

The Leasing Contract – Concept and Types

Veselin Konstantinov Hristov

Abstract— In recent years, the lease contract has become more and more applicable and occupies a key place in commercial relations and business. In Bulgaria, the legal regulation of the leasing contract is relatively new and imperfectly developed. There are many legal loopholes and it is they that determine the need for a comparative legal analysis.

The purpose of the study is to analyze the various European legislations regarding the leasing contract and to find effective solutions for the legal system of Bulgaria.

First of all, are examined the concept of the leasing contract, which originated in the United States of America around the 1950s and its spread in Europe, and the etymology of the term "leasing" .

After that, the main types of lease contracts – financial and operational – are examined and analyzed in detail. Their features and characteristics were studied, as well as a comparative analysis was made between them.

Next, in the research, a comparative-legal analysis of the leasing contract in different European countries was made in terms of its development and distribution, as well as its legal characteristics. The mechanism of action and functioning of the leasing contract in several European countries is analyzed. Conclusions are made regarding the legal framework under which the lease contract is most effective. Types of leasing contracts specific only to certain European countries and their advantages are examined.

In conclusion, recommendations are made to improve the legal framework of the leasing contract in Bulgaria.

Keywords— Alternative Financing, Leasing Contract, Financing Instruments, Innovation.

I. INTRODUCTION

The leasing as asset financing is the largest provider of financing to business customers and consumers after the traditional form of lending (the bank loan). The leasing can be defined as an investment loan transformed into a material form alternative to the classic investment bank loan.

The vehicles are the most leased asset, followed by machinery, technical equipment, aircrafts, yachts, drilling rigs, etc. A lot of companies (from the smallest to the largest multinationals) are turning to the leasing as an alternative financing product. The start-up companies also very often use the leasing services. The so-called MUSH sector (municipalities, universities, schools, hospitals) is also using leasing as a fast and effective financial instrument to introduce high-tech assets into their activities without having to invest their own large amounts. So, the leasing is a key factor for the economy development of every country

Veselin Konstantinov History, Lecturer, Head of Non-performing Exposures in UniCredit Leasing, Bulgaria

II. HISTORY OF THE LEASING

A. Background

Unlike the bank loan, which received its legal regulation with the first commercial laws in Europe, dating from the 17th-18th century, the leasing contract received its legal regulation in the 50-60s of the 20th century.

Despite fact that the legal regulation of the leasing contract is relatively new, its basic concept - to use someone else property for remuneration - has found expression in various transactions and legal relationships since ancient times.

Some authors believe that Aristotle in his treatises "Wealth is used, not possessed", written around 350 BC, has given the original concept of the leasing contract, as a type of rental relationship.

Other authors, such as the English historian T. Clark, argue that leasing was known long before that. They consider that several provisions of the Hammurabi Act, dating from 1760 BC, entitled "Title 65, concerning leasing and hiring", constitute the oldest evidences founding of the existence of a leasing relationship.

In this context, the leasing contract is settled later in Roman private law in The Code of Justinian, dating from 529 AC

B. The modern concept of the leasing contract.

The modern leasing contract originated from the United States of America in the 1950s of 20th century when, in 1952, in San Francisco, the world's first leasing company was founded - United States Leasing Corporation.

About a decade later, the idea crossed over the ocean and reached Europe, where the first European leasing company was founded in 1962 in Düsseldorf, Germany.

In the 60-70s of the 20th century there was rapid growth in the development of the leasing sector. The reasons for this growing were, on one hand, the increasing lending requirements of the banks and, from another, the foundation of specialized leasing companies which start to offer a new investment financial product. The leasing industry was developing progressively in the 70s when a significant number of leasing companies were founded in Western Europe. In 1972 the European Federation of Leasing Associations - Leaseurope was founded. Its members are leasing companies from almost all European countries.

In the countries of Central and Eastern Europe, such as Poland, Czech Republic, Hungary, Bulgaria and the countries of the former Soviet Union, the leasing contract start its development in the 90s of the 20th century. During the period

of the transition to a free market economy in these countries the leasing was not only a new method of financing, but also was an important factor for their economic reforms and development.

In Bulgaria the leasing for the first time was regulated in the Commercial Act of 1996. The first Bulgarian leasing company was founded in 1997. To the present date the registered leasing companies in Bulgaria are more than 45.

C. *The Leasing Contract Nowadays*

Nowadays the leasing contract, as a legal institute, is a subject of study by the legal science. It is widely used in the trade turnover and developing itself as a legal institute. This leads to the appearance of new types of leasing contracts, such as leaseback, leverage leasing, eco-leasing ect

III. DEFINITION AND TYPES

The etymology of the term 'lease' is derived from the English verb 'to lease' and has English roots. From comparative law point of view, as well as in the Bulgarian legislation, there is no precise translation of the term. This is most likely due to the different term translation in the individual national legal systems.

An interesting fact is that the term "lease" was used for the first time during the Second World War to refer to an operation which was not a typical leasing relationship - "land-lease" - naval deliveries of arms, combat equipment ect. from USA to the Allies.

There are some differences between the two terms – "lease" and "leasing." It should be clarified that 'leasing' refers and it is equivalent to the 'leasing contract', whereas 'to lease' refers to the using of an asset for a remuneration.

IV. MAIN ADVANTAGES OF THE LEASE FINANCING

The main reason the leasing to be established as a stable financial instrument is the advantages it has over the traditional bank lending, as follows:

-Financial leasing could cover up to 80% of the value of the asset without providing any collaterals by the lessee, unlike traditional bank loan, which usually covers 70-75% of the investment value and usually requires the borrower to provide some additional collateral (mortgage, pledge, bank guarantee).

