



# **FIJI INSTITUTE OF ACCOUNTANTS**

**Submission to the Ministry of Economy**

**For the 2017/2018 National Budget**

**May 2017**

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### **1. INTRODUCTION**

The Fiji Institute of Accountants (“FIA”) (please refer to Appendix A for details on the functions of the FIA) thanks the Ministry of Economy for the invitation and welcomes the opportunity to make a submission on the 2017/2018 National Budget. It notes government’s continuous recognition of FIA’s contribution in the past in considering some of its recommendations and hopes that government will continue with this trend. The FIA has also continued to work with the Fiji Revenue and Customs Authority (“FRCA”) with a view to improving tax compliance and tax collection within the ambit of the tax legislation.

In making this submission, the FIA has invited comments from all its members and all appropriate feedback received from the members is included in this submission.

The focus of our submission is:

- Promoting investments and economic activities at large and in particular in the Micro, Small and Micro Enterprise (“MSME”) sector so that economic growth is more balanced and broad based.
- Improving tax administration and compliance policies, procedures and practices to enhance tax collection in an accurate, fair and consistent manner.
- Review of the taxation system and policy framework with an emphasis on developing a broad based, business focused, sustainable and consistent revenue collection system.
- Developing the agricultural potential of the country including investment therein, and viable food security and energy alternatives.
- Reforming Fiji’s public sector to reduce its size and increase efficiency and productivity.
- Investing in the quality of tomorrow’s workforce aimed at increasing the productivity and building the HR capacity.

Continued challenges reflect the need for the effective planning, implementation of action plans to achieve the desired results in the short to medium term, and measurement of performance outcomes.

## **2. EXECUTIVE SUMMARY**

Our submissions on the 2017/2018 National Budget are provided in detail in Part 3. This executive summary focuses on some of the key areas, the more important of which if properly addressed by Government should result in economic growth by –

- Providing certainty for businesses;
- Providing a more transparent and easy to follow tax system which will lead to increased investor confidence;
- Ensuring consistent tax treatments between different taxpayers which would result in increased investment by individuals especially in the MSME sector;
- Reducing overall record keeping requirements and compliance costs for businesses resulting in the ease of doing business; and
- Reducing overall cost of doing business.

### **2.1. IMPROVING BUSINESS ENVIRONMENT AND INVESTOR CONFIDENCE**

The key to moving forward and achieving Government objectives lies within continually improving the business environment and creating greater investor confidence, and thereby promoting further investments and economic activities.

One of the key factors to achieving Government objectives is to promote investments through the ease of doing business. Improvements in the ease of establishing and doing business in Fiji through the streamlining of regulatory processes and reduction in compliance costs including from the simplification of, or elimination of duplicate, requirements and procedures are critical to improving Fiji's ease of doing business.

### **2.2. STREAMLINING TAXES AND PROVIDING CERTAINTY**

A common concern being raised by taxpayers and investors is the current uncertain tax environment created by FRCA with the sole objective of revenue collection. FRCA should, without compromising its position, be working with taxpayers and investors in collecting the fair amount of tax revenue and not against them.

Some recent tax amendments have retroactive effect and increase compliance costs. Furthermore, tax laws are applied inconsistently and policies, practices and interpretations are being changed ad hoc. This cannot but have a negative impact on the mind-set of investors. Investors need clear policies, practices and interpretations that are applied prospectively to make informed decisions which form the basis for their investments.

An over-arching simple tax policy framework is critical to the formulation, interpretation and application of tax laws and tax compliance. The tax policy framework should be articulated and disseminated to the public so that the public, businesses and individuals alike, are aware of and able to contribute to Government's tax policies and can visualize the roles they play in those policies.

### **2.3. INCENTIVES**

There is a need for the review and streamlining of incentives and support to targeted industries which have potential for creating further employment, exports, economic activities together with meeting social obligations spread across the wider population.

### **2.4. DEVELOPING MICRO, SMALL AND MEDIUM ENTERPRISE SECTOR**

The development of the micro and SME sector is critical for the social and economic development of the country spread across remote and rural areas. This sector needs to be given due attention, nurturing and support.

### **3. OUR SUBMISSION**

#### **3.1. PROMOTING INVESTMENT AND DOING BUSINESS IN FIJI**

A key component to Fiji's prosperity and stability is investment and economic activity which are achieved through improved investor confidence and business environment.

Some of the matters have been covered in past years' submissions by the FIA. These are reiterated in this year's submission as important aspects to promoting investment and business in Fiji.

- Compliance Cost and Regulatory Burden – All levels of government, including Statutory Bodies, need to remain focused on reducing unnecessary legislative burden on business by looking at ways to reduce red tape and compliance costs, leading to an improvement in the ease of doing business. A good example is the documentation requirements that are duplicated for each of the regulatory bodies. There is a need for a “one stop shop” concept and FIA considers that any proposed legislative/administrative changes should be subject to stringent tests on its necessity, design and impact on investors and businesses alike.

