

VOLKSWAGEN

AKTIENGESELLSCHAFT

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EFRAG
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Consultation Document regarding the endorsement of IFRS 16 Leases

Dear Sir or Madam,

Thank you for the opportunity to comment on your consultation document regarding the endorsement of IFRS 16 Leases.

The Volkswagen Group is one of the world's leading automobile manufacturers and the largest carmaker in Europe. With our 100%-owned subsidiary Volkswagen Financial Services AG we are also the largest automobile financial services provider in Europe. Volkswagen is affected by lease accounting in multiple ways: among other things as lessor of vehicles in Business-to-Consumer and Business-to-Business leases, as lessor of apartments to employees and third persons and as lessee of different leased goods all over the Group.

Our answers to your questions listed in the consultation document, are contained in the annex of this letter.

Best Regards,
Dr. Ingrun-Ulla Bartölke

Annex - Questions

Question 1

Do you have any information or evidence on the extent to which leases (that you are party to or otherwise aware of) will be eligible for each of the short-term and low-value assets exceptions identified in paragraph 24? If so, please provide details.

If you are a preparer, do you expect to use the exceptions? If so, please:

- (i) quantify the number and annual lease payments for each category;
- (ii) indicate the proportion of your leases (by volume and/or value) you estimate to be covered by each of the exceptions.

We are planning to utilize the exception rule for short-term and low-value leases.

There is a significant amount of short-term and low-value leases across the Volkswagen Group. However, with regard to the total number of leases these short-term and low-value leases occur at a normal frequency. A precise quantification of these leases is still pending.

Question 2

If you are a preparer, which approach to transition do you expect to take? Please explain your reasons for this decision.

Due to the short term between publication and first-time application of the standard we are planning to apply the “modified retrospective transition method” according to IFRS 16.C5(b). Since IFRS 16 implies a variety of professional, systematic and organizational changes, a complete retrospective adjustment according to IFRS 16.C5(a) is practically excluded for time reasons.

Question 3

Are you aware of:

- (i) any contracts that you consider to be leases that would not be classified as leases under IFRS 16; or
- (ii) any contracts that you consider to be service contracts (or other non-lease contracts) that would be classified as leases under IFRS 16?

If so, please provide details of these contracts and why you consider that the classification would not be appropriate.

We haven't identified any essential contracts so far, which will change their classification as a result of the new definition of leasing.

Question 4

EFrag is interested in understanding whether leases of intangible assets (other than rights held by a lessee under licensing agreements within the scope of IAS 38) are common. Do you have any information or evidence as to how frequently such leases of intangible assets arise in practice? If so, please provide information about the types of intangible assets that are subject to leases and the significance in operating and monetary terms.

Across the Volkswagen Group there are leases of intangible assets that do not fall into the scope of IAS 38. A precise quantification of these leases is currently pending.

Question 5

Do you have any comments on the comparison of IFRS 16 with IAS 17?

We believe, that the regulations of IAS 17 adequately reflected the different economic substance of leasing transactions. Even if the distinction in „operating leases“ and “finance leases” due to the often difficult and sometimes subjective classification (and thus accounting) is often exposed to criticism, this distinction is still based on an economically understandable analysis of the allocation of the economic benefits and risks of the leasing asset. Leasing arrangements can be used for services (which can be fulfilled only by an asset) as well as to ensure the long-term use of specific assets. This is not always a clearly describable process from an accounting perspective; nevertheless this distinction is based on a fundamental economic justification. The blank assumption that a lease always

represents a financing purchase, leads in our opinion neither to an objective nor to a proper accounting for leasing transactions. The unsystematic result of IFRS 16 is enhanced by the different accounting treatment of leases at the lessor and the lessee.

We do not see any substantial benefit for the users of financial statements by IFRS 16. The IASB itself expects that the new leasing standard won't have any significant impacts on important operative figures (e.g. EBIT, leverage ratio), since the amendments in accounting for lease arrangements caused by IFRS 16 were already anticipated by the users of financial statements under IAS 17. Insofar by the evaluation of the explanatory notes the users of financial statements have always been able to obtain a comprehensive picture of a leasing-transaction. Despite IFRS 16 the majority of users of financial statements will not quit their own, extensive balance sheet analysis in the future. Hence, the argument of the improved provision of relevant and reliable information is redundant.

