

# Decision

Title of Matter:

COMPANY V

(Applicant)

V

FIJI REVENUE AND CUSTOMS AUTHORITY

(Respondent)

Section:

Section 82 Tax Administration Act 2009

Subject:

Application for Review of Reviewable Decision

Matter Number(s):

ITA Action No 04 of 2017

Appearances:

Mr P Knight, Cromptons Barristers & Solicitors, for the Applicant Mr O Verebalavu & Mr Qalo, FRCA Legal Unit for the Respondent

Date of Hearing:

12 September 2018

Before:

Mr Andrew J See, Resident Magistrate

Date of Decision:

13 January 2019

KEYWORDS: Transfer of Assets upon Sale; Section 11 Capital Gains Tax Act 2011- Costs of Acquisition; Section 46 Tax Administration Act 2009, Imposition of Penalty for False and Misleading Statement

# CASES CITED:

Investment Ltd Company v Fiji Revenue & Customs Authority [2015] FJHC 348; HBT10.2013 (13 May 2015)

## Background

- [1] This is an Application for Review of an Objection Decision of the Chief Executive Officer of the Fiji Revenue and Customs Authority, dated 14 August 2017. The Application for Review has been made in accordance with Sections 17 and 82 of the Tax Administration Act 2009. The Applicant asks that the Tribunal vary or set aside the Objection Decision of the Respondent dated 14 August 2017, whereby the Chief Executive Officer wholly disallowed an objection to a capital gains tax assessment of \$47,791.00 and a penalty of \$9,558.00, assessed on the sale by the Applicant of its assets (a tourist resort) to a Hong Kong Holding Company for \$2,382,342.00, on or about 14 November 2014.
- [2] The Taxpayer Company V claims that it acquired the assets from a related entity Company S for the sum of \$3,557,654.00 and subsequently incurred further costs of development of \$1,905,432.00, which it submits exceeded the consideration on sale, thereby resulting in a loss.

#### History of the Acquisition and Sale

- [3] To understand the events that gave rise to the dispute, the parties have prepared a Statement of Agreed Facts, that has been extracted as follows:-
  - (a) The Applicant Company V and its related entity Company S are both companies registered in Fiji with common shareholders and Directors.
  - (b) On or about 23 April 2007, the Native Land Trust Board, as it then was, issued a lease of land to Company S, after which time, that entity proceeded to construct a tourist resort on that land.
  - (c) On or about 1 January 2009, the assets comprising the resort, including the leased land, were transferred from Company S to Company V for a written down value of \$3,557,654.00.
  - (d) In 2013, the leased land was transferred back in the books of both companies to Company S, as no transfer of the lease had ever been executed to Company V.
  - (e) On or about 30 May 2014, an agreement was entered into between Company S as vendor and a Hong Kong Holding Company for the sale of the assets of the resort. The sales price of \$1,500,000.00 AUD, included the transfer of the lease of which \$75,000.00 was assigned for the value, with the balance of \$1,425,000.00 constituting the buildings and improvements, office equipment, furniture and fittings, plant and equipment, boats and motors and goodwill.
  - (f) The agreement acknowledged that some of the assets to be transferred were owned by Company V and that Company S, the vendor, would ensure that these were delivered to the purchaser's nominee on settlement.
  - (g) On 14 November 2014, the leased land was transferred from Company S to the purchasers nominee, after which time the Taxpayer Company V, together with its related entity prepared and signed Capital Gains Tax Declarations and returns that reflected the following:-

#### Company V

Cost Price -Assets \$5,335,300.00 FJ Sales Price: \$1,425,000.00 AUD \$2,383,342.00 FJ

### Company S

Cost Price - Land \$127,786.00 FJ Sales Price: \$75,000.00 AUD \$125,439.00 FJ

(h) The Respondent Authority issued Capital Gains Tax Certificates to Companies V and S on 4 November 2014.

- (i) That sale of the resort was completed on 14 November 2014, with the leased land transferred to a nominated local holding company for consideration of \$75,000.00 AUD and the assets transferred to a second nominated local holding company, for consideration of \$1,425,000.00 AUD.
- (j) On or about June 2016, the Respondent Authority assessed capital gains tax due by Company V arising out of the sale of the resort, in the amount of \$57,349.20.

