IN THE HIGH COURT OF NEW ZEALAND
AUCKLAND REGISTRY

CIV-2008-404-3018

UNDER	The Companies Act 1993
BETWEEN	MANAGED FASHIONS LIMITED Applicant
AND	COMMISSIONER OF INLAND REVENUE Respondent

Hearing: 6 March 2009

Appearances: Mr Judd for Applicant
Mr Wood for Respondent

Judgment: 2 April 2009 at 4 p.m.

JUDGMENT OF ASSOCIATE JUDGE DOOGUE

This judgment was delivered by me on
***2 April 2009 at 4 pm**, pursuant to*
Rule 11.5 of the High Court Rules.

Registrar/Deputy Registrar

Date……

Counsel:

Mr S R Judd, P O Box 3320, Auckland

S J Eisdell Moore, Crown Solicitor, P O Box 2213, Auckland (C Wood)

[1] The respondent served a statutory demand pursuant to s 289 of the Companies Act 1993 on the applicant, claiming the sum of $1,910,421.74. The statutory demand related to core tax assessments of $61,072 and penalties thereon of $1,845,898.47. Mr Judd for the applicant said that he accepted that the Court:

> Does not have jurisdiction to rule on the correctness of the underlying tax assessments. Parliament had made clear in tax legislation that a taxpayer may only challenge assessments through the statutory procedures, …

[2] Mr Judd accepted that the applicant had exhausted its remedies with regard to the correctness of the underlying assessments, having brought proceedings in the Taxation Review Authorities and appeals from that tribunal to higher courts on that issue.

[3] Nonetheless, it was his submission that did not mean that the amount claimed in the statutory demand was correctly stated. Essentially he said there were three grounds upon which the application to set aside the statutory demand were brought:

a) The respondent has failed to honour his obligation to deduct $50,000 from the core tax in accordance with his undertaking to the Court (in other proceedings) to do so;

b) As the assessments relied upon by the applicant did not state a new date for payment, the additional taxes, being penalties, are not recoverable;

c) The respondent's conduct has resulted in the income assessed to the applicant as the income of another taxpayer.

[4] Mr Wood for the Commissioner strongly opposed each of those propositions.

[5] During the course of the argument I put it to Mr Judd that there was a difficulty in the path of the applicant, which was this: The amounts which the statutory demand claimed had been assessed as owing by the applicant in the case of core tax, and the interest and other charges thereon were 'add-ons' which were

calculated by reference to statutory provisions which charged interest and penalties on unpaid money. If the core tax had been finally assessed, how could the Court ignore that fact in a proceeding under the Companies Act 1993? Moreover, if the interest, costs and the like represented a statutory consequence of the assessment of the fixing of the undisputed core tax, how could this Court ignore that fact?

[6] This led Mr Judd to supplement his submissions in the following way. He said that if his primary submissions concerning the fact that the amounts owing were inconsistent with undertakings that the Commissioner had given to the Court were not upheld, then the applicant would have to apply for judicial review of the Commissioner's decision. As part of that approach, the applicant would ask the Court to defer consideration of the statutory demand until the process of judicial review had run its course.

[7] Pressed by me, Mr Judd agreed that he had to demonstrate that there was a reasonable argument that the applicant would succeed in judicial review proceedings to obtain orders to compel the Commissioner to re-assess the core tax in a way that was consistent with what Mr Judd described as his obligation to deduct $50,000 in accordance with his undertaking to the Court to do so.

[8] My understanding is that before this Court can exercise its jurisdiction to set aside the statutory demand, it must be affirmatively persuaded that the applicant has some reasonable prospect of persuading a Court with the appropriate jurisdiction to:

a) judicially review the Commissioner's actions; and

b) conclude that the Commissioner of Inland Revenue has acted erroneously; and

c) direct him to reassess the core tax in a way which is consistent with his statutory obligations.

[9] If all that were to occur, Mr Judd said, the Commissioner could be compelled to pass a credit of $50,000 against the core tax liability which would leave the sum of $11,072 still owing.

The claimed $50,000 reduction

[10] It is not necessary to review the long and tortuous history of the various proceedings between the Commissioner and Mr Judd's clients – as well as other parties. Reduced to its essentials, what I am told has happened is that a number of the individuals involved in a "Russell-template" tax avoidance scheme were assessed by the Commissioner on the basis that the scheme was voidable. Various taxpayers affected by this determination took proceedings to review and appeal the determination of the Commissioner. Some of the taxpayers (but not the applicant) entered into agreements with the Commissioner, pursuant to which they would pay some tax, but not the amount that had been assessed by the Commissioner. Deeds were executed in which this arrangement was enshrined. However the Commissioner apparently overlooked the necessity to obtain the consent of the Minister to these arrangements to the extent that such consent was necessary before there could be write-offs of more than $50,000 in tax. Such consent was not forthcoming and the arrangements where the tax exceeded $50,000 were unenforceable. Nonetheless, the Commissioner agreed to give effect to the arrangements to the extent of $50,000.

