



THE INCOME TAX (AMENDMENT) BILL 2005



**THE INCOME TAX (AMENDMENT)
BILL 2005**

**A
BILL
Entitled**

AN ACT TO AMEND THE LAW RELATING TO INCOME TAX; TO MAKE TAX DEDUCTED FROM CERTAIN PAYMENTS A FINAL TAX ON THE INCOME TO WHICH THE PAYMENTS RELATE AND FOR OTHER MATTERS CONNECTED THEREWITH OR INCIDENTAL THERETO.

ENACTED by the National Parliament of Solomon Islands.

THE INCOME TAX (AMENDMENT) BILL 2005

ARRANGEMENT OF CLAUSES

CLAUSE

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✓ 1. (1) This Act may be cited as the Income Tax (Amendment) Act 2005. Short title and commencement

(2) This Act shall come into force on 1st January, 2006 and, subject to subsection (3), shall apply for the year commencing 1st January 2006.

(3) This Act shall apply to payments referred to in a tax deduction provision made on or after 1st January, 2006.

✓ 2. Section 2 of the Income Tax (hereinafter referred to as the "principal Act") is hereby amended in subsection (1) as follows - Amendment of section 2 Cap 123

(a) by inserting the following definition after the definition of "approved annuity contract"-

"approved form" means a form approved by the Commissioner for the purposes of any application, notice, or other document to be furnished under the Act or any rules made under the Act;"

(b) by deleting the definition of "business" and substituting therefor the following new definition -

"business" includes any trade, or profession, vocation, or other services of an independent nature, and any concern or adventure in the nature of trade, but does not include employment;"

(c) by inserting thereafter the following definitions in proper alphabetical sequence -

"employee" means an individual engaged in employment;

"employer" means a person who engages or remunerates an employee;

"employment" includes -

(a) a directorship or other office in the management of a company or body of persons;

(b) a position entitling the holder to a fixed or ascertainable remuneration;

(c) the holding or acting in any public office;

(d) performance under a contract principally for work or services where the Minister provides by Order that the relationship will be regarded as one of employment for the purpose of the tax deduction provision; or

(e) performance under a contract principally for work or services where the parties voluntarily agree with the Commissioner that the relationship will be regarded as one of employment for the purpose of the tax deduction provision;

“employment income” means gains or profits from employment as determined under section 5 of the Act;”.

“interest” means -

(a) an amount, whether described as interest, discount, premium or otherwise, whether periodical or a lump sum, as consideration for the use of money or being given time to pay;

(b) an amount that is functionally equivalent to an amount referred to in paragraph (a); or

(c) a commitment, guarantee, service, or similar fee payable in respect of a debt or other instrument or agreement giving rise to interest under paragraphs

(a) or (b);”;

“paid” includes -

(a) applied on behalf of a person either at the instruction of the person or under any law;

(b) distributed, reinvested, accumulated, or capitalised;

(c) credited to an account; or

(d) made available to a person; “; and

“tax deduction provision” means sectiond 36,

36A, 36B, 37 or 38;”;

3. ✓ Section 3 of the principal Act is repealed and the following new section substituted therefor - Repeal and replacement of section 3

“Income in respect of which tax charged

3. (1) Subject to this Act, tax shall be charged for each year upon the income for that year of any person in respect of -

(a) gains or profits from -

of time

(i) any business, for whatever period of time carried on;

(ii) employment; or

(iii) any right granted to any other person for the use or possession of any property;

(b) dividends, interest or discounts;

(c) any pension, charge or annuity;

(d) any amount received by way of alimony or allowance under a decree of divorce, a judicial order of separation or maintenance, or a deed of separation or maintenance;

(e) income from any other source whatsoever; or

(f) any amount deemed to be income under this Act.

(2) For the purposes of subsection (1) -

(a) the income of a resident person includes income accrued in, was derived from or was received in Solomon Islands, or elsewhere; or

(b) the income of a non-resident person includes income accrued in or was derived from Solomon Islands."

Amendment
of section 4

✓ 4. Section 4 of the principal Act is amended in subsection (1) by deleting the words "section 3(a)(i)" and substituting therefor the words "section 3(1)(a)(i)".

Repeal and
replacement of
section 5

✓ 5. Section 5 of the principal Act is repealed and the following new section substituted therefor -

"Provisions
relating to
income from
employment

5. (1) For the purposes of section 3(1)(a)(ii) and subject to subsection (2), gains or profits from employment means any amount, whether of a revenue or capital nature, arising from employment, including -

(a) any wages, salary, leave pay, payment lieu of leave, overtime pay, bonus, commission, fees, gratuity, or work condition supplements, and including any remuneration paid to the holder of an office;

(b) the value of any benefit-in-kind, whether convertible to money or not;

(c) the amount of any allowance provided by an employer to an employee, including a cost of living, subsistence, rent, utilities, education, entertainment, meeting, or travel allowance, but not including any allowance expended wholly and exclusively in the performance of the employee's duties of employment;

(d) the amount of any expenditure incurred by an employee that is paid or reimbursed by the employer, other than expenditure incurred on behalf of the employer wholly and exclusively in the performance of the employee's duties of employment;

(e) amount as consideration for the agreement by a person to -

- (i) enter into employment;
- (ii) any conditions of employment or any changes to the employee's conditions of employment; or
- (iii) a restrictive covenant in respect of any past, present, or prospective employment:

(f) any amount received on termination of employment, whether paid voluntarily or under an agreement, including any compensation for redundancy or loss of employment and golden handshake payments; or

(g) any pension, annuity, or supplement to a pension or annuity received in relation to employment.

(2) The following amounts are not included in gains or profits from employment -

(a) the cost of passages paid by an employer for passage of an employee within Solomon Islands or between Solomon Islands and any place outside Solomon Islands;

(b) the cost of any medical services paid by the employer; or

(c) the amount paid by an employer as a contribution to any approved pension fund or the Solomon Islands National Provident Fund to the extent that such amount does not exceed fifteen per centum of the employee's employment income for the year in which the contribution is made.

(3) The rate of tax payable by an employee on an amount paid by a terminating employer and included in employment income of the employee under subsection (1)(f) shall be computed according to the following formula -

A/B

where -

A is the total tax paid by the employee on employment income paid to the employee by the terminating employer in the termination period; and

B is the total employment income paid to the employee by the terminating employer in the termination period.

(4) Any gains or profits from employment exercised in the Solomon Islands shall be deemed to be derived from the Solomon Islands whether or not they are received in the Solomon Islands.

(5) In this section -

“terminating employer” means an employer who has paid an amount to an employee referred to in subsection (1)(f); and

“termination period” means the lesser of -

(a) the current year prior to the date of termination of employment and the previous two years; or

(b) the actual period of employment with the terminating employer prior to the date of termination.”.

Amendment of
section 6

✓ 6. Section 6 of the principal Act is amended by deleting the words “section 3(a)(iii)” and substituting therefor the words “section 3(1)(a)(iii)”.

Amendment of
section 7

✓ 7. Section 7 of the principal Act is amended by deleting the words “section 3(b)” and substituting therefor the words “section 3”.

Amendment of
section 18

✓ 8. Section 18 of the principal Act is amended by deleting subsection (5).

9. ✓ Section 20 of the principal Act is amended as follows - Amendment of
section 20

- (a) in subsection (2) -
- (i) by deleting the full stop at the end of subsection (2) paragraph (h) and substituting therefor a semi colon; and
- (ii) by inserting the following paragraph after paragraph (h) -

“ (i) any expenditure incurred in deriving employment income;”;

- (b) by adding the following new subsection after subsection (2) -

“ (2A.) If a person is required to deduct tax from a payment under a tax deduction provision and, in the absence of this subsection, the person would be allowed a deduction under the Act for the payment, the person shall not be allowed the deduction until the correct tax required to be deducted has been paid to the Commissioner.”

