

**IN THE HIGH COURT OF NEW ZEALAND
WELLINGTON REGISTRY**

CIV-2009-485-582

UNDER The Judicature Amendment Act 1972 and
the Tax Administration Act 1994

BETWEEN JILLIAN CLAIRE LARMER
Applicant

AND THE COMMISSIONER OF INLAND
REVENUE
Respondent

Hearing: 19-20 October 2009

Counsel: R P Harley for Applicant
H W Ebersohn and KIS Naik-Leong for Respondent

Judgment: 11 December 2009 at 11.30am

I direct the Registrar to endorse this judgment with a delivery time of 11.30am on the 11th day of December 2009.

RESERVED JUDGMENT OF MACKENZIE J

Introduction

[1] The applicant Ms Larmer has arrears of income tax and GST, which as at 7 July 2008, amounted to \$175,641.68. The arrears are the subject of debt recovery proceedings in the District Court at Wellington.

[2] On 8 July 2008, Ms Larmer made an application to Inland Revenue for financial relief under the serious hardship provisions of the Tax Administration Act 1994 (the Act). She claimed that her serious hardship was the result of significant

financial difficulty that arose because of her inability to meet minimum living expenses according to normal community standards. On 18 August 2008 the Commissioner determined that Ms Larmer did not meet the criteria for serious hardship and declined her application for relief. On 19 August 2008 judicial review proceedings were brought in this Court. At a settlement conference on 23 October 2008 it was agreed that the Commissioner would consider a new application for relief. That was filed on 10 December 2008.

[3] On 18 February 2009, the Commissioner determined that Ms Larmer met the criteria for serious hardship in respect of the income years ended 31 March 2000 to 31 March 2003 inclusive, but did not meet the criteria during the tax years subsequent to 2003. In this proceeding, Ms Larmer seeks judicial review of the decision dismissing the application for relief.

The Legislation

[4] The most relevant provisions of the Act are ss 176, 177, 177A, and 177C, the relevant parts of which provide as follows:

176 Recovery of tax by Commissioner

- (1) The Commissioner must maximise the recovery of outstanding tax from a taxpayer.
- (2) Despite subsection (1), the Commissioner may not recover outstanding tax to the extent that—
 - (a) recovery is an inefficient use of the Commissioner's resources; or
 - (b) recovery would place a taxpayer, being a natural person, in serious hardship.

177 Taxpayer may apply for financial relief

- (1) A taxpayer, or a person on a taxpayer's behalf, applies for financial relief by either—
 - (a) making a claim stating why recovery of outstanding tax would place the taxpayer in serious hardship; or
 - (b) requesting to enter into an instalment arrangement with the Commissioner by telephone or in writing.

- (2) The Commissioner may require a taxpayer, or a person on a taxpayer's behalf, to apply for financial relief under subsection (1)(a) [[by notice]].
- (3) Upon receiving a request, the Commissioner may—
 - (a) accept the taxpayer's request; or
 - (b) seek further information from the taxpayer; or
 - (c) make a counter offer; or
 - (d) decline the taxpayer's request.
- (4) A taxpayer has 20 working days, or a longer period allowed by the Commissioner, to provide the information sought or to respond to a counter offer.
- (5) If the Commissioner receives information or a response from a taxpayer outside the time period allowed under subsection (4), the receipt of the information or the response will be treated as a new request for financial relief.

177A Definition of serious hardship

- (1) In this section and sections 176, 177, 177B and 177C, serious hardship, in relation to a taxpayer, being a natural person,—
 - (a) includes significant financial difficulties that arise because of—
 - (i) the taxpayer's inability to meet minimum living expenses according to normal community standards; or
 - (ii) the cost of medical treatment for an illness or injury of the taxpayer or the taxpayer's dependant; or
 - (iii) a serious illness suffered by the taxpayer or the taxpayer's dependant; or
 - (iv) the cost of education for the taxpayer's dependant; and
 - (b) does not include significant financial difficulties that arise because—
 - (i) the taxpayer is obligated to pay tax; or
 - (ii) the taxpayer may become bankrupt; or
 - (iii) the taxpayer's, or the taxpayer's dependant's, social activities and entertainment may be limited; or

- (iv) the taxpayer is unable to afford goods or services that are expensive or of a high quality or standard according to normal community standards.

