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Liquidators not required to withhold proceeds to satisfy capital gains tax liability in the absence of an assessment

The recent Federal Court decision in *Australian Building Systems Pty Ltd ACN 094 238 678 (in liquidation) v Commissioner of Taxation* [2014] FCA 116 (**Decision**) is a significant step towards resolving a controversy that has existed for some time between the Commissioner of Taxation (**Commissioner**) and insolvency practitioners: to what extent is a liquidator required to withhold monies from the proceeds of the sale of company property for the purpose of satisfying an anticipated capital gains tax liability?

Facts and analysis

The liquidators of Australian Building Systems Pty Ltd (**ABS**) sold real property (**Property**) in the course of the company's winding up, which triggered CGT event A1 (disposal) for the purpose of the *Income Tax Assessment Act 1997* (Cth) (**ITAA 1997**). The liquidators sought a private ruling from the Commissioner to determine to what extent, if any, the liquidators were required to retain monies from the proceeds of sale of the Property to apply towards the anticipated tax liability of the company for the applicable income year (which would include an amount of CGT liability referable to the disposal of the Property). An income tax assessment had not yet been issued to ABS in respect of the relevant income year.

The private ruling provided that, pursuant to section 254 of the *Income Tax Assessment Act 1936* (Cth) (**ITAA 1936**), the liquidators:

- were required to account to the Commissioner, **out of the proceeds of sale**, for any capital gains tax liability that crystalised on the sale of the Property; and
- the monies were required to be retained **at the point of crystalisation** (as opposed to at the time when an income tax assessment is issued).

Section 254 relevantly provides that a liquidator will be:

> *'answerable as taxpayer for the doing of all such things as are required to be done by virtue of this Act in respect of the income, or any profits or gains of a capital nature ...'*

Further, he or she is authorised to:

> *'**retain from time to time** out of any money which comes to him or her in his or her representative capacity so much as is sufficient to pay tax **which is or will become due** in respect of the income, profits or gains'.*

The liquidators objected to the private ruling (which was upheld) and subsequently sought review of that objection decision. The threshold issue in contention was whether section 254 of the ITAA 1997 operated on the liquidators (and thus imposed an obligation to retain monies from the date of sale of the Property) prior to an assessment being issued to ABS for the relevant income year.

Justice Logan held that prior High Court authority (*Bluebottle UK Ltd v Deputy Commissioner of Taxation* (2007) 232 CLR 598) regarding the interpretation of section 255 of the ITAA 1936 could be extrapolated and applied by analogy to the current matter. In particular, the requirement in section 254(1)(d) of the ITAA 1997 to retain an amount sufficient to pay tax *'which is or will become due'* was found to refer only to tax that is: (a) subject to an assessment and which is due for payment; or (b) subject to an assessment but which is not yet due for payment. Therefore, section 254 of the ITAA 1997 would only operate on the liquidators if a notice of assessment had been issued for the income year in which the Property was sold. Accordingly, section 254 of the ITAA 1997 had no application to the liquidators because there was no outstanding income tax assessment at the time that the Property was disposed.

Highlights

- Section 254 of the ITAA 1997 is a 'collection' provision that imposes obligations on a liquidator only following a primary taxation liability being assessed to the company.
- Liquidators are **not** required to withhold monies from the proceeds of the sale of company property to satisfy anticipated tax liability unless the company is in receipt of an income tax assessment.
- The Decision is not directly instructive on the issue of whether liquidators are required to withhold monies from the proceeds of sale of property to satisfy **any** outstanding income tax assessment (eg, an income tax assessment for the year preceding the disposal of property). Caution should be exercised by liquidators who intend to refrain from withholding monies from the sale of property in circumstances where the company has an outstanding income tax assessment(s).
- The Decision should not be taken as a mandate to distribute the proceeds derived from the sale of company property to creditors prior to an income tax assessment being issued for the applicable income year. The court stated that a 'prudent liquidator' would be entitled to retain any gain until such time that the tax position for the year in which the gain was made can be ascertained.

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