

ATO RECEIVABLES POLICY

PART B The collection of taxation debts

Chapter 36

FREEZING ORDERS

(ALSO KNOWN AS MAREVA INJUNCTIONS OR ASSET PRESERVATION ORDERS)

The policy in this chapter is to be followed by ATO staff. We have made every effort to ensure it is technically accurate, but in the interests of clarity it has been written in 'plain English' and should not be read or interpreted like legislation. If you feel that something in the chapter is wrong or misleading, please advise the ATO.

Date of effect: 30 November 2010

Key legislation: Federal Court Rules, Order 25A; State Court Rules: NSW: Rule 25 Uniform Civil Procedure Rules ("UCPR"); QLD: Section 260A UCPR; VIC: Section 37A Supreme Court (General Civil Procedure) Rules 2005; SA: Rule 247 Supreme Court Rules; WA: Order 52A Supreme Court Rules; TAS: Section 937 Supreme Court Rules 2000.

PURPOSE

1. This chapter should be read in conjunction with Chapter 3 'Risk management'. It outlines the circumstances and risk factors which will determine when the Commissioner will utilise the freezing order or mareva injunction.

INTRODUCTION

2. The equitable remedy of a mareva injunction (named after the case of *Mareva Compania Naviera SA v. International Bulkcarriers SA [the Mareva]* [1975] 2 Lloyd's Rep 509) is now incorporated as part of the rules of civil procedure in Commonwealth and State jurisdictions. In line with these rules the term "freezing order" is used interchangeably in this Chapter with the term "mareva injunction".
3. In terms of Order 25A Rule 2 of the *Federal Court Rules*, the purpose of a freezing order is to "prevent the frustration or inhibition of the Court's process by seeking to meet a danger that a judgment or prospective judgment of the Court will be wholly or partly unsatisfied".
4. The Commissioner will generally apply to the court for a freezing order where it is concluded that action of certain debtors to dispose of or deal with assets, present an unacceptable level of risk to payment of the liability or the enforcement of a judgment he may subsequently obtain should legal action become necessary to recover the debt.
5. A freezing order is essentially a form of injunction that is used to restrain the respondent or their agents from removing assets from the jurisdiction, or otherwise disposing of or dealing with those assets pending further orders by the court (for example until final judgment is obtained against the respondent). The order does not create a security or interest as such in the assets for the applicant.

6. The law which governs the granting of mareva injunctions is well-settled and the courts have been prepared to adapt mareva injunctions to a range of situations where the Commissioner has sought to preserve assets at risk of being dissipated.
7. In addition to relevant case law, there are both Federal and State court rules which allow a court to make a freezing order in similar circumstances to those necessary for the granting of a mareva injunction. The wording of Order 25A of the *Federal Court Rules* has been largely adopted by the states in their respective rules.
8. To justify a freezing order, there must be in the view of the court a real and not merely fanciful risk 'that in the absence of an injunction any assets wherever located which the respondent may have, will be dissipated or dealt with in some fashion such that the applicant will not be able to have the judgment satisfied'.

POLICY

9. The Commissioner has a duty to collect money legally owed to the Commonwealth as a result of the operation of those Acts that he administers. This duty requires him to ensure that debtors do not evade their liability by dealing with their assets in such a way so as to frustrate the execution of judgment.
10. As a successful application for a freezing order depends on the level of risk attributable to any case, the Commissioner's decision to embark on this process will invariably necessitate consideration of the principles in Chapter 3 'Risk management'.
11. Where the risk assessment process establishes there is an unacceptable level of risk to the revenue, the Commissioner will make a decision to minimise that risk. That decision may involve the instigation of a number of processes including the application to the court for a freezing order to preserve assets.

Requisite elements for a freezing order

12. The risk assessment process requires due regard to the requisite elements for a freezing order as prescribed by the relevant court rules and as settled by the court. In *Third Chandris Shipping Corp. v. Unimarine S.A.* (1979) Q.B. 645 at 668, Lord Denning outlined the requisite elements that the plaintiff must address in an application for a mareva injunction. In the case of the Commissioner as applicant for a freezing order, the following are considered relevant:

Prima-facie cause of action

- In the first instance, the Commissioner must establish a prima-facie cause of action against the tax debtor. A prima-facie case is one that has a real possibility of ultimate success as opposed to a speculative case. Therefore the Commissioner must demonstrate a good arguable case against the tax debtor. The cause of action is the non-payment of the debt by the date that it was due to be paid.
- Although it is an advantage to have commenced legal recovery proceedings before embarking on an application for a freezing order, it is not an essential prerequisite. It will not always be possible to commence legal action because the assessed amounts due to the Commissioner may not be payable at the point in time when action to obtain a freezing order is commenced (that is, payable at a future date).

