



[2014] UKUT 0200 (TCC)

Appeal number: FTC/13/2013

*VAT – SUPPLY – whether a particular type of motor vehicle finance agreement, called “Agility”, was a supply of goods or services*

**UPPER TRIBUNAL (TAX AND CHANCERY CHAMBER)**

**MERCEDES-BENZ FINANCIAL SERVICES UK LIMITED**                      **Appellant**

- and -

**THE COMMISSIONERS FOR HER MAJESTY’S  
REVENUE AND CUSTOMS**    **Respondents**

**TRIBUNAL: MR JUSTICE NUGEE**

**Sitting in public at the Rolls Building, London EC4A 1NL on 17-18 March 2014**

**Kevin Prosser QC instructed by Mishcon de Reya for the Appellant**

**Owain Thomas & Matthew Donmall instructed by the General Counsel and Solicitor to  
HM Revenue and Customs, for the Respondents**

## DECISION

**Mr Justice Nugee:**

### *Introduction*

1. This is an appeal to the Upper Tribunal by Mercedes-Benz Financial Services UK Ltd (“**MBFS**”) from a decision (“**the Decision**”) of the First-tier Tribunal (Judge Michael Tildesley and Ms Ruth Watts Davies) (“**the FTT**”), first released to the parties on 22 September 2012 and released in a final version incorporating corrections on 17 December 2012. It is brought with the permission of the FTT (Judge Tildesley) granted on 10 December 2012.
2. The issue between the parties concerns the classification for VAT purposes of a particular type of motor vehicle finance agreement, called “Agility”, which MBFS has entered into with its customers since 1 August 2007 and which may lead to the customer acquiring the vehicle. MBFS contends that the agreement constitutes a supply of services. Her Majesty’s Commissioners for Revenue and Customs (“**HMRC**”) contends that it constitutes a supply of goods, and issued assessments to VAT on that basis. The FTT dismissed MBFS’s appeals against the assessments.
3. MBFS now appeals, effectively on three grounds, namely (i) that the FTT made an error of law in its interpretation of the relevant legislation, namely Article 14(2)(b) of the Principal VAT Directive (Council Directive 2006/112/EC) (“**the Directive**”); (ii) that the FTT made findings of fact that had not been contended for by HMRC and in so doing acted in a procedurally unfair way; and (iii) that in any event those findings were misconceived. I will refer to these as “**the Interpretation Issue**”, “**the Procedural Issue**” and “**the Factual Issue**” respectively.

### *Facts*

4. I propose first to give a brief account of the facts which were either agreed, or apparent from the terms of sample agreements in evidence before the FTT, or otherwise not disputed, without at this stage dealing with those factual findings of the FTT that are criticised in MBFS’s appeal. I do not propose to set out the entirety of the Statement of Agreed Facts which were agreed by the parties for the FTT hearing: they can be found set out in the Decision at [30]-[44].
5. MBFS is a subsidiary of Daimler AG. It offers financial products to its customers. Since 1 August 2007 when Agility was launched, the three options given to the customer are “Hire Purchase” (“**HP**”), “Agility” and “Leasing” contracts. Under each of them, the customer obtains the use of a Mercedes Benz vehicle and makes monthly payments to MBFS for a specified period; under HP and Agility the customer also has the option at the end of the period to acquire the vehicle. If a customer has decided at the outset that they would like to purchase the vehicle, an HP product may be recommended; if they have

decided they do not wish to, a Leasing product will be recommended; if they are undecided or would like to keep their options open, the Agility product will be recommended.

- 5 6. Sample agreements of each of the three types were put before the FTT. The simplest is the Leasing agreement. This is described as a “Hire Agreement regulated by the Consumer Credit Act 1974”. The particular example in evidence was for the hire of a new Mercedes-Benz LCV Sprinter 3 (a type of van) for a period of 36 months, with equal monthly rental payments due of £435.42 a month. The agreement contains no option to purchase the vehicle, 10 and at the end of the 36 months the customer is obliged to return it to MBFS. If the vehicle has travelled more than a specified allowed distance, the customer will become liable for an excess distance charge. The customer is also obliged to keep the vehicle properly maintained in accordance with the manufacturer’s recommendations and the agreement contains a detailed statement of “vehicle return standards” specifying the condition that the 15 vehicle should be in when returned. It is common ground that this agreement does not constitute a supply of goods for VAT purposes, but is a supply of services.
- 20 7. The HP Agreement takes the form of an agreement for hire with an option to purchase at the end of the hire period, exercisable for a small fee called an “Option to purchase fee”, typically of £95. Some HP agreements provide for equal monthly payments: one of the sample agreements in evidence (described as a “Hire Purchase Agreement regulated by the Consumer Credit Act 1974”) was for the hire-purchase of a Mercedes-Benz C-Class car where the amount 25 of credit was £23,555 and the payments due were 36 equal monthly instalments of £791.00. Other HP agreements provide for lower monthly payments for the first 35 months with a substantial “balloon” payment due as the final monthly payment: the example in evidence (also described as a “Hire Purchase Agreement regulated by the Consumer Credit Act 1974”) was for the 30 hire of a Mercedes Benz LCV Vito van with a total cash price of £18,517.45 of which £2,415.32 (13%) was to be paid by way of deposit, leaving just over £16,000 to be financed. This was payable by 36 monthly payments of £328.31 (totalling £11,815.56, made up of £7,957.13 capital (43%) and £3,858.43 interest), together with a balloon payment of £8,145 (44%) payable with the 35 final instalment. Although not directly comparable with the first example (as the capital financed is much lower), it can be seen that the effect of the balloon payment is to reduce the monthly payments significantly. Being agreements regulated under the Consumer Credit Act 1974 (“CCA”), the agreements specify certain financial information on their face including the amount of 40 credit, the APR, the total payable, the total cash price of the vehicle and the total charge for credit.
- 45 8. The HP agreement is drafted on the basis that the customer is obliged to make all the monthly payments, including the balloon payment if there is one. It does not oblige the customer to pay the £95 Option to purchase fee, but if the customer has made all the contractual payments, he would by the end of the

contract period have paid the entire cash price of the vehicle so it would make commercial sense for him to pay the £95 to acquire the vehicle.

9. However if the agreement is a regulated agreement (as the example agreements in evidence were), then the CCA gives the customer certain statutory rights. One of these is the right to terminate the agreement. If this right is exercised, the maximum that MBFS can claim is half the total amount that would be due under the agreement, so if this has already been paid, no more is payable: see ss. 99 and 100 of the Act. The HP Agreement contains a notice of these rights as follows:

10 **TERMINATION: YOUR RIGHTS**

You have a right to end this agreement. To do so, you should write to the person you make your payments to. We will then be entitled to the return of the goods and to half the total amount payable under this agreement, that is £..... If you have already paid at least this amount plus any overdue instalments and have taken reasonable care of the goods, you will not have to pay any more.

10. The HP Agreement obliged the customer to keep the vehicle properly maintained in accordance with the manufacturer's recommendations, and if the agreement was determined (either by the customer, or by MBFS on the customer's default) then the customer could be liable to compensate MBFS if the vehicle was not returned in good condition, repair and working order; but there was no annexed statement of vehicle return standards as there was with the Leasing agreement. Nor was there any allowed distance specified, or obligation to pay an excess distance charge if it were exceeded.

11. It is common ground between the parties that an HP agreement, whether of the equal instalment type or of the balloon type, is a supply of goods for VAT purposes, although they do not agree on the reason why this is so.

12. The Agility agreements in evidence have some similarities to both the Leasing agreement and the HP agreements. Like the HP agreements, they are described as a "Hire Purchase Agreement regulated by the Consumer Credit Act 1974", and contain a period of hire of 36 months with an option to purchase thereafter; and, being regulated agreements, they contain a notice of the customer's rights including the right to early termination, and a statement of financial information including the amount of credit, the APR, the total amount payable, the total cash price of the vehicle and the total charge for credit. Like the Leasing agreement, the Agility agreements contain a specified allowed distance and require the customer to pay an excess distance charge if the vehicle is returned having travelled more than the allowed distance; and a detailed list of vehicle return standards against which the condition of a vehicle would be measured if returned.

13. The structure of the payments under an Agility agreement is as follows.

5 Unlike the HP agreement, the payment due on exercising the option to  
purchase (called the “Optional Purchase Payment”) is a substantial payment.  
It is calculated to be equal to the anticipated market value of the vehicle at  
contract maturity (taking into account the anticipated mileage), or “residual  
10 value”. Since there is a considerable demand for second-hand Mercedes-Benz  
vehicles, the residual value is a substantial proportion of its initial value: the  
first example in evidence is of an LCV Sprinter with a cash price of  
£22,325.00, a deposit of £3,325 (15%) and an Optional Purchase Payment of  
£9,500 (42.5%). The monthly payments are then set to pay off the difference  
15 between the cash price (less deposit) and the residual value, together with  
interest. In this example this leads to 36 monthly payments of £373.35  
(totalling £13,440.60 of which £3,940.60 is interest and £9,500 the balance of  
capital). The corresponding figures for the second example (a C-Class car) are  
cash price of £23,555, deposit of nil, Optional Purchase Payment of  
£11,450.00 (48.6%), and 36 monthly payments of £516.20 totalling  
£18,583.20 (of which £6,478.20 is interest and £12,105 the balance of capital  
(51.4%)). If the option to purchase is exercised, a fee of £95, called the  
Purchase activation fee, is payable as well as the Optional Purchase Payment.

