

Customs & Trade in Israel

A Legal Newsletter

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The Customs Authority Rejected a Discount - The Court Approved It

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A recent ruling (TA 46492-01-16) given on 4.6.20 by the Lod District Court is highly significant for the customs field. In the following article, we will review the ruling regarding discounts given to a car importer, as well as its ramifications.

The car importer is Delek Motors, the Israeli importer of Mazda vehicles. Delek received a discount for the purchase of spare parts, subject to meeting annual goals. The agreement which includes the discount states that if the importer fails to meet the target purchases, it will be required to reimburse the supplier with the discount's value. Later agreements omitted the requirement of returning the value of the discount in case of failure to meet the goals.

The Tax Authority issued a tax notice to the importer, as it viewed the discount as a conditional discount, which according to the Tax Authority does not qualify as a discount for customs purposes. The Tax Authority claimed that under section 132(b)(2) of the Customs Ordinance, the transaction value is not admissible if the sale of the goods or their price is subject to any condition or recompense that cannot be estimated for valuation purposes. The Tax Authority argued that at the determining date (the release of the goods) it was impossible to ascertain whether the importer will meet its target purchases; therefore, the conditional discount is not admissible and the goods' value is their full price without the discount.

On the other hand, the importer argued that the discounted is a permanent discount independent of the purchase targets, and that contrary to the agreement with the supplier the importer never reimbursed it with the discount value, even when it failed to meet purchase targets. The importer claimed that this proves the parties intent that the discount will be granted regardless of meeting the target purchases. In addition, the importer argued that the Tax Authority's position is contrary to international agreements, and results in a paradox, for if a discount is a quantity-based discount received in advance - the Tax Authority will reject it, claiming it is an inadmissible conditional discount; and if the discount will be granted post factum, the Tax Authority will argue that it is impossible to retroactively amend the declared price. In effect, this results in voiding any possibility of an importer receiving a quantity-based discount.

The court ruled in favor of the importer, rejecting the Tax Authority's position.

In its ruling, the court offered a detailed analysis of the both the factual aspect (whether there was indeed a conditional discount in this case) and the principal legal aspect (is a conditional discount admissible). In the principal legal aspect, the important aspect for our purposes, the court ruled in

favor of the importer, ruling that if the discount was indeed conditional, and the importer would have been required to return it if it failed to meet the target purchases - the discount is still admissible for customs valuation purposes.

The court based its ruling on various sources, including the Supreme Court's ruling in the Amcor case, determining that the basic guiding principal is that customs duties should be levied based on the actual price paid for the goods, even if the price includes a conditional discount, and even if it is uncertain at the time of import that the condition will be met. All the above is assuming the discount is "set and given in advance according to a predetermined, set framework". The reasoning of the ruling is that the basis of customs valuation should be set according to the World Trade Organization's guiding principal - goods' value should be determined by the actual transaction price.

The court did not determine whether the Tax Authority may reexamine the declared price and issue a retroactive tax assessment in a case in which an importer reimburses a supplier for a conditional discount. As noted above, in the case brought before the court the Tax Authority did not claim the discount was returned, rather that the discount is a conditional discount that includes a condition whose value cannot be estimated. Even so, the court noted in passing that if the discount was returned to the supplier through an increase in the price of subsequent shipments, the Tax Authority would automatically receive the tax differences as a result of the increased import value in the following shipments. Either way, the court did not provide any clear, binding statement in the matter.

The court criticized the Tax Authority for creating a hybrid that does not conform to a single position: on the one hand, the Tax authority argued that the condition's value cannot be estimated and therefore is not admissible; on the other hand, it charged the importer with a tax deficit equal to the amount of the discount, indicating that it's an exact amount. One cannot have it both ways.

A few commentary notes on the above:

First of all, it is important to note that the Tax Authority issued a guideline over a decade ago stating that for a discount to be admissible it must be set, final and unconditional. The legal deliberation in Delek's case directly clashed with this guideline, ultimately rejecting it, and the case is therefore highly significant in the principal aspect of the matter.

The ruling continues the principal direction expressed by a three-judge panel at the Lod District Court in the Pelephone case, where the court ruled that goods provided without charge for warranty purposes or sale promotions are not dutiable, contrary to the Tax Authority's position. This is true in cases where it may be proved that the goods' value is included in the framework of a commercial transaction common in the field, where small quantities of goods are supplied free of charge alongside larger quantities of goods paid for in full, for warranty or sale promotion purposes.

The spirit of the Pelephone ruling is evident in our ruling as well, although no direct reference was made. The court sought to adapt an essential test that examines the economic value of the transaction and its general characteristics, presenting a willingness to draw a line in the sand regarding later transactions as well and accept a situation in which the reimbursement of the discount will be performed through a future transaction, at which point the Tax Authority will receive the difference in import duties.

As this is a precedential ruling regarding conditional discounts, it may be assumed that the Tax Authority will appeal the decision before a three-judge panel of the Supreme Court. Therefore, it can be carefully assumed that the final word has yet to be said in the matter. While the ruling of a District

Court is not a binding law, it has been ruled in the past that an assessee may rely on a District Court ruling so long as it was not overturned by the Supreme Court, and the circumstances of the case are similar.

Importers must therefore consider whether to rely on the District Court ruling in the Delek Motors case regarding conditional discounts, hoping that the ruling will be upheld by the Supreme Court, or opt for the conservative approach and await a final, binding ruling on the matter.

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

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