

Lloyds Bank Export Finance Limited

Appellant

v.

The Commissioner of Inland Revenue

Respondent

FROM

THE COURT OF APPEAL OF NEW ZEALAND

JUDGMENT OF THE LORDS OF THE JUDICIAL COMMITTEE
OF THE PRIVY COUNCIL, DELIVERED THE
19TH JUNE 1991

Present at the hearing:-

LORD KEITH OF KINKEL
LORD TEMPLEMAN
LORD JAUNCEY OF TULLICHETTLE
SIR ROBERT MEGARRY
SIR DAVID CROOM-JOHNSON

[Delivered by Lord Jauncey of Tullichettle]

This appeal involves the construction of certain sections of the New Zealand Land and Income Tax Act of 1954 which was consolidated in the Income Tax Act 1976. Before looking in detail at the relevant sections it may be convenient to summarise the circumstances giving rise to the appeal. The fiscal year in New Zealand runs from and to 31st March, so that the year ending 31st March 1980 would be described as the 1980 year. The appellants ("the taxpayers") submitted the necessary returns for the years 1976 and 1977 showing small profits. However, because of substantial losses in prior years which they were entitled to carry forward and set off, the respondent ("the Commissioner") made determinations to the effect that no tax was payable by them in the two years in question. Some five years after the last of the two determinations the Commissioner sought to assess the taxpayers to tax in respect of the above two years. The taxpayers challenged the assessments upon the ground *inter alia* that they were statute barred by reason of the provisions of section 24 of the 1954 Act. Tompkins J. upheld the taxpayers' objection to the assessments but the Court of Appeal quashed the orders made in the High Court and declared that the Commissioner was not barred by section 25 of the Act of 1976 (the re-enactment of the section 24 of the Act of 1954) from making the assessments. The judgment of the Court of

Appeal which was delivered by Richardson J. found it convenient to refer to the provisions of the 1976 Act rather than to the corresponding provisions of the 1954 Act and their Lordships are content to do likewise.

It is now necessary to examine the relevant provisions of the 1976 Act in detail. Section 9, which imposes the duty on a taxpayer to make annual returns, is in the following terms:-

" 9. Annual returns by taxpayers - Subject to this Act or any regulations under this Act, every taxpayer shall for the purposes of the assessment and levy of income tax furnish to the Commissioner in each year a return or returns in the prescribed form or forms setting forth a complete statement of all the assessable and non-assessable income derived by him during the preceding year, together with such other particulars as may be prescribed."

"Assessable income" is defined by section 2 as "income of any kind which is not exempted from income tax otherwise than by way of a special exemption expressly authorised as such by this Act". In calculating assessable income, expenditure or loss incurred in the production of that income may be taken into account (section 104).

Section 19 which imposes the duty on the Commissioner to make assessments is in the following terms:-

" 19. Commissioner to make assessments - From the returns made as aforesaid and from any other information in his possession the Commissioner shall in and for every year, and from time to time and at any time thereafter as may be necessary, make assessments in respect of every taxpayer of the amount on which tax is payable and of the amount of that tax."

Section 23 deals with amendment of assessments in the following manner:-

" 23. Amendment of assessments - (1) The Commissioner may from time to time and at any time make all such alterations in or additions to an assessment as he thinks necessary in order to ensure the correctness thereof, notwithstanding that tax already assessed may have been paid.

(2) If any such alteration or addition has the effect of imposing any fresh liability or increasing any existing liability, notice thereof shall be given by the Commissioner to the taxpayer affected."

Section 25 which is relied upon by the taxpayers provides:-

" 25. Limitation of time for amendment of assessment - (1) When any person has made returns and has been assessed for income tax for any year, it shall not be lawful for the Commissioner to alter the assessment so as to increase the amount thereof after the expiration of 4 years from the end of the year in which the assessment was made.

(2) Notwithstanding subsection (1) of this section, in any case where, in the opinion of the Commissioner, the returns so made are fraudulent or wilfully misleading or omit all mention of income which is of a particular nature or was derived from a particular source, and in respect of which a return is required to be made, it shall be lawful for the Commissioner to alter the assessment (being an assessment made on or after the 1st day of April 1958) at any time so as to increase the amount thereof."

