Corporate Tax Association 2011 GST Corporate Intensive

Twenty Five Years of Tax Cases in the AAT;
Eleven years of the "practical business tax"

Venue: The Grace Hotel, Sydney

17 October 2011

The Hon. Justice Garry Downes AM
President of the Administrative Appeals Tribunal

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Twenty Five Years of Tax Cases in the AAT

On 1 July 1986 the *Administrative Appeals Tribunal* assumed the taxation jurisdiction which had previously been conferred on Taxation Boards of Review. On 1 July last the Tribunal had accordingly been hearing tax cases for 25 years.

Most of the members of the Boards became members of the Tribunal. These included Harry Stevens, the legendary chairman of the No. 1 Board, who became a senior member, but remained for only a short time. Dr Paul Gerber, who had been a member of the No. 3 Board, became the powerhouse behind the taxation jurisdiction of the Tribunal and made a significant contribution to the high reputation the Tribunal has in tax matters today. Other former members of the

Boards of Review who made significant contributions to the Tribunal include Keith Beddoe, who had been Chairman of the No. 3 Board and Dean Trowse who had been with the No. 2 Board. Both Keith Beddoe and Dean Trowse stayed with the Tribunal until 2004, giving nearly 20 years' service to the Tribunal. Dr Gerber became a deputy president and remained with the Tribunal until 1999.

The Tribunal accordingly began its taxation jurisdiction with a distinguished group of taxation specialists. That position has continued throughout its 25 year history. In Melbourne, Bruce Pascoe, a retired senior member, was and is extremely highly regarded by tax lawyers. So too is Deputy President Julian Block, who retires shortly. Graham Hill once told me he was one of the best tax lawyers he knew.

The present Tribunal is not short of tax lawyers. They include, of course, Federal Court judges such as Justice Edmonds. The present taxation specialists in the Tribunal include Stephen Frost in Sydney, Frank O'Loughlin in Victoria, Deputy President Hack SC and Peter McDermott in Queensland, Rodney Dunne in South Australia and Andre Sweidan and Chelsea Walsh in Western Australia.

Depending upon fashions in tax avoidance, the numbers of taxation cases in the Tribunal fluctuate significantly. However, the last year or so does not seem to have included any irregular spike in appeals. In 2010-11, 1,103 cases were instituted in the Taxation Appeals Division of the Tribunal. One thousand two hundred and fifty one cases were finalised during that year and 1,429 were current at the year's end. The total filings in the Tribunal for the year were 6,179. The figures for 2009-10 are not significantly different, except that 2,008 cases were finalised during the year, partly representing the tail of some scheme cases. By contrast, 171 taxation matters were filed in the Federal Court. This is out of total fillings of 3,642 for 2009-10. Three hundred and five taxation cases were current in the Federal Court as at 30 June 2010. On these figures, which for both

the Court and Tribunal, include bulk cases, tax cases represent about 5% in the Court and nearly 20% in the Tribunal.

Many smaller tax cases are filed in the Tribunal, but the Tribunal still hears a significant number of large to very large corporate tax cases. *News Australia Holdings Pty Ltd and Commissioner of Taxation,*[1] relating to the capital gains tax consequences of the News Group's relocation to Delaware, comes to mind, as does *Qantas Airways Ltd and Commissioner of Taxation*[2] and two recently heard GST appeals in the Tribunal's Melbourne registry.

The significance of the Tribunal's jurisdiction is such that the Government has recently agreed to the appointment of two additional deputy presidents to hear taxation cases in the Tribunal. There will be two deputy presidents and a senior member specialising in taxation in Sydney and one deputy president and a senior member in Melbourne. These appointments, of course, will confirm the Tribunal's taxation experience at the highest level in all its registries so that, using the words of its statutory obligation,[3] it will be able to bring to the corporate community, as well as individuals, the highest level of "fair, just, economical, informal and quick" resolution of taxation disputes.

