Inland Revenue
Te Tari Taake

CASE SUMMARY

Official Assignee directed to comply with deduction notice issued by the Commissioner of Inland Revenue in the event that forfeiture orders are not made and restraint is lifted in proceeds of crime proceeding

Decision date: 4 November 2024

CSUM 25/03

CASE

***Commissioner of Police v Cheng* [2024] NZHC 3242**

LEGISLATIVE REFERENCES

Criminal Proceeds (Recovery) Act 2009, ss 6, 25, 37, 38, 43, 52, 53, 55, 56 and 83

Tax Administration Act 1994, ss 6, 15B, 89AB, 89D, 106, 109, 113 and 157

Income Tax Act 2007, s CD1

Goods and Services Tax Act 1985, s 43

CASE LAW REFEERENCES

Commissioner of Police v Cheng [2023] NZHC 606

Commissioner of Police v Snook [2018] NZHC 2537

Westpac Securities NZ Ltd v Commissioner of Inland Revenue [2014] NZHC 3377

Arai Korp Ltd v Commissioner of Inland Revenue [2013] NZHC 958

Tannadyce Investments Limited v Commissioner of Inland Revenue [2011] NZSC 158; [2012] 2 NZLR 153

Commissioner of Inland Revenue v Wilson (1996) 17 NZTC 12,512 (CA)

O'Neil v Commissioner of Inland Revenue [2001] UKPC 16, [2001] 3 NZLR 316, (2001) 20 NZTC 17,051, [2001] WL 535706 (PC)

Miller v Commissioner of Inland Revenue; Managed Fashions Ltd v Commissioner of Inland Revenue (1998) 18 NZTC 13,961 (CA)

McIlraith v Commissioner of Inland Revenue (2007) 23 NZTC, 21,456, [2007] WL 2121918 (HC)

LEGAL TERMS

Restraint, forfeiture, deduction notice

Summary

The Commissioner of Inland Revenue (CIR) filed an interlocutory application in a proceeds of crime proceeding seeking orders that, in the event forfeiture orders are not made and restraint over restrained funds is lifted, the Official Assignee is to pay funds belonging to 11 respondents to the proceeding to the CIR to reduce the outstanding tax liabilities of those respondents.

The High Court granted the orders sought and directed the Official Assignee to pay the CIR the lesser of the amounts held on behalf of the 11 respondents or their outstanding tax liability as at the date restraint is lifted.

Impact

The judgment reiterates that tax assessments that have not been challenged using the statutory disputes process are deemed to be correct in all respects under s 109 of the Tax Administration Act 1994 (TAA).

While a taxpayer can request a s 113 assessment, there is no obligation on the CIR to reopen assessments where a taxpayer did not use the statutory disputes procedure in the first

instance. The Court affirmed that an application under s 113 does not 'stay' the operation of s 109 nor does it mean that tax liability may not be enforced under that section. Section 113 is not intended to be used to circumvent the statutory disputes procedure.

Facts

In 2016 a restraining order was obtained by the Commissioner of Police (CoP) over properties and funds that were linked to the alleged methamphetamine dealing of Thomas Cheng (the First Respondent) and the alleged tax evasion and money laundering by William Cheng (the Eighteenth Respondent) (Mr Cheng) and Niyoh Chew Hong (the Nineteenth Respondent). Ultimately, the value of restrained assets included properties and bank accounts worth approximately $20 million.

The CIR had assessed income tax and GST liabilities for each of the 11 respondents on the basis of rental payments received from the properties owned by each respondent. Rental payments had gone into the bank accounts of Mr Cheng and Worldwide Models Limited (the Ninth Respondent). Mr Cheng is the authorised signatory on the company's account. None of the 11 respondents disputed the assessments of their tax liability which before interest and penalties amounted to $1,679,246.33.

In March 2023 Cooke J determined the CoP's application for profit forfeiture orders in relation to the total sum of $20,102,053.22. The application insofar as it related to Mr Cheng and Nyioh Chew Hong was founded on allegations of tax evasion and money laundering. It was not alleged that they were involved with the significant drug dealing in which Thomas Cheng had been engaged. Justice Cooke accepted the profit forfeiture claim relating to Thomas Cheng's drug dealing offending. In relation to the other respondents, the CoP had proven that there was significant criminal activity of tax evasion, but the allegations of money laundering were not accepted.

The tax liability by the time of the forfeiture hearing had increased to $11,443,457.36 due to penalty and interest provisions under the TAA. However, the benefit of the tax evasion in the proceeding was assessed at $1.6 million on the basis that the interest and penalties were not a benefit derived from the offending itself. Rather, they were penalties faced by the respondents for their tax evasion. To avoid double recovery, Cooke J declined to make a forfeiture order in relation to the $1.6 million, concluding that the best course of action was for the CIR to use his extensive powers to effectively call for the payment of those monies.

The CoP filed an appeal in relation to the core tax liability of $1,679,246.33. The appeal was heard in July 2024 and the decision is yet to be released.

