IN THE TAX COURT OF THE HIGH COURT OF FIJI
AT SUVA

Tax Court Appeal No: HBT 07 of 2014

IN THE MATTER of the Income Tax Act 1974

AND

IN THE MATTER of Section 82 of the Tax Administration Decree 2009 (Decree No. 50 of 2009)

BETWEEN	:	DEO CONSTRUCTION DEVELOPMENT COMPANY LIMITED
		Applicant
AND	:	CHIEF EXECUTIVE OFFICER, FIJI ISLANDS REVENUE AND CUSTOMS AUTHORITY
		Respondent
Coram	:	The Hon. Mr Justice David Alfred
Counsel	:	Mr. B.Solanki for the Applicant Ms. R. Malani and Ms. F. Gavidi for the Respondent
Dates of Hearing	:	25 and 26 May 2015 and 1 July 2015
Date of Judgment	:	17 February, 2017

JUDGMENT

1. This is the Applicant's Amended Application for Review (Application) seeking an Order that this Court revise or set aside the decision of the Respondent dated 14 October 2014 (Decision) partly disallowing the Applicant's objection dated 6 June 2014 to the tax assessments for the years ended 31 December 2009 and 31 December 2012 and demanding payment by the Applicant of the sum of $228, 812.26 (Disputed Sum) as Income Tax and penalties.

2. The grounds of the Application are that the Decision is wrong in law and in fact because the Respondent (Revenue) did not take account that:

   (1) The Applicant is not in the business of buying and selling properties.

   (2) The properties were not acquired with the purpose of selling or otherwise disposing of their ownership.

   (3) The gain on the sale was not derived from the carrying on or out of any undertaking or scheme entered into or devised for the purpose of making a profit.

   (4) The properties sold were capital assets subject to Capital Gains Tax (CGT) which was paid and not subject to income taxation.

   (5) The gain made is not subject to taxation under s. 11 or s. 11(a) of the Income Tax Act 1976 (ITA).

   (6) The penalties imposed were unreasonable, unjust and excessive.

3. The Statement of Agreed Facts and Issues include the following:

Agreed Facts

1. The Applicant's directors are Vimal Deo and Saleshni Deo.
2. The Applicant's core business is landlord and construction.
3. The Applicant on 29 October 2004 purchased Lot 17, Riverside Garden, Denarau for $195,000 plus VAT of 12.5% (lot 17).

4. The Applicant constructed a residential building which was rented out from 1 November 2005.
5. On 7 August 2012, the Applicant sold lot 17 for $1,000,000.
6. On 6 February 2003, the Applicant purchased lot 45, Fairways Palm, Denarau for $91,000 plus VAT (Lot 45).
7. The Applicant constructed a residential building thereon and rented it out from 1 December 2005.
8. On 27 April 2009 lot 45 was sold by the Applicant at a price of $700,000.
9. Bakula Beach Resort Limited (BBRL), a limited liability company, has as its directors, Vimal Deo, Saleshni Deo and Vineeth Deo.

Issues Include:

1. Whether the gains made by the Applicant are subject to tax under s.11 and 11(a) of the ITA.
2. Whether the Applicant is in the business of buying and selling properties.
3. Whether the properties were acquired for the purpose of sale or disposal.
4. Whether the gain from their sale was derived from the carrying on or out of an undertaking or scheme entered into or devised for profit making.
5. Whether the properties were sold solely to meet the Applicant's working capital requirement.
6. Whether the Respondent correctly imposed penalties under s. 46 of the Tax Administration Decree (TAD).

4. The Applicant opened its case by calling its first witness, Vimal Deo, its managing director. He said their principal activity is that of a building contractor and a developer, and they have some rental properties as well. They have been in business since 1993. Exhibit P5 is the agreement for the purchase of shares in BBRL. PW1 said he had to sell the property Lot 17 to fund repayment of the loan from the Bank with which he had

purchased the said shares. The said property was acquired for $321,719, the capital gain was $679,282 and the CGT was $67,828 which the Applicant paid.

5. PW1 said Lot No. 45 was purchased in February 2003 for the Applicant to build a house and to rent it. The Applicant build the house and rented it out.

6. The Court noted the tenancy agreement is between Vimal Deo as landlord and Radisson Resort Fiji Denarau Island as tenant. (see Exhibit P13).

7. PW1 said the rent receipts were issued by the Applicant and the tax was paid by the Applicant. The Applicant later sold Lot 45 to finance construction projects awarded to it viz 3 big residential projects. Once they did the job the Applicant would then get paid.

8. At this juncture, Counsel for the Applicant produced 2 documents which were given to Counsel for Revenue. Ms. Malani objected to both letters. The Court ruled these documents could not be tendered in evidence.

9. PW1 continued that the company built a house for Prakash in 2009.

10. Ms. Malani again objected to Exhibit P14 as it is of a different Company from the Applicant. The Court ruled that as it is an Exhibit, Counsel could submit on its value at the submission stage.