✓ 10. Section 28 of the principal Act is amended as follows - Amendment
of section 28

- (a) in subsection (1), by deleting the words “a resident individual” and substituting therefor the words “an individual”; and

- (b) by deleting subsection (2) and substituting therefor the following new subsection -

“ (2) Where -

(a) an individual has become a resident individual for the purpose of engaging in any employment or carrying on of any business in Solomon Islands; or

(b) a non-resident individual is in Solomon Islands for the purpose of engaging in any employment or carrying on of any business in Solomon Islands,

and the individual is present in Solomon Islands for part only of a year, the individual shall be entitled for that year to only such portion of the exemption as the total period of the individual's presence in Solomon Islands for the year bears to the whole of the year."

Repeal of
section 29

✓ 11. Section 29 of the principal Act is repealed.

Repeal and
insertion of new
sections 36, 36A
and 36B

✓ 12. Section 36 of the principal Act is repealed and the following new sections inserted as sections 36, 36A and 36B respectively -

"Deduction
of tax from
dividends

36. (1) Subject to subsection (2), a resident company shall deduct tax from the gross amount of any dividend paid at the rate of -

(a) in the case of a resident corporate or individual shareholder, twenty per centum; or

(b) in the case of a resident body of persons, other than a corporation and a non-resident shareholder, the rate prescribed in section 33(1).

(2) This section does not apply to a dividend exempt from income tax.

Deduction
of tax from
employ-
ment

36A. (1) Subject to subsection (2), an employer shall deduct tax from the gross amount of employment income paid to an employee as prescribed in the Tax Deduction Rules 2005.

(2) This section does not apply to employment income that is exempt from income tax.

(3) The obligation of an employer to deduct tax under subsection (1) -

(a) shall not be reduced or extinguished because the employer has a right, or is otherwise obliged, to deduct any other amount from a payment of employment income; and

(b) shall apply notwithstanding any law that provides that the employment income of an employee is not to be reduced or subject to attachment.

Deduction
of tax from
interest

36B. (1) Subject to subsection (2), a resident person or a permanent establishment in Solomon Islands of a non-resident person shall deduct tax from the gross amount of interest paid to a resident person at the rate of 10%.

(2) This section does not apply to interest income -

- (a) that is exempt from income tax;
- (b) paid to a financial institution; or
- (c) interest income paid by a resident individual who is not carrying on a business.

(3) In this section -

“non resident partnership” means any partnership that is not a resident partnership; “non-resident person” includes a non-resident partnership;

“permanent establishment” has the same meaning as in section 38(2);

“resident partnership” means any partnership that has a resident person as a partner; and

“resident person includes a resident partnership.”

13.

Section 37 of the principal Act is amended as follows -

Amendment
of section 37

- (a) in subsection (2) -
 - (i) by deleting the full stop at the end of paragraph (g) and substituting therefor a semi colon; and
 - (ii) by inserting the following new paragraph after paragraph (g) -
 - “(h) income from stevedoring services; and
 - (i) any other income or class of income provided by order of the Minister;”;

- (b) by deleting subsections (3), (4), (5) and (6); and
- (c) in subsection (7) -
- (i) by deleting the full stop after the definition of royalties” and inserting a semi colon; and
- (ii) by inserting the following definition after the definition of “royalties”-

“income from stevedoring service” means
gross payments for the service of

(a) loading or unloading of
cargo onto or from ships;

(b) loading or unloading of
ship’s stores, coal or fuel oil (whether for
bunkers or not), passengers’ luggage, or
mails onto or from ships;

(c) handling or storage of
cargo or other goods at or adjacent to a
wharf;

(d) driving or operating
mechanical appliances in connection with
the loading or unloading of ships, or with
the handling or storage of cargo or other
goods at or adjacent to a wharf;

(e) hauling or trucking from
ship to shed or shed to ship;

(f) removing or replacing of
beams or hatches;

(g) handling of dunnage or
ballast;

(h) preparing or cleaning of
holds; or

(j) preparing gear for use in
connection with the loading or unloading
of ships ,”.

- ✓ 14. Section 38 of the principal Act is amended as follows -

Amendment
of section 38

- (a) in subsection (2) -
 - (i) by deleting the definition of “interest”;
 - (ii) by inserting at the beginning of the definition of “management services” the words “income from;”;
 - (iii) by deleting paragraph (i) of the aforesaid definition and substituting therefor the following new paragraph -

“(i) employment income; or;” and

- (iv) by deleting paragraph (i) of the definition of “professional services” and substituting the following paragraph -

“(i) employment income; or;”;

- (b) in subsection (3) -
 - (i) by deleting the word “and” at the end of the paragraph (g);
 - (ii) by deleting the full stop at the end of paragraphs (h) and substituting therefor the word “and”;
 - (iii) by inserting the following paragraph after paragraph (h) -

“(i) income from management services;”;

“(j) any other income or class of income provided by order by the Minister.”;

- (c) by deleting subsections (4), (5) and (6).

↓ 15. The principal Act is hereby amended by inserting the following new sections as sections 38A to 38J respectively -

"Payment of tax deducted"

"Failure to pay tax deducted"

38A. Tax required to be deducted by a person under a tax deduction provision shall be paid to the Commissioner within fifteen days after the end of the month in which the person was required to deduct the tax.

"Failure to pay tax deducted"

"Payment of tax deducted"

38B. (1) If a person -

(a) fails to deduct tax as required under a tax deduction provisions; or

(b) having deducted tax fails to pay the tax to the Commissioner as required under section 38A,

the person shall be personally liable to pay to the Commissioner the amount of tax, and any penalty and additional tax due in respect of the failure.

(2) A person liable for an amount of tax under subsection (1) as a result of failing to deduct the tax shall be entitled to recover the tax (but not any penalty or additional tax due in respect of the failure) from the recipient of the payment.

"Recovery of tax from recipient" → insert

38C. (1) If a person fails to deduct tax as required under a tax deduction provision, the Commissioner may recover the tax from the recipient of the payment provided the total amount recovered does not exceed the tax that should have been deducted;

(2) Notwithstanding the recovery of any tax under subsection (1), the person who failed to deduct the tax shall continue to be liable for -

(a) any other legal action in relation to the failure;

(b) the imposition of any penalty or additional tax in respect of the failure; and

(c) the disallowing of a deduction for the expenditure to which the failure relates under section 20(2A).

Evidence of
tax
deduction

38D. A person deducting tax under a ^{tax} deduction provision shall, at the time of deducting the tax, furnish the recipient of the payment with written evidence that tax has been deducted from the payment.

Priority of
deducted tax

38E. (1) Tax deducted by a person from a payment under a tax deduction provision -

(a) shall be held by the person in trust for the government; and

(b) shall not be subject to attachment in respect of any debt or liability of the person.

(2) In the event of the death, liquidation or bankruptcy of a person who has deducted tax, any tax deducted shall not form part of the person's estate and the Commissioner has first claim for that amount before any distribution of property is made.

(3) An amount of tax that a person is required to deduct from a payment under a tax deduction provisions shall be -

(a) a first charge on the payment; and

(b) deducted prior to any other amount that the person may be required to deduct from the payment by virtue of an order of any Court or under any other law.

Indemnity

38F. A person who has deducted tax under a tax deduction provision and remitted the tax to the Commissioner shall be indemnified against any claim by the recipient for payment of the deducted amount.

Annual tax
deduction
certificate

38G. (1) A person deducting tax from a payment under a tax deduction provision shall furnish the recipient of the payment from which tax has been deducted with an annual tax deduction certificate in the form and manner prescribed.

