

***TAX AVOIDANCE AND THE HIGH COURT SINCE
SIR GARFIELD BARWICK
By A. J. MYERS***

Introductory

May I begin this talk with a personal statement! I come to this subject as an almost retired barrister, who used to do a good deal of taxation work, about 20 years ago. However, by way of preparation for this evening I have taken from the shelves every volume of the Commonwealth Law Reports from (and including) volume 110, that is some 116 volumes, and I have scanned or read every case to which, according to the index, the Federal Commissioner of Taxation was a party. My diligence should not be in doubt; nor, I fear, my lack of judgment.

Until about 1973 (and I have not looked up the Commonwealth Acts to check the precise accuracy of this remark), the High Court of Australia had vested in it original jurisdiction to determine references and appeals under the Income Tax Assessment Act 1936 and other Commonwealth taxation legislation. When I came to the Bar in 1975, income tax appeals had started to come to the Supreme Courts. This continued until the Federal Court was established. However, as late as 1976 or 1977, I was engaged as counsel on behalf of the Federal Commissioner of Taxation in a sales tax appeal heard by a single Judge (Murphy J). The matter had been to a Taxation Board of Review, but the so called “appeal” to the High Court was, for constitutional reasons, a fresh hearing of the whole matter.

If one looks through the volumes of the Commonwealth Law Reports during the time Sir Garfield Barwick was Chief Justice, it is not uncommon to see half a dozen income tax cases to a volume. Nowadays, it is not uncommon to see only one tax appeal in half a dozen volumes of the Commonwealth Law Reports.

It is also notorious that income taxation law has become more complex since the time Sir Garfield was Chief Justice. Sir Harry Gibbs has written recently that “the laws relating to income tax are a disgrace”. He refers to legislation which is “absurdly voluminous”, “which is obscure to the point of being incomprehensible”. He refers to “unacceptably wide discretionary powers, including those given by the anti – avoidance provisions of IVA inserted in an overreaction to some earlier decisions of the High Court”. Sir Harry also says that many “practising accountants no longer try to unravel the mysteries of the legislation by reading its provisions. Rather they rely on the various documents and rulings issued by the Australian Taxation Office – a subordination of the rule of law to the opinions of the Executive.”

My purpose in mentioning the extent of the jurisdiction of the High Court in income taxation matters during much of the time Sir Garfield was Chief Justice, the number of income tax matters decided by the High Court during that time and the increasing complexity of income taxation law, is to remind you that the High Court during Sir Garfield’s time was generally more knowledgeable about income taxation law than is the High Court bench nowadays.

The Barwick Court

Sir Garfield was sworn in as Chief Justice on 27 April 1964. It was his third career, having been a leading barrister and afterwards Commonwealth Attorney – General and Minister for Foreign Affairs.

In his memoirs, entitled “A Radical Tory” (The Federation Press, 1995) at p 229,

Sir Garfield Barwick sets out, as plainly as may be, his views upon taxation. He said,

“Criticism from some quarters of my decisions in taxation cases warrants a brief reference to them. They are fairly numerous and relate to many aspects of the assessment of taxation. As I remark elsewhere, the Commonwealth Statute of 1936, which resulted from Mr Justice Ferguson’s efforts and those of David Roper (later Chief Judge in Equity), his assistant secretary, was generally understood and gave no undue difficulty in its administration. It has, however, suffered frequent amendment, so that now it is a patchwork which often lacks consistency. Into the detail of my decisions on this hotchpotch of legislation I will not go, but I will indicate the principle upon which I acted, a principle denied by some politicians but one which is fundamental to the operation of income tax law and has had the endorsement of earlier courts.

The liability to pay income tax is wholly derived from the law imposing and providing for the assessment of that tax. The obligation to pay it is a legal one. Some politicians try to treat it as a moral obligation. But it is not. The citizen is bound to pay no more tax than the statute requires him to pay according to the relevant state of his affairs.

Consistently with this view, it has long been a principle of the law of income taxation that the citizen may so arrange his affairs as to render him less liable to pay tax than would be the case if his affairs were cast in some different form. In the language of the layman, the citizen is entitled to minimise his liability to pay tax. This is sometimes expressed as a right to avoid tax, an expression which is in contradiction to the evasion of tax, a failure to pay tax which is properly due.

On this principle, I regularly acted. Provided the citizen’s transactions were not shams, pretences, the form of his transactions and their legal consequences would affect his liability to tax, even though that form might be unusual and adopted for the express purpose of limiting the liability to pay tax.

