STANDARD INTERPRETATION GUIDELINE 2021-18

INCOME TAX ACT 2015 – SECTION 88 - RE-ORGANISATION

This Standard Interpretation Guideline (SIG) sets out Fiji Revenue and Customs Service's (FRCS) policy and operational practice in relation to the deferral rules under section 88 of the Income Tax Act 2015 available for disposal of assets between an individual or partnership to a company and between resident group companies.

It 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 and its Regulations (unless otherwise stated)

This SIG is in effect from 1 August 2021 and replaces SIG 2020-32. The SIG may need to be reviewed in the event of any relevant legislative amendments.

CONTENT

PURPOSE

1. The purpose of this Standard Interpretation Guideline (SIG) is to provide guidance to the taxpayer community on the deferral rules for the recognition of a gain on the transfer of assets between resident individuals and partnerships to transferee companies and between group companies under section 88 of the Income Tax Act 2015.

2. The Chief Executive Officer (CEO) has received a number of applications from taxpayers for confirmation of the applicability of section 88 on the disposal of assets. As such, the CEO has acknowledged the need to provide awareness to the general taxpayer community on the same.

3. The need to provide awareness is further created by changes to section 88 of the Income Tax Act 2015 brought upon by the 2021-2022 National Budget amendments.

INTRODUCTION

4. Prior to the effective date of the SIG, section 88 of the Income Tax Act 2015 was only applicable to individual and corporate reorganisation disposals. However, from 1st August 2021, the scope of section 88 has been widened to include transactions between a resident partnership to a transferee company which is wholly owned by the partners in the resident partnership.

   Furthermore, the definition of group companies has been widened to include arrangements where the transferor and transferee companies that are owned by common shareholders, qualify for deferral as well.

5. Reorganization by an individual refers to when a resident individual may transfer their assets into a company at the point of incorporation of the company or as a means of contributing additional capital. In most cases, such disposal does not change the underlying economic ownership of the asset and there is no gain or loss incurred by the individual.

   Similarly, reorganisation by a partnership refers to when a resident partnership transfers their assets into a company at the point of incorporation of the company. As with individual organization, such disposal does not change the underlying economic ownership of the asset and there is no gain or loss incurred by the partnership.

6. A corporation may undergo restructuring or reorganisation for various strategic reasons such as
   a) merger;
   b) consolidation;
   c) corporate divisions;
   d) asset or share acquisition; or
   e) in order to meet changing regulatory requirements.

7. Reorganization has become an increasingly relevant topic in Fiji leading to the question of how entities involved in reorganisation transactions, as well as their shareholders, should be taxed for the transfer of assets amongst the transferor individual and company with the transferee and transferee companies.

8. The Income Tax Act 2015 provides some rules in relation to the transfer of assets on such re-organisation. The Act recognizes that in these transactions, the economic ownership of the asset does not change and ultimately rests with the transferor individual or the transferor company.

9. The SIG discussed the income tax implications under section 88 of ITA 2015 only and does not discuss the VAT implications on the transfer or disposal.

10. 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 particulars case may be analogous with particular examples, but rather on the basis of applying the correct tests established by the law.

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

LEGISLATIVE ANALYSIS

12. The deferral rule under section 88 of the ITA 2015 is applicable in the following scenarios:
    a. when a resident individual or a resident partnership disposes of an asset, at the cost of the asset or, in the case of a depreciable asset at is written down value, to a resident company which is wholly owned by the transferor (individual and partnership reorganisation);
    b. when a resident company disposes of an asset, at a cost which is not in excess of the cost of the asset, to another resident group company (company reorganisation).

13. If the deferral rule under section 88 applies, then:
    a. no gain or loss is taken to arise on disposal of the asset
    b. the transferee or transferee company is treated as acquiring an asset of the same character as the asset disposed of by the transferor or transferor company; and
    c. the transferee or transferee company's cost on acquisition of the asset is equal to the transferor or transferor company's cost of the asset or, in the case of a depreciable asset, written down value at the time of disposal.

Consideration

14. If a, individual, partnership or company has acquired an asset for $1000, the transfer to the transferee company or to resident group company must not exceed $1000. The transfer may be at nil consideration but in order to qualify for the deferral, the transfer should not exceed the cost.

15. If the disposal or transfer is for consideration exceeding the cost, the fair market value must be used for transactions between associates[1]. The normal income tax rules would apply in such cases.

[1] Section 89 of ITA 2015.

16. For transfer of depreciable assets, the consideration should not exceed the written down value of the asset. This is to ensure that the depreciation deductions are not claimed repeatedly by the transferor and transferee on the same asset.

17. The deferral under section 88 of the ITA 2015 may also be claimed for individual assets. It is not necessary for the entire assets of the company to be disposed in order to qualify for the deferral for company reorganisation disposals.

Deferral of Gain on disposal of asset.

18. A deferral of a gain on disposal of an asset provides that no gain is recognised on the part of the supplier on the disposal but the gain is deferred to the recipient of the asset.

    For example, A had purchased an asset for $100 which has a current market value of $500. The asset is transferred to B (a related party) at no cost. Under normal rules, the transfer would be deemed to be provided at fair market value and A would have made a gain of $400 ($500 - $100) and B would be deemed to have acquired the asset at $500.

    The transaction if deferred would mean that B is treated to have acquired the asset for $100 and not at the market value of $500.

19. Furthermore, the asset is treated as having the same character in the hands of the transferee as it did in the hands of the transferor.

INDIVIDUAL AND PARTNERSHIP REORGANISATION

20. Section 88 of the Income Tax Act 2015 provides that the deferral rules for individual or partnership reorganisation are met when the following conditions are met:
    a) a resident individual or a resident partnership disposes of an asset to a resident company; and
    b) the transferee resident company is wholly owned by the resident individual or the partners in the resident partnership.

