



## **STANDARD INTERPRETATION GUIDELINE 2020-31**

### **INCOME TAX ACT 2015 – DISPOSAL OF REAL PROPERTY OUTSIDE OF TAXABLE ACTIVITY**

This Standard Interpretation Guideline (SIG) sets out Fiji Revenue and Customs Service's (FRCS) policy and operational practice in relation to the tax liability which may arise from the disposal of real property where the taxpayer is not in the business of buying or selling real property.

This SIG is to be read in conjunction with the SIG on Value Added Tax Act 1991 - Disposal of Real Property Outside of Taxable Activity 2019 - 10

The SIG is issued with the authority of the Chief Executive Officer (CEO) of FRCS.

All legislative references in this SIG are to the Income Tax Act 2015 (unless otherwise stated)

This SIG is in effect from 1 August 2020 and may need to be reviewed in the event of any relevant legislative amendments.

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## EXECUTIVE SUMMARY

1. A taxpayer who is not in the business of dealing in real property may dispose his or her real property due to a number of reasons.
2. The CEO is of the view that the tax implications of the disposal are discussed in order to provide clarity to the taxpayer community.

## INTRODUCTION

3. There are three tax types a taxpayer must be aware of when disposing land or real property. These are:
  - a. Capital Gains Tax or Income Tax<sup>1</sup>; and
  - b. Value Added Tax<sup>2</sup>.
4. This SIG will focus on all the tax implications including Capital Gains Tax (“CGT”) or Income Tax on the disposal of real property, while a SIG on the related Value Added Tax issued would be issued separately.
5. This SIG is based on the assumption that the taxpayer who is disposing the real property is not in the business of dealing in real property.
6. Real property is a common law term which refers to land and all structures (also called improvements or fixtures) integrated with or affixed to the land.
7. The CEO of Fiji Revenue and Customs Service is appreciative of the growth in the real estate industry and the need to provide clear and precise guidelines in relation to taxation of the same.
8. The examples used throughout this SIG are merely illustrative. They do not cover the infinite number of factual scenarios that may arise. The relevant legislative provisions must be considered and applied to each case on its particular facts.

That is, conclusions should not be drawn by determining whether the facts of a particular case may be analogous with particular examples, but rather on the basis of applying the correct tests established by the law

9. The full text of the legislative provisions is contained in the Appendix herein.

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<sup>1</sup> Value Added Tax Act 1991

<sup>2</sup> Income Tax Act 2015

## LEGISLATIVE ANALYSIS

### CAPITAL GAINS TAX

10. Section 65 of the Income Tax Act 2015 states that a tax to be known as “Capital Gains Tax” is imposed at the rate of 10%<sup>3</sup> on a person who has made a capital gain, other than an exempt capital gain, on the disposal of a capital asset.
11. A capital asset includes real property and any structural improvement to real property, an interest in real property or an interest in a structural improvement to real property<sup>4</sup>.
12. The capital gain is calculated by reducing the cost of acquiring the capital asset from the consideration on disposal.



#### Consideration on Disposal

13. The consideration for the disposal of an asset is the total amount received or receivable for the asset, including the fair market value of any consideration in kind determined at the time of the disposal<sup>5</sup>.
14. This means that capital gains is calculated on the sum that has been received or will be received by the vendor for the disposal of the real property.

#### Vendor Financing Agreements or Payment in Instalments

15. In Vendor Financing Agreements consideration for capital gains tax would be calculated on the amount received and any pending payments yet to be received for the disposal of the capital asset.

For example, Jim sells his real property to Smith for \$250,000. The terms of the sale and purchase agreement stipulate the following:

- Smith to pay Jim \$150,000 in order to effect settlement of the transfer
- Smith to pay Jim \$5,000 every month until the remaining \$100,000 is paid
- An additional \$5000 is to be paid with the final payment as interest.

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<sup>3</sup> Paragraph 7 of Schedule of Income Tax (Rates of Tax and Levies) Regulations 2016

<sup>4</sup> Section 2 of Income Tax Act 2015

<sup>5</sup> Section 86(2) of the ITA 2015

The consideration for the disposal of the real property would be calculated as follows:

Amount Received	+	Amount Receivable	=	Consideration
\$150,000	+	\$100,000	=	Consideration
		\$250,000	=	Consideration

The additional \$5000 would not be included in the consideration as the sum is not for the disposal of the real property but it is income earned by Jim for providing financing services, therefore to be included in Jim's gross income. In the event Smith defaults in his payment and the property is forfeited to Jim, Jim may amend his CGT return to reflect the correct amount received for the property<sup>6</sup>. Any non-refundable deposit retained by Jim would be added to his gross income<sup>7</sup>.

### **Damaged or Destroyed Real Property**

16. In the event that the real property has been destroyed (usually in the event of natural disaster) any compensation indemnity, or damages received by the person as a result of the loss or destruction is included in the consideration on disposal<sup>8</sup>.

For example, Jonathan resides in Sigatoka with his family. He owns the land (and building) on which he resides and the same is insured. In 2017, the building on which Jonathan was residing in was damaged by fire. Jonathan decides to sell the real property without any repairs or improvements.

Jonathan sells the property to Samantha for \$100,000

The insurance company indemnifies Jonathan for the damages in the sum of \$120,000

Therefore, the consideration for the disposal of the real property is \$220,000. If the insurance payment is received following the settlement of the transfer to Samantha at \$100,000, Jonathan must amend his CGT return to reflect the insurance compensation received. If no voluntary amendment to the return is made by the taxpayer, the CEO may issue an amended assessment and it is highly likely that administrative penalties would apply.

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<sup>6</sup> The initial CGT return would be nullified through the amended assessment.

