



Update

Insolvency

September 2009

The ATO can't jump the queue, or can it?

On 26 August 2009 the High Court of Australia handed down its decision in the appeal from the decision of the Full Court of the Federal Court of Australia in *Federal Commissioner of Taxation v Bruton Holdings Pty Ltd (in Liq) (2008) 173 FCR 472*. The High Court overturned the decision of the Full Federal Court. It found that a garnishee order issued by ATO under section 260-5 of the Taxation Administration Act (the **Administration Act**) after the date of liquidation was void.

The Facts

In this case, the ATO issued an assessment to Bruton assessing the company's tax liability at more than \$7.7million. The assessment was issued shortly before the creditors of Bruton resolved to wind it up. After it had been wound up, the ATO lodged a proof of debt in the liquidation and also issued a notice (pursuant to section 260-5 of the Administration Act) to one of Bruton's creditors requiring it to pay money it held on deposit for Bruton to the ATO. A notice under section 260-5 gives the ATO the right to recover from a third party an amount that the third party owes or may later owe to a taxpayer who is indebted to the Commonwealth for tax.

The Decision

The critical issue for the Court was whether, the application of property of a company, as described by sections 501 and 555 of the Corporations Act, which enshrines the pari passu principle, could be avoided by the ATO by the engagement of section 260-5 of the Administration Act. The High Court held that the notice under section 260-5 was void. It said that a notice under this section can be described as a garnishee order. It creates positive rights, namely, "a right to give a valid receipt and discharge for the money, and a right in case of non-payment to obtain execution against the garnishee."

Implications

The real effect of this decision is to restore the proper position regarding the distribution of assets in an insolvency. It is also consistent with the decision by the High Court in *International Air Transport Association v Ansett Australia Holdings Ltd (2008) HCA 3*. However, the Financial Review has reported that the position may be different with respect to GST if a bill which the Federal Government is about to introduce into Parliament is enacted. Another interesting question is whether a notice issued under 260-5 by the ATO within the relation back period is also void? If it isn't, the equal distribution of assets to all unsecured creditors is disturbed.

If you require any further information, please contact:

MELBOURNE

Penelope Pengilley
Partner

T +61 3 9321 9821

E penelope.pengilley@holdingredlich.com.au

SYDNEY

Greg Wrobel
Partner

T +61 2 9234 4411

E greg.wrobel@holdingredlich.com.au

BRISBANE

Toby Boys
Partner

T +61 (0)7 3135 0649

E toby.boys@holdingredlich.com.au

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