HMRC - VATSC30500 - Consideration: Definition Of Consideration

Consideration is a payment for the supply of goods or services. It is usually a payment in money, but can also be of a “non-monetary” nature, such as goods or services supplied in return.

Consideration and profit

Consideration should not be confused with profit. Whether a payment yields profit or loss is immaterial and has no bearing on whether or not it is consideration. This was brought out in Heart of Variety (LON/75/15) where the tribunal said that:

the concept of consideration and profit are wholly different, and the fact that a trader makes no profit on a supply does not, in our view, mean that there is no consideration for it.

Legal definition

There is no definition of consideration in either the EC Principal VAT Directive or the VAT Act 1994. In the UK, the meaning was originally taken from contract law, but the European Court of Justice (ECJ) has confirmed that the term is to be given the Community meaning and is not to be variously interpreted by Member States. The Community definition used in ECJ cases is taken from the EC 2nd VAT Directive Annex A13 as follows even though this Directive is no longer in force:

the expression “consideration” means everything received in return for the supply of goods or the provision of services, including incidental expenses (packing, transport, insurance etc), that is to say not only the cash amounts charged but also, for example, the value of the goods received in exchange or, in the case of goods or services supplied by order of a public authority, the amount of the compensation received.

The phrase in return for the supply is interpreted to mean that there must be a direct link between the supply and the consideration.

Therefore in order that a supply for a consideration can be made, there must be at least two parties and a written or oral agreement between them under which something is done or supplied for the consideration. There is a direct link between the supply and the consideration because the supplier expects something in return for his supply and would not fulfil his obligation unless he thought that payment would be forthcoming.

ECJ cases on direct link between supply and consideration

The requirement for a direct link is brought out in three ECJ cases.

The Dutch potato case

The case of Staatssecretaries van Financien v Cooperatieve Aardapplenbewarr-plaats ((1981) ECR 445; (1981) 2 cmlr 337) involved a co-operative providing cold storage facilities to its members who had the right to store potatoes because of the share each member held in the co-operative. Charges were normally made to the members for the storage but for two consecutive years no charges were made. This resulted in a drop in the value of the shares (reflecting the co operative’s reduced profits because of the lack of storage fee income). The Dutch tax authorities argued that the reduction in value of each members share was effectively consideration for the storage which had been provided for no fee. The ECJ rejected this argument. There was no direct link between the services of storage and the decrease in share values. Additionally the reduction in value of the shares could not be equated directly to the cost or any other measure of the value of the services provided.

BAZ Bausystem Gmbh v Finanzamt Munchen Fur Korperschaften

Here the ECJ held that interest awarded to an undertaking by a judicial decision was not consideration where the reason for the award was that the balance of the consideration for services was not paid by the due date, because it had no connection with the services provided and did not constitute consideration relating to a commercial transaction - it was simply compensation for the delay in payment.

Apple & Pear Development Council (APDC), (ECJ (1988) STC 221; (1988)2 CMLR 394)

The Council is a statutory body formed to promote the sale of apples and pears. Commercial growers were required to register with the council and pay an annual levy. The industry as a whole received the benefit of its promotional activities. The point at question was whether the levy was consideration for the promotional activities. The European Court held that there was no direct link between the supply made and the “payment” received, that is benefit, was not directly related to payments made, and individual growers were obliged to pay the levy, regardless of whether they benefited.

The points which demonstrated this were:

The benefits of APDC’s services accrue to the whole industry, individual growers deriving benefits indirectly from those accruing to the industry as a whole.

There was no relationship between the level of benefits which individual growers obtained and the amount of charges they were obliged to pay.

The charges were always recoverable from each grower as a debt due to APDC regardless of whether or not a given service conferred a benefit to them.

Tolsma

Another ECJ case, Tolsma C-16/93 (1994 STC 509), confirmed that for us to see a supply there should also be ‘reciprocal performance’. See VATSC50400 for details of this case.

Other points from ECJ cases

Other points on consideration which can be drawn from these cases are:

Consideration is to be defined widely to bring within the tax everything which the taxable person receives as consideration for the goods or services supplied.

The consideration must be capable of being expressed in money.

In some circumstances a person may pay for a supply to be made to someone else, for example, where a holding company pays for items such as fuel and electricity which are supplied to its associated companies. As long as there is an agreement between the supplier and the recipient there is still a direct link between the supply and the consideration. However, the supply is to the recipient, not to the payer.

Next page