177C Write-off of tax by Commissioner

- (1) The Commissioner may write off outstanding tax that cannot be recovered.

Consideration of the hardship application

[5] In considering the taxpayer's application, the Commissioner was required to consider whether recovery of the outstanding tax would place the taxpayer in serious hardship, as defined in s 177A. The relevant issue here was whether, under s 177A(1)(a)(i), the taxpayer had significant financial difficulties arising because of her inability to meet minimum living expenses according to normal community standards. Ms Larmer submitted a statement of financial position and supporting information. The Commissioner obtained additional information from Ms Larmer's banks pursuant to information requests under the Act. Mr Amor, the debt collection officer handling the case within Inland Revenue, prepared a written submission including a recommendation for his area manager, who was a person having delegated authority to decide a hardship application.

[6] In his consideration, Mr Amor applied a household debt expenditure guide prepared by Statistics New Zealand, which Inland Revenue uses to assist in determining minimum living expenses according to normal community standards. The guide specifies different average expenses depending on the type of household and geographical area where the taxpayer resides. Using that guide, Mr Ambrose considered that the minimum living expenses according to normal community standards for a person in Ms Larmer's situation were \$22,978.80 per annum in 2008. He applied that to Ms Larmer's situation for the then current position, and for the year ended 31 March 2008, in the following terms:

In comparison the Taxpayer's total income, so far this tax year, up to and including November 2008, is \$134,757.92 including GST. Net of GST it is \$126,825.44 with four months still to add for an annual total. In her IR590 of August 2008 the Taxpayer states that she takes \$1,000 per week for self employed income. Up until the end of November 2008 she would therefore

have taken \$35,000 for her living expenses. By the end of the 2009 tax year her self employed income will total \$52,000. Income Tax would need to be allowed for in this total but clearly, as was apparent at the Judicial Review Conference of 23rd October 2008; the Taxpayer is not currently in a position of serious hardship as evidenced by the statutory test of section 177 of the Tax Administration Act 1994.

The Taxpayer's recent application for financial relief was received 10/12/2008. It was completed as at the Taxpayer's financial position of 31/03/2008 in line with her Income Tax return of that date. In the 2008 tax year the Taxpayer's total income was \$171,518 including GST. Net of GST her total income was \$162,757.62. After expenses, the Taxpayer had a taxable income of \$30,987.87. Allowing for tax on the taxable income of \$5,937.00 the Taxpayer was left with \$25,050.58 for her living expenses. This amount is still more than the \$22,978.80 per year that the Commissioner considers to be the minimum living expenses according to normal community standards for a person in the Taxpayer's situation. The taxpayer was not in a position of serious hardship on 31/03/2008 as evidenced by the statutory test of section 177 of the Tax Administration Act 1994.

[7] The report then considered the 2001, 2002, and 2003 tax years, by comparing the taxpayer's income to the 2005 household expenditure guide (which was the earliest the Commissioner had) and reached the conclusion that Ms Larmer was in a position of serious hardship for those years. The report then said:

The Taxpayer's total income improves markedly from the 2004 tax year onwards and her net income after tax is more than the minimum living expenses according to normal community standards for a person in the Taxpayer's situation, when compared with the appropriate Household Expenditure Guide, for each year after that.

[8] The recommendation was that the Commissioner write-off tax for the 2001 to 2003 years, but reject the application for serious hardship for the later periods. That recommendation was supported by Mr Amor's team leader, and adopted by Ms Hengeveld the area manager.

The legal principles

[9] It is first necessary to consider the extent to which the exercise of the Commissioner's powers may properly be the subject of judicial review. That is an issue which I addressed at some length in *W v Commissioner Inland Revenue* (2005) 22 NZTC 19,602. It is unnecessary for me to repeat what I said there, in particular in paragraphs [15] to [26]. For the reasons there given I consider that this is a case

where judicial review, to ensure the correct application by the Commissioner of the statutory test, is potentially available.

