessee remains a tangible asset in

its factual use. To enable the differentiation between the leased and actually purchased assets, additional information in the balance sheet with regard to the leased asset should be given. In contrast, the fundamental recognition of leased assets as intangible assets would rather follow the legal form.

In summary, it shall be stated that in accordance with the financial components approach, all rights of use that are transferred to the lessee have to be capitalized by the lessee. In their evaluation the unavoidable payments, made by the lessee, have to be taken into consideration. Besides the transfer of limited rights of use and the corresponding obligation to pay lease installments, which are part of every lease agreement, additional rights and obligations result from lease agreements. Their treatment with regards to the balance sheet from the perspective of the G4+1 working group will be discussed in the following sections. In doing so, a distinction will be made between the purchasing option, extension option, cancellation option, adjustable lease payments and regarding the residual value, which, due to their influence on the right of use option of the lessee have to be capitalized by the lessee. Consequently, the identification of the transferred rights of use and the regulations of the unavoidable lease payments of the lessee will be the focus of the analysis.

Capitalization of Additional Lease Contract Components.

Optional Lease Payments. Lease agreements often include optional components and their variety increases the complexity considerably. Often the contract parties agree on various options. In the opinion of the G4+1 working group, the exercise of the option to extend the contract economically constitutes the non-exercise of a cancellation option and should therefore be treated in the same way in the balance sheets. Thus, the following explanations focus on capitalization of the extension option and the purchasing option (IASB, 2000, 4.29).

If the purchasing option of the leased asset at the end of the lease term is agreed on in the contract, or if a contract extension is agreed on, according to the financial components approach, these options have to be capitalized as independent components, separate from the right of use (Sabel *et al.*, 2008, pp. 199–201). In the view of the G4+1 working group the rights to exercise these options should be capitalized as independent and fundamental rights of the lessee, independent from the probability of their later exercise. For the purpose of capitalization, the exercise of the extension and purchase options should – contrary to the current capitalization of leases – not be anticipated (IASB, 2000, 4.9). The probability of a future exercise of the agreed options will, however, influence the evaluation of the agreed options, because the conditions of the option usually affect the amount of the lease payments, agreed by the contract parties.

Following the reform proposals, the options will only have to be capitalized separately, if they contain a crucial part, which also must be verifiable with reasonable certainty (IASB, 2000, 4.10, 4.12). The value of the options should be determined through a comparison with another contract, which does not contain the options. Thus, the options have to be declared at their fair value (IASB, 2000, 4.9). Since the lease agreement is valid only until the potential exercise of the options, the compensation for the options must be made during this time period. Therefore the minimum lease payments have to be distributed during the contract term – which is also the period of the right of use and the additional options, because the right to exercise the option is compensated as part of the lease payments (IASB, 2000, 4.10).

Since the lessor is not obliged to exercise the option, and since the outflow of financial resources during the optional time period can be influenced by his own future decisions, the lessee is not obliged to make payments at the beginning of the lease agreement according to the reform proposal (IASB, 2000, 4.19). Thus, besides the capitalization of the right to exercise the option, the lessee does not capitalize a right of use during the optional time period because the lessee does not have the necessary right of disposal regarding the decision that he has to make. The future payments have to be only capitalized during the option period, after the lessee exercises his right to the option (IASB, 2000, 4.14). For example, in the case of a contract extension option, only the actual right to the extension has to be declared until the point in time of an actual exercise of the option. The possible right of use and the resulting lease payment obligation have to be capitalized only if the contract extension is actually exercised. Accordingly, the suggested evaluation will show differences to the regulations in the IAS 17 and the US GAAP, since in the framework of the current accounting standards the agreed “favorable” options have to be anticipated if the probability is appropriately high. Thus, in accordance with current regulations, payments that are attributed to the option time period, and in the case of a lease agreement that must be capitalized and has a “favorable” option, have to be already considered at the first evaluation of the asset that has to be capitalized and the liability, which is part of the minimum lease payments (Nailor *et al*, 2000).

In the proposal of the G4+1 working group the decisive point regarding the waiver of exercising the option is the possibility of choosing whether to exercise the option or not. If the exercise of the option is restricted by other agreements in the lease contract in deviation from the normal case, the exercise of the formal – but not factual – right of the option has to be assumed (IASB, 2000, 4.47). Thus, the rights and obligations, resulting from the exercise of the only formally agreed option, have to be included in the first evaluation, because the lessee cannot prevent their formulation independently. Especially, if the exercise of the agreed option is prevented by economic reasons, the formal existence of the option agreement is insignificant. The difference in capitalization options, which

the lessee can freely exercise, and options where the free exercise is not available due to economic or legal reasons, serves the objective – following the financial components approach – to capitalize exclusively lease payments that cannot be avoided (Nailor *et al.*, 2000).

If the lessee can freely exercise his right to the option, then the reform proposal suggests the capitalization of this right, and in the following periods until the possible exercise of the option it has to be carried forward as acquisition costs, including possible impairments (IASB, 2000, 4.11). If the option is exercised, its carried forward valuation will be capitalized as part of the acquisition costs of the acquired right of use of the leased item or the purchased leased item. If the option is not exercised, its remaining residual value has to be recorded as an expense.

In summary, it has to be stated that by following the proposal of the G4+1 working group, optional lease contract components have to be capitalized as separate rights until the time of their possible exercise. The lessee capitalizes – besides the central right of use, which is part of every lease agreement during the agreed and fixed minimum term – only the right to exercise the option itself because the possible lease payments during the optional time period can normally be avoided by the lessee, and because the lessee always assumes the earliest possible termination of the lease agreement.

Changeable lease installments. Besides the optional contract components discussed earlier, the lease contract parties often also agree on changeable lease installments. In such cases, the lease installment usually consists of a clearly fixed (concerning the amount) component and of a variable component. The variable component can, for example, be tied to the intensity of the use of the leased asset, or to the profits generated through the use of the leased asset, and thus be connected indirectly to the intensity of the use or to independent parameters, e.g. the inflation rate (IASB, 2000, 4.3). The capitalization of these variable components suggested by the G4+1 working group depends on the influence of the lessee on the parameters, to which the contingent lease installments are tied. This influence is limited to the decision regarding the use of the leased asset. In contrast to the currently valid capitalization of leases according to IAS 17 and SFAS 13 the inclusion of contingent rental is not categorically excluded. This is so because in the opinion of the working group the exclusive capitalization of contingent rentals in comparison with the transferred right of use can result in inappropriately low valuations. Since different capitalization methods are suggested for the three different categories of variable lease installments – depending on the possibility of influence by the lessee – they have to be dealt with separately.

If the contract parties have agreed on lease payments that are independent of the use of the leased asset, and if the extent of the use of the leased asset can be influenced by the lessee, then the contingent rental payments do not have to be considered in the evaluation of the right of use by the lessee. In the opinion of the G4+1 working group, such an agreement can – economically – be compared with a contract renewal option since it provides for the lessee the possibility to purchase an additional, restricted right of use of the leased asset (IASB, 2000, 4.59–4.62). Thus, in compliance with the suggested capitalization of extension options at the beginning of the contract term, only the contingent rentals installments, resulting from the right of use option, have to be capitalized. However, the lease installments that depend on the usage have to be included as expenses only in the period, during which the basic condition is fulfilled and the lease installment is unavoidable from the viewpoint of the lessee. The obligation to payment arises only at the time of the actual use of the leased asset and thus, it is not exclusively dependent on the passage of time – as is the case with obligations from agreed un-contingent rental installments. Although the exchange of performances has been agreed in principle between the contract parties, the actual performance and the value of the performance becomes only concrete in the course of time. Before each decision regarding the additional use of the leased asset, the lessee has the possibility of avoiding the lease payments, which depend on the use of the leased asset. Since the basic concept of the reform proposal suggests that only unavoidable lease payments should be capitalized by the lessee, at the beginning of the contract only right of use option-components and their corresponding liabilities should be presented. The estimation of the future use of the leased asset is not supported by the G4+1 working group.

Besides lease payments dependent on the usage, often lease payments dependent on the successful performance are agreed on as part of lease contracts. These lease contracts differ from those where the lease payments depend on the usage; the lessor participates not only in the quality of the use, but also in the price development of the lease payments (which depend on the turnover). In the case of profit-based lease payments the lessee also participates in the expenditure development. Profit-based lease payments depend not only indirectly on the usage, but on the success of the usage of the leased asset, achieved by the lessee. However, the lessee purchases only the right of use in the case of profit-based lease payments, which will be applied for every use at a variable compensation. At the beginning of the contract no payment options exist; they will only arise based on the future success. Nevertheless, the G4+1 working group suggests the evaluation of future success-based lease payments and their inclusion in the evaluation of the rights of use as well as the corresponding liabilities because avoidance of the success-based payments can be guaranteed for certain (IASB, 2000, 4.65–4.71). The working group cites this viewpoint as an example for long-term leases of the right of use of selling space, where annual rent comprises

a minimum base rental of 10 000 plus $\frac{1}{2}$ per cent of the store's turnover during each year (IASB, 2000, 4.65). In the view of the working group, the amount of the profit-based lease payment does not depend on the purchase of additional, limited rights of use, but on the participation of the lessor in the economic success of the lessee, and thus, the avoidance of the lease payments, independent from the success, can only be assumed (IASB, 2000, 4.71–4.75). In accordance with the reform proposal the right of use should be determined through the comparison – except the contingent rental payments – of lease payments of identical lease agreements. In doing so, the variable which determines the amount of the contingent rental payments is assumed for the evaluation of the right of use that has to be capitalized. If in the following periods the actual lease payments due vary from the originally assumed amount, the difference has to be recorded in the income statement.

Consequently, the G4+1 working group suggests a different capitalization approach for the usage-based and profit-based lease contract components. While in the case of the usage-based lease contract component only the right of usage-option and the corresponding liability have to be capitalized at the beginning of the contract, an assessment-based determination of the future lease payments for the profit-based lease payments is suggested, which will increase the valuation of the right of use and the lease obligation considerably. However, the general opinion does not see the economic necessity of a different capitalization models for usage-based and profit-based lease payments, because the two variants differ from contingent rental payments only in the measuring method of the contingent contract components – which regularly depend on the nature of the leased asset – and through the participation of the lessor in the economic success of the usage of the leased asset. The proposed capitalization of the profit-based lease payments constitutes a deviation from the financial components approach, in which only unavoidable payments of the lessee are included in the evaluation of the right of use and liabilities. The problem of this distinction becomes obvious through the expansion of the profit-based lease agreements regarding selling space, where the lessee has to consider minimum opening times (of a store) (IASB, 2000, 4.71). The view of the working group in this case is that the avoidance of the profit-based payments cannot be guaranteed definitely but can only be presumed. Thus, the capitalization of the expected profit-based lease payments has to be deducted at the beginning of the contract. Lease contracts with variable payments show significant commonalities and essentially do not differ in the scope of rights of use, transferred to the lessee, or in the unavoidability of the lease payments. The different models of capitalization, proposed by the working group, therefore appear problematic.

So far rental installments have been discussed, which are directly or indirectly connected with the use of the leased asset and therefore allow the influence of the lessee. Besides this type, leasing parties also agree on contingent rental

payments with parameters (price index, market interest rate etc.) where the lessee does not have any influence. While a future payment by the lessee is decided at the beginning of the contract, the actual amount of the payment will be fixed later. Contrary to the previously discussed variants with contingent rental payments, the usage of the leased item does not influence the lease payment of the lessee. The lessee does not have to pay for the use of the leased asset. With the right of use the lessee receives a resource to which a future economic inflow of profit is connected. The payment obligation arose with the obligation of possibly agreed un-contingent rental payments at the time of the transferring of the leased asset. Following the reform proposals, the part of the lease payment to which the uncertainty is attached, has to be assessed at the beginning of the lease agreement (IASB, 2000, 4.78–4.85). During the following periods the initial estimates of the asset and liability amount would need to be reviewed at each balance sheet date (IASB, 2000, 4.86–4.87). Contrary to the directly or indirectly usage-based lease contract components, the lessee cannot avoid the payment of rental installments if they are connected to unswayable parameters. However, the amount of these future payments is still uncertain. Considering this background, the evaluation of the future lease payments and their inclusion in the minimum lease payment as evaluation benchmark for the use of right and the corresponding liability at the lessee – suggested by the G4+1 working group – should be supported. However, the adaptation of evaluations – which is charged neutrally – in cases of deviations in the following periods, has to be looked at critically because the evaluation of the income statement related later evaluation of rights of use and liabilities has obviously been influenced.

With regard to the variable lease installments the working group recommends independence of the setup of the variable contract components. In the case of profit-based and thus indirectly usage-based lease payments and rental installments, which depend on factors that cannot be influenced by the lessee; the evaluation of the future leasing payments and their being a part of the minimum lease payments is proposed. These variable contract components therefore influence the evaluation of the right of use and the leasing liability that have to be determined. The G4+1 working group explains the necessity of capitalization with the unavailability of such payments. Usage-based rental payments, in contrast, are considered as avoidable and therefore they should not be included in the minimum lease payments. As stated in the previous explanations, usage-based and profit-based, and indirect usage-based lease payments show clear similarities, and thus, a different mode of capitalization does not appear meaningful.

Residual Value Oriented Contract Components. Besides the optional and variable lease contract components the lessor and the lessee regularly agree on regulations which allow the lessee to participate in the rewards and risks of the utilization of the leased item at the end of the contract term. There are many

possible contract variations – from the participation of the lessee in the utilization proceeds to a residual value guarantee of the lessee, and as far as the transfer of the legal ownership of the leased item at the end of the contract term.

If the legal ownership of the leased asset is transferred to the lessee at the end of the contract term, then – according to the reform proposals – the lease payments should be capitalized in accordance with the International GAAP and the US GAAP already at the beginning of the contract – corresponding with the economic content as a purchase. The decisive criterion is the transfer of the complete economic life of the leased asset from the lessor to the lessee. Therefore the lessee has to capitalize the complete leased asset already at the beginning of the contract period at its fair value, which would correspond with the present value of lease payments during the contract term (IASB, 2000, 5.16). The subsequent evaluation should be carried out in accordance with the assets that have already been in the legal ownership of the lessee. Thus, the leased assets have to be depreciated independently from the contract term in accordance with the useful economic life (IASB, 2000, 5.17).

However, if the leasing parties have agreed on a residual value guarantee, the lessee is obliged to make a payment in addition to the agreed rental installments. Since the lessee himself cannot influence the amount of the payment at the end of the contract term, the expected guarantee payment has to be added to the present value of the rentals to arrive at the initial carrying amount for the asset (IASB, 2000, 5.22–5.23). Contrary to the currently valid regulations of the International GAAP and US GAAP, according to the reform proposal only the expected actual amount – and not the maximum amount of the guaranteed residual values – has to be taken into consideration (IASB, 2000, 5.34). The refusal to capitalize the guarantee in the full amount corresponds with the basic concept of the financial components approach, according to which the right of disposition of the lessee has to be always stated. Capitalization of possible but unlikely guarantee payments would result in valuation approaches for rights of disposals and obligations, which would signal a significantly higher than the actual future inflow of benefits from the leased asset for the lessee.

Regarding the capitalization of the obligations resulting from the agreed residual value guarantee, the G4+1 working group discussed two possibilities. In the reform proposal the argument is for the inclusion of the expected guarantee payment in the lease liabilities (IASB, 2000, 5.23–5.27). This variant is based on the accurate assumption, namely that the inclusion of a significant residual value guarantee will result in lower than usual lease installments during the contract period (IASB, 2000, 5.27). As an alternative, the guarantee could be capitalized as an accrual and then be estimated at the best possible assessment in the amount of the expected guarantee payment (IASB, 2000, 5.28–5.31). In this case the obligation of the lessee would have to be divided into a liability of the fixed

payments and into the provision for the expected guarantee amount. However, capitalization of the provision is preferable, since the common capitalization of several guarantee obligations from similar lease agreements would be possible, which would make the determination of the expected values easier.

If the evaluation of the due guarantee payments changes during the following periods, then in accordance with the reform proposal, the evaluation of the obligation and of the right of use have to be recognized at their fair value by the lessee (IASB, 2009, 5.37). This method does not appear problematic because in the case of an increase in the expected due guarantee payment – and consequently a reduction in the originally expected residual value of the leased item – the difference from the originally expected guarantee payment will have to be capitalized as additional purchasing costs of the right of use. The right of use therefore has to be assessed higher, although the lower expected residual value is caused by factors, which also reduce the recoverability of the right of use. A direct recognition as periodic expense would be more proper in this case (Pferdehirt, 2007, p. 139).

Another participation version in the rewards and risks of the usage of the residual value of the leased asset for the lessee is the lessee's participation in the sales proceeds. In this case the lessee pays the agreed rental installment not only for the limited right of use of the leased asset during the contract term, but also for his receivable from the sales proceeds. This receivable on the residual value – according to the view of the working group – has to be estimated at the beginning of the contract, and it will reduce the depreciable amount of the right of use that has to be capitalized, which has to be depreciated during the contract term. The receivable on the sales proceeds therefore does not have to be capitalized separately (IASB, 2000, 5.43–5.44).

Regarding the capitalization of residual value related contract components, the G4+1 working group suggests consequently including unavoidable payments and corresponding liabilities of the lessee in the evaluation of transferred right of use, which is part of the lease agreement. In the case of the residual value guarantees, only the actually expected guarantee payments should be capitalized – which is in contrast with the currently valid lease capitalization of the International GAAP and the US GAAP – and thus the valuations of the transferred rights of use will be reduced significantly.

4.2.3. Capitalization of Lease Agreements by the Lessor

Characterization. The reform proposal suggests that the capitalization by the lessor should in principle correspond with the capitalization of the lessee (IASB, 2000, 8.1). To do so, all rights of use and the complete usage potential, connected with the leased asset, are divided in the lease contract and attributed

to and capitalized by the respective party that has the right of disposal. While in accordance with the financial components approach, the lessee has capitalized the purchase of the rights of use, the lessor should capitalize the sale and the resulting transfer of rights of use, or a combination of rights of use and acquisition rights. Consequently, after the transfer of the leased asset, the lessor capitalizes a receivable regarding the agreed future lease payments and the retained right of disposal as a residual value. The residual value – as a non-financial asset – has to be capitalized in the same position it would be capitalized in accordance with general capitalization rules if no lease contract had been concluded.

The lessor therefore capitalizes a receivable and an interest in the residual value as two separate assets. The amount of each kind of asset would vary depending on the nature of the lease: if the lease term is short in relation to the economic life of the leased asset, the receivable would be small; and conversely, if the lease term is long, the lessor's asset would almost all be represented by the amount of receivable (IASC, 2000, 8.9). The separate classification of these two assets is considered necessary by the working group due to the different risks connected to these assets (Lipe, 2001, p. 308). While the issue of the credit-risk of the lessee is connected with the receivable, the residual value of the leased asset – which remains with the lessor – carries property-specific risks (IASC, 2000, 8.11).

The receivable of the lessor resulting from the lease agreement has to be fixed at the fair value (IASC, 2000, 8.13). The fair value of these rights conveyed by the lease cannot be less than the present value of the minimum payments required by the lease (IASC, 2000, 8.14). In accordance with the reform proposal the amount of the minimum lease payments is the same for both contract parties. The interest rate implicit in the lease that is used for the discounting of the minimum lease payments is a composite rate that reflects both the time value of money and the averaged risk relating to the total expected cash flows (IASC, 2000, 10.4). Consequently, the minimum lease payments are not to be discounted at the interest rate that is the basis of the lease agreement since this interest rate implies the risks of the receivable as well as the residual interest asset-related risks (McGregor, 1996, p. 24, IASC, 2000, 10.4). Following the reform proposals, the future lease payments received by the lessor have to be discounted at the interest rate that considers only the credit-worthiness.

The conclusion of the lease agreement leads to a split-off of the right of disposal-position on the part of the lessor from the actual leased asset, and to a transformation of these split-off parts in the lease receivable (IASC, 2000, 8.8). Consequently, the book value of the leased asset that is capitalized by the lessor until the transfer to the lessee has to be reduced by the partial book value of the part which is transferred for use (by the lessee). This applies if the leased asset

was capitalized by the lessor before the transfer. The remaining residual value represents the receivable of the lessor to the proceeds from the following valuation of the leased asset after the termination of the lease agreement (IASC, 2000, 8.6–8.7).

The lessor fulfills the lease contract through the transfer of the rights of use into the control of the lessee, in addition to transfer the leased asset and the financing during the contract term. In principle the G4+1 working group presumes that there should be a presumption that no gain or loss arises at the beginning of the lease term (IASC, 2000, 8.18). An initial realization of sales proceeds – in the view of the working group – is only possible if the lessor is also the manufacturer or dealer of the leased asset, or the amount at which the property is carried in the lessor's books immediately before the beginning of the lease is based on a historical cost that was established long before the lease was granted. The selling profit should be recognized to the proportion of the normal selling price of the equipment that is represented by a receivable, rather than by the lessor's interest in the residual value (IASC, 2000, 8.22). In this case the realized profit is limited to the partial hidden reserves of the part of the utility potential of the leased item, which was transferred to the lessee as part of the contract. However, the residual value receivable by the lessor has to be capitalized at its partial book value because it is not part of the lease contract and remains with the lessor. In determining the partial book value of the residual value receivable, the relation of the fair value of the residual value receivable and the whole leased item have to be considered. The determination of the present value of the total expected cash flows with the fair value of the leased property is referred to as the interest rate implicit in the lease in the present accounting standards. If applicable, any realized profit is the proportion of the present value of the lease payments to the selling price to profit. For example, if the manufacturing costs of the equipment were 100 and normal selling price is 120, then the total profit will be 20 but the realized profit is 12. It can be found as the proportion of the present value of lease payments (70) to the selling price (120) to the total profit (20). The present values of the lease payments and the estimated residual value, calculated by discounting the expected cash flows to the selling price of 120, are determined as 70 and 50 respectively (IASC, 2000, 8.23).

If the conditions of the realization of profits do not exist at the beginning of the lease agreement, the asset swap of lease receivables and the transferred limited right of use does usually not affect the results in the view of the G4+1 working group.

In the following periods the respective remaining lease receivable has to be reduced – by considering the effective interest method – at the amortization part of the minimum lease payments, received by the lessor (IASC, 2000, 12.3–12.4). The interest included in the lease payment is declared as affecting the net

income. Since – in accordance with the reform proposal – an accumulated and risk-specific interest rate should be applied to the residual interest receivable of the lessor during the following periods, the lessor realizes income from the interest from the following valuations of the receivable of the residual interest (IASB, 2000, 12.5–12.14).

If the impairment value test – which must be carried out regularly – results in a lower than expected residual value, the carrying amount should be written down (IASB, 2000, 12.15–12.16). In contrast – according to the reform proposal – increases of the originally estimated residual value are not permitted and increases in value can only be collected at their realization as part of the following liquidation (IASB, 2000, 12.18).

Additional Lease Contract Components. Similarly to the capitalization of the transfer of the central right of use, from which a receivable of the lessor regularly results that corresponds with the liability of the lessee, the reform proposal pursues that also other contract regulations are capitalized symmetrically for the two leasing parties (IASB, 2000, 11.2). Accordingly, the capitalization of the lessor does not anticipate the exercise of favorable options but rather assumes the earliest possible termination of the lease contract by the lessee (IASB, 2000, 11.3–11.4). Therefore receivable of the lessor is based on the present value of the minimum lease payments, which the lessee has to perform during the non-optional time period. Contrary to the view regarding the capitalization by the lessee, the working group does not consider the separate recognition of purchase, extension, and cancellation options, or the grantor's position resulting from the option, as necessary. Agreed options are implicitly considered as part of the lease receivable by the lessee. Regardless of the type of the option, the retention of part of the right of use and the right of ownership with the lessor after the shortest possible contract period is assumed, which has to be capitalized as a residual value besides the lease receivable. Only if the renewal or purchase option is exercised, or the cancellation option is not exercised by the lessee, does a transfer of the right of disposition, which remained with the lessor, result. Thus, a reduction of the residual value receivable and the receivable of formerly optional payments become effective (IASB, 2000, 11.7–11.8).

According to the financial components approach capitalization of contingent rental payments by the lessor should be also done similarly to the capitalization by the lessee, depending on the parameters applied to the lease payments. In the opinion of the G4+1 working group, lease payments, which depend on the use and therefore can be avoided by the lessee, have to be capitalized in accordance with their economic content in the same way as extension options. On the basis of the assumed preventability, these contingent rental payments must not be considered as part of the minimum lease payments and as a benchmark for the

lease obligation of the lessor. Only at the time of the actual extension that is compensated by the non-contingent rental payments, should it be recorded as affecting the net income (IASB, 2000, 11.9–11.10). If, through the additional usage of the leased item, the fair value of the right of disposal, retained by the lessor, is reduced in comparison to the evaluation at the beginning of the lease contract, the residual value has to be capitalized and recognized as an expense (IASB, 2000, 11.10, 12.27). If the contingent rental payments depend on the success of the usage of the leased item, or on other external parameters which cannot be influenced by the lessee, these variable rental payments have to be included as part of the minimum payment and in the valuation of the receivable by the lessor. In doing so, the fair value of profit-based lease payments has to be determined as best as possible through comparison with similar lease agreements without contingent rental payments and the fair value of the lease payments, which are tied to external parameters (IASB, 2000, 11.11–11.17). If, during the contract period, the valuation of the lease receivable changes in comparison to the evaluation made at the beginning of the contract, the necessary re-measurement of the receivable has to be carried out by the lessor in relation to his income statement (IASB, 2000, 12.21).

If the contract parties agreed on a residual value guarantee, the lessee commits himself to the payment of the difference between the guarantee amount and the amount of the sales proceeds at the end of the contract period. The lessor has to consider this agreed residual value guarantee in the evaluation of the expected residual value (IASB, 2000, 9.15–9.18). A separate recognition of the residual value guarantee in the amount of the expected utilization and the non-guaranteed part of the expected residual value is not considered by the reform proposals. However, the components of the expected residual value have to be explained additionally (IASB, 2000, 9.17). This joint recognition leads to a simplification of the overall position of the following evaluations because the value decreases of the expected residual value are compensated by the value increases of the residual value guarantee, and thus, the overall position is not subject to changes of the value. This applies if the residual value guarantee corresponds to the residual value expected at the beginning of the contract (IASB, 2000, 9.16). If the lessee guarantees a significantly higher value than the expected residual value at the beginning of the lease agreement, the amount above the guarantee has to be considered in accordance with the economic content as part of the minimum lease payments and thus, with increased support (IASB, 2000, 9.19).