[11] Mr Wood while accepting the outline of matters as I have set them out in paragraph [10], would not accept that the applicant was entitled to a $50,000 credit or that the Commissioner had ever committed himself to passing such a credit to the applicant. That was because the applicant had never entered into a deed of settlement. He said there was therefore no issue of equality of treatment that would justify the Courts in reviewing the Commissioner's determination.

[12] As I see it the nub of the matter was stated by Baragwanath J in his decision of 11 August 2003 in *Miller and Ors v Commissioner of Inland Revenue* (AK HC, N103/93 and N1002/92, 11 August 2003):

> The plaintiffs are each equally entitled to a $50,000 reduction of their tax, the settlements being ineffective to that extent; they have never yet received credit for it.

[13] As I see it, this makes it quite clear that the $50,000 reduction of tax was to be available only to those parties who signed deeds that turned out to be only partially effective. It is correct that in several passages in the judgment Baragwanath J referred to 'the plaintiffs' in a context where it could be argued that the applicant was one of the parties being referred to. However, if instead of looking at textual subtleties of that kind, one stands back and looks at the overall arrangement and the reasons why the taxpayers other than the applicant were entitled to a $50,000 reduction, it becomes quite clear that the deed is the central distinguishing feature. There has been no compelling reason advanced why all the Russell-template taxpayers should be given a $50,000 credit irrespective of whether they entered into the deed or not. The fact is that those taxpayers that entered into the deeds in many cases partially fulfilled their obligations under the deeds before the fact of partial invalidity of the deeds became apparent. Quite obviously those persons had a good case to be given a credit. Instead of taking this course, the applicant took review and appeal proceedings. Mr Wood told me that a number of those who entered into the deeds of arrangement made payments pursuant to the deeds. He contrasted their cases with that of the applicant who has never paid anything on account of its tax liability.

[14] It may be that the opportunity to enter into a deed was not offered to the applicant. There does not seem to be any evidence on this aspect of matters. It might be that the Commissioner decided not to offer the compromise to the applicant. He may have assessed the case of the applicant as being less deserving. It may be that the Commissioner took the view that the applicant has been closely associated with the interests of Mr Russell – the author of the scheme, and that for that reason any question of an accommodation with the architect of the tax avoidance scheme was out of the question.

[15] I mention all these matters to demonstrate what the applicant regarded as being as almost self-evident – that the principal of equality of treatment had been breached - is perhaps not as obvious as Mr Judd in his submissions assumed it was.

[16] My conclusion is that it is difficult to assess the likelihood that an application for judicial review would result in the core tax being abated. The question of whether the actions of the Commissioner are likely to be judicially reviewed because of a perceived disparity of treatment between the applicant and the other Russell-template taxpayers was not something that was gone into in any depth before me.

[17] A more serious problem for the applicant is represented by the following passage from the Court of Appeal decision in *Westpac v IRD* (CA, 20/2/09, CA624/07):

> Our approach to the availability of judicial review
>
> [59] We think it appropriate to continue to apply the established principles as to judicial review in tax cases. We accept that judicial review is available where what purports to be an assessment is not an assessment. Associated with this, we accept that judicial review is available in exceptional cases and thus may be available in cases of conscious maladministration (as was recognised in *Futuris*). We can reconcile this with ss 109 and 114 on the basis that in such cases (ie no genuine assessment or conscious maladministration) what is challenged is either not an assessment, or at the least, not the sort of assessment which the legislature had in mind in enacting those sections. On this basis we see the availability of judicial review as depending on the claimant establishing exceptional circumstances of a kind which results in the amended assessment falling outside the scope of ss 109 and 114 and thereby not engaging those sections.
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> [60] We see any broader approach to judicial review as inconsistent with the statutory scheme. Despite the repetition, we set out s 109 which provides:
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> Except in . . . a challenge under Part VIIIA,—
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> (a) No disputable decision may be disputed in a court or in any proceedings on any ground whatsoever; and
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> (b) Every disputable decision and, where relevant, all of its particulars are deemed to be, and are to be taken as being, correct in all respects.
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> A taxpayer who seeks judicial review of an assessment might be thought to be disputing it and doing so in flat defiance of s 109(a). Section 109(b) deems an assessment to be "correct in all respects"

> which might be thought to necessarily extend to its validity. In the context of the present case, we have difficulty with reconciling the statutory requirement that the 1999 amended assessment be taken as "correct in all respects" with the proposition advanced by Westpac that it is nonetheless invalid and ineffective.
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> [61] We also consider that the broad approach contended for by Westpac places too much emphasis on the assessment as an exercise of a statutory power of decision. An assessment should reflect the correct tax position and a taxpayer's liability to pay tax exists independently of the assessment. If the assessment is correct, it is hard to see why complaints about process should result in the taxpayer not paying tax on a correct basis. Where there are very large sums of tax at stake (as there are here), this raises fairness considerations in relation to other taxpayers who have met their liabilities for the tax year concerned. If the assessment is wrong, it can be corrected in later challenge proceedings. If it is correct, the tax should be paid. It is frankly difficult to see what is unfair in this approach.

