

Palau Marine Indus. Corp. v. ROP, 15 ROP 103 (2008)
PALAU MARINE INDUSTRIES CORP.,
Appellant,

v.

REPUBLIC OF PALAU,
Appellee.

CIVIL APPEAL NO. 07-037
Civil Action No. 06-205

Supreme Court, Appellate Division
Republic of Palau

Decided: May 19, 2008¹

Counsel for Appellant: Johnson Toribiong

Counsel for Appellee: David Fifer

BEFORE: ARTHUR NGIRAKLSONG, Chief **1104** Justice; LOURDES F. MATERNE, Associate Justice; C. QUAY POLLOI, Associate Justice Pro Tem.

Appeal from the Trial Division, the Honorable KATHLEEN M. SALII, Associate Justice, presiding.

MATERNE, Justice:

This case presents the question whether “Gross Revenue” as defined by 40 PNC § 1002(o) includes money repaid to Appellant Palau Marine Industries Corporation (PMIC) by independent fishing vessels following the offload and sale of the vessels’ catch, or whether such money is a “refund” as defined by 40 PNC § 1002(o)(1) and therefore excludable from the calculation of Gross Revenue. The trial court held for the Republic of Palau (ROP) and entered judgment for \$644,654.71 in principal, \$1,211,145.50 in interest, and \$4,037,484.57 in penalties. Appellant challenges only the ultimate question of tax liability and does not challenge the large amounts of penalty and interest on appeal.

BACKGROUND

Under the Uniform Longlining Agreement (ULA) between PMIC and the ROP, PMIC procures for independent fishing vessels multiple fishing licenses to fish within the Exclusive Economic Zone (EEZ). PMIC pays a fee to the ROP and applies for a fishing permit, providing the ROP with “a charter, agreement, contract, or other document evidencing the existence of the

¹ Upon reviewing the briefs and the record, the panel finds this case appropriate for submission without oral argument pursuant to ROP R. App. P. 34(a).

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legal relationship between [PMIC] and the fishing vessel owner(s) for whom [PMIC] is applying for the fishing permit(s).” ULA Section 3.3. The ULA also provides that “[i]f the permit is cancelled or suspended after issuance, there shall be no refund or pro-rata refund of the permit fee. If a permit is cancelled by [PMIC] within fifteen (15) days of issuance and the fishing vessel has not yet conducted any fishing activities pursuant to the permit, [PMIC] will be allowed to apply the permit to another permit application, if that application is made within another 3 months.” ULA Section 3.4. PMIC “shall serve as the agent for the licensed vessel” (ULA Section 5.1); “shall ensure that its fishing vessels do not fish in the waters of Palau without first obtaining permits” (ULA Section 5.3); and “shall ensure that all its permitted fishing vessels are registered with the . . . Forum Fisheries Agency.” (ULA Section 5.4).

Section 13 of the ULA is entitled “Purchase of Provisions” and provides: “The Company shall not provision vessels that are not permitted to fish in Palau’s waters. Permitted fishing vessels . . . shall purchase all of their provisions, including fish bait, food, packaging materials, fishing gear, or equipment, spare parts, water, electrical power, and fuel from sources in the Republic of Palau unless such goods or services are not reasonably available from such sources.” Through separate agreements with the independent vessels, PMIC supplies the independent fishing vessels with ice, fuel, bait, and other necessities for fishing expeditions and collects the fish from the vessels for shipment to Japan. One such separate agreement between PMIC and an independent fishing vessel that was introduced at trial provided: “Eighty five per cent (85%) of the total Japan auction sales will be remitted to PMIC for the partial offset of [independent vessel]’s payables. If there should be any outstanding balance, [the independent vessel] shall remit the balance within one week. **L105** The balance of the eighty five (85%) less the one percent (1%) service fee due to PMIC after deducting all its outstanding account shall be deposited to the account of [the independent vessel].” Pl.’s Ex. 5, Section IV. Another such agreement between PMIC and an independent vessel contains similar provisions. Pl.’s Ex. 6, Sections II and III.

An audit of PMIC’s books and records conducted by the Office of Revenue and Taxation revealed that PMIC was not paying taxes on what PMIC was calling “Monies Held in Trust” (MHIT). PMIC explained to the auditors that “this column’s contents are the actual expenses for all the vessels PMIC spends its own money by supplying the vessels, and, in return get[s] commissions from the proceeds of sales MHIT are the actual expenses that included things like fuel, ice, food, and other necessary supplies that the vessels need when they go out fishing, and the money collected will go directly to the vendors, e.g. Shell.” Pl.’s Ex. 1 at 2-3.

The auditors concluded that the MHIT was Gross Revenue as contemplated by the Unified Tax Act (40 PNC § 1001 *et seq.*) and the ROP sued to collect past due taxes, interest, and penalties. The trial court agreed with the auditors, holding that “PMIC expends monies to provision the fishing vessels . . . PMIC is in the business of providing these services, it receives revenue therefore, and Palau’s tax code requires PMIC to pay taxes on said revenue.” Tr. Ct. Decision at 5-6.