Individual Reorganisation

Resident Individual

21. An individual is a resident of Fiji if they satisfy the conditions under section 6 of the Income Tax Act 2015.

22. The CEO has issued a separate SIG in relation to the residency rules under the Income Tax Act 2015. The SIG [SIG 2018-32] can be accessed on the FRCS website or directly through the link below: https://www.frcs.org.fj/wp-content/uploads/2018/09/SIG-2018-32-Residency-for-Individuals.pdf

Resident Company

23. Section 88(4) of the Income Tax Act provides that a "company" for the purposes of the corporate re-organisation rules refers to incorporated bodies. Although "company" under its normal definition includes unincorporated bodies as well, the deferral rules are limited to where the transferee is an incorporated body only.

24. The deferral rules do not apply for asset disposals between a resident company and a non-resident company. This ensures that the deferral rules are not used to transfer an asset tax-free outside the Fiji tax base.

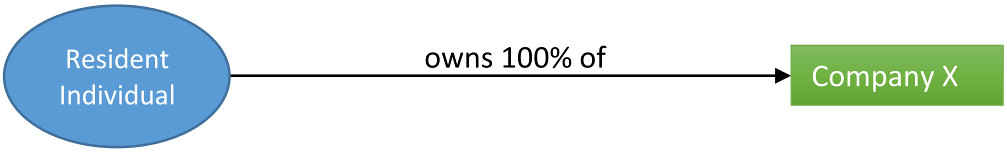
Transferee Resident Company to be wholly owned by the Resident Individual

25. In order to qualify for the deferral, it is required that the resident individual should wholly own the transferee resident company. This is achieved when 100% of the issued shares in the company is wholly owned by the transferor (individual)[2] either directly or through one more interposed persons.

26. An interposed person refers to an incorporated company[3].

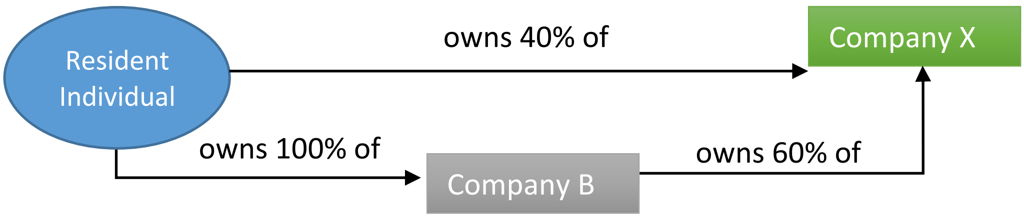
27. This is achieved through the following scenarios:

Direct Ownership



Resident Individual owns 100% of the shares in Company X

Indirect Ownership



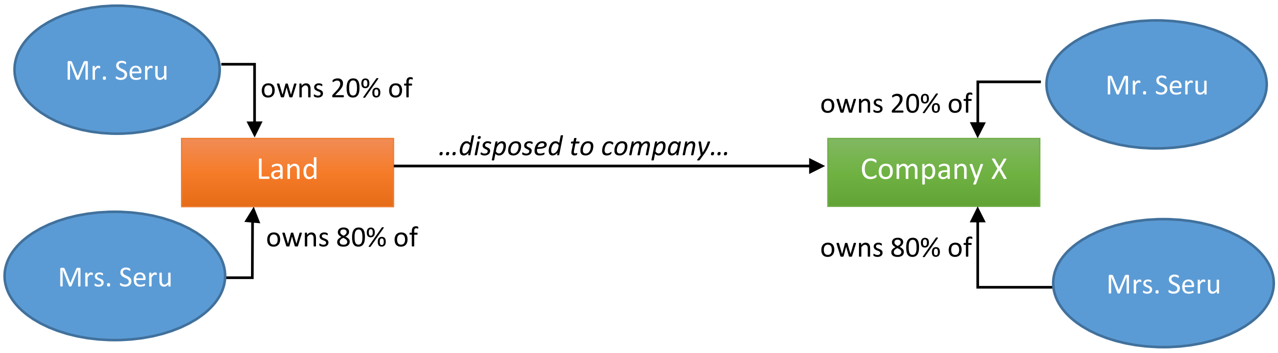
Resident Individual owns 40% of the shares in Company X directly and the remaining 60% is owned indirectly through an interposed person (Company B).

28. In the event that there is a collective disposal of an asset between resident co-owners of an asset, it is required that the percentage of ownership in the asset or the depreciable asset should be the same as their percentage of beneficial ownership of the issued shares in the transferee[4].

For example, Mr. and Mrs. Seru own a piece of land on a 20% and 80% basis respectively. In order to qualify for the deferral under section 88 of the ITA 2015, Mr. Seru should own 20% of the issued shares in the transferee company while Mrs. Seru should own 80% of the issued shares.

[2] Section 88(2A) of the ITA 2015
[3]
[4] Section 88(2B) of the ITA 2015

That is;



The deferral rules will not apply if a joint owner of an asset is disposing their ownership or interest in an asset. That is, in the above example, the deferral rule will not apply if only Mr. Seru disposes his 20% share of the land to the company. The co-owners of the asset must collectively transfer the asset to the transferee company.

Partnership Reorganisation
Resident Partnership

29. A partnership is a resident partnership when the partnership—
    a) is formed in Fiji; or
    b) has any part of its central management and control located in Fiji[5].

30. A partnership is formed in Fiji if the same is registered in Fiji or if the partnership agreement is executed in Fiji.

31. The determination of whether a partnership has any part of its central management and control located in Fiji is made by looking at a number of factors, such as:
    a) the location of directing authority of the partnership and not the day-to-day management of its operations; and
    b) the location of partners' meetings.

Transfer by a Resident Partnership to a Resident Company wholly owned by the Resident Partnership

32. In order for a resident partnership to qualify for deferral, it is required that the resident partnership (or the partners) should wholly own the transferee resident company. This is achieved when the percentage of ownership in the partnership (based on the profit sharing agreement) is the same as their percentage of beneficial ownership of the issued shares in the transferee company[6].