[10] It is however desirable to emphasise that what is available is judicial review, not an appeal on the merits. It is necessary for the applicant to establish that the Commissioner has failed to properly apply the relevant administrative law principles in reaching the decision, before an application for judicial review can succeed. Particulars of the respects in which it is contended that the Commissioner has not properly applied administrative law principles must be fully pleaded, with sufficient particularity to enable both the Commissioner and the Court to properly evaluate the contention. Here, the pleadings are sparse. The grounds on which the applicant seeks relief are set out in paragraphs 6 and 7 of the application for review. Those paragraphs simply assert that the Commissioner and officers of the department were exercising, or refusing to exercise, statutory powers of decision. The particulars given of the respects in which it is alleged that the exercise, or refusal to exercise the statutory powers was wrongful are sparse. It is asserted:

- (a) The Commissioner has taken into consideration incorrect and irrelevant information;
- (b) The Commissioner declined the application for relief on the basis that he did not consider that the applicant was in a position of serious hardship during the tax years subsequent to 2003.

[11] In her written submissions, counsel for the applicant submits:

- 6. Section 177(3) does not permit the Commissioner to accept the taxpayer's request in respect of some income years and decline the taxpayer's request in respect of other income years. In terms of s 177(1)(a) of the TAA, the taxpayer's application for financial relief was by way of:
 - “make a claim stating why recovery of outstanding tax would place the taxpayer in serious hardship.”
- 7. In this case, the Commissioner accepted the taxpayer's request in respect of the income years ended 31 March 1999 to 31 March 2003 inclusive **and** declined the taxpayer's request in respect on income years ended 31 March 2004 to 31 March 2008 inclusive, but under s 177C of the TAA.
- 8. The taxpayer's requests were in respect of recovery of outstanding tax arising from the income years ended 31 March 1999 to 31 March 2008 inclusive. The taxpayer's requests were made in the income

years ended 31 March 2008 and 31 March 2009. The taxpayer met the Commissioner's standard of serious hardship at the dates of application. On that basis:

- the Commissioner was required to accept the taxpayer's requests for financial relief on the grounds of serious hardship in the income years ended 31 March 2004 to 31 March 2008 inclusive.

The Commissioner ought to be directed to:

- Reconsider his dismissal of the taxpayer's application for relief in respect of the income years ended 31 March 2004 to 31 March 2008 inclusive pursuant to s 677 of the TAA, and
- Determine to grant the taxpayer's relief in respect of the income years ended 31 March 2004 to 31 March 2008 inclusive.

[12] That is amplified later in the submissions where counsel submits:

56. In terms of the Tax Administration Act, the taxpayer's requests for financial relief must be assessed at the date of that those requests are made and, in respect of "recovery of outstanding tax": that is all outstanding tax as a global sum.
57. In other words, the taxpayer's requests for financial relief cannot be assessed on an annual basis.
58. The effect of the legislative scheme is that the Commissioner is not entitled to accept the taxpayer's requests for relief in respect of some income years and decline the taxpayer's request for relief in respect of other income years both consequent on the taxpayer's application for relief.
59. For the applicant it is submitted that the Commissioner having accepted taxpayer's requests for relief made in 2008, cannot decline those requests for relief in respect of the income year ended 31 March 2004 to 31 March 2008.

The grounds for review

[13] The first question is whether the scheme of the Act is such that an application for relief must be considered on a global basis and not a year by year basis. The taxpayer's claim, under s 177(1)(a), must state why recovery of outstanding tax would place the taxpayer in serious hardship. Serious hardship as defined in s 177A includes significant financial difficulties that arise because of the taxpayer's inability to meet minimum expenses according to normal community standards, but does not

include significant financial difficulties that arise because the taxpayer is obligated to pay tax. The Commissioner has considered whether, in the year in which the obligation to pay the tax arose, the taxpayer was able to meet minimum living expenses according to normal community standards. In those years in which the Commissioner has determined that the taxpayer was unable to meet minimum living expenses according to normal community standards the Commissioner has granted relief.

