



**PRACTICE
STATEMENT No. 3**

2nd Release

SUBJECT	INLAND REVENUE SERVICE: ADMINISTRATION OF THE EXPORT INCOME DEDUCTION
DATE OF EFFECT	22 April 2004 (Note: This Practice Statement replaces the 1 st Release dated 1 April 2003)
CONFIDENTIALITY STATUS	May be released to the public
LEGISLATIVE REFERENCES	<i>Income Tax Act 1974</i> Sections 21B, 109
PRACTICE CO-ORDINATOR	Deputy Director-General (Operations) Compliance Division Inland Revenue Service

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SUMMARY OF CHANGES

This is Version 2 of Practice Statement No. 3. Major changes from Version 1 are:

- Insertion of a new interpretation on the meaning of “income” in section 21B in relation to the 2001 year (paragraphs 12 to 16).
- Two new examples of situations which do not attract the section 21B deduction (paragraph 8).

INTRODUCTION

1. This statement sets out the practice of the Inland Revenue Service (IRS) in relation to the administration of the export income deduction in section 21B of the *Income Tax Act 1974*. It is issued with the authority of the Chief Executive Officer of the Fiji Islands Revenue and Customs Authority, who is also Commissioner of Inland Revenue.

LEGISLATIVE BASIS

2. Section 21B of the *Income Tax Act 1974* was introduced, effective from 1 January 2001, to encourage export of goods and services from Fiji so as to promote economic growth and inflow of foreign exchange. It states, after an amendment effective from 1 January 2002:

“Export Income Deduction

21B.(1) In determining the total income a deduction for export income shall be allowed in accordance with this section.

(2) The amount of the deduction representing a percentage of the export income is set out in the following table.

Year of Assessment	% of Export Income to be Deducted
2001 and 2002	100%
2003 and 2004	75%
2005 and 2006	50%
2007 and 2008	25%
2009 and every year thereafter	0%

(3) For the purposes of this section, “export income” means profit derived by a taxpayer from the business of exporting goods and services but excludes re-exports.

(4) The Commissioner may, where separate records for export income are not maintained, determine such income on the basis of the following formula:-

$$\frac{A}{B} \times C$$

Where:-

A is total export sales

B is total sales

C is total profits arising from all sales.

(5) A deduction may not be claimed under this section in respect of income for which a deduction or rebate is claimed or allowed under the Fifth Schedule.”

INTERPRETATION OF LEGISLATION FOR 2002 AND LATER YEARS

3. The term “profits” is not defined in section 21B or elsewhere in the Act. For the purposes of Section 21B “profit” will be defined as “total income as defined per the Act, less all deductions, other than the section 21B deduction”. It does not mean “accounting profits” or any other interpretation. In the case of sole traders, it does not include deduction of dependant or personal allowances.
4. The term “the business of exporting goods and services” means a business which has been specifically established to sell goods and/or services on the export market. It will include businesses which have only export sales/income, or which have a mixture of export and domestic sales/income, such as a regional enterprise which sells on the Fiji domestic market and exports to other regional countries. It does not include businesses set up to cater primarily for the Fiji domestic market, which might occasionally receive income from overseas, such as an legal firm with a small number of non-resident clients. On the other hand, a legal firm which was specifically established in Fiji to service non-resident clients would meet the definition.
5. In order for a taxpayer to show that they carrying on the business of exporting goods and service, they must be able to demonstrate that they have sought export markets eg by advertising their products overseas, having overseas agents, or making business trips overseas in order to secure export sales.
6. The term “sales” in the formula in subsection 21B(4) includes sales income from the sale of goods, and gross income from the provision of services.

EXAMPLES

7. In general terms, the following are some examples of cases which qualify for the section 21B deduction:
 - income arising from the supply of goods and services to international carriers (air and sea) provided those supplies are consumed outside Fiji. For example, the provision of meals to international airlines will qualify, where those meals are consumed after the plane leaves Fiji. But cleaning of international aircraft while on the ground in Fiji would not qualify;
 - a Fiji resident contracts with a non-resident company to provide services, and the services are provided either in Fiji or another country; and

- a shipping agent earns commission income from non-resident shipping firms, or and insurance company earns commission as acting as agent for non-resident insurers.
8. In general terms, the following are some examples of cases which do **not** qualify for the section 21B deduction:
- income arising from supplies to a foreign tourist on holiday in Fiji with goods and services by hotels, duty-free shops, jewellers or other businesses;
 - a Fiji resident contracts with a Fiji resident company to provide services, and the services are provided either in Fiji or another country;
 - a Fiji resident contracts to supply goods to a person in Country Y. The contracting and financing transactions take place within Fiji. The goods are shipped from Country X to Country Y without ever landing in Fiji; and
 - a Fiji telephone service provider provides an inbound visitor to Fiji with a roaming service for which the Fiji provider receives a fee from an overseas provider.