For example, the need to obtain approval from both Investment Fiji and the Reserve Bank of Fiji for changes in shareholding is unnecessary, increases compliance costs and is time consuming. Approval should only be required from one regulatory authority and the different regulatory authorities should be talking to each other.

- Commerce Commission – review and improve policies, practices and procedures within the Commerce Commission with the objective of reducing compliance cost. Align the functions and activities of Commerce Commission to Government policy of promoting investments and economic developments, and particularly for the development of the MSME sector.
- New Income Tax Act – The Income Tax Act (“ITA”) 2015 has been in effect since 1 January 2016.

The FIA has previously recommended that:

- a) The application of the legislation be prospective, instead of retrospective.
- b) All provisions of the Act be thoroughly reviewed and further submissions are invited from the respective professional bodies and other stakeholders.

These recommendations are still relevant notwithstanding the introduction of the ITA 2015. There are still a number of provisions that require review and amendment and FRCA continues to change its mind on interpretation as well as application of the law retrospectively.

### **3.2. INTERNATIONALLY COMPETITIVE TAX REGIME AND FIJI REVENUE AND CUSTOMS AUTHORITY (“FRCA”)**

#### **3.2.1. Prospective Imposition of Tax Laws**

Tax laws and its practical implementation should be applied prospectively.

Examples (also noted in FIA’s last budget submission) include the Income Tax (Withholding Tax) Regulations 2013 which was gazetted on 22 November 2013 but is applicable from 1 January 2013 and amendments to ITA, Income Tax (Amendment) (No 4) Decree 2013 (Decree No 37 of 2013) promulgated in November 2013 wherein various sections of this Decree have been made effective from 1 January 2012 and others from 1 January 2013.

More recent examples include the following:

- ITA 2015 gazetted on 23 November 2015 which, by subsequent amendment gazetted on 24 December 2015, includes provisions imposing a transitional tax of 1 percent on the net profit after tax of a company where the profits were not distributed as a dividend prior to 1 January 2015 as well as FRCA’s interpretation that the provision extends to undistributed profits of the 2015 tax year.
- Introduction of the concept of “depreciable assets” and thereby imposing income tax on assets which previously fell within the definition of capital assets.

The retrospective introduction of law creates uncertainty for all stakeholders and affects business confidence and investment.

#### **3.2.2. Consistency of Policy, Practices and Interpretation**

All economic activity interacts with and is impacted by the country’s revenue policies and practices.

The FIA makes the following comments and suggestions:

- There should be an overall documented tax policy framework and tax legislation should be consistent with the tax policy framework. We note some commendable changes to the legislation in the recent past, however quite often these positive changes are contradicted by other amendments to the legislation (e.g. reducing the corporate tax rate to 20% but introducing withholding tax on dividends, reducing the loss carry forward period to 4 years while introducing a number of other indirect taxes which add to the cost of doing business). A properly documented tax policy framework would assist in ensuring that any change to legislation is consistent with the overall framework. Ensuring collective focus in achieving National goals is paramount.



FIA believes that it is critical to have a tax policy framework as this will create certainty and provide the level of confidence in the tax regime needed by investors. The framework should focus on how tax fits with the government economic, fiscal and revenue strategy.

- FRCA must articulate and apply its policies and interpretations consistently.

FIA has noted that FRCA has been changing its policies, practices and interpretation on a number of issues, the most recent being deemed dividends on sale of shares, dividends generally and sale of residential properties by registered persons.

The mechanism for challenging decisions of FRCA are simply through the Tax Tribunal which can be an expensive and a lengthy endeavour and cost inefficient, particularly where the matter is one of principle and the quantum of tax is not significant. Such practices create more uncertainty for businesses, discourage further investment and erode the confidence of doing business in Fiji.

It is noted that FRCA has reviewed its processes dealing with disputes and objections and has established an independent Objection Review Team within FRCA which is headed by a senior officer of FRCA. This provides an opportunity to taxpayers to present their case to a totally independent team without any fees and costs. FIA would like FRCA to further ensure a high level of independence in this regard.

- Changes in interpretation, policies and practices by FRCA should not be introduced with backdated effect; nor be applied at the discretion of line officers, but rather by specific policy of the Authority which should be prospective in application. FRCA has provided some assurance on this matter.
- The provisions for binding public and private rulings in the Tax Administration Decree 2010 should be made effective. In accordance with its powers under these provisions, FRCA should issue binding public and private rulings to ensure consistency in FRCA practices and certainty for taxpayers and investors. FRCA has advised that work in underway in this area.

### **3.2.3. Role of FRCA in Promoting Investments and Economic Activities**

FRCA should understand and not underestimate its role in promoting investment and economic activities. The FIA appreciates that FRCA is in the midst of various institutional review processes (including IT, transfer pricing, gold card taxpayers, etc.).

