

PRACTITIONER ARTICLES

[1457] Stay of recovery of tax debts - a swing back to taxpayers

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In *DCT v Denlay* [2010] QCA 217 (reported at 2010 WTB 37 [1448]), the Queensland Court of Appeal unanimously dismissed an appeal by the Commissioner against a decision of the Supreme Court of Queensland to grant a stay of enforcement of a judgment for outstanding tax, penalties and interest obtained by the Commissioner. The decision of Chesterman JA, with whom Muir JA and McMurdo P agreed, in allowing the continuation of the stay:

- prevents the Commissioner from bankrupting the taxpayers;
- allows the taxpayers to continue a Federal Court appeal under Pt IVC of the *Taxation Administration Act 1953* (TAA) against the amended assessments; and
- goes some way to curtailing the Commissioner's administrative power to issue what may otherwise have proved to be an incontestable assessment.

Legislative background

The significance of this decision is best highlighted against the background of the "pay now - argue later" legislative regime under which the assessments are issued. Section 177(1) of the ITAA 1936 provides that:

"The production of a notice of assessment ... under the hand of ... a Deputy Commissioner, purporting to be a copy of a notice of assessment, shall be conclusive evidence of the due making of the assessment and, except in proceedings under Part IVC of the Taxation Administration Act 1953 on a review or appeal relating to the assessment, that the amount and all particulars of the assessment are correct."

Part IVC of the TAA allows taxpayers to challenge assessments by seeking a review of the assessment in the AAT or appeal against them to the Federal Court. However, s 14ZZR of the TAA provides that:

"The fact that an appeal is pending in relation to a taxation decision does not in the meantime interfere with, or affect, the decision and any tax, additional tax or other amount may be recovered as if no appeal were pending."

Section 14ZZM is in similar terms but refers to reviews of decisions in the AAT rather than appeals to the Federal Court. The Commissioner is therefore permitted to proceed to recover outstanding amounts of tax claimed in an assessment or amended assessment notwithstanding that the taxpayer is in the process of judicially testing whether the tax is in fact payable. From a revenue protection point of view, this regime guards against taxpayers expending significant resources on defending tax assessments and, in the event they are unsuccessful, being unable to pay the tax because they had exhausted their resources in funding the litigation against the Commissioner. Whilst it is suggested there is some justification for this concern, the prospect of an "incontestable assessment" as highlighted by the late Justice Hill in *McCallum v FCT* (1997) 36 ATR 256 is equally undesirable.

An incontestable assessment

In his strong dissenting judgment in *McCallum*, Hill J outlined the following scenario (at p 265):

"The Commissioner issues an assessment. The taxpayer objects to it. The assessment may be recovered as a debt. The Commissioner proceeds to do so. The taxpayer seeks a stay, but on the principles enunciated by the court of Appeal in FCT v Mackey ... the stay is refused. The Commissioner proceeds to judgment and then issues a bankruptcy notice. That notice can not be challenged because if one sought to go behind the judgment debt one is met by an assessment unchallengeable under section 177:... On the same basis, the taxpayer

is made bankrupt. He is insolvent as a result of the tax debt. There may or may not be other creditors. The Commissioner appoints a trustee in bankruptcy or perhaps the Official Receiver becomes trustee. In either case the trustee has no interest in fighting the objection in the Administrative Appeals Tribunal. It is immaterial to the trustee. And the trustee has no funds to do so. Hence the taxpayer loses the right to appeal and is made bankrupt without ever having a right to challenge the assessment. It could not happen, could it?"

Effect of bankruptcy

Section 60(2) of the *Bankruptcy Act 1966* provides that:

"An action commenced by a person who subsequently becomes a bankrupt is, upon his or her becoming a bankrupt, stayed until the trustee makes election, in writing, to prosecute or discontinue the action."

Justice Hill's fear was that the administrator of the tax law can become the adjudicator and enforcer of his own opinion that the correct amount of tax as determined by the Commissioner must be paid or he will bankrupt the individual and so stifle any Pt IVC appeal. The result is that the Commissioner can conceivably issue an assessment, bankrupt the taxpayer and ensure there is no challenge to the assessment.