11. PW1 continued that there is a Deo Construction Limited and another company Deo Construction Development Company Limited. The sale of Lot 45 provided an income of $509,000. The Applicant is not in the business of buying and selling properties. It is a building contractor; it hires equipment for construction and builds houses for rental income. The Applicant did not buy properties for resale. It did not carry out a scheme to make a profit.

12. During cross examination, PW1 said it is correct that when the Applicant sold lot 17, it intended to buy another property. Exhibit P5 is the agreement made between Ananth and himself, but he denied it was in his personal capacity. The proceeds were used to finance the purchase of BBRL from which the Applicant will benefit. The agreement was between Ananth and himself. It was not between Ananth and the Applicant. When lots 17 and 45 were bought they did not have plans. Their plans after that were to build and rent. The Applicant benefitted from the sale of lots 17 and 45. The proceeds of the sale were to fund the purchase of 3 projects. PW1 did not preplan to buy and then sell.

13. In re – examination PW1 said the Applicant has been taxed on the gain made but he has not been taxed.

14. With that the Applicant closed its case.

15. The Respondent opened its case with its senior auditor, Jeenal Chand, DW1 giving evidence. He said they found there were a couple of lots that were purchased and disposed of but not correctly classified for tax purposes. Lot 45 was sold in 2009 and the net gain was classified as an extraordinary gain. As the auditor, he classified the transaction under s. 11 of the ITA. Lot 17 was sold for $1 million and the net gain assessed for tax under s. 11. Lot 45 was sold in 2009 for $700,000 and then 3 years later lot 17 was sold for $1 million. These transactions were classified under s. 11 based on the fact that the disposal was made for profit motive. The holding period according to DW1's analysis was too short. As soon as the property was acquired it was rented out and then disposed of to get a faster return.

16. DW1 said the Applicant gave the justification that the disposal was for investment purpose but when another property was sold in 2012, the same justification was provided. Revenue believed these transactions were not moving away but moving up for better profitable ventures.

17. During cross –examination, DW 1 said the holding period is 6 years not 3 years. He did not agree it was not for sale purposes. The Applicant has sold properties. It is in the business of buying and selling properties. Lot 45 was sold for working capital for 3 other projects and lot 17 for a bigger profit venture i.e BBRL. He thought the Applicant acquired properties with the intention to resell them. These properties are purchased for returns.

18. When re – examined, he said lots 17 and 45 are fixed assets and the motive was to make profits and this could be ascertained. It was not a mere capital gain on disposal of an asset, but a careful analysis has been done to realize enough profits for the intended project. The intention of the disposal was to get faster and more return.

19. The next witness was Pio Batiniu Gaberieli, DW2, an auditor with Revenue. The Applicant is the construction arm of the group of companies. After going through the objection, Revenue's position was to partially allow the objection put forward by the group. Regarding lot 45, they did their own verification and concluded it would be assessed under s. 11 as the company acquired the property in order to sell to get a gain.

20. Regarding lot 17, they made the same decision as above. They ascertained that the taxpayer was in the business of acquiring property and selling it at a high price, and this will be subject to s. 11.

21. DW2 said the penalties imposed were 20% under s. 46 of the Tax Administration Decree (TAD). The penalty was imposed because the taxpayer did not cooperate with the Revenue audit that was done. The penalty was reduced from the original 75% to 20%.

22. Under cross –examination DW2 said the taxpayer was taxed on s. 11 which covers a gain received from the sale of property. S. 11 is the aggregate of all sources of income from any trade or profession. S. 11(a) is also applied here. He agreed that the sale of lot 17 was

after a reasonably long time and the sale of lot 45 was not after a short period. There was a series of transactions going on with a gain on sale.

23. DW2 said the penalty was for false statement. Their review showed the taxpayer is in the business of acquiring property and then selling it. The sale of the 2 properties produced revenue. The statement made by the taxpayer was incorrect so a penalty was imposed.

24. With that Revenue closed its case. Thereafter both Counsel put in their written submissions and after that made their oral submissions.

25. Counsel for the Applicant said the Court has to decide whether s. 11 or s. 11 (a) applies. He submitted neither did. The Applicant is not in the business of buying and selling properties. Not all gains are income; some can be capital.

26. At this juncture, Counsel for Revenue confirmed they were confining their case to the first 2 limbs of s. 11(a).

27. The Applicant's Counsel continued that the dominant purpose was to rent. There was no documentary evidence but oral evidence consistent with the objection letter. There were only 2 sales. Revenue reclassified capital gains as income. This was not a false return. There should not be a penalty.

28. Counsel for Revenue in her submission said profits from the sale of the 2 properties constitute income under s. 11 and s. 11 (a). This was because there was a significant gain on the sale of lot 17 and a significant profit from the sale of lot 45. This is income under s. 11. It was only necessary to see if there was a gain and there was no need to look at the Applicant's intention. For s.11 (a) to apply one needs to look at the intention of the Applicant. Here there was a sale of 2 properties to get a maximum profit so Revenue is correct to tax the Applicant under s. 11 and 11(a). She said no evidence was provided regarding lot 45 that the gain was to fund other investments in BBRL. As for lot 17,

insufficient evidence was provided to show that the sale was to pay off loans and no agreements were presented to show this.