33. If the partnership is dissolved following the disposal of assets from the resident partnership to the transferee company, any disposal of assets by shareholders to the transferee company (as a means of

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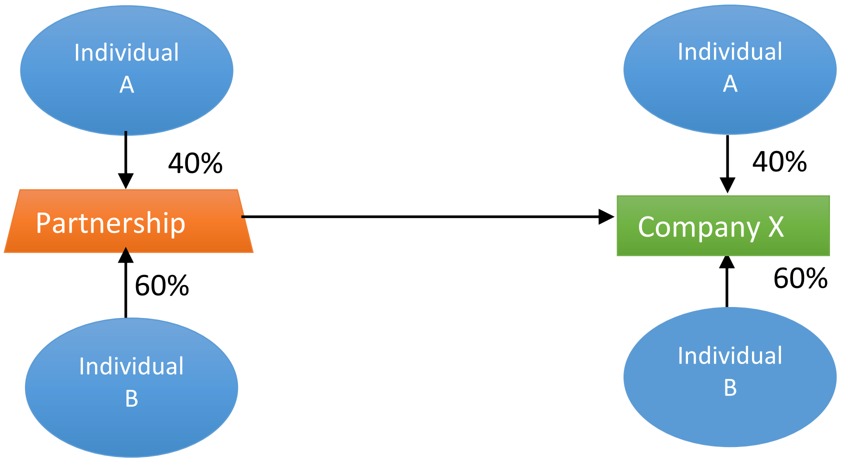
[5] Section 2 of the ITA 2015
[6]

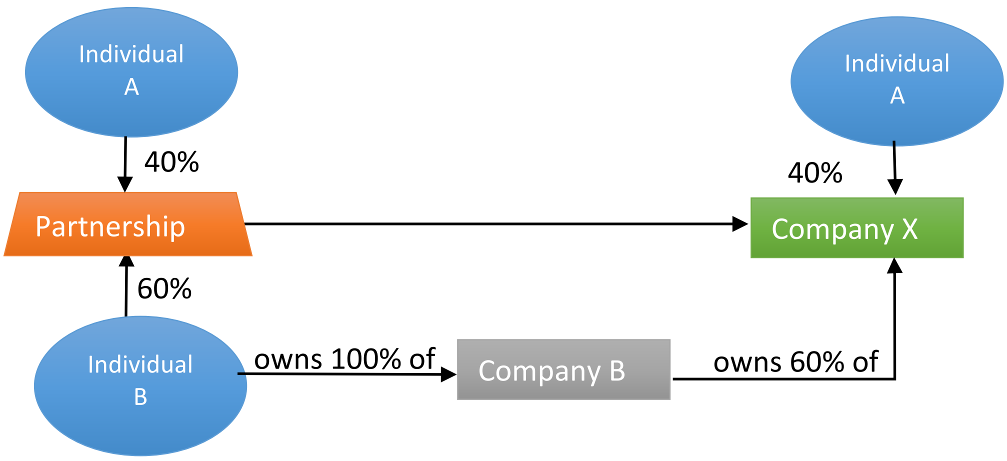
contributing additional capital) would need the meet the requirements of an individual reorganisation as the asset would no longer be considered to be a partnership asset.

34. The requirements are satisfied through the following scenarios:
Scenario One - Direct Ownership



The partners in the resident partnership owns 100% of the shares in Company X directly in percentages equal to the percentage ownership in the partnership.

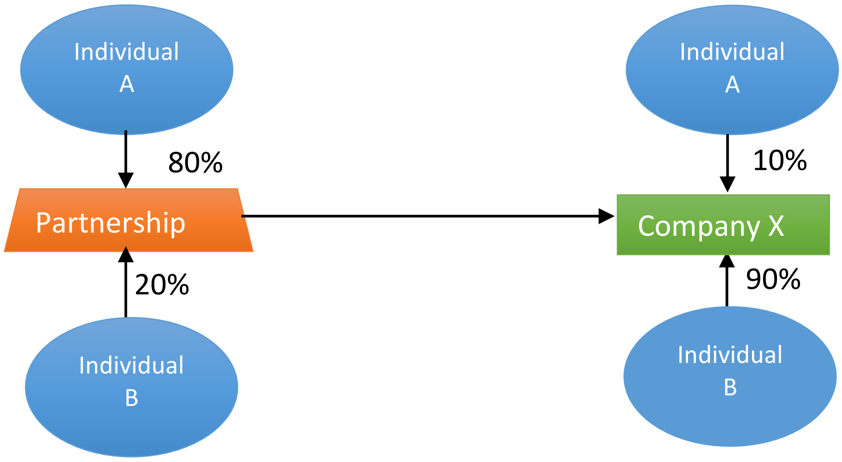
Scenario Two - Indirect Ownership



In this scenario, Individual A owns 40% of the shares in Company A directly which is the same is their percentage ownership in the partnership, while Individual B owns the remaining 60% of shares in Company X, which is the same is their percentage ownership in the partnership. The 60% ownership in Company X is owned indirectly through an interposed person (Company B).

35. As highlighted above partnership reorganisation will not qualify for deferral under section 88 if the percentage ownership in the partnership as per the partnership agreement is not the same as the percentage ownership in the issued shares of the company.

For example,



In this example, the underlying ownership in an asset held by the partnership would be 80% by Individual A and 20% by Individual B. A disposal of an asset from the partnership to Company X would change the underlying beneficial in the asset whereas Individual B's underlying ownership will increase from 20% to 90% while for Individual A the underlying ownership will reduce from 80% to 10% in the asset.

As such, deferral will not apply in such an arrangement.

