IN THE
SUPREME COURT OF THE REPUBLIC OF PALAU
APPELLATE DIVISION

BESURE KANAI,
Appellant,
v.
REPUBLIC OF PALAU,
Appellee.

Cite as: 2016 Palau 25
Civil Appeal No. 15-026
Appeal from Civil Action No. 14-076

Decided: November 23, 2016

Counsel for Appellant .....J. Toribiong
Counsel for Appellee .....L. Wofford

BEFORE: ARTHUR NGIRAKLSONG, Chief Justice
KATHLEEN M. SALII, Associate Justice
LOURDES F. MATERNE, Associate Justice

Appeal from the Trial Division, the Honorable R. Ashby Pate, Associate Justice, presiding.

OPINION

PER CURIAM:

[¶ 1] Besure Kanai appeals the Trial Division's order that he must pay taxes along with accrued penalties and interest on a lump sum lease payment of $1,391,300.90. For the reasons below, we **AFFIRM**.

BACKGROUND

[¶ 2] On December 20, 2007, Kanai leased land in Ngaraard to Palau Resort Developments, Ltd. ("PRD") for a term of 50 years, plus an option to renew for an additional term of 49 years. In return for granting what is, in effect, a 99-year lease, Kanai received a lump sum lease payment of $1,391,300.30 on July 25, 2008. After learning of the sale, the Bureau of Revenue, Customers, and Taxation in the Ministry of Finance ("the Tax Bureau") assessed a 4% gross revenue tax on these proceeds. Kanai did not

pay the tax, nor did he institute any agency or judicial proceedings to challenge the assessment or any of the accruing penalties and interest.

[¶ 3] After years of discussions between the Tax Bureau and Kanai, including at least two informal hearings, the Republic filed this lawsuit against Kanai on June 9, 2014, seeking a judgment requiring Kanai to pay the overdue tax, plus accumulated penalties and interest. On April 8, 2015, the Republic filed a motion for summary judgment. The Trial Division granted this motion on August 19, 2015 after taking testimony and hearing oral arguments, and entered judgment for the Republic in the amount of $547,133.48. This appeal followed.

STANDARD OF REVIEW

[¶ 4] We review Orders granting summary judgment *de novo*, viewing all evidence and inferences in the light most favorable to the non-moving party. *Ngarametal Ass'n v. Ingas*, 17 ROP 122, 124 (2010). The Trial Division's conclusions of law are also reviewed *de novo*. *Rengechel v. Uchelkeiukl Clan*, 16 ROP 155, 158 (2009).

DISCUSSION

[¶ 5] We are asked to determine whether the gross revenue tax provisions of the Unified Tax Act, 40 PNC § 1201 *et seq.*, apply to rental payments for long-term leases. The catch-all provision of the gross revenue tax, 40 PNC § 1204, states that "[e]very person engaging in any business, trade, activity, or calling . . . shall pay a tax of four percent (4%) of the gross revenues of the business, trade, activity, or calling . . . ." The central question in this appeal is whether Kanai "engage[d] in [a] business, trade, activity, or calling" within the meaning of § 1204 by entering into a long-term lease with PRD. The Trial Division held that Kanai's lease transaction was taxable as "business" under the broad definition of 40 PNC § 1002(d), or, in the alternative, that even if it was not a business, the long term lease is at least a taxable "activity" because it is a revenue generating activity carried on for the purpose of economic gain. *ROP v. Kanai*, Civ. Action No. 14-076, at 10-11 (Aug. 21, 2015) ("Trial Decision").

[¶ 6] We hold that a long-term lease of land for money is "commercial activity," defined by 40 PNC § 1002(f) as " any form of activity carried on for the purpose, in whole or in part, of economic gain . . . ." A "commercial activity" is an "activity" covered by 40 PNC § 1204, so rent paid to a landlord pursuant to a long-term lease of land within Palau is subject to the 4% gross revenue tax. Kanai's argument that this tax should not apply because the signing of this long-term lease was an un-taxable "one-time isolated transaction" ignores the fact that a long-term lease is, by definition, a continuous economic relationship between lessor and lessee.

