

THE RANK OF TAX IN THE ORDER OF PRIORITY OF DEBTS DURING OFFICIAL LIQUIDATION: THE POSITION OF THE LAW AND PRACTICE

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Abstract

This article examines regulatory framework governing the winding up of insolvent entities, excluding private liquidation where priority of debt is not a material issue. The analysis centers on section 59 of the Revenue Administration Act, which mandates strict timelines for the Ghana Revenue Authority (GRA) to notify liquidators of tax liabilities. In practice, however, the GRA often initiates tax audits that exceed the statutory 14-day window, raising questions about the consistency of this approach with the law's strict construction. The article further explores the definition of 'priority debts', referencing the Corporate Insolvency and Restructuring Act, which classifies debts into categories that determine their ranking relative to taxes. The analysis focuses on the legal and practical alignment of tax legislation with the order of priority for debt payments during official liquidation in Ghana. The findings reveal that taxes do not always take precedence over all other debts, and payment is subject to specified costs outlined in the insolvency legislation. The article concludes by recommending a review of the statutory timelines to better reflect practical realities and reduce potential tax controversies during liquidation.

1. INTRODUCTION

This article aims to provide practical insights into the extent to which tax legislation is aligned with the practice of dealing with the order of priority of debt payment during the official liquidation process as they relate to taxes. The regulatory framework governing the official winding up of entities in Ghana with respect to taxes is also covered. For the avoidance of doubt, private liquidation is not covered in this article as priority of debt is not a material issue in private liquidation because a fundamental pre-condition to trigger a private liquidation is for majority of directors of the company to demonstrate that the company's assets exceed its debts and liabilities through an affidavit of solvency pursuant to section 275 of the Companies Act.¹ Hence, sufficient assets are reasonably expected to be available to defray debts (including taxes) in the course of private liquidation, thereby making priority of debt redundant.

A company is generally incorporated to operate as a going concern into the foreseeable future in accordance with International Financial Reporting Standards (IFRS) 18, unless management intends to liquidate the entity or cease operations, or has no realistic alternative but to do so. However, where a company is unable to pay its debts as they fall due, it is said to be insolvent as can be gleaned from the meaning of being 'solvent' pursuant to the First Schedule to the Companies Act. As a result, official liquidation may be commenced by a special resolution of the company. Where a company is undergoing an official liquidation, it is unlikely to be able to pay its debts in its entirety during the winding-up process. This is because, from the outset, it was considered insolvent. As a result, the issue of priority of debt during an official winding up becomes a significant matter, unlike under a private liquidation.

1. The position of the tax law and practice with regards to priority of debt during official liquidation

To answer this question, the applicable provision pivotal in addressing the issue is section 59 of the Revenue Administration Act.² In sum,

- a. *the liquidator must comply with a 14-day notice threshold to the Commissioner-General (CG) of the Ghana Revenue Authority (GRA). However, the notice period could be earlier if the liquidator took possession of the assets of the company earlier;*

¹ Companies Act 2019, Act 992 (as amended) 'Act 992'.

² Revenue Administration Act, 2016, Act 915 (as amended) 'Act 915'.

- b. *the CG has a 14-day period to serve the liquidator with notice of tax payable, if any, after receipt of the notice;*
- c. *the liquidator must subsequently give an account of the assets of the taxpayer to the CG; and*
- d. *the liquidator must prioritise payment of tax payable relative to other debts, save **priority debts**, failure of which the liquidator assumes personal liability for the tax.*

In practice, however, following from the notice to the CG under ‘a’ above, the CG is more likely than not to undertake a tax audit into the affairs of the entity, as the outstanding amount of tax payable may not be readily known at the time of receipt of notice. The CG may not have the necessary information to make a reasonable estimate of the tax. As a result, in my experience, the CG’s notice under ‘b’ above could be a trigger point for a tax audit by notifying the liquidator of the audit. Further, the duration of a tax audit may be 2 months (or marginally more or less), depending on factors such as the complexity of the entity under liquidation, the number of open tax years, and the flow of documentation from the taxpayer as may be requested by the tax auditors.