<sup>7</sup> A comprehensive SIG on "non-refundable deposits" may be developed in due course

<sup>8</sup> Section 86(4) of ITA 2015

## Joint Sale

17. There may be instances where two or more assets (including real property) are disposed as part of a single transaction. Usually the consideration for each asset forming part of the transaction is specified<sup>9</sup> however, there may be circumstances where the consideration per asset is not specified. In such cases, the consideration would be apportioned to the fair market value of each asset<sup>10</sup>.

For example, Ms. Lee is selling the following in a single transaction to Abdul for \$350,000:

- Land and building
- Motor Vehicle
- Tractor and Accessories

The sale and purchase agreement does not specify the consideration for each item, therefore the fair market values would be used to apportion the consideration sum. This is done as follows:

Market value conducted on land shows a market valuation at \$275,000

Market value for motor vehicle and tractor with accessories is \$50,000

Therefore, the apportionment is done as follows:

Land and building  $275,000/325,000 \times 100 = 84.6\%$

84.6% of \$350,000 is \$296,100

Therefore, the consideration for the land and building would be \$296,100

## Consideration in Kind

18. Not all disposal of real property may be for money. There may be instances where there is consideration in kind for the disposal of the property. In such cases the fair market value of the “consideration in kind” would be taken as consideration<sup>11</sup>.

For example, Jone sells his real property to Aman. In return Aman pays Jone \$150,000 and transfers his motor vehicle valued at \$35,000 to Jone. The consideration for the real property would be calculated as follows:

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<sup>9</sup> In the sale and purchase agreement

<sup>10</sup> Section 86(5) of ITA 2015

<sup>11</sup> Section 86(2) of the ITA 2015

Cash	\$150,000
Motor Vehicle	<u>\$35,000</u>
Consideration	\$185,000

### Disposal for Settlement of Debt

19. Real property may also be disposed in settlement of a debt. In this case the consideration would amount to the outstanding amount of a loan owed by the supplier to the recipient.
20. The CEO of Fiji Revenue and Customs Service takes guidance from the Australian case laws of *Brookdale Investments Pty Ltd v FC of T (No 2)*<sup>12</sup>, and *Rod Mathiesen Truck Hire Pty Ltd v FC of T*<sup>13</sup>, where it was held that the consideration received at settlement for the sale of vacant land included the amount owing under a loan agreement between the vendor and the purchaser.

21. The illustration of this application is as follows:

Mark owes \$250,000 to Kevin. Mark and Kevin agree to allow for full settlement of the debt on the disposal of a land owned by Mark. Mark transfers the land to Kevin and as agreed Kevin renounces the debt owed by Mark.

The consideration on the disposal would therefore be \$250,000.

Alternatively, Mark owes \$250,000 to Kevin. Mark and Kevin agree to transfer land owned by Mark to Kevin in lieu of payment in the amount of \$200,000. In this case the consideration on disposal would be \$200,000

### Disposal at Non-Arm Length's Transactions

22. The arms-length principle requires the taxpayer disposing off the real property in a non-arm's length transaction<sup>14</sup> to deem the consideration received to be equal to the fair market value of the real property at the time of the disposal<sup>15</sup>.
23. Subsequently, the recipient would be treated to have acquired the real property at the fair market value at the time of the disposal<sup>16</sup>.

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<sup>12</sup> [2013 ATC ¶10-304](#)

<sup>13</sup> [2013 ATC ¶10-327](#)

<sup>14</sup> As defined in section 2 of ITA 2015

<sup>15</sup> Section 89(a) of ITA 2015

<sup>16</sup> Section 89(b) of ITA 2015

24. For example: ABCo is disposing real property to its subsidiary XYCo. In the Sale and Purchase agreement the real property is sold for a value of \$5000. However, a market valuation carried out on the real property shows that the market value is \$150,000.

Therefore, the consideration on the disposal by ABCo would be \$150,000. In turn XYCo would be treated as having acquired the real property at \$150,000. XYCo is not required to give \$150,000 to ABCo but for taxation purposes, the disposal would have deemed to have occurred on the consideration of \$150,000.

### Cost of Real Property

25. The cost of the real property would include the following:

a. Cost of Acquisition

If the real property is bought: the total consideration given by the taxpayer for acquiring the real property, including the fair market value of any consideration in kind given to acquire the real property.

If building on the real property is constructed: the cost of acquiring the real property and the cost of constructing the building.

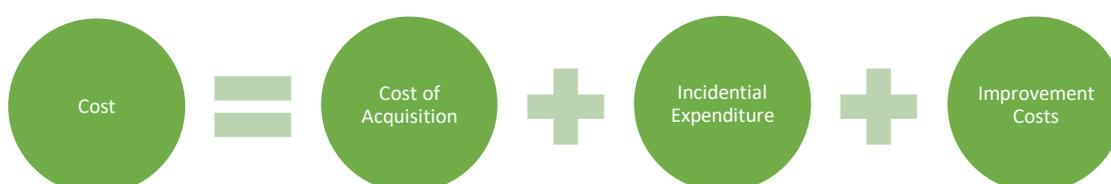
b. Incidental Expenditure

Any incidental expenditure incurred on acquiring and disposal of real property. This includes professional fees (such as for the services of an agent, lawyer, valuer, auctioneer or surveyor), and advertising costs (particularly on disposal)

c. Improvement costs

The cost of the real property would include costs install, alter, renew, reconstruct or improve the real property. Improvement costs does not include repair and maintenance costs for the purposes of CGT, but the same may be deductible for income tax purposes

26. If expenses have been claimed under capital gains tax, these expenses cannot be claimed again under income tax returns.



## No Records of Expenditure

27. In the event where the taxpayer is:
- a. unable to produce any record of any expenditure relating to the cost of acquiring and improving the real property which the taxpayer intends to include in the cost; and
  - b. the CEO has decided not to allow the inclusion of such expenditure in the cost of the real property:

the taxpayer may apply to the Solicitor-General to appoint an independent assessor to provide an assessment of the amounts sought to be included as expenditure, in the cost of the real property, including any expenditure incurred in carrying out improvements to the real property<sup>17</sup>.

