

## COMMISSIONER OF TAXATION AND FIXED CHARGES

Comment by

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It has fallen to my lot to consider issues of general significance arising from two 1984 tax decisions relating to this topic. The first I am to refer is that of the Full Court of New South Wales Supreme Court in DFC of T v AGC (Advances) Ltd 84 ATC 4177. The other is a decision of the Full Court of the Victorian Supreme Court in Horsburgh v DFC of T 84 ATC 4501.

Both decisions concern the relative positions of the Commissioner of Taxation to whom unpaid employee tax instalment deductions are due and of a creditor of the defaulting employer to whom has been granted a specific charge. Of importance here, with respect to the Commissioner, are the provisions of subs 221P(1) of the Income Tax Assessment Act 1936, as amended; in particular, the stipulation in the subsection that, where the property of a defaulting employer has become vested in, or where the control of that property has passed to, a trustee, the trustee is liable to pay the unpaid tax instalments to the Commissioner. Under the Act, the definition of "trustee" includes a receiver or liquidator: see subs 5(1) of the Act.

In the AGC case, the company Wallyn Industries Pty Ltd had charged all its present and future book debts in favour of AGC (Advances) Pty Ltd (AGC) as security for advances made by AGC. The deed of charge provided that the charge created was to operate as a fixed charge subject to certain conditions. On 26 July 1982, an order was made for the winding-up of Wallyn and a liquidator was appointed. On 12 August 1982, AGC appointed receivers under its deed of charge.

Prior to appointment of receivers by AGC, the liquidator had collected some book debts. He was advised on 16 August 1982 of the appointment of the receivers and of their claim that any book debt collected during the course of the liquidation must be held on their behalf. The Commissioner of Taxation claimed priority under s 221P over the receivers to the proceeds of the book debts to meet unremitted tax instalments deducted by Wallyn. Pending resolution of the competing claims of the Commissioner and AGC, the liquidator continued to collect the book debts and put those which he collected in a separate interest bearing deposit.

At first instance, Wootten J decided that AGC was entitled to the proceeds of any book debts received since 12 August 1982 in priority to the Commissioner. Upon appeal by the Commissioner, the Full Court upheld the finding at first instance. On my reading of the judgments, there was some differences as to the basis upon which the finding at first instance should be upheld.

Hutley and Priestley JJA both, it appears to me, viewed the matter as one depending upon meaning of the word "control" where used in s 221P. Both rejected a submission made by the Commissioner that because the liquidator was permitted to collect the book debts, which were the subject of the charge, he was in control of the assets of the company for the purposes of s 221P. The rationale behind this rejection, on my reading, is that "control" for the purpose of s 221P cannot be achieved in respect of assets subject to specific charges. In other words, the trustee must obtain control of the complete legal and equitable interest in the relevant property.

Mahoney JA, on the other hand, expressly stated that:

"The fact that there is a specific charge does not, I think, prevent the liquidator taking the relevant property under his control: at least it does not do so where the chargee has not, by the exercise of the powers under the charge, already taken control of it." (at p 4183)

Mahoney JA rejected the Commissioner's claim with reference to the principle adopted in Barnes' case (75 ATC 4262) expressed by him to be that "the interest of a chargee under a specific charge was outside the effects of the operation of the section [221P] ..." (at p 4183).

Turning to the decision in Horsburgh's case, in short, both Messrs Horsburgh and Newman were receivers and managers of a company Intercab Pty Ltd under a debenture granting a floating charge over the company's assets. The receivers paid the net proceeds of their receivership to the debenture holder and paid nothing to the Commissioner of Taxation. The Commissioner brought an action to recover the unremitted group tax claiming priority under s 221P.

Prior to the appointment of the receivers, but after defaulting on its obligations to the debenture holder, Intercab granted a fixed and specific charge over certain book debts to secure a further advance by the debenture holder. The net proceeds received by the debenture holder from the receivers roughly equalled the amount realised on the book debts and was less than the amount secured by the fixed charge. Accordingly, the receivers argued that the fixed charge had priority over the floating charge given by the debenture which did not crystallise until their appointment. The receivers further argued that the book debts had not passed into their control for the purposes of s 221P.

The debenture contained a restrictive clause prohibiting the creation of charges ranking equally or in priority to the charge created by the debenture. Accordingly, Anderson and Murray JJ in

the Full Supreme Court of Victoria rejected the receivers' argument on the basis that, according to ordinary priority rules, the subsequent fixed charge ranked in priority after the debenture. Their Honours could find no evidence to suggest that a debenture holder intended to vary the terms of the debenture or otherwise create security over a specific asset which would have had the effect of preventing the asset from passing into the control of the receivers.

McGarvie J dissented from the findings of his brethren because of a provision in the debenture which provided that nothing in the debenture should operate to, amongst other things, prejudice any other obligation or security from time to time binding the borrower in favour of the lender. The relevant provision went on to say that all such securities and obligations would be deemed collateral. McGarvie J found that the debenture and the fixed charge ranked equally and concluded that:

"Where there are several equally ranking security interests over an item of property which is insufficient to satisfy them all, there are principles which determine the allocation of the available sum between them." (at p 4513)

Accordingly, his dissenting view was that the Commissioner was entitled to his statutory priority in respect of a proportion of the proceeds of the book debts.

What principles or rules can, then, be gleaned from these two cases? There are two which I wish to refer to. The first, in confirmation, it seems, of the decision in Barnes' case (75 ATC 4262), is that the interest of a chargee under a specific charge is outside the operation of s 221P of the Income Tax Assessment Act, provided that it ranks in priority to any prior floating charge. This issue of priority must be carefully considered having regard for the terms of the prior floating charge and the terms of the subsequent specific charge.

Secondly, both cases are a clear lesson that every endeavour should be made to avoid letting control, in any sense of that word, of property subject to a specific charge fall to a liquidator or receiver to whom s 221P applies. The AGC case indicates the limitation of "control" within the meaning of s 221P but also indicates the difficulties that can arise should a liquidator or receiver take any action with respect to property the subject of a specific charge.