Section 29 requires the Commissioner to give notice to the taxpayer after an assessment has been made and is in the following terms:-

" 29. Notice of assessment to taxpayer - (1) As soon as conveniently may be after an assessment is made the Commissioner shall cause notice of the assessment to be given to the taxpayer:

Provided that where -

- (a) The taxpayer has, in his return to which the assessment relates, calculated the amount on which tax is payable or the amount of the tax; or
- (b) The assessment has been made on default by the taxpayer in furnishing any return for the year to which the assessment relates; or
- (c) The Commissioner causes a separate statement in relation to the assessment to be given to the taxpayer setting forth the amount on which tax is payable and the amount of the tax, -

it shall not be necessary to set forth in the notice of the assessment any particulars other than particulars as to the amount of tax to be paid by the taxpayer or the amount of tax to be refunded, as the case may require.

(2) The omission to give any such notice shall not invalidate the assessment or in any manner affect the operation thereof."

The issue between the parties is whether the determinations, to use a neutral word, by the

(2) Any taxpayer who satisfies the Commissioner that he has, in any income year, incurred a loss shall, subject to this section, be entitled to claim that the loss be carried forward and deducted from or set off against the assessable income derived in the first income year after the income year in which the loss was incurred, so far as that income extends, and, so far as it cannot then be deducted or set off, be deducted from or set off against the assessable income derived in the next income year, and so on."

It was as a result of the application of 188(2) that the prior losses incurred by the taxpayers resulted in nil determinations in the years 1976 and 1977. Mr. Jenkin argued that the distinction between assessable income and taxable income was crucial to section 188(1). If section 188 had intended that a loss could be a subject of an assessment, the set off in subsection (2) would have been against taxable and not assessable income. Their Lordships consider that this argument is unsound and that in any event the terms of section 188 cannot assist in the proper construction of sections 19 and 25. It is purely fortuitous that the new determinations in this appeal arose as a result of the application of section 188; they could equally well have arisen because the taxpayers had made a loss in the year of assessment or because their assessable income had been exactly reduced to nil by the special exemptions.

Mr. Jenkin next argued that section 38 contemplated that there could only be a year of assessment in relation to a taxpayer when he had taxable income. Section 38 so far as relevant for this argument is in the following terms:-

"... (2) Subject to this Act, income tax shall be payable by every person on all income derived by him during the year for which the tax is payable.

(3) The year in which income is so derived is in this Act referred to as the income year, and the year for which income tax is payable is in this Act referred to as the year of assessment."

If income tax was not payable by a taxpayer for a particular year then that year could not be a year of assessment and therefore no assessment had been made upon it. Their Lordships reject this argument. Section 9 requires the taxpayer to make a return of all income assessable or not derived during the preceding year (emphasis added), and subsection (3) draws a distinction between the years in which income is derived and assessed. Income is derived in one year which is the income year and the tax is assessed in another year, probably the following, which is the year of assessment. If in subsection (2) the words "during the year" etc are read with "shall be payable" rather

than with "income derived" the whole thing falls into place and the subsections cannot bear the construction which Mr. Jenkin seeks to place upon them. There can still be a year of assessment although the relevant income year produces no income upon which tax is payable.

Finally, Mr. Jenkin referred to section 21 which provides *inter alia* that "if any person makes default in furnishing any return" the Commissioner -

"... may make an assessment of the amount on which in his judgment tax ought to be levied and of the amount of that tax, and that person shall be liable to pay the tax so assessed, save in so far as he establishes on objection that the assessment is excessive or that he is not chargeable with tax."

He submitted that the final eight words of the section showed that if a person had a nil tax liability no assessment should be made upon it. Their Lordships do not so construe these words. They appear to have been intended to cover a situation where a person was not a taxpayer at all within the definition in section 2 at the relevant time, e.g., because he had by then ceased to be an agent or trustee or had never been such, and not to cover the situation where an admitted taxpayer has a nil taxable income.

