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By PwC Deutschland | 20. Oktober 2017

VAT – Supply of goods – Finance lease with option to purchase

On 4 October 2017 the European Court of Justice decided that a finance lease with an option to purchase should be qualified as a “supply of goods” where the exercise the option appears to be the only economically rational choice that the lessee could make at the appropriate time. As a result the whole of the VAT becomes due when the object to be leased is handed over.

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The Facts

The plaintiff, Mercedes-Benz Financial Services Ltd, a subsidiary of Daimler AG, offers three types of standard contract for financing the use of motor vehicles: a standard hire agreement known as “Leasing”, a “Hire Purchase” agreement, and a leasing agreement with an option to purchase called “Agility”, which combines certain features of the first two types of agreement and which allows customers to postpone choosing between leasing and purchase until after the vehicle has been handed over

The ‘Leasing’ agreement excludes any transfer of ownership and, moreover, sets a maximum mileage beyond which the customer is liable to pay a penalty. In the case it was not disputed that this type of agreement falls within the category “supply of services”, with VAT falling due on the monthly instalments.

The “Hire Purchase” and “Agility” agreements, on the other hand, both provide for a transfer of ownership, but on different terms.

Under the “Hire Purchase” agreement, the total monthly payments made over the term of the agreement generally represents the total sale price of the vehicle, including the cost of financing. A small additional fee is to be paid in order to acquire ownership of the vehicle at the end of the contract. That final payment is provided for in the agreement and does not depend on the option being exercised. Again it was not disputed that this type of agreement falls within the category “supply of goods”, with VAT falling due upon the handing over of the vehicle.

This dispute arose in respect of the “Agility” agreement, under which the monthly instalments are generally lower than under a ‘Hire Purchase’ agreement, with total instalments (including the financing costs) representing approximately 60% of the vehicle sale price. If the user wishes to exercise the option to purchase the vehicle, he must therefore pay approximately 40% of the sale price. That “balloon” payment represents the estimated average residual value of the vehicle at contract maturity. The customer is asked, three months before the end of the contract, whether he wishes to exercise the option.

The Decision

The plaintiff argued that the “Agility” agreement should fall into the category “supply of services”, with VAT falling due on the monthly instalments, as the agreement did not necessarily provide for the transfer of ownership.

The question was how the words ‘contract for hire which provides that in the normal course of events ownership is to pass at the latest upon payment of the final instalment’, used in Article 14(2)(b) of Council Directive 2006/112/EC of 28 November 2006 on the common system of value added tax (Article 14 providing the definition of the “supply of goods”), should be interpreted.

The Court decided that they should be interpreted as applying to a leasing contract with an option to purchase if it can be inferred from the financial terms of the contract that exercising the option appears to be the only economically rational choice that the lessee will be able to make at the appropriate time if the

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contract is performed for its full term. As an example the Court mentioned a situation where at the end of the contract term the lessee would not be obliged to pay a substantial “balloon” payment as the market value of the vehicle was not substantially higher than the instalments already paid.

Source:

ECJ decision of 4 October 2017 - C-164/16

Schlagwörter

Finance leases, Supply of goods, VAT, car leasing