Some other avenues available to FRCA to assist in this role include:

- Identification and implementation of specific measures to improve dialogue and understanding between business community / investors and FRCA. Establish forums to consult business and community /investments. In this respect, we note that the FRCA has been consulting with the FIA on various matters.
- Continuing to undertake independent review of the tax administrative policies, procedures and activities to assess its impact on business activities and economic activities, and its impact on the economic development of the country. Such reviews are carried out regularly in a number of countries with the objective of identifying difficulties and problems faced by businesses and taxpayers, with suggestions for improvements and systems and processes aimed at promoting business activities and economic growth.
- Improving customer service levels and internal efficiencies to allow business processes to be completed effectively and efficiently by relevant officers, and minimizing the duplication of effort and time to attend to tax payer matters.
- Exercise of Commissioner's discretion in all tax laws to consider changing technologies in the various industries.

### **3.2.4. FRCA – As Business and Commercial Enterprise**

There is a need for FRCA to view its operations from a commercial or cost/benefit approach. Inefficiencies in business and IT processes as well as time spent by staff in resolving matters are all costs to business.

An example of this is the legislative requirement that various taxes be paid on the last business day before month end. To assist taxpayers comply with this requirement FRCA, instead of changing the legislation to revert to payment being due by the next business day after month end, pays staff overtime to work on a Saturday (say) so that taxpayers can meet their payment obligations. The gesture is appreciated, however from a cost/benefit perspective it would likely be more cost effective to allow payment on the next business day rather than incurring additional costs for minimal added benefit as there are generally few months in a calendar year where the month ends on a weekend (or public holiday).

Other measures that can be reviewed include:

- Working with other regulatory bodies such as Investment Fiji and the other Ministries of government on approved projects by proactively reaching out to these taxpayers and working out solutions to ensure that projects are not stalled.

- Further profiling of taxpayers with the objective of providing greater flexibility to taxpayers (including MSMEs and individuals) maintaining high standard of compliance. Furthermore government needs to look at the ease of doing business, particularly for MSME's. There are many procedures and requirements just to start a business along with the related costs every step of the way. This issue needs to be properly reviewed and addressed so that MSME's can be quickly set up and flourish without too much cost and unnecessary red tape.

FIA acknowledges and commends FRCA on the introduction of a taxpayer profiling process for the purposes of compliance. However FIA suggests that this process be developed further and shared with taxpayers to promote transparency and positive working relationships. This process will be of further benefit if it was also used to reward compliant tax payers with improved *ease of doing business* and tax compliance processes (similar to Gold Card).

- Create a special window of providing service to Tax Agents similar to “Gold Card” system currently in place for high value business taxpayers.
- Review the “Gold Card” system to:
  - extend it beyond high value business taxpayers so that compliant SMEs can avail themselves to the benefits of being *good tax citizens*
  - minimise the processes and procedures that Gold Card taxpayers still encounter, so that the privilege of being a Gold Card member brings with it special efficient services but also has certain responsibilities that require the taxpayer to adhere to.
  - remove the additional duty concessions and personalized services afforded to individuals because of the Gold Card status of the business entity. This will eliminate issues of potential fringe benefits and discretion.

### **3.2.5. VAT and Income Tax Refunds and Interest on Delay in Refunds**

As an encouragement to FRCA to continue to improve with its refund practice, interest should be paid for the delay in issue of refunds as allowed under the respective legislation.

### **3.2.6. Tax Agents Portal and Tax Agents Lodgement Program (“TALP”)**

We note that work is currently being slowly undertaken on the Tax Agents Portal project. The success of this project is imperative to the enhancement of tax agents acting as “satellite offices” of FRCA.

The FRCA should continue with its TALP and give extensions for filing of tax returns by tax agents. Similar programs currently exist in both Australia and New Zealand, with the respective tax departments recognising that tax agents need to spread their work load. This will encourage more filing of tax returns by tax agents and ensure quality of tax returns.

### **3.2.7. Taxpayers' Charter and Tax Dispute Resolution Service**

Long overdue is the establishment and promotion of the Taxpayers' Charter and the Associated Tax Dispute Resolution Service. These will allow tax payers an avenue to seek redress on their issues, but also more importantly set a bench mark for FRCA's service standards and practices.

It is noted that a draft Tax Agents' Code of Conduct was circulated by FRCA for review and comment by FIA during 2016. We suggest that the FRCA staff code of conduct also be circulated to tax agents for their information and also to assist in ensuring that the code is followed.

### **3.2.8. Tax Ombudsman**

The taxpayer perception of a tax system is critical to ensuring voluntary compliance. Further to the setting up of FRCA's Objection Review Team, the appointment of an independent tax ombudsman could further provide assurances that there is an independent review available to taxpayers before the courts

In most countries the tax ombudsman is seen as a critical role in providing an independent avenue for taxpayers to lodge complaints and seek an impartial review of tax office decisions.