### Case of the Taxpayer

- [4] The Taxpayer relied on the evidence of its Director and Shareholder Ms D, to provide the Tribunal with an understanding of the history that underpinned the acquisition, development and disposal of the resort. Ms D told the Tribunal that the land located on an island within the Yasawa group, was initially earmarked by family members to develop a backpackers resort and had commenced with informal lease payments being made to the local Mataqli. The Company Director stated that Company V was incorporated in 2006 and was responsible for finishing the construction of the resort and undertook its operations. According to the witness, a related entity, Company S, that had common Directors, also had incurred "some development costs" at the beginning of the project and was the owner of the 99 year lease that had been acquired on 23 April 2007<sup>1</sup>.
- [5] In 2007, Company S transferred its assets to Company V and thereafter up and until the sale of the resort, the Taxpayer completed VAT returns consistent with the requirements of a business operator. The Tribunal was shown the Statement of Financial Position of Company S as at 31 December 2009<sup>2</sup>. Within the table of Current Assets, Company S shows that it was owed \$3,522,517.00 by Company V and according to the witness; there was no transfer of cash, because of the fact that there were common Company Directors<sup>3</sup>. At the time of the transfer of the assets, there had been no transfer of the lease. According to Ms D, the ownership of the resort brought with it financial pressures on the family members that were owners and contributors. The witness said that after several years of difficulties and pressure to sell from the Mortgagee, that a purchaser was subsequently found.
- [6] Mr Knight took the witness to the Sales and Purchase Agreement entered into between Company S and a Hong Kong Holding Company on 30 May 2014 and it was noted that the sale included the transfer of assets that were in the possession of Company V, as the operator of the resort. The Tribunal's attention was also brought to the fact that the lease was subsequently transferred to a nominee company at the time of sale out of the total sales price and apportioned the value of \$75,000.00 AUD4.

<sup>5</sup>ee Folio 1 of the Common Bundle of Documents.

<sup>5</sup>ee Folio 11 of the Common Bundle of Documents at page 7.

It is noted that the statements shows the Fixed Asset to be worth \$3,557,664.00.

See Folio 3 of the Common Bundle of Documents.

### Capital Gains Declaration and Return by Taxpayer

- [7] Exhibit A5 (Folio 5) of the Common Bundle of Documents, contains the Declaration that was made by the Taxpayer coinciding with the sale of the assets. As mentioned above, Company V is claiming the cost of acquisition in the amount of \$5,335,300.00 FJ and that it had recorded a loss against the sales price (\$2,383,342.00FJ) of \$2,951,958.00<sup>5</sup>. Ms D told the Tribunal that the costs associated with the resort were largely development costs incurred in 2009, with further development and upgrade costs being borne in 2010 to 2014.
- [8] In cross examination, the witness was taken to the Capital Gains Declaration and asked how the figure for the cost of acquisition came about. Ms D said that she was unable to comment and did not have documents in her possession that could prove the costs incurred. When asked did the Authority request a substantiation of the costs identified within the return, the witness responded, "not to my knowledge." Ms D confirmed that her signature was contained on page 2 of the declaration. In relation to the Objection Decision, Ms D maintained that the cost of acquisition should have been the 1 January 2009 Book Value amount of the debt owed to Company S for construction costs to date (\$3,557,654.00FJ) plus further development costs in the amount of \$1,905,432.00FJ.
- [9] Ms D told the Tribunal that Company S was registered, but no longer operating and Company V was "waiting for things to finalise." The witness told the Tribunal that there was no relationship at all between Companies V and S and the Hong Kong Holding Company that acquired the resort.

### The Case of the Respondent Authority

- [10] The first witness to be called to give evidence on behalf of the Authority, was Mr Pio Gaberieli, an Auditor who carried out the audit of the Taxpayer in 2014. Put simply, the witness indicated that in reaching the evaluation of the cost of acquisition, that the written down value of the asset as identified as a debt owing to Company S, was deducted from the total claim. Mr Gaberieli explained that the reason why the total claim of approximately \$5.3 million FJ in acquisition costs was not allowed, was that during the audit is was discovered that the \$3,557,654.00FJ costs had been incurred by Company S and not Company V. The witness said that the costs incurred by Company V were the only relevant ones to be considered, as Company S was treated as a separate entity with its own history of transactions. More specifically, Mr Gaberieli explained that when the auditors reviewed the development costs that were incurred by Company S and analysed the VAT returns for the relevant periods, it was revealed that Company S had been claiming full input credits against these costs as if they had been incurred by that company alone.
- [11] According to the witness, the Authority gave the related entities two options. In the case of Company S, because there was no corresponding income, to disallow the input credits; or alternatively, to assess Company V on the capital gains application as made. During cross examination it was put to the witness that as the Authority had issued CGT Certificates to both companies in 2014, that it had in effect endorsed the position relating to the tax liabilities for each entity. The witness rejected that proposition and said that the issuing of certificates and the assessment of taxation owed, were two separate activities. Mr Knight referred the witness to the Financial Statements for Company S, for the year ending 2009 and referred the witness to the value.