- If legal action has not commenced, the applicant must establish a claim against the tax debtor. The courts would appear to be satisfied that the Commissioner has a sufficiently strong case where notices of assessment have been issued. Production in court of notices of assessment, by virtue of section 177(1) of the *Income Tax Assessment Act 1936*, is deemed to be conclusive evidence of the making of the assessments. (See *Commissioner of Taxation v. Rosenthal* [1984] 16 ATR 159) and *DFC of T v. Sharp & Anor, Ex parte DFC of T* 88 ATC 4572). Where legal action has not commenced, it is to be expected that the court will require an undertaking that proceedings for recovery be commenced within a fixed time.

Disclosure to the court

- In an ex-parte application, it is essential for the applicant to make full and frank disclosure of all material matters, to avoid injustice to the tax debtor. Such matters should include any evidence that may be prejudicial to the applicant's case and any assumption made in the absence of sufficient evidence or suspicion of a particular course of conduct by the tax debtor, which may not be fully substantiated.
- A failure to make full disclosure places the applicant at risk of an application being made by the tax debtor for the freezing order to be discharged on the basis that the order would not have been made ex parte had the undisclosed matters been brought to the attention of the court.
- Hearsay evidence is admissible as long as the source of information is explicitly stated.

Assets within the jurisdiction

- The Commissioner must provide evidence of the existence of assets owned by the tax debtor within the jurisdiction. The nature of the assets, their location and their approximate value should be identified with as much detail as possible.
- It is however, not a fatal obstacle that the applicant for a freezing order has little or no knowledge of the financial circumstances of the party against whom the injunction is sought, nor that with more diligence something more might have been discovered. Commercial reality often requires an application for this relief to be brought quickly and without notice before detailed enquiries can be made, otherwise its very purpose could be frustrated.
- The case of *Riley McKay Pty Ltd v. McKay* [1982] 1 NSW LR 264 established the principle that a tax debtor is required to make an affidavit of discovery of assets in aid of a mareva injunction.
- In the event, however, that the applicant can identify the tax debtor's assets with sufficient particularity to enable the court to make an effective order, no discovery will be required. Discovery should be sought where the precise form and whereabouts of a tax debtor's assets are in doubt or where distribution of assets among a number of persons is unclear. Without the aid of discovery, it may be impossible to enforce the order or to oblige third parties to comply with it. Tax debtors are obliged to disclose all

assets including those in which they have only a contingent interest, when making their affidavit of discovery.

- Information can also be obtained by issuing notices pursuant to section 353-10 of the *Taxation Administration Act 1953* provided such notices issue *before* the commencement of any proceedings.
- Some Australian decisions indicate that a freezing order may be granted to restrain a person from dealing with assets wherever they are located, and regardless of whether they have ever been within the jurisdiction. In *DFC of T v. Hickey & Anor* 96 ATC 4892, the Supreme Court of WA ruled that a *mareva* injunction can apply to assets outside the territorial jurisdiction of the Court (in this case New Zealand). However, this is not settled law and there appears to be some judicial conflict on the question of jurisdiction (see *FC of T v. Karageorge & Ors* (96) ATC 5114; *National Australia Bank Ltd v. Dessau & Ors* (1988) VR 521 and *Brereton & Ors v. Milstein & Ors* (1988) VR 508). Generally, the Commissioner will apply for an injunction covering assets in Australia and overseas.

