TC02545

Appeal number: TC/2011/06973

Customs Duty - transaction value – whether marketing costs can be deducted or operate as a credit which reduces price paid or payable – no – whether retrospective price adjustment – no – appeal dismissed

FIRST-TIER TRIBUNAL
TAX CHAMBER

WIDGET UK LIMITED **Appellant**

- and -

THE COMMISSIONERS FOR HER MAJESTY'S REVENUE & CUSTOMS **Respondents**

TRIBUNAL: JUDGE DR K KHAN
RUTH WATTS DAVIES MHCIMA FCIPD

Sitting in public at Bedford Square in London on 5 December 2012

Mr Steve Cock, Consultant for the Appellant

Mr David Bedenham, Counsel, instructed by the General Counsel and Solicitor to HM Revenue and Customs, for the Respondents

DECISION

Introduction

1. This an appeal against a decision by the Commissioners for Her Majesty's Revenue & Customs ("the Commissioners") dated 4 August 2011. The decision upheld a reconsideration decision made on 31 May 2011. The earlier decision refused an application for repayment of import duties totally £40,258.35. The Application for repayment had been made pursuant to Article 236 of the Customs Code (Council Regulation 2913/92).

Background & relevant facts

2. The facts in this case are not disputed. The relevant facts are outlined below.

(1) Widget UK Ltd ("the Appellant") (No 3956797) is a company which imports and distributes consumer electronic products. Their registered office is Unit 4, The 10 Centre, Arlington Business Park, Whittle Way, Stevenage, Hertfordshire SG1 2BD.

(2) On 2 March 2009, the Appellant entered into a distribution agreement ("the Agreement") with a US supplier, Pure Digital Technologies Incorporated ("Pure Digital") for the purchase and resale of products manufactured by Pure Digital. This included flip video camcorders, tapeless camcorders for digital radios and a range of other similar camcorders. These camcorders were largely used in making short video recordings. The Appellant imported several of these video camcorders from the USA between March 2009 and December 2009. The importation took place within the terms of the Agreement. The total importation amounted to some £14,000,000 with duty of £821,599 of which 4.9% (£40,255) is sought to be recovered.

(3) Pure Digital invoiced the Appellant for the imported products. The invoice price was the price paid by the Appellant as a transaction value on which the applicable customs duty was to be paid (being the price paid or payable by the buyer to the seller).

(4) Under the Agreement Clause 2.8 provides for a Marketing Development Fund ("MDF") which provides:

> "MDF is accrued by Widget UK Ltd per camcorder purchase from the PDT….. The fund is allocated to Widget customers based on the completion by the customer(s) of agreed marketing actions…… Widget UK Ltd will transfer these funds in line with their contractual relationship with the customer(s)……."

(5) The Appellant asserts that the payment pursuant to Clause 2.8 of the Agreement constitutes a reduction in the price paid or payable by the buyer to the seller for the goods.

(6) The basis of the claim is that the Customs value originally paid in respect of the camcorders when they were purchased from the Pure Digital and

imported into the UK should be reduced to take into account amounts shown on credit notes issued by Pure Digital in respect of payments made from the MDF.

(7) The core issue therefore is the MDF credit and the quantum of that credit. The Appellant asserts that the amount claimed is 4.9% of £821.599 which is £40,258.35.

(8) In October 2010 the Commissioners rejected the claim of the Appellant on the grounds that there were two transactions and the marketing payment could not be deducted from the import value. After further representations by the Appellant, the Commissioners upheld their decision.

(9) On 26 January 2011, the Appellant's representatives, The Customs Consultancy, submitted a further C285 Form, containing a repayment of customs duty claim under Article 236 of the Community Customs Code ("CCC"), which constituted a second claim for the duty. On 31 May 2011, the Commissioners rejected this new claim on the grounds that the repayment was the same as those made in the earlier claim. For clarification, the new claim was treated as a resubmission of the earlier claim on the grounds that the repayment was the same as that in the earlier claim.

