TC03030

Appeal number: TC/2013/00620

Value Added Tax - Whether goods were sold for a combination of cash and the value of part-exchange items, or whether the part-exchange items were in substance the equivalent of a discount so that the goods should be treated as sold for the cash consideration alone - Appeal dismissed

FIRST-TIER TRIBUNAL
TAX CHAMBER

AV CONCEPTS LIMITED **Appellant**

-and-

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

TRIBUNAL: JUDGE HOWARD M. NOWLAN
GILL HUNTER

Sitting in public at 45 Bedford Square in London on 24 October 2013

Timothy Brown, counsel, on behalf of the Appellant

L. Bingham of HMRC on behalf of the Respondents

DECISION

Introduction

1. This was superficially a very simple case. The feature that rendered even the basic question more difficult than it might have been was that the person who had been responsible for the transactions in question had left the Appellant company, and there was nobody at the hearing from the Appellant (apart from the Appellant's counsel and instructing solicitor or accountant) so that there was some considerable difficulty in establishing what had truly happened.

2. On further consideration however, particularly when certain facts emerged half way through the hearing that nobody had appreciated in advance, the Appeal plainly came close to some very complex areas of VAT law, in relation to which we had not been addressed. We will mention these in passing, but since they related to the various situations carefully considered by Lord Justice Chadwick in the Court of Appeal decisions in the *Littlewoods, Lex Services, Bugeja* and the *Kuwait Petroleum* cases, all reported at [2001] EWCA Civ 1542, we will merely touch on those issues that could be material to the Appellant in this case in future transactions. They were not strictly relevant to the actual decision that we had to reach.

The point in contention

3. The Appellant had two lines of business, and we were only concerned with the more minor line of business. That consisted of supplying (generally, if not always, to schools) sophisticated "white boards". It is immaterial whether we quite understood what the products were, but they sounded like large schoolroom display boards, on which teachers could write, and from which printed copies of the material on the boards could be printed off for the pupils. Since much of the Appeal related to the fact that when the boards were supplied, the Appellant generally took back some near obsolete projectors, we imagine that the boards could also project pictures and perhaps film.

4. The point in issue (ignoring one complication at this point) was that the boards were, it seemed, invariably supplied for cash, plus the supply by the school, back to the Appellant, of various obsolete projectors or other similar equipment. The point in dispute was whether the sale was therefore a part-exchange or barter transaction, in which the consideration (however valued) consisted of the receipt of the cash plus the value of the part-exchange item, accompanied of course by the fact that the school would simultaneously be supplying the obsolete item that the Appellant might or might not subsequently sell. The alternative possibility was that the transaction should be treated as one where the obsolete item taken in exchange should be treated just as a discount (with the consideration then being confined just to the cash) in the way that many retailers will sell new TVs and washing machines, giving say £50 for the customer's old TV or washing machine, regardless of its condition. HMRC had published guidelines indicating that when such concessions were given for old equipment, and the concession was given without regard to model, condition etc, the reality was that the retailer was giving a discount of £50 on selling the new product, making the customer happy because he had got rid of the old product and had not self-evidently just thrown it away, and thereby hopefully boosting sales for the retailer.

5. There was no dispute between the parties that the VAT treatment was relatively clear once the facts had been examined, and once it was possible to determine whether there really was a part-exchange transaction, or whether the "allowance on the old equipment, regardless of its identity and condition" was a cash discount. In the event that the analysis here is that the transaction was a part-exchange transaction, there does in fact remain a quite difficult VAT question, which is how the Appellant should value that element of the consideration. We will revert to that below.

6. We should add that the amount in contention in relation to the particular VAT period involved was the relatively trivial amount of £1,236. The greater significance of the Appeal was rather to establish the point of principle, which was likely to apply in relation to many other similar transactions.

The facts material to the part-exchange or discount issue

7. Since no evidence was given on behalf of the Appellant, we had to base our understanding of the facts on a few letters that had been written by the one time Finance Manager of this area of business, namely Donna Bartram. Unfortunately we find this information somewhat confused.