[¶ 7] Kanai also argues that his lease proceeds are exempt from taxation under 40 PNC § 1002(o)(3), which exempts proceeds from the sale of land from the definition of "Gross Revenue," or cannot be taxed under Palau Const. art. XIII § 9, which states that "No tax shall be imposed upon land." We recognize that 40 PNC § 1002(o)(3) provides that the gross revenue tax does not apply to the *sale* of land; and that Article XIII § 9 forbids Palau from imposing a direct tax on the *value* of land. However neither of these provisions prohibits a tax on *revenue* generated by the leasing of land. As such, we affirm the Trial Division's judgment that Kanai must pay $547,133.48, which represents his overdue tax liability along with accumulated penalties and interest.[1]

[¶ 8] In reaching this decision, we need not, and do not, address whether entering into a long-term lease is also "business" under 40 PNC § 1002(d), or whether entering into a long-term lease is "engaging in business" under 40 PNCA § 1501.

I. Kanai engaged in commercial activity taxable under 40 PNC § 1204 when he entered into a long-term lease with PNC.

[¶ 9] Section 1204 levies a 4% gross tax on "gross revenue of the business, trade, activity, or calling," allowing only for the deduction of salaries paid to Palauan citizen employees. The statute defines gross revenue as:

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[1] While Kanai vigorously disputes that he owes any tax on the lease proceeds, he does not contest, and it appears that he has never contested, the Republic's calculation of the amount of taxes, penalties, and interest he owes.

> *the total sums of all receipts from sources within the Republic* whether in the form of cash or property derived from business, from the exploitation of capital whether *in the form of receipts from* the disposition of capital, assets, interest, dividends, royalties, *rentals*, fees, or otherwise, however, such receipts may be labeled without deduction or offset of any kind or nature. Every taxpayer shall be presumed to be dealing on a cash basis.

40 PNC § 1002(o) (emphasis added). Kanai's rental receipts from his 99-year lease of land located within the Republic of Palau are clearly covered by this broad definition.

[¶ 10] Whether these gross revenues are generated by "engaging in any business, trade, activity or calling" under 40 PNC § 1204 is a closer question. There is no statutory definition of "activity," but the statute does define a "commercial activity" as:

> any form of activity *carried on for the purpose*, in whole or in part, *of economic gain*, including, but not limited to manufacturing, processing, hotel keeping, retailing, boardering, selling, transporting, the practice of a profession or trade, the exercise of a skill and the exploitation of personal assets.

40 PNC § 1002(f) (emphasis added). Commercial activities satisfy the "activity" prong of 40 PNC § 1204. Whether or not there are other activities which satisfy this prong but are not "carried on for the purpose of economic gain" has not been briefed by the parties, and is not a question we need address in this case.

[¶ 11] In interpreting the language of 40 PNC § 1002, the Trial Court held that the phrase "carried on" limits the reach of the gross-revenue tax by excluding "isolated and non-continuous activities" because "they are not 'carried on' in any meaningful sense of that term." Trial Decision at 8-9. Kanai essentially agrees with the Trial Court's interpretation of "carried on," but contends that the Court erred by holding that a long-term lease is, by definition, a continuous transaction, which confers certain rights and duties on both lessor and lessee over its term. Trial Decision at 10; Kanai Opening Br. at 12-14. Kanai argues that his "single transaction" should not be

characterized as continuous engagement in a taxable activity, and that "the alleged [gross revenue tax] was being assessed on the rental from the lease he signed; not on subsequent activities that he may engage in." Kanai Opening Br. at 22-23. He also analogizes his situation to a number of United States tax cases, arguing that the gross revenue tax should not apply here because (1) he does not meet the standard of conducting a business set forth in U.S. case law and (2) a sale of property under the circumstances of this case would be taxed in the U.S. at the lower capital gains rate, not as ordinary income. Kanai Opening Br. at 17-22.