Accordingly, FIA considers that there is a need to create an independent body outside the jurisdiction of FRCA where taxpayers, particularly small and medium enterprises, could appeal to if they feel that they had been treated unfairly by FRCA, especially when many could not afford to go the legal route.

The basic function of the office of tax ombudsman will be to diagnose, investigate, redress and rectify any unfair action and treatment, bias or prejudice or faculty procedures or unfair administration of the tax laws by FRCA. This is not to detract from the current objection and appeal procedures against an assessment that the taxpayer believes is incorrect.

### **3.3. TAX LAWS AND ADMINISTRATION**

With the introduction of the new Income Tax Act, the FIA's comments on the area of tax laws and administration is limited to existing anomalies that we believe should be reviewed and amended/repealed or introduced. Separate submissions have been made (and will continue to be made) in respect of the new tax Act. However FIA would like to stress to Government that there needs to be an overall framework policy set in place to provide a practical application of policies with respect to the intentions of the new ITA.

The most critical issues include PAYE final tax and quarantining of tax losses, dividend withholding tax and deemed dividend provisions, 1% transitional tax and taxation of dividends distributed from pre-2014 profits, taxation of depreciable assets, Capital Gains Tax ("CGT") introduced in 2011 without any indexation or grand-fathering rules, non-resident withholding tax ("NRWT") on payments for professional services, NRWT on reimbursements, contractor's provisional tax (CPT) and social responsibility tax ("SRT") which if properly addressed would achieve Government's overall objectives and economic growth.

#### **3.3.1. PAYE Final Tax and Business Losses for MSMEs**

The current policy framework of treating PAYE tax as a final tax and the quarantining of business losses has an adverse effect on investments, particularly for MSMEs and results in distortions in taxes payable by individuals and potentially discourages investment by wage earners.

The current treatment discourages investment by employees who would not be able to offset their business losses against their employment income but would have to pay taxes on business profit.

We suggest a review of the existing treatment of PAYE as final taxes. To assist MSMEs which includes employees, government should seriously look at allowing employee income to offset business losses. This would then be an incentive for employees to increase economic activity in the MSME sector.

#### **3.3.2. Dividend Withholding Tax and Deemed Dividend Provisions**

The combined effect of these provisions is an effective tax rate of 22.4% to 27.2%. Government consider increasing the current corporate tax rate to 22.4% and 27.2% (for companies with local and foreign shareholders respectively) and removing the dividend withholding tax and deemed dividend provisions.

### **3.3.3. 1% Transitional Tax and Taxation of Dividends Distributed From Pre-2014 Profits**

The overall application of the 1% transitional tax and non-resident withholding tax (“NRWT”) on dividends should be reviewed to ensure that the provisions are not discriminatory and retrospective in nature and sending out wrong signals to investors.

### **3.3.4. Taxation of Depreciable Assets CGT Introduced in 2011 Without any Indexation or Grand-Fathering Rules**

The removal of depreciable assets from the definition of capital assets effectively imposes income tax on all gains derived from the sale of depreciable assets (which includes buildings). This is a major shift in policy and is a form of retrospective tax on gains that were not subject to any tax before May 2011. We suggest Government review the overall policy and make appropriate amendments to the ITA to impose only CGT on capital gains unless the assets were held on revenue account.

### **3.3.5. Withholding Tax**

A clearly **articulated and applied** position and reasoning in respect of the levying of withholding on cross border payments is essential for business. These tax rules should be consistent with the overall provisions of the Income Tax Act and strictly adhere to the provisions of the double tax agreements that Fiji has with many countries.

As Fiji continues to grow economically and Fiji businesses utilize foreign professional services, the impact on business costs increases significantly when FRCA incorrectly levies withholding tax on these services and the Fiji business is required to bear the cost of the incorrect imposition of withholding tax. Furthermore, resources including funds that may be used for deriving more income (which means more revenue in the form of taxes for the Government) are diverted to unproductive purposes in objecting to the incorrect imposition of withholding taxes.

Additionally, where the profit margin on professional services is very low (say 7%) it is inequitable to charge withholding tax at a rate of 15%. To address this inequity we suggest that the old rules be reintroduced and allow abatement or rebate of withholding tax paid to non-residents by allowing the non-resident to lodge income tax return and claim credits for withholding tax paid.

The above change would be consistent with international practice and reduce the cost of doing business as the tax is often borne by the Fiji entity on a grossed up basis.