(10) There was further correspondence between the parties in June 2011. The Appellant provided further information relating to the circumstances that gave rise to the claim and further argument. After reconsideration by the Commissioners, on 4 August 2011, the Commissioners notified the Appellant that their second repayment claim was rejected. This is the decision which is the subject of this Appeal.

(11) The Commissioners disagreed with the Appellant's contention that the payments made pursuant to Clause 2.8 constituted a reduction in the price paid or payable by the buyer to the seller for the goods imported. The payments were treated as being made for undertaking certain marketing activities. This is supported by the fact that the payments were made for the benefit of customers.

Relevant Legal Provisions

3. Article 29.1 of the CCC provides in relevant part:

"The customs value of imported goods shall be the transaction value, that is, the price actually paid or payable for the goods when sold for export to the customs territory of the Community, adjusted, where necessary, in accordance with Articles 32 and 33…."

4. Article 29.3 then provides in relevant part:

"The price actually paid or payable is the total payment made or to be made by the buyer to or for the benefit of the seller of the imported goods and includes all payments made or to be made as a condition of sale of the imported goods by the buyer to the seller or by the buyer to a third party to satisfy an obligation of the seller. …."

5. Article 236(1) provides:

> *"Import duties or export duties shall be repair in so far as it is established that when they were paid the amount of such duties was not legally owed or that the amount has been entered into the accounts contrary to Article 220"*

Witness Statement of Mark Needham

6. Mark Needham is the Chairman of Widget UK Ltd. He provided a Witness Statement dated 11 May 2012 and oral evidence. He made the following points;

(1) The MDF is stated as relating to the need for retailers to engage in marketing activities, but in reality its use was quite different. It would be used to provide credits to help him show the maintenance of retail price through rewards to compliant customers. Alternatively, it might be used to provide additional credits in relation to securing larger sales, particularly at quarter end to ensure that sales targets were met by Widget.

(2) The use of the MDF was not the sole discretion of Widget. In addition to his own sales staff, the marketing of the Flip product range to retailers also undertaken by the staff of Pure Digital. The use of the MDF relation to securing sales was undertaken at the direction of Pure Digital's marketing team.

(3) The MDF was used as a means to control price by allowing for reductions in the value of the imported goods.

(4) Retailers would ask for a percentage of the purchase price to be allocated for marketing. This would impact on the profits of the Appellant. The MDF provides a mechanism for paying these additional costs which a retailer may add when contracting the Appellant.

(5) The money paid under the MDF was treated as a credit which was held in the account of the Appellant. Pure Digital would give their permission to dispose of the money once retailers undertook suitable marketing activities.

(6) The Appellant obtained a discount or price reduction on the price paid to Pure Digital for products.

(7) A credit note would only be given to the Appellant after it was approved by the customer relations manager appointed by Pure Digital.

Appellants Submission

7. The Appellant makes two core submissions.

8. The first is that under the terms of the Agreement, the MDF credits would allow for a reduction in the price paid or payable for the products. This is because pursuant to Article 29 3(a) of the CCC the costs in undertaking marketing activities are not to be included in the value for Customs under the transaction method of valuation. Article 29, 32 and 33 of the CCC provide for certain additions and exclusions to and from the transaction value. One such exclusion is the cost of marketing activities undertaken by the buyer. Such a payment is not considered to be an "indirect

payment to the seller" even though it might be regarded as a benefit to the seller or have been undertaken by agreement with the seller.

9. Marketing activities for the purposes of Article 29.3(b) of the CCC is given a broad definition and includes "all activities relating to advertising and promoting the sale of the goods in question and all activities relating to warranties or guarantees in respect of them".

10. Article 148 of the Implementing Regulations ("IR") to the CCC states that such marketing activities are treated as being undertaken by the buyer on their own account and not on behalf of the seller even though they are performed in pursuant of an obligation and the buyer is in agreement with the seller.

11. The point being made by the Appellant is that marketing costs shall not be added to the price actually paid or payable in determining the customs value of imported goods. This is confirmed Article 29.3 (a).