[¶ 12] In interpreting 40 PNC § 1002(f), we look first to the plain language of a statute, reading that language "with [its] context" and interpreting terms "according to the common and approved usage of the English language." 1 PNC § 202; *Diaz v. ROP*, 21 ROP 62, 63 (2014). "In ascertaining the plain meaning of the statute, the court must look to the particular statutory language at issue, as well as the language and design of the statute as a whole." *Id.* (quoting *Noah v. ROP*, 11 ROP 227, 233 (2004)). If statutory language is clear and unambiguous we must apply its plain meaning, "which we may discern by consulting both general and legal dictionaries." *Tellames v. Congressional Reapportionment Comm'n*, 8 ROP Intrm. 142, 143 (2000).

[¶ 13] In both general and legal usage, "carrying on" or "engaging in" an activity requires that there be continuous involvement in, or at least repetition of, the activity in question. Webster's Third New International Dictionary defines "carry on" as "to continue one's course or activity." *Webster's Third New Int'l Dictionary* 344 (Merriam-Webster's 1986) (1961). Black's Law Dictionary also defines "carry on" as requiring some degree of continuous involvement: "[t]o conduct, prosecute or continue a particular avocation or business as a continuous operation or permanent occupation. The repetition of acts may be sufficient." *Black's Law Dictionary* 214 (6th ed., 1991). "Engaging in" an activity is synonymous with "carrying on" that activity," Webster's Third New International Dictionary defines "engage in" as "to begin and carry on an enterprise, especially a business or profession." *Webster's Third New Int'l Dictionary* at 751.

[¶ 14] While some form a continuous involvement is required for the gross revenue tax to be imposed, a single long-term lease is sufficiently continuous to meet that requirement. Kanai's argument attempting to portray his long-term lease as a "single transaction" that is distinct from "subsequent activities that he may engage in" ignores the fact that, by that single transaction, he began a contractual relationship with PRD that is intended to carry on for 99 years. The payment he received for this transaction was made in a single lump-sum, but its purpose is to compensate Kanai for permitting PRD's quiet and peaceful possession of the property which Kanai has title to over a 99 year period.

[¶ 15] Kanai's analogies to United States tax law are unpersuasive. There are substantial differences between the Palauan *gross revenue* tax and the United States *income* tax in the scope, structure, and definitions used. Whether Kanai's activity would meet the standard of "carrying on a business" in the United States (such that he would be able to deduct his expenses in calculating his net income) is of minimal relevance in determining whether Kanai's long-term lease is "commercial activity" under Palauan tax law. Similarly, the fact that a *sale of land* in Kanai's circumstances would likely qualify for capital gains treatment under United States tax law has no relevance on whether the *rent* paid to Kanai under the *long-term lease* actually at issue in this case are covered by Palau's gross revenue tax.

II. Kanai's additional arguments are without merit.

[¶ 16] Kanai's makes two additional arguments for why the proceeds of his long-term lease of land are non-taxable. First, he argues that 40 PNC § 1002(o)(3), which exempts "sales of land" from the definition on "gross revenue," should also be construed to exempt proceeds from the "sale of a leasehold interest" in land.[2] Kanai's argument is creative, but meritless. The

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[2] Section 1002(o) states:

> "Gross revenue means the total sums of all receipts from sources within the Republic whether in the form of cash or property derived from business, from the exploitation of capital whether in the form of receipts from the disposition of capital, assets, interest, dividends, royalties, rentals, fees, or otherwise, however, such receipts may be

fact that our case law occasionally discusses a lessee's rights as the "purchase of a leasehold interest,"[3] does not mean that the Olbiil Era Kelulau intended to include the granting of a leasehold estate in the term "sales of land." Rather, an examination of the Palau National Code shows that the Olbiil Era Kelulau uses the phrase "interest in land" when it wishes to refer to a broader categories of rights in land, including easements and leaseholds. *See, e.g.*, 35 PNC § 317 ("[the record] shall state the particular land or interest in land which the national government has acquired" in an eminent domain proceeding); 39 PNC § 502 (requiring contracts to be in writing when they are "for leasing for a longer period than one year from the making thereof, or the sale of any lands, or any interest in lands"); 35 PNC § 1317(b) (addressing transfers of interests in land "when an owner of an interest in land dies").