It is also worth noting that the date of acquisition provided by the Taxpayer within the declaration reads: "From 24 April 2007 til 31 December 2013."

of the Total Current Assets held on that company's books. Mr Gaberieli responded to the observations, by stating that there was a distinction between loans owed to a company, as opposed to the costs incurred for acquisition of an asset.

- [12] Mr Knight sought to re-clarify the position and asked of the Auditor, "If there was an asset transfer from one company to another and recorded as a debt owing from one company to another, the company that acquires that debt cannot claim against the cost of acquisition? Mr Gaberieli responded, "no the liability is separate". Mr Knight continued, "Had (Company V) paid it, it would have been accepted as a cost? Mr Gaberieli replied, yes. The witness repeated the position that the Authority can only allow for the costs of acquisition and not for a loan.
- [13] In relation to the penalty payment that was imposed by the Authority pursuant to Section 46 of the Tax Administration Act 2009, Counsel queried the rationale for reaching a conclusion of 'false statement', as opposed to having made an error or wrong assumption. The witness responded by indicating that once the Taxpayer had signed the declaration as being correct, that act constituted the making of a false statement. The Tribunal asked of the witness did the Authority have subsequent discussions with the tax agents for the Company, to which Mr Gaberieli confirmed and indicated that following discussions with the Accountants that they had agreed to the amount of \$57k FJ. That is, the amount of the recalculated capital gain (\$47,791.00) and the penalty payment of \$9558.00. The Tribunal clarified this statement with the witness, who stated that the "tax agents had acknowledged that a mistake in approach had been made."
- [14] The final witness to give evidence on behalf of the Respondent Authority was Ms Laisa Bainimarama, the Principal Auditor of the Objection Review Team. The witness was taken to the Objection Decision dated 14 August 2017, that set out the basis for maintaining the position of disallowing the Taxpayer's claim. The decision stated inter alia:

There were insufficient accounts, documents and records provided to substantiate the acquisition costs of \$3,557,654, therefore the amount of \$1,905,432 will remain allowable for Capital Gains Tax purposes.

[15] The witness clarified that the disallowed amount, was the value of an asset disposed of by Company S in 2009 and were not acquisition costs incurred by Company V. In cross examination, Ms Bainimarama agreed with the proposition put by Mr Knight, that the acquisition costs were costs that had been incurred, but they had not been incurred by Company V.

# Analysis of Issues - Calculation of Capital Gain

[16] The Capital Gains Tax Act 2011 came into force on 1 May 2011 and applies to capital gains arising on the disposal of capital assets on or after that date<sup>7</sup>. The capital gain made by a person on the disposal of a capital asset, is the consideration received on disposal, less the cost of the asset at the time of the disposal. Section 11 (2)of the Act provides:

(2) Subject to this section, the cost of a capital asset of a person, other than an intangible asset, is the sum of the following amounts —

This is of course hearsay evidence, but the court record will show that Counsel for the Taxpayer was nonetheless provided with an opportunity to further cross examine the witness following questions asked by the Tribunal.

See Section 2 of the Act.

- (a) the total consideration given by the person for the asset, including the fair market value of any consideration in kind determined at the time the asset is acquired and, if the asset is constructed, produced or developed, the cost of construction, production or development;
- (b) any incidental expenditure incurred by the person in acquiring or disposing of the asset;
  and
- (c) any expenditure incurred by the person to install, alter, renew, reconstruct, or improve the asset.
- [17] The consideration received by a person on disposal of a capital asset is the total amount received by the person for the asset, including the fair market value of any consideration received in kind determined at the time of the disposal<sup>8</sup>. In the present case, the Taxpayer has identified the consideration as being the amount received by Company S. That is, \$1,500,000.00 AUD less the \$75,000.00 AUD as the nominal cost of the lease agreement. The net result is that the consideration has been calculated in the amount of \$1,425,000.00 AUD (\$2,383,342.00FJ). The total cost of acquisition for Company V was established as \$1,905,432.00.

#### Calculation of Capital Gain

\$2,383,342.00 Consideration (\$1,905,432.00) Cost of Acquisition

\$ 477,910.00 Capital Gain @10%= \$47,791.00

[18] Having regard to the submissions of the parties, it would seem that the Respondent's approach to the treatment of the calculations should be the preferred one. The most influential factor that draws the distinction between the two entities and the way in which their costs should be treated, comes about from the situation where Company S had been allowed to claim input costs during the resort's construction stage and thereby treating such costs as its own. From thereafter, it cannot seek the further concession of those amounts, regardless of whether or not they are now held on the books of that company as a debt owed by Company V. Put simply, they were not costs incurred by Company V, but costs assumed by Company S. They had already been treated as such.

