

IN THE STATUTORY TRIBUNAL, FIJI ISLANDS
SITTING AS THE TAX TRIBUNAL

Action No 8 of 2009

BETWEEN: **COMPANY C FROM NEW ZEALAND**

Applicant

AND: **FIJI REVENUE & CUSTOMS AUTHORITY**

Respondent

Counsel: **Mr A Khan, Khan & Company Barristers and Solicitors**
Ms I Ratuvalu, FRCA Legal Unit for the Respondent

Date of Hearing: **Wednesday 10 April 2013**

Date of Decision: **Thursday 16 May 2013**

DECISION

Section 11 INCOME TAX ACT (Cap 201); Sale and Disposition of Property – Section 11(a) Purpose of Acquisition

Background

1. Company C was incorporated under the *Companies Act* 1993 (NZ) on 1 June 2005.¹
2. The Directors of that Company were two brothers who were both citizens of New Zealand.

¹ The purpose of the incorporation will be canvassed later within this decision.

3. Some time on or around 19 July 2005, the Company purchased a vacant block of land at Denarau, Nadi, Fiji (Certificate of Title No 34545, Lot 4 on DP No 8880) for the sum of FJ\$500,000.00.
4. Company C proceeded to construct a five bedroom residential property on that site and sold the completed property on 21 January 2008 for the sum of NZ \$3,650,000.00.²
5. The Respondent raised a Tax Assessment against the Taxpayer, showing income derived through the venture as:

	NZD	FJD
Sale Price	\$3,650,000.00	\$4,412,575.67
Less Land Cost		\$500,000.00
Less Construction Cost:		\$3,675,839.73
Total Cost of Land & Construction		\$4,175,839.73
Net Income		\$236,735.94

6. By Amended Assessment No 1 dated 21 April 2008, the Taxpayer was required to pay \$73,388.14 as income tax.
7. On 29 April 2008, the Taxpayer made a formal objection to the assessment.
8. The Taxpayer seeks the Application of Review of the Respondent's Objection Decision dated 24 November 2008, whereby the Respondent maintained its assessment.

² Included within that price was the amount of \$510,000.00 for chattels identified within the Third Schedule to the Sale and Purchase Agreement.

Grounds Relied On By the Applicant

9. There are two main grounds, upon which the case of the Taxpayer is based:-

(A) The Respondent erred in fact and in law by requiring the Appellant taxpayer to pay \$73,388.14 according to s.11(a) of the Income Tax Act on the ground, given verbally, that the taxpayer was a dealer in properties either individually or via partnership or via company. The Respondent is in error for the following reasons:

(a) The said ground is not a valid and/or legal ground, as the test laid down in the first limb of s.11(a) of the Act is whether the taxpayer is in the business of dealing in property.

(b) According to the first limb of s.11(a), it is not possible to levy taxation on a personal property transaction on the basis that a taxpayer is in the business of dealing in real property, and it is not possible to levy taxation on a real property transaction on the basis that the taxpayer is in the business of dealing in personal property. Whatever the subject property, the taxpayer must be in the business of dealing in such property in order to be caught by the relevant provision.

(c) The subject transaction was a sale of a property located at Cove 4, Denarau. The Act obliges the Respondent to demonstrate that the Appellant taxpayer was in the business of dealing in personal property, but the Respondent did not do so. The Respondent merely asserted that the Appellant dealt in a property which is immaterial.

(B) The Respondent erred in fact and in law in holding that the Appellant taxpayer was engaged in a scheme or undertaking for the purpose of making profits from sale or real property and therefore caught under Section 11(a) for the following reasons:-

(a) The sale was not an operation of business. The sale represented the frustration of any such scheme or business, because:-

- i. The Appellant taxpayer was unable to secure a residence permit to reside at his property in the Fiji Islands.
- ii. The Taxpayer feared that the financial value of the title of Cove 4 Ltd was insecure by reasons of political movements;
- iii The sale was not an adventure in the nature of trade, or a business deal. The sale did not yield income but capital only;
- iv The sale was the mere realisation of a security and was so intended on the grounds pleaded above;
- v The gain derived does not represent any profiteering by the Appellant taxpayer, there being no over value.

(b) The Appellant taxpayer is not liable to be taxed under the second limb of s.11(a) of the Income Tax Act because he did not acquire the land at CT34545 for the purpose of selling or otherwise disposing of the ownership of it.

(c)The profit or gain derived from the transaction is not taxable under the third limb of s.11(a) because it was not part of a series of transactions and was not in the nature of trade or business.

10. The application is heard in accordance with the relevant provisions of the *Tax Administration Decree 2009* and the *Magistrates Court (Amendment) Decree 2011*.

