Operating Leasing and IFRS 16

How IFRS 16 affects lessees?

How can simplifications benefit lessees?

Why operating leasing remains attractive?

How Autohellas Hertz can support you?

Autohellas Hertz
Operating Lease

Q&A

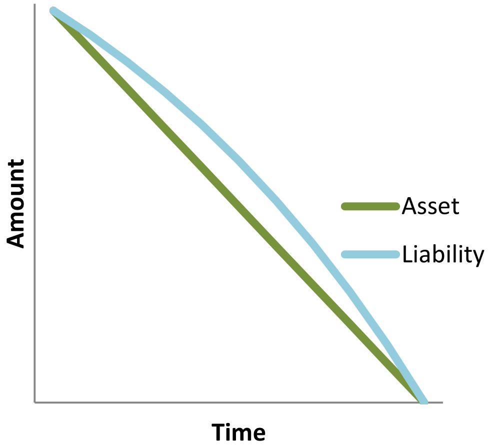
Question	Answer
Who is affected?	Entities acting as lessees, having adopted the International Financial Reporting Standards (IFRS) for the preparation of their financial statements.
What is defined as a lease?	The new reporting standard defines a lease as a contract, or part of a contract, that conveys the right to use an asset (the car) for a period of time in exchange for consideration.
Why the change?	The new reporting standard is introduced in an effort to ensure that information that faithfully represents lease transactions is reported and provides a basis for users of financial statements to assess the information stemming from a lease.
What is new?	Under the new reporting standard, any discrimination between operating and financial leasing is eliminated and a single lessee accounting model is introduced.
Are there exemptions to this new reporting standard?	The only (optional) exemptions are those lease agreements that meet one of the following conditions: A) lease period <12 months B) value of the asset when new <US $5,000
When will the new reporting standards come into effect?	Companies will have to comply with the new reporting standards, as of 1.1.2019.
What support does Hertz Autohellas provide?	Customers of Hertz Autohellas will be able to download all the data needed during the duration of the lease contract, through a newly-customized tool that can be found on our website soon.

Hertz® Lease

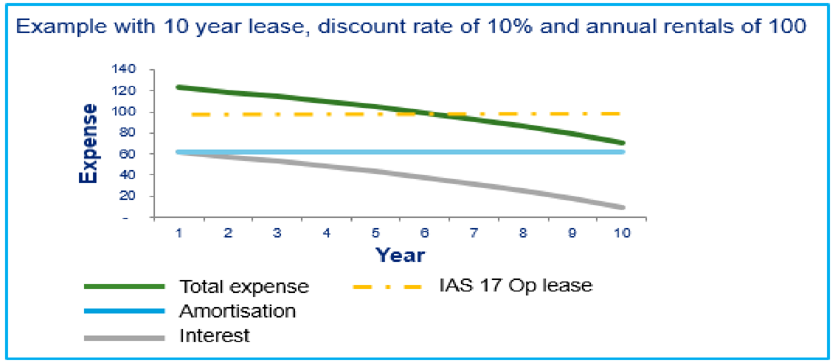
How IFRS 16 affects lessees?

		Before	After
P&L	Lease (expense)	√	-
	Interest Expenses	-	√
	Depreciation	-	√
Balance Sheet	Assets - Right-of-use asset	-	√
	Liabilities - Lease Liability (contractual agreement)	-	√

Balance sheet



Income statement



Income Statement	**Balance Sheet**
EBITDA	Total Assets, Total Liabilities
EAT (in early years)	Net Assets (in early years)

- Companies that report under IFRS will have to recognize a **right of use asset** and a **lease liability** on their balance sheet for all types of leases of vehicles, as of January 1st 2019.
- Under previous guidance (IAS 17), payments for operating leases of vehicles were recognized **as operating expenses** in the income statement on **a straight line basis**.
- Impact on the income statement is that the total lease expense will be **front-loaded** even when cash rentals are constant.
- IFRS 16 will have an impact on lessees' **financial ratios**.

How can simplifications benefit lessees?

Lessees need to consider the simplifications provided by the new standard in order to **reduce the effort and costs** associated with the application of IFRS 16.

Optional recognition exemption for short – term leases:

IFRS 16 offers lessees a recognition exemption for **short-term leases** of vehicles (less than 12 months).

For these leases, lessees can continue to straight-line the expense in the income statement and keep them off balance sheet.

Unbundling lease from non-lease components:

Vehicle lease contracts usually contain non-lease components, such as maintenance.

IFRS 16 requires allocation of contract payments between lease and non-lease (service) components on basis of **relative standalone prices**. Relative standalone prices may not be readily available and lessees may need to apply considerable judgement in order to **estimate** these prices.

IFRS 16 provides lessees a practical simplification to treat entire contracts that contain a lease as a single lease, **removing the need for an unbundling exercise**.

Discount rate:

Under IFRS 16, lease payments included in the lease liability should be discounted using the interest rate implicit in the lease, if this can be readily determinable; otherwise the **incremental borrowing rate** shall be used.

The IASB provided the alternative of incremental borrowing rate, considering that it is likely difficult for lessees to obtain the relevant information from lessors in order to determine the interest rate implicit in the lease.

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Why operating leasing remains attractive?

Focus to core business by outsourcing a non-core activity

Greater **liquidity** compared to use own capital to acquire vehicles

Reduced risk (e.g. residual value risk)

Predictable lease costs

Improved **EBITDA**

Administrative and **economic benefits** arising from negotiations performed by specialists (e.g. insurance, maintenance)

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