## Exempt Capital Gains

28. There are number of exemptions available to a taxpayer who has made a gain from the disposal of the real property. These exemptions are available to assist taxpayers, promote growth in targets sectors or to reduce administrative costs. The exemptions are discussed henceforth.

### Gain does not exceed \$16,000 – De Minimis [Section 67(1)(a)]

29. A capital gain made by Fiji resident or a Fiji citizen that does not exceed \$30,000<sup>18</sup>. The exemption is a *de minimis* exemption included for administrative convenience.
30. Therefore, if a taxpayer sells real property and upon calculation of the gain made on the sale of the real property ascertains that the gain does not exceed \$30,000, the said gain would be exempt from capital gains tax.

### First Residential Property or Principal Place of Abode [Section 67 (1)(b)]

31. There has been numerous discussion amongst the taxpayer community on how this exemption is to operate. Initially, the legislative provision was read and interpreted as applying to the first residential property which the taxpayer had acquired, and any subsequent residential property in which the taxpayer had their principal place of abode.

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<sup>17</sup> Section 85(11) of the ITA 2015

<sup>18</sup> Effective 1<sup>st</sup> August 2020

32. However, this was not the intention of the legislature. The intention was that only the capital gain made on the first disposal of an individual's first residential property or principal place of residence is an exempt capital gain<sup>19</sup>.
33. This means that the exemption is available to a taxpayer once.

#### First Residential Property

34. A "first residential property" is defined as meaning the residential property that a resident individual or Fiji citizen has acquired, and has sole or joint ownership with his or her spouse. Spouse includes a spouse under a de-facto relationship<sup>20</sup>.
35. This means that if the (real) property is jointly owned by the taxpayer and someone apart from their spouse (including a spouse under a de facto relationship), the property cannot be regarded as the "first residential property" for the purposes of the exemption.
36. Vacant land does not qualify as a residential property and therefore cannot qualify for an exemption under section 67(1)(b) of the Act.
37. Strata titles are also regarded as first residential property if it is the first residential property that the Fijian resident or citizen has acquired either solely or jointly with their spouse. A strata title allows the taxpayer individual ownership of part of a property (such as an apartment) with shared ownership of the remainder (such as foyer or driveway).
38. A person may not necessarily be residing or have resided in the first residential property at the time of disposal in order to qualify for the exemption. Relevance is placed on "ownership" rather than occupation of the said property<sup>21</sup>.
39. The person may qualify for the exemption as long as the following conditions are satisfied:
- a. The exemption is available to a resident or a Fijian citizen (including someone who holds a dual citizenship) only;
  - b. The real property includes a dwelling and is not vacant; and

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<sup>19</sup> Made evident in Bill 47 of 2016 – Explanatory note 2.10

<sup>20</sup> Defined in section 2 of the ITA 2015 and section 42 of Family Law Act 2003

<sup>21</sup> Section 67(4)(1)(a) of ITA 2015

- c. The property was the first acquisition and ownership of the taxpayer, or of the taxpayer with their spouse.

### Principal Place of Abode

- 40. The principal place of abode simply refers to place of residence where the individual lives<sup>22</sup>. In order to qualify for the exemption, the taxpayer must be residing in the real property at the time of disposal.
- 41. In the recent case law of Taxpayers J1 and J2 v Fiji Revenue and Customs Authority [2018] FJTT 1; ITA6.2016 (13 March 2018) where the taxpayer had claimed that the real property was their principal place of abode (and their first residential property as well) although they had moved overseas, the tribunal said the following:

*“[28] ... For the sake of completeness in any event, the Tribunal does not accept that the former home of the Taxpayer at the relevant time, was also her principal place of residence at the time of its disposal. As mentioned earlier, the immigration records do not support that fact and more tellingly, the property was being rented out by the Taxpayer, as she had been living overseas. At the time of disposal, the property was not the Taxpayer’s principal place of residence...”*

### **Disposal amongst Current Owners [Section 67(1)(f)]**

- 42. A capital gain made by a resident individual or a Fiji Citizen on disposal of his or her interest in a family home, provided however that the disposal of the interest is by way of transfer to an existing joint tenant or tenant in common is exempt from capital gains tax<sup>23</sup>.  
A joint tenant or a tenant in common has legal interest or ownership in the real property.
- 43. A “family home” means a residential property in which family members, whether immediate or extended, hold an interest as joint tenants or tenants in common. The family members need not reside in the residential property during the transfer to qualify for the exemption.

For example, the Smith family own a family home where each member holds interest in the land as tenants in common:

- a. James Smith                      30% ownership
- b. Lynda Smith                        30% ownership
- c. Jenifer Smith                        20% ownership
- d. Jonathon Smith                      20% ownership

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<sup>22</sup> Section 67(4)(1)(b) of ITA 2015

<sup>23</sup> Section 67(1)(f) of the ITA 2015

Jonathon Smith (son) decides to transfer his entire ownership in the family home to Jenifer (sister). According to the arm's length principle, Jonathon makes a gain on the disposal of his interest in the family home. However, this gain would be exempt from capital gains tax under section 67(1)(f) of the ITA 2015.

### **Disposal by Trustee or Beneficiary of a Deceased Estate [Section 67(1)(h)]**

44. A capital gain:
- a. made by a trustee or beneficiary of a deceased estate on the disposal of an asset forming part of the estate (in this case, the real property); and
  - b. if the gain had been made by the deceased on a disposal of the asset immediately before death the gain would be an exempt capital gain to the deceased;

the gain made would be exempt from capital gains tax provided that the asset is disposed of by the trustee or beneficiary within 2 years after the death of the deceased or within such further time as the CEO allows.