The ultimate question for the Tribunal in taxation cases is the same as that for the Federal Court. The issue in the Tribunal[4] and the Federal Court[5] is whether the taxpayer has satisfied

> *the burden of proving that:*
>
> *(i) if the taxation decision concerned is an assessment (other than a franking assessment) – the assessment is excessive; or*
>
> *(ii) if the taxation decision concerned is a franking assessment - the assessment is incorrect; or*
>
> *(iii) in any other case – the taxation decision should not have been made or should have been made differently*

[1] (2009) 75 ATR 971, [2009] AATA 750.
[2] (2010) 119 ALD 199, [2010] AATA 977.
[3] *Administrative Appeals Tribunal Act 1975* (Cth) s 2A.
[4] *Taxation Administration Act 1953* (Cth) s 14ZZK(b).
[5] *Taxation Administration Act 1953* (Cth) s 14ZZO(b).

There is, however, a major difference between the two jurisdictions because the Tribunal is generally authorised to exercise afresh the discretions which are given to the Commissioner, while the Federal Court is bound by those decision unless the Commissioner "exercises his discretion capriciously, or fancifully, or upon irrelevant or inadmissible grounds".[6]

The Tribunal has this discretionary power because s 43(1) of its Act confers on the Tribunal "all the powers and discretions that are conferred on…", relevantly, the Commissioner. The exercise of the powers is, however, limited to "the purpose of reviewing the Commissioner's objection decision".[7]

Because making findings of fact can be mixed up with discretions, the best course seems to be to bring cases in the Tribunal, at least when there is a discretion involved or when there are disputed questions of fact.

There are, of course, other advantages in bringing tax cases in the Tribunal. The most important, to corporate taxpayers, can be confidentiality.[8] The fact that adverse costs orders are not made against unsuccessful applicants in the Tribunal can be another advantage.

The Tribunal, of course, has the obligation to correctly determine the applicable law and to apply it properly so that an application in any case will be effectively brought in the Tribunal, whether it raises questions of fact or law or both; however much is at stake and however difficult the case will be.

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[6] *The Australasian Scale Company Limited Appellant v The Commissioner of Taxes (Queensland)* (1935) 53 CLR 534, 555.
[7] *Liedig v Federal Commissioner of Taxation* (1994) 50 FCR 461, 464, [1994] FCA 1058, [12]; see also *Shi v Migration Agents Registration Authority* (2008) 235 CLR 286 esp at 324,5 per Kiefel J.
[8] *Taxation Administration Act 1953* (Cth) ss 14ZZE, 14ZZJ.

I have been involved in the process of selection of the new taxation specialist members of the Tribunal. I expect that the appointments of the highest quality will be made before the end of the year. With its new compliment of specialist members joining the current group I hope that the Tribunal will be able to offer efficient and informal, yet high quality, service to taxpayers at all levels, who are not satisfied with decisions of the Commissioner.

Eleven Years of the "Practical Business Tax"

Are we clear about what is a "supply"?

It has always intrigued me that, in an income tax act of more than three thousand pages, the core concept of "income" is not defined. It demonstrates, more than anything else, that income tax legislation began with a simple proposition: "that income will be taxed" and developed largely as a response to attempts to arrange affairs so that receipts were not income.

Value added tax, or goods and services tax as it is called in Australia, does not exactly fit this mould, although it is still based on a simple idea. The idea is to tax the supply of goods and services to consumers. The complicating factor is the need to avoid "cascading", or multiple taxation, which either leaves a continuing burden on businesses, as progressive supplies are taxed through a chain, or heaps it all on the consumer, at the end. But this complexity does not impact on the simple question of what is a supply.

Just as the concept of "income" is left undefined in the *Income Tax Assessment Act 1997* (Cth), so the concept of "supply" is largely left undefined in the *A New Tax System (Goods and Services Tax) Act 1999* (Cth).

These considerations have led to an important notion underlying tax law, particularly where fundamental concepts such as "income" and "supply" are

involved, that primary reference should be made to common law concepts underpinning the legislation in determining how the legislation should be applied.