Grounds for believing that there is a real risk of dissipation

- The Commissioner must provide grounds for believing that there is a risk of the assets being moved from the jurisdiction or dissipated so that if judgment is obtained, it may go unsatisfied. A fear held by the Commissioner that the assets are likely to be improperly dealt with is not sufficient to seek a freezing order.
- Evidence should be provided that the risk has materialised or will probably do so. Wherever possible it should be shown that the tax debtor may be organising their affairs and assets so that any judgment obtained will be frustrated.
- It may be difficult to establish a clear case of real risk, but evidence as to the previous conduct of the tax debtor may hold significant weight in such matters. Situations may arise where evidence relevant to the cause of action itself is also relevant to the question of risk of dissipation of assets.
- The same factors that go toward establishing a *prima-facie* cause of action may in certain cases be used to establish the question of risk of dissipation. This is particularly so in cases in which the *prima-facie* cause of action against the tax debtor involved evidence of gross dishonesty.
- The case of *Patterson v. BRT Engineering (Aust) Ltd* (1989) 18 NSWLR 319 involved a claim by the plaintiff that the defendant had fraudulently misappropriated a large sum of money from a company under his control. It was held by the court that the nature of the scheme in which the defendant appeared to have engaged was such that it was 'reasonable to infer' that he was not the sort of person who would, unless restrained, preserve his assets intact so that they might be available to his judgment creditor. The evidence used to bring on the action was also held to be relevant in establishing the question of the risk of asset dissipation.
- The courts were also prepared to find a real risk of dissipation of assets by the tax debtor based on evidence of earlier dishonest conduct in the decisions of *DCT v. AES Services [2009] VSC 527* and *DCT v. Gashi and Anor [2010] VSC 120*. In these cases the court granted freezing orders despite the fact that there was no direct evidence of intention to avoid the debts or of any preparations to dissipate assets. The courts were prepared

to find a real risk of dissipation of assets by the tax debtor based on evidence of earlier dishonest conduct.

- To enable the court to evaluate an application, the Commissioner's affidavit should disclose the inquiries which have been made about the tax debtor and their business and the results of those inquiries, including evidence of any relevant dishonest conduct. The affidavit should also include details of any statements or inferences from the tax debtor indicating an intention to move assets as well as any threats made by the tax debtor. Financial statements, such as balance sheets may also be used to support the application, together with evidence of intended overseas travel, particularly if there is evidence of a regular pattern of overseas travel.
- The strength of the evidence contained within the affidavit presented to the court will be the deciding factor in whether the freezing order is granted.

Undertaking as to damages

- A freezing order may have serious consequences on a tax debtor's business, which may lead to substantial claims being made against the Commissioner in the event that it is found that the injunction was unjustified. The Commissioner would ordinarily be required to give an undertaking as to damages, which may be supported by a bond or other security.
- In this regard, the Commissioner must ensure that the injunction is not too wide, catching unnecessarily assets of which he was unaware, or extending to assets greater in value than are necessary to meet the claim.

Third parties

13. During investigations of the tax debtors' affairs, including their compliance history, it may become apparent that tax debtors have deliberately structured their financial affairs in a manner so as to defeat any judgments made against them. For example, the tax debtor's matrimonial home may have been transferred to a related third party such as a spouse, a family company or trust.
14. Accordingly, where such third party assets appear to be at risk of dissipation by the tax debtor or the third party, the Commissioner would often seek to include such assets within the scope of a freezing order.
15. The decision of the High Court in *Cardile and Others v. LED Builders Pty Ltd* [1999] 198 CLR 380, assessed the basis of a mareva order with particular focus on its application against third parties who are non-parties to the main proceedings. By majority judgment, the High Court found that a mareva order may be granted against non-parties, where it is necessary to prevent the dissipation of assets so as to protect the administration of justice. The High Court said that such an order against a third party may be appropriate, assuming the existence of other relevant criteria and discretionary factors, in circumstances in which:
 - the third party is in possession or means of control of assets of the judgment debtor or potential judgment debtor, or
 - some process, ultimately enforceable by the courts, is or may be available to the judgment creditor as a consequence of a judgment against that actual or potential judgment debtor, pursuant to which (whether by appointment of a liquidator, trustee in bankruptcy, receiver or otherwise)

the third party may be obliged to disgorge property or otherwise contribute to the funds or property of the judgment debtor to help satisfy the judgment against the judgment debtor.

16. Order 25A Rule 5(5) of the *Federal Court Rules* deals with third party assets and states that a freezing order can be made over third party assets if the Court is satisfied that there is a danger that a judgment or prospective judgment will be wholly or partly unsatisfied because the third party:
 - holds or is using or has exercised or is exercising a power of disposition over assets of the [prospective] judgment debtor, or
 - is in possession of or is in a position of control or influence over assets of the [prospective] judgment debtor.