Change of Ownership in the Transferee Company

36. As highlighted earlier, the deferral rules under section 88 recognise that there is no change in economic ownership where an asset is disposed by a resident individual or resident partnership to a transferee company if the company is wholly owned by the individual.

37. In this regard, if there is a change in ownership or shareholding in the company, the change translates to a change in economic ownership of the asset which was the subject of the disposal.

38. Therefore, if there is a change in shareholding of the transferee company within two years from the date of disposal, any taxes applicable at the time of disposal shall immediately become payable[7].

For example; Shubhas and Esther have joint ownership of a manufacturing equipment on a 40%:60% basis, which they intend to transfer to their company. Their shareholding in the company is on a 40%:60% basis as well. The transfer of the equipment qualifies for the deferral under section 88 and the same is transferred on 1st September 2020. If the disposal would not have qualified for the deferral, the joint owners would have paid capital gains tax of $15,000.

Six months following the disposal, on 1st March 2021, the company issues new shares and welcomes Jone as a shareholder where Jone now owns 10% of the company and Shubhas and Esther own the remaining shares on a 36%:54% basis.

[7] Section 88(2C) of the ITA 2015

With the change in shareholding, the economic ownership of the equipment changes as well. Therefore, the capital gains tax of $15,000 which was payable by Shubhas and Esther on 1st September 2020 immediately becomes payable by Shubhas and Esther on 1st March 2021.

39. A change is ownership may be realized in the following scenarios:
   a) Entry of new shareholders;
   b) Exit of an existing shareholder; or
   c) Change in ownership of shares between existing shareholders.

40. If the change in ownership occurs after the two-year period from the date of disposal, then there is no reversal of the deferral implications applicable initially.

CORPORATE REORGANISATION

41. Section 88 of the Income Tax Act 2015 provides that the deferral rules for company reorganisation are met when the following conditions are met:
   a) a resident company transfers an asset to another resident company; and
   b) the transferor company is a group company in relation to the transferee company.

Resident Company

42. In order to qualify under corporate reorganisation, the transaction must be between a resident company to another resident company. A resident company refers to a company that is incorporated, formed or settled in Fiji or has any part of its central management and control located in Fiji[8]. A branch of a foreign company does not qualify as a resident company.

43. The deferral rules do not apply for asset disposals between a resident company and a non-resident company. This ensures that the deferral rules are not used to transfer an asset tax-free outside the Fiji tax base.

Group Company

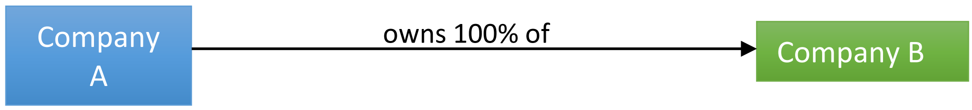
44. In order to qualify for the deferral under section 88, it is a requirement that the supplier and the recipient are group companies as per the definition under section 88(3) of the ITA 2015.

45. Under section 88(3), two companies are group companies if:
   a) one company owns, directly or through one or more interposed persons, 100% of the issued shares in the other company;
   b) another company owns, directly or through one or more interposed persons, 100% of the issued shares in both companies; or
   c) all shareholders of the transferor company and the transferee company are common shareholders who have the same percentage of ownership in the issued shares of the transferor company and the transferee company, either directly or indirectly through an interposed person.

[8] Section 2 of ITA 2015

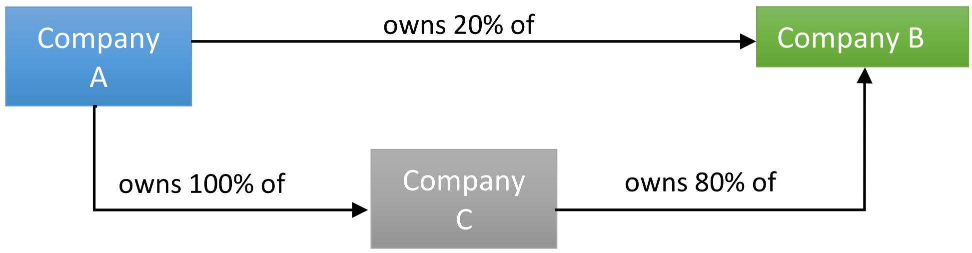
46. Section 88(3)(a) provides that two companies (company A and company B) are group companies where one company owns the other company directly or through an interposed person. This is achieved under the following scenarios:

Scenario One – Direct Ownership



Company A owns 100% of the shares in company B

Scenario Two - Indirect Ownership



Company owns 20% of the shares in Company B directly and the remaining 80% is owned indirectly through an interposed person.

47. The requirement under sections 88(3)(a) for group companies as exemplified above is that one company must have 100% ownership in the other company. Shareholding structures where there are minority shareholders with minimal shares would not qualify unless the shares are held in trust or for the benefit for the majority shareholder. This should be clearly documented and substantiated with evidence.

For example

Company A has the following shareholding structure:

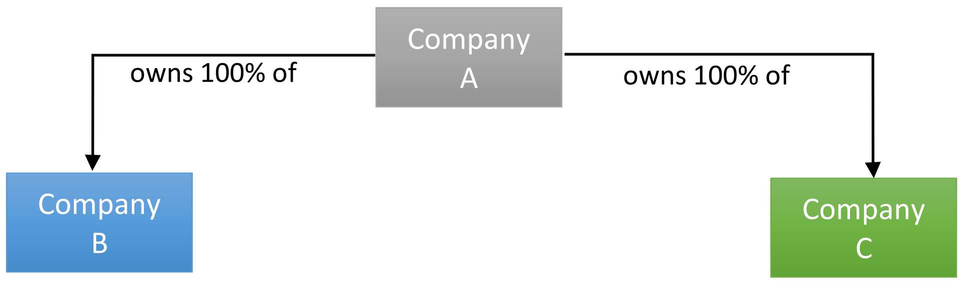
Shareholders	**Shares**	**Address**
Company B	999 shares	Lot 1 Rivera Drive, Suva P O Box 823, Suva
John Doe	1 share	32 Frankton Street, Suva P O Box 123 Nabua

Under the above shareholding structure, Company B does not own 100% of the shares in company A, therefore the two companies are not group companies; even if company B owns 99.9% shares in company A.