In my opinion, the above practice of the CG initiating a tax audit, in the first instance, to determine an amount payable appears to be inconsistent with the strict reading of section 59(4) which provides as follows:

The CG shall within fourteen days of receiving a notice under subsection (1) serve the receiver with a written notice specifying an amount that appears to the CG to be sufficient to provide for tax due or that will become due by the taxpayer.

Tax laws are strictly construed in Ghana pursuant to the holding of the Supreme Court in *MultiChoice Ghana Limited v. Internal Revenue Service*.³ Ergo, one may want to subject section 59(4) of Act 915 - which appears to tie the hands of the CG to strict timelines in providing a response and the determination of tax assessment, if any - to strict interpretation. Section 59(4) says in part that ‘the CG **shall** within fourteen days ... serve the receiver with a written notice **specifying an amount** that appears to the CG to be sufficient ...’.⁴ In my opinion, the use of ‘shall’ is more likely than not to be interpreted by Ghanaian Courts to mean that the CG is mandatorily required to respond within 14 days. Does it mean that the CG is

³ [2010-11] SCGLR 783.

⁴ Emphasis mine.

statute-barred from making an assessment after the 14-day threshold? The law further requires the CG to provide ‘written notice **specifying** an amount’ in his response. Does it mean that the CG must necessarily include the assessed amount in the said notice and that failure to do likewise bars the CG from making an adjusted assessment because of lapse of time?

In the case of *Eastleigh Mall Limited v. Commissioner of Investigations & Enforcement*⁵, the High Court of Kenya had to deal with mandatory terms under section 51(11) of the Kenya Tax Procedures Act⁶ which provides that ‘the Commissioner shall make the objection decision within sixty days from the date of receipt of a valid notice of objection, failure to which the objection shall be deemed to be allowed’. The High Court of Kenya said that the provisions of the said section 51(11) of the Kenya Tax Procedures Act are in mandatory terms, and the timeline is not a mere procedural technicality.

The question is, how will the Ghanaian Courts construe section 59(4)? Thus, where, for example, the CG fails to provide an amount in his written response to the receiver but seeks to undertake an audit to confirm same, will it make any subsequent tax assessment arising from the tax audit defective by reason only of the fact that the CG is time-barred from making an assessment after the 14 days?

In my opinion, the Ghanaian Courts are more likely than not to align with the Kenyan decision, considering tax laws are construed strictly in Ghana and non-compliance with procedure is not considered lightly by the Courts especially where it relates to fundamental matters including breach of the Constitution, 1992, breach of natural justice, failure to comply with substantive law and the jurisdiction of the court as indicated in the case of *The Republic v The High Court Ex parte, Allgate Company Limited (Amalgamated Bank - Interested Party)*⁷ In this case of section 59(4), the non-compliance with the 14-day threshold, in my opinion, goes to jurisdiction of the CG to make an assessment after the 14 days.

It seems section 59(4) is at variance with the practicality of the duration required to determine the correct amount or estimated amount of tax payable as a tax audit is a necessary mechanism for such a determination. And there is no leeway under the said section to cloth the CG with the power to have additional time to decide on a correct or estimated tax amount. Thus, at worst, the CG may have to make

⁵ [2023] KEHC 20000 (KLR).

⁶ Kenya Tax Procedures Act, No.29 of 2015 (as amended).

⁷ Suit No. CM/Tax/0118/2022.

a reasonable estimate of tax within the set timeline. This could be gleaned from the phrase ‘... notice specifying an amount that **appears** to the CG ... that **will become due**...’⁸ as that entitles the CG to make a judgement call based upon information available to him at the time of responding to the notice. It seems to me that the strict construction of the provision does invite the CG to make baseless assessment (within the limited time) and shift the burden to the taxpayer to prove otherwise.

Flowing from the above, the question is, is the practice of undertaking an audit before confirming the correct amount inconsistent with the strict construction of the law? It appears the response is in the affirmative as explained above.

I now deal with the vexed question of **what constitutes the ‘priority debts’** referred to in Act 915?