29. At the conclusion of the arguments, I said I would take time to consider my decision. Having done so I now proceed to deliver my judgment.

30. The facts of this case are contained within a small compass. The Applicant sold 2 properties and made what are patently gains. The pivotal issue is were those gains subject to income tax.

31. This necessitates a close study of section 11(a) ITA. Section 11 describes total income as the aggregate of all sources of income. It's proviso is reproduced below.

"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".

32. I paraphrase the relevant parts of the above, for our present purposes, as follows: A gain derived from the sale of any real property, if the property was acquired for the purpose of selling is income; but the gain derived from a transaction of purchase and sale which is not part of a series of transactions and which transaction is not a trade or business shall be excluded. I am of the view the second limb (underlined) above comes into play.

33. There are two things to be considered here:

(i) Whether the real property was acquired for the purpose of selling.

(ii) The gain is excluded if the transaction is not part of a series of transactions and is not itself a trade or business. Here I note the Oxford Dictionary defines "trade" as "buy and sell" and "business" as "buying and selling".

34. Taking (i) first, requires the Court to consider the 2 properties concerned. Lot 17 was acquired on 29 October 2004 for $195,000, rented from 1 November 2005 and sold for $1,000,000 on 7 August 2012. Yet the only lease agreement provided to the Court was one dated 4 September 2011 for a lease running from 7 September 2011 to 7 September 2013. Thus the stated date of its expiry is one year and one month after the date of its sale.

35. The fact that no other tenancy agreement were produced to the Court and the fact that the property was sold in the middle of the lease would raise the very reasonable inference that any renting of the property between acquisition and disposal was only for the purpose of what could accurately be described as a holding operation, pending the arrival of a golden opportunity to sell it at a very much enhanced price, which is precisely what happened here.

36. Lot 45 was purchased on 6 February 2003 for $91,000, rented out from 1 December 2005 and sold on 27 April 2009 for $700,000. Not a single tenancy / lease agreement executed by the Applicant was provided to the Court. What was however produced, was a tenancy agreement made on 1 September 2007, executed by Vimal Deo as the landlord and not by the Applicant. It is trite law that a limited liability company is a separate and distinct legal entity from its director or shareholder.

37. With regard to lot 17, in his evidence in court, Vimal Deo, the managing director of the Applicant said the Applicant sold lot 17 to purchase the shares of BBRL. Yet the Exhibit P5 tendered was of an agreement to purchase shares in BBRL where the purchaser was

Vimal Deo and not the Applicant. Again what I said in paragraph 36 above applies here with equal force.

38. I consider the majority decision of the New Zealand Court of Appeal in: C.I.R. vs National Distributors Limited: CA 137/87 (1989) 11 NZTC 6,347 as being of persuasive authority, in fortifying the decision I have arrived at. I adopt the words of Casey J (one of the 2 judges in the majority of the Court) that unless the taxpayer could show the main or dominant purpose which led him or her to acquire the property was not to sell or otherwise dispose of it, then the profits or gains were taxable.
Here I find and I so hold the Applicant has failed to do this in regard to both lots.

39. At the end of the day, I am of opinion that the Applicant clearly purchased lot 17 and lot 45 for the purpose of selling them when the time was opportune to do so. The sales were part of a series of transactions one following the other within the space of a mere 3 years and each transaction was in itself in the nature of a trade or business. Both fell within the ambit of s. 11(a) ITA and both did not come within the exclusion at the end thereof.

40. I therefore affirm the Amended Assessments for the years ended 31 December 2009 and 31 December 2012 respectively raised by the Revenue.

41. I come finally to the penalties imposed under s. 46 of the Tax Administration Decree 2009 (TAD). This provides a penalty of 75% if a false or misleading statement was made knowingly or recklessly and a penalty of 20% in any other case. The original penalties imposed were reduced by the Revenue to 20% although I note s. 48(7) does not allow the Revenue to remit any penalty imposed under s. 46.

42. The Applicant attempted to prevent itself from falling within the ambit of s. 46 by saying the gains were properly recorded in its financial statements. But it made no attempt to invoke s. 46 (5) (a) to show that 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. If it had done so, then no penalty at all would have been payable.

43. In the light of the way I have taken to arrive at my decision, I can see no way how it can conceivably be contended by the Applicant that the penalties "are unreasonable, unjust and excessive". I therefore affirm the penalties imposed by the Revenue.

44. In the event it is inexpedient to refer to the other authorities cited by both sides or to any arguments that may draw a red herring across the trail.

45. In the result, I hereby dismiss the Amended Application for Review, decline to grant the Orders sought therein and make no order as to costs.

Delivered at Suva this 17th day of February, 2017.

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David Alfred
JUDGE of the High Court of Fiji.