However, if John Doe holds the shares in Company A under trust and for the benefit of Company B, Company B would be regarded as having 100% ownership in company A indirectly, satisfying the group company requirements.

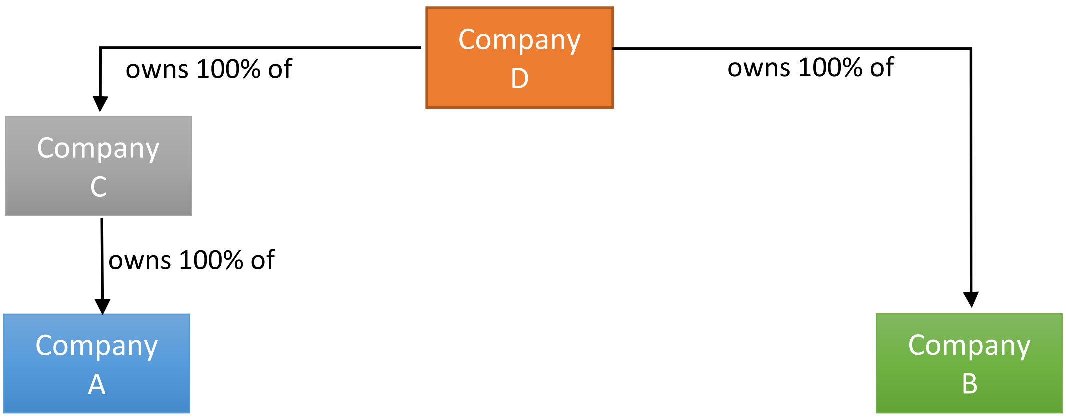
48. Section 88(3)(b) provides that companies are group companies where another company owns both companies, either directly or through an interposed person. This is achieved under the following scenarios:

Scenario One – Direct Ownership



Under scenario one, company A, B and C are considered as group companies as company A wholly owns company B and company C.

Scenario Two – Indirect Ownership



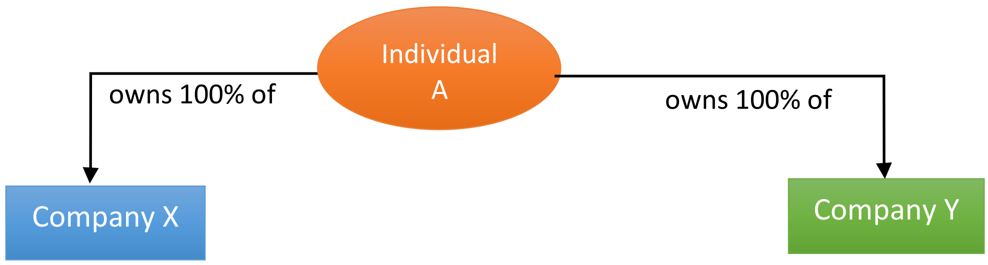
Under scenario two, companies A, B, C and D would be regarded as group companies. Therefore, if A disposes an asset to company B, the disposal would be between group companies. (any combination)

49. Section 88(3)(c) provides that companies are group companies if all shareholders of the transferor company and the transferee company are common shareholders, who have the same percentage of ownership in the issued shares of the transferor company and the transferee company, either directly or indirectly through an interposed person.

50. Common shareholders would include individuals, partnerships, trusts, government and a political subdivision of a government, or international organisations.

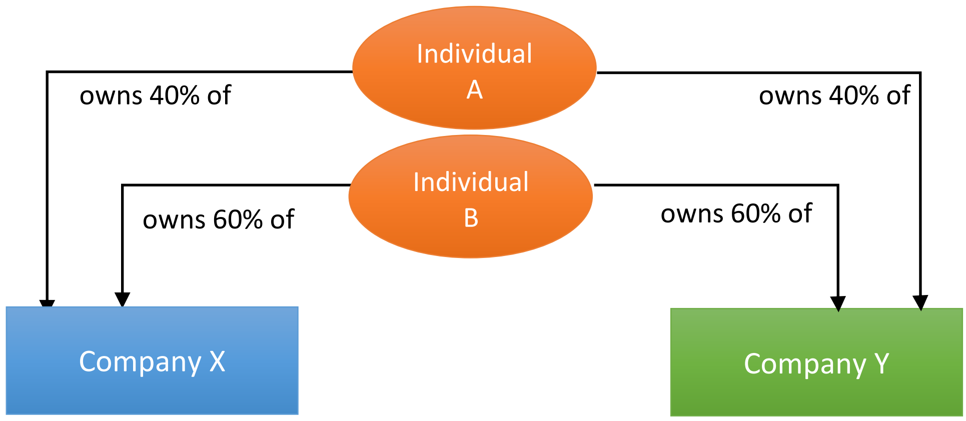
51. Group company is achieved as per section 88(3)(c) under the following scenarios:

Scenario One – Direct Ownership (Single Shareholder)



Under scenario one, company X and Y are considered as group companies as Company X and Y have a common shareholder that has the same percentage of ownership in the issued shares of the transferor company and the transferee company directly.