(2) A person required to furnish a return of income for a year shall attach to the return the annual tax deduction certificate for any income in respect of which the deducted tax is not a final tax on the income.

Monthly
summary

38H. A person deducting tax from a payment under a tax deduction provision shall furnish to the Commissioner a monthly summary in the form and manner prescribed.

Deducted
tax treated
as tax.

38J. Tax deducted under a tax deduction provision shall be treated as tax for the purposes of sections 83(4), 84, 85, 87, 88, 89 and 89A.”.

Repeal and
insertion of new
sections 40 and
40A

16. Section 40 of the principal Act is repealed and the following sections inserted as sections 40 and 40A respectively -

“Set-off
of tax
deducted

40. (1) For the purposes of this Act, if tax has been deducted from a payment under a tax deduction provision, the amount derived by the recipient of the payment shall be the amount of the income before the deduction of the tax.

(2) Subject to subsection (3), if tax has been deducted from a payment under a tax deduction provision, the recipient shall set off the deducted tax against tax charged on the income represented by the payment.

(3) Subsection (2) shall not apply if -

(a) the tax deducted is a final tax on the income under section 40A; or

(b) the recipient does not attach an annual tax deduction certificate to the recipient’s return as required under section 38G(2) as evidence of the amount of tax deducted.

Deducted
tax as a
correct
final tax

40A. (1) Subject to subsection (2), this section applies to tax deducted under the following sections provided the correct amount has been deducted and paid to the Commissioner -

(a) section 36 if the dividend is paid to -

(i) a person who is not resident in Solomon Islands;

(ii) resident body of persons other than a company; or

- (iii) resident individual person;
- (b) section 36A;
- (c) section 36B, if the interest is paid by a financial institution and is derived by a resident individual;
- (d) section 37, if the payment is -
 - (i) made to a resident body of persons other than a company;
 - (ii) made to a resident individual when the total income of the individual including the payments covered by section 37 for the year is less than \$10,000; or
 - (iii) income is covered by section 37(2)(d) and is derived by a resident individual; or
- (e) section 38.

(2) This does not apply to tax deducted under -

(a) section 36 from dividends, section 36A from director's fees, and section 36B from interest if the total amount of dividends, director's fees, and interest income derived by a resident individual person for a year is more than \$10,000; or

(b) section 36A from employment income (including director's fees) if the employee has three or more employers concurrently at any time during a year and the total employment income of the employee for the year is more than \$60,000.

(3) If this section applies, the tax deducted shall be a final tax on the income of the recipient in respect of which the tax has been deducted and -

(a) the income shall not taken into account in calculating the total income of the recipient;

(b) no deduction shall be allowable under this Act for any expenditure incurred in deriving the income; and

(c) if the only income derived by the recipient for a year is income covered by this section, the recipient shall not furnish a return of income as required by section 57 for the year.

Repeal of
section 43

✓ 17. Section 43 of the principal Act is repealed.

Amendment to
section 57

✓ 18. Section 57 of the principal Act is amended in subsection (1) by inserting the words "deriving income" before the words "chargeable to tax".

Amendment
to section 58

✓ 19. Section 58 of the principal Act is amended -

(a) in subsection (1) -

(i) by deleting from paragraph (c) the words "tax certificate or an annual summary as required under rules 25, 26, 27, 28 and 29 of the Tax Deduction Rules 1981" and substituting therefor the words "an annual tax deduction certificate or monthly summary as required under the Tax Deduction Rules 2005; and

(ii) by deleting all the words that appear thereafter in paragraph (c) and substituting therefor the following -

"the person shall be liable for a penalty of a sum of five hundred dollars and an additional fifty dollars for each month or part month of default,"; and

(b) by deleting subsection (2) and substituting there for the following new subsection (2) -

" (2) The Commissioner may, by notice in writing, require a person in default under subsection (1) to furnish such return, certificate, or summary within such period as may be specified in the notice".

Repeal of sections
59 and 60

✓ 20. Sections 59 and 60 of the principal Act are repealed.

Amendment
of section 63

✓ 21. Section 63 of the principal Act is amended by inserting the following subsection after subsection (3) -

" (4) The Commissioner may require a police officer to be present for the purposes of exercising powers under this section,".

- ✓ 22. Sections 64, 65 and 66 of the principal Act are repealed. Repeal of section 64, 65 and 66
- ✓ 23. Section 70 of the principal Act is amended by deleting subsection (1) and substituting therefor the following subsection - Amendment of section 70
- “ (1) If a person required to deduct tax under a tax deduction provision -
- (a) fails to make the deduction either in whole or part; or
- (b) makes the deduction or purports to make the deduction and fails to remit the deducted tax to the Commissioner in whole or part,
- the Commissioner may, when satisfied that such failure was not due to any cause beyond the person’s control, charge the person with an additional amount, not exceeding double the amount of tax not deducted or remitted to the Commissioner, as the case may be.”.
- ✓ 24. Section 90 of the principal Act is amended in subsection (1) by deleting the words “in respect of any assessment”; and by inserting the word “assessment,” before the words “deduction or otherwise”. Amendment of section 90
- ✓ 25. Section 96 of the principal Act is amended - Amendment of section 96
- (a) by numbering the existing section as subsection (1);
- (b) by deleting from paragraph (a) of subsection (1) so renumbered the words “under this Act or under any notice” and substituting therefor the words “under this Act, the Tax Deduction Rules 2005 or under any notice”; and
- (c) by inserting the following subsection as subsection (2) -
- “ (2) A Court may order, by notice in writing a person guilty of an offence under paragraph (a) or (b) of subsection (1) to furnish the document or return within such period as may be specified in the notice.”.

Amendment
to sixth
Schedule

✓ 26. The Sixth Schedule to the principal Act is amended in paragraph (xiv) by inserting the words “income from” before the words “management services”.

Amendment
to Seventh Schedule

✓ 27. The Seventh Schedule to the principal Act is amended in paragraph (vii) by inserting the words “income from” before the words “stevedoring services”.

THE INCOME TAX (AMENDMENT) BILL 2005

Objects and Reasons

This Bill seeks to amend the Income Tax Act so as to make the deduction of tax from certain payments as final tax on the income to which the payment relates.

As the provisions of the Bill are detailed and technical in nature, an explanatory memorandum is attached to the Bill. The memorandum provides detailed explanations in respect of the particular clauses that are to be amended.

MINISTER OF FINANCE

A handwritten signature in black ink, appearing to read 'J. Bynum', is written below the text 'MINISTER OF FINANCE'. The signature is fluid and cursive, with a large loop at the end.

THE INCOME TAX (AMENDMENT) BILL 2005

EXPLANATORY MEMORANDUM

The Income Tax (Amendment) Bill 2005 (the Bill”) proposes the amendment of the Income Tax Act (Cap. 123) (the “Act”) to make the deduction of tax from certain payments a final tax on the income to which the Act the payment relates. The Bill also makes a number of technical corrections to this Memorandum provides an explanation of the Bill.

1. Short title and commencement

Subsection (1) provides that, when enacted, the Bill may be cited as the Income Tax (Amendment) Act 2005.

Subsection (2) provides that the Bill comes into force on 1 January 2006. It also provides that subject to subsection (3), the Bill applies to the tax year commencing on 1st January 2006 and subsequent tax years.

Subsection (3) provides that the Bill applies to payments referred to in a tax deduction provision made on or after 1 January 2006. “Tax deduction provision” is defined in section 2 to mean section 36, 36A, 36B, 37 and 38 of the Act.

2. Amendment to section 2

This section amends section 2 of the Principal Act, which defines terms used in that Act.

