

# Customs & Trade in Israel

## A Legal Newsletter

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### **The Court Accepted the Importer's Position Regarding the Admissibility of Discounts for the Purpose of Import Duties**

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#### **Case Facts:**

Israeli mobile network operator Pelephone purchased and imported BlackBerry cellphones to Israel from a supplier who owns the rights to the BlackBerry brand. Pelephone signed a framework agreement with the supplier, who provided the phones it imported to Israel.

As part of the agreement between Pelephone and the supplier, with each order the company was entitled to receive a number of additional devices, up to 5% of the original order, free of charge. The additional phones were referred to as a Swap Pool Inventory ("Swap") in the agreement, and were provided to the company in exchange for it waving the supplier's warranty for the appliances and related equipment purchased from the supplier.

In addition, as part of a sale promotion program by the supplier, called the "Handheld Purchase Program" ("HHPP"), the company was entitled to purchase an additional 10% of the devices originally ordered at a 50% discount for sale promotion purposes. The HHPP was offered to all the supplier's commercial clients throughout the world.

During the release of a shipment of devices purchased through the HHPP, Pelephone declared through its customs agent a transaction value based on the actual price paid for the devices. In addition, the company declared the full number of imported devices, including the Swap devices.

In 2013, the Customs Authority sent Pelephone an updated deficit notice amounting to 1,578,623 ILS. The company submitted an objection to the Customs Authority regarding the deficit notice and additional charges, but the Customs Authority rejected its claims, and the company therefore turned to the court.

#### **Parties' Arguments:**

Pelephone sought declaratory relief from the court stating that the value for purchase tax on import of cellular phones is the price actually paid to the foreign supplier, as per sections 130(1) and 132(a) of the Customs Ordinance.

Alternately, the company stated that if the court found that the actual price paid for certain phones is not to be considered the value for purchase tax purposes, the company asks that the court declare that

the shipment for which the deficit notice was issued is subject to section 3 of the Indirect Taxes Law (Overpaid Tax or Underpaid Tax), 1968.

Alternatively, the company stated that if the court found that section 3 of the Indirect Taxes Law does not apply, the company asks that the court declare that the VAT and fines included in the deficit notice are illegal, and therefore void.

On the other hand, the Customs Authority argued that under section 132 of the Customs Ordinance the value of goods for customs purposes is the price paid or to be paid, subject to several overlapping conditions. If the transaction price was affected by certain limitations placed upon the goods, alternate valuation methods must be used. The Customs Authority claimed that Pelephone did not meet the requirements of section 132 of the Ordinance, and the value of the transaction should not be accepted as the value for customs purposes in the case of goods imported as part of a warranty.

In addition, the Customs Authority claimed that Pelephone failed to submit its request to the Committee for Indirect Tax Returns, and its claim should be rejected for lack of exhaustion of remedies before the committee.

### **The Court's Ruling:**

#### **Swap devices:**

The court determined that under the agreement between Pelephone and the supplier, the supplier sought to avoid granting warranty to the devices it sold to the company, and added an additional 5% of the amount of devices ordered for the purpose of replacement parts and devices for defective devices. The provided devices came complete with their device kits. In other words, 5 extra kits substitute the warranty, and the value of the entire transaction is 105 devices for the price of 100 devices.

The court ruled that this is a financial transaction like any other, with the value of the absent warranty evident in the devices' price. The agreement was not exclusive to Pelephone, the supplier signed similar agreements with other Israeli mobile network providers that worked the same supplier. Therefore, the restriction of holding reserve device kits is not one required by Israeli law, which constitutes a restriction under section 132(b)(1). Even if the Customs Authority is correct and it is indeed a restriction, the court believes a 5% difference is a restriction which does not significantly impact the value of the goods, especially since the transaction in question involves a very large quantity of devices.

The second condition under section 132(b)(2) is that the sale or price of the goods is not subject to any condition or exchange which cannot be valued for the purpose of determining the goods' value. In this case, the court believes that the value of the Swap devices may be estimated, as they are identical to the rest of the devices and have a clearly identified purpose of use, as stated in the agreement between the supplier and Pelephone. The court therefore ruled that in this case the condition in section 132(b)(2) of the Customs Ordinance was met as well.

#### **HHPP devices:**



The court determined that according to the supplier's policy, purchasing HHPP devices is possible only **after** the purchase of 20 or more devices, for promotional purposes. It is therefore evident that the supplier itself views the sale of the HHPP devices as a continuation of the previous device purchase transaction. The amount of HHPP devices each client may purchase is reliant upon the amount of devices previously purchased - 10% of that amount. The purpose of the HHPP device sale is to promote sales, something which is in the hands of the supplier's clients, in order to increase device sales.

To the court's point of view, the sale of the HHPP devices is actually a 5% discount on the transaction that preceded the purchase of the HHPP devices. It is irrelevant if 10% of the devices are sold at a 50% discount or if 5% are given for free, the mathematical result remains the same. Here as well the supplier has a commercial consideration, as a sale which includes 5% of the devices for free for promotional purposes would result in the sale of less devices, whereas 10% of the devices previously purchased results in the sale of double the amount of devices through the HHPP.

The court determined that that the supplier's restriction upon the sale of the HHPP devices does not significantly impact the price of the goods, as it is essentially 5% of all devices in one transaction, and the company would have had to promote sales either way. If the promotion would have been performed without the HHPP devices, Pelephone would have sold less devices. But as the supplier's goal is to sell as many devices as possible, it was willing to sell the HHPP devices at a discount, which leads to the conclusion that from the supplier and the company's points of view, the restriction does not significantly impact the value of the goods.

The court therefore ruled that the purchase price which the company declared for the HHPP devices is the actual transaction price.

**Conclusion:**

The court granted the main relief sought by Pelephone, declaring that the value for purchase tax purposes on import of cellular phones is the price it actually paid to the foreign supplier. The court ordered the Customs Authority pay Pelephone legal expenses amounting to 100,000 ILS.

[TA 1356-01-15, **Pelephone Communications Ltd. V. Lod Ben Gurion Airport Customs House**, ruling given on 27.8.18. Presiding judge: Zecharia Yeminy]

**The above review is a summary. The information presented is for informative purposes only, and does not constitute legal advice.**

**For more information, please contact Adv. Gill Nadel, Chair of the Import, Export and Trade Law Practice.**

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