FIJI TAX TRIBUNAL

Decision

Section 89 *Tax Administration Decree* 2009

Title of Matter:	**A FREIGHT SERVICES COMPANY** **v** **FIJI REVENUE AND CUSTOMS AUTHORITY**	**(Applicant)** **(Respondent)**
Section:	**Section 82 *Tax Administration Decree* 2009**	
Subject:	**Application for Review of Reviewable Decision**	
Matter Number(s):	**Action No 5 of 2014**	
Appearances:	**Mr R Naidu and Ms N Basawaiya, for the Applicant** **Ms F Gavidi, FRCA Legal Unit for the Respondent**	
Date of Hearing:	**Thursday 30 October 2014**	
Before:	**Mr Andrew J See, Resident Magistrate**	
Date of Decision:	**6 January 2015.**	

ZERO RATING TAX AND EXPORT SERVICES-Imposition of Tax on Supply-Section 15(2) *Value Added Tax Decree* 1991; Paragraphs 10 and 15 of the Second Schedule - Determination of Zero Rated Transport Services.

Background

1. The Applicant Taxpayer is a freight forwarder involved in the international carriage of goods. On 19 May 2014, in accordance with Sections 17(1) and 82(1) of the *Tax Administration Decree* 2009, the Taxpayer made application for review *to* revise or set aside a tax decision of the Respondent dated 17 April 2014. Within that decision, the Respondent wholly disallowed the Taxpayer's objection against Amended Tax Assessments issued on 23 August 2013 for the taxable periods ending December 2010 to December 2012.

2. At the heart of the Taxpayer's objection, was the imposition by the Respondent of value added tax in the amount of $151,528.50 and penalties in the sum of $30,305.70. At the commencement of proceedings it was agreed between the parties that the Respondent had withdrawn the penalties the subject of this challenge. On that basis, the matter proceeds reliant on the first ground of review only. That is, that the Taxpayer was entitled to zero rate the supply

of transport services for the purposes of Paragraph 10 of the Second Schedule to the *VAT Decree* 1991, where any element of international carriage is involved in that supply.

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

Agreed Statement of Facts Between the Parties

4. The *Agreed Statement of Facts* prepared between the parties, are set out within the document filed on 5 August 2014 and have been reproduced with some minor alteration and redaction. The Applicant is a freight forwarder engaged in the international carriage of goods. It transports its customers' goods to Fiji (imports) as well as from Fiji (exports). According to the parties, the Taxpayer like other freight forwarders aims to provide a total transport solution, to achieve 'door to door' carriage of goods for customers.

5. As the Statement of Facts explains, in the course of providing this service to customers, the Taxpayer may acquire freight capacity on a ship for its customer. It is not the owner or charterer of the ship; but it is purchasing space in that ship. It will invoice its customer for the use of that space, with the aim of making a profit on this component of its service. The Taxpayer, in reliance on paragraph 10 of the Second Schedule of the *VAT Decree*, zero-rates the international freight component of its invoice to customers. The Respondent says it has no right to zero-rate this amount. The Taxpayer says that the freight cost for which it charges, is the same as that of a shipping company and it is the nature of the service supplied, not who supplies it, which is relevant.

6. In 2013, the Respondent as part of an industry review of the freight forwarding sector, audited the Taxpayer for VAT compliance. As a result of the audit, the Respondent issued a schedule of discrepancies dates 14 June 2014. The schedule of discrepancies identified two issues:

    a) "commission (mark-up) zero rated tax short-fall";

    b) "fringe benefits and adjustments";

    and proposed imposing penalties at 20 per cent of the tax shortfall.

7. The Taxpayer through its accountants responded to the schedule of discrepancies on 28 June 2013, with examples of invoices where the Taxpayer like all other freight forwarders zero-rated to its local customers the international freight portion of its invoice . The Respondent replied on 23 August 2013, stating that the "mark up on freight earned from local customers will be deemed (a) supply [taxable at 15% VAT] – meaning that:

    a) The Respondent would allow the Taxpayer to zero-rate to its customer its actual cost of freight (as paid to the international shipper) but
    b) To the extent of any mark-up on that freight cost to the customer (which FRCA refers to as "commission". VAT was payable at 15%.

