TD 2012/D7 - Income tax: does a receiver who disposes of a CGT asset as the agent for a debtor have an obligation under section 254 of the Income Tax Assessment Act 1936 to retain from sale proceeds sufficient money to pay tax which is or will become due as a result of disposing of that asset?

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Draft Taxation Determination

Income tax: does a receiver who disposes of a CGT asset as the agent for a debtor have an obligation under section 254 of the *Income Tax Assessment Act 1936* to retain from sale proceeds sufficient money to pay tax which is or will become due as a result of disposing of that asset?

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This publication is a draft for public comment. It represents the Commissioner's preliminary view about the way in which a relevant taxation provision applies, or would apply to entities generally or to a class of entities in relation to a particular scheme or a class of schemes.

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Ruling

1. Yes, a receiver who is an agent of the debtor is required by paragraph 254(1)(d) of the *Income Tax Assessment Act 1936* (ITAA 1936) to retain from the sale proceeds that come to them in the capacity of agent sufficient money to pay tax which is or will become due as a result of disposing of a Capital Gains Tax (CGT) asset.[1]

[1] The relationship between a receiver and a debtor is determined by the terms of the security documentation under which the receiver is appointed, and by the relevant State and Commonwealth legislation. The security documentation under which the receiver is appointed will usually expressly provide that the receiver is the agent of a debtor. However, where such a statement is not included, an agency relationship can usually be inferred from the security documentation (Dal Pont, G E, 2001, *Law of Agency*, Butterworths, Australia, p.36; *Gosling v. Gaskell & Grocott* [1897] AC 575 at 595, per Lord Davey). By way of contrast, a mortgagee in possession does not act in a trustee capacity and does not assume a fiduciary relationship with respect to the mortgagor (see for example: *Chant v. Deputy Federal Commissioner of Taxation* 94 ATC 4733; (1994) 29 ATR 403, *Deputy Commissioner of Taxation (Vic) v. General Credits Ltd* [1988] VR 571; 87 ATC 4918; (1987) 19 ATR 372). As such, a mortgagee in possession is generally not an agent or trustee of the debtor for the purposes of section 254 of the ITAA 1936.

2. When a receiver, as agent of the debtor, disposes of a CGT asset, the total sale proceeds from the disposal are moneys of the debtor.[2] The sale proceeds 'come to' the receiver in the capacity as agent. In these circumstances, the obligation on the receiver to retain under paragraph 254(1)(d) of the ITAA 1936 relates to the gross sale proceeds.

3. The receiver will have an obligation to retain money sufficient to pay tax which is or will become due.[3] Section 254 of the ITAA 1936 operates on the basis that the receiver will have the obligation to make returns and be assessed in their representative capacity in respect of the income, profits or gains of a capital nature arising from the disposal.

4. The fact that an increase in the value of the asset may have to some extent accrued before the appointment of the receiver does not affect the amount of the gain that is the subject of paragraph 254(1)(a) nor the tax liability that is the subject of paragraph 254(1)(d) of the ITAA 1936. The gain arises directly from the happening of the CGT event.

Example 1: Section 254 liability where receiver is agent of debtor

5. *Andrew is appointed to act as a receiver for Carl's Cars Pty Ltd (the debtor) by Big Bank Co (a secured creditor of the debtor) pursuant to a deed of appointment. The deed of appointment specifies that Andrew is an agent for the debtor. Andrew makes a gain of a capital nature through the sale of one of the debtor's assets. Andrew makes the gain in his representative capacity as receiver for the debtor.*

6. *Paragraph 254(1)(d) of the ITAA 1936 authorises and requires Andrew to retain from the proceeds so much as is sufficient to pay the tax which is or will become due in respect of the gain.*

Example 2: Section 254 liability where agent of creditor

7. *Bianca's Bikes defaults on its mortgage with Large Bank Pty Ltd. Large Bank Pty Ltd takes possession of the mortgaged land. Raymond is appointed to act as agent for Large Bank Pty Ltd. Raymond makes a gain of a capital nature by executing Large Bank Pty Ltd's power of sale as a mortgagee in possession and sells the mortgaged land. In these circumstances Raymond is not the agent for Bianca's Bikes and no income, profit or gain of a capital nature is derived by Raymond as a representative of Bianca's Bikes.*

8. *Paragraph 254(1)(d) of the ITAA 1936 does not apply to require Raymond to retain an amount from the income he derives as a result of selling the mortgaged land.*

[2] This is the case even if the asset is a secured asset.