45. In other words, if the disposal of an asset of a deceased person would have given rise to an exempt capital gain had the asset been disposed of by the deceased immediately prior to his or her death, then a subsequent disposal of the asset by the executor or beneficiary of his or her estate also gives rise to an exempt capital gain.
46. The 2-year period is intended to take account of the time that it may take to fully execute a deceased estate, particularly taking account of the fact that the deceased's will may be disputed.
47. For example, Ramesh has inherited real property from his late father who had passed on approximately 3 years ago. The property was the first residential property of Ramesh's late father. Upon inheriting the said property, Ramesh sells the real property to an interested buyer.

Ramesh seeks an exemption under Section 67(1)(h) of the Income Tax Act 2015.

The property would have been exempt if the same had been disposed of by Ramesh's father prior to his death. However, the exemption is only available for a period of 2 years or within such further time as the CEO allows. However, the CEO may consider additional factors such as reason for delay (such as

dispute in relation to the will) Having regard to the circumstances on a case by case basis, the CEO may approve the exemption under Section 67(1)(h) of the Income Tax Act 2015. If approved, the disposal would essentially have the same tax treatment as if it was disposed by Ramesh's late father.

In contrast, if the property would not have been exempt if the same had been disposed by Ramesh's father prior to his death, (that is, it was not the first residential property nor it qualify for any other exemption), Ramesh would have to account for CGT on the disposal as if he was making the disposal.

### **Deferral of Recognition of Gain or Loss**

48. There may be situations where instead of being exempt, the gain or loss made on the disposal is deferred. This simply means that the gain or loss is rolled over to the new owner of the real property and no gain or loss is taken to arise on the disposal.
49. In such cases, the new owner pays CGT on the gain that would have been made by the initial owner including any CGT applicable on any further gain made by the new owner.

#### Divorce or Matrimonial Settlement<sup>24</sup>

50. Where the real property is disposed between spouses as part of a divorce settlement or under an agreement to live apart, no gain or loss is taken to arise on the disposal.

For example, Mr. and Mrs. Smith are separating and as part of their divorce settlement (as documented in the deed of settlement) have agreed to transfer land initially being owned by Mr. Smith to Mrs. Smith. The CEO of FRCS would not recognize any gain or loss arising from the disposal as the transfer has been effected due to divorce or matrimonial settlement.

Similarly, for those living in a de-facto relationship, where a transfer of real property is made between the de-facto spouses in an agreement to live apart, no gain or loss arising from the disposal would be recognized.

In contrast, if the terms of the matrimonial settlement require a cash payment from one party to another, and one party sells a real property to the public to raise funds in order to effect the payment, the same would not be subject to the deferral as there is no disposal of the real property between

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<sup>24</sup> Section 87(1)(a) of ITA 2015

spouses. In such cases, CGT may be applicable depending on whether the taxpayer qualifies for other exemptions or deferrals.

#### Transmission on Death<sup>25</sup>

51. Where the real property is disposed by reason of the transmission of the asset on the death of a person to an executor or beneficiary, no gain or loss is taken to arise on the disposal.

For example, Mrs. Khan upon her passing bequeaths her real property to her daughter as per the terms of her will. As transmission on death gives rise to a deferral, the CEO will not recognize the gain or loss made on the disposal. Similarly, if Mrs. Khan had died intestate, or without leaving a will, any disposal to the executor and to any beneficiaries subsequently would give rise to a deferral as well.

#### Disposal by Love and Affection<sup>26</sup>

52. Where the real property (including a principal place of residence, first residential property, an interest in a capital asset) has been disposed by reason of love and affection between spouses, siblings, parents to children and vice versa, and grandchildren to grandparents and vice versa, no gain or loss is taken to arise on the disposal.

For example, Jonathon is transferring his real property to his son John. There is no consideration involved, as such, the transfer is done on the basis of natural love and affection. As the disposal by natural love and affection gives rise to a deferral, the CEO of FRCS will not recognize the gain or loss made on the disposal.

If the real property was Jonathon's first residential property or principal place of abode, John is deemed to have acquired the real property at the fair market value of the real property at the time of disposal. Please refer to paragraph 58 for further discussion on the same.

53. Section 87(3)(a) provides that if the above deferrals apply, the real property would retain its character in the hand of the transferee.

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<sup>25</sup> Section 87(1)(b) of ITA 2015

<sup>26</sup> Section 87(1)(c) of ITA 2015 – Section 87(1)(d) is not relevant for real property and is therefore, not discussed in this SIG.

For example, if the transferred real property is trading stock in the hands of the transferor, then it is also trading stock for the transferee. This is the case even if the transferee does not carry on business or deal in real property.

Similarly, if the transferor acquired the real property with the purpose of reselling it at a profit (so that any gain on disposal) is included in property income under section 18(1)(b) of ITA 2015), the transferee is treated as acquiring an asset that is impressed with the character of a profit-making asset.

However, if the real property that has been disposed is a principle place of abode or a first residential property of the transferor (vendor), the real property would only retain its character as such if the real property is the principle place of abode or a first residential property of the transferee (recipient).

54. If a principle place of abode or a first residential property has been disposed and the disposal has been deferred under section 87 (1) (a)(b) or (c) of the ITA 2015, the transferee is deemed to have acquired the real property at the fair market value of the real property at the time of disposal.

The rationale behind this specific rule is that the disposal of the first principle place of abode or first residential property would have been exempt in the hands of the transferor. In order to give effect to the exemption the transferee is deemed to have acquired the real property at the fair market value of the real property at the time of disposal.

55. In any other case, the transferee is deemed to have acquired the real property at the cost of the real property at the time of disposal. For example, if the transferor had acquired the real property for \$10,000<sup>27</sup>, the transferee is deemed to have acquired the real property for \$10,000 as well.