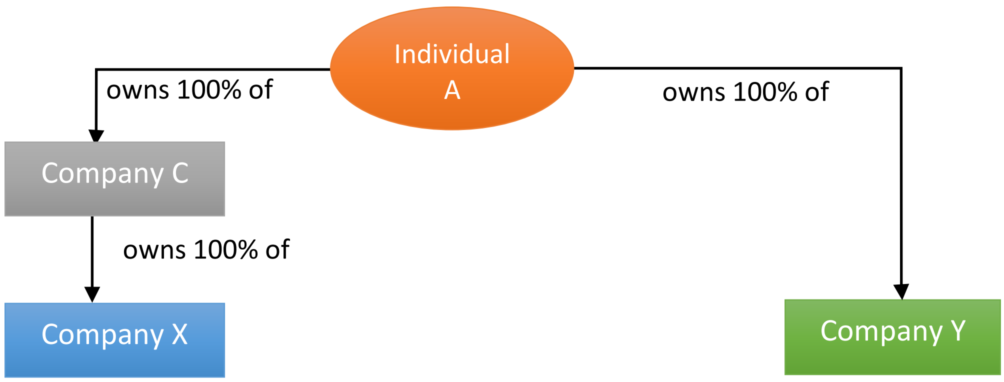
Scenario Two – Direct Ownership (Multiple Shareholders)



Under scenario two, company X and Y are considered as group companies as Company X and Y have common shareholders that has the same percentage of ownership in the issued shares of the transferor company and the transferee company directly.

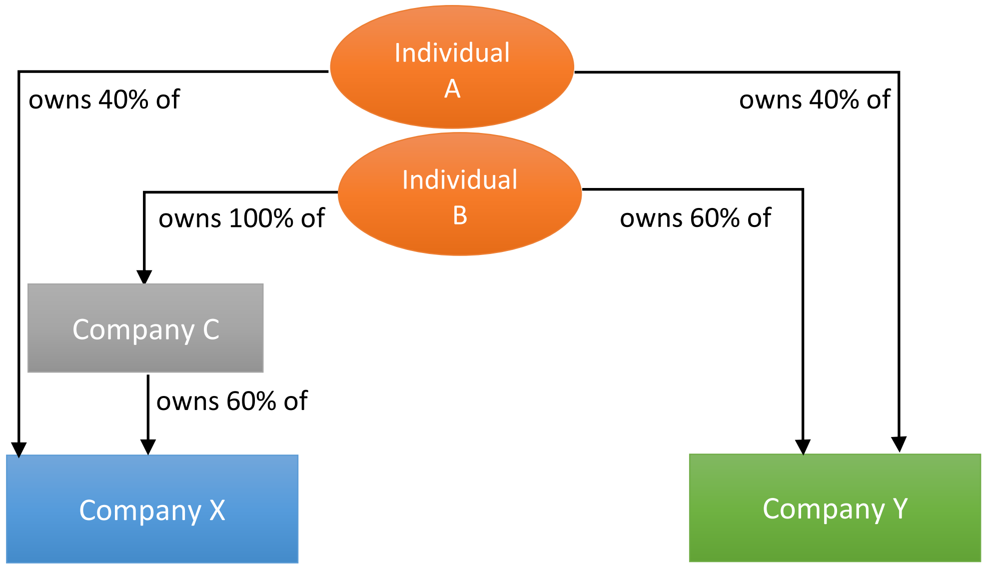
If the percentage ownership in both companies were different, then a disposal from company X to company Y would change the underlying beneficial ownership in the asset. Consequently, deferral would not apply in this case.

Scenario Three – Indirect Ownership (Single Shareholder)



Under scenario three, company X and Y (including C) are considered as group companies as Companies X and Y have a common shareholder that has the same percentage of ownership in the issued shares of the transferor company and the transferee company indirectly, that is through an interposed person.

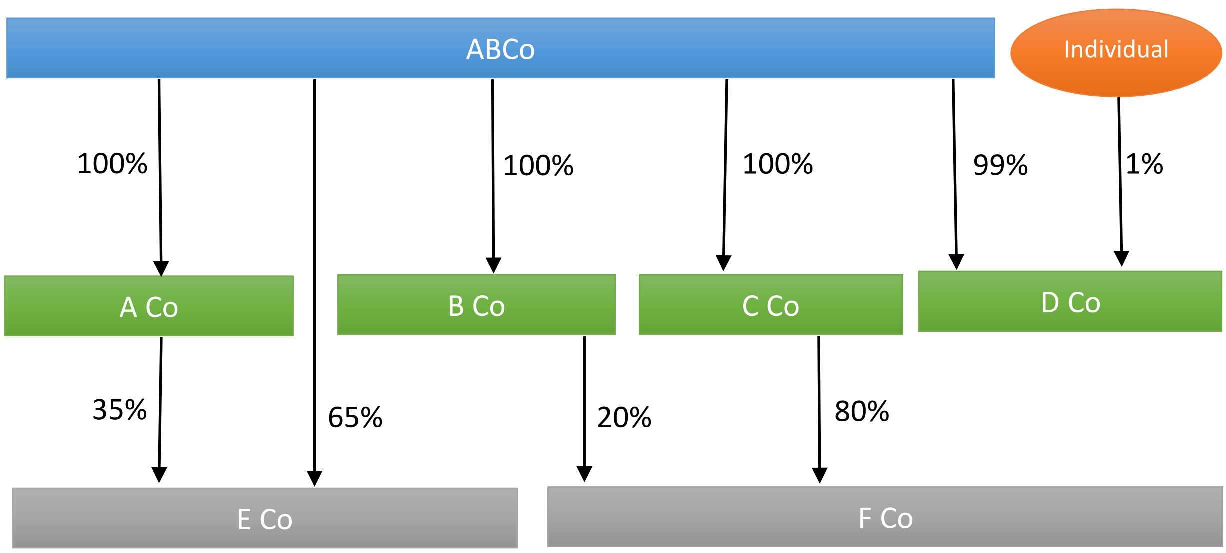
Scenario Four – Indirect Ownership (Multiple Shareholder)



Under scenario four, company X and Y are considered as group companies as Company X and Y have common shareholders that has the same percentage of ownership in the issued shares of the transferor company and the transferee company indirectly, that is through an interposed person.