-Financial leasing may provide for the payment of a residual value (so-called an option or open ended contract) at the end of the contract term, which can reaches up to 20-25% of the value of the leased asset. This option is highly in favor of the lessee, because it significantly facilitates his financial burden during „lifetime“ of the contract as at the end of the contract the lessee could choose whether to pay this residual value or to return the asset.

-The lessor manages all the incidental costs during the "lifetime" of the lease contract, such as insurance, taxes, fees, etc., which greatly facilitates the lessee (opposed to the bank loan where the borrower is responsible for this)

-The lessee does not have to close down some his own free financial resources, because he mainly uses the financial

resource of the lessor as keeping his owns for investment and developing his activity

- Tax efficiency for the lessee (VAT)

- The leasing contract does not require an explicit form for validity

-Fast and flexible financing - lower requirements compared to the investment bank loan, the deal is carried out in a shorter period and in better interest rates conditions

V. OPERATING LEASING

The two main types of leasing contract are operating and financial. This division is traditional and accepted in the legal systems of the most European countries.

An operating leasing is also known as an ordinary leasing. As a legal instiut it is similar to the rent contract that's why some authors categorise it as a type of a rent contract. The main purpose of this type of leasing is the using of a leased asset. In this type of leasing the lessor does not borrow its own financial resources to the lessee, investing them in the acquisition of a specific asset which will be the object of the leasing contract. At the date of the conclusion of the leasing contract the lessor is an owner of the asset which is object of the contract, and he don't acquire an asset to lease it. In this type of leasing contract the lessee cannot acquire the leased asset on the ground of the contract. This can only be happen if between the parties is concluded a new unrelated additional purchase contract for the sale of the leased asset. In this case the acquisition price of the asset will be its fair market value (not its residual leasing price as is in the financial leasing). That's why, usually, at the end of the operating leasing, the lessee returns the asset to the lessor, because the lessee is not interested to buy the asset at its fair market value.

VI. FINANCIAL LEASING

The other type of lease, defined as a financial leasing, is a form of leasing under which the lessor acquire an asset from a third party (supplier) on terms determinated by the lessee and lease it to the lessee for use. Upon performance of all its obligations under the financial leasing, the lessee may acquire the asset on its residual lease value or to return it. The specifics of the financial leasing are in its structure which involving three parties – the lessor, the lessee and a third party (supplier) and three relationships between them – mandate (primary) relationship, leasing contract and executive relationship (supply contract).

VII. SUBLEASING

The subleasing is not explicitly established as a separate type of contract. It is a derivative relationship existed between the lessee and a third party. Its legal nature is a type of rental relationship under which the lessee may lease the use of the leased asset to a third party with the lessor's approvement. There is not any special requirement for the form of the agreement between the lessee and the third party. The third party is only user of the leased asset and he could not claim

any rights of acquisition in relation to the leased asset. Only the lessee has such rights. The lessor does not have any rights in relation to the third party and could not claim any overdue payments against him.

VIII. LEASEBACK

The leaseback is a special type of a financial leasing contract which has no a legal regulation in most European countries. In relation to the leaseback are applied (accordingly) the general rules established for the financial leasing and commercial practices of the leasing companies.

The specifics of this legal instrument is that the figures of the lessee and the supplier match. On one side, the lessee enters into the relationships as a seller under the supply contract and, on the other, as a lessee under the leasing contract. There are two legal relationships between two parties. Ownership over the asset is transferred from the lessee (supplier) to the lessor, who lease back to the lessee the same asset. The main purpose of these transfers is to be accumulated free (operational) financial resources for the lessee.

In Bulgaria there is isolated case law which declared the leaseback as invalid, because it is contrary to mandatory provisions prohibiting agreements whereby the liability of the debtor (the lessee in our case) is settled in advance between the parties in the case of his default. In this case the creditor (the lessor in our case) is secured by the transfer of the ownership over the leased asset agreed in advance in its favour. The court held that the leaseback in fact is a loan secured by a commercial sale with buyback option which is prohibited by the law. According to the court interpretation, this case is about pre-arranged way of satisfying the creditor before any default by the debtor.

In Italy the legal lack of the regulation of the leaseback is overcome by a decision of the Italian Supreme Court according to which the leaseback is accepted as valid legal relationship.

In conclusion I would say that it is recommended the leaseback to be explicitly regulated in the national legislations of the European countries. Thereby its application will be secured and the interests of the parties will be better protected.

IX. CONCLUSION

In the 90s of the 20th century the leasing was established in over 80 countries worldwide. By 2020 the size of the global finance leasing market was USD 1 200 970 million and is expected to reach USD 1 995 380 million up to 2027. Due to the significant increasing of the leasing as a financial instrument, its legal regulation should be constantly improved and the existing legal gaps filled.

Nowadays it can be concluded that leasing has become one of the largest and fastest growing sources of capital investment, both in industrial and developing countries.

REFERENCES

- [1]The Commercial Law of Bulgari
- [2]Simon S. Gao, International Leasing, 1999,
- [3]John A. Humbach, The Common-Law Conception of Leasing: Mitigation, Habitability and Dependence of Covenants, 1983
- [4]Suzanne Hausknecht, Marketing and Leasing, 2015
- [5]Leaseurope Benchmarking and Leaseurope Paper
<https://www.leaseurope.org/>