Unfortunately, Act 915 did not specify what constitutes priority debt. In the case of *Orica Ghana Ltd v. Commissioner-General of the Ghana Revenue Authority*⁹ when the High Court was faced with what constitutes ‘manufacturing’ as mentioned in the Income Tax Act¹⁰ the Court relied on the meaning provided for in the Minerals and Mining Regulations¹¹ as Act 896 did not define it. The reliance on L.I. 2177 stemmed from the fact that Orica Ghana Limited’s activity was regulated by applicable mining laws. Therefore, ‘manufacturing’ had to be given its industry or technical meaning under the circumstances in the resolution of the first issue before the Court. Corollary, to the extent that the official liquidation process is governed by the Corporate Insolvency and Restructuring Act¹² reliance may be placed on the meaning of priority of debts provided for under section 107 of Act 1015, as Act 915 did not define priority of debts. Section 107 provides for the classification and priority of debts as follows:

(1) (...)

(2) *A debt shall be classified according to the ranking specified in subsection (3).*

(3) *A debt classified as a*

⁸ Emphasis mine.

⁹ *The Republic vs. The High Court Ex parte, Allgate Company Limited (Amalgamated Bank - Interested Party)* 2007-2008 SCGLR 1041.

¹⁰ Income Tax Act, 2015, Act 896 (as amended) ‘Act 896’.

¹¹ Minerals and Mining Regulations, 2012, L.I. 2177 ‘L.I. 2177’.

¹² Corporate Insolvency and Restructuring Act, 2020, Act 1015 ‘Act 1015’

- (a) **Class A** debt is a debt in respect of Post-Commencement Financing which takes priority over all other creditor claims including secured and preferential class and shall be paid in full;
- (b) **Class B** is a preferential debt which
- (i) ranks equally between other preferential debts against the estate of the company;
- (ii) shall be paid in full unless the remainder of the estate is insufficient to meet the preferential debt in which case the preferential debt shall be paid in equal proportions; and
- (iii) is debt or part of a debt which answers to either of the following descriptions:
- (aa) remuneration owed to an employee of the company regarding employment during the whole or a part of the four months preceding the date of commencement of administration or winding-up; or
- (bb) **rates, taxes or similar payments** owed to the Republic or a local authority which have become due and payable within the year preceding the date of the commencement of administration or winding-up
- (c) - (h) (...).¹³

Flowing from the above, and for the purpose and context of this article, the debt priority classification under Act 1015 is put under three categories:

- (I) *Category 1 - Specified expenses that have priority over taxes.*
- (II) *Category 2 – Specified expenses that have equal weighting as taxes.*
- (III) *Category 3 – Specified and other expenses that are weighted below taxes.*

With regards to Category 1 expenses (Class A), it refers to costs incurred on employee costs and company finance obtained during the liquidation process. For Category 2 (Class B), it covers costs payable to employees which were outstanding within the 4 months preceding the winding up, and taxes due within a year preceding the winding up. These category 2 costs are paid proportionately, *pari passu*, to the extent that available funds are unable to fulfil the outstanding debt. For category 3, which covers Classes C to H, it kicks in where available funds exceed amounts payable under Classes A and B. It could, therefore, be

¹³ Emphasis mine.

realised that taxes do not have priority over all debts. Thus, payment of taxes is, by operation of law, subject to other specified costs as contemplated under section 59(5) & (6) of Act 915.

2. CONCLUSION

In conclusion, the analysis herein demonstrates that Act 915 must be read together with Act 1015 to determine the priority of debts (as mentioned in Act 915) before payment of tax due by the liquidator. However, the practice of the CG conducting an audit to determine the correct amount payable by an entity in liquidation, which is likely to take more than 14 days, does not seem to align with the strict construction of the provisions in section 59(4). This calls for a review of section 59 to mitigate potential tax controversy that may arise because of the seeming limitation of time within which the CG has to make an assessment during liquidation. A reasonable and specific timeline of say 60 days (akin to the time allowed the CG to make a decision upon receipt of a refund application) - with the possibility of additional 30 days following a notice to the liquidator- will appear fair and practical.