12. The Appellants say that the MDF, is simply a provision requiring marketing activities to be undertaken and under Article 148 of IR to the CCC, it is clear that marketing activities linked to any MDF payments must be regarded as being undertaken by the Appellant on their own account and should not be added to the customs value of imported goods. The Article 148 of the IR to the CCC is consistent with the provisions of the third and fifth recitals to the Agreement on Implementation of Article VII of the General Agreement on Trade and Tariffs ("GATT") 1994. The third recital recognises the need to be fair, uniform and neutral in valuing goods for customs purposes and that precludes the use of arbitrary or fictitious custom value. The Appellant cites the case of C-306-04 *Compaq Computer International Corporation v Inspecteur Der Belasting Inest – Douane District Arnhem (*at para 30) were the Court (ECJ) stated that it would be unfair if the costs associated with marketing activities undertaken in the EU were on occasion subject to the customs duties and at other times was to be excluded from the value of the duty.

13. The fifth recital recognises that customs values should be based on simple and equitable criteria consistent with commercial practice and valuation practices and procedures should be of general application without distinction between sources of supply. The Appellant said that in order to be equitable and recognise commercial realities there should be a consistent application and interpretation of the relevant provisions and marketing costs should not adversely impact on the values for customs duties.

14. Irrespective of the position under Article 29 3 (a) of the CCC and Article 148 of the IR to the CCC, the Appellants submit that the MDF credits should not be the subject of duty. This results from the fact that the payments are made in accordance with the Agreement and consequently reduced the price or payable for the goods. The Appellant's draw reference to Commentary No. 8 of the Customs Code Committee dealing with the treatment of discounts under Article 29 of the CCC. The simple point is that a discount is taken to be a reduction of the list price for goods or services if given at the material time. The material time would be when the Agreement is

signed and thus the importation of the products took place pursuant to the Agreement. For the discount to be given it must relate to the imported goods and there must be a valid contractual entitlement at the time of signing of the Agreement under which the goods are imported. The Appellants say that the MDF satisfy all of the requirements in Commentary No. 8 of the Customs Code Committee. They state the conditions to be

(a) The MDF credit result in a discount to the list price of the goods.

(b) The potential for the discount and its value was known at the material time for Customs valuation.

(c) The discount was contractually provided for and specifically relates to the imported goods.

(d) Although not detailed in the suppliers' invoice, the fact that it is a contractual claim at the material time means that a discount should be recognised in the Customs valuation.

15. The Appellants' second submission is that the MDF is simply a price reduction. They contend that as implemented, the MDF credits received under the Agreement allow for a reduction in the price paid or payable for the products. The Appellant draws on the witness statement of Mr Mark Needham, Chairman of the Appellant company. In his oral and written evidence he stated that the MDF was simply used as a means to control price by allowing for reductions in the value of the products at the time of importation. Mr Needham stated that the MDF was used to ensure the maintenance of retail price through a reward system given to compliant customers or as a credit to secure larger sales.

16. The Appellants say that in reality the MDF was a discount which reduced the price paid or payable for the goods. Therefore it follows that the transaction value was accordingly reduced as contemplated by Article 29 of the CCC. In determining value it is not sufficient to rely on the Agreement. To do so may create arbitrary and fictitious customers values. This argument seems to focus on the reality of the commercial transaction rather than the written terms of the Agreement. The Appellants say that the MDF payments were "in reality" utilised as a price protection reduction to the value of the products and imports and consequently the Commentary No 8 of the Customs Code Committee is applicable in determining whether the price paid or payable for the product was altered. Again, the Appellant draws reference to the requirements stated by the Customs Code Committee which were itemised above and says that they are all satisfied with this case.

17. This form of price reduction is recognised by the Commissioners as stated in the letter of Tara Allitt of 24 September 2012. It further is provided in HMRC's Public Notice 252, Valuation of Imported Goods for Customs Purposes VIGCP, Section 30.3 which states

"Where, at the time of entry, there are contractual arrangements in place between you and the seller indicating the possibility of retrospective price

adjustments, the invoice price for the goods concerned would, in effect be provisional".