[3] At the time the obligation to retain arises there may not be an income tax assessment in respect of the tax liability (see draft Taxation Determination TD 2012/D6 *Income Tax: Must income tax have been assessed before an agent or trustee has an obligation under section 254 of the Income Tax Assessment Act 1936 to retain sufficient money to pay tax which is or will become due as a result of their agency or trusteeship?*).

Date of effect

9. When the final Determination is issued, it is proposed to apply to arrangements begun to be carried out from the date of issue. However, the Determination will not apply to taxpayers to the extent that it conflicts with the terms of settlement of a dispute agreed to before the date of issue of the Determination (see paragraphs 75 to 76 of Taxation Ruling TR 2006/10).

Commissioner of Taxation
19 September 2012

Appendix 1 – Explanation

This Appendix is provided as information to help you understand how the Commissioner's preliminary view has been reached. It does not form part of the proposed binding public ruling.

Explanation

10. Section 254 of the ITAA 1936 imposes a number of obligations upon agents and trustees in respect of any income, profits or gains derived by the agent or trustee in their representative capacity.

11. In so far as is relevant for the purposes of this draft Determination, section 254 of the ITAA 1936 provides:

> With respect to every agent and with respect also to every trustee, the following provisions shall apply:
>
> (a) He or she shall 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, derived by him or her in his or her representative capacity, or derived by the principal by virtue of his or her agency, and for the payment of tax thereon.
>
> (b) He or she shall in respect of that income, or those profits or gains, make the returns and be assessed thereon, but in his or her representative capacity only, and each return and assessment shall, except as otherwise provided by this Act, be separate and distinct from any other.
>
> …
>
> (d) He or she is hereby authorized and required 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.
>
> (e) He or she is hereby made personally liable for the tax payable in respect of the income, profits or gains to the extent of any amount that he or she has retained, or should have retained, under paragraph (d); but he or she shall not be otherwise personally liable for the tax.

12. A CGT event (usually CGT event A1) will happen in respect of a debtor's CGT asset when a receiver, in their capacity as an agent of the debtor, disposes of the asset. The debtor may make a gain of a capital nature as a result of a CGT event happening to a CGT asset of theirs.

13. In such circumstances the receiver would have obligations under paragraphs 254(1)(a) and 254(1)(b) of the ITAA 1936 in respect of any such gain.

14. Section 254 of the ITAA 1936 does not itself create a liability for tax.[4] Rather, any liability to pay tax is created under the relevant substantive liability provisions of the income tax legislation. Section 254 works in conjunction with these provisions to provide that an agent for a debtor is liable in relation to any such tax liability that arises in the course of their agency. It provides the machinery provisions that set out when an agent is liable to pay the tax.[5]

15. Where the receiver as agent for the debtor disposes of a CGT asset of the debtor, any capital gain from the disposal arises by virtue of the receiver's agency. Under the CGT regime, the capital gain arises when the relevant CGT event happens, and not progressively over the period of ownership of the asset. That is, the full amount of the gain is made by the debtor when the receiver disposes of the CGT asset.

16. For example, if an asset was purchased ten years earlier for $100,000, and it was worth $200,000 when the receiver was appointed as agent for the debtor, and subsequently it was disposed of for $210,000 during the period in which the receiver was the agent of the debtor, then the debtor's tax liability (if any) will relate to the whole of the $110,000 capital gain.[6] Any tax due in respect of that capital gain is the subject of paragraph 254(1)(d) of the ITAA 1936.

17. The fact that the receiver is bound to apply the money received to meet secured debts does not constitute the receiver as trustee for the secured creditor in respect of the receipt of those moneys, nor as agent for the secured creditor.[7] Therefore it is considered that the gross sale proceeds come to the receiver as agent for the debtor, and that is the money from which an amount sufficient to pay the tax liability must be retained.[8]

18. As a consequence, an amount retained in compliance with paragraph 254(1)(d) of the ITAA 1936 takes precedence over the contractual right of the secured creditor to the proceeds from the disposal of the secured asset. This is the case irrespective of the arrangements made for the payment of sale proceeds – for example, the receiver does not avoid this obligation by directing the payment of sale proceeds directly to the secured creditor.[9] The retention required by paragraph 254(1)(d) is a statutory requirement that takes precedence over other claims on the money. The obligation subsists despite other existing or potential claims over the retained amount.