### **3.3.6. Non-resident Withholding Tax (“NRWT”) on Payments for Professional Services**

The FRCA’s current practice is to impose NRWT on all payments for professional services. This is inconsistent with the provisions of most Double Tax Agreements (“DTAs”) resulting in many service providers not being able to claim credits for the NRWT paid in Fiji. Consequently, most service providers require payment on a grossed up basis thus resulting in increased costs of doing business in Fiji. NRWT should be imposed in accordance with the provisions of the relevant DTAs. Relevant DTAs should be renegotiated where Government intends to impose NRWT on all payments for professional services. In this respect we note that negotiations are currently underway with New Zealand.

### **3.3.7. NRWT on Reimbursements**

With the recent amendments to the law, NRWT is being imposed on all cost reimbursements even where there is no profit element. Such practice can be very detrimental to doing business and increases the overall cost of doing business as most service providers would require payment on a grossed up basis. NRWT should not be imposed on cost reimbursements especially where supporting documentation is available to substantiate the cost reimbursement.

Imposing NRWT on reimbursements is also not consistent with international practice.

### **3.3.8. Contractor’s Provisional Tax (“CPT”)**

The current law imposes CPT on payments for services under a written contract. This practice is contrary to the intention behind the deduction of CPT from payments for services (the intention being to collect tax payable by non-compliant service providers at source). It is unlikely that non-compliant taxpayers will enter into written contracts. Consideration should be given to repealing the current provisions relating to CPT and reintroducing the certificates of exemption which will reduce compliance costs for businesses and the FRCA’s workload. This will achieve the overall intention to CPT i.e. to catch within the ambit of tax non-compliant taxpayers.

### **3.3.9. Income Tax Rates and Levies, Including Social Responsibility Tax**

Whilst the income tax rates have generally been reduced, many new taxes and levies and accompanying requirements have been introduced which makes it so much more expensive and difficult to do business.

In view of the above and for tax system integrity and transparency reasons the income tax rates should be reviewed with a view to abolish all the tax levies that are imposed under Sections 7E through to 7H of the old ITA.

Alternatively, as a non-discriminatory policy and for equity reasons the SRT should be imposed at a reduced tax rate of say 5% but imposed on all taxpayers including corporate and individual taxpayers irrespective of residency status who derive taxable income in excess of \$270,000. This would not only be more equitable and non-discriminatory but is likely to result in higher tax collections from SRT.

Alternatively Government should consider increasing the income tax rate but repealing SRT and/or amending other taxes. This should be done as part of the recommended development of a tax framework for the country.

The environment levy, as the name suggests should be a levy to fund projects that protect, restore and improve our environment. However, there is no accountability on the current environmental levy collected. The environmental levy should be set aside for improving our environment and should be imposed on all those entities that have an impact on our environment and not just the tourism sector.

If the environmental levy is to remain, it should be imposed on a broader sector of the economy but at reduced rates. This will result in reducing the overall costs to the tourists but at the same time maintain revenue collection for Government and also make other taxpayers accountable for our environment.

### **3.3.10. Section 23 Employers FNPF Contributions**

The fact that the employer's contributions are required under the law, purely business in nature and keeping in mind that the contributions are for the employee's retirement benefit, the restriction of allowing only 50% of the employer's contributions as tax deductions should be removed allowing the 100% of the minimum statutory contributions made by the employer.

### **3.3.11. Other Charges to be Allowed as a Deductions**

Stamp Duty and Fringe Benefit Tax should be allowed as deductions as these are costs incurred in the conduct of business.

It should be noted that with the disallowance of 50% of FNPF and FBT, taxpayers could end up paying income tax although they have not made a profit. This is bad policy.



**3.3.12. Interest Withholding Taxes (“WHT”) as Final Tax**

The current interest WHT as a final tax policy should be reviewed as there should be equitable checks and balances built into the system (e.g. tax on interest: \$16,000 - nil; \$16,100 - \$1610 - whereas employee on \$16,100 would pay only \$7 in PAYE taxes). This policy on interest is important as it has flow on implications for savings and investment in the economy. This would encourage low salary earners who cannot afford the luxury of large investments to invest further through savings and encourage investment in the MSME sector.

**3.3.13. Penalties**

The current penalty rates of between 20% and 75% are very high and draconian. The high rate of penalty is also a deterrent for voluntary compliance by taxpayers. The penalty regime and practice for the implementation of the same should be reviewed to ensure that while it provides a deterrent for non-compliance, it also allows those who wish to voluntarily comply, do so without being unduly penalised.

**3.3.14. Review of Transfer Pricing Legislation**

Review of Transfer Pricing legislation to bring about clarity on documentation issues such as what should be included in Transfer Pricing Documentation, whether entities meeting a certain threshold be made to compulsory lodge or whether group documentations that include the Fiji entity be sufficient.

Consideration should be given for legislating the Advanced Pricing Agreement (APA) process. APA is an administrative approach that attempts to prevent transfer pricing disputes from arising by determining the transfer price(s) prior to the transactions taking place. The idea of APA is to reach an agreement prior to the transaction, whereas a transfer pricing audit examines the transaction after it takes place.