Question 6

Do you have any views or information on how IFRS 16 can be expected to affect the behaviour of investors and/or lenders? If so, do you have any views or information on whether and how IFRS 16 could, for European companies that apply IFRS, positively or negatively affect:

- (i) the overall cost of capital;
- (ii) access to finance and cost of credit?

Please provide any available evidence.

Due to IFRS 16 leading to a degradation of essential total capital and liquidity ratios, there is a risk that this will lead to higher capital costs, aggravated access to debt capital market and higher borrowing costs. As a result, there is the possibility that investors and lender that had not performed own balance sheet analysis so far, will accordingly adjust their investment decisions.

Question 7

Do you have views or information on how IFRS 16 might affect entities' use of leasing? For example, do you expect lessees to:

- (i) reduce their use of leases with a corresponding increase in purchases of assets;
- (ii) reduce their use of leases without a corresponding increase in purchases of assets;
- (iii) (iii) seek to change the terms of new or existing leases?

Please provide any available evidence.

There is a realistic possibility that companies will buy more assets instead of leasing assets as a result of the new leasing standard. Since off balance sheet leases will only be possible in very few cases, one major financial benefit of an entities' use of leasing will no longer exist. Companies will take this into account when determining their investment decisions.

Question 8

Do you have any additional information or views on how the endorsement of IFRS 16 can be expected to affect the leasing industry in Europe? EFRAG is particularly looking for views from the leasing industry.

Please provide any available evidence.

Since lessees, as shown under question 7, may increasingly question their leasing operations, this may also imply negative impacts for the lessors. We cannot reliably assess whether and to what extent this will eventually occur.

Question 9

Do you have any information or views on how the endorsement of IFRS 16 can be expected to affect SMEs in Europe?

Please provide any available evidence.

We are not able to provide information on this.

Question 10

Do you have any information or views on whether IFRS 16 is likely to endanger financial stability in Europe?

Please provide any available evidence.

We are not able to provide information on this.

Question 11

What is your view on the relative costs of applying IFRS 16 and US GAAP? Do you have any other views as to the advantages or disadvantages of IFRS 16 compared to US GAAP?

Please provide any available evidence.

We are not able to provide information on this.

Question 12

What is your view on the one-off and ongoing costs for preparers? (Please indicate whether you are (a) a lessee; (b) a lessor; (c) both a lessee and a lessor or (d) neither a lessee nor a lessor).

Will preparers that already report finance leases have lower costs than preparers without finance leases?

Please provide any evidence you have on the expected magnitude of the costs.

Entities within the Volkswagen Group operate as lessees and lessors. Through the new leasing standard we expect to require significant one-off implementation costs as well as a significant increase in current costs. The implementation cost mainly result from the IT-based inventory of the leasing stock, the adoption of new IT-systems and the development of new process structures. The current costs result from the operating of new IT-systems and the administrative processing of leasing contracts. We expect additional expenses within the single-digit million Euro range for each of the implementation as well as the current costs.

Question 13

If you are a user, are you aware of any costs in addition to those identified by EFRAG in paragraphs 116 to 118 of Appendix 3? Please quantify if possible and provide any available evidence.

We are not able to provide information on this.

Question 14

If a lessee has to develop new systems to support the accounting for leases, to what extent do you, as a lessee, expect internal benefits from the information provided by the new information? Please quantify to the extent possible.

Do you agree with the benefits for users and preparers identified above? Are there any additional benefits for users and preparers?

Please provide any available evidence.

As stated under question 5, we expect no significant improvements to the provision of relevant and reliable information for users of financial statements by IFRS 16 compared to IAS 17. We expect that most users of financial statements will hold on to their existing tools and methods for their subjective balance sheet analyses – irrespective of the introduction of IFRS 16.

From a user's perspective, we expect no substantial economic benefits for the Volkswagen Group as a result of the new lease accounting.

Question 16

Are there any issues that have not been raised in this Preliminary Consultation Document that should be considered by EFRAG? Please explain your view.

No.