8. One description of the steps in the transaction was given by Donna Bartram in a letter to HMRC of 6 July 2012, as follows:

> *"We would normally quote a school for new equipment and this would relate to our managed service lease agreements. At the quote stage the sales manager would perform a site survey and then send the school a letter and quote based on what equipment is required. Within this quote it would normally detail any agreement made between the school and [the Appellant] including any buy back deals. The buy back deals were a "discount" or "sweetener" in order to get the order approved. We would agree a set amount for the equipment and would never look at each piece of equipment in detail to find its worth. Once the new equipment was installed, the old equipment would be taken back to our warehouse and a credit note and cheque would be issued to the school. The old equipment would be serviced and placed on eBay for sale. We would then account for the VAT on any sale achieved. Admittedly a lot of the equipment bought back from schools is still sat down in the warehouse, even years after the orders were installed. I therefore believe that we have treated the bought-back equipment in accordance [with the HMRC guidance in relation to the discount analysis].*

9. HMRC had obviously referred to their guidance that had indicated that the discount analysis could and should be adopted where:

> *"a fixed allowance is offered;*
>
> *irrespective of the nature of the item traded in;*

for any item of a particular class without regard to make, age, model or condition;

for any item of a particular class or make irrespective of age, model or condition;

provided that no attempt is made to value the traded-in goods and there is no reason for the goods to be accepted other than for trade promotion (which would not apply where prior arrangements have been made for the traded-in goods to be reconditioned or sold)"

Donna Bartram had concluded that HMRC's objection to the transactions effected by the Appellant was that the discounts given had not been "fixed amounts", and she contended that the Appellant's practice actually strengthened the Appellant's case. It was then said in the Notice of Appeal that:

"We do not think this [i.e. the distinction between fixed discounts and discounts based on individual contracts] is relevant and in fact strengthens our case. A higher value is generally attached to the items being "part exchanged" on larger contracts precisely because the contract is larger. There is no relationship between the value at trade-in for the goods and the value (if any) of the goods themselves. This is in line with normal commercial practice of discounting larger contracts by a larger amount."

10. The only difficulty with the argument just quoted is that we were shown the table of the percentages of discount given in respect of seven deals, where the percentage discounts, and the gross value of the order sold, were all listed. Somewhat at variance from Donna Bartram's assertion just quoted, the table illustrated that in the seven deals, by far the largest deal (by a factor of about four in relation to the second largest deal) attracted the second lowest discount, at 4.78%, and the second smallest deal attracted the largest discount of 12.45%.

11. Another odd point was that, beyond the remark in the letter quoted in paragraph 8 above to the effect that the old equipment was "then serviced and sold on eBay", Donna Bartram provided a valuation of the equipment that had been taken back, and in some way she had calculated that it had been worth 44% of the allowances that had been given for it.

12. Another fact that we noticed was that in one particular deal a trade-in value had been given of £100 for each old projector, and the letter from the Appellant's salesman had obviously proceeded on the basis that 15 old projectors were being traded in because the financial calculations (designed to sell the deal), indicated implicitly that the school would receive £1,500 for the trade in of the old projectors. It seems that eventually the school only traded in 13 projectors and so received £1,300. We accept that in one sense this may not be damaging in that it indicated that a fixed allowance was being given for each projector, but if the total discount was said to be just a sweetener to secure the main sale, it seemed a bit odd that the trade-in allowance was reduced when 2 projectors were retained or for some reason not traded in.

13. We do note the claim by Donna Bartram that she said that in all sales on eBay, the Appellant had only received about £2,000. How that squared with the valuation that she put on the traded-in items, referred to at paragraph 11 above, where the valuation at 44% of the "allowances" had been a figure of £5,390 we are not entirely clear.

14. The factor that we consider decisive in addressing the question of whether the trade-in prices had nothing whatever to do with the old items taken in by the Appellant, is the feature that while Donna Bartram claimed that the percentage discounts were said to increase as the size of the orders increased, the table of discounts utterly failed to confirm this claim. Indeed it indicated the reverse. Our finding of fact, admittedly made more difficult by the fact that no actual evidence was given, was that the trade-in allowances were calculated by reference to the basic specification of the products traded in. We then suspect that the respect in which the traders paid no regard to item-by-item valuations was that the Appellant took the rough with the smooth. Accordingly nobody bothered to ascertain whether all 15 or 13 projectors worked. Any that were broken beyond repair would be thrown out, or conceivably be stored for spares. But a good percentage would doubtless work, and might be sold. But that still leaves us suspecting that better trade-in values would have been conceded for old items that had, for instance, been "top of the range", whereas far lesser allowances would have been conceded for cheap and virtually worthless old equipment.