Paragraph (a) inserts a definition of “**approved form**”. This is any form approved by the Commissioner for the purposes of any application, notice, or other document required to be furnished under the Act or any Rules made under the Act (such as the *Tax Deduction Rules 2005*).

Paragraph (b) substitutes a new definition of “**business**”. This is consequent upon the redrafting of section 3 of the Act, which deletes the words “or services rendered” from the former section 3(a)(ii) of the Act. The new definition makes it clear that the rendering of independent services is treated as a business. While, this was always the case under the Act, the purposes of the amendment is to avoid any argument that, as a result of the amendment to section 3, independent services are not covered by any paragraph in that section.

The new definition also expressly provides that business does not include any employment. The Bill includes a definition of “employment” in section 2. Thus, the concepts of business and employment are mutually exclusive. If an activity can be characterised as both employment and a business (as may be the case with the holding of some offices), the characterisation of the activity as employment has priority. This means, for examples, that section 36A (inserted by the Bill) applies to any income derived from the activity.

Paragraph (c) inserts definitions of “employee”, “employer”, “employment” and “employment income”. These definitions are primarily relevant to the redrafting of section 5 of the Act and to the deduction of tax from employment income under new section 36A.

“**Employee**” is defined to mean an individual engaged in employment. As discussed below, employment is defined broadly and includes the holding of an office. To ensure consistency with the definitions of “employee” and “employment”, “**employer**” is defined as any person who engages or remunerates an employee. This includes, for example, a person who remunerates an office holder.

The concept of employment is central to the definitions of “employee” and “employer”. “**Employment**” is defined inclusively so that it otherwise has its general law meaning. An employment relationship as ordinarily understood does not include an individual engaged on his or her own account as an independent contractor. An independent contractor is carrying on a business and therefore, the remuneration derived by the contractor is business income.

While there is no single test to determine whether a worker is an employee or independent contractor, the courts have identified various features of the relationship as a guide to answering the question. Such features include:

- the degree of control the payer has as to how the services are carried out;
- whether or not the contract is to achieve a specified result;
- the degree of risk borne by the worker;
- conditions of engagement such as:
 - the provision of benefits including, annual, sick leave; superannuation;
 - task allocation and control over the timing and scheduling of work;

- the place at which services are performed;
- who provides any tools, plant or equipment/facilities necessary to carry out the work;
- termination of engagement

Another way of looking at it is to consider whether the payee is actually carrying on a business rather than working in the business of another.

Paragraph (a) - (c) of the definition treat the holding of various offices as employment. While, in legal form, an office holder is not an employee, there is little practical difference in substance between the two relationships. In the case of an office holder the duties attach to the office itself whereas an employee derives their duties from the contract with the payer. In both cases, the remuneration paid is essentially for the labour of the person. Consequently, it is appropriate to treat them the same for tax purposes. Paragraph (a) treats the office of company director as an employment. This means that director's fees are treated as gains or profits from employment under the new section 5 and are subject to the deduction of tax under new section 36A. Paragraph (a) also includes any other office in the management of a company or body of persons (such as a club). Paragraph (b) treats any position entitling the holder to a fixed or ascertainable remuneration as an employment. Paragraph (c) treats the holding of a public office as an employment.

Paragraph (d) of the definition allows the Minister to determine that an independent contractor relationship between parties is, for the purposes of the Act, to be treated as if it were an employment relationship. The Minister is able to specify that certain workers, who may in fact meet the tests for an independent contractor relationship but are considered to be 'employee like' in nature, are to be treated as employees for tax purposes. An example of where the Minister may make such a determination would be where the contract is for the personal effort and skill of an individual and the individual is expected to bear little business expenditure in providing the services.

Paragraph (e) of the definition allows the Commissioners to accept voluntary registration of an employment relationship where the parties to an otherwise independent contracting relationship seek to have the relationship treated as an employment relationship for tax purposes. The Commissioner must agree to such treatment before the relationship can be treated in this manner.

"Employment income" is defined to mean gains or profits from employment as determined under the redrafted section 5.

Paragraph (d) inserts a definition of "interest". This is relevant to a number of provisions in the Act, including new section 36B, which provides for the deduction of tax by the lender from certain interest payments. The definition is an expanded version of the definition in section 38(2) of the Act, which is deleted by the Bill.

“Interest” is defined broadly to reflect the fact that there is enormous flexibility on monetary markets as to how financial instruments may be structured. Paragraph (a) of the definition includes any amount that is consideration for the use of money or for being given time to pay. An amount comes within paragraph (a) regardless of whether it is paid as a lump sum or periodically, and however it may be described. Paragraph (a) includes discounts and premiums as these are amounts paid for the use of money.

Paragraph (b) of the definition includes any amount that is functionally equivalent to an amount that comes within paragraph (a). Examples include an amount payable for the time value of money under a derivative financial instrument and a payment of defaulted interest by a guarantor.

Paragraph (c) of the definition includes a commitment, guarantee, service or similar fee payable in respect of a debt or other instrument or agreement giving rise to interest under paragraph (a) or (b). The reference to “other instrument or agreement” is intended to ensure that paragraph (c) co-ordinates with the broad definition of interest in the other paragraphs.

Paragraph (e) inserts a definition of **“paid”**. The definition is primarily relevant to the tax deduction provisions, particularly sections 36, 36A and 36B, it is an extended version of the definition in current section 36(6) of the Act, which is deleted by the Bill.

Paragraph (f) inserts a definition of “tax deduction provision”. This is a mechanical provision relevant to new section 38A-38J, and 40. **“Tax deduction provision”** is defined to mean those sections requiring persons to deduct tax from payments made by the person, namely sections 36 (dividends), 36A (employment income), 36B (interest), 37 (certain gross payments to residents) and 38 (certain payments to non-residents).

3. Insertion of new section 3

This section substitutes a new section 3 into the Act, which provides for the charging of tax on income. The redrafted section makes technical corrections to the current law.

The current section 3 does two things - first, it imposes income tax on the items of income listed in paragraphs (a)-(e); and secondly, it states the jurisdictional limits on the income tax (subsections (1) and (2)). While the intention is clear, the current drafting is a little confusing in that the items charged to tax are listed in paragraphs (a)-(e) that follow subsection (2). The Bill redrafts the section so that subsection (1) lists the amounts subject to income tax and subsection (2) sets out the jurisdiction limits.

The only change to the existing law is that the words “or services rendered” in current section 3(a)(ii) have not been reproduced. This is a simplification measure to facilitate the deduction of tax as a final tax on employment income. A definition of “employment” has been included in section 2. This definition is in broad terms and includes the rendering of services as part of the holding of an office. Thus, the

reference to employment in section 3(1)(a)(ii) will include employment within the ordinary meaning of the term (see the commentary to the definition above) and the holding of an office. As explained above, the provision of any other services is treated as a business.

4. Amendment to section 4

This section amends section 4, which explains the meaning of gains or profits from business for the purposes of section 3(1)(a)(i). The amendment changes the cross reference in subsection (1) to “section 3(1)(a)(i)” consequent upon the redrafting of section 3.

5 Insertion of new section 5

This section substitutes a new section 5 into the Act, which explains the meaning of gains or profits from employment for the purposes of section 3(1)(a)(ii). By virtue of the definition of “employment income” in section 2 of the Act (inserted by the Bill), any amount that is a gain or profit from employment under the new section 5 is treated as employment income for the purposes of the Act, including the tax deduction provision in section 36A.

The new section 5 involves some simplification and rationalisation of the existing section 5, in broad terms, any amount arising from employment is treated as employment income. An amount is treated as employment income regardless of whether it is revenue or capital in nature. This is intended to make the deduction of tax simple as it avoids employers having to decide whether a particular amount is revenue or capital in nature.

