



Who's debt?



Hands up those who prepare a set of company accounts showing a shareholders current account in the name of the husband and wife who are shareholders of the company?

Can we be so bold as to assume most of you raised your hand?

Have you ever thought however of the legal status of the current account if the current account is overdrawn and the business fails?

This issue was the subject of a recent very interesting decision of the High Court.

The Background

A couple formed a company owned by family trust 98%, 1% each by the husband and wife. The wife was not a director.

The accountant set up a current account in the name of the husband and wife which was then overdrawn when the company went into liquidation.

The husband filed for bankruptcy and the liquidator sought to recover the overdrawn current account from the wife.

The drawings from the company had been used to meet family costs such as food, school fees and lifestyle.

The wife was allocated a salary each year along with the husband. From time to time she signed

business papers when asked by the husband but she never saw the business mail, had no idea of the state of the finances and had no active involvement in the running of the company.

Importantly, the wife never discussed the accounting arrangements (including the joint current account) with the accountant and never entered into any formal arrangement with the company to borrow the money. That is, she never agreed to incur a debt.

It was the husband who drew funds from the company, paid the family costs and ensured that the family was provided for.

For her part, the wife assumed that all was well with the company as how else was the husband providing for the family? She simply assumed that it came from income.

The result

Justice Fogarty found that the wife had no contractual obligation for the debt, that is, she was not liable for it. Even though this was a closely held family company, it was a separate legal entity and there was no agreement by the wife to borrow. In the same way that a person could not be liable for a bank overdraft without entering into

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a contract with the bank the wife could not be liable for the current account without a contract with the company. The husband could not making a binding obligation with the family company for his wife.

The liquidator argued that if the wife escaped liability on the joint account due to her lack of knowledge then

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We wish you a safe and enjoyable Christmas.

We appreciate your continued support.



We will be closed from

22 December 2011

to

16 January 2012.



“Caveat fiduciary”

Concern has been expressed in the media recently that Inland Revenue is chasing independent trustees (usually accountants and lawyers) for unpaid tax debt.

Inland Revenue responded that it was not particularly doing so.

The simple message is this - if you are a trustee of a trust you are personally liable for its debts.

When it comes to tax - you cannot contract out of your obligations.

In our view, Inland Revenue would be failing in its duty if it did not chase trustees for unpaid tax of a trust and the so called independent trustee should not get special treatment from it.

Accountants and lawyers who act as trustee have no protection under the law and neither they should.

There seems to be a general misunderstanding as to liability trusteeship carries amongst the professions.

When it comes to GST, a trustee remains liable even after retirement from future GST liabilities

until Inland Revenue is advised that they are retired.

As we understand it, tax debts are not covered by your PI insurance as no one can insure against their personal tax debt.

Our concern for a long time has been that professionals have viewed trusteeship very lightly.

It is a matter of record that a lawyers trustee company took no active involvement in the trust that failed to pay its taxes and was held liable for the tax. Such non-involvement is a blatant breach of trust.

Our only suggestions are - if you don't like the risks - don't be a trustee and if you are a trustee - do your job - get involved.

As much as there are times when we get critical of Inland Revenue and we find it a frustrating organisation - it has a duty to collect tax owing and it cannot (indeed must not) treat accountants and lawyers who are trustees with favour.

The fault does not rest with Inland Revenue or the law.....

Barred?

You will be aware of the 4-year statute bar on the ability of Inland Revenue to increase a tax obligation.

In a recent Adjudication, it held that the statute bar could be lifted because a taxpayer did not disclose in tax returns that a business was not reaching projections and so no business ever commenced - scary!

PRIVACY NOTICE

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ON THE SPOT ADVICE

Our telephone/fax/email consultation service is available to enable practitioners to deal with any questions as they arise.

TAX OPINIONS

Providing fully researched opinions on the taxation effect of transactions.

TAX AUDITS

Reviewing tax compliance requirements (FBT, GST, PAYE etc) to identify any deficiencies prior to any visit from tax inspectors.

TAX DISPUTES

Preparation of responses to disputes with Inland Revenue.

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“commercial affairs in New Zealand would fall into disarray”. Fogarty J disagreed as no arm's length commercial party would rely on a spouse to bind another and the principle should apply to shareholder current accounts.

Your financial statements can label things however you wish - at the end of the day it is the legal position that matters. This case highlights the importance of understanding the implications of actions and provides both opportunity and warning.

As the husband was bankrupt the liquidator got nothing except a bill for the wife's costs to defend the liquidator's claim.