

LEASING

1.14

WHITE BOOK BALANCE SCORE CARD

Recommendations:	Introduced in the WB:	Significant progress	Certain progress	No progress
Initiation of amendments to the Law on Value-Added Tax concerning interest taxation, to abolish VAT charged on interest contained in the leasing fee.	2009			√
Amendment to the Law on Financial Leasing to explicitly transfer the obligation to settle unpaid parking tickets to the lessee, allowing the Parking Services to directly collect the payment from the lessees that are registered in the Registry of Motor Vehicles kept by the Ministry of Interior. Regulate operating leases by law and enable financial lease providers to offer operating lease services as well.	2016			√
The Law on compulsory traffic insurance should be harmonized with the Law on Financial Leasing, specifically the provisions on the right of the Guarantee Fund to seek recourse upon payment of damages caused by a vehicle not covered by mandatory insurance from the owner i.e. registered user of the means of transport, so that the insurance company may seek recourse from the lessee and not from the leasing company.	2012			√
In developing a program of incentives for the economy (industry, agriculture, etc.) and drafting laws and regulations on this matter, policy makers should envisage the possibility of using other forms of financing, including bank loans and financial leasing, to support the implementation of incentives. Given that financial leases are also a suitable form of funding, they should be included in the subsidized programmes of the Government of the Republic of Serbia, in order to improve the competitiveness of the financial market and the offer of favourable forms of financing.	2016		√	
Leasing and insurance companies should enjoy the same treatment as banks regarding Article 85 of the Law on Personal Income Tax, i.e. in the case of write-off of receivables they should not be required to pay additional personal income tax if they have previously met statutory requirements. Amendments should include a simple change such as adding the word "insurance company" or "lessor" next to the word "bank customer."	2016			√
Capital requirements for performing leasing operations involving immovable assets should be lowered in order to make real estate leasing more attractive on the Serbian market. We suggest that, for the performance of finance lease operations, the monetary share of the lessor's founding capital may not be below the Serbian dinar (RSD) equivalent of EUR 500,000 at the official median exchange rate on the date of payment, for leasing movable as well as immovable property.	2015			√
Urgently resolve the problem of inadequate legal protection of leased assets. There should be consistent application of the Law in court proceedings conducted in this legal matter which should be in accordance with the Law and the Constitution of Serbia.	2018			√

CURRENT SITUATION

The development of leasing in Serbia dates back to the beginning of 2003, when the Law on Financial Leasing was adopted. There are 17 leasing companies currently operating in Serbia, mainly affiliates of distinguished financial institutions, leaders in the banking and finance markets in Central and South-East Europe. These groups have applied their knowledge and high corporate business standards to the Serbian market as well. As a result of market competition, it is expected that the number of active leasing companies will adjust to the market needs and decline in the future. This will help further affirm the quality and high standards of leasing services offered by market leaders so far.

POSITIVE DEVELOPMENTS

In 2018 there were no improvements with respect to the remaining issues. In the meantime, the position of leasing companies has been further compromised due to the inadequate legal protection of leasing companies' assets, an issue that has not yet been resolved. The National Bank of Serbia has not initiated the adoption of changes of the Law on Financial Leasing.

REMAINING ISSUES

1. Interest in financial leasing is taxable

The Law on Value Added Tax (RS Official Gazette No 84/2004, 86/2004 - corr., 61/2005, 61/2007, 93/2012, 108/2013, 6/2014 - adjusted RSD amount, 68/2014 - as amended, 142/2014, 5/2015 - adjusted RSD amount, 83/2015, 5/2016 - adjusted RSD amount, 108/2016 and 7/2017 - adjusted RSD amount), treats products and services of financial institutions in a different manner when defining the subject of VAT taxation.

Specifically, Article 4(2a) of the Law clearly states that the turnover of goods under a leasing contract is subject to VAT. Pursuant to the aforementioned Law, the VAT base is the value of the leased asset and interest.

On the other hand, in Article 25 of the same Law, the legislature envisaged that credit and insurance services are exempt from VAT.

Different tax treatments of products and services of financial institutions has led to increasing the costs of financing through leasing in comparison with other types of financ-

ing, and consequently less favourable for certain segments of clients, given that VAT on interest is an additional cost, which means that financial leasing companies are placed in an unfavourable position.

2. Leasing companies are charged parking fees incurred by users of leased vehicles

According to the decisions on public car parks in the cities and municipalities in Serbia, users of public car parks are mainly the drivers or owners of a vehicle, if drivers are not identified. These decisions further envisage that any user of public car parks violating the provisions of these decisions by failing to pay the parking fee will be obliged to pay a fine. In the case of leased vehicles, decisions on public car parks do not take into account financial leasing transactions and thus fines are sent to leasing companies, even though these vehicles are used by the lessees.