Subsection (1) defines gains or profits from employment to mean any amount arising from employment. The words “arising from employment” require that there is a nexus between the amount received and the employee’s employment. It is intended that “arising from employment” be interpreted broadly. However, any amount that is a pure gift (e.g., a wedding present given to an employee) would not be employment income. Paragraphs (a) - (g) include specific amounts in employment income.

Paragraph (a) includes any salary, wages, or other remuneration such as leave pay, payment in lieu of leave, overtime pay, bonus, commission, fees, gratuities, or work condition supplements. An example of a work condition supplement is an additional amount paid as compensation for unpleasant or dangerous work conditions. Paragraph (a) also includes any remuneration paid to the holder of an office. This is intended to ensure that section 5 is consistent with the broad definition of “employment” inserted into section 2.

Paragraph (b) includes the value of any benefit-in-kind. It is expressly provided that the value of a benefit is included in employment income, whether it is convertible to money or not. This overrides the general principle that a benefit that is not convertible to cash is not income. Consequently, non-convertible benefits are taxable under the Bill.

Paragraph (c) includes the amount of any allowance provided to an employee. The paragraph specifically lists the following allowances as included in employment income: a cost of living, subsistence, rent, utilities, education, entertainment, meeting or travel allowance. The list is inclusive only and any other amount received by an employee that is within the ordinary meaning of allowance is included in employment income under this paragraph. An allowance is an amount paid to an employee for use by the employee in meeting particular expenses but with no requirement for the employee to vouch that the amount has been expended for the stated purpose. An allowance is distinguished from a reimbursement, which is the subject of paragraph (d) (see below).

There is an exception from inclusion in paragraph (c) for any allowance expended wholly and exclusively in the performance of the employee's duties of employment. An example of an allowance that may come within the exception is a travel allowance received by an employee to cover fares and accommodation expenses incurred when travelling solely for the purposes of employment. The exclusion will not apply to allowances wholly or partly for private expenditure of the employee (such as a cost of living, utilities or rent allowance).

Paragraph (d) includes two types of amounts in employment income. First, employment income includes the amount of any liability incurred by an employee that is discharged by the employee's employer. In this case, the legal liability for the expenditure rests with the employee, but the expenditure is paid directly by the employer. For example, an employee may incur a liability to pay school fees in relation to his or her child and the employee's employer may pay the fees direct to the school. In this case, the amount of the fees paid by the employer is treated as employment income of the employee.

Secondly, employment income includes any expenditure incurred and paid by an employee that is reimbursed by the employee's employer. A reimbursement differs from an allowance in that the employee must vouch the amount of the expenditure incurred and the amount paid to the employee does not exceed the actual amount expended by the employee.

There is an exception from inclusion in paragraph (d) for any expenditure incurred by an employee on behalf of the employee's employer wholly and exclusively in the performance of the employee's duties of employment. For example, an employer may reimburse an employee for the cost of a hotel. If the employee incurred the hotel expenditure while travelling solely for the purposes of employment, the amount of the reimbursement is not employment income.

Paragraph (e) includes certain amounts relating to the employee's conditions of employment. Sub-paragraph (i) includes any consideration for a person's agreement to enter into an employment relationship. This covers any inducement, such as a signing-on fee.

Sub-paragraph (ii) includes any consideration for an employee's agreement to any conditions of employment or an employee's agreement to any change in his or her

conditions of employment. For example, an employee may be paid a lump sum amount as consideration for giving up a benefit of employment under the employee's conditions of employment. Another example is an amount paid to an employee for his or her agreement to a condition to work for the employer exclusively for a specified period (also referred to as a "golden handcuff" payment).

Sub-paragraph (iii) includes any consideration for an employee's agreement to a restrictive covenant in respect of any past, present or prospective employment. This would cover, for example, an amount paid by an employer to an employee on termination of employment as consideration for the employee agreeing not to set up a competing business for a specified number of years after termination or within a specified geographical area.

Paragraph (f) includes any amount received on termination of employment. An amount is included under this paragraph regardless of whether it is paid voluntarily by the employer or under the terms of the employee's employment contract. The paragraph expressly includes any amount received as compensation for redundancy or loss of employment, such as a severance payment or golden handshake. A special tax rate applies to a termination payment under subsection (3).

Paragraph (g) includes any pension or annuity, and any supplement to a pension or annuity provided that the pension or annuity is received in relation to employment.

Subsection (2) specifies three amounts that are not included in an employee's gains or profits from employment. Subsection (2) is effectively a re-enactment of section 5(1)(b)(i) and (ii) of the current law. Paragraph (a) provides that the cost of passages paid by an employer for passage by an employee is not included in the employee's gains or profits from employment. This relates both to passage within the Solomon Islands and passage between the Solomon Islands and a foreign country.

Paragraph (b) provides that the cost of medical services paid by an employer for the benefit of an employee is not included in the employee's gains or profits from employment.

Paragraph (c) provides that any contribution made by an employer for the benefit of an employee to an approved pension fund or the Solomon Islands National Provident Fund is not included in the employee's gains or profits from employment. However, a ceiling is set on the non-taxable amount. The amount of the exclusion is not to exceed 15% of the employee's total employment income for the year. "Employment income" is defined in the amended section 2 of the Act to mean the gains or profits from employment as determined under the new section 5. Any contribution made in excess of this amount is treated as employment income.

Subsection (3) provides for concessional treatment of termination payments included in employment income under section 5(1)(f). The termination payment may have accrued over a period of years but, in absence of subsection (3), would be taxed in whole in the pay period in which it was paid. This may result in the employee being subject to a higher marginal rate of tax on the payment than would be the case if the payment was taxed as it accrued. To provide relief in this case, subsection (3) provides that the termination payment is subject to an average rate of tax rather than normal marginal rates. The average rate is based on the total tax paid by the employee on employment income in the current year prior to termination of employment and the previous 2 tax years as a percentage of total employment income paid by the terminating employer during this period. If the employee has been employed by the terminating employer for a lesser period, the average rate is based on that lesser period.

Subsection (4) provides a source rule for employment income. The gains or profits from any employment exercised in the Solomon Islands are treated as Solomon Islands-source income. This is the case regardless of the place of payment. Subsection (3) is a re-enactment of section 5(2) of the current law.

6. Amendment to section 6

This section amends section 6, which explains the meaning of gains or profits from any right granted for the use of possession of any property for the purposes of section 3(1)(a)(iii). The amendment changes the cross reference to “section 3(1)(a)(iii)” consequent upon the redrafting of section 3.

7. Amendment to section 7

This section amends section 7, which explains the meaning of dividends and provides a source rule for interest. The amendment changes the cross reference to “section 3” consequent upon the redrafting of section 3. This is because, after section 3 is redrafted, only section 7(a) is relevant to section 3(1)(b); section 7(b) is a source rule and is relevant to new section 3(2).

8. Amendment to section 18

This section amends section 18 of the Act, which provides for the allowance of deductions in the computation of the income of a taxpayer for a year.

The Bill amends section 18 by deleting subsection (5), which provides a resident individual with a deduction for the cost of certain passages. This is part of the measures introduced by the Bill to make deduction of tax from employment income a final tax on the income. It is not administratively feasible under a final deduction system to require employers to make judgements about whether particular expenditures incurred by employees are deductible in determining the amount of tax to be deducted from employment income. Thus, under the Bill, employees are denied a deduction for all expenditures (whether work related or otherwise).

9. Amendment to section 20

This section amends section 20 of the Act, which specifies expenditures for which no deduction is allowed under the Act.

Paragraphs (a) adds new paragraph (i), which denies a deduction for any expenditure incurred in deriving employment income. "Employment income" is defined in section 2 to mean gains or profits from employment as determined under section 5.