In summary, it can be stated that by following the financial components approach the capitalization by the lessor is done symmetrically to the proposed capitalization by the lessee. Contrary to the currently valid lease capitalization regulations, this should be guaranteed especially through the identical definition of the minimum-lease payments by both parties. The lessor and the lessee have

been declaring their respective right of disposition positions, whereby reference is always made to the unavoidable payments of the lessee.

4.2.4. Evaluation of the Information Transmission

The decision relevance of the reporting, in accordance with the financial components approach appears through the impact of all lease agreements on the lessee's balance sheet and through the standardization of the lease capitalization (with the help of the capitalization of the respective right of disposition-position of the contract parties). However, due to the omission of optional time periods and usage-based lease payments within the central evaluation benchmark of the minimum lease payments, the full transmission of information is restricted. In this context, an increased consideration for the probability with regards to the capitalization is due. The capitalization of the rights of disposal enables the capitalization of the continuous transfer from a short-term utility lease to a lease that is similar to a purchase, which corresponds with the economic approach (substance over form). However, this will increase the significance of the distinction between short-term and balance sheet effective lease agreements and pure rent contracts, which remain neutral in the balance sheets, which has not yet been discussed sufficiently. The liability is basically guaranteed by the standardization of the lease capitalization. To increase clarity, additional reporting is recommended, especially regarding the type of capitalized asset.

Reliable reporting, however, is only limited. Especially the separate evaluation of those lease contract components that go beyond the central right of use, which has to be done in accordance with the reform proposals, leads to numerous differences regarding the characterizations. As part of a possible further development of the financial components approach, additional reporting about the completed evaluations and applied premise should be made more precise. It becomes obvious that capitalization in accordance with the financial components approach basically leads to a decision-relevant transmission of information regarding the lease agreement. The numerous possible characterizations due to the increased complexity of the evaluation, however, result in a lack of reliability, and thus the decision usefulness of the suggested capitalization of leases is reduced significantly.

4.3. Whole Asset Approach

4.3.1. Capitalization of Leases

The concept of the whole asset approach – as does the financial components approach – goes beyond the basic principles of the currently valid lease capitalization according to the International GAAP and the US GAAP, because the leased items are no longer classified on the basis of the allocation of the rewards and risks either to the lessee or to the lessor. In contrast to the financial

components approach, no rights of use but always the whole leased item should be capitalized, regardless of the contract term and independent from the classification of the rewards and risks connected with the leased item. Following this standardization of lease capitalization, the classification of contracts will not be needed any longer.

Especially the US specialist literature promotes the whole asset approach. This is based on the fundamental assumption that the lessee controls the leased item during the contract term in its entirety, and not only a part of the transferred rights of disposal (Monson, 2001, p. 277). According to this assumption the capitalized amount of the entire leased item during the contract term is deducted – based on the fiction of an externally financed purchase. Consequently, the leased item should be capitalized at the beginning of the lease agreement – which is the assumed time of the purchase of the entire leased item – by the lessee at its fair value. The corresponding overall obligation of the lessee in accordance with the whole asset approach results from the payment obligation of the rental payments during the contract term and from the obligation to return the leased item at the end of the contract term (Monson, 2001, p. 277). The relationship between these two obligations, which have to be capitalized by the lessee, reflects fundamentally the relationship between the contract term of the lease contract and the economic life of the leased item.

The basic economic concept of the whole asset approach is based on the actual production process where always entire assets are used, and not only on a fraction or a related right of use. Therefore, the productive asset available to an enterprise should be reported in its entirety in the balance sheet, independent from the financing method (Monson, 2001, p. 283). The proposed capitalization, which corresponds to the purchase of the entire leased item, will lead to a leveling of the differences between temporary leases and temporally unlimited legal ownership. This undifferentiated observation has to be considered critically because especially the right of disposition-position of the lessee differs significantly from the position of legal ownership. While the lessee holds only a regular and only limited right of use and can only dispose of the leased item in a limited way, the legal owner holds basically all rights of disposal and thus, he has many more alternatives regarding his decision, e.g. the sale of the asset (IASB 2000, 3.20). Distinguishing lease agreements and classic lease contracts goes beyond the problems discussed here.

When following the whole asset approach, the lessee capitalizes the leased item at the beginning of the lease agreement at its fair value and a corresponding liability, which consists of the obligation to pay the agreed rental payments and to return the leased item at the end of the contract term. Thus, the first approach follows the assumption of a purchase of the entire leased item by outside financing. In contrast to the currently valid capitalization of finance leases, which basically also follows the concept of a purchase, according to the whole

asset approach, the leased item is not only set at the agreed minimum rental payments at the lessee, but also at the amount of the fair value. The contract components that go beyond the actual right of use are implicitly considered by the capitalization of the leased item at its fair value.

The liability has to be reduced by the amount of amortization part and by considering the effective interest method until the end of the contract term. In doing so, the incremental borrowing rate of the lessee has to be applied, which is comparable to an outside financing with a similar contract term (Monson, 2001, p. 281). According to the whole asset approach, the liability should correspond with the book value of the leased item at the end of the contract term. Specialist literature suggests tying the depreciation of the leased item to the development of the liability, in order to guarantee this objective (Sigloch, 2006, pp. 420–421). Following this suggestion, the leased item should be depreciated regularly and independently from the actual utility. Since the liability is amortized by the agreed lease payments of the lessee at the end of the lease agreement, the remaining liability can be interpreted as being the return of the leased item. At the end of the contract term or at the time of returning the leased item to the lessor, the residual value of the leased item has to be closed out without effect (Fülbier *et al.*, 2005, p. 283). After the transfer of the leased item the lessor has a receivable to the contractually agreed rental payments and to the return of the leased item at the end of the contract term.

4.3.2. Critical Evaluation

Following the suggested concept, the decision relevance of the reporting is rather restricted. The capitalization of the leased item at its fair value, regardless of the contract term, suggests incorrect future payment flows during the whole economic life of the leased item. This results in a systematic over valuation of the asset that has to be capitalized and of the corresponding liability at the lessee's side. From the perspective of the necessary economic approach (substance over form) the missing differentiation between the temporary limited lease and a purchase of the entire leased item with outside financing has to be criticized. Furthermore, the problematic distinction of lease agreements and rental contracts has to be discussed. The inter-company comparability is enabled in principle by the standardization of the lease capitalization. The transmission of information appears fundamentally reliable. Due to the standardized capitalization of a leased item, based on the marketability of the leased item that has to be evaluated, the neutral transmission of information is assured. Until now, only the basic outline of the whole asset approach has been developed detailed regulations, especially regarding the reporting, are not yet known conclusively. Thus, a final evaluation and verifiability are not possible at this time.

In summary, it has to be stated that the reporting of the whole asset approach on the side of the lessee has obvious flaws regarding the decision relevance, and thus, the decision usefulness of the transmitted information is significantly limited.

4.4. Critical Comparison of the Discussed Concepts

As a preparation for the comparison of the decision usefulness of the concepts of the transmitted information regarding the capitalization of leases discussed so far, the respective basic concepts will be outlined at the start. The basic assumption of the risk and reward approach of the currently valid lease capitalization is based on the different participation of the contract parties with regard to the rewards and risks in connection with the leased item, and in the fundamental indivisibility of the economic ownership of an asset. Therefore all lease agreements based on the division of rewards and risks should be distinguished into lease agreements, which, on the one hand, are similar to a purchase, and on the other hand, those which are similar to classic rental contracts. Then the capitalization of the lease agreement always follows the assumed purpose. In the case of a finance lease the lessee capitalizes the leased item regularly at the present value of the minimum lease installment as fictional purchase costs, while operating leases remain balance-neutral (all or nothing approach). In contrast, the lessor capitalizes either a lease obligation in the amount of the net investment value or the leased item that remains with him.

The financial components approach is based on the assumption that individual rights of disposition in relation to the leased item are separated from the legal ownership of the lessor and are transferred to the lessee. Consequently, the lessee always capitalizes the economic resources under his control with his rights of disposition and recognizes the lease liability that results from the payment obligation. In contrast, the lessor capitalizes the claim to the contractually agreed lease payments and, on a regular basis, the remaining right of use after the contract term.

In contrast, according to the basic concept of the whole asset approach the lessee controls the leased item during the contract term in its entirety. Thus, the lessee includes the leased item in its entirety as a tangible asset and a liability, which consists of the obligation to pay the lease installments and the return of the leased item at the end of the contract period. The lessor capitalizes his receivable to the agreed lease payments and to the return of the leased item.

On the basis of the presented discussion and the concepts of the capitalization of leases that have been analyzed so far, the following section will directly compare the decision usefulness of the respective transmitted information. For that purpose, first the decision relevance and then the reliability of the information

that is transmitted by the three capitalization concepts, will be compared. Regarding the evaluation it should be stated that neither for the financial components approach model nor for the whole asset approach a set of regulations has been developed that goes beyond the concepts.

As it has been stated, the decision relevance of the information transmitted by the currently valid capitalization regulations is dependent on the compulsory classifications of contracts, either as a finance lease or an operating lease, especially regarding the lessee. In the case of operating lease the balance sheet of the lessee does not provide helpful information with regards to future payments, due to the balance neutrality of the agreement. Although there is a basic report about finance leases in accordance with the all or nothing approach, the completeness of the transmission of this information is seriously flawed, especially due to the omission of all lease payments within the central measuring benchmark of the minimum lease payments. The standardization of all lease capitalizations, suggested by the financial components approach, will improve the completeness of the transmitted information considerably because all leases capitalized by the lessee, lead to the capitalization of his right of disposition and of the corresponding liabilities. With the exception of the capitalization of assets, the reporting of simple lease agreements, which is preferred by the G4+1 working group, is similar to the currently valid capitalization of finance leases. However, the minimum lease payments in accordance with the reform proposal encompass only the unavoidable payments of the lessee. Contrary to the currently valid capitalization of leases, the exercise of favorable options is not to be anticipated, and investors do not receive information regarding possible cash flows in optional time periods. Optional and other contract components, which go beyond the central right of use, are explicitly considered in the whole asset approach, because the lessee has to capitalize the entire leased item at its fair value regardless of the actual contract regulations. Reports about the lease agreement are therefore “more than complete”, since the limitations of the right of disposition that are transferred to the lessee are not taken into consideration.

Following the currently valid capitalization regulations, lease agreements are either capitalized by following the pattern of a purchase with outside financing, or similarly to normal rental contracts. This division into two categories of capitalization of leases suggests an impossibly selective categorization of tangible assets. Especially in the case of unclear content of contract, which the contract parties are perhaps motivated to use due to their neutrality in the capitalization, it must be questioned, whether the classification of the agreement corresponds with the content of contract. The contrasting way of capitalization of economically almost identical facts leads to a reporting, which does not correspond with the economic approach (substance over form). Through the standardization of the capitalization of leases, proposed in the financial components approach, the standardized capitalization of the continuous

transition from a short-term transfer of the right of use to the long-term agreement similar to a purchase with outside financing is made possible. Thus, the border area between finance leases and operating leases, currently allowing room for discretion and thus affecting the capitalization, will be eliminated. However, the distinction of classic rental contracts, which has not yet been sufficiently discussed, appears problematic because short-term lease agreements will no longer be balance-neutral according to the proposal of the G4+1 working group, and therefore they will be classified differently from normal rental contracts. The discussion concerning the distinction between comparatively short-term lease agreements and classic rental contracts is even more important in the whole asset approach because in this case also short-term leases are capitalized on the basis of the fictional concept of a purchase with outside financing. In addition, the standardized capitalization of the entire leased item by the lessee leads to a leveling of the economic differences between a temporary lease and the unlimited legal ownership – which constitutes another violation of the necessary economic approach (substance over form) in the reports.

In the currently valid capitalization of leases the standardization of the information transmission is significantly restricted due to the interpretation and discretion differences concerning the classification of contracts. The little inter-company comparability is not only the result of the content and categorization of contracts according to the International GAAP or the US GAAP, but mostly the unavoidable consequence of the splitting the lease capitalization into two according to the risk and reward approach. The standardization of the proposed capitalization of leases according to the financial components approach will increase significantly the homogeneity of the transmitted information. The classification differences, which restrict the inter-company comparability, result especially from the separate capitalization of agreed options and from the determination of the minimum lease payments. Through its standardized capitalization for all lease agreements and through the omission of lease-specific classification differences the whole asset approach facilitates the inter-company comparison of enterprises in comparison to the currently valid capitalization of leases. However, the difference between the transfer of a limited right of use and the purchase of the legal ownership, the comparison of two different ways of acquiring the potential carrier of success, is made more difficult.

The comprehensibility of the reports on the basis of the currently valid capitalization standards is satisfactory due to the low complexity. However, there is a lack of guidelines regarding the explanation of the central lease contract classification. Despite the omission of the concrete capitalization according to the opinion expressed here the report according to the financial components approach leads to comprehensible information for investors. Thus, in accordance to the whole asset approach the entire leased item has to be always capitalized by the lessee independent from the contract regulations, this concept

lacks comprehensibility about essential contract elements without additional information.

In summary, it becomes clear that the financial components approach has to be evaluated as the most positive one with regard to the decision relevance because in contrast to the two other capitalization concepts it connects the standardization of capitalization of leases and the balance sheet impact of all lease agreements. In addition, there is no systematic over valuation of the rights of disposition which are transferred to the lessee.

From now on, the reliability of the information, transmitted on the basis of three capitalization concepts discussed so far, will be compared. The currently valid capitalization regulations basically lead to the correct and by the book transmission of information. However, the different classification, especially regarding the contract classification, has to be mentioned as a downside. In contrast, the correctness of the reports according to the financial components approach and according to the whole asset approach cannot be assessed because so far only the two basic concepts have been developed, and no detailed capitalization regulations, which could serve as a basis for an evaluation exist.

The neutrality of the information transmission according to the currently valid capitalization regulations is restricted, especially due to the classification differences regarding the contract classification. Through the all or nothing approach the contract parties will be motivated to have the contract classification and/or the lease contract in such a way, that it can be classified as an operating lease and will thus enable the off balance sheet effect on the side of the lessee. The currently valid lease regulations may give rise to biased reports. Through the standardization of the lease capitalization in the financial components approach and in the whole asset approach the off balance sheet configuration of lease agreements is prevented. However, the different capitalization by following these two concepts can motivate a tendency to design agreements as classic rental contracts. This distinction has to be discussed thoroughly in any further development of these basic concepts. While, in accordance with the financial components approach, the classification differences result especially from the separate capitalization of contract components that go beyond the central right of use and thus can lead to biased reporting, the basic capitalization of the entire leased item by the lessee in accordance with the whole asset approach does not allow for any lease-specific classification differences.

The currently valid capitalization regulations lack sufficient verifiability of the transmitted information due to insufficient reporting. Especially the obligation to disclose and explain subjective evaluations with regards to the contract classification should help establish a minimum of objectivity of the accounting data. For the verifiability of the capitalization according to the financial

components approach and/or the whole asset approach some additional reporting about the use of classification differences and subjective assessments, plus additional disclosures of essential contract regulations, would be helpful. In all of this it has to be considered again that the two latter concepts have so far only been developed in their basic outline, and in contrast to the currently valid regulations a conclusive evaluation of the intended additional reporting is therefore not possible.

With due consideration of the detailed and different levels of development of the various capitalization concepts it has to be stated that the reliability of the information transmission according to the financial components approach, which has to be assessed as the most positive with regard to the decision relevance, is the particular reason for the restricted valuation of individual contract components. In contrast, reporting according to the whole asset approach, due to the absence of a lease-specific classification differences, leads to a higher degree of reliability. However, due to the classification differences and the division into two the lease capitalization according to the risk and reward approach needs to be improved from the viewpoint of reliable information transmission.

On the condition of a comprehensive revision of the original concepts, as revealed in the discussion paper of the G4+1 working group, in the opinion presented here the capitalization of leases on the basis of the financial components approach has to be evaluated as the most positive one from the viewpoint of decision usefulness. As part of any further development the separate capitalization of contract components beyond the central right of use should be reconsidered. In addition, guidelines for the supplementary reporting about subjective assessments and the use of the classification differences have to be developed.

4.5. Status of the Reform Proposals

4.5.1. Time Schedule of the Reform Project

To facilitate the later analysis of the discussion paper “Leases — Preliminary Views”, which was published on March 19, 2009, the process of the reform project until now will be outlined. The precondition for the current IASB/FASB lease project was the agreement of the general convergence project for the harmonization of the International GAAP and US GAAP in 2002, and the convergence timetable, which was agreed in February 2006 between the IASB and the FASB and updated in September 2008, for the two accounting systems (FASB/IASB 2009, p. 3).

With this background the two standard setters fundamentally agreed in April 2006 on a joint lease project and on the strengthening of this project with the help of an international working group. On July 18–21 2006 the IASB voted to

add a project on lease accounting to its agenda. The project was conducted jointly with the FASB. The project will reconsider all aspects of lease accounting and is expected to fundamentally revise the way lease contracts are recognized in the financial statements of lessees and lessors. The Board directed the staff to establish a working group of individuals with significant experience and expertise in lease accounting to assist the staff and the Board with this project (IASB, 2006, p.7). The sequence regarding the leasing project is presented in the Figure 11.

To provide the necessary overview for the discussion of selected aspects of the lease project and the current status of the reform project, a chronological outline of the discussions and decisions, taken by the two standard setters, will be presented. The fact has to be taken into consideration that the decisions taken so far by the IASB and FASB have by no means always been identical.

Within the scope of the lease project the two standard setters' first focus is on the illustration of a simple, irredeemable lease agreement, and then they apply the lessons learnt to more complex content of the contracts, which are closer to reality at a later point in time. This strategy appears somewhat problematic since the transfer of a capitalization model that was developed on the basis of simplified contract conditions cannot be applied easily to agreements, which contain unexpected complexities (Oversberg, 2007, pp. 379–380). Nevertheless, in March 2007 the standard setters discussed which rights and obligations for the contract parties result from a simple non-cancellable lease contract, and whether these fulfill the current definitions of assets and liabilities in the *Framework* (IASB, 2007a, p. 4).

The obligation of the lessee to return the leased item does not correspond to a liability in the sense of the definition, because in the view of the standard setters this does not constitute an outflow of resources. Corresponding to this, the right of the lessor to the return of the leased item at the end of the contract term does not fulfill the definition of an asset in the view of the two standard setters (IASB, 2007a, p. 4). Although, in the framework of the leased item, basic references to the currently valid definitions regarding assets and liabilities are made, possible changes to these definitions in the course of the yet incomplete Conceptual Framework Project have to be taken into consideration (IASB, 2007a, p. 4). According to the view of the standard setters the revision of definitions as part of the Conceptual Framework Project has not produced any effects on the definition of assets and liabilities until now.

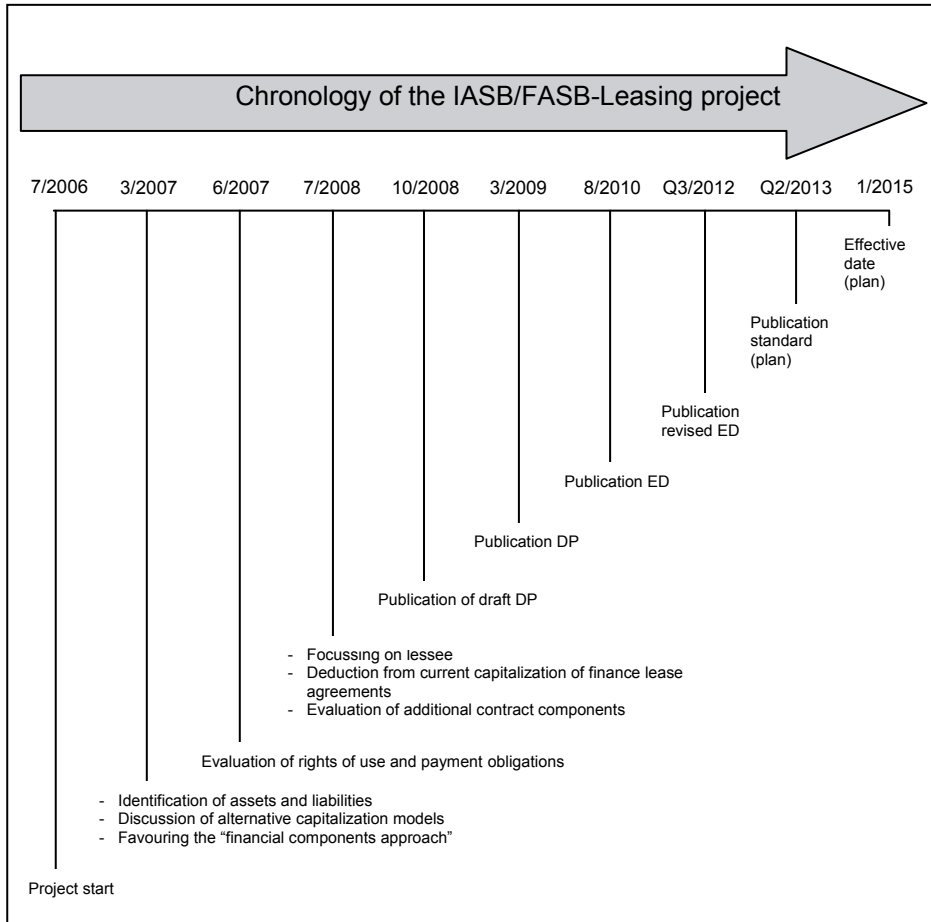


Figure 11. Chronology of the IASB/FASB-Leasing Project
 Source: compiled by the author

On the basis of the identified assets and liabilities which result from a simple lease agreement on the side of the lessee and on the side of the lessor, the IASB and FASB discussed various alternative basic concepts for the future of capitalization leases in March 2007. In the course, the two standard setters analyzed the currently valid regulations according to the International GAAP and US GAAP, according to the financial components approach and according to the whole asset approach from the perspective of the decision usefulness. Besides, they also examined the executory contract model (FASB/IASB 2007b, pp. 2–11). In the framework of the latter concept, all lease agreements are treated as suspended businesses during the contract term and thus are classified as operating leases in accordance with regulations (FASB/IASB 2007b, pp. 8–9). Therefore, in the case of the executory contract model, the balance-neutral and thus decision-irrelevant information transmission will be transferred to all lease agreements in accordance with the currently valid regulations for operating

leases. With this background and with the decision of the standard setters to not further pursue this concept, this model will not be studied any further here. In the course of the discussions of the various capitalization models the IASB and FASB have so far supported the further development of the financial components approach because it leads to the capitalization of the identified assets and liabilities. Furthermore, it guarantees the hope for equal treatment of all lease agreements with regard to capitalization.

This preliminary decision of the two standard setters is welcome from the view of the decision usefulness of the information transmission. As has been stated already and discussed as part of the IASB/FASB lease project, the decision relevance of the financial components approach has to be evaluated as the most positive one in comparison with others. However, the analysis of the financial components approach has shown that the limitation of the central evaluation benchmark of the minimum lease payments to the unavoidable payments prevents the full transmission of information, and that the separate evaluation of individual rights of disposition restricts the reliability of the information. Against this background a revision of the basic concept, developed by the G4+1 working group, appears necessary.

The preliminary focusing on the capitalization model the question, whether the lease project should include contract compilations of lease agreements for the time being raised, which would be part of the current lease standards, or all financial components approach transactions, and thus also, for example, service contracts. The restriction that was passed in April 2007 by the IASB and FASB to the already valid application scope according to the International GAAP and/or US GAAP has to be assessed critically in principle, because many problem areas, e.g. the differentiation of lease and service agreements, are not considered, and the current application scope of the two valid lease standards are by no means congruent (IASB, 2007a, p. 6). If these problem areas are not totally excluded in the coming discussions, the adapted focusing appears acceptable for now.

The assessment of the identified assets and liabilities so far has only been addressed on the side of the lessee by the standard setters. Regarding the assessment of the payment obligation by the lessee that results from the agreed lease installments, the IASB and FASB suggested in June 2007 a preliminary assessment in compliance with the currently valid regulations for financial obligations (IASB, 2007c, p. 2). Regarding the assessment of the rights of use, the standard setters discussed three alternative approaches, namely the basic capitalization as an intangible asset (intangible assets approach), the capitalization according to a newly developed model with more attention given to the fair value (separate accounting model approach), and the capitalization according to the type of leased item (nature of the leased item approach) (IASB,

2007c, p. 2). While the IASB came out in favor of the “nature of the leased item approach” in June 2007, the FASB favored an independent capitalization model for lease-induced rights of use at that time. With this preliminary decision, the FASB has left open the assessment of the fair value. Regarding the point in time approach, which was also discussed (time of the contract, conclusion of the time of the delivery/acceptance of the leased item); neither the IASB (IASB, 2007c, p. 2) nor the FASB has come to a decision.

In July 2008 the IASB and FASB decided to leave aside the capitalization by the lessor due to lack of time (IASB, 2008, p. 4). This was in response to the time schedule the standard setters had agreed on, namely to have a basic draft ready by 2011. Focusing like this will allow more attention to other ongoing projects (e.g. the Revenue Recognition Project) (Wüstemann *et al.*, 2008, pp. 150–153). In addition, a new conceptual orientation of the leasing project took place. It was agreed not to use the financial components approach for the future concept of capitalization by the lessee, but to return to the currently valid capitalization method for finance leases.

On the basis of these decisions, the IASB and the FASB published the discussion paper, “Leases – Preliminary Views” on March 19, 2009. Discussion papers have a rather conceptual character and usually contain favored suggestions as well as those alternative capitalization suggestions that have been rejected for the time being (Sonnemann, 1989, pp. 30–31). The deadline for comments regarding the future of capitalization of leases was on July 17, 2009. The next deadline for comments of the IASB and the FASB published exposure draft (ED/2010/9) was on December 15, 2010.