8. The Respondent on the same day issued a *Notice of Amended Assessment* as follows:

Table 1

	2010	2011	2012	Total
Commission zero rated	208,186.49	467,716.00	516,657.85	1,192,560.34
VAT Fringe Benefit Adjustment	2,708.50	3,250.20	3,250.20	9,208.90
VAT at 12.5% and 15%	25,840.33	64,256.71	70,640.36	160,737.40
20% S46 Penalty	5,168.07	12,851.34	14,128.07	32,147.48

9. The Taxpayer accepted the VAT adjustments for Fringe Benefit Tax, however objected to the VAT assessed on "commission". This amounted to $151,528.42. A further penalty of $30,305.68 was imposed, totalling $181,834.11 calculated as follows:

Table 2

	2010	2011	2012	Total
Commission zero rated	208,186.49	467,716.00	516,657.85	1,192,560.34
VAT at 12.5 % and 15%	23,131.83	61,006.43	67,390.15	151,528.42
20% s.46 Penalty	4,626.37	12,201.29	13,478.03	30,305.68
20% S46 Penalty	27,758.20	73,207.72	80,868.19	**$181,834.11**

10. The Applicant Taxpayer's Objection dated 27 September 2013, stated that the Respondent had:

a) erred in taking up as taxable at 15% VAT, the Taxpayer's "mark-up" on the freight and
b) incorrectly imposed penalties because:

i. no VAT was payable in the first place or

ii. alternatively, even if VAT was payable, the Taxpayer had made no "false or misleading statements", having fully disclosed the basis on which it was returning for VAT.

The Value Added Tax on Supply and the Zero Rating Scheme

11. Section 15 of the *Value Added Tax Decree* 1991 provides:-

> *(1) Subject to the provisions of this Decree, the tax shall be charged in accordance with the provisions of this Decree at the rate of fifteen percent*[1] *on the supply (but not including an exempt supply) in Fiji of goods and services on or after the 1st day of July 1992, by a registered person in the course or furtherance of a taxable activity carried on by that person, by reference to the value of that supply.*
>
> *(2) Where, but for this subsection, a supply of goods and services would be charged with tax under subsection (1) of this Section, any such supply shall be charged at the rate of zero percent where that supply is a zero-rated supply.*

12. The definition of what constitutes 'zero rated ' is found at Section 2 of the Decree to mean, " a supply described in the Second Schedule to this Decree". The Second Schedule thereafter provides for the category of cases that have been earmarked as gaining the benefit from the zero rating. That is, they are categories of goods and services exempt from the payment of value added tax.

13. Relevantly, paragraph 10 of the Second Schedule provides the following exemption for:-

> *The supply of transport services relating to the international carriage of passengers and goods –*
>
> *(a) from a place outside Fiji to another place outside Fiji; or*
> *(b) from a place in Fiji to a place outside Fiji; or*
> *(c) from a place outside Fiji to a place in Fiji; or*
> *(d) from a place in Fiji to another place in Fiji to the extent that the transport is by aircraft and constitutes —international carriage for the purposes of the Civil Aviation Act.*

What is Meant by Supply of Transport Services?

14. At Annexure 1 of the *Applicant's Closing Submissions,* the definition of 'supply' is provided. That definition calls up Section 2 of the *Sale of Goods Act* (Cap 230), that provides a non-exhaustive meaning as follows:-

> *"supply", when used as a verb, includes-*
>
> *(a) in relation to goods - the supply by way of sale, exchange, lease, hire or hire purchase; and*
> *(b) in relation to services - provide, render, grant or confer and when used as a noun has a corresponding meaning, and*
> *"supplied" and "supplier" shall have corresponding meanings;*

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[1] Note that the previous percentage was based on 12.5% and this was adjusted on and from 1 January 2011.