15. Whatever the basis of calculating the allowances, the one factor that appeared not to govern the calculations was that greater discounts were given for the larger orders, as Donna Bartram had claimed.

The managed service lease agreements

16. We mentioned above that during the hearing a particular fact emerged that appeared to us to be material, which had earlier been ignored. This was the point, hinted at by Donna Bartram's reference in the letter quoted at paragraph 8 above, to the effect that the products were provided (it was not clear whether this was invariably the case or not) on a "managed service lease basis". This appeared to mean, and other documentation produced during the course of the hearing plainly confirmed this, that the new equipment was not actually sold to the schools but sold to BNP Paribas who then leased it to the school. The particular significance of this is that it followed that if the gross price for the new equipment was 100, and 10 was being offered for the equipment bought back, the new equipment was clearly sold to BNP Paribas for 100; the rentals charged against the school all charged a rental equivalent of 100, and the 10 allowance paid by the Appellant was paid straight to the school. Indeed the school received the 10 at the outset, and certainly not just in the form of marginally reduced rentals. It therefore followed that the transactions were not really part-exchange transactions at all. This was of course confirmed by Donna Bartram's statement in the paragraph that had already referred to the leasing transaction (referred to for some reason as the "managed service lease agreements") as culminating in the Appellant sending a cheque directly to the school, effectively as the quite separate purchase price for the old equipment.

Our decision on the "discount" point

17. In the light of the conclusions reached in paragraphs 14 and 15 above, and indeed fortified by the observation in paragraph 16, we conclude that the Appellant's claim that the transactions were just discount sales, with the new equipment just being treated as being sold for the "net cash amount" is unsustainable. That claim is undermined because we do consider that in material respects the price given for the buy-back items was influenced by the general nature of what was bought back. Insofar as the new items were sold at the gross price to BNP Paribas, with the allowance for the old equipment being paid directly to the school, there would obviously be a further grave difficulty in somehow reaching the "discount" analysis.

The further issues that we must consider

18. Reverting to the possibility that some of the new equipment may have been sold directly to the school (i.e. without the interposition of BNP Paribas), whereupon the one single cash price might have been reduced from our example figure of 100 down to 90, we must then decide how the value of the non-cash consideration received by the Appellant should be valued. We do not of course actually know whether the Appellant ever effected a transaction on this basis, i.e. of receiving just the net cash plus the value (however calculated) of the exchanged equipment, but we will still consider it since this has a bearing on the calculation of the total consideration received by the Appellant on the "part-exchange" analysis which was assumed to be one possible issue in this Appeal.

19. Our understanding of the law, particularly in the light of the decision of Lord Justice Chadwick in the *Lex Services* and the *Bugeja* appeals, is as follows. If the transaction between the parties has placed a value on the trade-in item, then that value is taken to be the consideration received by the supplier, i.e. the Appellant in this case, that is to be added to the cash element. If no price has been put on the trade-in item, then the amount of the consideration is measured by the subjective value of the consideration received by the Appellant. In the *Bugeja* case, the appellant charged £20 on selling someone a video. If, however, the customer returned a video that they had earlier bought from the Appellant (clearly established by some stamp on the video), then the new video would be supplied for £10 plus the return of the earlier one. HMRC contended that the new video was still supplied for VAT purposes in that situation for £20. The Appellant's contention had roughly been that since he threw away about one third of the returned videos, and he (as the trader) could anyway buy brand new versions of the ones being returned for only £3, the realistic value to him of the "buy-backs" was £2 each (i.e. nil for 1 out of 3, and £3 for the other 2). That was therefore the "subjective valuation" of the consideration to Mr. Bugeja. While that figure had been treated as the correct measure of the non-cash consideration by the Tribunal and the High Court, Lord Justice Chadwick concluded that since the buy-back video was given in place of the "extra £10", £10 was the measure of the value of the non-cash element of the consideration, put on the transaction by the parties.