#### Imposition of Tax Penalty

[19] In relation to the imposition of a tax penalty, the relevant provisions within Section 46 of the tax Administration Act 2009 have been extracted underneath as follows:

# Penalty for making false or misleading statement Section 46

(1) This section applies to a person -

(a) who makes a statement to a tax officer that is false or misleading in a material particular or omits from a statement made to a tax officer any matter or thing without which the statement is false or misleading in a material particular; and

See Section 12(2) of the Act.

- (b) the tax liability of the person or of another person computed on the basis of the statement is less than it would have been if the statement had not been false or misleading (the difference being referred to as the "tax shortfall").
- Subject to subsection (3), a person to whom this section applies is liable
  - (a) if the statement or omission was made knowingly or recklessly, for a penalty equal to 75% of the tax shortfall; or
  - (b) in any other case, for a penalty equal to 20% of the tax shortfall.........
- (5) No penalty is payable under subsection (2) if
  - (a) the person who made the statement did not know and could not reasonably be expected to know that the statement was false or misleading in a material particular; or
  - (b) the tax shortfall arose as a result of a self-assessment taxpayer taking a reasonably arguable position on the application of a tax law to the taxpayer's circumstances in filing a self-assessment return.
- (6) For the purposes of this section, a statement made to a tax officer includes a statement made, in writing or orally –
  - (a) In any application, certificate, declaration, notification, tax return, objection, or other document furnished or lodged under a tax law;
  - (b) in any information required to be furnished under a tax law;
  - (c) in any document furnished to a tax officer;
  - (d) in answer to a question asked of a person by a tax officer; or (e) to another person with the knowledge or reasonable expectation that the statement would be passed on to a tax officer.
- [20] In Investment Ltd Company v Fiji Revenue & Customs Authority, <sup>9</sup> Kotigalage J stated:

Imposing penalty under Section 46 (2) cannot be effected in isolation or arbitrarily. The Respondent cannot overlook the Section 46(5) and the said provisions of the said Section should be applied to the facts of the case.

<sup>9 [2015]</sup> FJHC 348; HBT10.2013 (13 May 2015)

- [21] Ms D gave evidence that her involvement with the Company V came about in or around 2010, coinciding with the time when she became a Director. Sometime later, the company came into financial distress and according to the witness she was working 17 hours a day, seven days a week, in order to assist with the operations, up and until the sale of the resort. There are a couple of issues that are of concern. Firstly, there does appear to have been a degree of deliberateness about the way in which the relevant capital gains tax return was made. The CGT declaration for Company V, as well as the CGT Return were both signed by Ms D in her capacity as a Director. It would be quite extraordinary, if it were the case that Ms D of her own volition had come up with the strategy of calculating the acquisition costs in the manner in which she did. Whilst this issue was not fully explored by Counsel for the Authority, the Tribunal nonetheless senses that Ms D was perhaps an innocent party in some of what transpired. That being said, there still exists a distinction between Ms D and the Taxpayer.
- [22] The Tribunal is of the view that the Taxpayer either of its own volition or with the advice of others formed the strategy for submitting the acquisition costs in the manner in which they were. Whether that advice came from accountants, lawyers or others makes no real difference. A knowing approach that was inconsistent with the ordinary treatment of such matters should not have been 'tried on'. At that point, the activity of signing a declaration and return in that manner, assumes the characteristics of a knowing or misleading statement for the purposes of Section 46(6) of the Tax Administration Act 2009.
- [23] Company V, through its Directors and Advisors knew that the related Company S, had taken advantage of the input credits coinciding with construction costs associated with the resort's developments. To attempt to reclaim those credits through a separate entity, as if costs of that entity, in those circumstances, would appear wrong from several fronts. The Tribunal is of the view that the Taxpayer cannot say that it did not know and could not reasonably be expected to know that the statement was false or misleading in a material particular. According to Mr Gaberieli, in subsequent discussions with the tax agents, the Authority's revised treatment of the CGT Assessment had been recognised as being the appropriate course of action to take. The internal decision making or advice that got the Taxpayer to the point that it did, is a matter for the Taxpayer. For these reasons, the penalty as calculated is appropriate in the circumstances.

## DECISION

[24] The application of the Taxpayer is dismissed.