15. The Applicant says that a non controversial meaning to the term, "supply of transport services", is "to provide a service to take or convey people of goods from place to place". [2] The Respondent on the other hand, while not offering its own definition, has brought to the Tribunal's attention the case of *Auckland Regional Authority v Commissioner of Inland Revenue*[3],where the distinction has been drawn in relation to transport activities and ancillary transport activities. The inference apparently being that a similar dichotomy can be drawn up in the case of the definition of 'transport services' under Fijian law.

16. Within *Auckland Regional Authority,* reference is made to the Privy Council decision in *Databank Systems Ltd v Commissioner of Inland Revenue*[4], in which the Judicial Committee reaffirmed the view that:

> *The fundamental feature of the scheme of the legislation (was) to focus on the supply of goods and services by a supplier to a recipient and that tax is imposed on the supply.*

17. That appears to be the critical issue. What are the transport services supplied by the supplier?

Evidence of the Taxpayer

18. At the hearing of this matter, Mr Z, a Director and shareholder of the Taxpayer, provided the Tribunal with a good insight into the workings of the freight forwarding business. As part of his evidence, the witness attested to a *Witness Brief*[5] that had been earlier prepared and in which he had set out the nature of the services provided by the Taxpayer, how such services were charged and when it considered that the zero rating for VAT purposes should apply. As restated in the *Applicant's Closing Submissions,*

> *(The Taxpayer) would seek from a shipping company a cost for the "port to port" segment. (The Taxpayer would then apply its own mark-up (margin) to the shipping company quote and invoice the customer accordingly.*

19. During the course of the Director's evidence, he took the Tribunal through a line by line analysis of a typical invoice that would be issued on such occasions.[6]

Position of the Respondent

20. Counsel for the Respondent opened its case, by describing the manner by which the value of supply should be confined for the purposes of assessing eligibility to zero-rate. According to Ms

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2 See Paragraph 3 of Annex 1 of the Applicant's Closing Submissions.

3 (1994) 16 NZTC

4 (1990) 12 NZTC 7 at 227

5 See Exhibit A1.

6 Refer to the Tax Invoice 00052740 dated 5 March 2013 in the amount of $22,949.52.Note this document was not issued with an exhibit number, though should have and has been accepted by the Tribunal as part of the evidence of the Taxpayer.

Gavidi, the focus should be on the 'actual' transport services and not the steps taken in the 'facilitation' of the service.

21. To support or reaffirm the case of the Respondent, the evidence of Ms Emele Rokobulu, a Senior Auditor within the Respondent's Auditing and Compliance Section, was called. According to the witness, a key determinant in reaching its position was the fact that as a 'facilitator', the fees charged were over and above those associated with the direct transport costs.

22. Consistent with the *Closing Submissions of the Respondent*, the focus of the Respondent's argument, is centred around the definition found at Section 19 (2) of the *VAT Decree,* in which the "value of supply" is relevantly set out as:

> *the value of a supply of goods and services shall be such amount as, with the addition of the tax charged, is equal to the aggregate of, -*
>
> *(a) to the extent that the consideration for the supply is consideration in money, the amount of the money.....*

23. Within the Submissions, the Respondent makes reference to its internal *VAT Manual* that establishes the policy position, "that consideration is valued at the tax exclusive selling price".[7]

Interpretation of the Decree

24. As part of this review hearing, the parties were also asked to look at the history of the zero rating provision, having regard to the definition of "ancillary transport activities", particularly as it was previously located within Paragraph 22 of the Second Schedule of the *Decree*.[8]

25. The reason for asking that this be done was that at various locations within the Second Schedule, there appears a deliberate usage of the term. In response to this request and to summarise the positions of the parties, the Applicant is of the view that little appears to turn on that amendment, whereas the Respondent says that it "could not find any explanation for the repealed paragraph 22."[9]

26. Despite this, a comparison of Paragraphs 10 and 15 within the Second Schedule appears to shed some light as to the way in which the law is to be interpreted.

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7 See *Respondent's Closing Submission* at paragraph 17.