Any proposed introduction of penalties be carefully reviewed before its imposition and should be consistent with the Tax Administration Decree penalty provisions.

**3.3.15. Research and Development Tax Incentives**

Consider special tax incentives to allow business to innovate and to take the next step to improve their processes and productivity.

Innovation including research and development are fundamentals for improving future competitiveness and productivity of Fiji businesses. It is a key ingredient for the move towards a knowledge based economy.

Research and development will not only allow Fiji businesses to compete but it creates new investment, business opportunity, supports new growth and creates jobs.

### 3.3.16. VAT Decree

The VAT Decree was adopted from the New Zealand Goods and Services Act (GST Act). Since the time of introduction of the VAT Decree the GST Act has been amended to take into account complexity of transactions and new products. The VAT Decree should be reviewed with this in mind to ensure there is more certainty in pursuing new business initiatives using new products and processes.

### 3.3.17. VAT on Residential Accommodation

We understand that the intention of imposing VAT on residential rental is to impose VAT on high rental properties.

However, currently VAT is imposed on residential accommodation by reference to the rental income of the landlord as opposed to the rent paid by the tenant. This could have the potential of VAT being payable on low-end rental properties occupied mainly by low income earners where the landlord has a number of such low-end properties with the total rental income of the landlord exceeding the current \$100,000 threshold.

VAT should be imposed by reference to rent paid by the tenants as opposed to the total rental income of the landlord.

### 3.3.18. Thin Capitalisation Rules

Thin capitalisation rules were introduced with the new Income Tax Act 2015, with effect from 1 January 2016. The rules deny a deduction of interest to the extent that a non-resident company's debt to equity ratio exceeds 2:1 at any time during the tax year. The provision looks at the highest amount of debt during the tax year, and also excludes any "arms-length debt" defined not as the amount of debt on which there is *an arms-length interest rate* but as the amount of debt that a financial institution (unrelated to the taxpayer) is *willing to lend*.

In group structures and due to borrowing arrangements and investment structures, it is common for borrowings to pass through one entity to one or more entities in the group. In these cases, under the current thin capitalisation rules the entity that is actually not using the debt for operational purposes, is the entity that is tested for thin capitalisation purposes. Furthermore, transfer pricing rules require that an arms-length interest rate be charged on such cross border lending, and thin capitalisation rules then work to deny a deduction for the interest where the debt to equity ratio is more than 2:1.

Thin capitalisation rules should, for group entities within Fiji, apply on a net debt and net interest basis so that the test of eliminates borrowings which pass through one entity to another and interest expense which is offset by interest charged to another related party.

### **3.4. REVENUE GENERATING INITIATIVES**

#### **3.4.1. Tax Evasion and the Hidden Economy**

Review and implement initiatives taken by other countries for reducing the level of tax evasion and the hidden economy.

We note that the FRCA has introduced the whistle blower policy and aggressively looking at customs compliance issues.

### **3.5. TARGETED INDUSTRIES AND TAX INCENTIVES AND OTHER SUPPORT**

Industries and sectors which assist with import substitution, boost foreign reserves, have high employment numbers, show potential for growth and provide a competitive advantage should be strongly encouraged by putting in place appropriate policies including specific incentives.

Sectors and initiatives for consideration include:

#### **3.5.1. Agriculture Sector – Tax Incentives and Other Support**

Serious consideration should be given to:

- Introducing bold and effective incentive packages for the agriculture sector, including the industries that support the growth of the agricultural sector (e.g., primary input supplies such as fertiliser, etc. and secondary conversion of agricultural produce such as manufacturing, processing, etc.)
- Granting total tax exemption to income from agriculture.

Alternatively, current provisions should be amended to allow for tax incentives on a pro-rata basis where turnover exceeds \$500,000, and should be available to all kinds of Agricultural activities. Currently, tax incentives for SME's are available only if total turnover is less than \$500,000 per annum and is available for selected prescribed activities in Agriculture, Fisheries and Tourism sectors only.

- Establish processing ventures or incentives to encourage the same which would support rural communities and farmers creating opportunities through diversifying agriculture, fisheries and forestry ventures.
- Reintroduction of the indefinite carry forward of tax losses given the high risk of investing in the sector.

### **3.5.2. Exports – Tax Incentives**

The encouragement of export industries which contribute to foreign reserves is important for the Fiji economy.

Export income deduction available under section 23 of the ITA 2015 should be increased or maintained (at least) at 50% indefinitely. Government should seriously consider this to boost its foreign reserves.

Export incentives should be available to **all** exporters of goods and services to the maximum extent. We believe this will assist in promoting further investments, create jobs, business activities and economic activities.

### **3.5.3. Fishing**

Fish being a natural resource needs to be managed effectively and with the objective of retaining maximum value within Fiji. Specific measures should be provided to encourage processing and value added activities within Fiji.