18. In simple terms, the Appellants say that this is a reduction in the price and the true or real price should be the subject of Customs duty not a fictitious or artificial price which included an amount for marketing.

The Respondents Submissions

19. The Respondent's core submission is that customs duty is calculated on the transactional value which is to say the price actually paid or payable for the products. In this case that price is the invoice price charged by Pure Digital to the Appellant. While accepting that that price could be discounted, the amounts paid pursuant to the MDF (Clause 2.8 of the Agreement) are not retrospective price decreases but rather payments made for undertaking certain marketing activities. The price paid or the transactional price has not been altered.

20. The payments made under Clause 2.8 of the Agreement are for the benefit of the Appellant's customers and do not constitute a reduction in the price paid or payable to the seller.

21. The Appellant has not provided evidence of a contractual entitlement or price reduction based on Clause 2.8. This was required under Public Notice 252 Paragraph 30.3 which requires any claim for a price reduction to be "accompanied by appropriate evidence including full details of the contractual arrangements as well as rebates received from and issued by the seller". Therefore the evidential burden has not been satisfied by the Appellants. The Public Notice 252 lays out requirements which are not satisfied in this case.

22. Clause 2.8 of the Agreement does not provide a price reduction. There is no formal variation of the contract price which gives rise to an entitlement. There is no legal basis for the entitlement.

23. The reliance by the Appellant on Article 148 of IR which reliance runs contrary to the Appellant's ascertain that Clause 2.8, does not operate in practice as provided for by the wording of the Agreement. The reason is because Article 148 (2) makes clear that the cost of marketing "even if they are performed in pursuant of an obligation on the buyer following an agreement with the seller" are not to be taken into consideration for Customs valuation purposes. The obligation in this case is not on the buyer but rather on the retailers to do certain marketing. Therefore if it was a fund to provide repayment for marketing by retailers, the claim would fail.

24. The alternative argument, that it was a mechanism for price reduction is without support on the evidence provided. Clause 2.8 of the Agreement only provides that the money is to be used in marketing.

25. The Respondents say that there has been no over payment of duty justifying a repayment under Article 236 of CCC.

Discussion

26. Let us start by looking at the background.

27. The European Union ("the EU") is a member of the World Trade Organisation ("WTO"). On 1st January 1995 the WTO Agreement replaced the General Agreement on Tarrifs and Trade ("GATT"). The GATT was a multilateral Agreement regulating international trade. The WTO Agreement provides a framework within which the previous GATT tax operates subject to any modification. WTO Agreements therefore incorporate and update the GATT.

28. Article V11 of GATT 1994 deals with the valuation of products for Customs purposes. The value is based around actual value. The actual price is the price of which goods are sold or offered for sale in the ordinary course of business. In providing a basis for valuation of goods it was intended to provide a system which was simple and equitable and based on commercial principles and agreed valuation procedures. The Customs value of goods imported from outside the EU is determined on the basis of the CCC established by Council Regulation 2193/92, Articles 29-36 and the IR to the CCC established by Commission Regulation 2454/93, Articles 141-181 and Annexes 23-29.

29. In valuing goods, there are several possible methods of valuation. The *Ad Valorem* Customs value of imported goods is determined according to six possible methods. The methods of valuation must be attempted starting with method 1 and moving to method 6 in consecutive order. Method 5 is attempted before method 4. Method 1 is known as the transaction value which is determined by the price actually paid or payable for the goods when sold for export in the country of importation. The transaction value is accepted by both parties as being the appropriate valuation in this case. This therefore is a method of valuation to be used in determining the sales price between PD and the Appellants.

30. Article 29.3 (a) of the CCC a includes in making the valuation "all payments made or to be made as a condition of sale of the imported goods by the buyer to the seller or by the buyer to a third party to satisfy and obligation of the seller" Article 29.3 (b) excludes the costs of marketing activities from the price if undertaken by "the buyer on his own account".