[18] In my judgment, the imponderables, difficulties and uncertainties that lie ahead for the applicant if it now starts judicial review proceedings are such that it is impossible to say that there is a substantial dispute whether or not the debt will ultimately be found to be owing in respect of s 290(4)(a) of the Companies Act 1993.

No new date on notices of assessment

[19] The notices of assessment on which the statutory demand has based did not include a due date for payment. Mr Judd submitted that because no due date for payment had been fixed, no additional taxes could be charged. He said that *Withey & Ors v Commissioner of Inland Revenue* (1990) 18 NZTC 13,732 is authority for that proposition.

[20] Mr Wood drew my attention to the decision of Courtney J in *NTH Douglas & Ors, Applicant v Commissioner of Inland Revenue & Others* HC AK, CIV 2003-404-006359, 16 February 2009. In that judgment, Courtney J referred to s 398(5) of the Income Tax Act 1976. This section only applies where the Commissioner is satisfied that the taxpayer has not been guilty of 'wilful neglect or default in making due and complete returns for the purposes of that tax'. If the Commissioner is not so

satisfied, then he is not required in his notice of assessment, or amended assessment, or any subsequent notice to fix a new date for the payment of the tax.

[21] In this case, the Commissioner, Mr Wood said, was not so satisfied. As a result, the due date for payment of the tax assessed to the applicant was as set out in s388 and the Eighth Schedule to the Income Tax Act 1976. For taxpayers with balance dates within the months from March to September inclusive, the due date is 7 February in the following calendar year. The Commissioner having advised no due date means the due date for payment of the tax was therefore set by operation of statute. If that is so, then the extra tax could be assessed from the point when it acquired the status of being unpaid, that is from 7 February in the following calendar year.

[22] I consider that the Commissioner's submissions on this point are beyond argument. Mr Judd did not submit to me that there had been any miscalculation on the part of the Commissioner as to the amount that was owing. His submission was that because the Commissioner had not correctly followed procedures set down in the Act, the time had not yet arrived at which the tax was due, and therefore the extra tax that was claimed by way of penalty could not be due either. I consider that submission is wrong. The applicant does not have a reasonably arguable defence arising out of the alleged obligation of the Commissioner to set a due date.

Argument that tax assessed to Managed Fashions Limited has now been assessed to another tax payer

[23] The applicant, in effect, submits on this point that income which has been assessed to it has also been assessed in the hands of another taxpayer, Mr J G Russell.

[24] As the Commissioner explains matters, however, what has happened is that certain consulting fees were claimed as a deductible expense by the applicant. Those consulting fees were apparently rendered by Mr J G Russell. The consulting fees were disallowed by the Commissioner as a deductible expense in the hands of the applicant because they did not meet the criteria set out in s 103 of the Income Tax

Act 1976 (the Act). As a result, the taxable income derived by the applicant increased and its overall tax burden has been enlarged. At the same time, the Commissioner has assessed the fees as taxable income in the hands of Mr J G Russell.

[25] In my view, the submissions made for the applicant are misconceived. The Court of Appeal in *Miller v Commissioner of Inland Revenue* [1999] 1 NZLR 275 at 292 considered a similar argument. The Court of Appeal referred to s 99 (4) of the Act which provides:

> 4. Where any income is included in the assessable income … of any person pursuant to subsection (3) of this section then, for the purposes of this Act, that income will be deemed to have been derived by that person and shall be deemed not have been derived by any other person.

[26] The Court then went on to say:

> There is also a complaint that the Commissioner has assessed the Russell entity in respect of all the consulting fees. That does not, however, show any inconsistency. A payment by one taxpayer which is not deductible is frequently assessable in the hands of its recipient.

[27] There is nothing more that needs to be said on the subject. The increase in the applicant's assessable income which resulted from the disallowance of the deduction is logically quite separate from the question of the tax that might be paid by the other entity who charged the applicant with the expense.

Conclusion

[28] In my view the applicant does not have a reasonably arguable defence on any of the points that have been raised for consideration on the hearing of this application. The application is dismissed. The parties should confer on the matter of costs and if they are not able to agree I shall allocate a short hearing in one of my Chambers Lists to deal with the matter.

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J.P. Doogue
Associate Judge