This important natural resource of seafood is being depleted. There is a need for Government to review this industry and provide greater incentives for the sustainable development of the industry.

Zero rating to be extended to new packaging products for basic food items which improves quality and is affordable to consumers.

### **3.5.4. ICT Industry**

As a significant contributor to both foreign income and employment, the ICT sector is a fast growing area in Fiji's economy. Support in the way of tax breaks and capital expenditure incentives are important to ensuring the ongoing attractiveness and viability of the industry. These incentives should be available to all investors in the industry (both existing and new) and be measured against certain criteria such as income levels, employee numbers etc.

Consideration should be given to zero-rating for VAT purposes the supply of ICT services to exempt entities in Fiji. This would promote the growth of the industry and allow the industry to develop and offer world class services both locally and abroad.

### **3.5.5. Hotel Tax Incentives**

The introduction of developer profits exemption earlier is believed to have led to a substantial increase in investment and investment activity in the tourism sector. This should be revisited.

FIA notes governments inclusion of the villa owners in the definition of “project” under the 11<sup>th</sup> schedule of the Income Tax Act however the full extent of the concession granted to hotels have not been provided.

The tax incentive regime provided previously (until the changes announced in the 2016 budget address) to the Hotel industry facilitated the development and maintenance of the sector as the leading industry and backbone of the Fiji economy. We suggest that Government re-introduce the previous incentive regime to safeguard the continued development of the industry while trying to develop other potential industries.

### **3.5.6. Tourism industry**

Government should consider a review of the level of taxes imposed on the tourism sector with a view to ensuring that Fiji does not become an expensive destination for tourists, especially as tourism is currently Fiji’s largest industry and revenue earner. There are a number of cheaper and equally attractive options for tourists to consider, and Fiji should not outprice itself.

### **3.5.7. Tax Free Regions**

The “Look North” and similar incentives should be made available not only to new companies but also to existing entities for new investment projects. This would help achieve the overall investment and socio-economic goals while removing the unfair and unreasonable bias towards new companies.

In addition to the above, the existing legislation requires that a company which has a TFR licence should derive all of its income from the TFR. As Government would appreciate, there are a number of circumstances which may require a company which has a TFR licence to derive income or contract with entities outside the TFR. Hence, the existing requirements would be prohibitive and we recommend that the legislation be amended to allow some flexibility (for example, a company with a TFR licence should derive at least 70% of its income from the TFR).

Additionally we note that the provisions included in the Regulations to the ITA 2015 do not allow for an application by the licence holder to the Minister for the extension of time in which to complete a project. This aspect is vital especially where a project is unable to be implemented within 18-24 months because of the scope and quantum of investment of the project.

### **3.5.8. Social Policy Exemptions**

Non-profit and charitable organisations play an important role in our society. Every dollar that a charity spends on providing shelter or food and clothing to the poor is another dollar that the Government now has to spend on roads, hospitals and schools.

Currently, under the Income Tax (Exempt Income) Regulations 2016 any business income derived by a non-profit or charitable organisation is subject to tax.

Previously, under the Income Tax Act 1974, the business income of a non-profit or charitable organisation was not subject to tax provided that such income was to be expended either in Fiji or for purposes which resulted in the benefit of the residents of Fiji.

We suggest that Government reconsider the current taxation of business income of non-profit and charitable organisations and revert to the provision previously under the Income Tax Act 1974.

### **3.6. STRUCTURAL REFORMS**

#### **3.6.1. Public Sector Reform**

- Continue to implement public sector reform measures to deliver efficient and effective services.
- Enforce accountability in the public service.

Review disciplinary procedures for civil servants to expedite the process.

- The FIA understands that Government revenues now amount to approximately 32% of GDP. Assuming this is accurate, Government should relook at unproductive sectors within the various Ministries to make changes.
- Government should relook at strategies around the notion of a Private sector led economy and the efficiency and effectiveness of the use of resources.

#### **3.6.2. Government Services**

- Accelerate E-Governance initiatives.
- Overhaul as a matter of priority:
  - Registrar of Companies (ROC)  
With the introduction of the new Companies Act (FCA) there has been little to no awareness exercises carried out by the ROC and or relevant Government agencies. In view of the new requirements imposed under the FCA including the substantial new charges and penalties, we suggest that Government carry out extensive awareness campaigns including the waiver of any penalties (at least in the interim) to allow entities to become aware of and voluntarily comply with the law.
  - Titles Office
  - Department of Town and Country Planning

### **3.6.3. Laws of Fiji**

- We note that Government has updated all legislation and the whole set is now available but at a significant cost. This makes the updated law inaccessible to many citizens. Furthermore, the updated legislation will quickly become outdated as new amendments come about.

We suggest that the law be available and updated online to make it readily accessible and current at all times.

