**IN THE TAX COURT**
**AT SUVA**

**Action No. HBT 08 of 2013**

**IN THE MATER** of the Income Tax Act 1974

**AND**

**IN THE MATTER** of section 82 of the Tax Administration Decree 2009 (Decree 50 of 2009)

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| **BETWEEN** | : | **MATASAU HOLDINGS LIMITED**<br>*Applicant* |
| **AND** | : | **CHIEF EXECUTIVE OFFICER, FIJI ISLANDS REVENUE AND CUSTOMS AUTHORITY**<br>*Respondent* |
| **Coram** | : | The Hon. Mr Justice David Alfred |
| **Counsel** | : | Mr B Solanki for the Applicant<br>Ms F Gavidi (Ms S Nasiga with her for the Respondent |
| **Dates of Hearing** | : | 11 and 22 February and 17 March 2016 |
| **Date of Judgment** | : | 18 November 2016 |

# JUDGMENT

1. This is the Applicant's Amended Application for Review of the Respondent's decision dated 23 September 2013. It was originally heard by Kotigalage J, but the Applicant desired it to be heard de novo before me.

2. The hearing commenced with the director of the Applicant, Christopher James Donlon (PW1) giving evidence. He said he has been a director since 2003 and a shareholder of the Applicant. Sustainable Forest Industries Ltd (Sustainable) is the other shareholder.

3. PW1 said Revenue conducted on audit of the Applicant in September 2012. The issue was regarding the transfer of finance of F$6 million(m) provided to the Applicant by the original shareholders and approved by the Reserve Bank of Fiji (RBF). They were bewildered. The repayment of $6m was not made and was then converted into equity of the Applicant. The Applicant and Sustainable merged so that Sustainable became the holding company of the Applicant. The liabilities and assets remained within the Applicant and Sustainable took control of the Applicant. The Respondent's Additional Documents (RAD) tab 1 page 9, note 15 shows $6,036,705 which the Applicant needs to repay. Page 16, note 15 shows the advances totaling $6,036,705. The Applicant owed these 3 amounts.

4. The RAD tab 4 was the letter from Ernst & Young to the Financial Controller of the Applicant confirming the advances.

5. The Respondent's Documents (RD) tab 5 was the Deed dated 1 June 2011 (Deed), which was to settle disputes between the parties thereto. This was a deed of settlement of various liabilities. Sustainable purchased the debt and the Applicant paid $400,000 to be paid by the parties as stated in clause 2.1.

6. PW1 said he received the assessment and the notice of amended assessment. The total tax payable was $2,004,788.08. He signed the notice of objection which was disallowed. The Applicant's position is that the loan was forgiven. He said they (lender) never forgave the loan in black and white. The debt was taken over and the Appellant does not owe money to Pacific Resources.

7. PW1 said Exhibit A9 were 2 receipts from Parshotam & Co. (solicitors), one for $360,000 in favour of Feint Investments Limited (Feint) and the other for $40,000 in favour of Sustainable. Both were to the credit of Ross Davision Group, their client. Feint and

Sustainable received approval from the Ministry of Finance during the restructuring exercise. He said Murray Goodman is a representative of Pacific Resources and of himself.

8. During cross-examination, PW1 said he only owned one share in the Applicant, Feint owned the majority of Sustainable's shares. In Feint, he (PW1) is the majority shareholder. He said he has controlling interests in these companies of which he is a director. He said the Deed reflects the arrangement.

9. When questioned by Counsel for Revenue wheather clause 3 of the Deed suggested a waiver of debts owed by the Applicant, PW1 denied this and said they were transferred to the Donlon Group. He said the qualification of the auditors in their report is that they were unable to obtain confirmation of the shareholders' advance of $6m. There was a shareholders' deficit. He denied the debt owed to all 3 companies has been waived by the Deed. He also said that the accountants state they were unable to obtain evidence of the receivables of the Applicant and Feint. The qualification was done by an independent auditor. He has financial statements to show the debt is still owing. The loans were to be converted into shareholding rights in the Applicant.

10. PW1 said the debt was transferred to Sustainable. There is an obligation for the Applicant to pay Sustainable. There is a separate legal agreement of 2003 but it is not in evidence today. Shares were not issued to the 3 companies in the Applicant and Sustainable. It was not correct that the debt has been forgiven.

11. PW1 said re: Exhibit A9, that those were the only payments to the Ross Davision Group. It was not correct there was a gain of $5.6 to the Applicant.

12. When PW1 was re-examined, he said he signed the financials without being aware of the qualification.

13. With this the Applicant closed its case, and the Respondent opened its.

14. The Respondent's witness was Ms Tulia Takala (DW1), principal auditor in Revenue. She was involved in the audit of the Applicant and was a senior auditor then. In 2011, she had to audit Sustainable Mahogany Industries Limited. She discovered that it had a related transaction with the Applicant and Sustainable and Feint. All 3 companies had PW1 as their principal shareholder. It was found out a loan from 3 companies were made to the Applicant.