As discussed above in relation to the amendment to section 18, this amendment is necessary to facilitate the making of deduction of tax from employment income a final tax on the income.

Paragraph (b) inserts a new subsection (2A), which applies to persons required to deduct tax from a payment made. Subsection (2A) will apply if two conditions are satisfied -

- (1) The first condition is that a person is required to deduct tax under a tax deduction provision. By virtue of the definition in section 2, the following are tax deduction provisions: sections 36, 36A, 36B, 37 and 38.
- (2) The second condition is that the person would, in the absence of subsection (2A), be allowed a deduction for the payment from which tax has been deducted. In broad terms, this means that the expenditure has been incurred wholly and exclusively in the production of income charged to tax (section 18) and is not otherwise denied a deduction under section 20. This condition means, for example, that subsection (2A) will not apply to dividends as they are not a deductible expenditure.

If these conditions are satisfied, the person making the payment is denied a deduction for the payment until the tax required to be deducted from the payment has been paid to the Commissioner.

10. Amendment to section 28

This section amends section 28 of the Act, which provides resident individuals with a personal exemption of \$7,800.

The Bill amends subsection (1) by extending the personal exemption to all individuals regardless of whether they are resident or non-resident.

The Bill makes a consequential amendment to subsection (2) so that it also applies to a non-resident individual. Under current law, subsection (2) provides for the pro-rata allowance of the personal exemption for an individual who has become a resident individual for the purposes of employment or the carrying on of a business in the

Solomon Islands. This will be primarily relevant to the first and last years of an assignment in the Solomon Islands. The Bill applies the pro-rata rule also to non-resident individuals. The pro-rata is based on the number of days present in the Solomon Islands during the year as a percentage of the total number of days in the year. Thus, if an expatriate posted to the Solomon Islands for work arrives in the Solomon Islands on April 1 in a non-leap year, the amount of personal exemption allowed for the year is \$5877 ($\$7,800 \times 275/365$).

11. Repeal of section 29

This section repeals section 29, which provides an individual with a personal exemption of \$7,800. The section duplicates section 28 and, therefore, is repealed.

12. Insertion of new sections 36, 36A and 36B

This section deletes section 36 of the Act and inserts a new section 36, and sections 36A and 36B.

36. Deduction of tax from dividends

Section 36 of the provides for the deduction of tax from dividends. It has been deleted and replaced by a new section 36, which also provides for the deduction of tax from dividends. The substitution of a new section 36 is a simplification measure consequent upon the making of the tax deducted a final tax on certain classes of income. However, the rate of withholding from a “resident body of persons, other than a corporation”, has been increased to the corporate rate of tax. This has been done to overcome a loophole in the law that provides an inequitable advantage to a company that pays dividends to a body of persons (trusts, partnerships etc) rather than corporate or individual shareholders.

Subsections (1) and (2) effectively re-enact subsection (1) of the former section 36 other than the change of rate for body of persons from 20% to 30%. The obligation to deduct tax is set out in new subsection (1). It arises if a resident company pays a dividend. A resident company is a company that is resident in the Solomon Islands under paragraph (b) of the definition of “resident in Solomon Islands” in section 2. The Bill includes a definition of “paid” in section 2, which covers, inter alia., a distribution and a crediting of accounts. “Dividend” is defined in section 2.

If an obligation to deduct tax arises under subsection (1), the resident company must deduct tax from the gross amount of the dividend. The rate of deduction generally depends on the residence of the shareholder. For resident shareholders (but not including a body of persons, other than a company), tax must be deducted at the rate of 20% of the gross dividend. A resident shareholder is a shareholder who comes within the definition of “resident in Solomon Islands” in section 2. For non-resident shareholders (i.e, any shareholder who is not within the section 2 definition of “resident in Solomon Islands”) and a resident body of persons other than a company,

tax must be deducted at the rate specified in section 33(1) of the Act (i.e, 30% of the gross amount of the dividend). The rates are the same as under the former section 36.

Subsection (2) provides that the obligation to deduct tax in section 36(1) does not apply if the dividend is exempt from tax.

Subsection (2)-(6) of the current section 36 have not been reproduced in the new section 36 as the rules contained in those subsection have been re-included in the Act as rules of general application to all tax deduction provisions. The following table cross references to the new provisions -

Current Act	Bill
Section 36(2)	Section 36D
Section 36(3)	Section 36A
Section 36(4)	Section 38B and 38C
Section 36(5)	Section 40A
Section 36(6)	Section 2, definition of "paid"

Section 13 of the Bill also inserts new sections 36A and 36B. Section 36A provides for the deduction of tax from employment income and section 36B provides for the deduction of tax from interest paid to residents.

36A. Deduction of tax from employment income

Section 36A(1) obliges an employer to deduct tax from the gross amount of employment income paid to an employee. The rate of deduction is determined under the *Tax Deduction Rules 2005*. The Bill inserts definitions of "employer", "employee", "employment income" and "paid" into section 2 of the Act. "Employer" is defined as any person who engages or remunerates an employee. "Employee" is defined as an individual engaged in employment. A definition of "employment" has also been inserted into section 2 by the Bill. It includes employment within the ordinary meaning of the term and the holding of an office (such as a directorship). "Employment income" is defined to mean gains or profits from employment as determined under the new section 5 of the Act. "Paid" is defined inclusively so that it otherwise has its ordinary meaning, which would cover an actual payment. The definition also includes *inter alia*, the application of salary or wages on behalf of an employee. This would cover, for example, an employee who directs that part of his or her salary is paid direct to his or her spouse or a creditor.

Subsection (2) provides that the obligation to deduct tax in section 36A(1) does not apply if the employment income is exempt from tax.

Subsection (3) maintains an employer's obligation to deduct tax even though the employer may be obliged to deduct other amounts from employment income payable to an employee. For example, a creditor of an employee may have obtained a garnishee order requiring the employer to deduct regularly an amount from the

employee's salary and forward it to the creditor to be credited against the amount owed to the creditor. The effect of subsection (3) is to require the employer to deduct tax on the entire salary, including the part that is deducted for the benefit of the creditor. The subsection also gives priority to the Act over other laws that may prevent attachment or withholding of employment income. Subsection (3) is necessary as the deduction of tax from employment income will be a final tax on the income (see new section 40A).

36B. Deduction of tax from interest

Section 36B(1) obliges a resident person or Solomon Islands permanent establishment of a non-resident person to deduct tax from the gross amount of interest paid to a resident person at the rate of 10%. The Bill includes a broad definition of "interest" in section 2.

The obligation to deduct tax from interest is imposed on a resident person. A person is a resident person if the person is "resident in Solomon Islands" as defined in section 2. This includes a resident individual (other than if section 36B(2)(c) applies) and a resident body of persons. "Body of persons" is defined in section 2. The definition expressly excludes a partnership. To ensure that interest paid by a partnership is covered, section 36B(3) provides that, for the purposes of this section, resident person includes a resident partnership. A partnership is a resident partnership if at least one of the partners in the partnership is a resident person.

The obligation to deduct tax from interest is also imposed on a Solomon Islands permanent establishment of a non-resident person. Any person who is not a resident person is a non-resident person. Again to ensure that partnerships are covered, the definition of "non-resident person" in section 38(3) includes a non-resident partnership. A partnership is a non-resident partnership if all the partners in the partnership are non-resident persons. Subsection (3) provides that the definition of "permanent establishment" in section 38(2) applies for the purposes of section 36B. This means, for example, that the section 36B obligation to deduct tax applies to a Solomon Islands branch of a non-resident bank.

Section 36B applies only to interest paid to a resident person. Any interest paid to a non-resident person is subject to deduction of tax under section 38.

