

THEORETICAL AND PRACTICAL CONSIDERATIONS ON THE EXECUTION OF THE LEASING CONTRACT IN ROMANIA

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Abstract

Leasing contract: the present study was made with the scope to underline the ambiguity and the controversies between the national laws and the international norms which govern this type of contract, which is so widely used in economically developed countries.

The leasing contract is not a contract for instalments' payment nor a rental contract, it's a special type of contract, a form of financing by which all of the participants capitalize on their resources in a benefiting way, so no one loses and everybody wins.

These benefits can become a reality only by obeying strict and clear norms, which leave no room for interpretation, because any personal interpretation may radically change its legal form, converting it to something totally different from a legal point of view.

The main purpose is not to solve a previously solved equation, but to compare the national and international norms so as to raise necessary questions where they should be raised.

Keywords: *to lease, residual value, the lease term, financed amount, instalment, financial leasing, operational leasing.*

1. Introduction

Based on the translation of the word "leasing", excluding the strict morphological origin from English language, the verb "to lease"- giving towards usage, defines and benefits of a determined legal feature, to grant the right of the precarious detention (the use of something not owned) of an asset for a determined period of time, and at the end of the term having the possibility of transferring the property right, without confusing with the verb "to rent"- to lease, which consists of transferring the right of usage on a strictly determined period of time, at the end of which the owner will retrieve the asset. We make this statement in order to fundament the following theory on this principle.

Leasing is a way to finance individual or legal entities consumers , that wish to acquire movable or immovable assets, on a long time use, but which do not have financial possibilities or do not consider the investment stringently required. This way of financing comes to meet those who cannot or will not access bank loans by encumbrance of movable or immovable assets through the establishment of mortgages or liens. It has proven to be one of the most efficient means of financing productive investments, offering additional security to those who do not dispose of sufficient capital.

The complexity of this contract which at first sight seems so ordinary, together with the legislative gap in our ambiguous legislation, is and will be a constant source of research and informing, but also a controversial source of conflict.

Based on the assumption that in modern society the notion of leasing is almost known, I will

intentionally omit the thorough presentation of this contracts' legal features , insisting, on the other hand, upon this contracts' position in the context of current national and international law.

Due to its particular legal structure, but also to its alternative execution conditions, the leasing contract positions itself in a particular framework compared to the other types of contracts, being viewed on an individual basis in terms of enforcing international economic-financial provisions under current legislation.

The main issue that the leasing contract encounters in Romania is represented by the faulty and confusing legislation.

1. PERFORMANCE OF THE LEASING CONTRACT

In the operational area of the leasing contracts 'performance can be found:

- The purchase agreement
- A lease
- A contract of mandate
- A real estate sale-purchase promissory agreement

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The provisions of international regulations such as SIC 17¹ and UNIDROIT², regarding the leasing contract, have precise specifications about its performing, under one of the two categories, financial and operational, as well as to their defining features, from both the legal and economic point of view. These directing provisions were taken respectively also in the Romanian legislation. Thus, we notice the following:

– The financial leasing contracts are defined as the leasing operation that transfers, largely, on all the risks and benefits incidental to ownership of the asset. The title deed can be transferred, eventually, or not.

I. The features that normally lead to a classification of the leasing operation, as being financial leasing, are:

1. The contract states that the ownership of the asset will be transferred to the holder by the end of the leasing term.

2. The holder has the option of purchasing the asset at a sufficiently advantageous estimated price (small enough in relation to its fair value), so as at the beginning of the leasing, there is a reasonable certainty that this option can be exerted.

3. The leasing contract covers most of the activities' economic life, even if there is no transfer of ownership.

4. The value of the actual minimum of the leasing installments (minimum leasing payments), at the date of the contracts' commencement is at least equal to almost all of the active's fair value to hire.

5. The assets that are subject to the leasing contract are of special nature so as only the holder may use them without making any subsequent changes.