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<sup>27</sup> Under section 85 of the ITA 2015

## INCOME TAX

56. There may be instances where income tax is applicable on a sale of real property instead of capital gains tax. It is worth noting that either capital gains tax or income tax would apply on the disposal of the real property, and not both. There may be instances where income tax is applicable on the building and CGT applicable on the land. This is discussed later in the SIG.
57. In order for income tax to apply instead of capital gains tax, the disposal of the real property must be caught under sections 17 or 18 of the Income Tax Act 2015.

### Business Income [Section 17]

58. In the introduction, we stated that the SIG applies to taxpayers who are not in the business of dealing in real property. However, there may be instances when section 17 may still be applicable.
59. For section 17 to apply the net gain which arises from the disposal of:
- i. the conduct of a venture or concern in the nature of a trade, commerce, agriculture or manufacture;
  - ii. the carrying on or carrying out of a profit-making undertaking or scheme; or
  - iii. the disposal of an asset, other than trading stock or an asset subject to sub-paragraph (i) or (ii), held on revenue account by a person in carrying on a business;
60. In application of section 17 to real property, if the asset is held on revenue account by a person in carrying on a business then the net gain made from the disposal of the real property would be included in gross income<sup>28</sup> and therefore subject to income tax.
61. A person may hold an asset of a business on revenue account even though the person does not trade in the asset if the asset has been acquired in circumstances where it may be reasonably expected that the asset will be disposed of for a profit.

For example, the shares or other financial assets of a banking or insurance company may be acquired as an investment, but in circumstances where it is always expected that the assets may have to be sold for a profit to meet the claims of creditors.

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<sup>28</sup> Section 14 of ITA 2015

## Property Income [Section 18]

62. In addition to section 17, disposal of real property may also be captured under section 18 of ITA 2015 for the same to be captured under income tax rather than capital gains tax.

63. The relevant provision in section 18 is section 18(1)(b) which states:

*Property income*

*18.— (1) ... the following are included in the property income of a person—*

*(b) the net gain from the disposal of an asset that was acquired for the purpose of disposal at a profit;*

64. Therefore, if it is established that a real property was acquired for the purpose of disposal at a profit, any net gain from the disposal of the real property would be regarded as property income and subsequently added to gross income of the taxpayer.

65. The determination of whether the property was acquired for the purpose of disposal at a profit is done on a case by case basis. However, the CEO will look at the following factors:

- a. **Holding period** – a holding period below 3 years may demonstrate that the taxpayer had acquired the real property for purposes of resale at a profit.
- b. **Reason for sale** – if the reason for sale is determined to be to maximise gain then an inference can be made that there was a profit motive at acquisition. There may be instances where the sale is forced due to court orders or financial constraints. In these cases, the CEO may consider application of capital gains tax rather than income tax.
- c. **Is there a series of disposal?** – if the taxpayer has disposed a number of real property in quick succession, then it can be inferred that there was a profit motive at acquisition.

In contrast, the case of *McClelland v Commissioner of Taxation*<sup>29</sup>, the Privy Council concluded that a single transaction can fall within the notion of assessable income, where the undertaking or scheme exhibits features that give it the character of a business deal.

- d. **Purpose of acquisition of real property** – in some cases taxpayers may have acquired the property to earn passive income (rent). While this does not explicitly show the profit making motive but it may be a determinant while taking into account all the other factors mentioned above.

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<sup>29</sup> (1970)120 CLR 487

If a property was acquired for subdivision as an investment property there is clear indication that there is a profit making motive at the time of acquisition, regardless of whether the taxpayer was able to fulfil the acquisition purpose at the time of disposal.

In *Company L v Fiji Revenue and Customs Authority* [2012] the court deliberated:

*"[52] This was a planned development that ultimately was not completed by the Taxpayer. I believe that on the evidence, that the Taxpayers business and the profit arising out of the acquisition, development and disposition of the properties, came about due to the carrying out or carrying on of an undertaking or scheme"*

66. Ordinarily similar matters which have been disputed in court have resulted in *dicta* around the *Californian Copper Syndicate v Harris*<sup>30</sup> case, where Lord Justice Clerk, formulated the long accepted test:

*"where the owner of an ordinary investment chooses to realise it, and obtains a greater price for it than 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..."*

In *Taxpayer R v Fiji Revenue and Customs Authority* [2017] FJTT 1; ITA2.2016 (19 May 2017) the Tribunal deliberated on the California Copper case:

*"[13] If Californian Copper is to provide some guiding light, then the question seems to be whether the proceeds arise out of "merely a realization or change of investment" and not "an act done in what is truly the carrying on or carrying out of a business..."*

67. For the disposal to be caught under section 18 of the ITA, emphasis is placed on profit motive at the point of acquisition.
68. If caught under section 18 of the ITA 2015, the calculation of the net gain from the disposal is the consideration for the disposal of the asset reduced by the cost of the asset at the time of disposal<sup>31</sup>. This calculation is similar to how the gain is calculated under capital gains tax.

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<sup>30</sup> (1904) 5 T.C. 159

<sup>31</sup> Section 18(3) of the ITA 2015.