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[4] *Fermanis v. Cheshire Holdings Pty Ltd* (1990) 1 WAR 373; 90 ATC 4201 at 4203; (1990) 20 ATR 1862 at 1865, per Murray J.

[5] See footnote 4 of this draft Ruling and *Howey v. Federal Commissioner of Taxation* (1930) 44 CLR 289 at 294; [1930] HCA 45,per Rich and Dixon JJ, which considered section 89 of the *Income Tax Assessment Act 1922*, the predecessor of section 254 of the ITAA 1936.

[6] It should be noted that section 254 of the ITAA 1936 does not require the debtor's tax liability to have been assessed in order for the obligation to retain to arise (see draft Taxation Determination TD 2012/D6*).*

[7] *Buckeridge v. Mercantile Credits Ltd* (1981) 147 CLR 654; [1981] HCA 62, per Brennan J (Gibbs CJ, Murphy and Wilson JJ concurring).

[8] In *Australian Securities and Investments Commission (ASIC) v. Lanepoint Enterprises Pty Ltd; ASIC v. Bowesco Pty Ltd* [2006] FCA 1493; (2006) 64 ATR 524, a case relating to winding up proceedings, the receivers and managers had retained large sums of money for the potential tax liabilities of the two companies under receivership. Arguments were raised that no provision was required to be made for any potential tax liabilities. However, the receivers and managers contended that, in the course of their duties, they had sold properties and consequently had derived income and capital gains. They were concerned that, due to these sales, they may have a personal liability for taxes accrued in the course of their receivership and accordingly were entitled to make contingency provisions for the payment of those amounts. French J observed at paragraph 57 that 'the receivers were entitled to take the view that they were obliged to make appropriate provisions against tax liabilities'.

[9] *Fermanis v. Cheshire Holdings Pty Ltd* (1990) 1 WAR 373; 90 ATC 4201; (1990) 20 ATR 1862 supports this view of the statutory requirement to retain money under section 254 of the ITAA 1936. In that case Murray J held that the retention by the Public Trustee of sufficient money to cover the tax liability was correct and agreed with the Public Trustee that he could not be required to pay out to the plaintiff what the law required

Appendix 2 – Your comments

19. You are invited to comment on this draft Determination including the proposed date of effect. Please forward your comments to the contact officer by the due date.

20. A compendium of comments is prepared for the consideration of the relevant Rulings Panel or relevant tax officers. An edited version (names and identifying information removed) of the compendium of comments will also be prepared to:

- provide responses to persons providing comments; and
- be published on the ATO website at www.ato.gov.au

Please advise if you do not want your comments included in the edited version of the compendium.

Due date: **19 October 2012**

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him to retain. At ATC 4203; ATR 1865, Murray J referred to section 254 as a 'machinery provision' which 'expresses clearly a requirement to retain money so as to enable payment of tax which is or will become due…' The amount that was ultimately paid out had to be, at ATC 4205; ATR 1867, 'less the sum required to be retained by law'.

References

Previous draft:

Not previously issued as a draft

Related Rulings/Determinations:

TR 2006/10; TD 2012/D6

Subject references:

- CGT assets
- disposal of assets
- insolvency
- liability of trustee
- receivers & managers
- receivership
- representative of incapacitated entities

Legislative references:

- ITAA 1922 89
- ITAA 1936 254
- ITAA 1936 254(1)(a)
- ITAA 1936 254(1)(b)
- ITAA 1936 254(1)(d)

Case references:

- Australian Securities and Investments Commission (ASIC) v. Lanepoint Enterprises Pty Ltd; ASIC v Bowesco Pty Ltd [2006] FCA 1493; (2006) 64 ATR 524
- Buckeridge v. Mercantile Credits Ltd (1981) 147 CLR 654; [1981] HCA 62
- Chant v. Deputy Federal Commissioner of Taxation 94 ATC 4733; (1994) 29 ATR 403
- Deputy Commissioner of Taxation (Vic) v. General Credits Ltd [1988] VR 571; 87 ATC 4918; (1987) 19 ATR 372
- Fermanis v. Cheshire Holdings Pty Ltd (1990) 1 WAR 373; 90 ATC 4201; (1990) 20 ATR 1862
- Gosling v. Gaskell & Grocott [1897] AC 575
- Howey v. Federal Commissioner of Taxation (1930) 44 CLR 289; [1930] HCA 45

Other references:

- Dal Pont, G E, 2001, Law of Agency, Butterworths, Australia

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