

VAT treatment of end-of-lease transactions

This document should be read in conjunction with sections 3, 25 and 59 of the VAT Consolidation Act (VATCA) 2010.

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1 Introduction

This guidance sets out the VAT treatment of end-of-lease transactions where the lessor is a financial institution that buys an asset (moveable good) and leases it to a lessee.

2 What is a lease

A lease is an agreement whereby one party (the lessee) can use an asset owned by another party (lessor) for a specified period in exchange for payment. A lease does not contain a provision to transfer ownership of the asset to the lessee.

Items leased include plant, machinery and vehicles and these are typically leased for 3-to-5 years' duration. Leases of certain assets, such as construction assets, generally have longer terms, often of 7 years' duration.

The following sequence of events occurs in a typical asset lease arrangement:

- a) The lessee identifies an asset to lease,
- b) The financial institution purchases the asset from the seller of the goods,
- c) The financial institution (lessor) leases the asset to the lessee for a specified term.

3 VAT treatment of a lease

A lease is a supply of services and is generally subject to VAT at the [standard rate](#).

4 VAT treatment of end-of-lease options

At the end of a lease term the following options are available to a lessee:

- (i) The lessee can enter into a further leasing period (sometimes known as a 'secondary lease') for the same asset with the lessor (financial institution).
- (ii) The lessee can seek to lease a new asset, with the existing asset traded in against the new asset,
- (iii) The lessee can purchase the asset it was leasing, or
- (iv) The lessee can hand the asset back to the lessor (financial institution).

4.1 Secondary lease period

Where the lessor (financial institution) and the lessee enter into a follow-on (secondary) leasing period for the same asset at the end of the first lease period, this is a supply of services chargeable to VAT at the appropriate rate.

4.2 Trade-in of a leased asset against a new asset

The trade-in of an old asset against a new asset involves the lessor (financial institution) selling the leased asset, often to the original seller of the goods (this will be the dealer where the leased assets are vehicles) for an agreed trade-in value. The lessor (financial institution) charges VAT as appropriate.

The trade-in value of the original asset reduces the purchase price of the new asset being acquired by the financial institution and, subsequently, the new asset is leased to the lessee.

4.3 Purchase of leased assets by the lessee

Typically, the financial institution will use a special purpose vehicle (or SPV) for the disposal of leased assets. This process allows the lessee to obtain ownership of a lease asset without buying it directly from the financial institution. It is a separate process that stands outside of the lease and is generally offered as an option available to the lessee when a primary lease term expires.

Generally, the selling price of the asset to the lessee is set at a level that reflects the bulk of the lease payments made by the lessee over the course of the lease life. In such cases, the following transactions are necessary to affect the appropriate VAT treatment:

1. The lessor (financial institution) sells the asset to the SPV and issues an invoice to the SPV for the sale of the asset. The sale must be at market value at the time of the sale.
2. The SPV sells the asset to the lessee and invoices the lessee for the asset at the actual selling price to the lessee.
3. The lessor (financial institution) issues a credit note to the lessee which comprises a rebate of the lease payments paid by the lessee to the lessor (financial institution) for the duration of the lease. The rebate usually equates to the bulk of the sales price, as at step 1 above.

In circumstances where it is necessary to reverse the above, (e.g. where a mistake has been made or at the request of the lessee), the following transactions take place:

4. The lessor (financial institution) issues the SPV with a credit note for the asset.
5. The SPV issues a credit note to the lessee for the asset.
6. The lessor (financial institution) cancels the credit note referred to in step 3 above, to reverse the rebate of lease payments.

4.4 Sale of asset to third party

Where the lessee hands back the asset at the end of the lease period, the lessor (financial institution) may decide to sell the asset to a third party. In those circumstances, the lessor (financial institution) will charge VAT at the appropriate rate to the third-party on the supply of the asset.