II. Operational leasing contracts are defined as leasing operations which do not qualify as financial leasing.

The different aspect of land and buildings should be retained – overall, of real-estate assets – developed by SIC 17, putting this type of assets in a special class due to their longer lifespan, recommending their registration in terms of operational leasing in order to avoid, in the case of financial leasing, calculation of a high residual value or of a very high installment rate.

Within the meaning of IAS 17 (3rd paragraph), the following terms mean the following:

a) The fair value is the amount at which an asset can be traded or a liability settled, willingly, between knowledgeable parties, within a transaction in which the price is objectively determined, term which has been taken into OG 51/1997³, as an input value representing the acquisition cost of the asset.

b) The leasing term states the period of time, irrevocable, for which the lessee has contracted to

lease the asset [...], with or without additional payment, option for the exercise of which the lessee is certain, to a reasonable extent, at the beginning of the leasing. – this concept has been taken into OG 51/1997 referred to as the leasing period, but whose definition, although very important, cannot be found within the contents of the ordinance.

c) Economic lifespan is the period of time in which an asset is estimated to be economically used by one or more users; - term that cannot be found in the leasing national legislation, the legislator perhaps considering that the duration strictly concerns the funder;

d) The useful life is the estimated remaining period of time, from the beginning of the leasing term, without being limited thereto, during which it is expected that the incorporated economic benefits are consumed by the entity; - term that cannot be found in the leasing national legislation, the legislator perhaps considering that the duration strictly concerns the user;

e) Minimum leasing installments are payments which the lessee must or may be bound to make, during the leasing term, excluding contingent rent, cost of services and taxes that the lessee will pay and which will be reimbursed thereof – term which we absorb as installment, defined by OG 51/1997 as being “the share of the assets' entry value and the lease interest rate, which is determined based on the interest rate agreed by the parties” – in the case of financial leasing;

f) The residual value represents the estimated fair or market value of the leased asset, at the end of the contract; only did this notion was taken over by Law no.287/2006 as: “residual value represents the value at which, after payment by the user of all leasing installments stipulated in the contract and all other amounts due under the contract, the ownership transfer is made upon the asset to the lessee and is settled by the contracting parties”; whose interpretation taking over evidently raises a number of questions to those interested, being an ambiguous and generic definition which is economically and legally unrelated with the definition found in international regulations. In art. 27 alin. 3 of OG 51/1997, subsequently amended, residual value is looked upon as a random value that will be agreed upon willingly by the parties, in fact wholly misunderstood, from an economic point of view this value is mandatory agreed upon through specific regulations in the area.

In the case of returning the asset at the end of the leasing term, in order to be protected against various risks surrounding its activity and that may affect the residual value of the asset, upon request of the lessor, the lessee will ensure the achievement of the assets'

¹ IAS were issued between 1973 and 2001 by the International Accounting Standards Committee (IASC) and represents a set of accounting standards, all listed companies in the EU are now required to prepare consolidated financial statements in accordance with IFRS (new name). The main purpose of IAS 17 is the definition and disclosure of financial or operational leasing operations.

² International Institute for the Unification of Private Law, commonly known under the name UNIDROIT is an independent intergovernmental organization whose purpose is to study ways of harmonizing and coordinating the private law of states and groups of states and progressive preparation for the adoption by its various members of uniform rules of private law.

³ Government Ordinance no. 51 of 28 August 1997 on leasing operations and leasing companies, the issuer Government of Romania, published in Official Gazette no. 224 of August 30, 1997

residual value to at least a certain value, consented by the lessor, thus named guaranteed residual value. Such guarantee of the residual value can be directly made by the lessee or by means of an affiliated party to the lessee.

Only that this term in our legislation, I mention, was completely ignored, although of major importance in protecting the economic point of view of the financier. The contract provides, according to defining legal rules that ownership of the asset will be transferred to the lessee by the end of the lease term. Thus, given that the lessee takes possession of the title deed at the end of the lease, it will be clear that leasing installments shall have to be sufficient in order to return the lessor his costs plus the reimbursement of invested capital. International regulations make no reference to the lessor / funder accounting registration of amounts collected in advance and that they could claim starting of the lease term. In contrast, OG 51/1997⁴, article 6, section. (2) letter "c" specifies imperatively the insertion in the leasing contract of the value of the advance payment, so by default a sum paid in advance.