3. Operating leases are not regulated by the law and financial leasing companies cannot provide operating leases and the high level of required capital slows down the expected development of the leasing industry

The operating leases are not regulated by special regulations, but exclusively by the Law on Contracts and Torts (Official Gazette of the SFRY No 29/78, 39/85, 45/89 – Const. Court of Yugoslavia Decision and 57/89, Official Gazette of SFRY No 31/93 and Official Gazette of SCG No 1/2003 - Constitutional Charter) in Chapter XI - Lease, the Rulebook on criteria on the basis of which it is determined when the delivery of goods under a lease or lease contract is considered as the sale of goods (RS Official Gazette No 122/12) and a number of other legal acts regulating the exercise of rights and obligations under the lease itself (the object of an operating lease). Therefore, operating leases are not subject to supervision by regulatory bodies in charge of financial leasing. This is a negligible part of the overall operating lease market, i.e. lease of movable properties in the Republic of Serbia. Operating leasing, by its very nature, (customers, suppliers, the way of financing fixed assets, marketing strategies, etc.), is much closer to financial leasing than to classic short-term rent (rent-a-car). Concrete legal solutions for operating leasing in Serbia are needed, first and foremost amendments to the Financial Leasing Law, in terms of enabling financial leasing companies to provide long-term lease services, not only for items returned in financial leasing business activities, but also for newly purchased ones. This would be sufficient reason for even more finan-

cial leasing companies to start offering this type of service, i.e. financial products, and all of this under the supervision of institutions responsible for supervising the activities of financial leasing companies.

The level of required capital for real estate leasing is high, amounting to EUR 5 million. The high level of required capital in other financial institutions (banks, insurance companies or pension funds) is in line with the intention to provide security in the management of client funds. Leasing companies, on the other hand, manage their own funds and are not depository institutions, and they invest their own capital and the entire business.

4. The Guarantee Fund may file recourse claims against leasing companies for the damage caused by the lessee when using the leased asset

According to the Law on Compulsory Traffic Insurance, the Guarantee Fund of the Association of Serbian Insurers has the right to recourse, upon payment of the compensation of damages by the owner of the vehicle for the amount paid for damages, plus interest and costs.

The Law on Compulsory Traffic Insurance is not aligned with the Law on Financial Leasing, which introduced a completely new legal transaction into the legal system of the Republic of Serbia, which, according to the definition of the rules of liability for the use of leased assets, is in contravention of the existing rule on the Guarantee Fund's right to file a recourse claim against the owner of the vehicle. The Law completely disregards the fact that the lessor is not in a position to influence the behaviour of the lessee or other parties using the leased asset and prevent the use of vehicles in traffic without stipulating an agreement on compulsory insurance, as long as the lessee is in possession of the leased asset.

Currently, leasing companies are facing recourse requests by the Guarantee Fund of the Association of Serbian Insurers, which they can reject on the grounds of the Law on Financial Leasing. On the other hand, despite understanding the essence of the dispute, the Guarantee Fund has no legal means to subrogate against any other person, apart from the owner, and possibly the driver, of the vehicle, on the grounds of personal liability of the person who caused the damage.

5. Financial leases are not included in the financing options in some of the state financial incentives programmes

Financial leasing as a form of financing is not envisaged by the Law on Incentives in Agricultural Production (RS Official Gazette of the Republic of Serbia No 10/2013, 142/2014, and 103/2015). Specifically, Article 3, regulating the types of incentives, provides support in the form of loans, but not financial leasing, which prevents leasing companies from participating in these programmes together with banks. One of the conditions is that the fixed asset purchased for the purpose of performing activities in agriculture must be exclusively owned by the recipient of the incentive, which by unilateral interpretation excludes the acquisition of that asset through financial leasing, where the financial leasing company has legal ownership and the recipient of the incentive (lessee) has economic ownership. Also, one of the conditions for obtaining incentives is that the agricultural producer should not dispose of the fixed asset acquired with the use of incentives within a specified time period. If the fixed assets acquired with the use of incentives are acquired through a financial leasing contract, monitoring compliance with this condition by the relevant authority would be an extremely complex, if not impossible task, as financial leasing would be regulated by special acts, stipulating that the recipient of the subsidy cannot repay and/or dispose of the fixed asset before the expiry of the term prescribed by the incentive agreement, so that the financial leasing company would have the additional role of controller, on behalf of the relevant authority.

A positive example is the Decree of the Government of the Republic of Serbia on establishing the Small Business Support Programme for small enterprises to purchase equipment. This programme included leasing companies along with banks.

6. Leasing and insurance companies are required to pay income tax in the case of write off of receivables from personal income taxpayers

When a leasing company or insurance company fails to recover a debt from a customer through courts, and subsequently adopts a decision to write off the irrecoverable debt, that company is still obliged to pay a 20% personal income tax because written-off receivables have the status of "other revenues." This is defined in Article 85 of the Law on Personal Income Tax. Consequently, in addition to suffering a loss resulting from uncollected debts, the leasing or insurance company is also obliged to pay personal income tax on these.