Reference was also made to the Australian case of *Batagol v. Commissioner of Taxation of Commonwealth of Australia* (1963) 109 C.L.R. 243 where there was a similar issue as to whether an assessment was time barred. However the wording of the statute under consideration was significantly different and their Lordships agree with Tompkins J. that it is not of assistance in this case.

Their Lordships have no doubt that the arguments for the taxpayers are to be preferred and that the Commissioner's statutory duties under section 19 in relation to a taxpayer's return extend not only to the production of a result which produces taxable income but also to results which produce a nil return or a loss. Any other construction would produce the anomalies and illogicalities already referred to. Whichever of these three results the Commissioner arrives at he has made an assessment for the purposes of section 19 and hence section 25. It is to be noted that the latter section uses the words "assessed for income tax" that is to say "for the purposes of income tax" rather than "to income tax". Their Lordships cannot do better than quote the following passage from the judgment of Tompkins J.:-

"In my opinion the expression 'make assessments' in the context of s 17, means the process by which the Commissioner carries out his statutory obligation to ascertain the amount on which tax is payable and the amount of tax. I find nothing in the section, nor in the statutory scheme to justify

a conclusion that the Commissioner only makes an assessment where he determines that there is tax payable. A conclusion that there is no amount on which tax is payable and that as a consequence there is no tax payable involves making an assessment from the returns and other information in his possession just as much as if the result of the assessment were to find that there was an amount on which tax was payable and consequently there was tax payable." (The reference is to section 17 of the Act of 1954 which was later replaced by section 19 of the Act of 1976).

In reaching this conclusion their Lordships are fortified by two further considerations. In the first place the purpose of section 25(1) is to achieve finality and to enable the taxpayer and the Commissioner to close the books and dispose of their papers after the stipulated period. The exercise required to be carried out by the Commissioner in terms of section 19 is capable of producing three different results namely (1) that the taxpayer has taxable income, (2) that he has no taxable income, and (3) that he has a loss which he may carry forward in terms of section 188. To accept the argument of Mr. Jenkin and the reasoning of the Court of Appeal would mean that only in the first instance would finality be achieved whereas in the other two the Commissioner could reopen his determination at any time in the future. A result which would appear to be "contrary to the spirit of section 25", to quote the words of Cooke J. at page 430 in *C.I.R. v. V.H. Farnsworth Limited* [1984] 1 N.Z.L.R. 428.

In the second place the provisions of Part III of the Act headed "Objections to Assessments" envisage that such objections will be dealt with by the Taxation Review Authority, a body particularly experienced in taxation matters. It would be entirely logical that the legislature should have intended that all matters involving determinations by the Commissioner consequent upon receipt of a taxpayer's return as to tax payable or not payable should be dealt with by that body. Such a result would follow from the conclusions which their Lordships have reached. If on the other hand Mr. Jenkin's argument were correct it would mean that the determinations by the Commissioner resulting in a nil payment of tax or in a loss could only be challenged by a taxpayer in the ordinary courts by judicial review or some other legal process. This would appear to defeat substantially the purpose of Part III.

It only remains to refer to one further matter to which the Court of Appeal had some regard namely the amendment to section 19 occasioned by section 20 of the Income Tax Amendment Act 1980. The amendment of section 19 required the Commissioner to make determinations of losses and provided that such

determinations were to be treated as assessments. This amendment, it was said, reflected the common understanding in income tax practice that a letter confirming the assessment of the amount of a loss to be carried forward under section 188 was not an assessment. It is noteworthy that the amendment does not deal with a situation where there is no loss but simply no taxable income. Had the construction of the relevant section of the 1976 Act been *in dubio* it might have been appropriate to turn to the amendments for assistance. However, as their Lordships are of the opinion that the construction and intention of those sections are clear, it follows that that construction cannot be affected by the later amending Act.

Their Lordships will therefore humbly advise Her Majesty that this appeal should be allowed, the order of the Court of Appeal set aside and the order of Tompkins J. restored. The respondent must pay the appellants' costs in the Court of Appeal and before their Lordships' Board.