52. Ultimately, if a resident company disposes an asset to another resident group company the gain arising out of the disposal is deferred under section 88 of the Income Tax Act 2015.

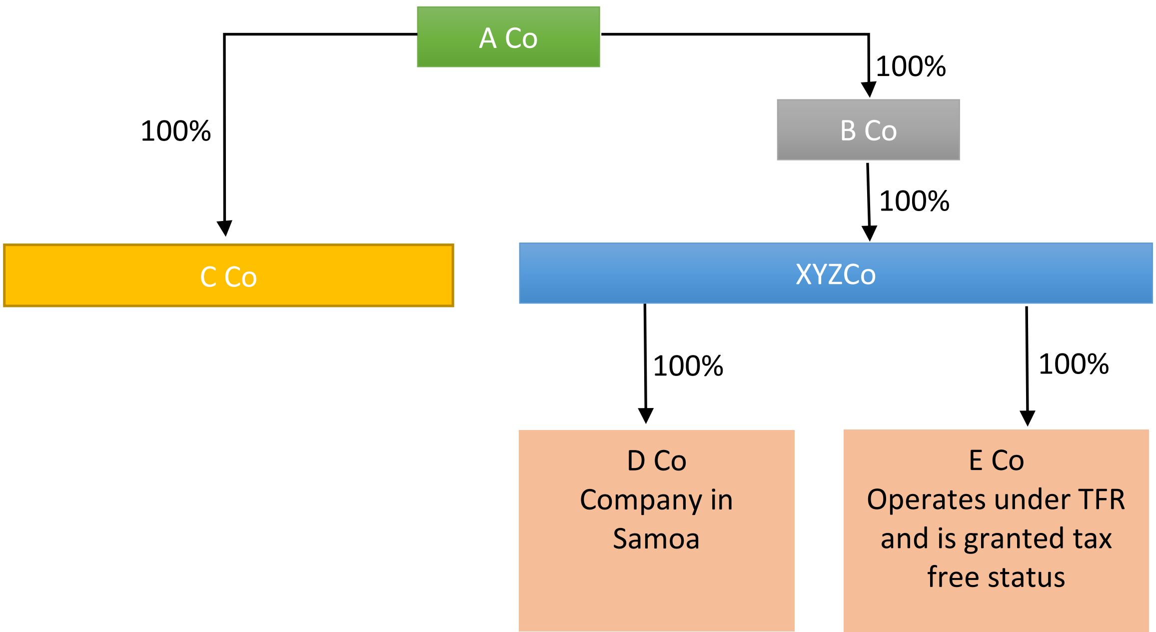
53. For example, ABCo is a resident holding company with the following shareholding structure:



The following is a representation of the application of section 88 of the ITA if ABCo decides to transfer an asset from ABCo to:

Company	Application of section 88 of ITA 2015
A Co	Since A Co is wholly owned by ABCo, a disposal of an asset from ABCo to A Co (or vice versa) would qualify under the deferral rules of section 88 of ITA 2015
B Co	Since B Co is wholly owned by ABCo, a disposal of an asset from ABCo to B Co (or vice versa) would qualify under the deferral rules of section 88 of ITA 2015
C Co	Since C Co is wholly owned by ABCo, a disposal of an asset from ABCo to C Co (or vice versa) would qualify under the deferral rules of section 88 of ITA 2015
D Co	ABCo does not own 100% of the shares in D Co which means that the definition of a group company is not satisfied. The disposal of an asset from ABCo to D Co would be subject to the normal rules of taxation.
E Co	E Co is wholly owned by ABCo through a transposed person (A Co). As such, a disposal of an asset from ABCo to E Co (or vice versa) would qualify under the deferral rules of section 88 of ITA 2015
F Co	F Co has another company (ABCo) which owns through interposed persons (B Co and C Co) 100% of the shares in E Co. As such, a disposal of an asset from ABCo to F Co (or vice versa) would qualify under the deferral rules of section 88 of ITA 2015

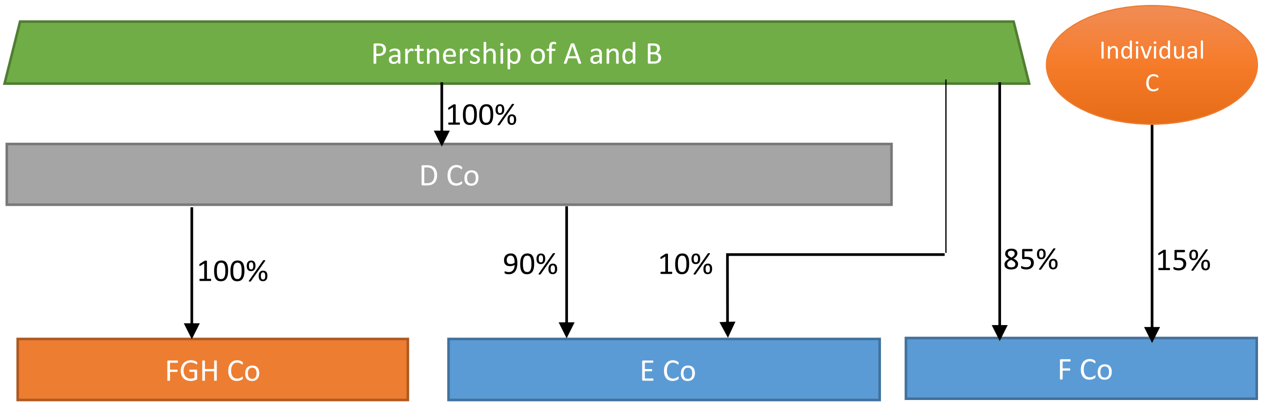
54. XYZCo is a resident company which has the following shareholding structure:



The following is a representation of the application of section 88 of the ITA if XYZCo decides to transfer an asset from XYZCo to:

Company	Application of section 88 of ITA 2015
A Co	A Co owns 100% of shares in XYZCo through an interposed person (B Co). As such, a disposal of an asset from XYZCo to A (or vice versa) would qualify under the deferral rules of section 88 of ITA 2015
B Co	B Co owns 100% of shares in XYZCo directly. As such, a disposal of an asset from XYZCo to B Co (or vice versa) would qualify under the deferral rules of section 88 of ITA 2015
C Co	C Co and XYZCo are wholly owned by another company (A Co) directly and through an interposed person (B Co). As such, a disposal of an asset from XYZCo to C Co (or vice versa) would qualify under the deferral rules of section 88 of ITA 2015
D Co	D Co is a nonresident company. The deferral rules only apply to resident company, therefore the disposal of an asset from XYZCo to D Co would be subject to the normal rules of taxation.
E Co	The income of E Co is exempt from income tax. The deferral rules do not apply in instances where the income of the recipient of the asset is exempt income, therefore the disposal of an asset from XYZCo to E Co would be subject to the normal rules of taxation.

55. FGHCo is a resident company with the following structural arrangement:



The following is a representation of the application of section 88 of the ITA if FGHCo decides to transfer an asset from FGHCo to:

Company	Application of section 88 of ITA 2015
D Co	D Co owns 100% of shares in FGHCo directly. As such, a disposal of an asset from FGHCo to DCo (or vice versa) would qualify under the deferral rules of section 88 of ITA 2015
E Co	E Co and FHGCo have common shareholders, that is D Co and ultimately Partnership A and B. The Partnership owns 100% of the issued shares in FGH Co and E Co through an interposed person (D Co). As such, a disposal of an asset from FGHCo to E Co (or vice versa) would qualify under the deferral rules of section 88 of ITA 2015

F Co	F Co and FHGCo do not have common shareholders. The Partnership owns 100% of FGHCo but does not own 100% of F Co. Consequently, the disposal from FGHCo to F Co will not qualify for deferral under section 88 of ITA 2015.
Partnership A and B	Reorganisation applies when the partnership would transfer assets to a company wholly owned by the partnership and not from the company to the partnership.
Individual C	Individual C has no connection with FGHCo therefore the disposal will not qualify for deferral under section 88 of ITA 2015.

EXCEPTION – Exempt Transferee Companies

56. The deferral rule under section 88 of the ITA 2015 does not apply if the income of the transferee company or the recipient company is exempt income[9].

57. For instance, if the transferee company has been granted tax free status as they are operating within the tax free region, or the transferee company is an approved NPO, the disposal of the asset to the transferee company would not qualify for the deferral rule under section 88 of the ITA 2015.

58. The rationale for the exception is to ensure that the deferral rules are not misused by disposing the asset to a company which would subsequently dispose the asset with no tax implications.

59. For further information and clarification in regard to this SIG, please email us at tipu@frcs.org.fj

[9] Section 88(2) of ITA 2015

APPENDIX: LEGISLATION

INCOME TAX ACT 2015

[Section 2] Interpretation

company means—

a) a body or association of persons corporate or unincorporated, including a statutory corporation and a company created by charter, but not including a partnership;
b) a foreign association of persons, other than a partnership, that the CEO has declared to be a company for the purposes of this Act; or
c) a trust approved as a managed investment scheme under the Companies Act 2015 and includes a unit trust to which section 743 of the Companies Act 2015 applies;

resident company means a company—
a) that is incorporated, formed or settled in Fiji; or
b) that has any part of its central management and control located in Fiji;

resident individual has the meaning in section 6;

resident partnership means a partnership—
a) that is formed in Fiji; or
b) that has any part of its central management and control located in Fiji;

[Section 88] Corporate Re-Organisations

1) If—

a) a resident individual or resident partnership (referred to as the "transferor") disposes of an asset, with or without liability not in excess of the cost of the asset or, in the case of a depreciable asset, written down value, to a resident company (referred to as the "transferee") and the transferee is wholly owned by the transferor; or
b) a resident company (referred to as the "transferor company"), disposes of an asset, with or without any liability not in excess of the cost of the asset or written down value in the case of a depreciable asset, to another resident company (referred to as the "transferee company") and the transferor company is a group company in relation to the transferee company,

then—

i. no gain or loss is taken to arise on disposal of the asset;
ii. the transferee or transferee company is treated as acquiring an asset of the same character as the asset disposed of by the transferor or transferor company; and

iii. the transferee or transferee company's cost on acquisition of the asset is equal to the transferor or transferor company's cost of the asset or, in the case of a depreciable asset, written down value at the time of disposal.

(2) Subsection (1) does not apply if the income of the transferee and transferee company is exempt income.

(2A) A transferee is wholly owned by the transferor if the transferor owns directly or through one or more interposed persons, 100% of the issued shares in the transferee.

(2B) For the purposes of subsections (1)(a) and (2A), where an asset under disposal is jointly owned by 2 or more tranferors, the percentage of ownership in the asset or the depreciable asset should be the same as their percentage of beneficial ownership of the issued shares in the transferee.

(2C) Notwithstanding section 87, the deferral granted under subsection (1)(a) will cease to apply and any taxes applicable at the time of disposal shall immediately become payable if there is a change in beneficial ownership of the transferee within 2 years from the date of disposal.

(2D) For the purposes of subsection (1)(a), where the transferor is a resident partnership, the percentage of ownership in the partnership should be the same as their percentage of beneficial ownership of the issued shares in the transferee.

(3) A company is a group company in relation to another company if—

a) one company owns, directly or through one or more interposed persons, 100% of the issued shares in the other company;
b) another company owns, directly or through one or more interposed persons, 100% of the issued shares in both companies; or
c) all shareholders of the transferor company and the transferee company are common shareholders who have the same percentage of ownership in the issued shares of the transferor company and the transferee company, either directly or indirectly through an interposed person.

(4) In this section, "company" and "interposed person" means an incorporated body.