STANDARD OF REVIEW

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Factual findings of the trial court are reviewed for clear error. *Temaungil v. Ulechong*, 9 ROP 31, 33 (2001). The Appellate Division reviews the lower court's conclusions of law, including its interpretation of a statute, *de novo*. *Wenty v. ROP*, 8 ROP Intrm. 188, 189 (2000). There are no factual questions at issue here, and we review the legal issue *de novo*.

DISCUSSION

Appellant bases his sole argument on appeal on 40 PNC § 1002(o)(1), which provides that “refunds, rebates, and returns” are not included in Gross Revenue for the purposes of the Uniform Tax Act. Appellant renews his argument made below that PMIC purchases fuel and other supplies for the independent vessels as a convenience to the vessels and not as a service or as part of PMIC's business relationship with the independent vessels. PMIC argues that the independent vessels cannot obtain credit from sources within Palau – necessary because the vessels often do not have money to pay for fuel and other supplies before embarking on fishing expeditions – because of the transient and international nature of the fishing industry. By purchasing these provisions for the independent fishing vessels PMIC merely advances payment to the vessels for these supplies. As such, when the independent vessels pay PMIC for these supplies after the vessels have made their money offloading the catch, this money is a “refund” and therefore not taxable as Gross Revenue. Appellant argues that it is unfair for PMIC to be taxed on services and provisions it supplies the independent vessels when it would not be taxed if the independent vessels were to buy their supplies outside of Palau.

There are many flaws in Appellant's theory. First, it seems the obvious intent of the [L106](#) OEK in enacting the “refunds, rebates, and returns” language in § 1002(o)(1) is to exclude what is known as “sales revenue” from calculations of Gross Revenue. Sales Revenue is a term used by retail stores that takes into account the inevitable refunds, rebates, and returns of merchandise that a retail store gives. If one were to buy a keyboard at Ben Franklin and return it that same day for a full refund, Ben Franklin would not include the refunded money as Gross Revenue. The money that PMIC receives from the independent vessels is not a refund or return in this sense and the OEK did not intend to allow such money to be excluded from Gross Revenue.

Second, both the agreement between PMIC and the ROP and the typical agreements between PMIC and the independent vessels contemplate that PMIC will supply the independent vessels with supplies.² Further, ¶ 13.1 of the ULA provides that all of the provisions for the independent vessels *must be purchased in the ROP* unless the provisions are not reasonably available in the ROP. Therefore, the ULA contemplated Appellant's argument that vessels could escape paying taxes on provisions bought in Palau by buying them elsewhere, and expressly mandated that the vessels buy supplies in Palau if reasonably possible. PMIC is licensed to provide the independent vessels not only with fishing permits but also with provisions and supplies. When PMIC supplies these independent fishing vessels with provisions, it is providing a service to the vessels as part of PMIC's contract with the vessels. PMIC acts as an

² “[PMIC] shall provide air transport service and fish handling services, packing materials and offloading, and supply provisions such as ice, water, fuel, lubricants, other needs of the fishing vessels.” PI's. Ex. 6 ¶ I.A.4; PI.'s Ex. 5 ¶ I.A.4; *see also* PMIC and ROP agreement, ¶ 13.1.

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intermediary between the Palauan companies that sell fuel, ice, bait, and other necessary supplies and the foreign fishing vessels that may not have the local knowledge or connections to obtain such supplies. The money PMIC receives from the fishing vessels as payment for the supplies must be considered revenue. Section 1002(0)(1) provides that Gross Revenue constitutes “all receipts . . . without deduction or offset of any nature.” To allow PMIC to deduct or offset its Gross Revenue on the basis of monies received for services rendered would circumvent Palau’s Gross Revenue tax.

Third, Appellant’s Trial Exhibit D, Civil Action No. 181-95, (Tr. Div. 1995), provides support for the inference that prior to 1995 “PMIC owed and paid taxes on the gross revenues generated from its sale of supplies to the fishing boats in Palau.” *Id.* at 2. The most plausible inference is that the Trial Division’s decision in that case led PMIC to reconsider its payment of taxes on the sale of supplies to the independent vessels.

Finally, any argument that Appellant does not profit from selling supplies and provisions to the independent fishing vessels is unavailing. The agreement between PMIC and the independent vessels provides: “Eighty five per cent (85%) of the total Japan auction sales will be remitted to PMIC for the partial offset of [independent vessel]’s payables. *If there should be any outstanding balance, [the independent vessel] shall remit the balance within one week.*” Pl.’s Ex. 5, Section IV (emphasis added). According to the agreement, PMIC will never lose money on supplies that it sells to the **1107** independent vessels. Even if the auction sales from the catch do not pay for the supplies PMIC provides to the vessels, the vessels must still pay the remaining balance. There is no risk to PMIC of losing money by not recouping the money it spent to outfit the fishing vessels. PMIC will, at a minimum, make back the money it spent (including whatever markup PMIC places on the supplies) plus the commission charged to the vessels. In this sense, PMIC does not act like a bank, merely fronting the money and taking the risk that it might not all be paid back upon the offload of the catch. Rather, PMIC provides a service to the independent vessels for which it is duly compensated. This compensation is not a “refund” within the meaning of the Unified Tax Act and should be taxed accordingly as Gross Revenue.

CONCLUSION

The judgment of the Trial Division is affirmed.