The Case of Company C

11. This matter was first called on for mention before the current Member on 6 July 2011. On two occasions after that date³, the Taxpayer was cautioned that the matter would be struck out, if there was not some tangible sign that it was actively seeking to prosecute its case.
12. On 4 February 2013, despite the fact that a former Director of the Taxpayer flew from New Zealand to attend the hearing of the matter, still as it transpires, Counsel was unable to commence his case.
13. When the matter was finally heard before the Tribunal, the former Directors of Company C gave their evidence over the telephone.
14. The first witness called was a former Company Director, Mr C. It was his evidence that he had formed the company with his brother with an intention to remain as equal shareholders. It was Mr C who initially funded the purchase of the land at Denarau, by providing \$500,000.00 as capital.
15. According to the witness he sold his shares in the company, because of a change in his personal situation.⁴ His evidence was that “he didn’t have the funding to tie up in holiday home”. When asked by Mr Khan did he participate in any profits from sale, the answer was “No”. The witness stated, that it was ”my choice to sell at the time I did”. On cross-examination, Mr C indicated that the company was “owned to purchase a holiday home”.
16. When questioned by the Tribunal, the witness indicated that there was no formal agreement between himself and his brother for the sale of shares, “because it was family”. He stated, that “(Company C) was just to hold property”.

³ 31 May and 12 June 2012.

⁴ As it later transpired, the share transfer certificate was not signed until 18 February 2008. That is after the sale of the property. (See Exhibit A1)

17. The second witness to give evidence was Mr M. His evidence in chief was that all funding for Company C came from his family Trust. In all, an amount of \$2.5million dollars was borrowed. Mr M indicated that he had placed his personal home as security to gain this funding through the involvement of a Family Trust.

18. It was Mr M's evidence that there was in place a formal agreement between himself and his brother as controlling shareholders to undertake a 50/50 joint venture. He claims that the house was designed with 2 Master bedrooms to account for that fact. He indicated that the property was sold after construction because the costs became intolerable. Mr M stated that he was ultimately approached by a real estate agent. According to the witness, the house was never rented. It was a fully furnished family home.

19. When questioned, "When did your brother move out of the joint venture", Mr M replied:

Can't recall date. Early on in construction project. Had started building.

20. The witness advised that the construction was completed in March 2007. When asked did he ever reside on the property once completed, he advised the Tribunal:

Spent a lot of time there.... Friends and families and other children stayed there.

21. When asked by Ms Ratuvuku, why the Respondent had not been provided with bank statements and other accounting and financial information?, the witness indicated that he was of the belief that these had been provided, though conceded that he had used different Counsel at that time.

22. When asked by the Tribunal what arrangements did the company make for the management of the property?, the witness indicated that there was a gardener and pool person. Mr M conceded that the property was empty for approximately 30 – 35 weeks.

Case of the Respondent

23. Mr Seveci Rokotakala was called as the witness for the Respondent, in the capacity as Chief Auditor, Fiji Revenue and Customs Authority. The witness has worked in the Authority for 20 years and was responsible for the Notice of Assessment that was raised in 2008.
24. Mr Rokotakala stated that in reaching a conclusion that the profit achieved from the sale of profit was amenable to income taxation, he considered the following factors:
- The property was sold in a very short period of time;
 - Upon completion it was only held for 18 month period;
 - The Shareholders and Directors had no connection with Fiji;
 - The Property was constructed with a view to profit; and
 - Mr M was the Managing Director of a Property Development company.
25. According to the witness, the taxpayer provided bank statements in relation to the funding of the construction in Denarau, however provided no statements from the bank to indicate that the taxpayer was in financial difficulty and that it was a forced sale. He said, “we requested Taxpayer to produce documents, some statements (were) forwarded to us, but none from financial institutions”.
26. Upon cross-examination by Mr Khan, the witness was asked about the deductions that would have been allowed to have been claimed as part of the construction costs. This included legal fee and stamp duties, operating expenses, bank charges and interest. The witness agreed that these deductions had not been claimed, but that they would be allowable expenses. Having said that, the witness was of the view that (the Respondent) had been fair in the way in which the Authority had approached the matter.
27. On re-examination, the witness also indicated that he had not received any documentation from the Taxpayer regarding expenses, such as claims for stamp duty

and that since the assessment had been raised, had no further specific discussions with Directors.

28. According to the witness, if the assessment was done on a dollar for dollar basis, the outcome would mean a reduction in the construction cost and a net increase in calculated profit.⁵
29. As Exhibit A1 reveals, Company C was placed into voluntary liquidation by special resolution of members on 11 June 2009.