14. 20 If an Agility customer does not exercise the option to purchase, the vehicle is  
returned to MBFS. MBFS has a guaranteed buyback agreement with a sister  
company which owns the used car network in the UK. This means that MBFS  
can dispose of the returned vehicles at retail value and does not take any risk  
on “the metal”. MBFS is therefore neutral as to whether an Agility customer  
25 exercises the option or not. 3 months before the end of the contract, MBFS  
sends the customer a “Maturity Pack” asking them if they wish to return the  
vehicle, purchase the vehicle outright or purchase the vehicle and use it as a  
deposit for a new vehicle. The percentage of Agility customers returning their  
vehicles on maturity rather than purchasing them has fluctuated from about  
25% to about 75%, with an average percentage of 50%.

30 15. HP customers are not sent the same list of options on maturity. The  
“Welcome Pack” which they are given at the outset of the contract tells them  
that the “Option to Purchase” fee will be debited from their account in the last  
month, and that “once you’ve made all your payments, your Mercedes-Benz is  
yours to keep”; the option fee is taken by direct debit.

35 16. The FTT found as a fact that there was a similar high rate of return under HP  
agreements as under Agility agreements relying on what Mr May, who was  
the former Chief Financial Officer of MBFS and who gave oral evidence  
before the FTT, had said. In its Grounds of Appeal MBFS asserted that this  
was incorrect and based on a misunderstanding of Mr May’s evidence; but  
40 there is no note of the oral evidence and Mr Prosser QC, who appeared for  
MBFS, accepted that there was no material before me on which I could reject  
this finding of the FTT.

*The Interpretation Issue*

17. VAT is charged in the UK under the Value Added Tax Act 1994 (“VATA”). s. 4(1) of VATA imposes a charge to VAT on any supply of goods or services made in the UK where it is a taxable supply made by a taxable person in the course or furtherance of any business carried on by him. s. 5(1) provides that schedule 4 applies to determine what is, or is to be treated as, a supply of goods or a supply of services. Sch 4 para 1 provides as follows:
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- “(1) Any transfer of the whole property in goods is a supply of goods; but, subject to sub-paragraph (2) below, the transfer –
- 10 (a) of any undivided share of the property, or
- (b) of the possession of goods,
- is a supply of services.
- (2) If the possession of goods is transferred-
- (a) under an agreement for the sale of the goods, or
- 15 (b) under agreements which expressly contemplate that the property also will pass at some time in the future (determined by, or ascertainable from, the agreements but in any case not later than when the goods are fully paid for),
- 20 it is then in either case a supply of the goods.”
18. The Agility agreement as a matter of English law is not a transfer of the whole property in goods, but is a transfer of possession of goods. It is not an agreement for sale of the goods as there may never be a sale, this being a matter at the option of the purchaser. So the question under VATA is whether the agreement expressly contemplates that the property will pass at some time in the future.
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19. In fact however the question has not been argued either before the FTT or before me by reference to the text of VATA. VATA is intended to implement the Directive, and therefore has to be construed in conformity with it. This means that the argument has in fact taken place solely by reference to the relevant provision of the Directive, which is Article 14. Art 14(1) and 14(2) provide as follows:
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- “1. 'Supply of goods' shall mean the transfer of the right to dispose of tangible property as owner.
- 35 2. In addition to the transaction referred to in paragraph 1, each of the following shall be regarded as a supply of goods:

- (a) the transfer, by order made by or in the name of a public authority or in pursuance of the law, of the ownership of property against payment of compensation;
- 5 (b) the actual handing over of goods pursuant to a contract for the hire of goods for a certain period, or for the sale of goods on deferred terms, which provides that in the normal course of events ownership is to pass at the latest upon payment of the final instalment;
- 10 (c) the transfer of goods pursuant to a contract under which commission is payable on purchase or sale.”

The relevant question therefore is whether the Agility contract falls within Art 14(2)(b). It is a contract for the hire of goods for a certain period under which there is an actual handing over of the goods, so this resolves itself into the question whether the Agility contract is a contract which provides that in the normal course of events ownership is to pass at the latest upon payment of the final instalment.

20. I was also referred by Mr Thomas, who appeared for HMRC, to the French text of Art 14(2)(b), which reads as follows:

20 “b) la remise matérielle d'un bien en vertu d'un contrat qui prévoit la location d'un bien pendant une certaine période ou la vente à tempérament d'un bien, assorties de la clause que la propriété est normalement acquise au plus tard lors du paiement de la dernière échéance;”

25 It can be seen that the French text has “normalement” (or “normally”) where the English has “in the normal course of events”. Each version of the text is equally authoritative; neither counsel referred to any other language version of the Directive, from which I assume that none of the other versions of the text sheds any further light on the question of interpretation.

30 21. Before the FTT Mr Thomas argued firstly that “in the normal course of events” qualified *when* the ownership was to pass under the contract, a contention that was rejected by the FTT (see the Decision at [89]) and which HMRC has not sought to appeal, and Mr Thomas did not seek to re-argue. But the FTT accepted his second argument which is that a contract falls within Art 14(2)(b) if the terms of the contract are such that the passing of title is a normal event rather than an event which may only arise in limited and exceptional circumstances: see the Decision at [91]-[96]. In other words, “normal” is being used in contradistinction to “abnormal”.

40 22. Mr Prosser contends that this is wrong and that the FTT erred in law. His submission in summary is that Art 14(2)(b) applies to contracts where the terms of the contract are such that ownership will normally pass. Before the FTT he adopted a test for what was ‘normal’ of something that was more

likely than not; in his written submissions before me he preferred a test of something that was expected to happen, although this was modified in the course of his oral argument.

23. The parties are agreed that there is no decision of the Court of Justice (“**ECJ**”) on the interpretation of Art 14(2)(b). There is one decision, *Eon Aset Menidjmont OOD v Direktor na Direktsia ‘Obzhalvane i upravlenie na izpalnenieto’ – Varna pri tsentralno upravlenie na Natsionalnata agentsia za prihodite* Case C-118/11 (“**Eon Aset**”) in which the ECJ referred to Art 14(2)(b), and both counsel, as appears below, referred me to what the ECJ said, but it is agreed that it is not directly in point.
24. The general principles laid down by the ECJ for the interpretation of European legislation such as the Directive were not in dispute. Mr Thomas summarised them as being that the interpretation must be determined by reference to the terms in question, the context in which they are found, the purpose of the provisions, and the system of the relevant legislation as a whole, this being what is sometimes termed the ‘teleological’ approach to interpretation. Mr Prosser did not dissent from this statement of the principles.
25. Although there is no decision of the ECJ on Art 14(2)(b) I was referred to a number of decisions on the Directive (and its predecessor, Council Directive 77/388/EEC, known as the Sixth Directive) for general statements of principle. I derive the following from these decisions and the other material to which I was referred:
- (1) As recital (1) to the Directive shows, the Directive is intended to harmonise the laws of the Member States relating to turnover taxes and provide for a “uniform basis of assessment”.
  - (2) It is therefore not surprising that the ECJ has said that the notion of supply of goods is not to be determined by national law: the purpose of the Directive might be jeopardised if the requirements for a supply of goods were to differ according to the civil law of the Member State concerned: see *Atkiebolaget NN v Skatteverket* Case C-111/05 at [32].
  - (3) The concept of supply of goods is objective in nature. It applies without regard to the purpose or results of the transactions concerned and without its being necessary for the tax authorities to carry out inquiries to determine the subjective intention of the taxable person in question: see *Newey v Revenue and Customs Commissioners* Case C-653/11 (“**Newey**”) at [41]; *Dixons Retail plc v Revenue and Customs Commissioners* Case C-494/12 (“**Dixons**”) at [21].
  - (4) Consideration of the economic and commercial realities is a “fundamental criterion” for the application of the common system of VAT. Since the contractual position normally reflects the economic and commercial reality of a transaction, the relevant contractual terms

constitute a factor to be taken into consideration; but sometimes contractual terms do not wholly reflect the economic and commercial reality of a transaction, in particular if it becomes apparent that the contractual terms constitute a purely artificial arrangement which does not correspond with the economic and commercial reality of the transaction: *Newey* at [42]-[45]. This passage has very recently been referred to and relied on by the Supreme Court in *Secret Hotels2 Ltd v Revenue and Customs Commissioners* [2014] UKSC 16 at [29] per Lord Neuberger.

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(5) In a passage cited by Jonathan Parker LJ in *Tesco plc v Customs and Excise Commissioners* [2003] EWCA Civ 1367 (“*Tesco*”) at [41], the Advocate General (Tizzano) said this in his opinion in *Customs and Excise Commissioners v Mirror Group plc* Case C-409/98 and *Customs and Excise Commissioners v Cantor Fitzgerald International* Case C-108/99:

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“27. In order to identify the key features of a contract, however, we must go beyond an abstract or purely formal analysis. It is necessary to find the contract's economic purpose, that is to say, the precise way in which performance satisfies the interests of the parties. In other words, we must identify the element which the legal traditions of various European countries term the cause of the contract and understand as the economic purpose, calculated to realise the parties' respective interests, lying at the heart of the contract. In the case of a lease, as noted above, this consists in the transfer by one party to another of an exclusive right to enjoy immovable property for an agreed period.

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28. It goes without saying that this purpose is the same for all the parties to the contract and thus determines its content. On the other hand, it has no connection with the subjective reasons which have led each of the parties to enter into the contract, and which obviously are not evident from its terms. I have drawn attention to this point because, in my view, failure to distinguish between the cause of a contract and the motivation of the parties has been the source of misunderstandings, even in the cases under consideration here, and has complicated the task of categorising the contracts at issue.”

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Jonathan Parker LJ later in his judgment made the point that the “economic purpose” here referred to by the Advocate General is not the same as “economic effect”: two transactions may have the same economic effect but that does not necessarily mean that they are to be treated in the same way for VAT purposes: see *Tesco* at [159].