I subscribe to the course of performing the leasing contract, only by paying installments, without paying any amounts as advance, as defined by international regulations and established by practice, in general, through the annex schedule to the contract, thereafter being registered as revenue for the lessor/financier and as an expense for lessee/user.

Unlike loans, leasing essence is to ensure full funding of an investment, hence the entire cost of acquisition of asset that is subject to the contract.

All leasing companies in Romania claim their customers payment of an amount in advance, and this prior to purchasing the asset that is subject to a leasing contract. Under these circumstances, the financed amount becomes lower than the asset's cost of acquisition, reducing itself by the advance payment paid by the client, with which it basically auto finances.

I believe that by imposing the lessor/financier to make an advance payment as well as by paying the residual value simultaneously with the installments – the leasing contract becomes a sale- purchase agreement with installment payments, starting with the collection of the advance payment, the lessor/financier losing the capacity of lessor, while remaining financier - him becoming a promissory seller, and the lessee/user by accepting to make the advance payment, as well as the residual value simultaneously with leasing installments receives the status of a promisor buyer, thus eliminating from the very beginning the essential and defining feature of the leasing contract, being the temporary transfer of right to use, with the right to option regarding purchase or restitution of the asset that was subject to the contract, because making the advance payment confers the lessee/user not only a

precarious right of possession but rather a right to effective property.

Assuming that the lessee/user, after accepting the contracts' conditions on advance payment and inclusion in all or part of the residual value in the installments, due to factors beyond their control or dependent, give up the option of buying the asset or of continuing their leasing contract during its performance, then the amounts representing advance payment, as well as the residual value collected by the financier, may constitute unjust enrichment, not constituting the subject of a leasing contract *stricto sensu* (strict sense).

In the case of leasing contracts, the investment is the lessor's/of the financier, who has the necessary funds to purchase certain movable or immovable assets, which he then gives to be used for an amount to be paid consecutively in installments as leasing rates, on a preset time, the value of the installments, upon enforcement of the contract is at least substantially equal with all of the value of the leased asset, so that at the end of this period the lessee/user can opt for termination of leasing or purchasing the asset. Only then through the collection of the market value or of the amount remaining to be depreciated, strictly defined as residual value and that will benefit the lessor/financier, as owner of the asset, in order to recover the investment made, a transfer of ownership will be done. Since leasing is different from loan precisely because it's meant to provide financing to those who lack equity or attracted (loans) for purchasing the asset, we believe that clear regulations should be imposed upon this issue in the leasing legislation, so that they could contract an asset in a leasing type system without a down payment.

2. TERMINATION OF LEASING

The leasing contract is considered terminated under the following circumstances:

- a) If the user refuses to receive the asset upon the deadline stipulated in the lease.
- b) If the user is in a state legal reorganization and/or bankruptcy.
- c) Failure of the user's right to option.
- d) Failure to perform full payment of installments obligations.

I consider analyzing for the Romanian legislator appropriate, especially the situation in which termination occurs for default of payment, as this situation has that generated most disputes relating to the leasing market in Romania last years.

Whenever there is any cause of early termination of the contract, of the nature of wrongful default by a Contracting Party of the obligations derived from the contract, the New Civil Code states that: "*When, without justification, the borrower fails to perform the*

⁴ The Act includes changes in the following documents: Tax Code published in 2003; Law no. 533/2004, Law no. 287/2006, Law no. 241/2007; Law no. No 93/2009 published in the MOF. 259 of 21/04/2009; Law no. No 383/2009 published in the MOF. 870 of 14/12/2009.

obligation and is in default, the creditor may, at its discretion and without losing the right to penalty clauses whether due to him [...] 2. obtain, if the obligation is contractual, retroactive termination or termination of the contract or, where appropriate, reducing their correlative obligations; [...] S. N. "this being confirmed by para. (2) art. 1516.