## Sale of a Depreciable Asset

69. The structural improvement to the land or the building is classified as a depreciable asset as the building:
- has a useful life exceeding one year;
  - is likely to lose value as a result of normal wear and tear or obsolescence; and
  - is used to derive rental income which is included in gross income<sup>32</sup>.
70. Prior to 1st August 2020, a depreciable asset did not qualify as a capital asset and any disposal of a depreciable asset would be subject to income tax if depreciation was claimed on the asset. However, from 1st August 2020, a depreciable asset qualifies as a capital asset (unless the same is trading stock or is caught under section 17 and 18 of the ITA 2015)
71. Section 34 of the ITA 2015 provides rules for the taxation of depreciable assets which is applicable in situations where real property is disposed with a building (depreciable asset).
72. When the real property with a building is sold the following implications arise<sup>33</sup>:

Where...	
<b>Consideration exceeds written down value (excess)</b>	Any depreciation claimed on the asset up to the amount of the excess is included in the gross income of the taxpayer
	The excess is subject to Capital Gains Tax under Part 3 of the Income Tax Act 2015
<b>Consideration is less than written down value (loss)</b>	The loss is allowed as a deduction against gross income of the taxpayer

73. For example, Jonathon an employee of an engineering firm owns a residential dwelling with which he earns rental income. The residential dwelling was acquired on 1<sup>st</sup> January 2010 for \$250,000 and Jonathon has been claiming depreciation from 2010 onwards. On 1<sup>st</sup> November 2020, Jonathon sells the property for \$300,000. The tax implications will be as follows:

Cost	Accumulated Depreciation	Written Down Value	Consideration on Sale
\$250,000	\$56,250 [9 years at \$6250]	\$193,750	\$300,000

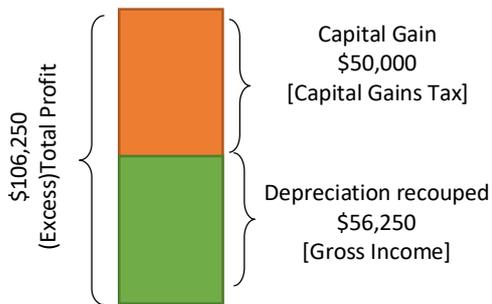
Depreciation was claimed on a straight line method at a rate of 2.5% per annum (\$6250). Depreciation for 2020 will not be allowed.

<sup>32</sup> Section 2 of the ITA 2015.

<sup>33</sup> Section 34(1) of the ITA 2015

In the above case, the consideration exceeds the written down value by \$106,250, therefore the following will eventuate:

- a. Depreciation of \$56,250 claimed will be included in the gross income of the taxpayer (subject to income tax); and
- b. The excess of the consideration over cost \$50,000 will be subject to Capital Gains tax.



74. For further information and clarification in regard to this SIG, please email us at [tipu@frcs.org.fj](mailto:tipu@frcs.org.fj)

**APPENDIX ONE: PROPERTY INCOME (SECTION 18 of ITA 2015)**

<b>Factors to determine whether taxpayer had acquired the real property for disposal at a profit</b>	
<b>Factor</b>	<b>Rule of Thumb</b>
Holding Period	Less than 3 years
Reason for Sale	Sale meant to maximise gain Not a forced sale (court order, matrimonial settlement)
Series of disposals	if yes, a scheme for profit may be established
Reason for acquisition	Acquired for land development and resale Acquired to earn revenue

## APPENDIX TWO: LEGISLATION

### INCOME TAX ACT 2015

#### [Section 2] Interpretation

“arm’s length transaction” means a transaction between persons dealing at arm’s length with each other;

“capital asset” means—

(a) real property, a structural improvement to real property, an interest in real property or an interest in a structural improvement to real property, and includes the following—

- (i) a lease of real property;
- (ii) a lease of a structural improvement to real property; or
- (iii) an exploration, prospecting, development, or similar right relating to real property;
- (iv) information relating to a right referred to in sub-paragraph (iii);

(b) a ship or boat;

(c) a yacht;

(d) a membership interest in a company, security, or other financial asset;

(e) an intangible asset;

(f) an interest in a partnership or trust;

(g) an airplane, helicopter or other aircraft;

(h) an option, right or other interest in an asset referred to in the foregoing paragraphs,

but does not include an asset that is trading stock, or a business intangible;

“de facto spouse” in relation to an individual, means an individual not of the same sex, who lives with the first-mentioned individual as spouses on a genuine domestic basis although not legally married to each other;

“depreciable asset” means any tangible personal property or structural improvement to real property that—

(a) has a useful life exceeding one year;

(b) is likely to lose value as a result of normal wear and tear, or obsolescence; and

(c) is used wholly or partly to derive income included in gross income;

“disposal”, in relation to an asset, has the meaning in section 84;

#### [Section 14] Income included in gross income

1) Subject to this Act, the gross income of a person for a tax year is the total of the following—

(a) employment income, business income, and property income derived by the person during the year;

(b) income according to ordinary concepts, other than income referred to in paragraph (a), derived by the person during the year;

(c) unexplained and unidentified deposits during the year in any bank account if the deposit can be sourced to the person;

(d) income that a section of this Act includes in the gross income of the person for the year; and

(e) forfeited deposits and instalments on capital assets.

#### [Section 17] Business income

17.—(1) The following are included in the business income of a person conducting a business—

(c) the net gain from—

(i) the conduct of a venture or concern in the nature of a trade,

commerce, agriculture or manufacture;

(ii) the carrying on or carrying out of a profit-making undertaking or scheme; or

(iii) the disposal of an asset, other than trading stock or an asset subject to sub-paragraph (i) or (ii), held on revenue account by a person in carrying on a business;

#### [Section 18] Property income

18.— (1) Subject to subsection (2) and section 19, the following are included in the property income of a person—

(b) the net gain from the disposal of an asset that was acquired for the purpose of disposal at a profit;

#### [Section 34] Disposal of Depreciable Asset

(1) Subject to this section, if a person disposes of a depreciable asset in a tax year the person is not allowed a depreciation deduction for the year and—

a) any excess of the consideration for the disposal of the asset over the written down value of the asset at the time of disposal, up to the total amount of depreciation deduction previously allowed in respect of the asset, is to be included in the gross income of the person for that year; and

b) where the asset is a capital asset, any excess of the consideration over the cost of the asset does not form part of the total income, but is to be subject to Capital Gains Tax in accordance with Part 3; or

c) if the written down value of the asset at the time of the disposal exceeds the consideration for the asset, the person is allowed a deduction in that year for the amount of the excess.