5 (6) In *MBNA Europe Bank Ltd v HMRC* [2006] EWHC 2326 (Ch) (“*MBNA*”), Briggs J referred to the same passage from Advocate General Tizzano’s opinion in saying (at [35]) that the Court is not hidebound by the labels which the parties have chosen to apply to their transactions but must where necessary ascertain the “essential character of the transaction in issue”. He continued (at [36]):

10 “The identification of the “cause” of a contractual transaction, where necessary to establish whether it constitutes a supply, and if so to categorise it as taxable, exempt or specified, may legitimately entail its interpretation by reference to the relevant matrix of background facts known to the parties of the type classically explained by Lord Hoffmann in *West Bromwich* [2005] UKHL 44.”

15 26. These being the applicable principles, the first question is as to the terms of Art 14(2)(b). Mr Thomas pointed out that the focus of the language is on the provisions of the contract: the English text refers to “a contract ... which provides that...” and the French text is, if anything, even clearer, referring to “la clause que ...”. One must therefore necessarily look to the terms of the contract to see what they provide: the wording is concerned with the provisions of the contract, not with what is likely to happen or expected to happen.

25 27. The next step in his carefully formulated argument is that contractual provisions do not usually say anything about the likelihood of certain things happening. They contain obligations, and provisions as to what is to happen in certain circumstances. They do not contain predictions as to performance. One only has to envisage a contractual provision to the effect that “the customer will probably exercise the option to acquire the vehicle” to see that it would be absurd.

30 28. It follows, he says, that Art 14(2)(b) cannot be referring to a contract which contains a provision or clause that says in terms that title will “normally” pass or pass “in the normal course of events”, as this is not what contracts do.

35 29. The next point is that Art 14(2)(b) contains two limbs, one being the sale of goods on deferred terms, and the other being the hire of goods for a certain period. It is implicit that these are two different types of contract, and it follows that a contract for the hire of goods can be within Art 14(2)(b) without being a contract under which the customer is committed to acquiring the goods. If it was confined to contracts under which the customer was bound to purchase the goods, they would all be sales of goods on deferred terms. So a contract for hire which makes provision for the purchase of the goods, but caters for the possibility that property may not pass, can still be within Art 14(2)(b).

40 30. So far Mr Prosser I think agrees with him, and so do I. I accept that Art

14(2)(b) is concerned with the terms of the contract, that the terms of the contract are unlikely to say anything directly about the likelihood of an option being exercised, and that Art 14(2)(b) must extend to at least some contracts for hire which provide for the hirer to acquire title but do not commit the hirer to this.

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31. The conclusion Mr Thomas seeks to draw is that a contract for hire falls within Art 14(2)(b) as long as the acquisition of title is a normal method of contractual performance rather than an abnormal or exceptional outcome; or as he put it, the option for the passing of title is a central or essential feature of the contract, not a tangential one.

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32. The difficulty with this interpretation however is that it does not sit easily with the language of the Article (either in English or French). It is tantamount to saying that any contract for hire which contains an option for the hirer to acquire the goods (save one exercisable only in narrow and exceptional circumstances) is within the Article, as it is not easy to see how any contract containing such an option could be characterised other than as one where the acquisition of the goods was a normal outcome of the contract. But this is not what the Article says: it does not refer to contracts for the hire of goods which contain provisions or a clause under which the ownership *may* pass; what it refers to are contracts which provide that ownership “*is to*” pass “in the normal course of events” or which contain a clause that the ownership “*est normalement acquise*”. This language is not on its face apt to extend to all contracts which make provision for the possibility of title passing, or which contemplate it as *a* normal outcome of the contract, but only one where this is *the* normal outcome. Indeed Mr Thomas accepted in argument that the phrase “in the normal course of events” was not the best choice of phrase to capture what he said the Article was intended to do.

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33. My conclusion on the language of Art 14(2)(b) is that it is not at all evident that Mr Thomas’s interpretation reflects the language of the Article or expresses what the provision appears to be aimed at.

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34. The next step is to consider the purpose of the provision in its context, understood against the system of the legislation as a whole. Mr Thomas points out that Art 14(2)(b) is a deeming provision. As such its purpose is to extend the concept of supply of goods to other contracts, namely those which comply with that description. This is all very well as far it goes but does not seem to me to provide any form of explanation as to why such contracts should be treated as if they constituted a supply of goods.

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35. Mr Thomas pointed out that the practical effect of a supply being a supply of goods rather than a supply of services was primarily to affect the way in which VAT was accounted for. Under Art 2(1)(a) and (c) of the Directive both a supply of goods and a supply of services are subject to VAT, and under Art 63 VAT is chargeable when the goods or services are supplied. However Art 64(1) provides:

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5                   “Where it gives rise to successive statements of account or successive payments, the supply of goods, other than that consisting in the hire of goods for a certain period or the sale of goods on deferred terms, as referred to in point (b) of Article 14(2), or the supply of services shall be regarded as being completed on expiry of the periods to which such statements of account or payments relate.”

10                   Art 73 provides that the taxable amount includes everything which constitutes consideration “obtained or to be obtained” by the supplier in return for the supply. Art 90 however provides that in the case of cancellation, or partial non-payment or where the price is reduced after the supply takes place, the taxable amount is reduced accordingly.

15                   36.       The practical effect of these provisions is that if the Agility contract is not within Art 14(2)(b), MBFS will have to account for VAT on the consideration payable each month. (MBFS’s position is that this is not in fact the whole of the monthly hire payments as part of the payment is a charge for credit which is exempt, but Mr Thomas reserved HMRC’s position on this particular point, and it was not argued, so I express no view on it). If therefore the customer does not exercise the option to purchase, MBFS only pays VAT on the monthly payments, and then only as and when they fall due. If however the Agility contract is within Art 14(2)(b) MBFS pays VAT on the entire consideration, including the amount potentially payable on exercise of the option to purchase, up front. In the latter case however if the customer does not in the event exercise the option and complete the purchase there is an adjustment for the amount of the payments not made. Mr Thomas relied on this as showing that there was no great difference between whether the supply was one of goods or services; this merely entailed a difference in accounting treatment. In these circumstances he said that he resisted being drawn into a debate about the policy underlying Art 14(2)(b); his case was not that there was any particular underlying purpose in treating contracts within Art 14(2)(b) as a supply of goods – it was just the fact that the legislation did it.

20                   37.       I understand the point that in the end the same amount of VAT is likely to be payable whether a contract falls within Art 14(2)(b) or not. But I do not think this is a complete answer to the question of the underlying policy. There are practical consequences that flow from whether Art 14(2)(b) applies or not, and this must have been obvious to those responsible for drawing up the legislation, not least because Art 64(1) expressly cross-refers to Art 14(2)(b). The most obvious consequence is a cashflow one, which indeed is why MBFS is pursuing this appeal. The assessments under appeal (by which HMRC issued assessments for the difference between the VAT MBFS actually accounted for and the VAT that would be due if the Agility contracts are within Art 14(2)(b)) total some £10m, but that is only for the period from the introduction of the Agility contract in August 2007 to the end of August 2008, and I was told that the VAT in issue is now estimated at some £160m. The cashflow advantage to MBFS in not having to pay this upfront at the outset of the contract (and then receive an adjustment up to 3 years later, with no

provision for interest), as opposed to paying only if and when the money from the customers falls due, is self-evidently likely to be very substantial.

5 38. In principle there may be other consequences as well, for example in identifying the place of supply. This is dealt with in some detail in Title V (Arts 31 to 61) of the Directive, the general rule in the case of a supply of goods being that the place of supply is the place where the goods are when they are supplied (Art 31), but the general rule in the case of a supply of services being that the place of supply is the place where the supplier has established his business (Art 43). It is not suggested that this is of any practical significance in the present case, where MBFS both operates from, and supplies vehicles in, the UK, but one can well see that in other cases it might be a live issue. Since the place of supply determines which Member State collects the VAT (and hence the rate payable and any other provisions of national law which apply), this could be a matter of considerable practical importance.

20 39. In these circumstances I think it is a legitimate question to ask why the Directive makes special provision in Art 14(2)(b) for certain contracts, which on any view do not necessarily lead to a transfer of ownership, nonetheless to be treated as a supply of goods. Mr Thomas as I said did not wish to put forward any particular policy reason why this should be so.

25 40. Mr Prosser however did. His submission was that the purpose of Art 14(2)(b) was to bring within the net of a supply of goods a contract where the economic reality was that the customer had agreed to buy the goods, even though legally he was not committed to doing so. The paradigm example of that was a hire purchase agreement such as MBFS's HP agreement. If one considers first an HP agreement with equal monthly instalments, the customer agrees to pay 36 instalments and by the time he has paid them, he has paid the entire price of the vehicle (as well as interest on the reducing capital balance). Thus although he has an option to purchase the goods or not at the end of the hire period, the option price is minimal (£95) and is merely an administration fee: the customer has by that stage paid for the goods and can be expected to purchase them. Mr Prosser referred to the description of hire purchase in textbooks: see eg *Bradgate, Commercial Law* (3<sup>rd</sup> edn) at 237f where it is said:

35 "The truth is that the objective of hire purchase is the supply of goods on credit terms, coupled with security for the supplier"

and *Benjamin, Sale of Goods* (8<sup>th</sup> edn, 2010) at §1-053:

40 "In practice, hire purchase is a device used in order to give possession and the use of goods to an intending buyer over a period during which the price is paid, with interest, by instalments, while the seller retains the title to the goods as security for the unpaid balance of the price."