Subsection (2) specifies three cases when the obligation to deduct tax in section 36B(1) does not apply. First, it does not apply if the interest income is exempt from tax in the hands of the recipient. Secondly, it does not apply if the recipient of the interest is a financial institution. Thirdly, it does not apply if the interest is paid by an individual who is not carrying on a business.

13. Amendment to section 37

This section amends section 37, which provides for the deduction of tax from certain amounts paid to residents.

Paragraph (a) amends subsection (2) by including new paragraph (h), which refers to income from stevedoring services. This is a technical correction to ensure that section 37 properly co-ordinates with the Seventh Schedule. Paragraph (c) includes a definition of “income from stevedoring service” in subsection (7).

Paragraph (a) also amends subsection (2) by including new paragraph (i), which provides the Minister with a general authority to include any other income or class of income within the operation of the withholding tax regime from residents.

Paragraph (b) deletes subsection (3)-(6). This is because the rules contained in those subsections have been re-included in the Act as rules of general application to all tax deduction provisions. The following table cross references to the new provisions -

Current Act	Bill
Section 37(3)	Section 38D
Section 37(4)	Section 38A
Section 37(5)	Section 38B and 38C
Section 36(6)	Section 40B

14. Amendment to section 38

This section amends section 38, which provides for the deduction of tax from certain amounts paid to non-residents.

Paragraph (a) amends subsection (2) in two respects. First, it deletes the definition of “interest” in subsection (2). This is consequent upon the inclusion of a definition of interest in section 2 of the Act. Secondly, it changes the definition of “management services” to a definition of “income from management services”. This ensures consistency with the terms of the definition. It also amends paragraph (i) of what is now the definition of “income from management services” so that it excludes “employment income”. This is consequent upon the use of the of employment income to describe the amounts subject to wage withholding. A similar amendment has been made to the definition of “professional services”.

Paragraph (b) amends subsection (3) by including new paragraph (i), which refers to income from management services. This is a technical correction to ensure that section 38 properly co-ordinates with the Sixth Schedule.

Paragraph (b) also amends subsection (3) by including a new paragraph (i), which provides the Minister with a general authority to include any other income or class of income within the operation of the withholding tax regime for non-residents.

Paragraph (c) amends section 38 by deleting subsections (4)-(6). This is because the rules contained in those subsections have been re-included in the Act as rules of general application to all tax deduction provisions. The following table cross references to the new provisions -

Current Act	Bill
Section 38(4)	Section 38D
Section 38(5)	Section 38A
Section 38(6)	Section 38B and 38C

15. Insertion of new sections 38A-38J

This section inserts new sections 38A-38J, which provide for administrative matters relating to the deduction of tax under a tax deduction provision, namely sections 36, 36A, 36B, 37 and 38.

38A. Payment of tax deducted

This section requires a person who has made a payment that is subject to a tax deduction provision to remit the deduction tax to the Commissioner within fifteen days after the end of the month in which the person was required to deduct the tax. The same remission date applies for the purposes of all tax deduction provisions.

By virtue of section 38J, tax that is required to be deducted under a tax deduction provision is treated as "tax" for the purposes of a number of sections relating to the recovery of tax and imposition of late payment penalty. Thus, for example, the late payment of the deducted tax to the Commissioner may give rise to a penalty under section 84.

38B. Failure to pay tax deducted

This section applies if tax that is required to be deducted under a tax deduction provision is not remitted to the Commissioner.

Subsection (1) applies to two classes of case. First, it applies if a person required to deduct tax under a tax deduction provision fails to do so. Secondly, it applies if a person deducts the tax but fails to remit it to the Commissioner as required under section 38A. In each case, the person required to deduct the tax is personally liable to pay the tax to the Commissioner. The person may also be personally liable for additional tax under section 70 and late payment penalty under section 84.

Subsection (2) provides a person liable under subsection (1) with a legal entitlement (i.e., a cause of action) to recover the tax from the recipient of income if the person has failed to deduct the tax. The right to recover does not extend to any additional tax or penalty imposed as a result of the late payment of the deducted tax.

38C. Recovery of tax from recipient

This section allows the Commissioner to collect tax from the recipient of a payment if the person that was required to deduct the tax failed to do so. However, the tax cannot

be recovered twice - it may be collected from the person who was required to deduct it or the recipient of the income or partly from each, but the total collected may not exceed the tax that should have been deducted.

Subsection (2) makes it clear that, if the Commissioner recovers the tax from the recipient, the person who failed to deduct it is still liable in respect of the failure. For example, such person may be liable under section 84 for penalty accruing as a result of the late payment of the tax.

38D. Evidence of tax deduction

This section obliges a person who deducted tax under section 36, 36A, 36B, 37 or 38 to provide the recipient of the payment with written evidence that tax has been deducted. The legislation does not prescribe any particular form that the evidence should take, although normally it would be expected that the deduction would be noted on the pay slip given to the employee.

38E. Priority of tax deducted

This section provides for a priority in favour of the Solomon Islands Government for any tax deducted under a tax deduction provision (i.e., section 36, 36A, 36B, 37, or 38).

Subsection (1)(a) provides that any deducted tax is held in trust for the Solomon Islands Government. Subsection (1)(b) prevents any deducted tax from being attached by any other person, meaning that another person cannot claim it in satisfaction of a debt owed to that other person.

Subsection (2) provides that, in the event of the death, liquidation or bankruptcy of a person deducting tax, any tax deducted does not form part of the person's estate. This means that the tax does not form part of the assets available for distribution to beneficiaries, creditors or owners of the deceased or bankrupt person.

Subsection (3) confirms that the deducted tax takes priority over any other charge that may be required to be made on income under another law or Court order.

38F. Indemnity

This section provides that a person who has deducted tax under a tax deduction provision and remitted the tax to the Commissioner is protected from claims by the recipient of the payment. In effect, it treats the recipient as having received the gross amount of the payment (i.e., without deduction of the tax).

38G. Annual tax deduction certificate

This section obliges a person who is required to deduct tax under section 36, 36A, 36B, 37 or 38 to furnish the recipient with an annual tax deduction certificate. The certificate must be furnished in the form and manner prescribed in the Tax Deduction Rules 2005.

Subsection (2) obliges the recipient to attach the certificate to his or her return of income for the year to which the certificate relates, but only if the income to which the certificate relates is not subject to section 40A (i.e., the deducted tax is not a final tax).

38H. Monthly summary

This section obliges a person who is required to deduct tax under section 36, 36A, 36B, 37 or 38 to furnish to the Commissioner a monthly summary of tax deducted for a year. The summary must be furnished in the form and manner prescribed in rule 11 of the Tax Deduction Rules 2005.

38J. Deducted tax treated as tax

This section treats are deducted under a tax deduction provision as “tax” for the purposes of several procedural provisions in the Act. The provisions are -

- Section 83(4) - this provides the Commissioner with discretion to extend the time for payment of tax or to permit tax to be paid by installments. The effect of section 38J is that the discretion applies also to tax deducted under sections 36, 36A, 36B, 37 and 38 that is due under section 38A.
- Section 84 - this provides for the imposition of penalty for late payment of tax. The effect of section 38J is that the late payment penalty applies also to tax deducted under section 36, 36A, 36B, 37 and 38 that is not paid by the due date set out in section 38A.
- Section 85 - this empowers the Commissioner to appoint a person to be the agent of a defaulting taxpayer. The effect of section 38J is that section 85 can also be used to recover tax owing by a person who has failed to pay tax required to be deducted under section 36, 36A, 36B, 37 and 38.
- Section 87 - this provides for a special collection mechanism if the Commissioner believes a person may default in the payment of tax, including a person who may depart the Solomon Islands without paying tax. The effect of section 38J is that section 87 can apply also in respect of tax deducted under sections 36, 36A, 36B, 37 and 38.
- Section 88 - this provides for the collection of unpaid tax by suit. The effect of section 38J is that section 88 can apply also to unpaid amounts required to be deducted under sections 36, 36A, 36B, 37 and 38.
- Section 89 - this provides for the collection of unpaid tax by distraint. The effect of section 38J is that the distress procedure can be used also to recover unpaid amounts required to be deducted under sections 36, 36A, 36B, 37 and 38.
- Section 89A - this provides the Commissioner with a broad power to recover unpaid tax that has not been recovered under the other provisions of the Act. The effect of section 38J is that this power may be used to recover unpaid amounts required to be deducted under sections 36, 36A, 36B, 37 and 38.