In the case of the leasing contract when the lessee / user does not perform the obligation to pay the full installments for two consecutive months, calculated from the due date specified in the lease, according to art.15 of OG 51/1997, the lessor / financier has the right to cancel the lease and the lessee/user must return the asset and pay all amounts due up to the date of the refund under the leasing contract.

Art. 15. –*"If the contract does not provide otherwise, if the the lessee / user does not perform its obligation to pay in full of the leasing rate for two consecutive months, calculated from the due date stipulated in the lease, the lessor / funder has the right to cancel the lease and the the lessee / user is required to return the asset and pay all amounts due, until restitution under the lease."*

Corroborating this benefit conferred by law to the lessor/financier with the power of enforceability of the lease term (art.8 of OG51/ 1997), recovery of the prejudice seems apparently usual. As such, issues arising from the provisions relate to its interpretation and practical application of the law, being the courts attribute.

In the matter of interest here, according to art. 8 O.G. no. 51/1997 on leasing operations and leasing companies, leases, are enforceable titles: "*Art. 8. - leases and real and personal guarantees, established in order to guarantee the obligations under the lease, are writs of execution*". If the lessor / funder will cancel the lease for failure to pay the lease rate according to art.15, the question is whether we can proceed to forced execution of the the lessor / user based on the power conferred by art.8 the lease term of the ordinance?

I think not, because once the lease terminated, it is no longer effective, it no longer has any an output between contracting parties, and a claim to that effect coming from the creditor would amount to the performance of the contract, provided that it opted itself for dissolution of the contract.⁵

1. Both the old Civil Code, the State under art. 1021, that the party who has fulfilled its contractual obligations has choice or to compel the other party to perform the convention if possible or to request cancellation of the convention with damages.

2. Furthermore in the New Civil Code the court prerogatives are intended to restore, where appropriate, the contractual balance of the consideration of benefits and avoid excessive

conspicuously abuses, thus as cancellation of the contract for failure to pay, the company financing will be subject to the following provisions:

"Art. 1755 Reserve property and risks

When a sale with the installment payment, the payment obligation is guaranteed with reservation of ownership, the buyer acquires ownership of the date of payment of the final installment of the price; But good risk is transferred to the buyer upon delivery of it.

Art. 1756 Failure to pay a single rate of price

Unless otherwise agreed, failure to pay a single rate, which is more than an eighth of the price, does not give the right to terminate the contract and the buyer retains the benefit period for successive rates.

Art. 1757 Termination of contract

(1) When obtained terminate the contract for failure to pay the price, the seller is required to repay all amounts received but is entitled to retain, in addition to other damages, fair compensation for the use of the asset by the buyer.

(2) When it was agreed that the amounts received as rates remain, in whole or in part, acquired by the seller, the court may nevertheless reduce these amounts properly applying the provisions relating to the court reduced the amount penalty clause.

(3) The provisions of par. (2) applies if the lease and of the lease, if, in the latter case, it is agreed that upon termination of ownership of the property to be acquired by the lessee after payment of the agreed "

Therefore, if the creditor has chosen cancellation of the convention, it cannot require the debtor, naturally, than liquidated damages, damages that can, of course, be proved.

I appreciate therefore that obvious inconsistency between the provisions of the Civil Code and art.15 of OG 51/1997, make it impossible for them to be simultaneously enforced, the legislator being left at the interpretation of the court's judgement to resolve this conflict of laws.

Due to the unusual and complex leasing contract, and due to the lack of clear legislation in this field, leases are subject to numerous interpretations thus generating a large number of disputes.

Hoping to revitalize the leasing market in Romania, I consider it appropriate to revise the current legislation and its completion in accordance with international regulations, for this the beginning being constituted by the provisions of the New Civil Code, which already began to have effect. Based on this, although major inconsistencies appear between theory and practice, sometimes daunting, we remain nevertheless at the opinion that the variant of leasing, financial or operational, gives the user account of the undeniable advantages in comparison to other methods of buying or renting.

⁵ Civil Sentence no. 1332-1307 Vaslui pronounced by the Court in April 2010 in case no. 1610/333/2010.

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