A related concept which applies to GST is the idea that GST is a "practical business tax" which should be applied in a practical way. The description "practical business tax" was first given by Stone J in the Federal Court in *Sterling Guardian Pty Ltd v Federal Commissioner of Taxation*[9]. The description recognises that, although the burden of the tax is ultimately borne by consumers, "in terms of 'imposition, collection and administration', it is a tax on business".[10] The phrase was used by the Judge in the following context:[11]

> *The clear thrust of the GST Act, both in its wording and as explained in the explanatory memorandum, is that of a practical business tax imposed with respect to elements of commerce.*

Because the business nature of the tax relates to its "imposition, nature and collection", rather than its burden, the references to the practical nature of the tax emphasise this nature as an aspect of its administration and collection and not of its burden.

Stone J returned to the theme in the Full Court in *Saga Holidays Ltd v Commissioner of Taxation* in a judgment in which Gyles and Young JJ agreed. She said: [12]

> *The court has tended to adopt a purposive approach to the interpretation of the GST Act, rejecting strict grammatical analyses in favour of a consideration not only of the syntax but also of 'the policy and the surrounding legislative context" of the relevant provision:* HP Mercantile Pty Ltd v FCT (2005) 143 FCR 553 at 568[66]*. Consideration of these aspects of the GST Act has led to the tax being described as "a practical business tax":* Sterling Guardian Pty Ltd v FCT (2005) 60 ATR 502*.*

[9] (2005) 60 ATR 502, 514;[2005] FCA 1166, [39].
[10] Ibid.
[11] Ibid.
[12] (2006) 64 ATR 602, 610; [2006] FCAFC 191, [29].

Context and purpose are important. A construction which is unworkable or even one which does not advance the policy or purpose of the Act, is generally to be avoided.

The twin characteristics of a culture of interpretation steeped in the underlying common law associated with ideas of the practical business nature of the tax, on the one hand, and legislative provisions of great detail and complexity, on the other, lead to some challenging issues in tax law. Exactly how a determination is to be made as to what is a supply, and whether there has been a supply in a particular case, still seems to me to be subject to some fundamental uncertainty.

Aspects of these issues have been thrown up by a recent decision of the Full Federal Court. I know it well because the Court unanimously overruled me. The name of the case is *Qantas Airways Ltd and Commissioner of Taxation*.[13] At first I thought this decision might best be left as "the elephant in the room" for my talk today, but I ultimately decided that the elephant was too big to ignore! I can note, however, that the Commissioner has applied to the High Court for special leave to appeal.

The reason why *Qantas* is important is that it addresses the fundamental question of what is a supply in circumstances which do not involve complex or unusual circumstances. It may then provide guidance which will be useful in a range of cases, particularly if the High Court ultimately determines it.

There are already a significant number of GST cases dealing with what is a supply. Two of them are decisions of the High Court. In *Federal Commissioner of Taxation v Reliance Carpet Co Pty Ltd*[14] the Court held that a supply had been made on the making of a contract for sale of land. It relied upon the statutory

[13] (2010) 119 ALD 199, [2010] AATA 977; [2011] FCAFC 113.
[14] (2008) 236 CLR 342.

definition. In *Travelex Ltd v Federal Commissioner of Taxation*[15] the Court held that a purchase of foreign currency involved a supply in relation to the rights that attach to ownership of the currency. Again, the definition was considered important. French CJ and Hayne J referred to arguments put in the Full Federal Court about an approach which required the Act to be addressed from "a practical and business point of view" without apparent disagreement, but also without express endorsement.[16] The important question may be how the High Court approaches this issue in practice.

The question in *Qantas* was whether a supply occurred when a potential traveller made and paid for an airline booking. Qantas claimed a refund when a passenger cancelled or did not show and no refund was claimed or paid. The Full Court said that the only supply was the actual journey and when that did not occur there was no supply. *Qantas* was decided in the Full Court almost exclusively by reference to the ordinary meaning of the word "supply", without regard to the statutory definition. The decision was facilitated by the apparent acceptance by the Commissioner that there was only one supply.

The reason *Qantas* seems to me to throw up the challenges I have been referring to is because the Court decided the case by considering what the one supply was and it did this, as I see it, without looking at the definition of supply in the Act and, ultimately, without determining whether or not there was a contract. Again, this approach might have been made easier because the arguments put on behalf of the Commissioner apparently did not depend on a determination of these issues.