Alternatively, the Court can make a freezing order if it is satisfied that there is a process ultimately available to the applicant as a result of a [prospective] judgment under which the third party may be obliged to disgorge assets or contribute towards satisfying the [prospective] judgment.

17. From a taxation perspective, a freezing order or mareva will be used to restrain the disposal or removal of assets held by third parties where it can be demonstrated to the court that the judgment debtor has control over property held by a third party and that execution of the judgment would be successfully levied against such property.
18. Alternatively, a freezing order may be granted against third parties where they have obtained the assets of the tax debtor by means of sham transactions or fraudulent conveyances. The court has taken the view on a number of occasions that assets, even though in the name of the tax debtor's spouse, were in reality assets beneficially or equitably held on behalf of the tax debtor against which a judgment creditor should be able to levy execution.
19. The evidentiary onus lies on the applicant to convince the court that assets of a third party are, in reality, available to the respondent to meet his obligations.
20. A freezing order cannot be used to affect the legitimate rights which a third party may have acquired over the respondent's property. For example, a respondent cannot be prevented from paying his legitimate debts or disposing of his assets in the normal course of business (see *A.J. Bekhor & Company v. Bilton* [1981] 2 ALL ER 565).

Breaches

21. A freezing order is a court order. Consequently, wilful breaches are punishable as a contempt of court with appropriate penalties.
22. As a model litigant, the Commissioner has a duty to bring such contempt to the attention of the court.
23. In an unreported ATO matter, a tax debtor who purported to assign his half share of his matrimonial home to his estranged spouse under a Family Law settlement while a mareva injunction was in force, was sentenced to two months imprisonment.
24. On the other hand, because the mareva injunction is an equitable remedy, the court will not tolerate any abuse of the procedure. Accordingly, improper conduct by the applicant, such as not commencing recovery proceedings until well after the due

date of an assessment or putting unfair pressure on the tax debtor, may lead the court to refuse to grant or continue the injunction.

Roles of the ATO technical areas

25. Given the complexity of the matters requiring address in a decision to proceed with a freezing order, the relevant technical area in Operations **must** be consulted at the earliest opportunity to assess the available evidence on which the application will rely.
26. As a freezing order may impose considerable constraints on a taxpayers' resources which could adversely impact on their business, extreme care needs to be exercised in reaching a decision to utilise this remedy. Accordingly, the authority to approve an application for a freezing order will be limited to senior officers after consultation with the relevant technical area.
27. The services of Legal Services Branch should be utilised as early as possible if an application for a freezing order is being considered. Advice can be provided to assist in respect of the gathering of evidence to support the application. It may also be necessary to liaise with other stakeholders to co-ordinate the timing for issue of notices of assessment with the filing of the application with the court. Once a decision has been reached to proceed with the application, the manager of the Legal Services Branch will decide whether a solicitor within the Legal Services Branch will conduct the matter in house or alternatively whether the services of an external legal provider will be required.

TERMS USED

Freezing order – an order restraining a person from removing any assets, in or outside Australia or from disposing of, dealing with, or diminishing the value of those assets.

Mareva injunction – an interlocutory injunction which restrains a debtor or the debtor's agents, servants or otherwise from removing assets from the jurisdiction or disposing of or dealing with those assets so as to frustrate a creditor seeking to recover from the debtor.

Injunction – an order by which the court directs someone to refrain from acting in a particular way, or in some instances, to perform a particular act (known as a mandatory injunction).

Interlocutory – proceedings or applications are those actions taken during the course of a legal proceeding which are incidental to the principal object of the proceeding. In the collection context, it may be a further application made after a writ or summons has been issued for the recovery of a debt. These proceedings can also be taken prior to legal action being initiated provided the Commissioner gives an undertaking he will issue the relevant process (for example, writ or summons) within a certain time.

Ex parte – a matter dealt with by a court with only the applicant present. The respondent is not usually present to put forward an argument to refute that of the applicant.

Chapter 36 - Archived versions

Version 4 – July 2006 (will link to chapter 36 pdf)
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Version 5 – August 2008 (will link to chapter 36 pdf)
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