20. Similarly in the *Lex Services* case, the buyer of the new car was given a trade-in allowance of £2,000 on the old car, but the contract then clarified that the true value of the old car was £1,400 and the balance of £600 was effectively discount.

Accordingly if the whole transaction had to be reversed, and the old car had been sold by Lex Services so that Lex Services had to reverse the transaction by paying back the cash value of the old car, it would only have had to refund to the counter-party £1,400 and not £2,000. But the £2,000 was still the cash value put on the non-cash element of the consideration by the parties for VAT purposes.

21. Those two conclusions were based on the proposition that the transaction between the parties had placed a price on the value of the non-cash consideration (£10 and £2,000 respectively), and it must inevitably follow that that has been done in this case. It is absolutely clear that the contract price for the new equipment was specified at its gross level (£100 in our example), and whether the Appellant ended up supplying the new equipment for £100 reduced by the £10 (i.e. for £90 plus the trade-in item), or whether it sold the new equipment to BNP Paribas for £100, and actually passed cash of £10 straight to the school, all those figures put a cash price on the consideration. Accordingly we cannot look at how much the trade-in items were subjectively worth to the Appellant, in just the way that the appellant in the *Bugeja* case could not calculate the subjective value of the trade-in video at merely £2. He had put a cash price on the amount of the non-cash consideration and that governed the valuation of the non-cash consideration for VAT purposes.

22. There is one other matter that we should mention, though we will also indicate why we consider it to be immaterial on the facts of this case.

23. The Appellant's basic claim in this case has been that the trade-in items were valueless, and that the allowance for them was the equivalent of a discount. We have not been able to accept that claim on the evidence. If, however, the Appellant substantiated that it just took the old equipment away and scrapped it (or otherwise complied with the guidance to which HMRC appear to adhere) so that the price for the new equipment is then fixed at a "discounted £90", there is no particular complication if the transaction is a two-party transaction just involving the Appellant and the school. It presumably also follows that if BNP Paribas is interposed, and the new equipment is sold at a discounted £90, and the rentals are geared to the £90, not the £100, there is no great complication. If, however, the new equipment was sold to BNP Paribas at £100, and the rentals were based naturally on the £100, with £10 being paid straight to the school, it would appear that careful consideration would have to be given to some of the "cash-back" cases such as *Elida Gibbs* and several others referred to in Lord Justice Chadwick's decision referred to above. We consider this irrelevant on the facts of this Appeal, because the £10, in our example, paid to the school was demonstrably paid for the trade-in goods, and it is not remotely worded as a "cash-back" incentive, paid by the Appellant, that might conceivably result in some adjustment of the consideration received for the goods. As we indicated at the beginning of this decision, we consider this to be a relatively complex matter, which it would be inappropriate to consider since it is not actually raised by the facts in this Appeal, and we were certainly not addressed in relation to it.

24. One other point that also appears irrelevant in this Appeal is worth mentioning. This is that, had the white boards been supplied by the Appellant to taxable persons, who were liable to VAT in respect of the supply in the reverse direction, then that would have eliminated the significance of the "discount/part-exchange" issue altogether. Even, in other words, on the analysis that the new equipment had been

sold for £100, if the old equipment had been bought from a taxable person for £10, the position would have been the equivalent of the new equipment having been sold at £90. On the facts here, this is irrelevant. No consideration was given by the parties to whether any of the local authorities should have accounted for VAT on supplies of surplus school equipment, and so we ignored this issue.

Our decision

25. Our decision is that VAT should have been paid on the total of the cash element of the consideration and the value of the part-exchange item, and that that value was established by the transaction terms between the parties, in the sense that if the sale price had been reduced from £100 to a net £90, the non-cash consideration had to be worth £10. The Appeal is accordingly dismissed.

Right of Appeal

26. 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.

JUDGE HOWARD M. NOWLAN

TRIBUNAL JUDGE

RELEASE DATE: 8 November 2013