4.5.2. Analysis and Assessment of the Topical Discussion Paper

The discussion paper “Leases – Preliminary Views” that was published on March 19, 2009 focuses mostly on the future capitalization of leases and summarizes the decisions taken so far by the IASB and the FASB (Findeisen *et al.*, 2009, pp. 1885–1894; Leibfried *et al.*, 2009, pp. 408–413). The objective of the discussion paper is the standardization of the capitalization of leases by the lessee for all lease agreements. The future of capitalization of leases will, however, not be directly based on the financial components approach, conceived by the G4+1 working group, but will be derived from the currently valid capitalization for finance leases. For this purpose the capitalization should be modified and leases which until now have been classified as operating leases will be transferred. In the course of the intended standardization the current classification of lease agreements will be discarded on the basis of the risk and reward approach. This standardization brings changes to the basic concept of the capitalization of leases by the lessee. While until now the capitalization of finance leases was based on the fictional purchase of the leased asset, future

lease agreements will be interpreted as the purchase of the right of use of the leased asset for the time of the lease term. The application scope of the lease standards that will be developed will follow the application scopes of the currently valid capitalization of leases. Regarding possible exceptions for certain lease agreements, e.g. the ones with short contract periods or insignificant lease agreements; no decision has been made so far.

According to the discussion paper, regardless of the contract details, the lessee always has to capitalize an asset, which constitutes his right of use of the leased item during the lease term. Thus, all lease agreements will be reported in the balance sheet and the former and current all or nothing approaches will be renounced. The asset that results from the lease agreement has to be recognized at the present value for the lease payments (IASB, 2009b, 3.26). The lessee has to report also the liability that results from the obligation to perform as part of the first evaluation in the amount of the discounted lease payments. The discounting of the lease payments should always follow the incremental borrowing rate of the lessee because in the opinion of the standard setters the waiver of the obligatory (until now) determination of the interest rate that is the basis of the lease agreement will simplify the lease capitalization significantly (IASB, 2009b, 4.17)

The lease payments will continue to be the central value of measure of capitalization of leases. Contrary to the capitalization according to the financial components approach which was favored for some time by the standard setters, the agreed option for the extension or cancellation should not be capitalized as separate assets. Instead they should be considered in the determination of the contract term, which affects the lease payments (IASB, 2009b, 6.8). Two standard setters have decided for the time being that the lessee should determine the expected total time of use through his best possible estimation (IASB, 2009b, 6.36). The future regulations of capitalization of leases will probably abandon the likelihood of favorable options, which are part of the current regulations. The two standard setters suggest (as the method for the best possible estimation) the determination of the likely contract period without consideration for the likelihood of individual alternatives. Until the publication of the discussion paper the method of the best possible estimation was disputed between the two standard setters, because the IASB had also considered the determination of the lease term on the basis of the probability-proposed best possible estimation. For the determination of the likely lease term, the standard setters will present a catalogue with criteria, which will include contractual, non-contractual financial and business factors and also lessee specific factors (IASB, 2009b, 6.39.–6.41). The possible need of adapting the lease term has to be checked at each reporting date on the basis of any new facts or circumstances (IASB, 2009b, 6.47).

According to the discussion paper, contingent rental payments have to be always considered as part of the lease payments (IASB, 2009b, 7.11). In the case of deviation from the financial components approach, all contingent rental payments, regardless of their related parameters, should be reported in the balance sheet as part of the first evaluation. The contingent rental payments should be determined through the best possible estimation in the same way as the lease term. While the IASB has opted for (for now) the determination of the contingent rental payments by using the probability-weighted estimation, the FASB favors the determination of the likely value without consideration for the probability of individual alternatives for action (IASB, 2009b, 7.20.–7.21).

Regarding the capitalization of agreed residual value guarantees the two standard setters have decided for the time being not to include them in the guaranteed maximum amount of payments, but in correspondence with the determination of the contingent rental payments and the lease term in the amount of the best possible estimation (IASB, 2009b, 7.46).

While the FASB favors the determination of the most likely value without considering individual alternatives, the IASB supports the determination with the help of probability-proposed estimations (IASB, 2009b, 7.48). The lease payments, which due to their determination can be identified as expected lease payments, remain the central valuation standard for the capitalization of leases even after the discussion paper. However, it differs significantly from the currently valid capitalization of leases as well as from the financial components approach. The asset that has to be capitalized in the amount of the present value of the expected lease payments by the lessee has to be presented in the balance sheet on the basis of the nature of the leased item. The discussion paper proposes, in addition, that the leased asset is significantly different from an owned asset and should be presented separately from owned assets (IASB, 2009b, 8.16).

Regarding the subsequent measurement of the asset, the two standard setters suggest that a lessee should subsequently measure the asset on an amortized cost basis (IASB, 2009b, 5.42). The capitalized asset has to be amortized similarly to the valid leasing standards during the shorter of the two time periods – lease term and/or economic life of the leased asset (IASB, 2009b, 5.40).

In summary, it can be stated that the proposed capitalization by the lessee is based on the economic comparability of the use on the basis of the lease agreement and the use of a purchased asset. The type of the leased asset is taken into consideration. Due to the focus of the future capitalization by the lessee, the future capitalization by the lessor will not be addressed in detail in the discussion paper. The two standard setters discuss especially various possibilities of the

transfer of the proposed capitalization from the lessee to the lessor (IASB, 2009b, 10.5).

4.5.3. Characterization of the Decision Relevance

The proposed standardization of the capitalization of leases by the lessee by means of capitalization of the right of use in the amount of the expected lease payments and the ensuing balance sheet impact effectiveness of all lease agreements has to be assessed positively due to its completeness. The inclusion of all contingent rental payments constitutes a significant improvement to the currently valid capitalization of finance leases and the financial components approach due to the complete transmission of information. Essentially, the concept that is the basis of the draft, suggests that all contract details be included in the evaluation of the purchased right of use. From the perspective of the completeness of content, this basic principle should be supported. However, this principle is violated by the best possible estimation of the expected lease term, because the two standard setters suggest the determination of the expected lease term without considering the likelihood of individual action alternatives. On the basis of a probability-proposed best possible estimation, investors would not receive important information regarding the duration of the lease contract and the expected lease payments for the assessment of future payments during the optional time periods. The currently valid capitalization regulations for finance leases provide this information also in incomplete form because only lease payments in the optional time period of favorable extension options have to be capitalized. According to the financial components approach, even the exercise of favorable options is not anticipated, and thus the completeness of reporting is impaired.

However, the two standard setters do not yet agree regarding the method for the best possible estimation of contingent rental payments and the expected utilization of residual value guarantees. This is so because both the waiver of considering the likelihood of individual action alternatives and the probability-proposed best possible estimation are considered. From the view of the completeness of the transmitted information the probability-proposed best possible estimation should be given preference in the further development of the discussion paper because all action alternatives are included in the evaluation, and thus, the report would not just be about the most likely scenario.

The standardization of the capitalization the single right of use by the lessee as proposed in the draft on hand is to be supported from the economic approach viewpoint (substance over form). The reason for that is analogous to the financial components approach, the capitalization of the continuous transition from a short-term term of a right of use to an agreement, similar to a purchase with outside financing, is made possible. Due to the balance sheet impact of

even short-term lease agreements, the discussion on the distinctions of classic rental contracts is still unresearched, and which remain un-reflected in the balance sheet, appears to be an urgent matter. Thus, from the economic approach perspective no changes come about regarding the financial components approach and the sole transfer of valid regulations for finance leases to all lease agreements.

Despite the standardization of the capitalization of leases by the lessee through the capitalization of rights of use, the comparability of reports will be restricted in accordance with the discussion paper due to the proposed best possible estimation of the lease contract term and due to the contingent rental payments. The results in determining the expected lease payments will avoid a proper comparison of enterprises through the capitalization of leases. The consistency of the proposed reporting cannot be conclusively assessed due to the conceptual character of the discussion paper. However, in the process of the planned integration into the current accounting systems it can be assumed that the proposed capitalization will lead to a continuous transmission of information.

The proposed basic capitalization of the right of use by the lessee in principle results in reports that are comprehensible for investors. However, in addition, the setting of the expected lease payments and the best possible estimation of the lease contract period have to be discussed thoroughly. The line of arguments by FASB and IASB, which dismisses the probability-proposed estimation of the lease term and the contingent rental payments due to their limited comprehensibility, is not acceptable. If the most likely value, which has to be always used, in accordance to the discussion paper, does not change from the time of its first capitalization, the development of the underlying probability is not reported about. This kind of imprecise transmission of information is not in the interest of investors. The proposed updated evaluation in the discussion paper in accordance with the valid regulations for finance leases has to be supported because they do not contain any leasing-specific exceptions, but are geared towards standards for purchased assets. Consequently, the right of use that results from the lease agreement has to be reported in the same balance sheet position, which the leased asset itself would be reported because a leased asset remains an asset regardless of the actual use. In addition, the clarity of the reports will be improved through the categorization into leased and purchased assets in their respective balance sheet positions.

Regarding the decision relevance of the transmitted information on the basis of the discussion paper draft on hand, it shall be stated that the standardized capitalization of assets for all lease agreements in the amount of the expected lease payments will especially improve the completeness of the information transmission in comparison to the financial components approach and the current capitalization of finance leases.

Due to the conceptual character of the discussion paper, which does not contain a holistic overall regulation for a possible future capitalization of leases by the lessee, but also discusses various and temporary decisions by the two standard setters, no conclusive opinion can be expressed on whether the concepts fulfill the additional condition of correctness in the sense of an information transmission in accordance with the regulations. However, from the lack of unambiguous accounting regulations until now it cannot be concluded that from the implementation of the capitalization concept no guideline that would serve the accuracy would result. Especially in the context of neutrality with regards to the best possible estimation of the lease contract term and the contingent rental payments, which require the development of precise capitalization regulations has to be discussed.

Since investors need neutral information for open and unbiased predictions of future cash flows, the vulnerability of the concept proposed in the discussion paper with regard to arbitrary influences by the decision makers of capitalization has to be checked. Following the basic concept of the lease, the lessee acquires a single right of use for the expected contract term, and thus he has to capitalize the expected lease payments. In the process, freedom for the decision makers of capitalization arises, especially regarding the determination of the expected contract period and the expected payments from contingent rental installments. The effects of these unavoidable depictions of freedom vary with the methods of the best possible estimations, which were discussed by the two standard setters. The determination of the likely period, which is favored by both standard setters, without considering the likelihood of individual action alternatives can have the result that even smallest changes of the estimated likelihood by the decision makers of capitalization, have significant results in the reporting. Since the likelihood of single events will always remain subjective, the advantage of the probability-proposed best possible estimation is to keep the effects of unavoidable subjective reporting as low as possible.

In contrast to the regulations of finance leases more opportunities from reporting in accordance with the discussion paper because the expected payments from the contingent lease installments have to be included in the evaluation of assets and liabilities. Due to turning away from the all or nothing approach the unavoidable freedom of decisions cannot be used for an off balance sheet construction by the decision makers of capitalization.

In order for investors to be able to see the use of unavoidable depiction leeway, extensive guidelines for the additional reporting have to be created in the further development of the discussion paper. Regarding the method of the best possible estimation the probability-proposed estimation has to be preferred. Due to its comparatively small effects on the evaluation of assets and liabilities, the decision makers of capitalization will have less motivation towards purposeful

actions. The action alternatives, considered as part of the probability-proposed estimation, and their assumed probability of occurrence will have to be explained in addition. Nevertheless, the neutral transmission of information, as a result of the depiction leeway contained in the discussion paper, has not yet been assured.

In addition the verifiability of the reporting according to the discussion paper cannot be assessed due to its rather conceptual character. To enable investors to check the congruency of the facts and their possibilities for capitalization, the subjective estimations of the decision makers of capitalization have to be explained. Especially the explanation of the assumed likelihood of the various action alternatives can contribute to verifiable capitalization. The additional reporting has to go significantly beyond the currently mandatory explanations of lease agreements.

4.5.4. Interim Summary and Outlook

The decision relevance of the capitalization by the lessee according to the discussion paper basically exists due to the balance sheet impact effectiveness of all lease agreements and due to the capitalization of the right of use that is transferred to the lessee. The inclusion of all expected payments from the contingent lease installments during the expected contract period leads to the complete transmission of information contrary to the financial components approach and the sole transfer of current regulations of the finance lease. The inter-company comparability is restricted by the freedom to decide that results from the determination of the expected lease payments. The best possible estimation of the lease payments should be made probability-proposed, because all action alternatives will be included in the evaluation and the corresponding information transmission appears more precise in comparison to the likely value. Through the adoption of the valid regulations for the subsequent measurement of the finance leases and through the inclusion of the right of use in the same balance sheet position, where the leased item itself would be reported, the capitalization according to the discussion paper leads to comprehensible information transmission.

The reliability of reporting has improved significantly in comparison to the financial components approach and the currently valid capitalization methods for finance leases. The central importance of the expected lease payments leads to freedom of decisions with regard to the regulations for the expected contract period and the contingent rental payments. Through the determination on the basis of the probability-proposed estimation, the subjectivity of likelihoods cannot be avoided, but the effects on the capitalization could be limited. The capitalization of the expected lease payments requires, in every case, a comprehensive additional reporting about the necessary estimations.

In summary, it can be stated that the discussion paper in principle leads to a decision-relevant entity report of the lessee. On the basis of the concept that the expected lease payments will serve as the central valuation standard, as proposed in the lease project of the IASB/FASB, significant improvements with regard to the decision relevance can be expected. It should however be added that the two standard setters have not yet reached a final agreement in various areas. The implementation of the recommendations would increase the decision relevance and reliability significantly.

In principle, it should be emphasized that the standard setters recognize the urgent need for reforms of the current capitalization of leases and that they seek to bring a fundamental change to the capitalization of leases with this project. The analysis of the currently available discussion paper shows that the deliberations regarding the capitalization of leases by the lessee are likely to lead to an increase in the decision usefulness regarding the reporting for investors, in contrast to the former and current capitalization of leases and in contrast to alternative concepts. The pragmatic new direction that was decided in July 2008 for the project – the tentative switch from the further development of the financial components approach to the continued development of the currently valid concepts for the capitalization of finance leases – appears to help also in reaching the objectives. A thorough analysis shows that the financial components approach and the current model for the capitalization of finance leases differ only in their respective basic assumption after the purchase of the rights of disposal and/or the purchase of the leased item. Thus only a slight adjustment of the project was applied. The changed basic direction only results in a different disclosure because by following the current regulations for finance leases – and despite the fictional purchase of the leased item – the lessee even now sets the capitalized leased asset only in the amount of the present value of the minimum lease payment. If an identical measure of value is applied to the lease payments, basically the same transmission of information would result from the two capitalization concepts. Only the need, discussed by the G4+1 working group, for the separate capitalization of options is an exception, which has to be criticized anyway due to its restricted reliability.

The detailed implementation of the central valuation standard of the expected lease payments is decisive for the transmission of basic decision useful information on the basis of the discussion paper. A focus on the probability-proposed best possible estimation of the expected contract period and on the corresponding expected lease payments is recommended. This method should be strictly mandatory for all estimations because it will limit the effects of the unavoidable subjectivity of likelihood on the balance sheet. In the same way, probability-proposed best estimations should be mandatory for the determination of the expected lease payments and the expected utilization of residual value guarantees. The proposal of the IASB should be followed here. Determining the

probability of the various action alternatives that are included needs a detailed explanation.

The decision by the two standard setters in January 2009 to include the future of the capitalization by the lessor in the discussion paper is to be supported in principle, although the need for reforms of the current lessor balance regulations is not that urgent, and the influence of other reform project has to be taken into consideration (IASB 2009a). Moreover, the capitalization regulations for the lessor concern much fewer than the ones for lessees. The early harmonization of the lessee and lessor capitalization has to be endorsed otherwise there would be a danger that the two lease contract parties would have to depict identical facts according to completely different basic concepts despite an identical information basis. This would limit the comparability immensely. In the discussion paper the capitalization by the lessee is only addressed at a highly abstract level. Furthermore, the two standard setters have not yet made a decision with regard to the capitalization by the lessor.

In the future, the capitalization of the expected lease payments by the lessor, which the lessor can expect to receive during the probability-proposed estimated contract period, should be of central importance. In the course of the contract term, the lease payments, expected by the lessee and the lessor, would become gradually closer, due to the lower uncertainty, while at the beginning they would differ due to the subjectivity of the likelihood. The conclusive assessment of the possible future capitalization of leases by the lessee is not possible at this moment, especially because the necessary additional reporting to guarantee the reliability of the information transmission has not yet been addressed. It can be expected that the standard draft (ED), which will be developed on the basis of the discussion paper and by considering the statements that were received until July 19, 2009, will deviate significantly from the conceptual discussion paper. Until the publication of the standard draft (ED) the IASB and the FASB intend to develop one unified opinion (IASB 2009b).

In light of these common objectives, the standard setters have analyzed problem areas of the lease capitalization during the commenting period, which so far have not been addressed. For example, in June 2009 the transition rules for the application of the new lease standard were discussed, which from the present perspective are very significant due to the expected change of paradigms. The standard setters have reached a preliminary decision that lessees have to set all leasing agreements, which exist at the time of the transition, at the present value of the expected lease payments (IASB 2009c p. 4). The proposed basic standardization of the lease capitalization through the capitalization of the expected rental payments would thus not only be mandatory for lease agreements, which were concluded after the date of the implementation.

The interested public could in the meantime use the opportunity to comment and influence the process of setting the standards for the future of capitalization of leases. In September 2009 the duly received comments were analyzed. Approximately one third of the 290 comments received rejected the proposed basic concept in the discussion paper (IASB/FASB 2009, 2, 8). Numerous supporters of the basic concept criticized the complexity of the capitalization of contingent rental payments and optional contract elements that were presented in the discussion paper.

When the received comments are considered, a clear development of the future regulations that are proposed in the discussion paper can be expected with regard to the planned standard draft (ED) in 2010. It remains to be seen whether the future regulations of the capitalization of leases will in fact contribute to an improvement of the decision usefulness of the capitalization of leases, or whether the potential of the concept of the expected rental payments, which should be supported in principle, will not be used to the possible extent due to a flawed implementation.

4.6. Conversion of the Right of Use Concept in Capitalization Leases According to the IFRS by the ED/2010/9 “Leases”

4.6.1. Introduction

With the publication of the joint standard draft “Leases” on August 17, 2010 (ED/2010/9) the IASB and the FASB intended to create a common basis and common regulations for lease capitalization. While the discussion paper that was published in March 2009 by the IASB (IASB 2009b) only intended to regulate the capitalization by the lessee, the current standard draft includes regulations for both the lessor and the lessee. Overview of the most important changes of the ED/2010/9 in comparison to DP/2009/1 is illustrated in Table 3.

The right of use concept that will be used in the future provides a completely new basis for the currently valid regulations of the IAS 17. The objective of the new concept is to provide useful information for the users of financial statements about the amount, the timing and the uncertainties of cash flows from lease contracts. The new regulations are not only intended for newly established lease contracts, but also for already existing lease contracts.

The proposed changes are presented and critically evaluated hereafter. Special attention is paid to the analysis of the effects from a balance sheet point of view and the comparability of the regulations with the future IASB framework concept.

Table 3. Overview of the Most Important Changes of the ED/2010/9 in Comparison to DP/2009/1

	DP/2009/1	ED/2010/9
Application fields	Two possible approaches were introduced: <input type="checkbox"/> Taking over from existing regulations (IAS 17 or SFAS 13) <input type="checkbox"/> Completely new reorientation	<input type="checkbox"/> Orientation on the application fields of IAS 17 and SFAS 13 <input type="checkbox"/> Clarifying differences between both standards
Object of the regulation	<input type="checkbox"/> Capitalization by the lessee <input type="checkbox"/> Initial considerations regarding the capitalization by the lessor	<input type="checkbox"/> Final rules for the Capitalization by the lessee and lessor
Short-term lease contracts	<input type="checkbox"/> Inclusion of short-term lease contracts (max. 12 months) or exception from the application field?	<input type="checkbox"/> Simplified inclusion
Identification in the Performance Obligation Approach on the side of the lessor	Gross disclosure: <input type="checkbox"/> Assets leased + Lease receivables <input type="checkbox"/> Lease liabilities	<input type="checkbox"/> Capitalized as asset or liability net position from the capitalizing of the leased item, receivables and liabilities
Discounting rate for determining the lease obligation	<input type="checkbox"/> Incremental borrowing rate of interest of the lessee	Right of choice: <input type="checkbox"/> Incremental borrowing rate of lessee or <input type="checkbox"/> Effective interest rate of the lease contract
Adopting the discounting rate in the subsequent evaluation	<input type="checkbox"/> No final position of IASB/FASB	<input type="checkbox"/> No adaptation (exception: contingent rental instalments which depends on a reference interest rate)
Subsequent evaluation of the right of use of the lessee	<input type="checkbox"/> Subsequent evaluation of amortized acquisition costs	Right of choice: <input type="checkbox"/> Subsequent evaluation of amortized acquisition cost <input type="checkbox"/> New evaluation at fair value permitted, if all other property assets are newly evaluated as part of the properties in accordance with IAS 16 at their fair value
Depreciation of the right of use on the side of the lessee	<input type="checkbox"/> No final position of IASB/FASB	<input type="checkbox"/> Depreciation according to IAS 16 (depreciation of property assets)
Dealing with purchasing options	<input type="checkbox"/> Same treatment as with the option to renew the lease <input type="checkbox"/> Exercise price at cash value of the leasing payment has to be considered when the liability is determined	<input type="checkbox"/> No consideration of acquisition prices of a purchasing option

Source: compiled by the author

4.6.2. The Standard Draft “Leases”

Changes of basic capitalization principles of leases. According to the currently valid IAS 17, leased items always have to be capitalized by the beneficial (economic) owner. While the legal ownership of a specific leased item is usually attributed to the lessor, the beneficial owner in accordance with IAS 17.7 has to be established under the application of the risk and reward approach. Commonly applied evaluation instruments are, in particular, the existence of a bargain purchase option test (IAS 17.10b), the economic life time test (IAS 17.10c) and the recovery of investment test (IAS 17.10d). If one of these three evaluation instruments shows a positive result, we talk about a finance lease, in which case the leased item has to be fully capitalized by the lessee. If this is not the case, the leased item remains completely in the balance sheet of the lessor (operating lease).

This basic concept, which does not permit allocate the leased item between the lessee and the lessor, is relinquished in the presented standard draft. In future, the lessee fundamentally will have a right-of-use asset for the leased item and an obligation to capitalize the rental payments. In the future, for the lessor the capitalization will depend on whether significant rewards and risks in connection with the leased item remain with him. If this is the case, the lessor cannot write off the leased asset. If all relevant rewards and risks are transferred to the lessee, only a residual value in the amount of the remaining rights to the leased asset remains on the balance sheet of the lessor. The standard draft only assumes a complete transfer of the beneficial ownership to the lessee if the legal ownership of the leased asset is also automatically transferred to the lessee at the end of the agreed lease term, or if a bargain purchase option exists. In this case, the lease contract is considered a sales transaction.

Application field. Fundamentally, the regulations of the standard draft should be applied to all lease contracts, including the lease of right-of-use assets in sub-lease contracts. The only exceptions where the standard draft is not applied are the following (ED/2010/9 5, 7, 8):

- intangible assets (see also IAS 38 Intangible Assets),
- exploration of minerals and fossil energy sources (see also IAS 6 Exploration for and Evaluation of Mineral Resources),
- regarding biological assets (see also IAS 41 Agriculture),
- suspended situations from which a loss is expected (see also IAS 37 Provisions, Contingent Liabilities and Contingent Assets),
- investments in real estate, which according to IAS 40 Investment Property have to be valued at their fair value,
- in cases of an almost complete transfer of the opportunities and risks to the lessee and
- after the purchasing option is exercised by the lessee.

The nearly complete transfer of rewards and risks to the lessee is given in cases when, for example, the legal ownership is automatically transferred to the lessee at the end of the contract period, or if a bargain purchases option in the form of a very bargain price is offered to the lessee (ED/2010/9 B10). In such cases, the lease contract is considered as a sales transaction of the leased item, which then has to be evaluated by applying the general regulations for the purchase and/or sale of property assets. For contracts, which contain both a leasing and a service component, these two components have to be separated if they are distinguishable. The service component then has to be capitalized in accordance with the ED/2010/9 Revenue from Contracts with Customers.

4.6.3. Capitalization by the Lessee

At the beginning of the lease term, the lessee, in accordance with the ED/2010/9 10, has to capitalize a right-of-use asset as the leased asset and a liability for the rental payments (see Table 4). In the statement of comprehensive income, the following positions have to be recorded (ED/2010/9 11):

- a) interest expenses for the lease liabilities,
- b) amortization on the right-of-use asset,
- c) revaluation gains and losses,
- d) changes that result from the new valuation of the lease liability
- e) impairment losses on a right-of-use asset.

The lease obligation has to be capitalized at the beginning of the lease term in accordance with the ED/2010/9 12a in the amount of the discounted lease payments. The discounting method has to be carried out by applying the incremental borrowing rate of interest of the lessee, or, if it can be established, with the interest rate used by the lessor for calculating the rental installments. Only rental installments that will occur with a higher probability than 50% have to be taken into consideration. If the contract has a flexible duration period with an extension option, the probability of it being exercised has to be evaluated for each option. An exercise price for a purchasing option must not be included in the installments. The right-of-use asset has to be capitalized in the amount of the lease liability plus any other initial direct costs incurred by the lessee (ED/2010/9 12b).

During the lease term, the lease liability has to be measured at the amortized cost and at the effective interest rate method, unless a new valuation becomes necessary on the basis of a new assessment of the lease term and the contingent rentals (ED/2010/9 16a in connection with 17). The amortization of the right-of-use asset takes place during the lease term or over the life of the leased item by using IAS 38 (ED/2010/9 20).