He also referred to HMRC's own publication VATSC72800 where in discussing the question whether a contract falls within sch 4 para 1(2)(b) VATA and Art 14(2)(b), the question is expressed as follows:

5                   “Are the customers in reality buying the goods – that is will ownership pass in the normal course of events ?”

41. Mr Prosser accepted that a similar analysis also applied to the HP agreement with a balloon payment. Here too the customer was contractually committed to paying the full price for the goods, leaving only a minimal option fee of £95 to be paid on exercise of the option.
- 10 42. I accept Mr Prosser's submission on the policy behind Art 14(2)(b). In my judgment the discernible policy purpose behind the inclusion of certain contracts of hire in Art 14(2)(b) is to tax transactions where the customer has in reality agreed to buy the goods as if they were contracts of sale, even though in law the customer is not contractually obliged to complete the purchase. This explains why the language of Art 14(2)(b) refers to the ownership of goods passing in the normal course of events, or normally – it is not concerned with every contract under which there is a possibility of the ownership passing, but only with those contracts where this can be described as the normal outcome.
- 15
- 20 43. It follows that neither a consideration of the terms of Art 14(2)(b), nor a consideration of the context in which they are found, the purpose of the provisions, and the system of the relevant legislation as a whole, supports the interpretation put forward by Mr Thomas on behalf of HMRC. This would bring within the net of Art 14(2)(b) contracts where there was no reason to think that ownership would normally pass, or would pass in the normal course of events, and no reason to regard the contract as one where in reality the customer had agreed to buy the goods, simply on the basis that this was a possibility and not an abnormal or exceptional one.
- 25
- 30 44. But if this is right, it still leaves the problem how one is to ascertain that a contract is one under which the ownership will normally pass. It is common ground, and obviously right, that this cannot be tested in hindsight by reference to whether any particular customer in fact purchases the vehicle, as the classification has to be carried out at the time the contract is entered into. Nor (as Mr Prosser accepts) can it turn on the subjective intentions of the customer at the time of entry into the contract in any particular case. This is also plainly right, given the principle as stated in *Newey and Dixons* that the concept of supply of goods is objective in nature and the tax authorities cannot be required to carry out inquiries to determine the subjective intention of the taxable person; they equally cannot be required to inquire as to the subjective intentions of the customer. It would also presumably mean that some Agility contracts were supplies of goods and other supplies of services and this seems unlikely to be what the Directive intended.
- 35
- 40

45. Mr Prosser also disclaimed any reliance on the evidence as to the actual rates of return of the vehicles by the customers. Again this must be right. When the very first Agility contract was entered into, it was either a supply of goods or a supply of services and in principle it should have been possible to classify it as one or the other then; there would then however be no evidence as to the rates of return under such contracts. In any event the rates of return fluctuate over time, depending on the state of the second hand market and other factors; but it cannot sensibly be supposed that contracts in precisely the same form should fluctuate between being supplies of goods or services depending on the state of the market.
46. So it is common ground that the question whether a contract falls within Art 14(2)(b) has in principle to be determined at the date of entry into the contract and by reference to the provisions of the contract. Since the provisions of the contract are unlikely to say what “normally” happens, that leads back to the conundrum identified by Mr Thomas of what is meant by a contractual provision that ownership is to pass in the normal course of events.
47. Mr Prosser, as already indicated, submitted to the FTT that this meant a contractual provision which had the effect that it was “more likely than not” that ownership would pass, a submission that was rejected by the FTT as focusing on the performance of the contract rather than what the contractual terms said. I agree that this is not a satisfactory test, as it might leave it quite uncertain whether a particular contract was one where it was likely or not. As Mr Thomas said, contracts are not about what is likely or not likely, but about parties’ mutual promises and rights. Before me, Mr Prosser preferred the formulation that it meant a contractual provision under which it was “expected” that ownership would pass. This too has its problems: it has the flavour of a subjective test, which is inappropriate, and raises the questions whose expectations are relevant, and how they are to be established.
48. What I have found most helpful is the guidance given by Advocate General Tizzano cited and followed in *Tesco*. This requires one to find the contract’s “economic purpose”, that is to say, “the precise way in which performance satisfies the interests of the parties”; or the element (termed in some legal systems the cause of the contract) which is the “economic purpose, calculated to realise the parties’ respective interests, lying at the heart of the contract.” It seems to me to follow that the question under Art 14(2)(b) is whether the contract is one whose economic purpose is for the customer to acquire ownership of the goods. This is to be identified by looking at the interests which performance of the contract satisfies; or, as I suggested in argument (a suggestion adopted by Mr Prosser) by looking at what the contract is designed to achieve: compare the formulation in sch 4 para 1(2)(b) of VATA which refers to “agreements which ... contemplate that the property ... will pass” (although this has its own difficulties: see below).
49. In the case of the equal instalment HP agreement, it is easy to see that this test is satisfied. Although there is no legal obligation on the customer to exercise

the option to purchase, performance of the contract will in fact lead to the customer paying MBFS the entire purchase price of the vehicle together with interest over 3 years, at the end of which he is able to acquire the ownership of the vehicle for a minimal fee. One does not need to examine the marketing material, or the subjective intentions of the parties, to see that the interests which performance of the contract satisfies are (i) the customer's interest in being able to finance the acquisition of a vehicle by having 3 years to pay the purchase price by instalments, with interest on the reducing balance, and then being in a position to acquire the vehicle at no extra cost (beyond a minimal fee) and (ii) MBFS's interests in receiving the purchase price, together with interest, and having security for payment in the shape of retention of ownership until the price has all been paid. Put another way, the contract is designed to achieve sale of the vehicle to the customer with the customer being given time to pay and MBFS being given security; the structure of the contract is such that it can be said that it contemplates that property will pass. Such a contract would appear to be the paradigm example of a contract within Art 14(2)(b): indeed, as Mr Thomas said, if HP contracts are not within the first limb of Art 14(2)(b) it is very difficult to see what sort of contract might be.

50. Equally in the case of the balloon type of HP agreement. As I have said it was not disputed by Mr Prosser that such a contract would fall within Art 14(2)(b), and I agree. Here too performance of the contract will lead to the customer paying the entire price of the vehicle by the end of the 3 year period, and it seems to me that the interests of the parties which performance of the contract will satisfy are the same.

51. This is so even though (assuming the agreement is a regulated one) the customer has a right to terminate the contract early; and even though as a matter of fact a significant number of customers exercise this right. This is not because, as Mr Prosser at one stage submitted, the right to terminate is a right under statute rather than under the contract. I do not think this makes any significant difference: the agreement itself refers prominently to the right to terminate, and as Mr Thomas said even if the rights are statutory they form part of the terms on which the transaction takes place. It cannot matter whether the statute is regarded as directly modifying the terms of a contract, or as giving a statutory right outside the contract: the effect is the same, which is that a customer under a regulated agreement has a right to terminate it early on payment of the specified amount.

52. Rather in my judgment the reason why early termination rights do not prevent the contract being one within Art 14(2)(b) is because the exercise of a right to terminate the contract early is not a performance of the contract, but a means of avoiding performance. In other words when asking the question what are the interests of the parties that performance of the contract satisfies, one assumes that the contract will be performed, not brought to an early end, even if early termination is lawful rather than a breach of contract. I derive this simply from the way in which Advocate General Tizzano describes the task of

finding the contract's economic purpose; but it is also reinforced by the wording of Art 14(2)(b). If one is asking what a contract provides for "in the normal course of events" this in my judgment requires assuming that the contract will be performed, not prematurely terminated.

5 53. It may be noted that this conclusion is entirely in line with the decision of the  
VAT Tribunal in *General Motors Acceptance Corporation (UK) plc v*  
*Customs and Excise Commissioners* (2002) VT 17990 ("**GMAC**"), which  
concerned hire purchase contracts for Vauxhall cars. Although there was no  
dispute about this, the Tribunal proceeded on the basis that the contracts in  
10 question constituted a supply of goods, despite the fact that some at least were  
of the balloon type, and that customers were more frequently choosing not to  
exercise the option or to exercise their rights to early termination under the  
CCA: see at [4]–[5]. An appeal to the High Court proceeded on the same  
basis: see [2004] EWHC 192 (Ch) at [2] per Field J.

15 54. It is also consistent with the result in *Hogarth t/a Hogarth Associates v*  
*Commissioners for Customs & Excise* (1994) VT 13259 ("**Hogarth**") another  
decision of the VAT Tribunal which concerned a hire purchase agreement of  
the balloon type, with an option to purchase for £10. This agreement was later  
modified by a second agreement. In the event the appellant exercised the  
20 option to purchase under the second agreement; he argued that as the option  
under the first agreement was never exercised, that agreement was merely one  
of hire. The Tribunal (Mr Simpson) rejected this, and said:

25 "What usually happens under a hire-purchase transaction is that the  
customer makes the payments and eventually becomes the owner of  
the goods, in both cases in accordance with the hire-purchase  
agreement. In my judgment that course of events is one which is  
referred to in Article 5.4 as the 'normal course of events', and such  
an agreement is an example of an agreement which 'expressly  
contemplates' that the property 'will' pass as mentioned in paragraph  
30 1(2)(b). In my judgment the fact that the agreement also  
contemplates other possible events in which the property will not  
pass, such as the premature termination of the agreement, does not  
prevent the agreement from being an agreement which contemplates  
the property will pass; I construe 'will' in this context as meaning,  
35 not 'will inevitably', but 'will in certain events'."