[15] (2010) 241 CLR 510.
[16] Ibid 519.

In the Tribunal, the first matter addressed was the extended definition of supply in the Act and particularly that part which provides that "an entry into… an obligation… to do anything" is a "supply".[17]

The Federal Court considered this to be "back to front".[18] The Court preferred to look at the ordinary meaning of supply. The Court looked at "the essence, and whole purpose, of the transaction" which was "[t]he prospective supply… of air travel, dare we say, in the face of *Reliance Carpet (at [13])*, 'nothing more or less'." [19] That concluded the matter because, since there was ultimately no journey, there never was a supply.

I note in passing that the Court commented on the Tribunal's distinguishing of the UK legislation from the Australian legislation, the distinction being that the Australian legislation did, and the UK legislation did not, have a definition extending supplies to an obligation to do anything. The Court could not see a reason for the Tribunal referring to this. What you may not know is that senior counsel for Qantas, both in the Tribunal and in the Federal Court, was an English silk. I know him well. We are both members of the same set of London chambers. I will leave you to ponder whether the Tribunal made the remark because it thought that counsel for Qantas might have been viewing the matter with a mindset developed from the English legislation and that this might have been inferred from the Tribunal's remarks.

To return to my theme, however, it seems to me that it must be the idea that GST is a practical business tax, which needs to be applied by reference to the policy behind it, which lies behind the position, both of the Federal Court and, apparently, the Commissioner, of leaving the case for determination by reference to the ordinary meaning of supply, without regard to the apparent statutory intention to extend supply to obligations to do something. Whether it is better to

[17] *A New Tax System (Goods and Services Tax) Act 1999* (Cth) s 9-10(2)(g).
[18] *Qantas Airways Ltd v Commissioner of Taxation* [2011] FCAFC 113, [5].
[19] Ibid [56].

deal with a statutory definition first or last may be a moot point, but I venture to suggest that it is only in a GST case that it might be thought appropriate not to deal with it at all.

So is there a different regime for the interpretation of the GST Act? Is there some overriding policy which the Act must conform to? This question was asked by Michael Wigney SC in a recent paper.[20] Having referred to occasions which he said had "not always been encouraging" in which he had submitted to judges that the GST Act "should be construed and applied in a broad and practical, not narrow and technical way" he posed the question "is there any reason or basis for construing the GST Act in a way different to other legislation?".[21] He answered the question firmly in the negative, but recognised that the nature of the tax as a practical business tax could inform the interpretation of the GST Act through "application of the general principles and canons of construction that apply to all legislation".[22] I agree.

What is the scope for such an approach? First, the conclusion that there cannot be a different basis for interpreting the GST Act means that the scope is somewhat limited. The words of the Act cannot be passed over in favour of a general policy of the Act. Secondly, a question arises as to the extent to which practical considerations or an understanding of the policy of the Act can affect the interpretation of sections of the Act. In *Qantas,* for example, there might be competing policy questions. On the one hand a policy to confine the tax to the essence of a supply might be practical. On the other hand, accepting that GST will often be collected and paid before the essential supply occurs, as was the case in *Qantas*, practical considerations might be thought to include whether GST should be refunded to a supplier where it has already been collected and paid and where it will not be refunded to the consumer.

[20] Michael Wigney SC, 'Text, context and the interpretation of a "practical business tax"' (2011) 40 *Australian Tax Review* 94.
[21] Ibid 95.
[22] Ibid.

The question will, however, ultimately be answered by the High Court, perhaps in *Qantas*. What can we say about the answer that might be given? Mr Wigney gave a qualified assessment which left room for a practical business approach in the High Court in the future. He looked at a number of GST cases, both in the High court and the Federal Court, before arriving at this conclusion. Mr Wigney may be right. It seems to me, however, appropriate to look as much at cases in the High Court which indicate the thinking of the Court generally, in answering the question, as it is to look exclusively at GST cases.

Recent trends in the High Court do not suggest to me that the response of the High Court, to an argument that policy and practicality rule, will be very "encouraging": to echo Mr Wigney.