According to the ED/2010/9 25, the lease liability has to be separated from other financial liabilities on the balance sheet. In the same way, the right-of-use asset as if they were tangible assets within tangible assets but separately from other tangible assets. The amortization and interest expenses from lease contracts have to be declared in one of the two – either a statement in the comprehensive income statement or in the notes (ED/2010/9 26). In accordance with the ED/2010/9 27 the lease payments have to be declared separately under the cash flow from financing activities in the cash flow statement.

Table 4. Overview of Capitalization by the Lessee

	Approach	Disclosure	Evaluation	
			Initial evaluation	Subsequent evaluation
Right of use	<input type="checkbox"/> Contract is in the application field of ED <input type="checkbox"/> Approach at the beginning of the lease agreement	<input type="checkbox"/> Separate within the tangible assets	<input type="checkbox"/> Cash value of rental payments plus direct costs	Conditional right of choice: <input type="checkbox"/> Amortized acquisition cost (amortization during the contract period or during a shorter economic ND); regarding the depreciation IAS 36 has to be taken into consideration or <input type="checkbox"/> Fair value, if all assets are evaluated as part of the tangible asset according to IAS 16 at fair value; regarding the depreciation IAS 38 has to be taken into consideration
Liabilities from future rental payments	<input type="checkbox"/> Contract is in the application field of ED <input type="checkbox"/> Approach at the beginning of the lease agreement	<input type="checkbox"/> Separate disclosure (separate from other financial liabilities)	<input type="checkbox"/> Cash value of rental payments	<input type="checkbox"/> Amortized acquisition cost under the application of the effective interest method

Source: compiled by the author

According to the ED/2010/9 25, the lease liability has to be separated from other financial liabilities on the balance sheet. In the same way, the right-of-use asset as if they were tangible assets within tangible assets but separately from other

tangible assets. The amortization and interest expenses from lease contracts have to be declared in one of the two – either a statement in the comprehensive income statement or in the notes (ED/2010/9 26). In accordance with the ED/2010/9 27 the lease payments have to be declared separately under the cash flow from financing activities in the cash flow statement.

Example. An enterprise signs a lease contract as a lessee for the use of a machine (average useful life: 8 years) for 6 years with an annual rental installment of €30,000, which has to be paid at the beginning of each year. The lease contract does not include options for extension or purchase. Maintenance and repair costs are covered by the lessee. The internal interest rate that is applied by the lessor is not known to the lessee. The incremental borrowing rate of interest of the lessor is 6%. The lease liability is €156,371 and is based on the rental installments that are discounted by the incremental borrowing rate of interest. The value calculated on the basis of the effective interest method is €126,371 as of December 31, 2011. The right to use the leased item also has to be evaluated with €156,371 at the time of the start. If a straight line depreciation of €26,062 is applied to the lease term of six years, a book value of €130,309 as of December 31, 2011 results.

The balance sheet of the lessee therefore contains the following items on December 31, 2011:

<i>Right to use the leased item</i>	130,309
<i>Lease liabilities</i>	126,371

In the comprehensive income statement of the lessee for the year 2011 the following items from the lease contract have to be included:

<i>Depreciation regarding the right to use the leased item</i>	26,062
<i>Interest expenses resulting from the lease contract</i>	7,582
<i>Loss from the leased contract</i>	33,644

4.6.4. Capitalization by the Lessor

Choosing a method. The standard draft provides two different capitalization methods of lease contracts for the lessor, namely the performance obligation approach (see Table 5) and the de-recognition approach (see Table 7). The decisive element for the use of these methods is the level of rewards and risks that remain with the lessor with regard to the leased item and subsequent to the termination of the lease term. If significant rewards and risks remain with the

Table 5. Overview of Capitalization by the Lessor According to the Performance Obligation Approach

	Approach	Disclosure	Evaluation	
			Initial evaluation	Subsequent evaluation
Leased item	<input type="checkbox"/> General approach criteria according to framework and IAS 16 or IAS 40 in the case of investment properties	Separate disclosure of leased asset, receivables, liabilities and net balance → Disclosure of a net position as an asset or liability	<input type="checkbox"/> According to IAS 16 or IAS 40	<input type="checkbox"/> According to IAS 16 or IAS 40 in connection with IAS 36
Receivables from lease payments	<input type="checkbox"/> Contract is in the application field of ED <input type="checkbox"/> Approach at the beginning of the lease agreement		<input type="checkbox"/> Cash value of lease payments plus direct costs	<input type="checkbox"/> Amortized acquisition costs by application of the effective interest method <input type="checkbox"/> If necessary, new evaluation of the parameters lease term, conditional rental instalments, transfer fees and residual value guarantees <input type="checkbox"/> Application of IAS 39 (depreciation in cases of financial assets)
Obligations resulting from leave for use	<input type="checkbox"/> Contract is in the application field of ED <input type="checkbox"/> Approach at the beginning of the lease agreement		<input type="checkbox"/> Cash value of rental payments	<input type="checkbox"/> Reduction according the economically useful life <input type="checkbox"/> If necessary, mirror image adaptation to receivables

Source: Compiled by the author

lessor, the performance obligation approach has to be applied; otherwise the de-recognition approach has to be applied (ED/2010/9 28).

Performance obligation approach. At the beginning of the lease term, the lessor, in accordance with the ED/2010/9 30, has a right to receive rental payments (lease receivables) and to recognize lease liability. The leased item must not be de-recognized. During the contract term, the following items have to be declared in the comprehensive income statement (ED/2010/9.31):

- a) interest income from lease payments.
- b) lease income in the amount of fulfilling the lease liabilities.
- c) changes resulting from a new valuation of the lease receivables according to ED/2010/9. 39.
- d) impairment losses on the right to receive of lease receivables.

Lease income has to be declared as sales revenues if lease is part of the usual business activity of an entity. The lease receivables and the lease liabilities have to be capitalized at the beginning in the amount of the discounted rental payments, plus any initial direct costs of the lessor; the interest rate that is used by the lessor to charge the lessee has to be applied as the discounting rate (ED/2010/9 33). The valuation of the lease receivables during the lease term is based on the amortized cost and on the effective interest method. According to the ED/2010/9 37b, the remaining lease liability has to be set at the amortized cost. If it cannot be determined clearly, the lease liability has to be amortized in straight line. The leased items, the lease receivables, the lease liabilities and the resulting net leased asset value or net lease liability have to be recognized on the balance sheet of the lessor (ED/2010/9 42). The interest income from lease receivables, the lease income from the fulfillment of lease obligations and the depreciation on the leased item in accordance with the ED/2010/9 44 have to be declared separately from other positions in the comprehensive income statement.

Example. An enterprise in the role of the lessor acquires a machine on January 2, 2011 with an average useful life of 8 years. The acquisition cost is €200,000 (plus VAT). At the same time, the lessor concludes a lease contract with a lessee for the use of this machine for a period of 6 years, with an annual rental payment of €30,000. The payments have to be paid at the beginning of each year. This lease contract does not include options for extension or purchase. Maintenance and repair costs are covered by the lessee. The lessor expects proceeds of €60,000 through the sale of the machine at the end of the lease term. The lessor has to set the leased item at the beginning at the acquisition cost of €200,000. As of December 31, 2011, the book value has to be reduced by the scheduled depreciation of €25,000. For the evaluation of the lease receivables and the lease liabilities, the internal interest rate of the lease agreement has to be determined. For this, the expected series of payments has to be set up (Table 6).

Table 6. Calculations for Expected Series of Payments

	Jan. 2, 2011	Jan. 2, 2012	Jan. 2, 2013	Jan. 2, 2014	Jan. 2, 2015	Jan. 2, 2016	Jan. 2, 2017
<i>Acquisition cost</i>	-200,000						
<i>Rental payments</i>	+30,000	+30,000	+30,000	+30,000	+30,000	+30,000	
<i>Proceeds from sale</i>							+60,000
<i>Total amount</i>	170,000	+30,000	+30,000	+30,000	+30,000	+30,000	+60,000

Source: compiled by the author

The internal interest rate for this payment series is 5.77%. To determine the lease receivables and the lease liability, the six rental payments of €30,000 each have to be discounted with the internal interest rate, and thus the initial figure of €157,155 results. On 31.12.2011, the balance sheet amount of the lease receivables is reduced to €134,496 by applying the effective interest rate because only five rental payments are still open. Due to the absence of information about the utility structure of the lessee, the lease liability has to be amortized over a period of six years by €26,192 to €130,963. Therefore, in the balance sheet of the lessor the following items are included on December 31, 2011:

<i>Leased asset</i>	175,000
<i>Lease receivables</i>	134,496
<u><i>Lease liability</i></u>	<u>(130,963)</u>
<i>Net leased asset value</i>	178,533

The comprehensive income statement of the lessor for the year 2011 includes the following items from the lease contract:

<i>Interest income from the lease receivables</i>	7,341
<i>Lease income from fulfilling the lease liabilities</i>	26,192
<u><i>Depreciation on the leased asset</i></u>	<u>(25,000)</u>
<i>Profit from the lease agreement</i>	8,533

De-recognition approach. If only insignificant rewards and risks from the leased asset remain with the lessor, the de-recognition approach is applied. When this approach is used, the rights to receive rental payments have to be capitalized at the beginning of the lease agreement. In return, the balance sheet amount with regard to the leased assets has to be reduced by the value of the right of use by the lessee. The residual asset value, which represents the rights to the leased asset that remain with the lessor, remains part of the assets of the lessor.

Table 7. Overview of the Capitalization by the Lessor According to the De-recognition

	Approach	Disclosure	Evaluation	
			Initial evaluation	Subsequent evaluation
Leased item	<input type="checkbox"/> General approach criteria according to the framework and IAS 16 or IAS 40 in cases of investment properties	Disclosure in „Residual value“	Residual value =	No subsequent evaluation, except: <input type="checkbox"/> in cases of change of the leasing period or <input type="checkbox"/> application of IAS 36 (depreciation of assets)
Right of use of the lessee from the perspective of the lessor	<input type="checkbox"/> Contract is in the application field of ED <input type="checkbox"/> Approach at the beginning of the lease agreement		<input type="checkbox"/> Book value Leased item in $t_0 - q$ with: <input type="checkbox"/> Disposal value $q = (\text{fair value of receivables} / \text{fair value leased item}) * \text{Book value leased item in } t$ <input type="checkbox"/> Book value according to IAS 16 or IAS 40	
Receivables from lease payments	<input type="checkbox"/> Contract is in the application field of ED <input type="checkbox"/> Approach at the beginning of the lease agreement	<input type="checkbox"/> Separate disclosure (separate from other financial assets)	<input type="checkbox"/> Cash value of lease payments plus direct costs	<input type="checkbox"/> Amortized acquisition costs by applying the effective interest method <input type="checkbox"/> If necessary, a new evaluation of the parameters lease term, contingent rental instalment, transfer payments and residual value guarantees <input type="checkbox"/> Application of IAS 39 (depreciation in cases of financial assets)

Source: compiled by the author

Lease income has to be reported as sales revenue if leasing is the usual business activity of an enterprise. The lease receivables have to be recognized in the balance sheet in the amount of the discounted rental payments plus any initial costs of the lessor; the discount rate of the interest rate, which the lessor charges to the lessee, has to be applied to this (ED/2010/9 49a). In addition, the residual asset in the amount of the remaining rights to the leased item has to be capitalized. To determine this value, the fair value of the rights (to the leased item) that were transferred to the lessee, have to be put into relation to the fair value of the rights that remain with the lessor. Based on this ratio, the book value of the leased item has to be divided between the lessor and the lessee. The value that has to be written off by the lessor at the beginning of the lease term is determined by applying the following formula (ED/2010/9 50):

$$\text{Value of the residual asset} = \frac{\text{Fair value of rental payments}}{\text{Fair value of leased item}} \times \text{Book value of leased item}$$

During the lease term, the lease receivables have to be valued at the amortized cost and by applying the effective interest method. This applies as long as no new valuation on the basis of new assessments regarding the lease term or contingent rental payments or impairment is necessary (ED/2010/9.54 in connection with 56 (a) and 58). A new valuation of the residual asset during the lease term does not have to be carried out, unless indications about the change of the lease term exist, or impairment is necessary (ED/2010/9 55 in connection with 56a and 59).

The following positions have to be declared on the balance sheet of the lessor:

- a) lease receivables, separate from other financial assets
- b) the residual asset, separate from other tangible assets (ED/2010/9 60).

The presentation in the comprehensive financial statement in line with the ED/2010/9 61 depends on the business model of the lessor. If the lessor offers leasing only as an alternative to the sale of goods, then the income and expenses from leases have to be reported analogously with sales revenue and cost of sales separately. However, if the lease is only a financing service, then the lease income and lease expenses have to be reported in a net position. Interest income from lease contracts has to be reported separately from other interest income in the comprehensive income statement. In the cash flow statement if the direct method is applied the cash receipts from rental payments are shown separately from operating activities. For indirect method the changes in the right to receive lease payments are shown separately from changes in other operating receivables.

Explanatory disclosure notes. With the help of numerous qualitative and quantitative explanatory disclosure notes detailed information should be conveyed to the recipients (ED/2010/9.70) of the annual financial statement, such as

- the amounts reported the financial statements and
- the effect from amount, timing and uncertainty to the future cash flow from the lease agreement.

According to the ED/2010/9 73, it is necessary to explain the nature of the lease agreement in detail.

4.7. Effects on Selected Subject Areas

4.7.1. Sale and Leaseback Transactions

Within the framework of a sale and leaseback transaction the legal ownership of a property asset is transferred from the seller to the buyer through a sales transaction. Subsequently, the buyer grants a right to the seller to use the same item of property.

The lease contract between the buyer in the role of the lessor and the seller in the role of the lessee has to be quantified as a finance or operating lease in accordance with the currently valid regulations of the IAS 17. If it is a finance lease, the beneficial ownership is transferred back to the seller. In this case, IAS 17.59 stipulates that any excess of sales proceeds over the carrying amount shall not be immediately recognized as income by the seller-lessee. Instead, it shall be deferred and amortized over the lease term. In the case of an operating lease, the legal ownership is transferred with the beneficial ownership to the buyer and thus, the seller has to realize the profit from the sale (IAS 17.61).

According to the ED/2010/9 66–69 the evaluation of a sale and leaseback transaction depends on, whether the sales contract meets the criteria of a purchase or a sale of the asset. If, through the contract almost all rewards and risks are transferred to the buyer, the seller has to capitalize the sale in accordance with the relevant IFRS and evaluate the lease contract in accordance with the ED/2010/9. The buyer also has to capitalize the asset in accordance with the relevant IFRS and has to disclose the lease agreement according to the performance obligation approach within the meaning of the ED/2010/9 30–45.

If the criteria for a sale are not fulfilled, for example, if the legal ownership is automatically transferred back to the seller at the end of the lease contract on the basis of a bargain purchase option, the seller cannot write off the asset and has to capitalize the sales price as a financial liability. At the same time, the buyer cannot recognize the item in his/her balance sheet and instead has to capitalize the purchasing price as a receivable.

If the sale price or the rental payments do not correspond to the fair value, the buyer has to adapt the evaluation of the right of use on his balance sheet for the leased item to the usual market conditions for rental payments and the profit or loss from the disposal of the leased item by the difference between the agreed rental payments and the usual rental payments in the market.

The buyer has to adapt the book value of the leased item and the lease liability to the usual market conditions for rental payments (ED/2010/9 69). In the framework of a sale-and-leaseback-transaction the lessee has an obligation to provide explanations in the notes. The most important conditions in connection with the transaction and the profits and losses resulting from the transaction have to be declared (ED/2010/9 76).

4.7.2. Multi-level Lease Agreements

Since IAS 17 does not include concrete regulations concerning multi-level lease agreements, within the meaning of IAS 8.12 and the regulation in ACS 840 has to be applied for the time being. According to the applied top-down-approach, first the main lease agreement and then the sub-lease agreement have to be evaluated. If, in the main lease agreement, the rewards and risks are transferred to the lessee (finance lease), then the lessee can in turn transfer the beneficial ownership to his lessee. However, if the main lease contract is already an operating lease, then the sub-lease agreements must also be qualified as operating leases.

According to the ED/2010/9 5 the general regulations for lease agreements are also applied to sub-lease agreements. Thus, at every level a new examination takes place on which rights to the leased asset have been transferred to the lessee. Then, based on the ratio of the remaining rights to the transferred rights, a division of the capitalization obligations between the lessor and the lessee is determined.

A lessee, who at the same time is lessor of the same leased item, has to recognize into the balance sheet the lease liability from the main lease agreement and the assets and liabilities from the sub-lease agreement individually. In addition, the balance of these three positions must be either capitalized as a net leased asset, or as a net lease liability from the sub-lease agreement (ED/2010/9 43 in connection with B29). Significant sub-lease agreements have to be disclosed additionally in the notes and separately from the main lease agreement (ED/2010/9 74).

4.7.3. Evaluation of the Standard Draft

Abolition of balance sheet related leeway concerning the approach. The current classification of lease contracts required by the accounting standards for lease agreements, namely the classification into finance leases and operating lease, has caused considerable problems of demarcation. The following balance sheet related instruments developed from that situation:

- in the case of lease agreements that are located in the peripheral area of these two categories, a certain scope of discretion with regard to the classification exists.
- through an arrangement of the facts, lease contracts can be prepared in such a way that the desired balance sheet consequences will result.

The classification to one of these two categories results in the fact that the leased asset has to be completely capitalized either by the lessor or by the lessee, a decision that has enormous effects on the balance sheet. Therefore, the accounting standards have considerable influence on the setup of the lease contract, and the original fiscal objectives of leases are sometimes moved into the background.

According to the new concept of the standard draft, the either/or decision concerning the classification of leased items will no longer exist. Instead, it will be analyzed as to which rights and obligations the contract partners have agreed on in the lease agreement. These rights and obligations will have to be evaluated and be capitalized in the respective balance sheets of the lessor and lessee as assets or as liabilities. Therefore, the economic consequences of the lease agreement can be portrayed much more precisely on the balance sheets. The current scope of discretion for companies with balance sheets will be abolished, and the depiction on the balance sheet will have much less influence on the contract setup in future.

Creation of new balance sheet related leeway within the framework of the evaluation. The advantages of the right of use concept in the framework of the balance sheet approach are brought through new balance sheet related leeway in the evaluation. The evaluation of individual balance sheet positions on the side of the lessee or lessor depends on the assessment of the probability that options are exercised or on the occurrence of certain conditions.

The more flexible the lease agreements are set up, the larger the scope of discretion in the evaluation will be. It should be noted as positive that the right of the lessee to use the leased asset does not have to be evaluated independently at the time of initiation, but will be set in the amount of the lease liability plus any direct initial costs. The lease liability results from the discounting of the

expected rental payments and by applying the interest rate, which the lessor will charge to the lessee or, if this rate is not known, the incremental borrowing rate of interest of the lessee is applied. Thus, the lessee has little influence on the applied interest rates. An independent evaluation of the right of use would lead to high complexity in cases of termination or extension options, purchasing options, right to tender, residual value guarantees or contingent rental payments. By the lessor the lease receivables and lease liabilities are also determined through the discounting of the rental payments plus any initial costs.

Relationship to the future IASB framework concept. According to the ED/2010/9, the financial reporting of lease agreements should be compatible with the new IASB framework concept, which is now under discussion. One question is whether optional or contingent rental payments can fulfill the definition of criteria for receivables/liabilities at all. According to the current state of the discussion on the future IASB framework concept, an asset should be defined as a present economic resource to which the entity has a right or other access that others do not have. However, it is not necessary that this right to the asset or the access to it is legally enforceable. Therefore it is likely that a lease receivable that the lessor will receive with a higher than 50% probability will be capitalized as an asset because according to the current economic circumstances it is more favorable for the lessee.

In future, a liability is to be defined as a present economic obligation to which the entity is the obligor. An entity is to be a debtor only in the sense of this definition, if the economic obligation is legally enforceable. Thus, a lessee should not capitalize an obligation for contingent or optional rental payments as long as the condition does not occur, or as long as the option has not been exercised. Therefore, the approach of lease liabilities to contingent or optional rental payments according to the ED/2010/9 contradicts the intended liability definition in the future IASB framework concept. However, the application of the planned asset and liability definition of the future IASB framework concept does not allow for a reasonable characterization of the economic reality. The lessor would have to capitalize lease receivables and a lease liability if the performance obligation approach were applied. The lessee, however, could only capitalize a right of use and could not capitalize lease liability. Here, it becomes a problem that legal enforceability is demanded for capitalization of a liability but not for the capitalization of an asset. A possible solution could be that legally not enforceable liabilities are capitalized as liabilities if the enterprise is likely to make this commitment in order to maintain or recognize an asset.

4.8. Interim Conclusions

In the case of the ED/2010/9 “Leases”, the lease capitalization in the IFRS-capitalization is placed on a new basis. While until the present time the leased

asset was completely allocated to the beneficial owner on the balance sheet with the right of use concept, from now on, as a rule, it will be necessary to divide it between the lessor and the lessee. The new concept reduces the balance-related leeway regarding the balance approach because an either/or decision regarding the allocation of the leased item can no longer be made. The division of the right to use the leased item between the lessor and lessee, required by the right of use concept – does increase the scope of discretion regarding the evaluation. However, more substantial and useful information on the economic consequences of lease agreements will be transmitted to the final recipients; therefore the reform has to be welcomed. Existing inconsistencies between the ED/2010/9 and the intended definitions of assets and liabilities will have to be corrected during the development of a new IASB framework concept.

The IASB did not only move away from its original proposals with regards to the lease capitalization. During the commenting period, more than 760 letters were received by the IASB. Although the endeavor to reform the lease capitalization was welcomed in principle, both the complexity of the new approach and the expected higher costs of the implementation met with criticism. The IASB has taken these points of criticism into consideration and in 2011, besides the development of the receivable and residual models, various changes were adopted. Some of these are the following:

- simplification of short-term lease agreements (contract duration period is shorter than 12 months)
- definition of the duration of the lease agreement
- inclusion of variable rental payments when determining the lease liabilities only if they are index-based or, from an economic perspective, are considered minimum rental payments

At this point in time the revision of the original standard draft by IASB and FASB has not yet been concluded. It can be expected that in the third quarter of 2012 the revised ED will be published and that the comment period of the revised ED will end in the second quarter of 2013. In the second quarter of 2013 the new standard should be published, and, after another comment period and an additional lead time of at least one year, the standard could be effective from January 1, 2015.

5. CONCLUSION

With the joint publication of the standard draft “Leases” (ED/2010/9) on August 17, 2010, IASB and FASB intend to place the regulations for the capitalization of leases on a common footing. While the discussion paper “Leases – Preliminary Views” by the IASB, published in March 2009, intended to regulate only the capitalization by the lessee, the current standard draft includes regulations for the lessor and the lessee. The right of use concept that will be used in future will place the capitalization of leases on a completely new basis in comparison with the currently valid regulations of the IAS 17. It is the objective of the new concept to convey useful information to the addressees of annual financial statements, especially concerning the amount, the timing and the uncertainties of the cash flow from lease contracts.

Against this background, the objective of the thesis has been to research the need to reform of the current capitalization of leases and to analyze reporting about lease agreements in the context of the capitalization concepts discussed as part of the current leasing project of the IASB/FASB and regarding their propagated and improved decision usefulness for the enterprises.

Regarding the evaluation benchmark for analyzing the current regulations and for the lease capitalization reform proposals, the economic approach according to the HGB had to be characterized and the significance of substance over form according to the International GAAP had to be researched. For the sake of precision of the selected object of research, lease agreements were analyzed on the basis of civil law with the help of the method of an overall observation. The transfer of the use could be identified as the main function of lease agreements. Depending on the will of the contract parties and the related construction of the lease agreement, the proportional relevance of the transfer of use function and the equally important finance function can vary. In the process of creating the contract, the distribution of the risk may vary between the lessor and the lessee. Separated from the national jurisdictions and on the basis of the property rights theory, and from an economic perspective, a concept for the further research of lease agreements was developed. According to this, a lease agreement constitutes the temporal transfer of rights of disposition against payment, which leads to, at least, the separation of the right of use from the legal ownership.

With this reference frame as a background, the currently valid regulations for lease capitalization according to the International GAAP and their decision usefulness were discussed. In doing so it was established that the current guidelines for the lease capitalization according to the International GAAP are based on the fundamental concept of risk and reward approach. For the purpose of capitalization, all lease agreements have to be classified as finance leases and operating leases, depending on the allocation of rewards and risks in connection

with the leased asset. The capitalization of the leased asset results from the classification. The International GAAP follows the all or nothing approach, according to which, in cases of finance leases, the leased asset and the corresponding lease liability have to be capitalized by the lessee, while in the case of operating leases the lessee does not have to report the lease agreement in its balance sheets. The effects on the balance sheet of this all or nothing approach have been illustrated, and the distinct interest of the lessee in a contract of the operating lease category has been pointed out. In addition, it was stated that with the current contract classification the resulting effects in the balance sheet of the lessor are far smaller than the ones on the lessee.

The analysis of the decision usefulness of the current lease capitalization showed that the decision relevance of the reporting, on the basis of the currently valid capitalization of leases, exists only in a restricted way. The all or nothing approach leads to an incomplete transmission of information because in the case of an operating lease the lessee capitalized neither the asset nor the obligation that results from the lease contract. Even mandatory additional reporting cannot prevent a lack of necessary information for investors about predicted payments. In addition, the omission of contingent rental payments and the exclusive consideration of favorable purchase and extension options prevent a complete transmission of information. The independent capitalization from the legal ownership of lease agreements according to the IAS 17 and the ASC 840 can fundamentally be supported from the economic approach perspective (substance over form) if the depiction of the facts correspond with the assumed constellation of an outside finance purchase or rent in finance leases and operating leases.