(The reference to Article 5.4 is to Art 5.4 of the Sixth Directive which was in  
similar terms to Art 14(2)(b) of the Directive). Mr Thomas suggested that his  
interpretation was supported by the final words in this passage, suggesting as  
it does that it is enough that the contract provides that ownership will pass in  
40 some circumstances (as long as they are normal and not abnormal  
circumstances). This rather illustrates the difficulties with the wording of the  
UK legislation, now found in VATA. A typical hire purchase agreement does  
not provide that ownership *will* pass: it provides for an option under which the  
ownership *may* pass. So in what sense does such an agreement "contemplate"

that ownership will pass ?

55. The answer I think can only be found in the principle that the domestic legislation must be construed in conformity with the Directive, which takes one back to the idea of ownership passing in the normal course of events; and for the reasons I have given that in my judgment requires one to identify the economic purpose as explained by Advocate General Tizzano. If the economic purpose in this sense is for the customer to acquire ownership of the goods, then this is what the contract expressly contemplates will happen, not just something that might happen in certain events. So although I agree with the result reached in *Hogarth*, I do not entirely agree with the way the reasoning is expressed.
56. The only other authority that I should refer to on this aspect of the case is the ECJ's decision in *Eon Aset*. Eon Aset was a Bulgarian company which had entered into two contracts, one described as a lease and the other as a financial leasing contract, under which it acquired the use of vehicles, which it used to provide its managing director with transport between his home and work. The question at issue was Eon Aset's ability to deduct the VAT payable under the contracts as input tax. This depended on whether the goods or services acquired were being used for the purposes of taxed transactions (see at [31]), and the criterion for determining this varied, depending on whether what was being acquired was a service or capital goods [45]. In this context the ECJ said that the leasing of a motor vehicle does not constitute a supply of goods and so must as a general rule be categorised as a supply of services [33]; but that the lease of a motor vehicle under a financial leasing contract "may, nonetheless, present features which are comparable to those of the acquisition of capital goods" [34], capital goods being goods used for a business activity and distinguishable by their durable nature and value and such that their acquisition costs are not normally treated as current expenditure but are written off over several years [35].
57. The ECJ continued:
- 36 Further, Article 14(2)(b) of the VAT Directive states that the actual handing over of goods pursuant to a contract for the hire of those goods for a certain period, which provides that in the normal course of events ownership is to pass at the latest upon payment of the final instalment is to be regarded as a supply of goods.
- 37 In the case of a financial leasing contract, there is not necessarily any acquisition of the goods since such a contract may provide that the lessee has the option of not acquiring those goods at the end of the lease period.
- 38 However, as is clear from the international accounting standard IAS 17 relating to leases, produced in Commission Regulation

(EC) No 1126/2008 of 3 November 2008 adopting certain international accounting standards in accordance with Regulation (EC) No 1606/2002 of the European Parliament and of the Council (OJ 2008 L 320, p. 1), an operating lease must be distinguished from a finance lease, the nature of the latter being that substantially all the risks and rewards of legal ownership are transferred to the lessee. The fact that a transfer of ownership is provided for on the expiry of the contract or the fact that the present value of the lease payments is practically identical to the market value of the property constitute, separately or together, criteria which permit a determination of whether a contract can be categorised as a finance lease.

39 As the Court has previously stated, the concept of 'supply of goods' does not refer to the transfer of ownership in accordance with the procedures prescribed by the applicable national law but covers any transfer of tangible property by one party which empowers the other party actually to dispose of it as if the recipient were the owner of the property (see Case C-320/88 *Shipping and Forwarding Enterprise Safe* [1990] ECR I-285, paragraph 7, and Case C-185/01 *Auto Lease Holland* [2003] ECR I-1317, paragraph 32).

40 Accordingly, where a financial leasing contract relating to a motor vehicle provides either that ownership of that vehicle is to be transferred to the lessee on the expiry of that contract or that the lessee is to possess all the essential powers attaching to ownership of that vehicle and, in particular, that substantially all the rewards and risks incidental to legal ownership of that vehicle are transferred to the lessee and that the present value of the amount of the lease payments is practically identical to the market value of the property, the transaction must be treated as the acquisition of capital goods.”

58. While acknowledging that this decision is not directly on point, and did not specifically consider the application of Art 14(2)(b) as such, both counsel sought support for their submissions in this passage. Mr Thomas relied on the reference in [38] to “the fact that a transfer of ownership is provided for on the expiry of the contract” as intended to include the case where a contract includes a provision enabling such a transfer of ownership, although he accepted that the formulation in [40] (“where a ... contract ... provides ... that ownership ... is to be transferred ... on the expiry of the contract”) is different. Mr Prosser referred to the characterisation in [38] of a finance lease as one where substantially all the risks and rewards of legal ownership are transferred to the lessee, and submitted that this was not the case with the Agility contract where substantial risks and rewards were left with MBFS.

59. For my part I do not find this passage of great assistance on the present

question. The ECJ was not directly concerned with the question whether the leases in question constituted a supply of goods or services for the purposes of output tax, but with the deductibility of input tax; and although I accept that one would normally expect that what is an acquisition of goods from the viewpoint of the acquirer would also be a supply of goods from the point of view of the supplier, I am not prepared to assume that there is any necessary identity between the two. And although the ECJ referred to Art 14(2)(b), it was not concerned to elucidate the precise scope of that provision, and appears to have referred to it simply as an illustration of the fact that although leasing contracts are in general a supply of services, sometimes they are more akin to an acquisition of capital goods.

60. For what it is worth, however, my view is that the passage read as a whole contains no support for Mr Thomas's submission that a contract which contains a provision under which ownership *may* be transferred is for that reason to be regarded as a supply of goods. Having stated in [36] that a contract where ownership is to pass in the normal course of events is a supply of goods, the ECJ in the remainder of the passage is to my mind indicating that this is not the only criterion for treating (at any rate for the purposes of input tax) a lease as the acquisition of capital goods. This can be done either by showing that ownership is to be transferred on the expiry of the contract; or that the present value of the lease payments is practically identical to the market value of the goods. Either of these suffices to show that substantially all the risks and rewards of ownership are transferred to the lessee. To my mind this tends to support Mr Prosser's submission that a contract under which the present value of the lease payments does not equate to the market value of the goods, and is not one under which ownership is to be transferred (although it contains provisions under which it may be), is not to be regarded as a contract under which substantially all the risks and rewards of ownership pass to the lessee and is not to be treated as a supply of goods. But as I have already said this is not a decision on Art 14(2)(b), and I do not find it of any great assistance.

61. Before me there was some debate as to whether this was an appropriate case to make a reference to the ECJ under what is now Art 267 of the Treaty on the Functioning of the European Union. I am grateful in particular to Mr Thomas (and his junior Mr Donmall) who produced a note which is a model of clarity on the relevant jurisprudence, and which I can summarise as follows. The Upper Tribunal is not the final court of appeal so I have a discretion to refer. In *R v International Stock Exchange ex p Else* [1993] QB 534 at 545 Sir Thomas Bingham MR had said that in a case where a Community law issue is critical, the appropriate course is ordinarily to refer unless the national court can "with compete confidence" resolve the issue itself. But more recent judgments in the Court of Appeal, such as that given by Chadwick LJ in *Customs & Excise Commissioners v Littlewoods Organisation* [2001] EWCA Civ 1542, indicate that this should now be read subject to the observations of Advocate General Jacobs in *Wiener SI GmbH v Hauptzollamt Emmerich* Case C-338/95. These were that "a measure of self-restraint" is required on the part

of national courts if the Court of Justice is not to become overwhelmed; and that experience has shown that the body of case-law developed by the ECJ now provides sufficient guidance for national courts and tribunals to decide many cases for themselves without the need for a reference. In the *Littlewoods* case itself, the Court of Appeal, having referred to there being ample guidance on the question of principle in the existing decisions of the ECJ, said that they felt confident that they could apply the principle to the particular facts of the appeals.

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10 62. In the light of these considerations I have concluded that this is not an appropriate case to make a reference. Although there is no ECJ guidance on Art 14(2)(b) itself, there is a considerable body of guidance on the appropriate approach and I feel able to look to the existing case-law to resolve the question of EU law without the need for a reference.

15 63. For the reasons I have given above, I accept Mr Prosser's submission that the FTT made an error of law in their interpretation of Art 14(2)(b). It is not sufficient for a contract to come within Art 14(2)(b) for it to contain a provision under which the hirer has an option to acquire the ownership of the vehicle at the end of the hire period, and that such acquisition is a normal outcome. In order for a contract to come within Art 14(2)(b) it must be *the* normal outcome of the contract, this being determined in accordance with the guidance given by Advocate General Tizzano by reference to the economic purpose of the contract, that is by looking at the parties' respective interests which performance of the contract satisfies.

#### *The Procedural Issue*

25 64. The second issue raised by Mr Prosser was that the FTT had proceeded in a procedurally unfair way. The essence of the argument is that the FTT described the Agility contract in the Decision as a contract for sale of goods; that this was not an argument that had been advanced by HMRC or anticipated by MBFS; and that it was unfair for the FTT to reach this conclusion without having informed MBFS of its intention to do so and given it an opportunity to address the point.

30 65. The structure of the relevant part of the Decision is as follows:

(1) Having set out the agreed statement of facts, and various other aspects of the evidence, the FTT began their discussion of the issues at [71ff].

35 (2) They said the starting point was to determine "the correct characterisation" of the Agility agreement [73]. They identified a difference between MBFS's position which was that the Tribunal was entitled to take into account "the wider circumstances" so as to ascertain "the commercial function" of Agility, and HMRC's position which was that attention should be directed to what was provided for in the contract, not the wider circumstances [74]; and said they preferred

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HMRC's approach: the wording of Art 14(2)(b) is concerned with the terms of the contract not with the wider circumstances [75]. The Tribunal then said that it should make its findings "in respect of characterisation" on the terms of the Agility agreement itself and not on whether it had striking similarities with the HP agreements [77].