Income Tax Act (Cap 201)

30. This Tribunal has previously set out the history of the development and rationale underpinning Fijian Income Tax law. (See for example *Company B v Fiji Revenue & Customs Authority* [2011] FJTT 1; *Taxpayer S v Fiji Revenue & Customs Authority* [2012] FJTT 18; and *A Property Management and Investment Company v Fiji Revenue and Customs Authority* [2013] FJTT 3)).
31. Central to those analyses was the observation that the general provision that is Section 11 of the Act, had a substantial role to play in the manner in which income tax was to be assessed for 38 years, prior to the introduction of the clarifying examples that make up Section 11(a).
32. As such and as had been said on many occasions, the starting point for any analysis of Section 11 of the Income Tax Act, is at the commencement of the provision where it sets out as follows:

Definition of total income

11. For the purpose of this Act, —total income means the aggregate of all sources of income including the annual net profit or gain or gratuity, whether ascertained and capable of computation as being wages, salary or other fixed amount, or unascertained as being fees or emoluments or as being profits from a trade or commercial or financial or other business or

⁵ The inference here being that the Taxpayer was treated most fairly in the circumstances.

calling or otherwise howsoever, directly or indirectly accrued to or derived by a person from any office or employment or from any profession or calling or from any trade, manufacture or business or otherwise howsoever, as the case may be, including the estimated annual value of any quarters or board or residence or of any other allowance or benefit provided by his employer or granted in respect of employment whether in money or otherwise, and shall include the interest, dividends or profits directly or indirectly accrued or derived from money at interest upon any security or without security or from stock or from any other investment, and whether such gains or profits are divided or distributed or not, and also the annual profit or gain from any other source including the income from, but not the value of, property acquired by gift, bequest, devise or descent, and including the income from, but not the proceeds of, life insurance policies paid up upon the death of the person insured, or payments made or credited to the insured on life insurance, endowment or annuity contracts upon the maturity of the term mentioned in the contract:

33. I am satisfied that the business of the Taxpayer Company was in the development of a property. A company had been formed for that purpose. The fact that the brothers as controlling shareholders could not sustain their grand plan, does not change the character of that initial purpose or rationale. This was the carrying on of a business. It was not the individual pursuit of family members, as they had opted to seek some protection from the status of an incorporated entity.
34. The nature of the business of Company C is therefore caught by the general approach set out within *Californian Copper*.
35. Such a fast tracked conclusion, understandably does not conform to the way in which parties before this Tribunal have sought to otherwise look for more definitive answers within the ‘three limbs of Section 11(a)’. As has previously been stated by the Tribunal, the clarifying examples of Section 11(a) are not meant to be an exhaustive list of the possible categories of case that make up the taxation of property. The section is nonetheless a clear guide as to what is intended to be canvassed and included within the scope of the general provision. Section 11(a) reads:

Provided that, without in any way affecting the generality of this section, total income, for the purpose of this Act, shall include

(a) any profit or gain accrued or derived from the sale or other disposition of any real or personal property or any interest therein, if the business of the taxpayer comprises dealing in such property, or if the property was acquired for the purpose of selling or otherwise disposing of the ownership of it, and any profit or gain derived from the carrying on or carrying out of any undertaking or scheme entered into or devised for the purpose of making a profit; but nevertheless, the profit or gain derived from a transaction of purchase and sale which does not form part of a series of transactions and which is not in itself in the nature of trade or business shall be excluded;

36. In *Taxpayer N*, and for related cases that ultimately deal with the disposition of property, the Tribunal has concluded that the governing principles that shape this question are set out within the decision in *Californian Copper Syndicate v Harris*, where Lord Justice Clerk formulated the test:

where the owner of an ordinary investment chooses to realise it, and obtains a greater price for it than (s)he originally acquired it at, the enhanced price is not profit in the sense of ...assessable to income tax. But it is equally well established that enhanced values obtained from realization or conversion of securities may be so assessable, where what is done is not merely a realization or change of investment, but an act done what is truly the carrying on or carrying out of a business..."

37. The Tribunal stated in *Taxpayer N*,

That is the first question that needs to be considered, was the act done by the taxpayer realised through the carrying on or carrying out of a business?.....

In Hope v Bathurst City Council, the High Court of Australia observed that the expression "carrying on a business", implies the repetition of acts and activities which possess something of a permanent character.

In Ferguson v Federal Commissioner of Taxation, a Full Court of the Federal Court of Australia were of the view, that there are many elements to be considered when looking at this question. These include, the nature of the activities, particularly whether they have the purpose of profit making; repetition and regularity of activities, or even the commencement of carrying on a business and whether there is an organization of activities in a businesslike manner.