#### [Section 65] Tax

#### Imposition of Capital Gains Tax

**65.—**(1) Subject to this Act, a tax to be known as “Capital Gains Tax” is imposed at the rate prescribed by Regulations made under this Act on a person who has made a capital gain, other than an exempt capital gain, on the disposal of a capital asset.

(2) The Capital Gains Tax payable by a person on the disposal of a capital asset is computed by applying the rate prescribed by Regulations made under this Act to the amount of the capital gain arising on the disposal.

(3) If the person who has made a capital gain is a non-resident person, subsection (1) applies only if the capital asset is a Fiji asset.

**[Section 66] Capital gain**

**66.—**(1) The capital gain made by a person on the disposal of a capital asset is the consideration for the disposal reduced by the cost of the asset at the time of the disposal.

(2) A capital gain made by a person on disposal of a capital asset is not reduced by any capital loss on the disposal of another capital asset.

(3) A capital gain made by a person on the disposal of a capital asset is reduced by any part of the gain that is included in the gross income of the person or that is exempt income.

**[Section 67] Exempt capital gains**

**67.—**(1) The following capital gains are exempt capital gains—

(a) a capital gain made by a resident individual or Fiji citizen that does not exceed FJD\$30,000;

(b) a capital gain made by a resident individual or a Fiji Citizen on the first disposal of either the individual’s first residential property or principal place of residence;

(c) a capital gain made by a person on the disposal of shares listed on the South Pacific Stock Exchange;

(d) a capital gain made on disposal of an asset that is used solely to derive exempt income;

(e) any gain made by a person on the disposal of an interest in a company within paragraph (c) of the definition “company” in section 2;

(f) a capital gain made by a resident individual or a Fiji Citizen on disposal of his or her interest in a family home, provided however that the disposal of the interest is by way of transfer to an existing joint tenant or tenants in common;

(g) a capital gain made by a resident person from the sale of shares where a private company goes through re-organisation, restructure or amalgamation for the purposes of listing or as part of a listing process on the South Pacific Stock Exchange, provided that—

(i) the private company is listed on the South Pacific Stock Exchange within 24 months from the date of commencement of re-organisation, restructure or amalgamation; and

(ii) where the private company is not listed with the South Pacific Stock Exchange in accordance with sub-paragraph (i), the gain from the re-organisation, restructure or amalgamation of

the private company shall be taxable under this Act;

(h) a capital gain made by the trustee or beneficiary of a deceased estate on the disposal of an asset forming part of the estate that, if the gain had been made by the deceased on a disposal of the asset immediately before death, the gain would be an exempt capital gain to the deceased under this subsection, but only when the asset is disposed of by the trustee or beneficiary within 2 years after the death of the deceased or within such further time as the CEO allows.

(2) If the CEO is satisfied that a capital asset has been disposed of in 2 or more parts for the purpose of taking advantage of subsection (1)(a), any capital gain arising from the disposals is exempt under subsection (1)(a) only if the total gain from the disposal of all parts does not exceed \$16,000.

(3) In the case of the disposal of a capital asset that is jointly owned, subsection (1) (a) applies only if the total capital gain made by all owners of the asset on disposal of the asset does not exceed \$16,000.

(4) For the purposes of—

(a) subsection (1)(b)—

(i) “first residential property” means the first residential property that a resident individual or Fiji citizen has acquired, and who has sole ownership or co-owns the same with his or her spouse and includes a spouse living in a de facto relationship as defined in the Family Law Act 2003; and

(ii) “principal place of residence” means the place of residence where the individual lives; and

(b) subsection (1)(f), “family home” means a residential property in which family members, whether immediate or extended, hold an interest as joint tenants or tenants in common.

**[Section 84] Disposal**

**84.—**(1) A person makes a disposal of an asset if the person parts with the ownership of the asset, including when the asset is—

(a) sold, exchanged, transferred or distributed; or

(b) cancelled, redeemed, relinquished, destroyed, lost, expired or surrendered.

(2) A person disposes of an asset at the time the person parts with the ownership of the asset, including when the person ceases to have legal title to the asset and when the asset is sold, exchanged, transferred, distributed, cancelled, redeemed, relinquished, destroyed, lost, expired or surrendered.

(3) If a person creates an asset in another person being an asset that did not previously exist, the first-mentioned person is treated as having made a disposal of the asset to the second-mentioned person and the disposal occurs when the asset is created.

(4) The transmission of an asset by succession or under a will is treated as a disposal of the asset by the deceased

and the disposal occurs at the time the asset is transmitted.

(5) A disposal includes the disposal of a part of an asset.

(6) If a trustee-in-bankruptcy, liquidator, or receiver disposes of an asset of a person, the person is treated as having made the disposal and the CEO can collect the tax payable by the person in respect of the disposal from the trustee-in-bankruptcy, liquidator, or receiver in accordance with section 26 of the Tax Administration Act 2009.

**[Section 85] Cost**

85.—(1) Subject to this Act, this section establishes the cost of an asset for the purposes of the Act.

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

(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;

(c) any expenditure incurred by the person to install, alter, renew, reconstruct or improve the asset.

(3) Subject to this section, the cost of an asset of a person that is an intangible asset is the total expenditure incurred by the person in acquiring, creating, improving and renewing the intangible asset, and any incidental expenditure incurred in acquiring or disposing of the intangible asset.

(4) The cost of an asset of a person includes any amount given for the grant of an option to the person to acquire the asset.

(5) The cost of an asset of a person is reduced by the amount of any deduction allowed to the person under Part 2 in respect of amounts included in the cost of the asset, other than a depreciation or amortisation deduction.