Contrary, capitalization according to the all or nothing approach of operating leases and finance leases motivates the contract parties towards less distinct contract constellations, which enable the classification as operating leases in accordance with current leasing standards. The current division of lease capitalization into two (categories) suggests the possibility of a clear classification of facts. Facts that are nearly identical from an economic viewpoint are projected in contrasting ways, something that is in contradiction to the side conditions of the economic approach. During the analysis of the currently valid capitalization guidelines for lease agreements, numerous depiction leeways, which prevent the inter-company comparability, have been identified. Since the contract classification according to the IAS 17 provides only qualitative orientation help, which is then integrated into the overall evaluation of the economic conditions, the contract categorization according to the International GAAP is similar to the actual right of choice. In contrast, the quantitative classification criteria in the HGB and in the US GAAP reduce the depiction leeways, but they enable the bypassing of these limiting values through the various contract constellations. The comparability is significantly

reduced through the contrasting capitalization by the lessee as a result of the contract classification according to the all or nothing approach. Due to the insufficient reporting about the perception of depiction leeways and the contract categorization, the comprehensibility of the transmitted information is reduced.

Following the results of the analysis of current regulations for the capitalization of leases, the information reliability needs to be improved. As has been stated, especially the neutrality of the information transmission regarding the contract classification is under threat due to the depiction leeways because the capitalization according to the all or nothing approach can lead to a biased report by a lessee who seeks to not capitalize the lease agreement. The flawed additional explanations for the use of the depiction leeways and contract categorization lead to a lack of verifiability of the information regarding the capitalization, and thus they do not serve the objective of the minimum objectification. The result of the analysis of the decision usefulness confirms the need for the reforms of the current lease capitalization that has been stated by the IASB and the FASB.

Based on these insights, the research in Chapter 4 examined whether the current reform efforts by the two standard setters could increase the decision usefulness of the information that is transmitted by the capitalization of leases. In the context of the capitalization concepts suggested by the of the G4+1 working group, namely the financial components approach and the whole asset approach had to be discussed as these two concepts served as the basis for the possible capitalization of leases in the framework of the leasing project. Both concepts basically suggest the standardization of the capitalization of leases and that the classification according to the current regulations should be omitted.

Through the financial components approach, the fundamental capitalization of rights of use by the lessee and the capitalization of the resources in form of assets and liabilities under the control of the lessee are proposed. The position papers of the G4+1 working group thus lead to turning away from the all or nothing approach, and depending on the contract constellations, they lead to the balance sheet impact effectiveness of all lease agreements. The contract regulations, in contrast to the currently valid leasing standards, would only influence the amounts stated regarding individual and separate rights of use (that have to be capitalized) and lease obligations, which would be determined by the unavoidable contractual payments by the lessee. In contrast, the lessor would have to capitalize the receivable to the contractually agreed payments and the remaining right of use, regularly with him, at the end of lease term; both contract parties would capitalize the part of the potential benefits, over which each of them has control.

The decision usefulness of the capitalization, according to the financial components approach, the decision relevance of the transmitted information due to the balance sheet impact effectiveness at the lessee and due to the standardization of the lease capitalization due to the capitalization of the respective rights of disposition of the contract parties is analyzed. However, it became clear that the full transmission of information is limited due to the omission of the optional contract periods and the use-based rental payments as part of the central valuation standard of the minimum rental payments. In this context, the enhanced consideration of likelihood-considerations in the balance sheet appeared recommendable. The analysis also showed that through the capitalization of rights of disposal, the continuous transition from a short-term cession of use to an agreement similar to a purchase is made possible, which corresponds with the economic approach. Through the standardization of the capitalization of leases the inter-company comparability will be guaranteed in principle.

However, it also became clear that the reliability of the capitalization, according to the financial components approach, is only available with restrictions. Especially, the separate evaluation of contract components beyond the central right of use, which has to be applied in accordance with the reform proposals, results in numerous leeway depictions. Therefore, as part of a possible further development of the concept of the financial components approach, especially the additional reporting about completed estimations and the premises under consideration should be made more precise.

As a result of the analysis of the financial components approach, it had to be stated that, in principle, decision relevant information about lease agreements is transmitted. The extensive leeway depictions due to the increased evaluation complexity lead to a significant lack of reliability, and through this the decision usefulness of the proposed capitalization of leases is reduced considerably.

Following the whole asset approach that is discussed as an alternative concept, the basic principles of the current capitalization of leases according to the International GAAP and the US GAAP would no longer be classified either to the lessee or the lessor in accordance with the distribution of the rewards and risks. However, contrary to the financial components approach, no rights of use but independent from the contract details the entire leased item should be capitalized by the lessee. The corresponding total obligation of the lessee according to the whole asset approach consists of the payment obligation of the rental installments during the lease term and of the obligation to return the leased item at the end of the contract. In contrast, the lessor capitalizes his receivable to the agreed rental installments and to the return of the leased item.

In the course of the analysis of the decision usefulness of the whole asset approach it could be demonstrated that the information transmitted in accordance with the proposed concept is only decision relevant in a very limited way. The first fixation of the leased item with the lessee, independent from the lease term, at the amount of the fair value suggests incorrect future payments for the whole economic life of the leased item. In addition, and with the background of the necessary economic approach (substance over form) the lacking differentiation between temporary leases and the purchase of the entire leased item with outside financing has to be criticized.

In contrast, the reliability of the information transmission according to the whole asset approach appears to be intact. Due to the standardized capitalization of the leased item at the fair value a neutral transmission of information is basically assured. Based on the insights of the research of the alternative capitalization concepts under discussion, the process of the current IASB/FASB leasing project – as part of the convergence project of the two standard setters, was outlined, and the discussion paper “Leases – Preliminary Views”, which was published on March 19, 2009 and the Exposure Draft 2010/9, which was published on August 17, 2010 were introduced.

The discussion paper that focuses on the future of capitalization of leases by the lessee, aims for a fundamental standardization of the lease capitalization by capitalizing the expected rental payments. Lease agreements are interpreted as the purchase of a right of use in the discussion paper. This basic assumption is similar to the current regulation of finance leases, which is based on the assumed purchase of the entire leased item; and it is also similar to the assumed purchase of several rights of disposition, which is in accordance with the financial components approach. However, this leads to a divergent capitalization. The expected rental payments are proposed as the central valuation standard.

The analysis of the capitalization by the lessee, as suggested in the discussion paper, showed that the decision usefulness of the transmitted information exists. This is due to the balance sheet impact effectiveness of all lease agreements and due to the capitalization of all rights of use that are transferred to the lessee. The inclusion of all expected rental payments from contingent rental installments during the expected contract period leads additionally, contrary to the financial components approach and the sole transfer of the current regulations for finance leases, to a more complete information transmission. However, the inter-company comparability is restricted through the depiction leeways, which result from the determination of the expected rental payments. The examination showed that the best possible estimation of the rental payments should be probability-proposed, because only then all alternatives will be included in the evaluation and the corresponding reports of capitalization are most probable.

Furthermore, the analysis of the discussion paper revealed that the reliability of the reporting would not improve significantly in comparison to the financial components approach and the current capitalization method of finance leases. Especially the central importance of the expected rental payments leads to leeway depictions in relation to the determination of the expected lease term and the expected contingent rental payments. Thus, determining the expected rental payments through the probability-proposed estimation is recommendable; although it would not avoid the subjectivity of likelihoods, but the balance sheet effects will be limited. The capitalization of expected rental payments requires in any case comprehensive additional reporting about the necessary estimations.

The currently valid capitalizing regulations of lease contracts required a categorization into finance leases and operating leases, which has caused considerable demarcation problems. Subsequently, the balance sheet related instruments for the capitalizing entity result in the following:

- concerning the lease agreements located in the border areas between these two categories, the capitalizing entity has a certain leeway with regards to the allocation;
- through the arrangement of facts, lease contracts can be designed in such a way that the desired balance sheet results will appear.

Classified into one of these two categories the leased item will be capitalized completely either by the lessor or by the lessee, and thus the balance sheet consequences of this decision are enormous. Thus, capitalization regulations have a considerable influence on the setup of lease contracts, and as a result, the original fiscal objectives of leasing are sometimes pushed into the background. In the new concept of ED/2010/9, this kind of either/or decision regarding the allocation of the leased item does not exist anymore. Instead an analysis of the rights and obligations the contract partners have agreed upon in the contract has to be made. These rights and obligations have to be evaluated and then capitalized in the respective balance sheet of the lessee and lessor as assets or as liabilities, respectively. The economic impact of the lease agreement can therefore be reflected much more precisely in the balance sheets. The leeway that capitalizing entities had so far in borderline cases will be eliminated and the reflection in the balance sheet will have much less influence on the contract setup in the future.

The evaluation of individual balance sheet positions on the sides of the lessee and lessor depends on the assessment of the likelihood of the exercise of an option or on the occurrence of conditions. The more flexible the agreement of lease is, the larger the leeway in the evaluation is. As a positive aspect, it should be mentioned that the right of use of the lessee to the leased item does not have

to be evaluated independently as part of the access, but it has to be set at the amount of the lease liability, plus possible direct initial costs.

The capitalization of lease agreements according to ED/2010/9 should be in accordance with the new IASB framework concept that is under discussion. It is particularly questionable whether optional or contingent rental installments can actually fulfill the definition criteria of liabilities. According to the current state of the discussion, in accordance with the future IASB framework condition, an asset should be defined as a present economic resource to which the entity has a right or other access that others do not have. However, it is not necessary for the right or the access to the asset to be legally enforceable. Therefore, a lease liability also can be capitalized as an asset, if the lessor will receive the lease liability with a probability of more than 50%, since it is more profitable for the lessee under current economic circumstances to exercise the renewal option, for example.

In future, a liability should be defined as a present economic obligation for which the entity is the obligor. According to with this definition, an entity should only be a debtor if the economic obligation is legally enforceable. Therefore, a lessee should not capitalize a liability for contingent or optional rental installments as long as the condition has not occurred, or the option has not been exercised. Therefore, the basis of a lease obligation for contingent or optional rental installments according to ED/2010/9 contradicts the intended liability definition in the future IASB framework concept. However, according to the future IASB Framework concept, the application of the planned asset/liability definitions would not allow a reasonable depiction of the economic reality. If the performance obligation approach is used, the lessor would have to capitalize lease receivables and a lease liability, but the lessee could only capitalize the right of use but not recognize the lease liability. The problem that arises here is the fact that for the recognition of a liability the legal enforcement is required, but this is not so for the recognition of an asset. A solution could be that legally not enforceable obligations are capitalized as liabilities, if they are entered by the entity in order to preserve or report an asset.

With ED/2010/9 “Leases” the capitalization of leases is placed on a new basis. If at present the leased item was capitalized completely in the beneficial owner’s balance sheet, then in future, according to the right of use concept, a division between the lessor and the lessee is required. The necessary division of the leased item in accordance with the right of use concept increases the leeway during the evaluation process. The new concept removes the balance sheet relevant leeway. Since the addressee of annual financial statements receives considerably more useful information about the economic consequences of the lease agreements, the reform has to be welcomed. Existing inconsistencies between the ED/2010/9 and the previously intended definitions of assets and

liabilities have to be eliminated during the development of the new IASB Framework concept.

It can be expected that in the third quarter of 2012 the revised Exposure Draft will be published and that the comment period of the revised Exposure Draft will end in the first quarter of 2013. In the second quarter of 2013 the new standard should be published and, after another comment period and an additional lead time of at least one year, the standard could be effective from January 1, 2015.

REFERENCES

- ALVAREZ, M., WOTSCHOFSKY, S., MIETHIG, M.** 2001. Leasing-verhältnisse nach IAS 17 – Zurechnung, Bilanzierung, Konsolidierung, in: Die Wirtschaftsprüfung (WPg), Booklet 18, Edn. 54, Düsseldorf: IDW Verlag, pp. 933–947.
- ARDEN, M.** 1993. The up-dated Opinion of English Counsel on true and fair (21 April 1993). In: Parker, R. H. and Nobes, C. W. An International View of True and Fair Accounting. London: Routledge, 1995. pp. 147–152
- ARDEN, M.** 1997. True and fair view: a European perspective. *European Accounting Review*, 6 (4), London: Routledge, pp. 675–679.
- BALL, K.** 1924. Steuerrecht und Privatrecht: Theorie des selbständigen Steuerrechtssystems, die gegenwärtigen Beziehungen zwischen Steuerrecht und Privatrecht und ihre Entwicklung, untersucht am Gegenstände der Besteuerung, eine verwaltungsrechtliche Studie, Mannheim: J. Bensheimer Verlag.
- BALLWIESER, W.** 2003. Rahmenkonzepte der Rechnungslegung: Funktionen, Vergleich, Bedeutung, in: Der Konzern, Köln: Carl Heymanns Verlag, pp. 337–348.
- BARSKÉ, K.** 1976. Die wirtschaftliche Betrachtungsweise, in: Neue Wirtschafts-Briefe für Steuer- und Wirtschaftsrecht, Fach 2, Herne: NWB Verlag, pp. 2937–2948.
- BAY, W., BRUNS, H.-G.** 2000. Internationalisierung der Unternehmenspublizität als Folge globaler Unternehmenstätigkeit, in: Haller, Axel/Raffournier, Bernard/Walton, Peter (Ed.), Unternehmenspublizität im internationalen Wettbewerb, Stuttgart: Schäffer-Poeschel Verlag, pp. 709–754.
- BECKER, E.** 1930. Die Reichsabgabenordnung: Erläutert von Enno Becker, Edn. 4, Steuer-Bücherei, Edn. 7, Berlin: Carl Heymanns Verlag.
- BEHR, G.** 2002. Rechtliche oder wirtschaftliche Betrachtungsweise, in: Festschrift für Jean Nicolas Druey zum 65. Geburtstag, Rainer J. Schweizer (Ed.), Zürich: Schulthess Verlag, pp. 31–47.
- BEISSE, H.** 1972. Auslegung, in: Hartz, Wilhelm a.o. (Ed.): Handwörterbuch des Steuerrechts unter Einschluss von Betriebswirtschaftlicher Steuerlehre, Finanzrecht, Finanzwissenschaft, Edn. 1, Bonn: Beck Verlag, pp. 91–98.

BEISSE, H. 1980. Handelsbilanzrecht in der Rechtsprechung des Bundesfinanzhofes, Betriebs-Berater (BB), Edn. 35, Frankfurt am Main: Deutscher Fachverlag GmbH, pp. 637–646.

BEISSE, H. 1981a. Die wirtschaftliche Betrachtungsweise bei der Auslegung der Steuergesetze in der neueren deutschen Rechtsprechung, in: Steuer und Wirtschaft (StuW), Edn. 58. (11.), Köln: Dr. Otto Schmidt Verlag, pp. 1–14.

BEISSE, H. 1981b. Auslegung, in: Strickrodt, Georg a.o. (Ed.): Handwörterbuch des Steuerrechts unter Einschluss von Betriebswirtschaftlicher Steuerlehre, Finanzrecht, Finanzwissenschaft, Edn. 2, München: Beck Verlag, pp. 134–142.

BEISSE, H. 1984. Zum Verhältnis von Bilanzrecht und Betriebswirtschaftslehre, in: Steuer und Wirtschaft (StuW), Edn. 61. (14.), Köln: Dr. Otto Schmidt Verlag, pp. 1–14.

BEISSE, H. 1988. Die Generalnorm des neuen Bilanzrechts, in: Handelsrecht und Steuerrecht, Festschrift für Dr. h.c. Georg Döllner, Brigitte Knobbe-Keug, Franz Klein, Adolf Moxter (Ed.), Düsseldorf: IDW Verlag, pp. 25–44.

BITZ, M., SCHNEELOCH, D., WITTSTOCK, W. 2003. Der Jahresabschluss: Rechtsvorschriften, Analyse, Politik, Edn. 4, München: Vahlen Verlag.

BLANCHET, J., CROOCH, M. 1999. Internationalization of Accounting and Financial Reporting: at the Crossroad?, in: Küting, Karl-Heinz/Langenbucher, Günther (Ed.), Internationale Rechnungslegung: Festschrift für Professor Claus-Peter Weber zum 60. Geburtstag, Stuttgart: Schäffer-Poeschel Verlag, pp. 3–11.

BLAUM, U., KESSLER, H. 2000. Das Ende der phasengleichen Vereinnahmung von Beteiligungserträgen in der Steuerbilanz? – Zum Beschluss des Großen Senats vom 7.8.2000 und zu seinen Konsequenzen für die Bilanzierungspraxis, in: Steuern und Bilanzen (StuB), Edn. 2, (24/2000), Herne: NWB Verlag, pp. 1233–1246.

BÖCKING, H.-J. 1994. Verbindlichkeitsbilanzierung: wirtschaftliche versus formalrechtliche Betrachtungsweise, Edn. 129, Neue betriebswirtschaftliche Forschung, Habilitations-Schrift, 1992, Wirtschaftswissenschaftliche Fakultät der Universität Frankfurt am Main, Wiesbaden: Gabler Verlag.

BÖCKING, H.-J. 1997. Betriebswirtschaftslehre und wirtschaftliche Betrachtungsweise im Bilanzrecht, in: Handelsbilanzen und Steuerbilanzen. Festschrift zum 70. Geburtstag von Prof. Dr. h. c. Heinrich Beisse, Wolfgang Budde a.o. (Ed.), Düsseldorf: IDW-Verlag, pp. 85–103.

BORDEWIN, A., TONNER, N. 2003. Leasing im Steuerrecht, Edn. 4, Heidelberg: C. F. Müller Verlag.

BRAKENSIEK, S. 2001. Bilanzneutrale Finanzierungsinstrumente in der internationalen und nationalen Rechnungslegung, die Abbildung von Leasing, Asset-Backed-Securities-Transaktionen und Special Purpose Entities im Konzernabschluss, Dissertation, 2001, Wirtschaftswissenschaftliche Fakultät der Universität Saarbrücken, Küting, Karlheinz/Weber, Claus-Peter (Ed.): Rechnungs- und Prüfungswesen, Herne: NWB Verlag.

BÜNNIG, M. 2006. Umsatzsteuerliche Behandlung des „sale-and-lease-back“ – Verfahrens, in: Betriebs-Berater (BB), Edn. 61, Booklet 31, Frankfurt am Main: Deutscher Fachverlag GmbH, pp. 1668–1671.

BÜHNER, A., SHELDON, C. 2001. US-Leasingtransaktionen – Grundstrukturen einer grenzüberschreitenden Sonderfinanzierung, in: Der Betrieb (DB), Edn. 53, Düsseldorf: Fachverlag der Verlagsgruppe Handelsblatt GmbH, pp. 315–318.

CAMFFERCAN, K., ZEFF, A. 2007. Financial Reporting and Global Capital Markets: A History of the International Accounting Standards Committee 1973–2000. Oxford: University Press.

CANARIS, C.-W. 1964. Die Feststellung von Lücken im Gesetz. Eine methodologische Studie über Voraussetzungen und Grenzen der richterlichen Rechtsfortbildung praeter legem, Schriften zur Rechtslehre, Booklet 3, Berlin: Duncker & Humblot Verlag.

CAPITAL LEASE. <http://www.accountingcoach.com/terms/C/capital-lease.html>

CAPITAL LEASE. <http://www.accountingtools.com/definitioncapital-lease>

CAPITAL LEASE. <http://www.businessdictionary.com/definition/capital-lease.html>

CAPITAL LEASE. <http://business.yourdictionary.com/capital-lease>

CAPITAL LEASE. <http://definitions.uslegal.com/c/capital-leasegaming-law/>

CAPITAL LEASE. <http://www.financialtermsdictionary.com/terms/11099-capital-lease.html>

CAPITAL LEASE. <http://financedictionary.com/definition/c/capital-lease/>

CAPITAL LEASE. <http://www.finance-lib.com/financial-termcapital-lease.html>

CAPITAL LEASE.

<http://www.investopedia.com/terms/c/capitallease.asp#axzz1p5vpTSgf>

CAPITAL LEASE. <http://www.qfinance.com/dictionary/capitallease>

CAPITAL LEASE. <http://www.ventureline.com/accountingglossary/C/capital-lease-definition/>

CLAPMAN, E. 2003. A Note on Embedded Lease Options, in: *Journal of Real Estate Research*, pp. 347–359.

COOK, A. 1997. Requirement for a true and fair view – a UK standard-setters perspective, *The European Accounting Review*, 6:4, London: Routledge, pp. 693–704.

COPELAND, T., WESTON, J. F., SHASTRI, K. 2008. *Finanzierungstheorie und Unternehmenspolitik – Konzepte der kapitalmarktorientierten Unternehmensfinanzierung*, Edn. 4, München: Pearson Verlag.

CORDES, H. 1971. *Untersuchungen über Grundlagen und Entstehung der Reichabgabenordnung vom 23. Dezember 1919*, Dissertation, 1971, Rechtswissenschaftliche Fakultät der Universität Köln, Köln: Kleikamp Verlag.

CORNELIUS, J. 1968. *Gesetzesauslegung und verfassungsmäßige Wertordnung*, Dissertation, 1968, Wirtschaftswissenschaftliche Fakultät der Universität Köln, Düsseldorf: Stehle Verlag.

COUNCIL OF THE EC 1979. Fourth Council Directive 78/660/EEC of 25 July 1978 based on Article 54 (3) (g) of the Treaty on the annual accounts of certain types of companies. *Official Journal*, L 222, 14 August 1978, pp. 11–31 (quoted as EC's Fourth Directive).

COUNCIL OF THE EC 1983. Seventh Council Directive 83/349/EEC of 13 June 1983 based on Article 54 (3) (g) of the Treaty on consolidated accounts. *Official Journal*, L 193, 18 July 1983, pp. 1–17 (quoted as EC's Seventh Directive).

DEEGAN, C., UNERMAN, J. 2006. *Financial Accounting Theory*, Berkshire: McGraw-Hill Education.

DICK, W., MISSIONER-PIERA, F. 2010. Financial Reporting under IFRS: A Topic Based Approach, Chichester: John Wiley & Sons.

DIETER, R. 1979. Is Lessee Accounting Working?, in: The CPA Journal, 1979, New York: NYSSCPA, pp. 13–19.

DP/2009/1 “Leases” <http://www.iasb.org/NR/rdonlyres/FF3A33DB-E40D-4125-9ABD-9AF51EB92627/0/DPLeasesPreliminaryViews.pdf>

DÖLLERER, G. 1971. Leasing – wirtschaftliches Eigentum oder Nutzungsrecht, in: Betriebs-Berater (BB), Edn. 26, Booklet 13, Frankfurt am Main: Deutscher Fachverlag GmbH, pp. 535–540.

DÖLLERER, G. 1980. Gedanken zur „Bilanz im Rechtssinne“, in: Jahrbuch für Fachanwälte für Steuerrecht (JbFSt), (1979/80), Herne: NWB Verlag, pp. 195–205.

EBERT, D. 1955. Die wirtschaftliche Betrachtungsweise als Auslegungsgrundsatz im Steuerrecht, Dissertation, Wirtschaftswissenschaftliche Fakultät der Universität Mainz, Mainz: Veröffentlichungen der Universität.

ED/2010/9 “Leases” <http://www.ifrs.org/NR/rdonlyres/C03C9E95-822E-4716-81ED-04B9CC4943BE/0/EDLeasesStandard0810.pdf>

EIBELSHÄUSER, M. 2002. Wirtschaftliche Betrachtungsweise im Steuerrecht – Herkunft und Bedeutung, in: Deutsches Steuerrecht (DStR), Edn. 34, München: Beck Verlag, pp. 1426–1432.

ELLIOTT, B., ELLIOTT, J. 2002 Financial Accounting, Reporting and Analysis. Essex: Financial Times, Prentice Hall.

ENGEL-CIRIC, D. 2003. § 15 Leasing, in: Lüdenbach, Norbert/Hoffmann, Wolf-Dieter (Ed.): Haufe IFRS-Kommentar, Freiburg: Haufe Verlag, pp. 390–468.

ENGISCH, K. 1977. Einführung in das juristische Denken, Edn. 20, Urban Taschenbücher, Edn. 7, Stuttgart: Kohlhammer Verlag, 1977.

ESSER, M. 2005. Leasingverhältnisse in der IFRS-Rechnungslegung: Darstellung der Leasingbilanzierung gemäß IAS 17 und IFRIC 4, in: Steuern und Bilanzen (StuB), Edn. 7, Booklet 10, Herne: NWB Verlag, pp. 429–436.

FASB 2007a: Minutes of the March 21, 2007 Board Meeting: Leases – Identification of Assets and Liabilities and Analysis of Different Accounting Models, March 2007.

FASB 2007b: Minutes of the June 27, 2007 Board Meeting: Leases – Measurement of a Lessee’s Liability and Right to Use Asset under a Simple Lease Contract; Initial Recognition of Assets and Liabilities in Lease Contract, June 2007.

FASB/IASB 2006: A Roadmap for Convergence between IFRSs and US-GAAP – 2006-2008: Memorandum of Understanding between FASB and the IASB, 27.02.2006, <http://www.iasb.org/NR/rdonlyres/874B63FB-56DB-4B78-B7AF-49BBA18C98D9/0/MoU.pdf>.

FASB/IASB 2007a: Information for observers: Analysis of different accounting models for a simple lease (Agenda Paper 6), Joint International Working Group on Leasing-Meeting, 15.02.2007, London
<http://www.iasb.org/NR/rdonlyres/F8C7378F-4620-49F1-9A4D-403B34E069AB/0/Obs6.pdf>.

FASB/IASB 2007b: Information for observers: Joint IASB/FASB Meeting: 24. April 2007, Project: Leases – Scope (IASB Agenda paper 16, FASB Memo No. 6),
<http://www.iasb.org/NR/rdonlyres/7B2B6779-E426-49EC-B0D4-13F4E5EF4508/0/Leases0704j16obs.pdf>.

FEINEN, K. 2002. Das Leasinggeschäft, Edn. 4, Frankfurt am Main: Knapp Verlag.

FINDEISEN, K.-D. 1997. Die Bilanzierung von Leasingverträgen nach den Vorschriften des International Accounting Standards Committee, in: Recht der Internationalen Wirtschaft (RIW), Edn. 43, Booklet 10, Frankfurt am Main: Deutscher Fachverlag GmbH, pp. 838–847.

FINDEISEN, K.-D. 2002. Internationale Rechnungslegung im Leasing-Geschäft, in: Finanzierung, Leasing, Factoring (FLF), Edn. 49, Booklet 2, Frankfurt am Main: Verlag für Absatzwirtschaft, pp. 62–67.