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(3) They then proceeded to make certain findings of fact in relation to the Agility agreement [78], including that it was a hire purchase contract [78(1)]; that it gave the customer an option to purchase [78(3)]; and that if the customer did not purchase s/he was required to return the vehicle and might be liable for excess distance and damage charges [78(5)].

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(4) They then reached their conclusions on the characterisation of the contract at [79]-[82] (see below).

(5) They then went on to consider whether the Agility contract met the requirement of Art 14(2)(b) that in the normal course of events ownership is to pass, the operative words being "in the normal course of events"; and discussed the parties' respective contentions as to what that referred to [83]-[96].

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(6) They then made findings on the wider circumstances in case they were wrong to exclude them from their consideration [97]-[104], including a table of 11 matters which MBFS asked the FTT to make findings of fact on, with their comments [104].

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66. The FTT's conclusions on the characterisation of the Agility contract at [79]-[82] should be quoted in full:

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"79 The Appellant suggested that the purpose of *Agility* as reflected in its terms was the hiring of a Mercedes Benz motor vehicle to a customer who wished to keep his/her options regarding ownership of the motor vehicle open until maturity. The Tribunal disagrees with the Appellant's characterisation of *Agility* agreement. The description of the agreement as a hire purchase, the provision for a deposit payment, the specified financial information including the cash price for the vehicle, the substantial capital payment inherent in the contract structure, and the option to purchase were compelling indicators of *Agility* being a contract of sale of a car. The requirement regarding the maintenance of the vehicle was consistent with a characterisation of a sale contract, in that it preserved the customer's capital investment in the vehicle.

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80 The Appellant contended that *Agility* gave the customer options at the maturity of the agreement. The reality as depicted by the terms and structure of the agreement was very different from that

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5 portrayed by the Appellant. The agreement was silent on the part-exchange option utilising the guaranteed future value of the vehicle. Examination of the terms demonstrated that the return of the vehicle was the default position for the customer who lost his/her capital investment and incurred potential liability for additional charges for excess distance and damage if the vehicle was returned. The Tribunal concludes that on a proper analysis the sole realistic option under the agreement was to purchase the vehicle.

10 81 The term in *Agility* allowing retention of title by the Appellant until exercise of the option to purchase mirrored the legal position under hire purchase. In the Tribunal's view, *Bradgate's* description of hire purchase as a supply of goods on credit terms coupled with security for the supplier neatly summed up the  
15 essence of *Agility*.

82 The Tribunal is, therefore, satisfied that *Agility* was a contract for sale of goods on deferred terms under which the vehicle was handed over to the customer who had the option of purchasing the vehicle upon payment of the final instalment.”

20 67. Reference should also be made to [91] where the FTT referred to their analysis of the *Agility's* terms as having:

“found that the option to purchase constituted the sole realistic option under the contract”

and to [92], which should also be quoted in full:

25 “92 The phrase *normal course of events* is directed at the legal realities of a contract for sale with an option to purchase. The phrase recognises that under the terms of such a contract ownership might not pass but that possibility did not prevent the contract from being a contract for sale under which ownership  
30 normally transferred. Thus the fact that ownership might not transfer under the *Agility* contract did not preclude it from being a contract for sale. The passing of title was central to *Agility* which meant that ownership would normally pass under its terms.”

35 68. It can be seen that the FTT did indeed repeatedly characterise the *Agility* contract as a contract of sale: at [79] (“a contract of sale of a car” and a “sale contract”), [82] (“a contract for sale of goods on deferred terms”) and [92] (“a contract for sale” (three times)). Mr Prosser complained that in doing so the FTT was finding that the *Agility* contract was within para 1(2)(a) of sch 4 of  
40 VATA (“an agreement for the sale of the goods”) despite the fact that this was never HMRC’s case.

69. Mr Thomas confirmed that it was not his case (and had not been before the FTT) that the Agility contract was in law an agreement for the sale of goods. He did not seek to bring it within the second limb of Art 14(2)(b) as being a contract “for the sale of goods on deferred terms”; he accepted that it was a contract for the hire of goods within the first limb. The question – and the sole question argued – was whether it fell within the concluding words of Art 14(2)(b). But he said that the FTT was not purporting to find otherwise; its description of the Agility contract as a contract for the sale of goods was an economic characterisation not a legal one. As such it was unexceptionable.
70. The FTT could certainly have reduced the scope for confusion by making it clear whether they were engaged in the legal characterisation of the Agility contract or in ascertaining its economic reality. When the FTT expresses its conclusion in [82] as that they were satisfied that it was “a contract for sale of goods on deferred terms”, it is not perhaps surprising that Mr Prosser reads this as intended to be a reference to the second limb of Art 14(2)(b) which uses the same language. If the FTT did mean to suggest that as a matter of law the Agility contract was a contract for the sale of goods on deferred terms within Art 14(2)(b) (or for that matter an agreement for the sale of the goods within para 1(2)(a) of sch 4 of VATA) then I would agree that this was not a conclusion they were entitled to come to when this had not been HMRC’s case. And the potential for confusion is not helped by the FTT referring at [92] to the “legal realities of a contract for sale with an option to purchase.”
71. However, with some hesitation, I accept Mr Thomas’s submission that this is not what the FTT was doing. Reading the Decision as a whole, I do not think they can have meant that the Agility contract was a contract for sale as a matter of law. They correctly identified it as a hire purchase agreement [78(1)]; they recognised that the contract gave the customer an option to purchase [78(3)], [92]; and they recognised that as a matter of law the customer was not obliged to exercise the option, so that ownership might not pass [78(5)], [92]. In the light of this, I think the FTT must have been intending to refer not to the legal characterisation of the contract (which is clearly not a contract for sale, but is a contract for hire with an option to purchase), but to the economic reality. This is why they refer at [80] to the reality being different from that portrayed by MBFS, and to the sole realistic option being to purchase (repeated at [91]).
72. Since it was Mr Prosser’s own case that it was necessary to have regard to the economic reality in ascertaining whether the Agility contract was one under which ownership would pass in the normal course of events, I do not regard this as involving any procedural irregularity by the FTT.
73. Mr Prosser also complained under this head that some of the findings of fact reached by the FTT (for example, that purchase was “the sole realistic option”) were not contended for by HMRC. Mr Thomas in terms accepted that purchase being the sole realistic option was not a submission that he made to the FTT. But he said that the FTT was perfectly entitled to reach its own

view of the facts.

74. I consider that questions as to whether this and other findings of fact were open to the Tribunal is more conveniently dealt with under the third issue, that of whether the FTT's factual findings can be successfully appealed.

5 *The Factual Issue*

75. There was no dispute between counsel as to the principles:

(1) An appeal to the Upper Tribunal only lies on a question of law: s. 11(1) Tribunals, Courts and Enforcement Act 2007.

10 (2) A challenge to the factual findings of the FTT can therefore only succeed in accordance with the principles laid down in the well-known case of *Edwards v Bairstow* [1956] AC 14: see at 29 per Viscount Simmonds (“if it appears that the commissioners have acted without any evidence or upon a view of the facts which could not reasonably be entertained”), and at 36 per Lord Radcliffe (“no person acting  
15 judicially and properly instructed as to the relevant law could have come to the determination under appeal” or (a formulation which he said he for his part preferred) “the true and only reasonable conclusion contradicts the determination”).

20 (3) The construction of the Agility contract is a matter of law, but its characterisation in terms of what economic interests it serves is a question of fact. Mr Thomas referred me to the recent statement by Lord Hope in *HMRC v Aimia Coalition Loyalty UK Ltd* [2013] UKSC 15 at [107] that “what the economic reality is in a given case must surely be a question of fact for the domestic court”; and Mr Prosser  
25 accepted that the economic characterisation of the contract was a question of fact.

30 (4) On the other hand, it is not a question of primary fact; it is a factual conclusion drawn from a consideration of the contractual provisions in their context. This undoubtedly makes it easier for an appellate tribunal to interfere with the conclusion on the basis that it is one that no reasonable tribunal properly directed could reach.

35 76. Mr Prosser seeks to displace the factual findings of the FTT, in particular its characterisation of the Agility contract as in effect a contract of sale, where the sole realistic option for the customer was to purchase the vehicle. He accepts that unless he can displace these findings, then the appeal must be dismissed even if I accepted, as I have, his submissions on Art 14(2)(b). His case in essence is that the customer had a genuine choice whether to exercise the option to purchase (rather than, as the FTT put it at [102], the question of choice being “illusory”), and that it is wrong to characterise the contract in  
40 those circumstances as a contract of sale. He relied on the agreed statement of facts which included the following:

5 “5. Three finance options are available from MBFS: Leasing, HP and Agility. Agility was launched on 1 August 2007. If the customer has decided that they would like to purchase the vehicle, then a “Hire Purchase” product may be recommended. If the customer has decided that they would not like to purchase the vehicle, then a “Leasing” product will be recommended. If the customer is undecided, or would like to keep their options open, then the Agility product will be recommended.

10 6. Under Agility the customer signs a contract and usually pays a deposit. They pay an acceptance fee after one month, and make monthly payments thereafter through the life of the contract. Three months before the end of the contract MBFS writes to them asking if they wish to return the vehicle, purchase the vehicle outright, or purchase the vehicle and use it as a deposit for a new vehicle. At contract maturity the customer exercises one of these three options.”

20 Mr Prosser said that to characterise the Agility contract in these circumstances as one under which the choice was illusory, the sole realistic option was to purchase, and the contract was one of sale is simply wrong: there is no reasonable basis for reaching such a conclusion.

