VAT Treatment of Personal Contract Plans

This document should be read in conjunction with section 19(1) and 25(1) of the VAT Consolidation Act 2010 (VATCA 2010).

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Revenue
Cáin agus Custaim na hÉireann
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Introduction

The purpose of this guidance is to outline Revenue's position with regards to the classification of a Personal Contract Plan (PCP) as a supply of goods or a supply of services.

The question of such a classification was examined in Mercedes Benz case (C-164/16) and provided some guidance as to when a PCP could be considered to be a supply of goods.

1 Legislation

A hire purchase agreement is defined as a supply of goods under section 19(1) (c) of the VATCA 2010, which states that the following is to be treated as a supply of goods:

"The handing over of the goods to a person pursuant to an agreement which provides for the renting of the goods for a certain period subject to a condition that ownership of the goods shall be transferred to the person on a date not later than the date of payment of the final sum under the agreement."

A lease agreement is a supply of services under section 25 (1) of the VATCA 2010.

2 HMRC v Mercedes Benz Financial Services UK Limited (C-164/16)

The background to this case is that a dispute arose between HMRC and Mercedes Benz Financial Services UK Limited (MBFS) as to whether a particular financing product amounted to a supply of goods or a supply of service.

The company offered car finance through a contract for regular payments; with a fee payable on the completion of the financing period should the customer choose to take ownership of the car. Alternatively, the customer could return the car to the supplier.

MBFS contended that this agreement amounted to a lease agreement, while HMRC disagreed on the basis that it was possible, as a consequence of the option written into the contract, that title to the goods would pass to the customer under the terms of the agreement.

The CJEU provided the following guidance in relation to the classification of a contract as a supply of goods:

"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'…must 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 contract is performed for its full term…”

3 Typical structure of a PCP in Ireland

A typical PCP product in Ireland operates as follows. The customer will place a large deposit on the vehicle (typically 10-30% of the value). Monthly repayments will commence for a period that is typically 3-5 years at a low level compared to a standard hire purchase arrangement. A guaranteed minimum future value (GMFV) will be set for the vehicle.

At the end of the financing period the customer has 3 options. Option 1 is to return the vehicle to the dealer and pay nothing further. Option 2 is to pay the final instalment of the GMFV to own the vehicle outright. Option 3 is to trade in the vehicle and enter into a PCP on a new vehicle.

Under Option 3, the dealer will pay the finance house the GMFV and take ownership of the vehicle. The difference between the market value of the vehicle and the GMFV can be used by the customer as a deposit for the PCP on the new vehicle.

4 VAT treatment of a PCP

Revenue is prepared to accept that a PCP may be treated as a supply of goods, in the same manner as a standard hire purchase arrangement, where at the outset of the agreement the only economically rational choice for the customer is to purchase the vehicle at the end of the contract.

In this regard Revenue is prepared to accept the requirement to purchase the vehicle at the end of the contract can be fulfilled by the exercise of either option 2 or 3, as outlined in the previous section.

The assessment of whether the economically rational choice will be to exercise either of these options will need to be made on a case by case basis.

In determining whether the economically rational choice will be to purchase the vehicle at the end of the term, consideration should be given to the GMFV and the predicted market value of the vehicle at the end of the term. Where the GMFV is clearly lower than the predicted market value of the vehicle, the economically rational choice will be for the consumer to exercise Option 2 or Option 3 outlined above. If the GMFV is clearly in excess of the predicted market value, then the economically rational choice for the consumer may be to proceed with Option 1.

If a taxpayer is in doubt as the applicable VAT treatment of a supply they are making they should contact their local Revenue Branch.