To make the paradox even greater, this is also included in the annual personal income tax base, and consequently, a person unable to settle their debt to a leasing or insurance company can become liable to pay the annual tax, if the value of the write-off, together with other revenues, exceeds RSD 2.4 million. This tax paradox was noticed by the Ministry of Finance, so the Law on Personal Income Tax was amended in 2013 to provide an exception for banks as creditors. However, other financial institutions, also under the supervision of the National Bank of Serbia (NBS), were “forgotten” on that occasion.

7. The lack of legal protection of leased assets of leasing companies is a problem.

As a precondition for the functioning of financial leasing (as a financing model in which leasing companies reserve the right of ownership) is an adequate and complete protection of leasing companies’ assets. However, in addition to other obstacles facing the leasing industry in Serbia, a new obstacle has arisen recently, threatening to quash financial leasing in Serbia - the lack of full legal protection of leased assets. According to the current jurisprudence, in the case of misappropriation of the leased assets, in the Supreme Court’s view there is no objective element of the criminal offense of misappropriation under Article 207 of

the RS Criminal Code, since a leasing contract, in its nature, leads to the acquisition of property rights. Contrary to constitutional principles, leasing companies in Serbia no longer have the constitutional right to protect their property. If the relevant prosecutor’s office continues to apply the Supreme Court’s misguided position, refusing to bring criminal charges for the criminal offense of misappropriation of lease assets, the result will certainly be a very quick withdrawal of all leasing companies from the market of the Republic of Serbia due to the complete absence of property protection. Furthermore, the aforementioned Decision of the Supreme Court could lead to a huge increase in the number of criminal offenses.

8. During the duration of a leasing contract, when registering the vehicle, the lessee each year must obtain a special authorization from the leasing company for holding and using the leased object.

This document is a prerequisite without which the lessee cannot register the vehicle with the Ministry of Interior. When obtaining this document, both the lessee and the leasing company are exposed to additional costs, as well as to spending resources and time. Also, in practice, there have been abuses and cases of counterfeiting this authorization.

FIC RECOMMENDATIONS

- Initiation of amendments to the Law on Value-Added Tax concerning interest taxation, to abolish VAT charged on interest contained in the leasing fee.
- Amendment to the Law on Financial Leasing to explicitly transfer the obligation to settle unpaid parking tickets to the lessee, allowing the Parking Services to directly collect the payment from the lessees that are registered in the Registry of Motor Vehicles kept by the Ministry of Interior. Regulate operating leases by law and enable financial lease providers to offer operating lease services as well.
- The Law on Compulsory Traffic Insurance should be harmonized with the Law on Financial Leasing, specifically the provisions on the right of the Guarantee Fund to seek recourse upon payment of damages caused by a vehicle not covered by compulsory insurance from the owner i.e. registered user of the means of transport, so that the insurance company may seek recourse from the lessee and not from the leasing company.
- In developing a program of incentives for the economy (industry, agriculture, etc.) and drafting laws and regulations on this matter, policy makers should envisage the possibility of using other forms of financing, including bank loans and financial leasing, to support the implementation of incentives. Given the fact that financial leases are also a suitable form of financing, they should be included in the subsidized programmes of

the Government of the Republic of Serbia, in order to improve the competitiveness of the financial market and the offer of favourable form of financing.

- Leasing and insurance companies should enjoy the same treatment as banks regarding Article 85 of the Law on Personal Income Tax, i.e. in the case of write-off of receivables they should not be required to pay additional personal income tax if they have previously met statutory requirements. Amendments should include a simple change such as adding the word "insurance company" or "lessor" next to the word "bank customer."
- Capital requirements for performing leasing operations involving immovable assets should be lowered in order to make real estate leasing more attractive on the Serbian market. We suggest that, for the performance of finance lease operations, the monetary share of the lessor's founding capital may not be below the Serbian dinar (RSD) equivalent of EUR 500,000 at the official median exchange rate on the date of payment, for leasing movable as well as immovable property.
- Urgently resolve the problem of the inadequate legal protection of leased assets. There should be a consistent application of the Law in court proceedings conducted in this legal matter which should be in accordance with the Law and the Constitution of Serbia.
- It is necessary, through the Serbian Business Registers Agency (SBRA), to allow leasing companies to supply the Ministry of Interior with the necessary data by automated means (e.g. web service), and in this way the lessee would be relieved of the obligation to obtain once a year a written authorization for vehicle registration when registering a vehicle. In addition to the above, the proposed solution would put a stop to abuses occurring in practice with the filing of counterfeits of these authorizations.