25 77. Mr Thomas, as I have said, accepted that it was not his submission to the FTT that purchase was the sole realistic option. Rather he said that the Agility contract is a means for a customer to acquire a vehicle: the essence of the agreement, just like the HP contract, is that the customer by making the instalment payments acquires the option to purchase the goods.

30 78. Before coming to the FTT’s findings in detail, I should say that I myself would have no difficulty in accepting both Mr Thomas’s and Mr Prosser’s characterisation of the contract as correct. Mr Thomas is plainly right that the Agility contract is a method of purchasing a vehicle. By paying all the contractual instalments, the customer does acquire the right to buy the vehicle. By that stage he has already paid the deposit (if there is one) and, by means of the monthly instalments, has also paid off a substantial part of the purchase price (in the examples given in paragraph 13 above either 57.5% or 51.4%), leaving a residual payment to be made. As Mr Thomas submitted, in this respect it is very similar to the balloon type of HP contract, where equally the customer by paying the monthly instalments acquires the right to purchase the vehicle and by the final month has paid off a similar amount of the capital (in the example given in paragraph 7 above 56%). The only difference is that in the HP contract the customer is by the terms of the contract obliged to pay the balloon payment (subject, at any rate if it is a regulated agreement, to his statutory right to terminate the agreement); whereas in the Agility contract the customer is under no obligation to make the final payment of capital as this is structured as the option payment. As Mr Thomas says this seems a very nice distinction on which to characterise the Agility contract differently from the

balloon type of HP agreement.

79. To that extent it seems to me indisputable that one of the economic interests which the Agility contract serves is the interest of the customer in being able to acquire the vehicle in a more affordable way than paying the full cash price upfront. Rather than finding, for example, £22,355 for a new C-class car, the customer can pay £516.20 per month for 3 years and then £11,450. It is easy to see that this may be a more attractive way of purchasing a car for some customers; and the (agreed) fact that if a customer shows no interest in purchasing a vehicle he is recommended a Leasing contract also serves to demonstrate that one of the purposes of the Agility contract is to enable customers to buy vehicles in this way if they want to.
80. Equally however for my part I would unhesitatingly accept that Mr Prosser is right that under an Agility contract the customer is not committed to the purchase at the outset. He is not committed legally because the option to purchase is an option which he is under no obligation to exercise. Nor would I conclude that he is committed economically: performance of the contract requires him to pay the 36 monthly instalments, but still leaves a substantial payment to be made. It does not seem at all a foregone conclusion that the customer will in fact exercise the option. The option payment is calculated to be equal to the anticipated residual value of the vehicle; but the actual value of the vehicle after 3 years will depend on the then state of the market for second-hand Mercedes vehicles which may not be as predicted. So there is no guarantee that it would make economic sense for the customer to exercise the option. But even if the vehicle is then worth its anticipated residual value, it is not difficult to see that some customers might not have £11,450 readily available; or might prefer in any event to start a new contract paying several hundred £ a month for a new vehicle rather than laying out over £10,000 for a 3-year old one.
81. In these circumstances, I would myself have no difficulty in accepting that another of the economic interests which the contract serves is the interest of the customer in being able to choose, 3 years down the line, whether to complete the purchase of the vehicle or whether to forego that opportunity. The fact that many of the customers (on average 50%) do not in fact acquire the vehicle would appear to show that this is a real, and not merely theoretical, interest.
82. So far as the economic interests of MBFS are concerned, there is not I think any difficulty and no real dispute. As the statement of agreed facts records, MBFS is neutral as to whether the customer ultimately purchases the vehicle because it does not take any risk on “the metal” (that is the second-hand value of the vehicle). The economic interests of MBFS which the Agility contract therefore serves are those of enabling it to provide vehicles to its customers on terms that they will either be purchased, or be returned at no loss to MBFS; at the same time MBFS receives interest on the finance it provides, with security in the shape of retention of title. As the FTT accepted at [99], the Agility

5 contract enabled MBFS to use its commercial knowledge of Mercedes vehicles (and its connection with its sister company) to eliminate the risks associated with the metal and thereby give MBFS a competitive edge over its competitors. Insofar as MBFS was exposed to other risks in the event of a vehicle being returned (namely that the customer might have run up greater mileage than expected or failed to maintain it, either of which could affect the value of the vehicle when returned), the Agility contract contained specific obligations designed to address these risks.

10 83. It seems to me therefore that it is not difficult to characterise the economic interests which the Agility contract serves. It serves the economic interests of the customer in having the ability to acquire a vehicle in an affordable way while not being committed to doing so at the outset, and having the opportunity to make that decision at the end of 3 years. It serves the economic interests of MBFS in the ways I have just described. None of this seems to me  
15 at all controversial: it is simply what the contract, objectively assessed, provides.

20 84. With that introduction, I can now consider the FTT's factual findings. The most pertinent are those at [79]-[82] which I have quoted in full above, as these contain the FTT's conclusions on its characterisation of the Agility contract simply based on the contractual provisions and without regard to the wider characteristics.

25 85. In [79] the FTT rejects MBFS's characterisation of the Agility contract as being a contract whose purpose was the hiring of a Mercedes Benz vehicle to a customer who wished to keep his options regarding ownership open until maturity. Five reasons are given by the FTT for characterising the contract instead as a contract of sale. The first is the description of the contract as a hire purchase contract. I agree with Mr Prosser that this is simply a consequence of the fact that the Agility contract, being a contract under which  
30 the hirer has an option to purchase the goods, is a hire-purchase agreement within the meaning of the CCA 1974 (see s. 189(1)) and that regulations require this to be stated in the agreement. Similarly the third reason (the specified financial information including the cash price for the vehicle) is due to the fact that regulations require this information in a regulated hire-purchase agreement. Neither of these indicators seem to me to demonstrate that the  
35 contract is anything other than it appears to be on its face, namely a hire of the vehicle under which the customer has an option to purchase.

40 86. The other three (the provision for a deposit payment, the substantial capital payment inherent in the contract structure, and the option to purchase) are all indicators that one of the purposes of the Agility contract is to enable the purchaser to acquire the vehicle. I have no difficulty with this and have already said that Mr Thomas is plainly right that one of the economic interests which the contract serves is the interest of the customer in being able to acquire the vehicle in an affordable way. The contract is one which is more than just a lease or hiring of the vehicle: it is plainly designed to enable the

customer to purchase the vehicle. If this is all that the FTT meant, then I would agree.

5 87. However this is not what the FTT said. It did not say that the purpose of the Agility contract was to give the customer the opportunity to purchase the vehicle; it said that the Agility contract was a contract of sale. When one reads this with the reference in [80] to the sole realistic option being to purchase the vehicle, with that in [81] to *Bradgate's* description of hire purchase as a supply of goods on credit terms coupled with security as neatly summing up the essence of Agility, and with that in [82] to Agility being a contract for sale of goods on deferred terms, it is apparent that the FTT meant more than that Agility provided the customer with an opportunity to purchase the vehicle. It must have meant that the economic reality was that Agility was in essence a sale although structured legally as an option.

15 88. But if this is what the FTT meant, I find myself driven to accept Mr Prosser's submission that there is no reasonable basis for the conclusion. The matters relied on in [79], far from being compelling indicators, do not justify the conclusion at all. They are all consistent with the contract giving the customer an opportunity to acquire the vehicle, in which case the deposit paid at the outset, and the capital paid off through the monthly instalments, would be set against the original cash price with the result that it is only the balance which needs to be paid to complete the purchase. So all that the customer has to pay on exercise of the option (ignoring the £95 purchase activation fee) is the balance of the purchase price, and this constitutes the Optional Purchase Payment. The deposit and the substantial capital payment therefore do indeed act as part payment of the original purchase price of the vehicle if the customer chooses to purchase it. But this fact, which is undoubtedly correct and which MBFS has not disputed, does not tell one anything about whether, as a matter of economic reality, the option is going to be exercised or not. That depends on a number of factors and simply cannot be assessed by looking at the contractual terms.

30 89. The FTT also refer in [79] to the requirement regarding maintenance as being consistent with a characterisation of the contract as a sale contract "in that it preserved the customer's investment in the vehicle". Mr Thomas did not suggest that this particular matter helped characterise the contract as one of sale; and I agree that he was right not to do so. If the customer is going to purchase the vehicle, MBFS has no interest in whether it is maintained or not; the customer does have an interest in maintaining what is going to be his own vehicle, but that is a matter for him and he has no interest in undertaking a contractual obligation to MBFS to do so. The only interest which this provision actually serves is the interest of MBFS in having the vehicle properly maintained in the event that the purchase is not completed. Thus although it is not inconsistent with the contract in reality being one of sale (as even in such a case MBFS has an interest in ensuring that the vehicle is properly maintained as there will be a risk of the purchase not being completed), this obligation provides no support for the conclusion.