Further the court held that "the fact that concurrently with the activities in question, the taxpayer carries on the practice of a profession or another business, does not preclude a finding that his additional activities constitute the carrying on of a business."^[10]

As the High Court of Australia determined in Martin v Federal Commissioner of Taxation, whether a person is carrying out a business is simply a question of the right conclusion to draw from the whole of the evidence.

Further within Fergusons's case, the Federal Court found, that a

person may conduct a business, albeit of a limited nature, the activities of which business are preparatory to or in preparation for the conduct of another business on a larger scale. The question is whether the activities at an earlier stage, standing alone, constitute a business.⁶

38. This is where there was some departure of the evidence of the two brothers. Mr C had given the impression that the whole exercise was informal, "because it was family". Referring to the transfer of his own interest in Company C, he stated:

"I didn't have enough to contribute and (Mr M) eventually bought me out"

39. As Exhibit A1 reveals, the share transfer did not take place until 18 February 2008. That is, approximately two weeks after the Settlement Date contained within the *Sale and Purchase Agreement*.⁷ It was also at this time that Mr C resigned as a Company Director. That is, nearly 12 months after the house had been completed.⁸ Again this

⁶ See paragraphs [29] to [35]

⁷ See Clause 3(b) as contained within the Sales and Purchase Agreement appended within the *Appellant's Statement of Response to Statement By the Respondent and Appellant's Submission*.

⁸ Evidence of Mr M in cross examination was that house was completed in March 2007.

account of events is quite at odds with the evidence of Mr C, that he had surrendered his interest when construction of the house had started, “but early on”. That it was his “choice to sell at the time (he) did”.

40. Why then a company remained in operation for a further 16 months, until it was placed into voluntary liquidation on 11 June 2009, is also quite strange.
41. My impression of the evidence is therefore that the Company was conducting a business of property development. The Directors were clearly seeking to take advantage personally from that arrangement, of which they are clearly entitled to do. The income arising out of such a business is nonetheless amenable to Fijian Income Tax Laws and is captured within both the general provision of Section 11 and possibly one or more of the illustrative examples of Section 11(a). That is, arising out of that fact, that the business of Company C comprises dealing in such property or perhaps even, that the activity was in some way a form of undertaking or scheme.
42. Such a conclusion can gain further support from the case of *Commissioner of Taxation v Whitfords Beach*⁹, where Gibbs CJ stated:

In deciding whether what was done was an operation of business, it is relevant to consider the purpose with which the taxpayer acted, and since the taxpayer is a company, the purposes of those who control it are its purpose.

43. Company C continued in operation until June 2009. If it’s purpose was only to meet the joint venture requirements of two brothers, then it seems to me that such a purpose would have no longer existed some time in 2006, when the early stages of building construction had taken place and Mr C had no longer sought to be involved in the exercise. In *Lowe v Commissioner of Inland Revenue*, Richardson J defined the words " scheme " to connote a plan or purpose which is coherent and has some unity

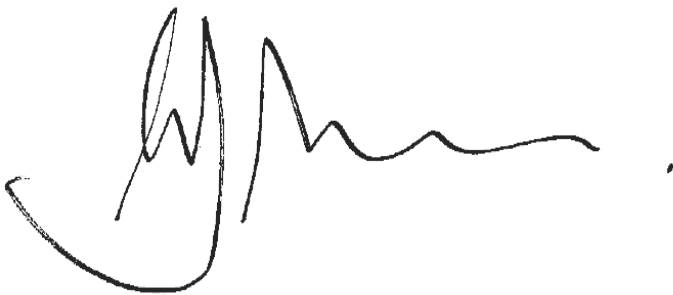
⁹ (1982) 150 CLR 355

of conception. He defined " undertaking " as a project or enterprise organized and directed to an end result.¹⁰

44. As Counsel for the Respondent adduced during the evidence of Mr M and Mr Rokotakala, Company C at no stage provided to the Authority its financial records, relating to the sale and disposition of the property, the sales of its own share and the manner in which profit from the sale of the property was ultimately distributed.
45. In *Closing Submissions* dated 16 May 2013, the Taxpayer has sought to reinforce to the Tribunal, the reasons motivating the sale of the property. These included financial hardship, foreign investment restrictions imposed on the renting out of the property and the refusal of a permanent residency for Mr M. Despite those submissions, the Taxpayer has not convinced the Tribunal that its activities were anything other than designed as profit maximising ones, undertaken as part of a business.
46. The Application is dismissed.

DECISION

- (i) The Application is dismissed.
- (ii) The Respondent is free to make application in relation to costs within 28 days.



Mr Andrew J See
Resident Magistrate

¹⁰

(1981) 5 NZTC 61