31. In looking at the price paid or payable in Article 29 of the CCC the IR provides a useful guide in Article 148 which states:

> "1. For the purposes of Article 29.3 (b) of the Code, the term "marketing activities" means all activities relating to advertising and promoting the sale of the goods in question and all activities relating to warranties or guarantees in respect of them.
>
> 2. Such activities undertaken by the buyer shall be regarding as having been undertaken on his own account even if they are performed in pursuance of an obligation on the buyer following an agreement with the seller"

32. The critical wording is "own account". This would suggest that costs associated with the buyer in conducting marketing activities on their own account, which is that they pay for them, are not to be included in the value for Customs under the transaction method.

33. Article 148 of the IR to the CCC extends the provisions of Article 29.3 (a) of the CCC. It provides that marketing activities performed as a result of a "contractual obligation" with the seller, shall be regarded as being undertaken by the buyer on their own account. This means that this cost should not be added to the price actually paid or payable in determining the customs value of imported goods.

34. What then does the contractual provisions provide? The MDF, a marketing agreement between the Appellant and Pure Digital, the Appellant is obliged to undertake certain contractual arrangements with its customers. In return for undertaking certain marketing activities customers receive payments from the Appellant. The Appellant asserts that marketing activities linked to any MDF payment must be regarded as being undertaken by the Appellant on their own account and so should not be added to the customs value of imported goods. They say that this approach is consistent with Article V11 of GATT 1994 which recognises a fair, uniform and neutral system for the valuation of goods and where values should be based on simple and equitable criteria.

35. The Tribunal disagrees. The price contemplated by Article 29 is the price charged by the seller to the Appellant on the day that the goods were released for free circulation. That is a material time for determining the customs value. At the time of export, the Appellant has no contractual entitlement to any payment from the MDF because that payment is subject to the retailer carrying certain marketing activities. Clause 2.8 of the MDF states that the "fund is allocated to the Appellant's customers based on the completion by customers of agreed marketing actions, validated by the Country Manager of Flip Video UK. "Widget UK Ltd will transfer these funds in accordance with their contractual relations with the customer(s). …."

36. The discount being offered to the Appellant through the MDF is both conditional and retrospective in nature.

37. The Commissioners guidance in Public Notice 252 provides for retrospective price adjustments, including discounts but this is provided "where we are satisfied that the price decrease stemmed from contractual arrangements in force at the time of entry of the goods concerned….". There is no disputing that the discounts provided by the MDF do arise from contractual arrangements between the parties at the time of the entry of the goods but these sums are not "payable" at the time of the export under Article 29.1. Further, the payments contemplated are for the benefit of the customers of the Appellants and only and on undertaking certain marketing activities. The payment is therefore too far removed from the material time when the sales transaction takes place.

38. Commentary No 8 of the Customs Code Committee (Customs Valuation Section) of European Commission deals with discounts under Article 29 of the CCC

and at paragraph 2 states; "For customs valuation purposes the discount must relate to the imported goods and there must be a valid contractual entitlement at the material time". The material time is the date of acceptance of the Customs Declaration by Customs authorities.

39. What emerges is that for any discount rebate or price adjustment to be taken into in determining of the customs value for the purposes of Article 29 of CCC, it must satisfy the following conditions:

(1) Relate to the imported goods;

(2) Be granted against the transaction on the basis of which the customs value was declared; and

(3) If granted retrospectively, it must be provided for in the contractual arrangements between buyer and seller in force at the time of the acceptance of the Declaration for release to free circulation.

40. The discount was not something the Appellant was entitled to. There was no legal obligation to make a payment of the specified amount in the future. The amount payable under the MDF is more flexible. It was an amount which may or may not become payable in the future on the basis of marketing activities which may or may not be undertaken by the Appellant's customer

41. The Tribunal therefore finds that there were two separate transactions. These transactions are;

(1) The sale of goods by Pure Digital to the Appellant in return for the payment of a wholesale price for goods pursuant to the Agreement; and

(2) The MDF payments made by the Appellant in accordance with Clause 2.8 of that Agreement, the purpose of which is to support the Appellant's customers in marketing the goods.