90. In [80] the FTT referred to the return of the vehicle as “the default position for the customer who lost his/her capital investment”. There was some discussion before me as to what the FTT meant by “the default position” but I think Mr Thomas must be right when he said that they meant the position the customer would be in if he did nothing, that is did not exercise the option. The description of the customer losing his/her capital investment is relied on as an indication that the sole realistic option was to purchase the vehicle. But this seems to me another conclusion without foundation. As I have already said, the structure of the contractual payments was such that if the customer exercised the option, he would get the benefit of the deposit and capital payments already made so that he would only have to find the balance of the cash price due by way of option payment. In this sense it is true that the payments already made in the 3 years of the contract period are a benefit to the customer if he proceeds with the purchase.
91. But this does not mean that he loses anything, or anything of value, if he chooses not to exercise the option. Mr Thomas said that the reference to the customer’s investment in the vehicle was not being used in any technical sense – the customer did not acquire part ownership of the vehicle – but was being used in an economic sense in that by making the monthly payments, the customer acquires the right to acquire the goods; and if he does not take up the option in that sense he loses the benefit of having made the payments.
92. What however the payments qualify him for is the opportunity to acquire the vehicle at a reduced price; and that reduced price is itself set at the expected residual value of the 3 year old vehicle. So what the customer has at the end of 3 years is the opportunity to pay, for example, £11,450 for a 3 year old C-class car expected to be worth £11,450. This may or may not be an opportunity that he wishes to take up, but it cannot be said that in failing to take it up he is missing out on an opportunity of great value or losing, in any relevant sense, a capital investment he has made. If he chooses not to exercise the option, the deposit and monthly payments simply represent the cost to him of having the use of the vehicle over the contract period; to MBFS they represent compensation for the depreciation in the value of the vehicle when it is returned, and interest on the finance they have provided.
93. The FTT also referred in [80] to the fact that a customer who did not exercise the option incurred a potential liability for excess distance and damage. This is true. Mr Thomas said that this constituted a powerful incentive to proceed with the purchase. The difficulty with this is that it all depends: if a customer did not exceed the stated mileage (and as I understand it the specified mileage is something chosen by the customer himself at the outset of the contract) and maintains the vehicle, these provisions do not apply. It has not been suggested to me that there was any evidence before the FTT – and certainly they do not refer to any – which would shed any light on how significant these provisions might be in practice. I can see that the FTT was justified in concluding that they might act as an incentive to some customers to exercise the option. They do not seem sufficient to justify the conclusion that the Agility contract is in

general to be regarded as in reality a form of sale. The purpose of them is evidently the protection of MBFS in the event that there is no sale.

- 5 94. In my judgment therefore the conclusion of the FTT at [80] that the sole realistic option under the agreement was to purchase the vehicle was indeed a conclusion which was unsupported by the material referred to by the FTT and was one that no reasonable tribunal, properly directed, could reach. The true and only reasonable conclusion from the material before the FTT was that the Agility contract gave the customer an opportunity to purchase the vehicle, but that it also gave him a genuine (and not illusory) choice as to whether to do so.
- 10 95. At [99]-[103] the FTT stated its findings on the wider circumstances in case they were wrong to exclude them. Mr Thomas submitted that they were right to exclude the wider circumstances. This I think goes too far: see the comments of Briggs J in *MBNA* cited at paragraph 25(5) above which indicate that the contract has to be interpreted by reference to the relevant matrix of background facts. I do however accept that the exercise of finding the contract's economic purpose, as explained by Advocate General Tizzano, must primarily depend on the terms of the contract.
- 15 96. I should therefore briefly consider the FTT's findings on the wider circumstances. At [99] they referred to the decisive factor for determining the commercial purpose for Agility as being the rationale for its introduction, Agility being essentially a repackaged hire purchase transaction incorporating MBFS's knowledge of its vehicles which eliminated the risk with the metal and gave MBFS a competitive edge over its competitors' hire purchase products. I accept that this was a finding open to them. It accurately identifies (at least some of) MBFS's interests which the contract is designed to serve. It does not it seems to me answer the question whether the contract was in effect a sale or not; indeed the very fact that MBFS introduced the contract to eliminate risks if the vehicle was returned (that is if there were no sale) tends to suggest the opposite. Indeed, as the statement of agreed facts records, it was the ability of MBFS to lay off the risks on the second hand value of the vehicle which made MBFS neutral as to whether the purchase proceeded or not.
- 20 25 30 35 40 97. At [100] the FTT referred to the striking similarities between the Agility and HP agreements, previously identified at [56]. It is true that there are many similarities between the HP agreements and the Agility contract: since the Agility contract is undoubtedly intended to provide the customer with an opportunity to purchase the vehicle, this is not surprising. So both are described as hire purchase agreements [56(1)] (this is in fact required by regulations); both contain an option to purchase [56(2)]; both have a £95 fee payable on exercise of the option [56(3)]; both include provision for a deposit [56(7)] (the agreed statement of facts was in fact that Agility customers "usually" pay a deposit); and both contain a detailed breakdown of financial information [56(8)] (again as required by regulations). All of this flows from the fact that the Agility contract was undoubtedly designed as a means by

which the customer could purchase the vehicle; and the FTT is right to note that in these respects the Agility contract is like the HP contract and unlike the leasing contract. The latter is described as a hire agreement not a hire purchase agreement; it contains no option to purchase, no deposit and no financial information other than the monthly rental payments.

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98. However other similarities noted by the FTT rather skate over the differences between the two products. Thus they refer to the fact that the HP contract could be of the balloon type “termed as the *final payment* rather than the term *optional purchase payment* as used in Agility” [56(4)]; and the fact that the financial profile of the balloon type of HP agreement was similar to Agility with deposit (13%), net monthly payments (43%) and final payment (44%). These similarities ignore the fact that the final payment in the HP contract is one that the contract stipulates will be paid, whereas in the Agility contract it is the option price and the customer has a contractual option whether to pay it or not. Similarly the FTT say that both contracts gave the customer the right not to exercise the option [56(5)], and that both provided the customer with the option either to purchase or to return so that downstream purchase was not obligatory [56(6)]. While this is true, they do not advert to the difference between them, namely that the option payment in the HP contract was only the nominal £95 so it would make no commercial sense for the customer, having made all the contractual payments, not to exercise the option, whereas in the Agility contract the option payment was a substantial payment equal to the anticipated residual value of the vehicle so that the same did not apply.

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99. The Tribunal’s conclusion at [100] is that the similarities between the Agility and HP contracts supported the characterisation of Agility as a hire purchase contract. As a matter of law the Agility contract is a hire purchase contract as it is a contract of hire with an option to purchase. But this does not it seems to me assist with the question whether it is in reality a contract of sale.

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100. At [101] the FTT referred to the marketing material. They concluded that it was contradictory, in that some of the material indicated that Agility was for customers who wished to keep their options open but in their view the pictorial depiction of the car and the use of the word “Your” gave the impression that Agility was about ownership of the vehicle. I rather doubt that I would have taken the same view myself as I regard the pictorial depiction and the use of the word Your as ambivalent at best, but I accept that this was a factual finding that was open to the FTT. Since however they regarded the marketing material overall as contradictory, it cannot by itself justify a conclusion that the transaction was in reality one of sale, and the FTT do not say that it does.

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101. At [102] the FTT referred to the question of choice as illusory. Mr Thomas accepted that this reflected the finding at [80] that purchase was the sole realistic option, and did not attempt to support it if it meant (as it appears to mean) that the customer did not in reality have a choice. For reasons already given, I do not regard this as a sustainable conclusion.

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102. In [103] the FTT expressed its conclusion from its assessment of the wider circumstances that:

5 “from a commercial perspective *Agility* would be categorised as an affordable hire purchase product which carried no risks on the metal for [MBFS].”

10 I have already said that as a matter of law *Agility* is undoubtedly a hire purchase agreement (and I see nothing inaccurate about describing it as an affordable product which carried no risks on the metal for MBFS), but that this does not assist in characterising it as in reality a contract of sale. So far as I can see that characterisation depends on the assessment of the FTT that the sole realistic option for the customer was to purchase the vehicle, and that the supposed choice for the customer was illusory. Neither in my judgment is capable of being supported by the material which the FTT relied on.

15 103. At [104] the FTT set out 11 findings of fact that MBFS asked it to make with its comments. I do not think it necessary to go through them: the FTT’s comments reflect the findings they had already made in earlier parts of the Decision, and I have dealt with the material points above.

20 104. Mr Thomas summarised his case on the facts as being that the FTT was entitled to come to the view that the *Agility* contract had features which supported the analysis that the economic purpose of the transaction was a sale of goods. For reasons already given I have no difficulty with the proposition that one of the purposes of the contract was to enable the customer to purchase the goods in a more affordable way than buying them outright. But this is not a complete or adequate description of the economic interests which performance of the contract serves. The contract also serves to give the customer a (real and not illusory) choice after 3 years whether to proceed with the purchase or return the vehicle, together with provisions designed to protect MBFS in the event that the customer chooses not to purchase the vehicle. This seems to me the true and only reasonable conclusion from the facts and I have been unable to find anything which would justify the FTT’s apparent factual findings to the contrary.

35 105. Mr Thomas also submitted that the economic reality of the *Agility* contract was indistinguishable from that of the balloon type of HP contract. The only difference between them was that in the HP contract, the balloon payment was one that was due under the contract (but which in the case of a regulated agreement the customer could in practice avoid paying by exercising his statutory right to terminate the contract early) whereas in the *Agility* contract the customer had a contractual right not to pay the balloon payment. This was, he said, too fine a difference to affect the characterisation of the contract. There is undoubtedly some force in this point, but in the end the question remains what is the economic purpose of the *Agility* contract in the sense explained by Advocate General Tizzano.

106. As explained above, the economic purpose of the contract is to be found by identifying the precise way in which performance satisfies the interests of the parties, and I have already set out the way in which the Agility contract satisfies the interests of the parties (see paragraphs 79 to 83 above). In  
5 summary it does so by affording the customer an opportunity to purchase but without committing him to do so, and by giving MBFS a return on the finance it provides in circumstances where either the vehicle will be purchased or it will be returned at no risk to MBFS.
107. I do not think this can be characterised as in effect a contract for sale of the  
10 vehicle. It is a contract which may well lead to a sale of the vehicle but equally may well not. In line with the views I have expressed above as to the scope of Article 14(2)(b), it is not in my judgment a contract under which ownership is to pass in the normal course of events.
108. I will therefore allow MBFS's appeal.  
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**MR JUSTICE NUGEE**

**RELEASE DATE: 02 May 2014**