15. DW1 said the audit revealed no profit had been made as the company made losses for all the 6 years. Revenue was not given any document to verify the loan or its repayment. Neither was the 6 years period depicting the loan injected into the Applicant. Then Revenue found out there was a Deed (Exhibit A5) whereby $400,000 was paid by the Donlon Group to the Ross Group so that all loans to the Applicant might be forgiven and a controlling interest might be taken by the Applicant. The Deed confirmed the debt had been forgiven. The parties are the Donlon Group and the Ross Group. Revenue looked at the financials and discovered that 3 companies were stated as lenders but in fact Adalec Trading Company Limited (Adalec) had been deregistered, Pacific Group Resources Limited, New Zealand (PGR) had been struck off by the New Zealand Registrar of Companies and Mr Murray Goodman was a non-resident (see Exhbiit A2 page 18).

16. DW1 said the findings of their audit found $400,000 was a gain to the Applicant because of the forgiveness of the debt of $5.6m. This is an economic benefit to the Applicant meaning an amount not paid off is wealth it can use. A loan is neither a gross profit to the borrower nor a tax deduction to the lender. The gain made by the Applicant from the forgiveness of the debt is $5.6m.

17. DW1 said the independent external auditor all the years made a qualification of the financials. Exhibit A1 page 6 is their qualification which means the external auditor

cannot validate or confirm an advance of $6m. The independent auditors cannot confirm $6.3m receivables and subordinated debts of $5.9m.

18. DW1 said Exhibit A6 is the assessment issued to the Applicant. The income is $5.6m, there is no tax deducted at source and penalties and total tax payable is $2m. The Applicant filed an objection and a decision was made by the objection review team. The forgiveness of debt is a gain to the borrower under section 11 of the Income Tax Act (ITA).

19. Under cross-examination, DW1 said PGR and Murray Goodman are parties to the deed as related to Revenue by PW1 who also gave them the receipts for the $400,000. The 2 receipts to the credit of Ross Davison Group do not mention Muray Goodman nor PGR. The objection decision is independent. The loan has been forgiven. It has not been assigned to Sustainable.

20. Referring to Exhibit A8, DW1 said there was no tax on the gain on the loan forgiven.

21. Adalec was deregistered prior to 1 June 2011 as it was not trading. Adalec had executed the Deed. DW1 said Murray Goodman and PGR are part of the deed even if their names are not mentioned. She concluded by saying her assessment of the Applicant is correct.

22. In re-examination DW1 confirmed Murray Goodman and PGR are part of the Ross Davision Group.

23. With that the Respondent closed its case.

24. On the next date of hearing, Counsel on both sides provided written submissions.

25. Counsel for the Applicant then made his oral submission. He said the main issues in dispute are (i) whether Sustainable can convert the amount into shares.

(ii) Even if forgiven the amount is not taxable. He said section 11(a) of the ITA is extraordinary. There is no case on forgiveness of debt in Fiji. The amount of the penalties is not being questioned; only whether the Applicant is obliged to be penalized. The debt has not been forgiven and Counsel submitted that the Application should be allowed and the penalties removed.

26. Counsel for Revenue then submitted. She said there was no written agreement to suggest that the amount of $6m will be repaid. The evidence in the trial and the deed ($400,000) is payment at a discount. The remaining $5.6m is a gain. The auditors' qualified accounts mean there was no documentary evidence to show liability in one and receivable in another. There was no documentary evidence that the debt will be repaid. There was no evidence that the debts has been converted into shares. No shareholding rights were given to the 3 entities who injected the $6m.

27. There should be an agreement in place to enforce the obligation particularly the time within which to repay. The penalties were lawfully imposed at 20% under section 46 of the Tax Administration Decree. As Revenue has correctly assessed the Applicant under Section 11 the Application should be dismissed.

28. Counsel for the Applicant replied.

29. At the conclusion of the hearing, I said I would take time for consideration. Having done so, I now proceed to deliver my judgment.

30. The pivotal issue here is whether the loan of $6m has been repaid in full by a payment of $400,000. In other words the question is whether the Applicant needs to repay the balance of the loan, *i.e* the sum of $5.6m (sum). The subsidiary issue is if the sum does not need to be repaid is it a gain upon which tax is assessable.

31. I shall start by perusing the Deed. The background makes for instructive reading.

A. states " *The parties hereto have for some years now have had considerable financial arrangements and dealings between them.*

B. states " *Over the period of the said years the parties hereto have had serious disputes and differences between certain groups and entities. They have now come to a resolution and forever settlement of their various rights and obligations on the term set out in this Deed.*

Clause 2.1 states the consideration for the Deed shall be the sum of $400,000 to be paid by Chris to Ross in 2 sums of $40,000 and $360,000.

32. Clause 4. is entitled "Mutual Releases "and reads as follows:

4.1 For the consideration of this Deed, but subject to the terms herein, the parties hereto release each other from all claims, suits, actions and demands of whatsoever kind and nature (whether done or omitted to be done), actual, contingent or otherwise and the forever release shall continue to subsist notwithstanding any rule of law or equity.

4.2 With respect to clause 4.1 above the Donlon Group undertakes and accepts all those obligations that exist in law and equity to be going to it as an integral and necessarily attached part of the assignments herein.