The MDF payments do not amount a revision or renegotiation of the price paid to Pure Digital for the imported goods after the entry of those goods.

42. Further the MDF accrues according to the number of Flip Video Camcorders purchased by the Appellant from Pure Digital. The payments contemplated by the MDF therefore are payments which would be made after the goods have imported. They do not relate to their sale but rather to their marketing. This is confirmed by the fact that the payments are made only after agreed marketing actions were undertaken by the Appellants customers.

43. The MDF is an internal fund created which can be rolled over to future periods and appears to be only related to the imported goods. Clause 2.8 states "the fund will be reviewed, quarterly, and the balance officially rolled over to the following quarter if both parties agree. If there is no agreement then the surplus is paid back to PDT and a deficit rescinded to Widget UK". In the Tribunal's view this does not amount to a discount of the purchase price and is clearly a conditional payment.

44. The Appellant asserts that the Clause 2.8 of the Agreement operated differently in practice. The evidence of Mark Needham suggested the MDF was used as a means to control price by allowing for reductions in the value of the goods at the time of importation. The MDF payments were reality discounts granted by the supplier to the buyer and reduced the price paid or payable for the goods. The Appellant says that the Agreement was implemented in a different way and reliance should not be placed on its terms. They also draw a reference to the fact that the Respondents confirmed that price protection credits, of the type provided by the MDF, can alter the price paid or payable for goods and can lead to the repayment of Duty. They draw reference to the HMRC's letter of 24 September 2012. In that letter, HMRC makes a distinction between payments made under the MDF and where a supplier drops their prices and a credit is given in relation to any stock that the Appellant is holding a the time of the price drop which was purchased prior to the price drop. The HMRC accepts that this is clearly a reduction in the price paid or payable for the goods. This is a different situation from the one in this Appeal. It must be added also that while the Appellants say the contract operated differently in practice, this is not what is stated on their Notice of Appeal. Or indeed what the contract itself says in its wording. This argument of the Appellant while interesting is not persuasive.

45. The Appellant has provided with the Application for Repayment Form (C285) details of the import valuation claim schedule, a copy of the MDF Agreement, calculations showing schedule of post import credits, examples of credit notes, examples of commercial invoice supporting entry, example of post import credits, copy of the relevant contracts, correspondence and MSS data listing all imports of the Flip Camcorder.

46. This information is helpful and was well presented. However while the accrual of the marketing fund seems to be based on the number of goods purchased, the payment out of the marketing fund are not linked to the goods but rather to the occurrence of certain marketing activities. The Tribunal cannot see how these payments constitute a price reduction in relation to the goods themselves. The Appellants further argument that the payments from the MDF were not conditional upon marketing activities but rather was a mechanism through which the price of the goods could be reduced. This appears to be a new argument and not one which is supported by the contractual documents. The Appellant bears the legal and evidential burden of establishing that their claim for the repayment of customs duty is correct. The onus is on the Appellant to prove their case and in the Tribunal's view they have failed to provide sufficient evidence to support their claim. The Appeal is therefore dismissed and the Commissioners refusal of the Appellants claim for repayment of the customs duty is upheld.

47. This document contains full findings of fact and reasons for the decision. Any party dissatisfied with this decision has a right to apply for permission to appeal against it pursuant to Rule 39 of the Tribunal Procedure (First-tier Tribunal) (Tax Chamber) Rules 2009. The application must be received by this Tribunal not later than 56 days after this decision is sent to that party. The parties are referred to "Guidance to accompany a Decision from the First-tier Tribunal (Tax Chamber)" which accompanies and forms part of this decision notice.

DR K KHAN
TRIBUNAL JUDGE

RELEASE DATE: 13 February 2013