ATO Receivables Policy

Chapter 28 of the ATO Receivables Policy sets out the Commissioner's view on the use of bankruptcy proceedings. Compliance with that Policy is mandated by Practice Statement PS LA 2008/13. The general rule is that where an objection, review or appeal has not been finalised and the Commissioner is satisfied there is little or no risk that the final tax will not be paid, the Commissioner will allow the taxpayer to enter into a 50/50 arrangement. Under a 50/50 arrangement, the taxpayer pays all undisputed debts and at least 50% of the disputed debt. In return, the Tax Office will agree not to recover the unpaid balance of the disputed debt until 14 days after the appeal decision is handed down and will remit 50% of the GIC.

According to paras 28.35 to 28.38 of the ATO Receivables Policy, if a tax debtor chooses not to enter into a 50/50 agreement, collection action is nevertheless unlikely to be commenced prior to the determination of the objection, review or appeal unless the circumstances of the case indicate an "unacceptable level of risk". Chapter 28 of the Policy also suggests that the Commissioner sees bankruptcy or liquidation as a last resort. However, this may be cold comfort to taxpayers who do not have sufficient funds to enter into a 50/50 arrangement as prescribed by the Policy.

In his dissenting judgment in *McCallum*, Justice Hill noted (at p 265) that:

"The view which the majority of the court has reached in the present case gives the Commissioner powers which are capable of abuse. It is no answer, in the remaining days of this century, to say that the Commissioner can be trusted. That is an argument which betrays a lack of realism and experience with tax administration. In so saying, I do not suggest that the present incumbent of the office of the Commissioner would in anyway abuse his powers. But it is possible, as the report of the tax Ombudsman makes clear, that some officers might."

Stays of execution of tax judgment debts

The legislative regime places the Commissioner in a position of special advantage in relation to the recovery of tax debts. However, each of the state and territory courts retain the discretion to stay the recovery of a tax judgment debt in special circumstances. The weight of authority requires this discretion to only be exercised "sparingly". In *Denlay*, Chesterman JA considered that the stay of recovery proceedings granted and further extended by Lyons J was within the scope of the discretionary power provided under rule 800 of Queensland's Uniform Civil Procedure Rules. His Honour considered the criteria set out below by French J (as he then was) in the Federal Court decision of *Snow v DCT* (1987) 18 ATR 439 (at p 458) which were later confirmed by French J in *DCT v Warrick (No 2)* (2004) 56 ATR 371 (at p

396) as relevant to the exercise of discretion to grant or refuse a stay of execution:

"It may generally be concluded from the preceding review, that the power of State courts to stay recovery proceedings instituted in them under the ITAA is well established and that courts exercising it have regard to the following propositions:

1. The policy of the ITAA as reflected in its provisions give **priority to recovery of the revenue against the determination of the taxpayer's appeal** against his assessment.
2. The power to grant a stay is therefore exercised **sparingly** and the onus is on the taxpayer to justify it.
3. The merits of the taxpayer's appeal constitute a factor to be taken into account in the exercise of the discretion (although some Judges have expressed different views on this point).
4. Irrespective of the legal merits of the appeal a stay will not usually be granted where the taxpayer is party to a contrivance to avoid his liability to payment of the tax.
5. A stay may be granted in a case of abuse of office by the Commissioner or **extreme personal hardship** to the taxpayer called on to pay.
6. The mere imposition of the obligation to pay does not constitute hardship.
7. The existence of a request for reference of an objection for review where appeal is a factor relevant to the exercise of the discretion." [Emphasis added]

Extreme personal hardship

In the absence of any other factual circumstances which might have been considered "extreme personal hardship", a key issue for the Court of Appeal in *Denlay* to determine was whether the possibility of the taxpayers being made bankrupt and therefore unable to continue the Pt IVC appeal in the Federal Court was an example of extreme personal hardship. The Commissioner relied in particular on *DCT v Ho* (1996) 32 ATR 269 in which Ireland J stated (at p 274) that:

"The possibility that the taxpayer may be bankrupted is not of itself an extreme personal hardship: Akers Counsel for the applicant conceded as much but submitted that the consequent deprivation of the [r]ight or ability to object to the notices of assessment and appeal against any disallowance was the relevant hardship....

In my view, however, if bankruptcy of itself is not sufficient hardship, the normal consequences of bankruptcy cannot effect a different result....