4.3 The parties shall be deemed to accept and hereby confirm that this Deed constitutes a full and final settlement between them of all matters.

4.4 Without limiting the generality hereof the parties further acknowledge and agree that this Deed can be used as a defence, bar or mitigation in respect of any matters or things now or hereafter arising between them herein.

33. To my mind, it is crystal clear that the entities that made the loans are in effect forgiving any obligation on the part of the Applicant to repay the former the balance sum of $5.6m The 2 receipts are also clear in their import. The 1st states the $40,000.00 is part payment of the settlement deed. The 2nd states the $360,000 is balance payment of the settlement deed. What could the settlement be if not of an outstanding debt. *i.e* the $6m loan (see clause 4.3).

34. The notes to the Applicant's Financial Statements for the year ended 31 December 2010 show at 15. Liabilities of $1,144,098 to Adalec, of $642,561 to Murray Goodman and of $4,250,046 to PGR. These came up to a total of $6,036,705 and are described as Shareholders/Directors Advance.

35. In the notes to the Applicant's Financial Statements for the year ended 31 December 2011, it is now shown that these liabilities have been extinguished for against Adalec, Murray Goodman and PGR the figure '0' appears against each name.

36. There is now a new entry in the name of Sustainable of a liability in the sum of $6,036,705. There is also notation that 'SFIL' has purchased the rights to shares and debt in the company in accordance with the agreements and settlement dated 1 June 2011.

37. One thing stands out here with the utmost clearness and this is there is no longer any obligation on the part of the Applicant to repay the advances (debts) to those 3 entities.

38. With regard to the other thing *viz* the supposed purchase of the debt, I have gone through the Deed with a fine toothcomb but have been unable to discover any purported assignment of the debts (owing to the 3 entities) to Sustainable, nor any purported acknowledgement by the Applicant of any liability/obligation to repay Sustainable any sum whatsoever.

39. On the contrary, clause 7.5 states the payments referred to in clause 2.1 ($400,000) "shall firstly be applied to discharge all loans advanced by the Davision Group to Matasau."

40. Further, the non-production of the agreement of 2003 alluded to in PW1's evidence leads to the inference that if it had been produced it would not have shown the debt is still due from the Applicant.

41. It is therefore as clear as daylight that the $5.6m balance of the loan ceased to be payable because it has been released and consequently is extinguished.

42. I must note Aliz Pacific, the independent auditor of Sustainable reports their qualification in Sustainable's Director's Report for the year ended 31 December 2011 that they were unable to validate nor could they obtain any documentary evidence for "Receivable – Matasau Holdings Limited - $6,036,705.

43. If the Applicant wants the Revenue to believe that the Applicant owed the said sum to Sustainable, what was the difficulty in providing the documents proving such receivable. Further, why has no document been provided to the court showing the Applicant is obliged to repay that sum in full. The absence of such documents points in the opposite direction i.e no obligation exists for the Applicant to pay the sum.

44. If, as I believe to be the case, there is no authority on the issue binding on this court, it is therefore unnecessary to go through the various authorities cited and it is enough if I were to state the conclusion which I have arrived at.

45. I therefore find and I so hold that the debt/loan has indeed been forgiven with the part payment/discount payment of $400,000 and that therefore the $5.6m is indeed a gain to the Applicant.

46. This conclusion necessitates my having to consider whether this gain is assessable to tax. Counsel for the Applicant has not cited any Fijian authority nor any section of the Income Tax Act or Decree which specifically provides for a gain, arising from a debt being forgiven, not to be assessable to tax. The mere statement of DW1 does not have the force of law. I have come to the conclusion that section 11 of the Income Tax Act is wide enough to bring within its remit such a gain. I therefore hold the $5.6m forgiven is a gain which is subject to taxation.

47. From start to finish, the Applicant's evidence, its Counsel's written and oral submissions were all most emphatic "that no debt was forgiven in the first place (para 37 of their

closing submission) and the Applicant still owes the debt but not to the three companies but to SFIL (para 33 of their opening submission). It is therefore a little strange, if I may say so, for the Applicant to then engage in blowing hot and cold by asserting the debt was forgiven but not assessable to tax.

48. The Applicant relies on the House of Lords decision in: *British Mexican Petroleum Co. Ltd v Jackson* [1932] 16 TC 570, but the facts there are distinguishable from those here. There the taxpayer never claimed for one moment that the debt was still outstanding.

49. As I am not advised that the Fijian tax regime has a provision for forgiveness of commercial debts, as is present in the Australian tax regime, I am unable to consider Counsel's alternative submission.

50. Finally, Counsel for the Applicant concedes the rate of and amount of penalties imposed by Revenue are not being challenged. He is merely submitting these penalties should not be imposed. However neither in his written nor in his oral submissions has Counsel shown me why it is contended the Revenue had no legal basis to impose the same. I therefore also uphold the imposition of penalties.

51. In fine, I hereby dismiss the Amended Application, uphold the Revenue's Decision but shall, in the circumstances, make no order as to costs.

**Dated this 18th day of November 2016.**


David Alfred
**JUDGE**
High Court of Fiji