(6) An amount is included in the cost of an asset on the earlier of the date that it is paid or payable.

(7) If a person disposes of a part of an asset, the cost of the asset is apportioned between the part of the asset retained and the part disposed of in accordance with their respective fair market values determined at the time the person acquired the asset.

(8) The cost of an asset of a person does not include the amount of any grant, subsidy, rebate, commission, or other assistance received or receivable by the person in respect of the acquisition of the asset, except to the extent to which the amount is included in the gross income of the person.

(9) The reference to “other assistance” in subsection (8) does not include a loan repayable with or without interest.

(10) If the acquisition of an asset by a person is the derivation of an amount—

(a) included in the gross income of the person, the cost of the asset is the amount so included plus any amount paid by the person for the asset; or

(b) that is exempt income, the cost of the asset is the exempt amount plus any amount paid by the person for the asset.

(11) If—

(a) a person seeks to include an amount of expenditure in the cost of a capital asset, including expenditure incurred in carrying out improvements to a capital asset;

(b) the person is unable to produce any record of the expenditure; and

(c) the CEO, after carrying out such investigation as he or she considers appropriate, has decided not to allow the inclusion of any such expenditure in the cost of the capital asset,

the person may apply to the Solicitor-General to appoint an independent assessor to provide an assessment of the amounts sought to be included as expenditure in the cost of the capital asset, including any expenditure incurred in carrying out improvements to the capital asset.

(12) The person appointed as an independent assessor under subsection (11) must be a person suitably qualified in carrying out valuation and assessment of such expenditure, and may include any person employed by the Government.

(13) The decision and assessment of the independent assessor appointed under subsection (11) is final and binding on all parties.

(14) The costs incurred in the appointment of, and assessment by, the independent assessor are to be borne by the Solicitor-General.

**[Section 86] Consideration**

86.—(1) Subject to this Act, this section establishes the amount of consideration for the disposal of an asset for the purposes of the Act.

(2) The consideration for the disposal of an asset is the total amount received or receivable for the asset, including the fair market value of any consideration in kind determined at the time of the disposal.

(3) The consideration for the disposal of an asset includes the consideration for the grant of an option in relation to the asset if the person has not been subject to tax in respect of any income or capital gain made on the grant of the option.

(4) If an asset has been lost or destroyed by a person, the consideration for the asset includes any compensation, indemnity, or damages received by the person as a result of the loss or destruction, including amounts received or receivable as a consequence of—

(a) an insurance policy, indemnity, or other agreement;

(b) a settlement; or

(c) a judicial decision.

(5) If two or more assets are disposed of by a person in a single transaction and the consideration for each asset is not specified, the total consideration for the disposal is apportioned among the assets disposed of in proportion to their respective fair market values determined at the time of the disposal.

(6) An amount is included in the consideration for the disposal of an asset on the earlier of the date that it is received or receivable.

**[Section 87] Deferral of recognition of gain or loss**

87. —(1) For the purposes of this Act and subject to subsection (2), no gain or loss is taken to arise on the disposal of any of the following—

(a) an asset between spouses as part of a divorce settlement or under an agreement to live apart;  
(b) an asset by reason of the transmission of the asset on the death of a person to an executor or beneficiary;  
(c) a principal place of residence, first residential property, an interest in a capital asset, or shares in a company, by reason of love and affection between spouses, siblings, parents to children and vice versa, and grandchildren to grandparents and vice versa; or  
(d) an asset by reason of the loss, destruction or compulsory acquisition of the asset (referred to as the “replaced asset”) if the consideration for the disposal is reinvested by the recipient in an asset of a like kind (referred to as a “replacement asset”) within one year of the disposal or within such further period as the CEO allows.

(2) If the person acquiring an asset referred to in subsection (1)(a), (b), or (c) is a non-resident person at the time of the acquisition, subsection (1) applies only if—

(a) a subsequent disposal of the asset by the non-resident will give rise to an amount included in the gross income of, or allowed as a deduction to, the non-resident person; or

(b) the asset is a Fiji asset.

(3) If subsection (1)(a), (b), or (c) applies, the person acquiring the asset is treated as acquiring—

(a) subject to subsection (4), an asset of the same character as the person disposing of the asset; and

(b) the asset for an amount equal to—

(i) for an asset that was the principal place of residence or first residential

property of the person disposing of the asset immediately before the disposal, the fair market value of the residence at the time of the disposal; or

(ii) for any other asset, the cost of the asset for the person disposing of the asset at the time of the disposal.

(4) If the asset to which subsection (3) applies is the principal place of residence or first residential property of the person disposing of the asset immediately before the disposal, the asset retains that character only if the person acquiring the asset uses the asset as their principal place of residence.

(5) If subsection (1)(d) applies and the consideration given by the person for the replacement asset is equal to or exceeds the consideration received or receivable for the replaced asset, the cost of the replacement asset is the cost of the replaced asset at the time of disposal increased by the amount of the excess, if any.

(6) If subsection (1)(d) applies and the consideration received or receivable for the replaced asset exceeds the consideration given for the replacement asset, the cost of the replacement asset is the cost of the replaced asset at the time of disposal reduced by the amount of the excess.

(7) Section 34(3) and not subsection (1)(d) applies if the asset is a depreciable asset.

(8) In this section, “first residential property” and “principal place of residence” have the meanings in section 67(4).

**[Section 89] Non-arm’s length transaction**

89. Subject to section 63, if an asset is disposed of by a person in a transaction that is not an arm’s length transaction—

(a) the person disposing of the asset is treated as having received consideration equal to the fair market value of the asset determined at the time the asset is disposed of; and

(b) the person acquiring the asset is treated as having a cost equal to the amount determined under paragraph (a).