FINDEISEN, K.-D., SABEL, E. 2009. Diskussionspapier von IASB und FASB zur Reform der Leasingbilanzierung, In: Der Betrieb (DB), (2009), Düsseldorf: Fachverlag der Verlagsgruppe Handelsblatt GmbH, pp. 1885–1894.

FITCH, T. P. 2006. Dictionary of Banking Terms. Fifth edition. Hauppauge: BARRON’S.

- FITCH, T. P.** 1990. Dictionary of Banking Terms. Hauppauge: BARRON'S.
- FRIEDLÄNDER, K.** 1956. Die wirtschaftliche Betrachtungsweise im Steuerrecht, in: Neue juristische Wochenzeitschrift (NJW), Edn. 9, München: Beck Verlag, pp. 1049–1053 and pp. 1299–1302.
- FRIEDMAN, J. P.** 2007. Dictionary of Business Terms. Fourth edition. Hauppauge: BARRON'S.
- FÜLBIER, R. U., PFERDEHIRT, H.** 2005. Überlegungen des IASB zur künftigen Leasingbilanzierung: Abschied vom off balance sheet approach, in: Zeitschrift für internationale und kapitalmarktorientierte Rechnungslegung (KoR), 7–8, Edn. 34, (2005), Düsseldorf: Fachverlag der Verlagsgruppe Handelsblatt GmbH, pp. 275–285.
- GAO, S.** 1994. International Leasing: Its Financial and Accounting Application, Preston: UCL Publications.
- GRIMM, C.** 1978. Das Steuerrecht im Spannungsfeld zwischen wirtschaftlicher Betrachtungsweise und Zivilrecht, in: Deutsche Steuerzeitung (DStZ), Release A, Edn. 66, (1978), München: Vahlen Verlag, pp. 283–290.
- GROH, M.** 1980. Zur Bilanztheorie des BFH, in: Steuerberater-Jahrbuch (StbjB), Edn. 31, (1979/80), München: Beck Verlag, pp. 121–140.
- GROH, M.** 1989. Die wirtschaftliche Betätigung im rechtlichen Sinne, in: Steuer und Wirtschaft (StuW), Edn. 66, Köln: Dr. Otto Schmidt Verlag, pp. 227–231.
- HALLER, A.** 1994. Die Grundlagen der externen Rechnungslegung in den USA – unter besonderer Berücksichtigung der rechtlichen, institutionellen und theoretischen Rahmenbedingungen, Edn. 4, Betriebswirtschaftliche Abhandlungen, Edn. 77, Dissertation, 1989, Wirtschaftswissenschaftliche Fakultät der Universität Augsburg, Stuttgart: Schäffer-Poeschel Verlag.
- HASTEDT, U.-P., MELLWIG, W.** 1998. Leasing: rechtliche und ökonomische Grundlagen, Edn. 99, Writings of Betriebs-Berater (BB), Frankfurt am Main: Deutscher Fachverlag GmbH.
- HAYN, S.** 1997. Internationale Rechnungslegung. Ursachen, Wirkungen und Lösungsansätze zur Überwindung internationaler Rechnungslegungsdivergenzen (inklusive Vergleich IAS und US-GAAP), Stuttgart: Schäffer-Poeschel Verlag.

HEDEMANN, J. W. 1929. Reichsgericht und Wirtschaftsrecht – ein Bild deutscher Praxis, Schriften des Instituts für Wirtschaftsrecht an der Universität Jena, Booklet 8, Jena: Gustav Fischer Verlag.

HELMSCHROTT, H. 2000a. Zum Einfluss von SIC 12 und IAS 39 auf die Bestimmung des wirtschaftlichen Eigentums bei Leasingvermögen nach IAS 17, in: Die Wirtschaftsprüfung (WPg), Edn. 53, (9/2000), Düsseldorf: IDW Verlag, pp. 426–429.

HELMSCHROTT, H. 2000b. Leasingbilanzierung im Umbruch – Betrachtung unterschiedlicher Konzepte der Bilanzierung von Leasinggeschäften unter besonderer Berücksichtigung neuerer Vorschläge von McGregor, Tweedie und Mellwig, Aachen: Shaker Verlag.

HEYD, R. 2008. Leasing im Bilanz- und Steuerrecht, in: Graf von Westphalen, Friedrich (Ed.), Der Leasingvertrag, Edn. 6, Köln: Dr. Otto Schmidt Verlag, pp. 1–113.

HIRSCH, R. 1998. International Accounting Standards: Eine neue Qualität im Jahresabschluss von Banken, Edn. 11, Diskussionsbeiträge zur Bankbetriebslehre, Hochschule für Bankwirtschaft, Frankfurt am Main, Diplomarbeit, Frankfurt am Main: Frankfurt School Verlag.

HOCK, K., FROST, H. 1993. Ratgeber Leasing – Leasing besser beurteilen, Edn. 2, Freiburg: Haufe Verlag.

HOPWOOD, A., VIETEN, H. 1999. The United Kingdom. In: McLeay, S. (ed.) Accounting Regulation in Europe, pp. 336–365. London: MCMILLAN PRESS, 1999.

IASB 2006. IASB Update July 2006 – Board Decision on International Financial Accounting Standards.

IASB 2007a. IASB Update March 2007 – Board Decision on International Financial Accounting Standards.

IASB 2007b. Information for Observers, IASB Meeting: March 22, 2007, London, Project: Leases – Identification of assets and liabilities arising in a simple lease (Agenda Paper 2A), <http://www.iasb.org/NR/rdonlyres/00D4398B-8A78-41F4-A3F4-7EE0387F9757/0/Leases0703b12aobs.pdf>.

IASB 2007c. IASB Update June 2007 – Board Decision on International Financial Accounting Standards.

IASB 2008. IASB Update July 2008 – Board Decision on International Financial Accounting Standards.

IASB 2009a. IASB Update January 2009 – Board Decision on International Financial Accounting Standards.

IASB 2009b. Discussion Paper DP/2009, Leases – Preliminary Views, London.

IASB 2009c. IASB Update June 2009 – Board Decision on International Financial Accounting Standards.

IASB 2009d *Framework for the Preparation and Presentation of Financial Statements* London: IASB.

IASB/FASB 2009. Leases – Comment Letter Summary,
http://www.fasb.org/DP_Leases.pdf.

IASC 2009: G4+1 Position Paper: Leases: Implementation of a New Approach, London.

KIRSCH, H. 2003. Leasingbilanzierung nach IAS im Vergleich zum deutschen Recht, in: *Wirtschaftswissenschaftliches Studium (WiSt)*, Edn. 32, (8), München: Vahlen Verlag, pp. 500–504.

KNOBBE-KEUG, B. 1993. Bilanz- und Unternehmenssteuerrecht, Edn. 9, Köln: Dr. Otto Schmidt Verlag.

KOBISCH, S., HUNDT, I., NEITZ, B. 2007. Das Konvergenzprojekt des IASB und des FASB – eine Prognose, in: *Praxis der internationalen Rechnungslegung (PiR)*, Herne: NWB Verlag, pp. 345–350.

KÖHLERTZ, K. 1989. Die Bilanzierung von Leasing: die deutschen Bilanzierungskonventionen für Leasing im Vergleich zu den US-amerikanischen Vorschriften, München: VVF Verlag.

KRATZER, J., KREUZMAIR, B. 1997. Leasing in Theorie und Praxis, Wiesbaden: Gabler Verlag.

KRUSCHWITZ, L. 2007. Investitionsrechnung, Edn. 11, München: Oldenbourg Verlag.

KUSSMAUL, H. 1987. Nutzungsrechte an Grundstücken in Handels- und Steuerbilanz, Edn. 4, Schriften zum Steuer-, Rechnungs- und Prüfungswesen, Habilitations-Schrift, Wirtschaftswissenschaftliche Fakultät der Universität Saarbrücken, Hamburg: Steuer- und Wirtschaftsverlag.

KÜHN, R. 1968. Abgabenordnung: Finanzgerichtsordnung, Steueranpassungsgesetz, Finanzverwaltungsgesetze, Nebengesetze, Edn. 9, Stuttgart: Schäffer-Poeschel Verlag.

KÜMPEL, T., BECKER, M. 2006. Leasing nach IFRS: Beurteilung, Bilanzierung und Berichtspflichten, München: Vahlen Verlag.

KÜTING, K., FIGGE, H. 1999. Mobilien-Leasing in der Handels- und Steuerbilanz, in: Betrieb und Wirtschaft (BuW), Edn. 53, Booklet 10, Berlin: Verlag Betrieb und Wirtschaft, pp. 361–364.

KÜTING, K., HELLEN, H.-H., BRAKENSIEK, S. 1998. Leasing in der nationalen und internationalen Bilanzierung: Eine vergleichende Darstellung unter Berücksichtigung neuer Ansätze, in: Betriebs-Berater (BB), Edn. 53, Booklet 28/29, Frankfurt am Main: Deutscher Fachverlag GmbH, pp. 1465–1473.

KÜTING, K., HELLEN, H.-H., BRAKENSIEK, S. 1999. Die Bilanzierung von Leasinggeschäften nach IAS und US-GAAP, in: Deutsches Steuerrecht (DStR), Edn. 37, Booklet 1, München: Beck Verlag, pp. 39–44.

KÜTING, K., HELLEN, H.-H., BRAKENSIEK, S. 2000. Leasingbilanzierung: Vorschlag zur Neuausrichtung nach dem Positionspapier der G4+1 Working Group, in: Betriebs-Berater (BB), Frankfurt am Main: Deutscher Fachverlag GmbH, pp. 1720–1721.

KÜTING, K., HELLEN, H.-H., KOCH, C. 2006. Das Leasingverhältnis: Begriffsabgrenzung nach IAS 17 und IFRIC 4 sowie kritische Würdigung, in: Kapitalmarktorientierte Rechnungslegung (KoR), Edn. 35, 11, Düsseldorf: Fachverlag der Verlagsgruppe Handelsblatt GmbH, pp. 649–657.

LARENZ, K. 1969. Methodenlehre der Rechtswissenschaft, Edn. 2, Enzyklopädie der Rechts- und Staatswissenschaft. Begründet von F. von Liszt und W. Kaskel, W. Kunkel (Ed.), Berlin: Springer Verlag.

LARENZ, K. 1975. Methodenlehre der Rechtswissenschaft, Edn. 3, (Enzyklopädie der Rechts- und Staatswissenschaft. Begründet von F. von Liszt und W. Kaskel. Herausgegeben von W. Kunkel, Abteilung Rechtswissenschaft), Berlin: Springer Verlag.

LARENZ, K. 1979. Methodenlehre der Rechtswissenschaft, Edn. 4, (Enzyklopädie der Rechts- und Staatswissenschaft. Begründet von F. von Liszt und W. Kaskel. W. Kunkel (Ed.), Abteilung Rechtswissenschaft), Berlin: Springer Verlag.

LAWRENCE, S. 1996. International Accounting. London: International Thomson Business Press.

LEE, T. A. 2006. Financial Reporting & Corporate Governance. Essex: John Wiley & Sons, Ltd.

LEHMANN, U. 1979. Wirtschaftliche Erkenntnis und rechtliche Entscheidung - Gedanken zu Problemen der Kooperation zwischen Wirtschaftswissenschaft, Rechtswissenschaft und Rechtspraxis, Dissertation, 1979, Rechts- und Wirtschaftswissenschaftliche Fakultät der Universität Bochum, Bochum.

LEIBFRIED, P., KLEIBOLD, T. 2009. Neuregelung der Leasingbilanzierung im IFRS-Abschluss des Leasingnehmers, in: Zeitschrift für internationale und kapitalmarktorientierte Rechnungslegung (KoR), Düsseldorf: Fachverlag der Verlagsgruppe Handelsblatt, pp. 408–413.

LEIPPE, B. 2002. Die Bilanzierung von Leasinggeschäften nach deutschem Handelsrecht und US-GAAP: Darstellung und Zweckmäßigkeitanalyse, Edn. 60, Betriebswirtschaftliche Studien Rechnungs- und Finanzwesen, Organisation und Institution, Ballwieser, Wolfgang/Kuhner, Christoph/Ordelleide, Dieter (Ed.), Dissertation, 2001, Wirtschaftswissenschaftliche Fakultät der Universität Bochum, Frankfurt am Main: Peter Lang Verlag.

LEWICKI, B. 2001. G4+1 – Vorstufe eines globalen Standardsetters – Internationale Kooperation von FASB und IASC, in: Der Betriebswirt, Gernsbach: Deutscher Betriebswirte Verlag GmbH, pp. 8–14.

LEWIS, R., PENDRILL, D. 2004. Advanced Financial Accounting. Seventh, edition. Financial Times Prentice Hall.

LIPE, R. 2001. Lease Accounting Research and the G4+1 Proposal, in: Accounting Horizons, Sarasota: American Accounting Association, pp. 299–310.

LORENZ, K. 2002. Wirtschaftliche Vermögenszugehörigkeit im Bilanzrecht, veränderte Dissertation, 2001, Wirtschaftswissenschaftliche Fakultät der Universität Frankfurt am Main, Düsseldorf: IDW Verlag.

LORENZ, K. 2003. Leasingverhältnisse, in: Löw, Edgar (Ed.): Rechnungslegung für Banken nach IAS, Wiesbaden: Gabler Verlag, pp. 429–463.

LÜDENBACH, N., FREIBERG, J. 2006. Wirtschaftliches Eigentum nach IAS 17 – die unterschätzte Bedeutung des Spezialleasings, in: Betriebs-Berater (BB),

Edn. 61, Booklet 6, Frankfurt am Main: Deutscher Fachverlag GmbH, pp. 259–264.

MAYER, S. 2003. Wirtschaftliches Eigentum an Kapitalgesellschaftsanteilen, Dissertation, 2003, Wirtschaftswissenschaftliche Fakultät der Universität Münster, Aachen: Shaker Verlag.

MCGREGOR, W. 1996. Accounting for Leases: A New Approach – Recognition by Lessees of Assets and Liabilities Arising under Lease Contracts, Norwalk, New York: FASB Publications.

MELLWIG, W. 1983. Bilanzrechtsprechung und Betriebswirtschaftslehre, Zu einigen Grundlagen der steuerlichen Bilanzrechtsprechung und ihrer betriebswirtschaftlichen Kritik, in: Betriebs-Berater (BB), Edn. 38, Frankfurt am Main: Deutscher Fachverlag GmbH, pp. 1613–1620.

MELLWIG, W. 1998. Die bilanzielle Darstellung von Leasingverträgen nach den Grundsätzen des IASC: Derzeitige Regelung und Reformvorschläge, in: Der Betrieb (DB), Edn. 51, Attachment Nr. 12/98 to Booklet 35, Düsseldorf: Fachverlag der Verlagsgruppe Handelsblatt GmbH, pp. 1–16.

MELLWIG, W. 2000. Leasing im nationalen und internationalen Handelsrecht, in: Eckstein, Wolfram/Feinen, Klaus (Ed.): Leasinghandbuch für die betriebliche Praxis, Edn. 7, Frankfurt am Main: Knapp Verlag, pp. 67–97.

MELLWIG, W. 2001. Leasing im handelsrechtlichen Jahresabschluss, in: Zeitschrift für das gesamte Kreditwesen (ZfgK), Booklet 6, Edn. 54, Frankfurt am Main: Knapp Verlag, pp. 303–309.

MELLWIG, W., WEINSTOCK, M. 1996. Die Zurechnung von mobilen Leasingobjekten nach deutschem Handelsrecht und den Vorschriften des IASC, in: Der Betrieb (DB), Edn. 49, (1996), Booklet 47, Düsseldorf: Fachverlag der Verlagsgruppe Handelsblatt GmbH, pp. 2345–2352.

MÖLLER, C. 1997. Die wirtschaftliche Betrachtungsweise im Privatrecht: dargestellt an den Kapitalaufbringungs- und Erhaltungsvorschriften im Recht der GmbH, Edn. 102, Schriften zum Wirtschaftsrecht, Dissertation, 1995/96, Wirtschaftswissenschaftliche Fakultät der Universität Bayreuth, Berlin: Duncker & Humblot.

MONSON, D. 2001. Commentary – The Conceptual Framework and Accounting for Leases, in: Accounting Horizons, Vol. 15, Sarasota: American Accounting Association, pp. 275–287.

MOONEY, K. 2008. *The Essential Accounting Dictionary*, Naperville: Sphinx Publishing.

MOXTER, A. 1983. Wirtschaftliche Gewinnermittlung und Bilanzsteuerrecht, in: *Steuer und Wirtschaft (StuW)*, Edn. 13, Booklet 4, Köln: Dr. Otto Schmidt Verlag, pp. 300–307.

MOXTER, A. 1989. Zur wirtschaftlichen Betrachtungsweise im Bilanzrecht, in: *Steuer und Wirtschaft (StuW)*, Edn. 19, Booklet 3, Köln: Dr. Otto Schmidt Verlag, pp. 232–241.

MOXTER, A. 1993. Saldierungs- und Abzinsungsprobleme bei Drohverlustrückstellungen, in: *Betriebs-Berater (BB)*, Edn. 48, Frankfurt am Main: Deutscher Fachverlag GmbH, pp. 2481–2485.

MOXTER, A. 1999. *Bilanzrechtsprechung*, Edn. 5, Tübingen: Mohr Siebeck Verlag.

MOXTER, A. 2000. Rechnungslegungsmythen, in: *Betriebs-Berater (BB)*, Edn. 55, Booklet 42, Frankfurt am Main: Deutscher Fachverlag GmbH, pp. 2143–2149.

MOXTER, A. 2003. *Grundsätze ordnungsgemäßer Rechnungslegung*. Wiesbaden: Gabler Verlag.

MURRAY, J. *Capital Lease*.
<http://biztaxlaw.about.com/od/glossary/g/capitalleasedef.htm>

MYERS, J. 1962. *Reporting of Leases in Financial Statements*, AICPA Accounting Research Study No. 4, New York.

NAILOR, H., LENNARD, A. 2000. *Leases: Implementation of a new Approach*, Norwalk, New York: FASB Publications.

OLDENBURGER, I. 2000. Die Bilanzierung von Pensionsgeschäften nach HGB, US-GAAP und IAS: Die wirtschaftliche Betrachtungsweise als Konvergenzkriterium, in: Böcking, Hans-Joachim (Ed.): *Schriftenreihe Rechnungswesen und Unternehmensüberwachung*, Dissertation, 2000, Wirtschaftswissenschaftliche Fakultät der Universität Mannheim, Wiesbaden: Deutscher Universitätsverlag.

OLDHAM, G. E. 1993. *Dictionary of Business and Finance Terms*, New York: Barnes & Nobles Books.

OVERSBERG, T. 2007. Paradigmenwechsel in der Bilanzierung von Leasingverhältnissen – Eine Einführung in das aktuelle IASB/FASB-Leasingprojekt, in: Zeitschrift für internationale und kapitalmarktorientierte Rechnungslegung (KoR), Düsseldorf: Fachverlag der Verlagsgruppe Handelsblatt GmbH, pp. 376–386.

PARKER, R. H., NOBES, C. W. 1995. An International View of True and Fair Accounting. London: Routledge.

PELLENS, B. 2001. Internationale Rechnungslegung, Edn. 4, Stuttgart: Schäffer-Poeschel Verlag.

PELLENS, B., FÜLBIER, R. U., GASSEN, J. 2006. Internationale Rechnungslegung: IFRS 1 bis 7, IAS 1 bis 41, IFRIC-Interpretationen, Standardentwürfe, mit Beispielen, Aufgaben und Fallstudie, Edn. 6, Stuttgart: Schäffer-Poeschel Verlag.

PFERDEHIRT, H. 2007. Die Leasingbilanzierung nach IFRS – Eine theoretische und empirische Analyse der Reformbestrebungen, Wiesbaden: Deutscher Universitätsverlag.

PREIBLER, G. 2002. „Prinzipienbasierung“ der IAS?, in: Der Betrieb (DB), Edn. 55, Booklet 46, Düsseldorf: Fachverlag der Verlagsgruppe Handelsblatt GmbH, pp. 2389–2395.

REIFNER, U. 2005. Wirtschaftliche Betrachtungsweise und verbundenes Geschäft – ein Beitrag zur Dogmatik der §§ 506 S. 2, 358 BGB, in: Zivilrecht im Sozialstaat, Festschrift für Professor Dr. Peter Derleder, Wolf-Rüdiger Bub (Ed.), Baden-Baden: Nomos Verlag, pp. 489–507.

RIEDEL-STEGNER, A. 2006. Die Bilanzierung von Leasingverhältnissen im internationalen Vergleich, Bremen: Europäischer Hochschulverlag.

RITTNER, F. 1975. Die sogenannte wirtschaftliche Betrachtungsweise in der Rechtsprechung des Bundesgerichtshofs: Vortrag 16. Januar 1975, Edn. 124, Schriftenreihe Juristische Studiengesellschaft Karlsruhe, Heidelberg: C. F. Müller Verlag.

ROSENBERG, J. M. 1986. The Investor's Dictionary. New York: John Wiley & Sons.

RUBIN, S. 1984. The House of US-GAAP, in: Journal of Accountancy, New York: AICPA, pp. 122–129.

SABEL, E. 2006. Leasingverträge in der kapitalmarktorientierten Rechnungslegung, Dissertation, 2006, Wirtschaftswissenschaftliche Fakultät der Universität Frankfurt am Main, in: Böcking, Hans-Joachim/Hommel, Michael (Ed.): Schriftenreihe Rechnungswesen und Unternehmensüberwachung, Wiesbaden: Gabler Verlag.

SABEL, E., VOGEL, M. 2008. Die Leasing-Vertragsoptionen im Rahmen der Reform des IAS 17 – „Mixed Model“ bei der Leasing-Bilanzierung?, in: Finanzierung, Leasing, Factoring (FLF), Frankfurt am Main: Verlag für Absatzwirtschaft, pp. 198–205.

SCHIMMELSCHMIDT, U., HAPPE, P. 2004. Off-Balance-Sheet-Finanzierungen am Beispiel der Bilanzierung von Leasingverträgen im Einzelabschluss und im Konzernabschluss nach HGB, IFRS und US-GAAP, in: Der Betrieb (DB), Edn. 57, Attachement Nr. 9/2004 to Booklet 48, Düsseldorf: Fachverlag der Verlagsgruppe Handelsblatt GmbH, pp. 1–12.

SCHMIDT-LIEBIG, A. 1986 Bauherrenmodell, wirtschaftliche Betrachtungsweise und Gestaltungsmissbrauch: zu den steuerlichen Auswirkungen zivilrechtlicher Sachverhaltsgestaltungen und die Grenzen der Relativität steuerlicher Rechtssatzbegriffe, in: Steuer und Wirtschaft (StuW), Vol. 63, No. 2, Köln: Dr. Otto Schmidt Verlag, pp. 128–143.

SCHNEIDER, D. 1983. Rechtsfindung durch Deduktion von Grundsätzen ordnungsmäßiger Buchführung aus gesetzlichen Jahresabschlusszwecken?, in: Steuer und Wirtschaft (StuW), No. 2, Köln: Dr. Otto Schmidt Verlag, pp. 141–160.

SCOTT, D. L. 2003a. The American Heritage Dictionary of Business Terms, New York: Houghton Mifflin Harcourt.

SCOTT, D. L. 2003b. Wall Street Words: An A to Z Guide to Investment Terms for Today's Investor. New York: Houghton Mifflin Harcourt.

SEELIGER, G. 1962. Der Begriff des wirtschaftlichen Eigentums im Steuerrecht (Spezialfragen im Steuerrecht), Ed. von Hartz, Wilhelm, Dissertation, 1963, Wirtschaftswissenschaftliche Fakultät der Universität Göttingen, Stuttgart. Fachverlag für Wirtschafts- und Steuerrecht Schäffer.

SIEBERT, H. 1996. Grundlagen der US-amerikanischen Rechnungslegung: Ziele und Inhalte der Verlautbarungen der SEC und des FASB sowie deren Unterschiede zum deutschen Bilanzrecht, Köln: Dr. Otto Schmidt Verlag.

SIEGEL, J. G., SHIM, J. K. 2010. Dictionary of Accounting Terms. Fifth edition. New York: BARRON'S.

SIGLOCH, J. 2006. Leasing-Transaktionen in der Rechnungslegung – „off- or on-balance sheet“?, in: Siegel, Theodor/Klein, Andreas/Schneider, Dieter/Schwintowski, Hans-Peter (Ed.), Unternehmungen, Versicherungen und Rechnungswesen, Berlin: Duncker & Humblot, pp. 409–425.

SONNEMANN, E. 1989. Institutionelle und konzeptionelle Grundlagen der externen Rechnungslegung in den USA, in: Sonnemann, Erik (Ed.), Rechnungslegung, Prüfung, Wirtschaftsrecht und Steuern in den USA, Wiesbaden: Gabler Verlag, pp. 17–52.

STOLOWY, H., LEBAS, M. J. 2006. Financial Accounting and Reporting: A Global Perspective. Second edition. London: Thomson.

STREET, D., SHAUGHNESSY, K. 1998. The Evolution of the G4+1 and its Impact on International Harmonization of Accounting Standards, in: Journal of International Accounting, Auditing & Taxation, München: Elsevier, pp. 131–161.

STÜDEMANN, K. 1984. Über das wirtschaftliche der wirtschaftlichen Betrachtungsweise. In: Finanzrundschau (FR), Edn. 39. (66.), (1984), Köln: Dr. Otto Schmidt Verlag, pp. 545–556.

TANSKI, J. 2005. Sachanlagen nach IFRS: Bewertung, Bilanzierung und Berichterstattung, München: Vahlen Verlag.

TIPKE, K. 1979. Steuerrecht: ein systematischer Grundriss, Edn. 7, Köln: Dr. Otto Schmidt Verlag.

TIPKE, K. 1981. Steuerrecht: ein systematischer Grundriss, Edn. 8, Köln: Dr. Otto Schmidt Verlag.

TIPKE, K., LANG, J. 2002. Steuerrecht, Edn. 17, Köln: Dr. Otto Schmidt Verlag.