Whilst in proceedings not involving sections 14ZZM and 14ZZR it has been said that the loss of the 'fruits of an appeal' is a sufficient special circumstance justifying a stay of execution ... the effect of sections 14ZZM and 14ZZR ... must be to prima facie preclude such a result ... It is the express policy of sections 14ZZM, and 14ZZR that the Commissioner has a right to the assessed tax irrespective of the pendency of an appeal.

...
The fact that the applicant may be deprived of an ability to object or appeal of itself does not justify the granting of a stay of the recovery proceedings in the face of ss 14ZZM and 14ZZR."

Chesterman JA was not critical of the outcome in *Ho's* case. His honour noted at [32] that:

"The decision in *Ho* cannot, I think, be criticised. The fact that *Ho* had not sought to challenge the assessments in the two and a half years since they were issued was not itself enough to refuse a stay. It was not really a case in which the bankruptcy would deprive the taxpayer of his right of challenge. The taxpayer had never sought to exercise that right. The remarks relied upon are, therefore, obiter dicta."

However, Chesterman JA was able to distinguish *Ho* from the facts of the case before the Court of Appeal, where the taxpayers had sought to have the assessments challenged and, at the time, those appeals were due to be heard in the Federal Court in September 2010. While acknowledging that the Supreme Court's power to stay execution of a tax judgment debt should be

exercised "sparingly" and "with great caution", his Honour said (at [50]):

"This leads to the [Commissioner's] third point, that the loss of their property and consequent inability to prosecute their appeals does not constitute extreme personal hardship. The point may be answered shortly. It is preposterous to contend that the loss of the respondent's entire estate, and with it any chance of demonstrating that the basis for the assessments were wrong so that they should not have lost their property, could not be a hardship rightly called extreme. It is not easy to imagine a greater hardship in this context." [Emphasis added]

No sufficient likelihood of bankruptcy

In relation to the contention that the likelihood of bankruptcy was not sufficient to justify the stay, the Commissioner argued that the outcome of any bankruptcy proceedings would be determined by a federal court which "might not" order sequestration because of the pendency of the Pt IVC appeals. The effect of this argument is to push the responsibility onto the court dealing with the bankruptcy petition. It was rejected by Chesterman JA at [48] because:

"It seeks to deprive the Supreme Court altogether of its power to stay execution in appropriate cases. The effect of the submission is that only a federal judicial officer can stand between a judgment debtor indebted to a Deputy Commissioner and bankruptcy."

Appeal to the High Court

As a general proposition, successfully obtaining a stay of recovery proceedings is the exception rather than the rule. The Commissioner may argue that the reasoning in *Denlay* is out of step with a number of cases including the NSW Supreme Court decision in *Ho* and the decision of the Full Court of the Supreme Court of Victoria in *Held v FCT* (1988) 19 ATR 1213. However, it is suggested that the Court of Appeal's reasoning in *Denlay* is sound and is consistent with the decision of the Queensland

Supreme Court in the unreported decision of *DCT v Jennings* [2005] QSC 312 where McMurdo J granted the stay of recovery proceedings on similar facts.

Had the Pt IVC proceedings still been scheduled for hearing on 13-16 September 2010, the Commissioner may not have been inclined to seek special leave to appeal to the High Court since the substantive tax dispute may have been quickly resolved. However, as the Pt IVC proceedings have now been vacated to a date which has not yet been determined, this may provide the impetus for Commissioner to apply for special leave to appeal.

How the High Court might view such an application is difficult to anticipate. The consistent characterisation of the power to grant a stay of execution as a discretionary matter of practice and procedure may weigh against the High Court supplying the Commissioner with any universal rule he might desire. In *Marina Estates Pty Ltd v DCT* (1974) 4 ATR 369 Barwick CJ, with whom the Full High Court agreed, stated that the exercise of discretion to grant a stay of recovery proceedings "... was a matter peculiarly within the discretion of the primary judge."

It will be interesting to see whether the Commissioner decides to pursue the matter further.

Conclusion

In this case, the Queensland Court of Appeal unanimously recognised that a taxpayer being made bankrupt and losing the ability to conduct appeals on the substantive taxation issues which gave rise to the tax liability may constitute "extreme personal hardship". Whilst the onus will still be on the taxpayer to show that a refusal to grant the stay of recovery would give rise to extreme personal hardship and the court's discretion may only be used "sparingly", this development should be welcomed as a step in the right direction and away from the risk of incontestable tax assessments identified by Justice Hill in *McCallum* over a decade ago.