TRANSITIONAL ARRANGEMENTS

9. Some taxpayers with a balance date other than 31 December may experience difficulties calculating their section 21B deduction. For example, a taxpayer may have a 2001 tax year running from 1 July 2000 to 30 June 2001, and the section 21B concession only operates from 1 January 2001.
10. Such a taxpayer would be entitled to a full year's deduction under section 21B, as the table in subsection 21B(2) refers to the "Year of Assessment", not calendar year. However, these taxpayers may not have the record keeping systems in place to calculate their entitlement for the period 1 July 2000 to 31 December 2000.
11. The IRS will accept any reasonable calculation of the section 21B deduction for this interim period. If requested, taxpayers must be able to show how they calculated their claim. The IRS will evaluate each claim on a case by case basis, bearing in mind that taxpayers will not have known during this period that the section 21B deduction would be available to them.

INTERPRETATION OF LEGISLATION FOR 2001 YEAR

12. FIRCA will interpret the section 21B in existence in 2001 in the same manner as outlined above for 2002 and later years, with one additional interpretation in relation to the meaning of the word "income".

13. A law change to Section 21B effective from 1 January 2002 changed the word “income” in subsection (3) to “profit”.
14. It is the position of FIRCA that this was not a conceptual change, but a clarification of existing policy. That is, the 2001 version of section 21B was intended to allow a deduction in respect of net profits rather than gross income.
15. This view is supported by reference to the Cabinet Memorandum of January 2001 prepared by the Minister for Finance and National Planning. That Memorandum states at paragraph 3.4:

“A tax deduction will now be granted to all *exporters* in respect of profits derived from export income. The deduction to be allowed is 100% of the export income in the first 2 years commencing 2001 but is gradually reduced to nil over a period of 8 years in order to comply with World Trade Organisation obligations in relation to export subsidies.”

16. Claims for section 21B deductions in 2001 returns will be allowed on the basis of the profit rather than the gross income approach. Objections to assessments made on the “profits” basis will be disallowed, and any appeals will be vigorously defended by FIRCA.

RECORD-KEEPING STANDARDS

17. The record-keeping provisions of the *Income Tax Act* are found in section 109, which states:

“Books of account

109. (1) If a taxpayer fails or refuses to keep adequate books or accounts for tax purposes, the Commissioner may require the taxpayer to keep such records and accounts as he may prescribe.

(2) Every taxpayer carrying on any trade, business or profession shall keep or cause to be kept proper books of account sufficient to record all transactions necessary in order to ascertain the profit or gain made or the loss incurred in each such trade, business or profession.

...”

18. In order to meet the requirements of section 109, taxpayers wishing to claim a section 21B deduction should maintain a “schedule of exports” which contains at least the following information, for each tax year:

- name of export customer
- name of the country where export customer located
- invoice date and number
- brief description of goods exported or services rendered

- value of goods and/or service exported
- export licence number (for exported goods only).

This schedule should be kept by the taxpayer for the record-keeping period prescribed in subsection 109(3), currently 7 years, and made available if an IRS assessor or auditor requests it.

RISK MANAGEMENT

19. If a taxpayer wishes to claim a section 21B deduction in their tax return, the IRS will assess the claim under risk management principles. Basically, no documentation needs to be submitted with a tax return to substantiate a claim, unless the assessor specifically asks a taxpayer to send in documentation. This may occur either before or after the assessment is made; or an auditor may subsequently ask for the information.
20. In the assessing process, claims for section 21B deductions are to be given a risk rating per the table below, and action taken accordingly.

Factors for consideration	Risk rating	Action
<ul style="list-style-type: none"> ▪ There is no information available to the assessor which indicates that the case belongs in the medium or high risk category. 	Low	The deduction should be allowed per the information in the return.
<ul style="list-style-type: none"> ▪ Past returns indicate that the taxpayer has both export and domestic sales, but no appropriate apportionment per the formula in subsection 21B(4) has been made. ▪ The taxpayer prepares their own return, without a tax agent. ▪ The return is prepared by a tax agent who is generally considered in IRS to have a high risk associated with returns prepared by them. ▪ The taxpayer has been audited in past years and their section 21B deduction adjusted as a result of the audit. 	Medium	The deduction should be allowed per the information in the return, and after assessment, a copy of the schedule of export income should be requested from the taxpayer.

Factors for consideration	Risk rating	Action
<ul style="list-style-type: none"> ▪ The schedule of exports has been requested from the taxpayer, and this has not been provided, or has been provided and does not meet the record-keeping standard above. 	High	The deduction should be disallowed.

21. FIRCA is currently developing a data warehouse which will include the IRS Fiji Integrated Tax System (FITS) and Customs ASYCUDA databases. Data on these databases will be matched in-house and any discrepancy relating to a section 21B deduction claim reported to Compliance section.