8 See Decree No 45 of 1991.

9 See paragraph 20 of Respondent's Closing Submissions.

Table 3 - A Comparison of Second Schedule Provisions

Paragraph 10	Paragraph 15
The supply of transport services relating to the international carriage of passengers and goods - (a) from a place outside Fiji to another place outside Fiji; or (b) from a place in Fiji to a place outside Fiji; or (c) from a place outside Fiji to a place in Fiji; or (d) from a place in Fiji to another place in Fiji to the extent that the transport is by aircraft and constitutes "international carriage" for the purposes of the Civil Aviation Act.	(1) The supply to a person in that persons' taxable activity capacity (and not in that person's private capacity) who in that capacity belongs in a country other than Fiji of services comprising of - (a) the handling or storage of goods at or their transportation to or from a place at which they are to be exported or have been imported or the handling or storage of such goods in connection with such transport; or (b) ancillary transport activities in relation to any ship or aircraft in a port or airport; or (c) the making of the arrangements for the supply of any of the services referred to in this paragraph and paragraph 7 of this Schedule. (2) For the purposes of this paragraph, "ancillary transport activities" includes loading, unloading, handling, landing, berthing and stevedoring.

27. Paragraph 15, addresses at least to some extent, the indirect transport services that are associated with international carriage. What it does, is extend for the benefit of Paragraph 10, what can be taken into consideration for the purpose of calculating the cost of supply, including most relevantly, the making of the arrangements for the supply of any of the services, such as handling, storage and transportation activities, where that supply is to a person's taxable activity capacity, other than in a private capacity. These appear to be the indirect costs associated with transportation and logistics, to and for places outside of Fiji. On its face, this would seem to be a bid to promote economic activity for Fiji businesses (export and related services), who are involved in providing services, whether in part or in whole, outside of Fiji.

28. The effect of this is that when applied together, Paragraphs 10 and 15 are capable of allowing for the zero rating of direct and indirect transport costs, only in certain categories of case. That is, where the transportation activities relate to services performed in the context of subparagraphs (a) or (b) of Paragraph 10 (that is from a place in or outside of Fiji to a place outside Fiji) and also involves arrangements or ancillary activities that fall within the scope of Paragraph 15 of the Second Schedule. In all other cases and in a manner ostensibly similar to the decision in *Auckland Regional Authority*[10], the focus appears to be whether or not the costs of providing the transport service, are in fact direct costs. Though it is nonetheless noted, as Barker J acknowledged, that caution needs to be taken against following interpretations of laws as they

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10 Op cit.

apply in different VAT regimes.[11] For that reason, the apparent distinction in the language relied on within the various paragraphs of the Second Schedule, must be used as the prevailing indicator when interpreting the law. If it was the case that the "making of the arrangements for the supply of any of the (transport) services"[12], was to be included within the definition set out in Paragraph 10 for all categories of case, then such inclusion through an interpretative statutory aid, such as marginal note or supplementary definition, would have been easy enough to achieve.

29. From a policy perspective,[13] the issue appears to be this. Can the "mark up" on the cost of supplying the transport services, be regarded as part of the "consideration" as the concept applies within Section 19 of the Decree? The answer would seem to be no. The reason for this is that a limitation needs to be imposed around what the actual cost of supply is. That cost cannot be an ever elusive and adjustable cost. The Tribunal is of the view that when it is priced by the shipping company who supplied it to the Taxpayer, that is the actual cost of the transport service. The broker of that supply or service may be at liberty to charge to the highest or sole bidder a 'marked up' price for the cost of that service, but that does not alter the actual cost of the service. This is not a situation akin to the provision of in-flight meals as referred to within Auckland *Regional Authority.* The brokerage or administrative costs do not form part of the direct costs of the carriage.[14] What has taken place is that the Taxpayer has sought to recover its costs of providing its services. It is well entitled to do that. It cannot though, seek to claim a zero rating on its margin or indirect costs, when doing so.