TWEEDIE, D. (1994) Foreword: The True and Fair View – A Standard-Setter's Perspective. In: Parker, R. H. and Nobes, C. W. An International View of True and Fair Accounting. London: Routledge.

URBAS, H. 1987. Die wirtschaftliche Betrachtungsweise im Steuerrecht, Europäische Hochschulschriften: Reihe 5, Volks- und Betriebswirtschaft, Dis-

sertation, 1984, Wirtschaftswissenschaftliche Fakultät der Universität Köln, Frankfurt am Main: Peter Lang Verlag.

VATER, H. 2002. Bilanzierung von Leasingverhältnissen nach IAS 17: Eldorado bilanzpolitischer Möglichkeiten?, in: Deutsches Steuerrecht (DStR), Edn. 34, Booklet 48, München: Beck Verlag, pp. 2094–2100.

WABMER, S., HELMSCHROTT, H. 2000. Leasingbilanzierung nach dem G4+1 Positionspapier: Fortschritt oder Rückschritt?, in: Der Betrieb (DB), Edn. 53, Booklet 41, Düsseldorf: Fachverlag der Verlagsgruppe Handelsblatt GmbH, pp. 2025–2026.

WAGENHOFER, A. 2001. International Accounting Standards: Bilanzierung und Bewertung, Auswirkungen auf den Jahresabschluss, Edn. 3, Wien, München: Redline Wirtschaftsverlag.

WAGENHOFER, A. 2003. Internationale Rechnungslegungsstandards – IAS/IFRS: Grundkonzepte, Bilanzierung, Bewertung, Angaben, Umstellung und Analyse, Edn. 4, Frankfurt am Main, München: Redline Wirtschaftsverlag.

WALTON, P., HALLER, A., RAFFOURNIER, B. 1998. International Accounting. London: International Thomson Business Press.

WANJIALIN, G. 2004. An International Dictionary of Accounting & Taxation, Lincoln: iUniverse.

WEINSTOCK, M. 1996. Accounting for Leases: Neuer Vorschlag des IASC zur Bilanzierung von Leasingverträgen, in: Die Wirtschaftsprüfung (WPg), Düsseldorf, IDW Verlag, pp. 794–800.

WEINSTOCK, M. 2000. Die Bilanzierung von Leasingverträgen nach IASC: Darstellung mit ausführlichen Beispielen, Europäische Hochschulschriften: Reihe 5, Volks- und Betriebswirtschaft, Dissertation, 1999, Wirtschaftswissenschaftliche Fakultät der Universität Frankfurt am Main, Frankfurt am Main: Peter Lang Verlag.

WEISS, M. 2006 Praxishandbuch Leasing: Grundlagen und Praxis der Bilanzierung nach HGB und IFRS, Saarbrücken: VDM Verlag Dr. Müller.

WERNDL, J. 1983. Wirtschaftliches Eigentum: Grundsätzliche Betrachtungen über die Zurechnung von Wirtschaftsgütern im Steuerrecht, Edn. 16, Steuerwissenschaft, Köln, Heidelberg: C. F. Müller Verlag.

WÜSTEMANN, J., KIERZEK, S. 2008. Revenue Recognition – Würdigung aktueller Entwicklungen aus prinzipienorientierter Sicht, in: Bock, Kurt/Werder, Axel von (Ed.), Unternehmenübernahme, Unternehmensaufsicht, Unternehmensberichterstattung, Stuttgart: Schäffer-Poeschel Verlag, pp. 141–160.

ZÜLCH, H., WILLMS, J. 2005. Die Identifizierung von Leasingverhältnissen **WILLMS** gem. IFRIC 4, in: Steuern und Bilanzen (StuB), Edn. 8, (7/2005), Herne: NWB Verlag, pp. 315–317.

Laws, Standards and Online sources:

All quoted or used laws/legal texts <http://dejure.org>; <http://www.jusline.de>; as well as the IAS/IFRS-Standards and IAS/IFRS interpretations respectively can be found in the :

<http://eifrs.iasb.org/eifrs/bnstandards/en/framework.pdf>

<http://eifrs.iasb.org/eifrs/bnstandards/en/ias8.pdf>

<http://eifrs.iasb.org/eifrs/bnstandards/en/ias16.pdf>

<http://eifrs.iasb.org/eifrs/bnstandards/en/ias17.pdf>

<http://eifrs.iasb.org/eifrs/bnstandards/en/ias27.pdf>

<http://eifrs.iasb.org/eifrs/bnstandards/en/ias36.pdf>

<http://eifrs.iasb.org/eifrs/bnstandards/en/ias38.pdf>

<http://eifrs.iasb.org/eifrs/bnstandards/en/ias40.pdf>

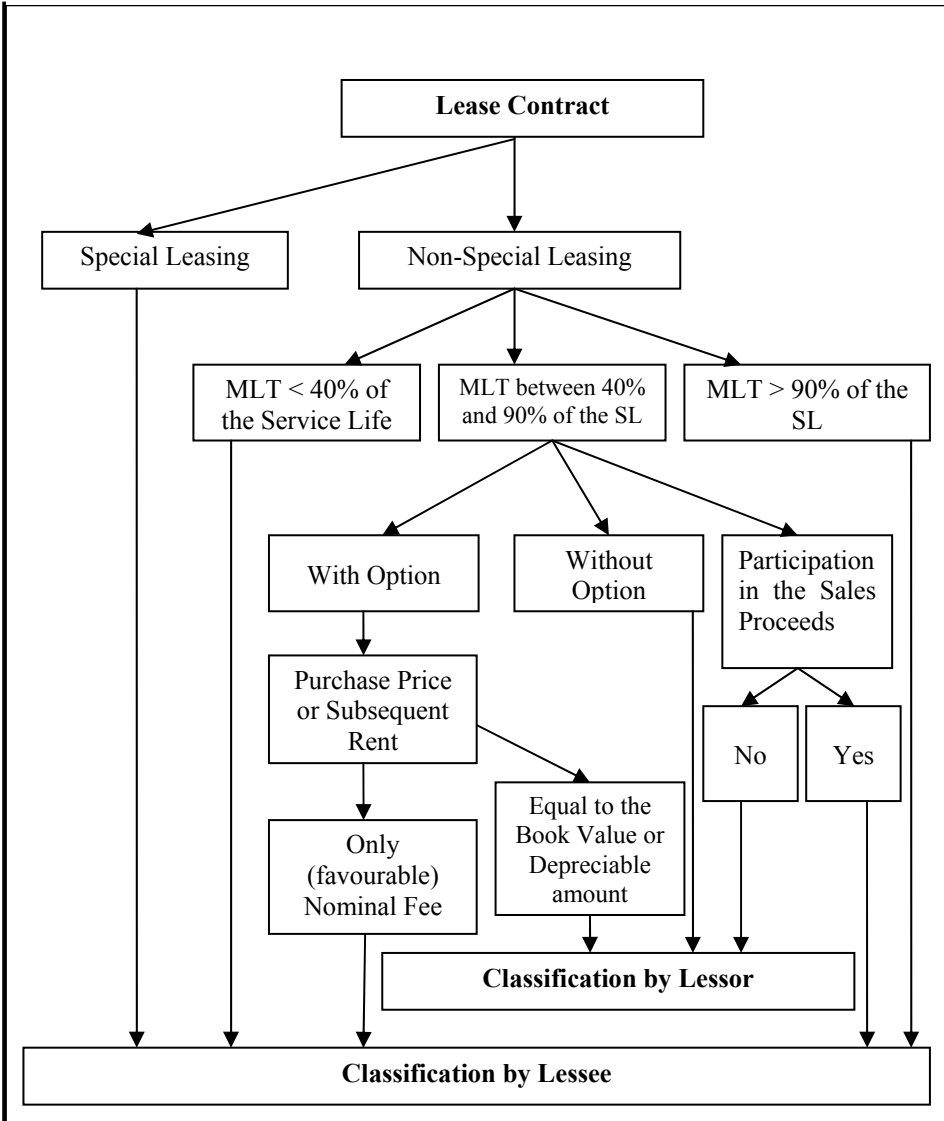
<http://eifrs.iasb.org/eifrs/bnstandards/en/sic12.pdf>

<http://eifrs.iasb.org/eifrs/bnstandards/en/sic15.pdf>

<http://eifrs.iasb.org/eifrs/bnstandards/en/sic27.pdf>

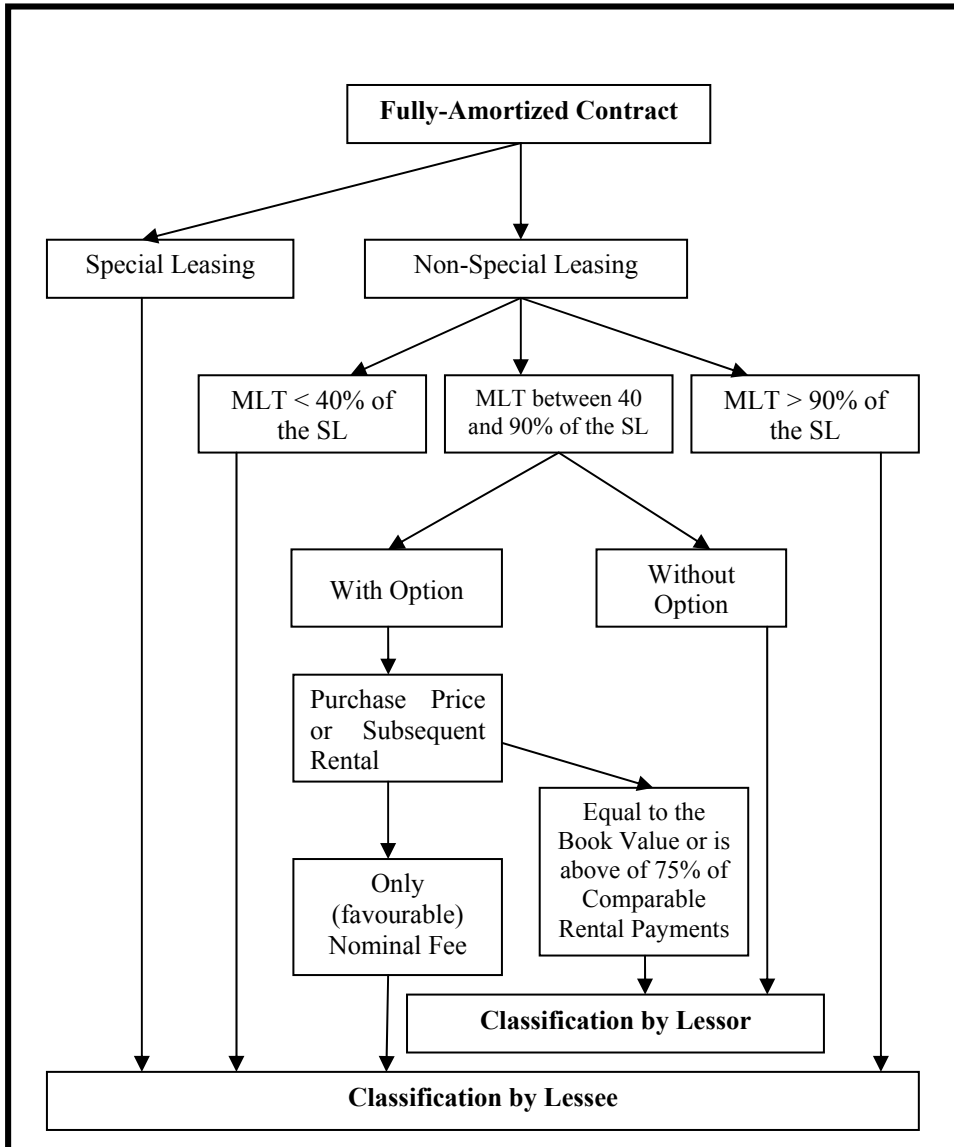
<http://eifrs.iasb.org/eifrs/bnstandards/en/ifric4.pdf>

Appendix 1. Fiscal Classification of Fully Amortized Contracts (Movables)



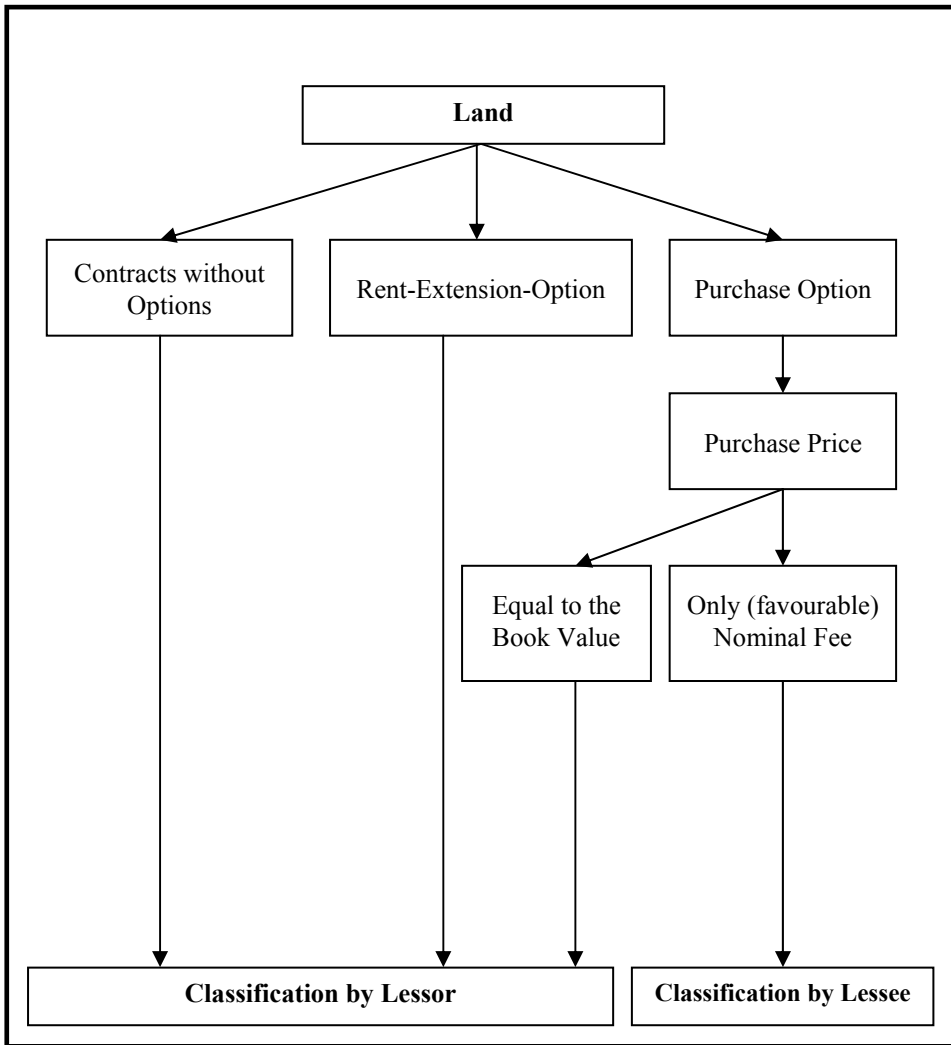
Source: Hock *et al.*, 1993, p. 194.

**Appendix 2. Fiscal Classification of Fully Amortized Contracts
(Immovable – Buildings)**



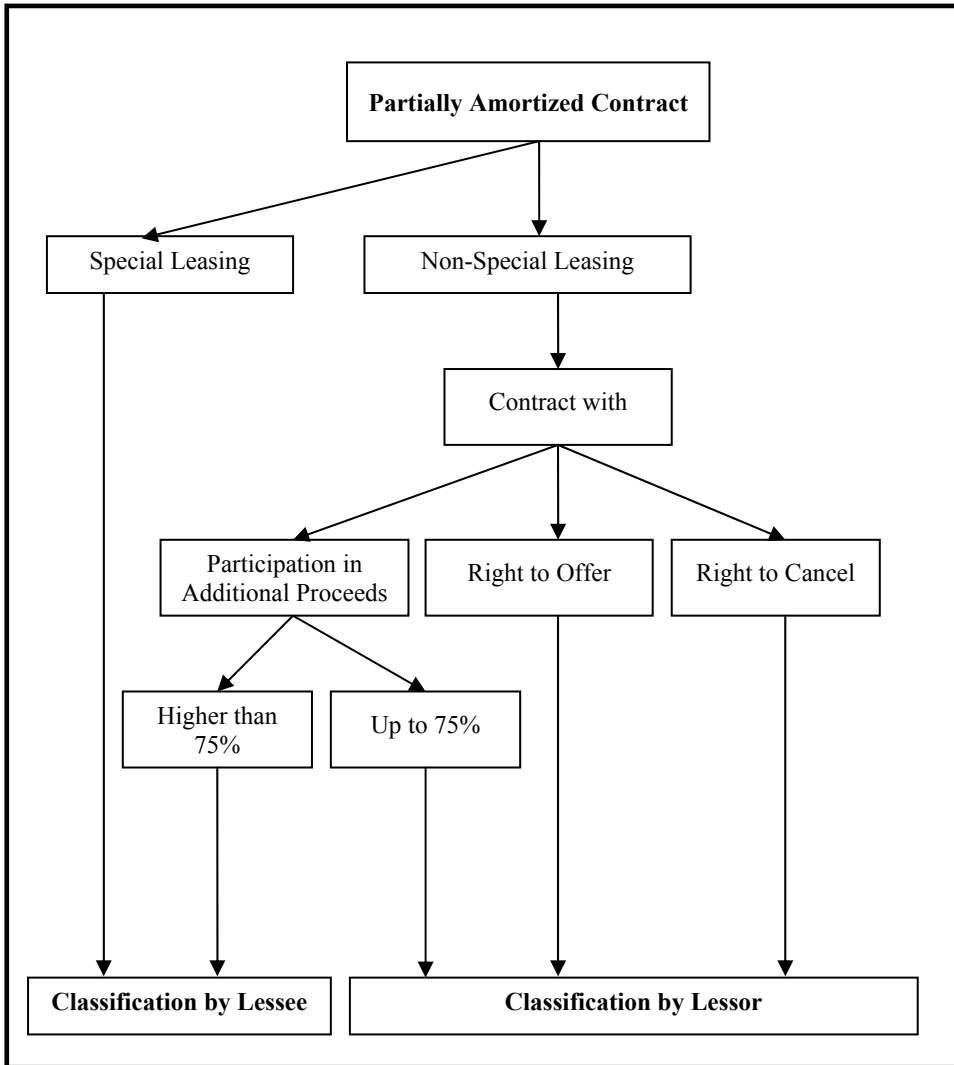
Source: Hock *et al.*, 1993, p. 212.

Appendix 3. Fiscal Classification of Fully Amortized Contracts (Immovable – Land)



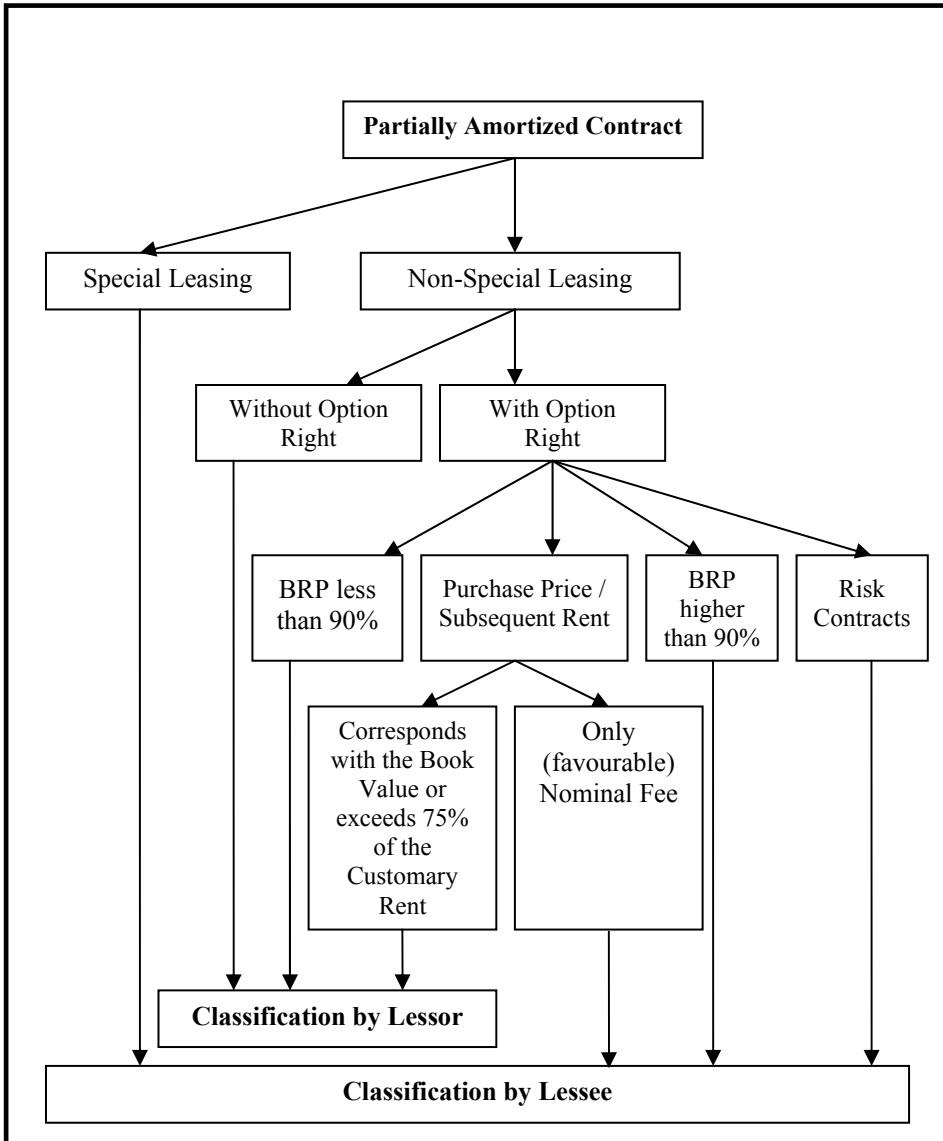
Source: Hock *et al.*, 1993, p. 209.

Appendix 4. Fiscal Classification of Partially Amortized Businesses with Movables



Source: Hock *et al.*, 1993, p. 217.

Appendix 5. Fiscal Classification of Partially Amortized Businesses of Immovable



Source: Hock *et. al.*, 1993, p. 220.

Appendix 6. Elulookirjeldus

1. Isikuandmed

Ees- ja perekonnanimi

Sünniaeg ja koht

Kodakondsus:

Tobias Markus Claus Wiebelt

17. veebruar 1981, Kaiserslautern,

Saksamaa

saksa

2. Kontaktandmed

Address

Telefon

E-posti aadress

Im Jungwald 36, 67663 Kaiserslautern,

Saksamaa

+49-177-7775510

tobias_wiebelt@web.de

3. Hariduskäik

Õppeasutus

Lõpetamise aeg

Haridus (eriala/kraad)

Tallinna Tehnikaülikool

2012

Doktoriõpe (Ärikorraldus)

Saarimaa Ülikool

2011

Õigusteaduse magister
(LL.M.)

Saarimaa Ülikool

2007

Ettevõtetmajanduse
magister (MBA)

4. Keelteoskus

Keel

Saksa

Inglise

Prantsuse

Tase

emakeel

kõrgtase

algtase

5. Täiendusõpe

Periood

September 2004 – juuli 2005

Oktoober 2005 – veebruar 2006

Täiendusõppe läbiviija nimetus

Warsaw School of Economics (Poola)

University of St. Gallen (Šveits)

6. Teenistuskäik

Töötamise aeg

01.04.2010 ...

Tööandja nimetus

Commerzbank

International S.A.,

Luxembourg

Ametikoht

Business Development

& Brand Manager

01.11.2007 – 31.03.2010	Dresdner Bank S.A., Luxembourg	Executive Assistant to the Management Board
01.01.2007 – 31.10.2007	KPMG S.a.r.l., Luxembourg	Auditiitori assistent

7. Teadustegevus

(1) Artiklid rahvusvahelistes ajakirjades või artiklite kogumikes:

Wiebelt T., Alver L. 2012 The Future Lease Reporting System: Decision-useful Transmission of information. Journal of International Scientific Publications. Economy and Business. Volume 6, Part 1. ISSN 1313-2339, <http://www.science-journals.eu> (ilmumisel ETIS 1.2.)

Wiebelt, T. M. C. 2011 Der Einfluss der Personalentwicklung auf den Unternehmenserfolg. Scientia Nova. Das interdisziplinäre Wissenschaftsmagazin (7– 12). Institut für Akademische Zusammenarbeit (ETIS 3.2.)

Wiebelt, T. 2010 Die Charakterisierung der wirtschaftlichen Betrachtungsweise nach HGB. Der Andere Verlag (ETIS 2.2.)

Wiebelt, T. M. C. 2010 Die Bedeutung der „substance over form“ nach IAS/IFRS. Scientia Nova. Das interdisziplinäre Wissenschaftsmagazin 33-40. Institut für Akademische Zusammenarbeit (ETIS 3.2.)

Wiebelt, T. M. C. 2008 Die historische Entwicklung der wirtschaftlichen Betrachtungsweise. Scientia Nova. 11, 39–43 (ETIS 1.2.)