[¶ 17] Second, Kanai argues that our Constitution's prohibition that "[n]o tax shall be imposed on land" should be interpreted to apply to the sale of leasehold interests in land as well. Palau Const. art. XIII, § 9. Kanai's argument is contrary to both the plain language and the clear intent of this constitutional provision. The term "Land Tax" or "Tax on Land" has a specific legal meaning. Black's Law Dictionary defines the term "Land Tax" as "Property tax. A tax laid upon the legal or beneficial owner of real property, and apportioned upon the assessed value of his land. A tax on land." *Black's Law Dictionary* 879 (6th ed., 1991). The tax assessed upon Kanai's rental proceeds is not a property tax, and therefore is not prohibited by Article XIII, § 9.

[¶ 18] Any doubt as to the meaning of Article XIII, § 9 is dispelled by the standing committee report which explained that its purpose was to prohibit all

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> labeled without deduction or offset of any kind or nature. Every taxpayer shall be presumed to be dealing on a cash basis. "Gross revenue" does not include:
>
> . . .
>
> (3) gross receipts from the sale of bonds or other evidence of indebtedness or stocks, or from the sale of land;"

[3] *Aguon v. Anastacio*, 5 ROP Intrm. 122, 126 (1995).

forms of property tax on real estate. The standing committee stated that this provision was intended "to prohibit the taxation not only of land but also of crops, plants, or trees" and "the ownership of a dwelling house on land." *Standing Committee on Transition Report No. 30*, Palau Constitutional Convention (March 4, 1979).[4] The Committee's concern was that a property tax would destroy traditional ways of life:

> many Belauan citizens who own lands have no financial means of support but depend on the use of their land to provide food and shelter. If taxes could be imposed on land, the Committee felt that many citizens would be forced to sell their land because they could not afford to pay the taxes.

Id. The report goes on to state that this Section:

> does not prohibit the taxation on revenue derived from the land such as revenue from office buildings, apartment buildings, or stores on said land since taxation of such activities would not be a direct tax on the land itself. Also, this Section would not prohibit taxation on profits from the sale of land, crops, plants or trees growing on the land. This report clearly prohibits a direct tax on land, it allows tax on revenues derived from improvements on land or profits from the sale of land, crops, plants, or trees.

Id. Indeed, we have previously stated that a tax on the revenue generated by land is not prohibited by this section because "[t]he land itself is not taxed . . . [i]t is the existence of revenue that triggers the obligation to pay." *Koror State Government v. Republic of Palau*, 3 ROP Intrm. 314, 320 (1993).

[¶ 19] Kanai argues that our statements in *Koror State Government* are *dicta* and asks that we "revisit[], distinguish[], and clarify[]" this decision.

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[4] The "guiding principle of constitutional construction" is to give effect to "the intent of the framers." *House of Delegates v. ROP*, 16 ROP 13, 17 (2008) (quoting *Ngerul v. ROP*, 8 ROP Intrm. 295, 296 (2001)). Palauan courts have often looked to the records and committee reports of the Constitutional Convention "to divine the meaning of constitutional language." *See Palau Chamber of Commerce v. Ucherbelau*, 5 ROP Intrm. 300, 302 (Tr. Div. 1995) (collecting cases).

Kanai Opening Br. at 30. Having reviewed the intent of the framers, we hold that under Article XIII, § 9 a direct tax on the *value* of land is prohibited, but a tax on any *revenue* generated by the sale or leasing of land is permissible. Kanai's contention that his lease proceeds should be shielded from taxation by Article XIII, § 9 because he is "us[ing] his land via the lease in order to generate revenues from the use of land to support himself and his family" is wholly without merit.

CONCLUSION

[¶ 20] The judgment of the Trial Division is accordingly **AFFIRMED**.

SO ORDERED, this 23rd day of November, 2016.