Following Justice Cooke's decision, on 15 December 2023 the CIR issued a deduction notice to the Official Assignee under s 157 of the TAA and s 43 of the Goods and Services Tax Act

1985. The deduction notice related to rental payments into the bank accounts that the CIR said belonged to the 11 respondents who had tax debts.

Issues

The CIR's position was that should the restraint be lifted, the restrained funds that were identified as rental payments would be payable to the 11 respondents but should instead, under the deduction notice, be paid to the CIR and applied towards the payment of their tax debts.

The respondents did not deny that the funds belonged to the 11 respondents, but objected to the orders sought on the basis that:

a) the default assessments issued by the CIR are incorrect;
b) Mr Cheng is in a current tax dispute with the CIR for the same alleged tax debt; and
c) the CIR's failure to collect tax for more than six years calls into question the integrity of the tax system in circumstances in which the CIR is claiming penalty interest for the period during which he failed to act.

Decision

Alleged erroneous default assessments

The respondents alleged that the amount specified in the deduction notice and sought to be deducted from the funds held by the Official Assignee is incorrect. They said that accountants now engaged by the respondents had identified errors in the default assessments of Harvest Property LLP (the Sixth Respondent), the respondent with the largest outstanding tax liability. An application under s 113 of the TAA to amend the default assessments has been made in relation to Harvest Property LLP.

The Court noted that if the statutory disputes process is not used to challenge a tax assessment, the assessment is deemed to be correct under s 109 of the TAA. While a s 113 application is being considered in relation to Harvest Property LLP, the Court held that it does not affect the operation of s 109. The 11 respondents' income tax, GST and evasion shortfall penalty assessments were not disputed and pursuant to s 109 have crystallised. Justice Radich noted that the respondents do not dispute that, and held that they cannot now seek to challenge the correctness of the assessments in this forum.

The Judge said that if the s 113 application is successful, then any new assessment issued would be incorporated in the updated summaries of account to be provided to the Official Assignee. In the event that a new assessment was issued after restraint was lifted and funds

had been paid to the CIR pursuant to the deduction notice, the CIR would treat any excess tax paid in the usual way. Justice Radich said:

> It is important that the system operates in this way. The administrative chaos … that would otherwise unfold would be significant. Inland Revenue receives vast numbers of tax returns continuously. In each case, the Commissioner has no knowledge of a taxpayer's affairs. The system would be unworkable if s 113 could be used to delay or avoid collection procedures where tax obligations have been ignored previously. The need for corrections could have been avoided if tax returns were filed on time or resolved through the statutory processes. Section 113 does provide a backstop means of protection but it cannot stop the operation of the time-sensitive mechanisms for the payment of tax in the first instance.

William Cheng dispute

Default assessments have been issued to Mr Cheng personally for the same debt as has been assessed for the 11 respondent companies. Mr Cheng issued a notice of proposed adjustment and the dispute is currently at the conference phase.

The Court agreed with the CIR that the two assessments are not necessarily inconsistent with each other. Any benefits received by the shareholder from a company can be regarded as being dividends in the circumstances and are taxable irrespective of whether the company has paid tax on the same income previously. In that case, the 11 respondents and Mr Cheng will have a tax liability. If Mr Cheng is not beneficially entitled to the funds then there will have been no transfer of value to him that could be taxed as a dividend. But, if the restrained funds do not belong to the 11 respondent companies, then the funds in Mr Cheng's account represent a transfer of value to him and the assessments to him and the companies can both stand. The Court said the tax liability will be met when someone pays it.

Justice Radich said that the Privy Council has found that the CIR may at any time amend inconsistent assessments to alleviate an inconsistency before proceedings objecting to or challenging assessments have run their course. The Court held that the CIR must be allowed some flexibility in the timing of adjustments to meet administrative demands and to enable him to await the outcome of objection or challenge proceedings.

Alleged inordinate delay and the integrity of the tax system

The respondents alleged that the CIR needed to act promptly and that through taking no action while the funds were restrained the tax debt has increased exponentially which is unfair to the respondents. They argued that for the CIR to take no action for six years and now to seek to recover penalty interest against the respondents is unduly burdensome and disproportionate.

The Court disagreed saying that cannot be so in circumstances in which the respondents have chosen not to meet, or to deal with, their tax liabilities until recently. The tax system is predicated on voluntary compliance by taxpayers. The Judge observed that the respondents

could have paid their tax debt at any time, either through unrestrained funds or filing an application to the court to have the restraint varied to enable their tax obligations to be met. Justice Radich said it is apparent that it is only since the CIR has issued a deduction notice and become actively involved in these proceedings that the respondents have taken steps relating to their tax obligations, adding that they have not complied with their filing obligations since April 2017 (the 2016 financial year was the latest assessment issued by the CIR).

Conclusion

The Court accepted the CIR's point that once the appeal was determined the restraining order will be lifted and there was a need for certainty on to whom the restrained funds should be paid. Having concluded that none of the arguments advanced by the respondents would prevent the orders sought, the Court granted the CIR's application.

About this document

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