I have four things in mind. To begin with, the Court's decision in *Commissioner of Taxation v Reliance Carpet Co Pty Ltd*[23] was rooted in the words of the definition of "supply". This was "the Gleeson Court" which one would expect to give full weight to commercial arguments. The decision in *Travelex Ltd v Federal Commissioner of Taxation*[24] is no different, notwithstanding the remarks quoted above. The majority judgment of French CJ and Hayne J begins by exploring the definition of "supply" in the Act.[25] Secondly, moving away from the tax cases, there may be a trend in the Court to rethink its previous tendency to give statutes a purposive construction. This was the theme of a recent paper written by the former New South Wales Chief Justice, James Spigelman.[26] Incidentally, he concluded "that the basic principles do not appear to be in dispute. It is in the application of these principles that differences emerge."[27] The thoughts I am expressing may be a surer guide to application than an examination of the strict

[23] (2008) 236 CLR 342.
[24] (2010) 241 CLR 510.
[25] Ibid 516.
[26] The Honourable J J Spigelman AC, 'The intolerable wrestle: Developments in statutory interpretation' (2010) 84 *Australian Law Journal* 822.
[27] Ibid 831.

principles. Thirdly, the Court has generally not shown a ready acceptance of arguments in public law cases calculated to advance practical considerations over the words of a statute. This approach is very much linked to the emphasis which the Court places on the constitutional separation of powers and the role of "Chapter III Courts" in the constitutional structure. In *Corporation of the City of Einfield v Development Assessment Commission,*[28] for example, the Court rejected the United States doctrine of "deference" to formal interpretations of US statutes by the executive agencies. This approach of the Court appears ultimately to be steeped in its separation of powers doctrine – only a court can authoritatively determine the law - but the general reasoning might preclude an approach which does not ultimately give full weight to the words of the parliament as binding. If stating the law is the exclusive function of a court, the implication is that the law will not depend so much on policy, which is not the preserve of judges, but on the interpretation of the words of the legislative branch of government, the parliament, which is the preserve of judges. Fourthly, the Court has shown a reluctance to embrace commercial and business arguments when they conflict with what it regards as the essential requirements of the administration of justice. An example is its recent approach to international arbitration. In *Esso Australia Resources Ltd v* Plowman[29] the Court decided that absolute confidentiality of documents and information was not a characteristic of arbitrations in Australia, although the principle was widely accepted, for commercial reasons, in many overseas jurisdictions. The Court very recently limited the idea, which is a very prominent commercial imperative in arbitration, that courts should be restrained in interfering with arbitral awards. The court held that arbitrators in an international arbitration had not given adequate reasons.[30] The commercial arguments in favour of restraint did not find favour with the majority judges (French CJ, Gummow, Crennan and Bell JJ) who found that "judicial power" and "the exercise of public authority" continued to have an

[28] (1999) 199 CLR 135.
[29] (1995) 183 CLR 10.
[30] *Westport Insurance Corporation v Gordian Runoff Ltd* [2011] HCA 37.

important role in governing private international arbitrations.[31] They went on to say, of error of law, that: “an error of law either exists or does not exist; there is no twilight zone between the two possibilities”.[32] That does not seem to encourage an approach to construction which depends on business practicality.

These illustrations are far removed from the interpretation of the GST Act, but the judicial philosophy underlying the decisions does not seem to me to augur well for the Court’s acceptance of a proposition that the nature of GST as a practical business tax should have more than a peripheral effect on the interpretation of the Act.

The GST remains a practical business tax. A construction of the Act which advances that role will generally be preferred to one that does not. There remains, however, a question of what is the outer-reach of an approach to construction which puts emphasis on the essence or nature of the tax. The answer will only come with time and will be contributed to, in no small manner, by future decisions of the High Court. My assessment is that, although the Court will pay significant regard to practical and commercial arguments, its position as the constitutional Chapter III court, will ultimately cause it to give primacy to the words of the parliament over other considerations.

[31] *Westport Insurance Corporation v Gordian Runoff Ltd* [2011] HCA 37, [20].
[32] Ibid [42].