[14] I consider that the Commissioner's approach to this question has been correct. That approach is a practical way of reconciling the rather difficult inter-relationship between paragraphs (a) and (b) of s 177A(1). If the matter had to be approached globally, as counsel for the taxpayer submits, then it would be necessary to consider the position at the time when the application was made. If, at that point, the taxpayer is assessed as being able to meet minimum living expenses according to normal community standards, then relief must be refused. In assessing whether, at that point, the taxpayer was able to meet minimum living expenses or not, no regard could be had to the obligation to pay tax which had arisen from earlier tax periods. A global approach might therefore disadvantage a taxpayer who had earlier failed to pay outstanding tax because of significant financial difficulties who, if application had been made at the time, might have obtained relief, but whose financial position subsequently improved to a point where the financial difficulties no longer existed. Conversely, a global approach might advantage a taxpayer who had failed to pay tax when financially able to do so, but was, by the time enforcement action was taken, in significant financial difficulties. I do not consider that either of these outcomes is consistent with the scheme and purpose of the Act. It seems more consistent with the purpose which the financial hardship regime is intended to achieve that the focus be on the ability of the taxpayer to pay the tax without significant financial difficulties at the time when the tax became payable. The exclusion from consideration, as possible grounds for serious hardship, of difficulties arising because of the obligation to pay tax, indicates a clear legislative intention that defaulting taxpayers may be pursued to a point which may result in serious hardship. That suggests that the appropriate focus is on the ability to pay the tax when the obligation arose, rather than at the point when enforcement proceedings are taken.

[15] This case is quite different from *W v Commissioner of Inland Revenue*. In that case, the issue was whether there were significant financial difficulties arising under s 177A(1)(a)(iii), not (1)(a)(i). The taxpayer's claim was that an earlier serious illness had resulted in a neglect of his tax affairs, with a consequent increased tax liability from penalties and interest. That case is of limited assistance on the different facts of this case. On the broad issue of whether a global approach or a year by year approach to financial difficulties is appropriate, I consider that nothing in that decision is inconsistent with the adoption of a year by year approach.

[16] For these reasons, I consider that the taxpayer has not demonstrated that the Commissioner's approach of considering the taxpayer's position on a year by year basis was wrong.

[17] Counsel for the applicant challenges the Commissioner's methodology by questioning the way in which the Commissioner has applied the household debt expenditure guide. The guide sets out figures for weekly average expenditure on certain items of expenditure for different categories of household (the one relevant for the applicant being a one person household). In applying that table, the Commissioner has omitted a number of line items for expenses which are not applicable to the taxpayer's particular circumstances – for example the line items for child care and school expenses (because the applicant has no dependent children) and for vehicle expenses (because the applicant does not own a vehicle).

[18] The use of the household expenditure guide is a tool to assist the Commissioner in determining what are the minimum living expenses according to normal community standards, for the particular taxpayer. The relevant question is whether or not the taxpayer is able to meet minimum living expenses according to normal community standards. This is a value judgment which the Commissioner must make. An application for judicial review is not an appeal against the Commissioner's decision. The onus is on the taxpayer to demonstrate that the Commissioner had erred in law in adopting the approach which he has. I consider that the taxpayer has fallen well short of demonstrating that the Commissioner's use of the household expenditure guide constitutes a reviewable error on the Commissioner's part.

[19] Mrs Harley also submits that the Commissioner has erred in his assessment of the information available to him as to the taxpayer's income for the relevant period. That, too, is an issue which goes to the merits, such as might be relevant on an appeal. I do not consider that any error of law or principle, within the purview of judicial review, has been demonstrated by the applicant.

[20] Mrs Harley further submits, in relation to paragraph 7 of her written submissions, that nowhere in any of the Commissioner's letters is there a specific reference to the statutory definition of serious hardship or whether the statutory test has been met. Nowhere is there reference to the s 176 prohibition on the recovery of outstanding tax to the extent that recovery would place the taxpayer in serious hardship. She submits that the Commissioner referred only to s 177C.

[21] There is no substance in this point. It is clear that the report upon which the Commissioner's decision was based was correctly focused on the correct statutory test, and explicit reference was made to s 177A. The Commissioner's letter of 18 February 2009 advising the decision also expressly referred to that section. The reference, in an internal summary dated 11 February 2009, referred to the write-off in the earlier years as being under s 177C. That was an appropriate reference in the context, and clearly not one intended to embrace all the relevant provisions. I consider that it is clear from the report on which the decision was based, read as a whole, that the Commissioner was correctly focused on the appropriate statutory test. No error of law has been demonstrated in this respect.

Result

[22] Those conclusions mean that the application for judicial review must fail. That decision makes it unnecessary for me to consider submissions which were addressed on the issue of the appropriate relief which might be granted, or as to the mechanics by which a write-off of tax is achieved in the event of a successful application for financial hardship.

[23] The respondent is entitled to costs which I fix on a 2B basis.

“A D MacKenzie J”

Solicitors: Crown Law Office, Wellington for Respondent
Mrs R P Harley, Barrister, Wellington for Applicant