16. Insertion of new sections 40 and 40A

This section deletes the existing section 40 and substitutes new sections 40 and 40A.

40. Set-off of tax deducted

This section provides for the set-off of tax deducted under a tax deduction provision.

If tax has been deducted from a payment under section 36, 36A, 36B, 37 or 38, subsection (1) provides that the amount included in the recipient's income is the gross amount (i.e., the amount before the deduction of tax).

Subsection (2) provides that the recipient of income from which tax has been deducted is entitled to set off the deducted tax against the tax charged on the income, if the amount of tax deducted exceeds the tax charged on the income, the excess is dealt with under section 90.

Subsection (3) provides that no set off is allowed in two classes of case. First, no set off is allowed if, under section 40A, the deducted tax is a final tax on the income from which it has been deducted. Secondly, no set off is allowed if the recipient of the payment(s) does not include an annual tax deduction certificate in support of the set off claim.

40A. Deduction tax as a final tax

This section treats the tax deducted under a tax deduction provision for certain classes of income as a final tax on the income from which tax has been deducted. This section applies only if the correct amount of tax has been deducted from the relevant payment.

Subsection (1) specifies the cases in which the deduction of tax is a final tax, namely -

- Tax deducted from dividends under section 36, other than dividends paid to a company.
- Tax deducted from employment income under section 36A.
- Tax deducted from interest under section 36A if the interest is paid by a financial institution to a resident individual.
- Tax deducted from a payment to a resident person covered by section 37 if the payment is -
 - made to a residential body of person (as defined in section 2), other than a company;
 - made to a resident individual when the total income of the individual for the year (including payments covered by section 37) is less than \$10,000; or
 - income from the issue of property referred to section 37(2)(d) derived by a resident individual.

Subsection (1) is expressed to be subject to subsection (2), which excludes the application of the section in two classes of case. First, the tax deducted from dividends, director's fees or interest is not a final tax on the income if the total amount of such income derived by the recipient for the year is more than \$10,000. Secondly, the tax deducted from employment income (including director's fees) is not a final tax if the income has been derived by an employee who, at any time during a year, has three or more employments at the same time and the total employment income derived for the year is more than \$60,000.

Thus, for a person deriving director's fees, there are two bases upon which section 40A may not apply. First, the total amount of director's fees, dividends and interest derived by a director for a year is more than \$10,000. This is the case even if the directorship is the employee's only employment for the year. Secondly, director has three or more employments at the same time and the total employment income for the year is more than \$60,000.

Subsection (3) provides for the treatment of deducted tax as a final tax on these classes of income. Paragraph (a)-(c) provide for a number of mechanical provisions to give effect to this.

Paragraph (a) provides that the income to which the section applies is not included in the total income of the recipient. Thus, the amount is not taxed on an ordinary assessment basis.

Paragraph (b) provides that no deduction is allowed for any expenditure incurred in deriving the income to which the section applies. This means that any such expenditure incurred is not deductible in computing the income of the person chargeable to tax.

Paragraph (c) applies to a person whose only income for a year is income for a year is income covered by subsection (1). Such a person is not to furnish a return of income under section 57 for the year. The explicit reference to section 57 ensures that the terms of the new section 40A override the obligation to file a return that would otherwise apply.

17. Repeal of section 43

This section provides for the repeal of section 43 of the Act. This is a simplification measure as part of the amendments to make the tax deducted by an employer from employment income a final tax on the income.

18. Amendment to section 57

This section amends section 57 of the Act, which provides for the lodging of income tax returns.

Subsection (1) is amended by inserting the words "deriving income" before "chargeable". The effect of the amendment is that the obligation to lodge a return falls on any person deriving income chargeable to tax. This means that

every person deriving an amount of income has an obligation to lodge a return. This is the case even if the person has made a loss for the year. The only exceptions to the obligation to lodge a return are those provided in the Act, such as under section 40A(3)(c) inserted by the Bill.

19. Amendment to section 58

This section amends section 58 of the Act, which provides for the imposition of penalty in respect of the failure to lodge a return or other documentation required under the Act.

Paragraph (a) amends subsection (1) in two respects. First, it deletes the reference in subsection (1)(c) to the documents required to be lodged under Tax Deduction Rules 1981 and substitutes a reference to the documents required to be lodged under the Tax Deduction Rules 2005. Secondly, it provides for the automatic imposition of penalty for the default rather than providing the Commissioner with discretion to impose penalty (as is the case under current section 58(1)(i)). There is imposed a flat penalty of \$500 for each default and a monthly penalty of \$50 for each month or part month the default continues.

Paragraph (b) deletes subsection (2) and substitutes a new subsection (2), which empowers the Commissioner to require a person in default under subsection (1) to lodge the outstanding return, certificate or summary. This is a re-enactment of current section 58(1)(ii), which was deleted by paragraph (a) of the amendment in section 20 of the Bill. Importantly, the \$50 monthly penalty applies regardless of whether the Commissioner serves a notice under subsection (2).

20. Repeal of sections 59 and 60

This section repeals sections 59 and 60 of the Act. The substance of section 58 is now covered by section 38H of the Act and Rules 10 and 11 of the Tax Deduction Rules 2005. The substance of section 60 is now covered by section 58(1)(c).

21. Amendment to section 63

This section amends section 63 of the Act, which provides the Commissioner with investigations powers.

A new subsection (4) has been inserted allowing the Commissioner to have a police officer present when exercising powers under the section.

22. Repeal of sections 64, 65, and 66

This section repeals sections 64, 65 and 66. The substance of these sections is now covered by section 38H of the Act and Rules 10 and 11 of the Tax Deduction Rules 2005.

23. Amendment to section 70

This section substitutes a new section 70(1) of Act, which provides for the imposition of additional tax if a person fails to deduct tax as required under a tax deduction provision. The change is a technical change to accommodate the new tax deduction provisions, there is no change in substance to the current law.

24. Amendment to section 90

This section amends section 90 of the Act, which provides for the refund of overpaid tax. Subsection (1) has been amended so that it applies to overpayments of tax deducted at source in all cases and not just on an assessment.

25. Amendment to section 96

This section amends section 96 of the Act, which provides an offence for failing to furnish any notice or return required under the Act, or failing to keep proper records.

The existing section is renumbered subsection (1). A reference to the Tax Deduction Rules has been included in paragraph (a) so that it applies also to annual tax deduction certificates and monthly summaries.

A new subsection (2) is inserted that empowers the Court to serve a notice on a person who is guilty of an offence under subsection (1)(a) or (b) requiring the person to furnish the relevant document or return within the time specified by the Court. A person who fails to do so is guilty of contempt of court.

26. Amendment to Sixth Schedule

This section makes a technical amendment to paragraph (xiv) of the Sixth Schedule by inserting the words “income from” before “management services”. This ensures that the Schedule properly co-ordinates with section 38.

27. Amendment to Seventh Schedule

This section makes a technical amendment to paragraph (viii) of the Seventh Schedule by inserting the words “income from” before “stevedoring services”. This ensures that the Schedule properly co-ordinates with section 37.