(2) Artiklid konverentsi kogumikes:

Alver, L, Wiebelt, T. 2011 Thoughts Come True: A Long Way Towards New Accounting Standard. In: Business Analysis, Accounting, Taxes and Auditing: Business Analysis, Accounting, Taxes and Auditing. Tallinn, 10.–11.11.2011 (Toim.) Alver J. Tallinn: Tallinna Tehnikaülikool, 2011, 2–0-25 (ETIS 3.4)

8. Kaitstud lõputööd

Magistritöö “Tarbijakaitse klausli väljajätmine kui turu juhtimise reegel. Vastavalt Saksa ebaausa konkurentsiseadusele (§ 4 Nr. 11 UWG). Kriitiline analüüs, 2011

Magistritöö “Majanduslik käsitlus saksa kommertsseaduses ja rahvusvahelistes finantsaruandluse standardites: liisingu näitel”, 2007

9. Teadustöö põhisuunad

Majandusarvestuse alased uuringud

Eraettevõtete strateegiline juhtimine

Pangandus ja rahandus

Appendix 7. Curriculum Vitae

1. Personal data

Name	Tobias Markus Claus Wiebelt
Date and place of birth	February 17, 1981 Kaiserslautern Germany
Citizenship	German

2. Contact information

Address	Im Jungwald 36, 67663 Kaiserslautern, Germany
Phone	+49-177-7775510
E-mail	tobias_wiebelt@web.de

3. Education

Educational institution	Graduation year	Education (field of study/degree)
Tallinn University of Technology	2012	Doctor of Philosophy in Business Administration
Saarland University	2011	Master of Laws (LL.M.)
Saarland University	2007	Master of Business Administration (MBA)

4. Language competence/skills

Language	Level
German	Native language
English	Fluent
French	Basic skills

5. Special Courses

Period	Educational or other organisation
September 2004 – July 2005	Warsaw School of Economics (Poland)
October 2005 – February 2006	University of St. Gallen (Switzerland)

6. Professional employment

Period	Organisation	Position
01.04.2010 ...	Commerzbank International S.A., Luxembourg	Business Development & Brand Manager

01.11.2007 – 31.03.2010	Dresdner Bank S.A., Luxembourg	Executive Assistant to the Management Board
01.01.2007 – 31.10.2007	KPMG S.a.r.l., Luxembourg	Audit Assistant

7. Scientific Work

(1) Articles in international journals and books:

Wiebelt T., Alver L. 2012 The Future Lease Reporting System: Decision-useful Transmission of information. Journal of International Scientific Publications. Economy and Business. Volume 6, Part 1. ISSN 1313-2339, <http://www.science-journals.eu> (accepted for publication ETIS 1.2.)

Wiebelt, T. M. C. 2011 Der Einfluss der Personalentwicklung auf den Unternehmenserfolg. Scientia Nova. Das interdisziplinäre Wissenschaftsmagazin (7–12). Institut für Akademische Zusammenarbeit (ETIS 3.2.)

Wiebelt, T. 2010 Die Charakterisierung der wirtschaftlichen Betrachtungsweise nach HGB. Der Andere Verlag (ETIS 2.2.)

Wiebelt, T. M. C. 2010 Die Bedeutung der „substance over form“ nach IAS/IFRS. Scientia Nova. Das interdisziplinäre Wissenschaftsmagazin 33–40. Institut für Akademische Zusammenarbeit (ETIS 3.2.)

Wiebelt, T.M.C. 2010 Die historische Entwicklung der wirtschaftlichen Betrachtungsweise. Scientia Nova. 11, 39–43 (ETIS 1.2.)

(2) Conference proceedings:

Alver, L., Wiebelt, T. 2011 Thoughts Come True: A Long Way Towards New Accounting Standard. In: Business Analysis, Accounting, Taxes and Auditing: Business Analysis, Accounting, Taxes and Auditing. Tallinn, 10.–11.11.2011 (Toim.) Alver J. Tallinn: Tallinna Tehnikaülikool, 2011, 20–25 (ETIS 3.4)

8. Defended Thesis

Master Thesis “Verbraucherschützende Klauselverbote als Marktverhaltensregeln nach § 4 Nr. 11 UWG – eine kritische Analyse”, 2011
(in English: Master’s Thesis “Consumer Protecting Clause Exclusions as Market Conduct Rules according to § 4 Nr. 11 UWG (German Unfair Competition Act) – A Critical Analysis”, 2011)

Master Thesis “Die Bedeutung der wirtschaftlichen Betrachtungsweise im deutschen Handelsrecht und nach IFRS – dargestellt am Beispiel des Leasing”, 2007

(in English: Master’s Thesis “The Relevance of the Economic Approach in the German Commercial Law and according to IFRS – illustrated by the Example of Leasing”, 2007)

9. Main areas of scientific work/Current research topics

Accounting researches

Strategic Management in private organisations

Banking and Finance

KOKKUVÕTE

IASB ja *FASB* standardi eelnõu ED/2010/9 "Leases", mis publitseeriti 17. augustil 2010, ühtlustab liisingu kapitaliseerimist. Kui 2009. aasta märtsis publitseeritud eelnõuga reguleeriti ainult rendilevõtja kapitaliseerimist, siis uus eelnõu reguleerib nii rendileandja kui ka rendilevõtja tehinguid. Kasutusõiguse kontseptsiooni kasutamine viib liisingu kapitaliseerimise võrreldes hetkel kehtiva standardiga IAS 17, täielikult uutele alustele. Uue kontseptsiooni eesmärk on anda finantsaruannete kasutajatele kasulikku infot seoses rendilepingu mahu, ajastatuse ja rahakäibega.

Doktoritöö eesmärk oli uurida rendilepingute kapitaliseerimise reformimise vajadust ja analüüsida rendilepingute kajastamist, lähtudes töös käsitletud kapitaliseerimiskontseptsioonidest ning otsusekasulikkusest. Kehtivast regulatsioonist ja liisingu kapitaliseerimise reformimise ettepanekute analüüsist lähtudes on iseloomustatud Saksamaal levinud majanduslikku käsitlust ning uuritud rahvusvahelisest *GAAP*-st lähtuvat sisu ülimuslikkust. Rendilepinguid on analüüsitud ka tsiviilõiguslikust seisukohast. Vaatamata sellele, et rahvusvahelises kontekstis valitseb erinev käsitlus, saab kasutusõiguse üleminekut vaadelda rendilepingu tähtsaima osana. Sõltuvalt rendilepingu osapoolte tahtest ja rendilepingu tingimustest võib kasutusõiguse ülemineku proportsionaalse jaotuse olulisus ja finantseerimisfunktsiooni võrdne tähtsus erineda. Lepingu koostamise käigus võib rendileandja ja rendilevõtja riskijaotus erineda. Võttes arvesse kohalikku õigussüsteemi ja omandiõiguse teooriat ning lähtudes majanduslikust perspektiivist, on töös loodud alus rendilepingute tulevaseks uurimiseks. Sellest lähtuvalt hõlmab rendileping kasutusõiguse ajutise ülemineku vastutasuks maksete eest, mis toob kaasa kasutusõiguse lahutamise juriidilisest omamisest.

Tuginedes erialakirjanduse analüüsile, on käsitletud hetkel kehtivat liisingu kapitaliseerimist vastavalt rahvusvahelisele *GAAP*-le ja otsusekasulikkuse teooriale. Analüüsi käigus jõuti järeldusele, et kehtivad juhendmaterjalid tuginevad riskide ja hüvede kontseptsioonile ning kapitaliseerimise eesmärgil tuleb kõik rendilepingud määratleda kas kasutus- või kapitaalrentimisena, sõltuvalt sellest, kuidas toimub renditud varaobjektiga seotud hüvede ja riskide jaotus. Jaotuse alusel toimub kapitaliseerimine. Rahvusvaheline *GAAP* lähtub „kõik või mitte midagi“-kontseptsioonist ja vastavalt sellele peab kapitaalrentimise korral rendilevõtja renditud varaobjekti ja rendikohustise kapitaliseerima. Juhul kui on tegemist kasutusrentimisega, ei kajasta rendilevõtja renditavat varaobjekti bilansis. Doktoritöös on vaadeldud „kõik või mitte midagi“-kontseptsiooni mõju bilansile ja rõhutatud rendilevõtja huvi renditavat varaobjekti mitte kapitaliseerida. Rentnikule on mõju bilansile tunduvalt suurem rendileandja omast.

Otsusekasulikkuse teooriast lähtudes on analüüsitud kehtivat kapitaliseerimissüsteemi. Selgus, et aruannete koostamisel lähtutakse otsuste langetamise oluli-

susest ainult piiratud kujul. „Kõik või mitte midagi“-kontseptsiooni rakendamine toob kaasa informatsiooni mittetäieliku esituse, sest kasutusrentimise korral rendilevõtja ei kapitaliseeri varaobjekti ega kohustist. Isegi täiendava info kohustuslik avalikustamine ei hõlma ära investoritele vajaliku info (tulevaste maksete kohta) puudumist. Lisaks sellele võib tingimuslike rendimaksete ja soodsa väljaostuvõimaluse avalikustamise puudumist tõlgendada info mittetäieliku avalikustamisena. Renditehingu kapitaliseerimist sõltumata juriidilisest omanikust toetab vastavalt standarditele *IAS 17* ja *ASC 840* täielikult ka majandusliku lähenemise kontseptsioon (sisu ülimuslikkus vormi suhtes). Seevastu „kõik või mitte midagi“-kontseptsioonist lähtuv kapitaliseerimine motiveerib lepingupooli lepinguid vähem eristama, mis omakorda võimaldab kergemini klassifitseerida renditehingud kasutusrentimiseks. Jaotus kaheks rendiliigiks eeldab faktide selget klassifitseerimist. Fakte, mis lähtudes majanduslikust käsitlusest on peaaegu identsed, tõlgendatakse vastuoluliselt, see aga on vastuolus majandusliku lähenemise endaga. Kapitaliseerimise juhendmaterjalide analüüsi käigus tuvastati hulk näiteid, mille puhul oli tegu majandusüksuse sisese andmete mittevõrreldavusega. Kui standard *IAS 17* annab juhiseid vaid kvalitatiivsete klassifitseerimiskriteeriumide kohta, siis Saksa *HGB* ja *US GAAP* toovad ära kvantitatiivsed kriteeriumid, mis vähendavad tõlgendamisvõimalusi. Samas on võimalik nendest kriteeriumitest suhteliselt lihtsalt mööda hiilida. Vastuolulisus kapitaliseerimisel vähendab rendilevõtja aruannete võrreldavust.

Analüüsi tulemusena saab väita, et informatsiooni usaldusväärsust tuleb tõsta. Eriliselt tuleb rõhutada, et lepingu klassifitseerimisel on info neutraalsus ohus, kuna eksisteerib mitmeid tõlgendamisvõimalusi ja „kõik või mitte midagi“-kontseptsioon võimaldab moonutada selle rendilevõtja aruandeid, kes püüab jätta rendilepinguid kapitaliseerimata. Lepingu klassifitseerimisel tekkiva tõlgendamisvõimaluste rohkusega kaasnevad puudused info kontrollitavuse suhtes ja minimaalsete objektiivsusnõuete täitmisel. Otsusekasulikkuse teooriast lähtuva analüüsi tulemusel leidis kinnitust, et kehtiv rendiarvestuse kapitaliseerimine vajab reformimist, mis praegu toimubki IASB-i ja FASB-i koostööna.

Tuginedes eelmainitule, on doktoritöö neljandas peatükis uuritud, kas käimasoleva reformi käigus suureneb otsusekasulikkuse teooria valguses rendi kapitaliseerimisel saadava info kasulikkus. Vastavalt töögrupi G4+1 soovitatud kapitaliseerimiskontseptsioonile tuleb eriti tähelepanu pöörata finantskomponentide põhisele ja koguvarapõhisele lähenemisele. Mõlemad lähenemised soovitasid rentimise kapitaliseerimist ja praeguse kapitaliseerimiskorra lõpetamist. Finantskomponentide põhise käsitluse kohaselt tuleks rendilevõtja kasutusõigus kapitaliseerida varaobjektina ja kohustisena. Töögrupi G4+1 uurimus rõhutab vajadust loobuda „kõik või mitte midagi“-kontseptsioonist. Erinevalt kehtivast rendistandardist, võiksid lepingutingimused mõjutada ainult summasid, mis on seotud kasutusõiguse (tuleb kapitaliseerida) ja rendikohustusega, mis määratakse kindlaks rendilevõtja lepingukohaste vältimatute maksetena. Rendileandja peaks kapita-

liseerima kokkulepitud maksete summale vastava nõudeõiguse ja rendilepingu lõpul allesjääva kasutusõiguse. Kumbki lepingupool kapitaliseerib selle osa potentsiaalsest kasust, mille üle tal on valitsev mõjuvõim.

Doktoritöös analüüsitakse sellist kapitaliseerimist, mis toimub otsusekasulikkusest tulenevalt finantskomponentide põhise lähenemise alusel. Otsuste langetamisele avaldab mõju edastatava info olulisus (viimane sõltub mõjust rendilevõtja bilansile) ja renditehingute kapitaliseerimise standardiseerimine. Selgus, et edastatava info kasulikkus on piiratud, kuna minimaalsete rendimaksete koosseisu pole lülitatud rendilepingu pikendamise võimalust ja rendimakseid, mis sõltuvad renditava varaobjekti kasutusest. Analüüsi tulemusel selgus, et võõrandamisõiguse kapitaliseerimisel on võimalik lühiajaline kasutusõigus peatada, mis on lepingus sama, mis ost ja mis ühtib majanduslikku lähenemisega. Selgus, et vastavalt finantskomponentide põhisele lähenemisele on kapitaliseerimise usaldusväärsus piiratud. Lepingukomponentide eraldi hindamisega, mida peaks vastavalt reformile rakendama, kaasneb hulk tõlgendamisvõimalusi. Seepärast on finantskomponentide põhise lähenemise edasiseks arenguvõimaluseks hinnangute selgem aruandlus. Finantskomponentide põhise lähenemise analüüsi tulemusena selgus, et otsuste langetamiseks vajalik info küll edastatakse, kuid kuna hinnangud tuginevad väga laiaulatuslikule infole, siis on vähenenud usaldusväärsus ja seetõttu on oluliselt vähenenud ka rendilepingute kapitaliseerimisest tulenev kasulikkus. Alternatiivse kontseptsioonina on vaadeldud koguvarapõhist lähenemist, mille kohaselt hetkel kehtivate rahvusvaheliste ja USA juhendmaterjalide kapitaliseerimisprintsipiidest, kus aluseks oli riskide ja hüvede üleminek, enam ei lähtuta. Rendilevõtja kohustus koosneb rendimaksete kogusummast ja kohustusest tagastada varaobjekt rendilepingu lõppedes. Koguvarapõhise lähenemise analüüsimisel otsuskasulikkusest lähtuvalt selgub, et mainitud lähenemise otsuste langetamise olulisus toimib vaid väga piiratud kujul. Renditava varaobjekti esmase kajastamisega reaalkaartuses, arvestamata rendilepingu pikkust, kaasnevad ebaõiged rendimaksud. Tuginedes majanduslikule käsitlusele (sisu ülimuslikkus vormi suhtes) on kritiseeritud klassifitseerimist ajutiseks liisinguks ja terve varaobjekti ostuks. Koguvarapõhisele lähenemisele tugineva info ülemineku usaldusväärtus on täielik. Standardiseeritud kapitaliseerimisel tähendab renditud varaobjekti reaalkaartuses kajastamine info neutraalset edastamist. Doktoritöös on käsitletud *IASB/FASB* 2009. ja 2010. aasta liisinguprojekte. Rendilevõtja seisukohalt on tulevane kapitaliseerimine standardiseeritud. Rendilepinguid käsitletakse kui kasutusõiguse müüki. Selline lähenemine on sarnane kehtiva kapitaalrentimisega, mis tugineb kogu renditud varaobjekti ostule ja on sarnane finantskomponentide põhisest käsitlusest tuntud mitme osa ostuga. Paraku toob see kaasa kapitaliseerimise hajumise.

Rendilevõtja kapitaliseerimispõhimõtete analüüs näitas edastatava info kasulikkust juhtimisotsuste langetamiseks. Selle tingib mõju bilansile ja kasutusõiguse üleminek rendilevõtjale. Ka kõikide tingimuslike rendimaksete olemasolu erine-

valt finantskomponentide põhisest lähenemisest soodustab info täielikku edastamist. Olgu märgitud, et firmasisene võrreldavus on piiratud, kui esineb erinevaid tõlgendamisvõimalusi, mis on tingitud eeldatavate rendimaksete määratlemisest. Uuring näitas, et kõige parem rendimaksete hinnang saadakse tõenäosusele tuginedes, sest ainult sel juhul võetakse arvesse kõik alternatiivsed variandid. Edasine analüüs näitas, et info usaldusväärsus ei tõuse praeguse kapitaliseerimise asendamisel finantskomponentide põhise mudeliga.

Kehtiva rendiarvestuse standardi kohaselt liigitatakse renditehingud kapitaal- ja kasutusrentimiseks, mis on toonud kaasa probleeme. On võimalik rendilepinguid koostada nii, et saavutada soovitud kajastus/mittekajastus bilansis. Renditehingute mainitud liigituse puhul toimub renditud varaobjekti täielik kapitaliseerimine kas rendileandja või rendilevõtja poolt ja mõju bilansile on suur. Seega on kapitaliseerimisregulatsioonidel suur mõju rendilepingute koostamisele ja renditehingu tegelik sisu võib jääda tagaplaanile. *ED/2010/9* kohaselt sellist mõju enam pole. Selle asemel, et analüüsida renditehingu osapoolte õigusi ja kohustusi, lepivad osapooled enne lepingu sõlmimist kokku. Need õigused ja kohustused hinnatakse ning seejärel kapitaliseeritakse kas rendileandja või rendilevõtja bilansis. Rendilepingu majanduslik mõju ilmneb sel juhul bilansis palju täpsemini. Seniste tõlgendamisvõimaluste „hall ala” kaob ja tulevikus on bilansis kajastamise/mittekajastamise mõju rendilepingutele palju väiksem.

ED/2010/9 kohaselt peab renditehingute kapitaliseerimine olema vastavuses *IASB* uue, koostatava raamistikuga. Tekib küsimus, kas tingimuslik ja valikuliste rendimaksetega rentimine vastab kohustise mõistele. Vastavalt hetkeseisule on tulevases raamistikus varaobjekti defineeritud kui olemasolevat majanduslikku ressursi, millele majandusüksusel on kas õigus või muu ligipääs, mida ei ole teistel. Seejuures ei ole vajalik, et õigus või ligipääs oleksid juriidiliselt määratletud. Seepärast võib rendikohustist kapitaliseerida varaobjektina, kui rendileandjale laekub rendikohustis suurema tõenäosusega kui 50%. Tulevikus tuleb kohustist defineerida majandusliku nüüdiskohustusena, kus majandusüksus on võlgnik. Selle definitsiooni kohaselt saab üksus olla võlgnik ainult siis, kui majanduslik kohustus eksisteerib juriidiliselt. Seepärast ei peaks rendilevõtja kapitaliseerima tingimuslikku või valikuliste rendimaksetega kohustist niikaua, kui need tingimused ei ole täidetud või valik aktsepteeritud. Seepärast on tingimusliku või valikuliste rendimaksetega rendileping vastavalt *ED/2010/9*-le vastuolus *IASB* tulevases raamistikus sisalduva kohustise definitsiooniga. Vastavalt raamistikus toodud varaobjekti ja kohustise uuele definitsioonile ei võimaldata hõlbimist majanduslikust reaalsusest. Juhul kui kasutatakse tegevuspõhist lähenemist, peab rendileandja kapitaliseerima rendinõuded ja rendikohustise, kuid rendilevõtja kapitaliseerib ainult kasutusõiguse ega kapitaliseeri rendikohustist. Probleem, mis tõstatub, on seotud asjaoluga, et kohustise kajastamiseks on vaja juriidilist alust, kuid see ei ole nõutav varaobjekti kajastamisel. Lahenduseks

oleks variant, mille puhul juriidiliselt mittekohustuslikke kohustisi kapitaliseeritaks siis, kui kajastatakse varaobjekt.

Standardi eelnõu *ED/2010/9* "Leases" on muutnud kapitaliseerimise aluseid. Kui hetkel kapitaliseeritakse renditud varaobjekt täielikult kasusaanud omaniku bilansis, siis tulevikus tuleb vastavalt kasutusõiguse põhisele kontseptsioonile teha jaotus rendileandja ja rendilevõtja vahel. Selline jaotus suurendab küll hindamisprotsessis tõlgendamisvõimalusi, kuid kuna finantsaruannete adressaat saab täiendavalt kasulikku infot rendilepingu majanduslike tagajärgede kohta, siis on reform igati tervitav. Varaobjekti ja kohustise definitsiooni erisuse võimaldab kõrvaldada *IASB* raamistiku projekti edasine areng. Standardi korrigeeritud eelnõu loodetakse avaldada 2012. aasta kolmandas kvartalis, millele järgneb kommenteerimisperiood peaks lõppema 2013. aasta esimeses kvartalis. Standardi uus eelnõu on kavas avaldada 2013. aasta teises kvartalis, millele järgneb jällegi kommenteerimisperiood, mis võib kesta üks aasta ning standard jõustub loodetavasti 1. jaanuaril 2015.

ABSTRACT

Leasing, as a financing instrument, is an integral part of today's entire economic life. The understanding that the advantage is not connected so much with the legal ownership of the fixed asset but primarily with the opportunity to use it is more and more widespread within business entities. Beneficial ownership in connection with lease agreements can be interpreted as an undercover purchase, combined with a loan financing by the lessor. Therefore, it is not surprising that the increase in the relative importance of leasing activities makes banks become more cautious. Leasing companies have seen a continuous growth even during economically difficult times, and in some areas, these increases are significantly higher than the overall economic growth.

Leasing activities have an enormous impact on the balance sheet. Leasing has a direct effect on the recognition and subsequent depreciation of a fixed asset. In addition, it affects the capital structure and thence the debt to equity ratio of an entity. To avoid negative rating assessments, lessees usually have a special interest in designing the lease contract in such a way that only the rental expense has to be reported. In this case the leased item and especially the relevant lease liability would not be recognized in the balance sheet and the liabilities and the debt to equity ratio would be unaffected. Therefore, the central question regarding leasing businesses is the classification of the leased items.

The objective of the thesis has been to research the need for the reform of the current capitalization of leases and to analyze reporting of lease agreements in the context of the capitalization concepts discussed as part of the current lease project of the IASB/FASB regarding their propagated and improved decision usefulness for the entity.

Regarding the evaluation benchmark for the analysis of the current regulations and for the reform proposals regarding the lease capitalization, a characterization of the economic approach according to the HGB had to be made and the significance of substance over form according to the International GAAP had to be researched. For the sake of precision of the selected object of research, lease agreements were analyzed according to the civil law with the help of the method of an overall observation. The transfer of the use could be identified as the main function of lease agreements. Depending on the will of the contract parties and the related construction of the lease agreement, the proportional relevance of the transfer-of-use-function and the equally important finance function can vary. In the process of creating the contract, the distribution of the risk may vary between the lessor and the lessee. Separated from the national jurisdictions and on the basis of the property rights theory, and from an economic perspective, the concept for the further research of lease agreements was developed. According to this concept a lease agreement constitutes the temporal transfer of rights

against payment, which leads at least to the separation of the right of use from the legal ownership.

With ED/2010/9 “Leases” the capitalization of leases in the IFRS balance sheet is placed on a new basis. While until now the leased item was completely recognized by the beneficial owner in the balance sheet, from now on, in accordance with the right of use concept, an allocation between the lessor and the lessee is required. The necessary allocation of the leased item between the lessor and the lessee in accordance with the right of use concept increases the leeway during the evaluation process. Since the user of financial statements receives considerably more useful information about the economic consequences of the lease agreements the reform has to be welcomed. The existing inconsistencies between the ED/2010/9 and the previously intended definitions of assets and liabilities have to be eliminated during the development of the new IASB framework concept.

**DISSERTATIONS DEFENDED AT
TALLINN UNIVERSITY OF TECHNOLOGY ON
*ECONOMICS***

1. **August Aarma**. Segmented analysis of bank customers and banking information: Estonian case. 2001.
2. **Enn Listra**. The development and structure of banking sector: retail banking in Estonia. 2001.
3. **Tatyana Põlajeva**. The comparative analysis of market's attractiveness. 2001.
4. **Tuuli Tammeraid**. Modeling flow of funds for Estonia. 2002.
5. **Ivo Karilaid**. The choice in general method for investment and performance evaluation. 2002.
6. **Hele Hammer**. Strategic investment decisions: evidence from survey and field research in Estonia. 2003.
7. **Viljar Jaamu**. The methods and instruments for solving the banking crisis and development of the banking sector in Estonia. 2003.
8. **Katri Kerem**. From adoption to relationships: Internet banking in Estonia. 2003.
9. **Ly Kirikal**. Productivity, the malmquist index and the empirical study of banks in Estonia. 2005.
10. **Jaanus Raim**. The PPP deviations between Estonia and non-transitional countries. 2006.
11. **Jochen Sebastian Heubischl**. European network governance – corporate network systematic in Germany, the United Kingdom and France: an empirical investigation. 2006.
12. **Enno Lend**. Transpordiühenduse ja logistikasüsteemi interaktsioon (Saaremaa ja Hiiumaa näitel). 2007.
13. **Ivar Soone**. Interrelations between retail service satisfaction and customer loyalty: A holistic perspective. 2007.
14. **Aaro Hazak**. Capital structure and dividend decisions under distributed profit taxation. 2008.
15. **Laivi Laidroo**. Public announcements' relevance, quality and determinants on Tallinn, Riga, and Vilnius stock exchanges. 2008.
16. **Martti Randveer**. Monetary policy transmission channels, flexibility of the economy and future prospects of the Estonian monetary system. 2009.

17. **Kaire Põder**. Structural solutions to social traps: formal and informal institutions. 2010.
18. **Tõnn Talpsepp**. Investor behavior and volatility asymmetry. 2010.
19. **Tarmo Kadak**. Creation of a Supportive Model for Designing and Improving the Performance Management System of an Organisation. Case studies. 2011
20. **Oliver Parts**. The Effects of Cosmopolitanism on Estonian and Slovenian Consumer Choice Behavior of Foreign versus Domestic Products. 2011.
21. **Mike Franz Wahl**. Basic Human Values & Will of Capital Companies' Ultimate Owners and Construction of an Ownership Typology. 2011.
22. **Jüri Kleesmaa**. Economic Instruments as Tools for Environmental Regulation of Electricity Production in Estonia. 2011.
23. **Mart Nutt**. Formation of the Competence of the Parliament of Estonia and Its Implementation in International Communication. 2011.
24. **Igor Novikov**. Credit risk determinants in the banking sectors of the Baltic States. 2011.