30. Without wanting to diminish the obvious contribution that the Taxpayer makes to the Fijian economy, the situation is still somewhat analogous to that which Barker J made reference to in the case of *Databank Systems Ltd v Commissioner of Inland Revenue*[15] , where his Honour stated, "banks could have operated without the computer services operated by Databank". The same could be said in relation to the present case. International Transport Carriers could still provide transport services, with or without the assistance of freight service companies who wishes to provide total logistic solutions. As his Honour noted:

> *The fact that Databank was enabling this function to be performed efficiently and speedily was immaterial. Databank was supplying a separate service other than the one specifically exempted by the legislation.*

31. The total service provided by the Taxpayer is clearly a worthwhile one for consumers, though that is not the issue. The issue is which parts of that activity should gain the benefit of the zero rating for the purposes of the Second Schedule. The actual cost of that supply from the carrier is the only conclusion that can be drawn. If as a result of the inter-relationship between Paragraphs 10 and 15, the Taxpayer can gain further relief from the Amended Assessments

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11 While the laws of Australia and New Zealand, for example, provide light on many issues, the structure and history of the law, needs to be interpreted firstly within its own context.

12 Note its usage within Paragraph 15.

13 What the effect of the policy appears to be, is to provide greater assistance to export related and offshore activities .

14 This is why they have been separately identified within subparagraph(c) of Paragraph 15.

15 (1987) 9 NZTC

issued by the Respondent, then that should take place. The Amended Assessments are to be remitted to the Respondent to review its decision, based on those findings. If though, the amended assessments have only been adjusted as a result of the incorrect claiming on 'mark up' to local customers, then it is envisaged that no further amendment will take place.

Other Issue

32. The other issue that was flagged between the parties at the outset of the proceedings is that relating to the penalties initially imposed by the Respondent. It is the case that these have been withdrawn by the Authority. The Applicant is seeking to rely on the decision of *Company P v Fiji Revenue and Customs Authority,*[16] in support of its claim that it should be able to gain interest on the return of the penalty sum paid. The Applicant relies on Section 67(3) of the Decree for the purposes of determining an appropriate rate of interest to be calculated, upon return of the principal amount.

33. The Tribunal is unwilling to issue any decision in relation to this matter. The terms of that withdrawal have not been ventilated before the Tribunal. It is for the Chief Executive to reassess the basis and terms for the reversal of any such decision. Under Section 48 of the *Tax Administration Decree* 2009, the Chief Executive is well within his or her powers to review the terms and or extent of the penalty imposed. Whether any subsequent decision of the Chief Executive Officer is a reviewable tax decision for the purposes of the *Tax Administration Decree,* is not an issue that needs to be considered at the present time.

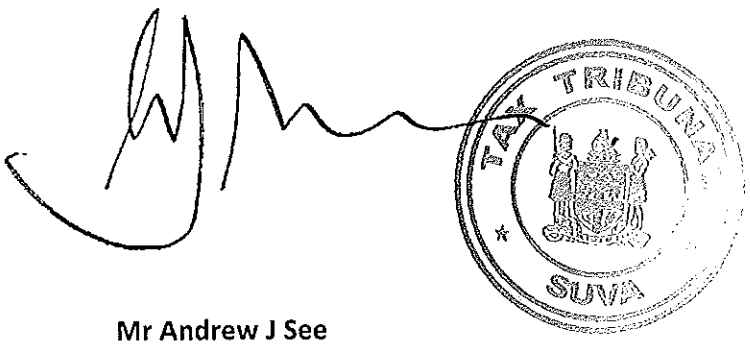
34. Finally, in view of the circumstances of this case and the ostensible change of position of the Respondent in relation to the penalties that it otherwise had imposed on the Applicant, it would seem appropriate that each party should bear their own costs.

Decision

The Tribunal orders:-

(i) That the Amended Assessments issued on 23 August 2013, be remitted to the Chief Executive Officer for review, having regard to the interpretation given to Paragraphs 10 and 15 of the Second Schedule of the Decree.

(ii) Each party to bear their own costs.



Mr Andrew J See
Resident Magistrate

16 [2013]FJTT17