## **3.7. FISCAL POLICY**

### **3.7.1. Government Debt and Expenditure Policy**

FIA supports Government's expenditure policy which is aimed at offering efficient Government services, developing infrastructure, and support and assistance to the needy. Emphasis however needs to be placed on proper management and control of expenditure and improving efficiencies within Government, thereby maximizing returns for each dollar spent and importantly getting it right the first time.

We also commend Government's initiative in increasing its level of capital expenditure. However, operating expenditure should be reduced, particularly for non-productive areas.

Government should also invest into maintenance of government assets to avoid huge capital expenditure in terms of replacement.

### **3.7.2. Health Care and Education**

There is a need for further improvements to hospitals and health centres from both a capital and operating perspective. There is also a need for improvements to the level of service and the standard of practices at these centres.

Increase investment for preventive health which must include early detection and education to tackle non-communicable diseases including cardiovascular diseases, obesity, and smoking. FIA considers that such investment will reduce vastly the impact on our on-going limited medical resources.

Commitment to education should be continued. The quality of the Fiji workforce is the key for transformation to a knowledge based economy. FIA considers that the government should ensure that our education and training bodies are sufficiently funded to support and train our workforce.

The focus must therefore be on investing in tomorrow's workforce, improving our management capability and encouraging lifelong learning.

This will be achieved by improving the educational facilities, improving academic resources and introducing strategies and measures to develop a pool of qualified, skilled and competent teachers.

Improving the teacher to students' ratio could improve the education standards.

### **3.7.3. Judiciary**

An efficient and independent judiciary is one of the critical factors for attracting investment.

Measures should be taken to further strengthen the Judiciary to provide assurance to investors on the effectiveness of the judicial system and processes.



#### **4. CONCLUSION**

Policy frameworks for the various relevant areas should be developed and reviewed consistently with the National Development Plan. The policy framework for relevant areas such as trade, investment, fiscal and monetary policy including taxation should then be used to ensure that the existing and future laws are consistent with this policy framework.

We note that while Government has announced some good initiatives in the recent past, these have sometimes been contradicted by other changes in legislation and regulations. The successful achievement of overall goals has been affected by these conflicting policies. The impact of such measures includes increasing the cost and reducing the ease of doing business, wasting limited resources on unproductive activities and reducing confidence and investment in the country.

Establishing clear and transparent policies after proper consultation with stakeholders and announcing these as part of the budget, allows stakeholders to plan accordingly. Ensuring these policies are consistent with the overall development plans while being properly and consistently applied would further enhance investor confidence.

Increasing investment, import substitution and exports in the medium to long term are imperative for economic stability and growth. New and innovative measures need to be introduced for the sustainable use of the vast potential in the various sectors including tourism, agriculture, ICT, mining, sports and small and micro enterprises.

Being the largest professional body in Fiji, the FIA has a wealth of knowledge and experience, and would be pleased to provide further assistance, guidance and support to Government, and work with Government to achieve our mutual National goals.

### **APPENDIX A – FIJI INSTITUTE OF ACCOUNTANTS**

The Fiji Institute of Accountants (FIA) is the professional organization representing the interest of professional accountants in Fiji, and is established under the Fiji Institute of Accountants Act (Cap. 259).

Our Institute is a fully registered member of the International Federation of Accountants (IFAC) which is the international parent body for most national accounting bodies in the World as well as a full member of the Confederation of Asian and Pacific Accountants (CAPA).

As a full member of IFAC, FIA has adopted, and conducts workshops and seminars for its members to encourage and ensure the effective implementation of various international standards, including:

- International Financial Reporting Standards (IFRS), including International Accounting Standards (IAS)
- International Standards on Auditing (ISA)
- International Code of Ethics
- International Standards on Education.

FIA, the pre-eminent body representing the diverse interests of more than 800 accounting, finance and business advisory professionals working in the private sector, public sector, public practice, industry and commerce, academe and the not-for-profit sector, is pleased to make this 2016/17 Budget Submission. Membership is on an individual, as opposed to an entity basis.

The overall governance of the FIA rests with the Council. The FIA has several committees covering Education and Membership, Accounting and Auditing Standards, Code of Ethics, Professional Development, Business & Government and Law Review, Journal, Act and Rules and Investigation and Disciplinary.

The key functions of the FIA are:

- To promote excellence in advocacy of the accounting profession and accountants' performance through education and professional development;
- To initiate research and formulate policies that facilitates improved performance of accountants;
- To represent the views and interest of accountants to Government, regulatory bodies and the community to foster improvements in adoption of economic and social policies for improvements in Fiji's productivity and economic progress ;
- To provide timely relevant and targeted information and support services to members and, where appropriate, Government and the community;

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- To maintain a members' code of professional and ethical conduct; and
- To develop strategic alliances with other organizations domestically and internationally to further the objectives of the FIA.