I do not countenance fraudulent dealings, or give effect to sham transactions or the destruction of records. But clearly I did not accept the view that there was a moral duty to pay tax. Further, I held the view that it is for the Parliament in passing laws imposing taxation to make its meaning as unambiguously clear

and certain as the use of language will permit. In the event of ambiguity in such legislation, the citizen, not the executive government, should have the benefit of that construction of the language of the statute which is most favourable to his or her interest.”

Can there be any proper criticism of the opinions expressed by Sir Garfield in the passage I have quoted? Yet Sir Garfield was the subject of very harsh criticism for his views and for his part in decisions of the High Court about income tax.

The criticism of Sir Garfield is distilled in a book written by David Marr, “Barwick” (1980, George Allen and Unwin). The Marr biography is an ideologically motivated attack on the character and work of Sir Garfield Barwick for his role in the dismissal of the Whitlam ministry in November 1975. Marr spares him no criticism. He finds reason to say, falsely, that Barwick’s parents’ marriage was unhappy and that Barwick’s mother pretended she was a widow while her husband was alive. He has no sympathy for Barwick, the self made man, who overcame bankruptcy on a guarantee of his brother’s debts: instead, Marr says this ordeal “left Barwick with a breezy, cocksure manner which kept the world at bay”. On income taxation, Marr says, at page 131,

“Section 260 was a provision for which he had no sympathy. It was designed to put an end to ingenious and artificial schemes of taxation avoidance, yet to Barwick’s mind the ingenuity of a scheme was always a positive attraction. He believed that citizens had the right to profit to the maximum from their enterprise. He found section 260 vague in its sweep and, to a lawyer’s mind like his, such vagueness tends to end up as everything or nothing: the mind that reads section 92 to mean a great deal is likely, as in Barwick’s case, to see section 260 as virtually meaningless. Could parliament have meant to in every arrangement which sets out even indirectly to alter the incidence of income tax? Barwick thought not, and on the whole the courts agreed. The process of reading down the limits of section 260, and the feats of construction and re-interpretation that involved, have proved the foundation of the tax avoidance industry”.

At page 293 of his book, Marr reflects upon Sir Garfield Barwick's 14 years on the bench (as at the time the book was published) in the following terms:

“Tax was Barwick's only triumph. The tax avoidance industry boomed in Australia in the late 1970's as a direct result of the work of the Barwick High Court. Under Barwick's guidance the court approached tax schemes with great precision and learning, dissecting them and taking little interest in their overall shape and the purposes for which they were put into operation. . . . Much of what was left of the power of the “catch-all” provision of section 260 of Income Tax Assessment Act was wrung out of it by Barwick and the court in 1976 in Mullens' case. It was a peculiar personal triumph for Barwick for he established there a principle which had been rejected when he put it first to the Privy Council 18 years before in Newton's case: that section 260 only struck down tax avoidance schemes set up to deal with previously accrued tax liabilities, that it only worked in the past tense.”

Before turning to some income taxation decisions of the High Court, let me remind you that, so far as material, section 260 of the 1936 Act provided:

“Every contract, agreement or arrangement made or entered into . . . shall, so far as it has or purports to have the purpose or effect of in any way, directly or indirectly preventing the operation of this Act in any respect, be absolutely void as against the Commissioner”.

In W.P. Keighery Pty Ltd v. Federal Commissioner of Taxation (1956) 96 C.L.R. 577, Sir Garfield Barwick, as counsel for the taxpayer, advanced the argument, accepted by the High Court, that section 260 must be read subject to the specific provisions of the 1936 Act and was not to be construed to remove from taxpayers choices as to the ordering of their affairs provided for or left open by specific provisions of the 1936 Act.

In Newton v. Federal Commissioner of Taxation (1958) 98 C.L.R.1, Sir Garfield Barwick was counsel for the taxpayers in the Commissioner's successful appeal to the Privy Council, whose advice was delivered by Lord Denning. The Privy Council drew a distinction, for the purposes of section 260, between arrangements implemented in a particular way so as to avoid tax and transactions capable of reference to ordinary business or family dealing. A striking feature of the advice of the Privy Council in Newton's case is the prominence accorded to Sir Garfield Barwick as advocate and the overtly personal terms in which his arguments were rejected.

In three cases in the mid 1970's, the Barwick High Court confined Newton's case to its facts and rendered section 260 ineffective as a general "anti avoidance" provision. Those cases were Mullens v. Federal Commissioner of Taxation (1976) 135 C.L.R. 290; Slutzkin v. Federal Commissioner of Taxation (1977) 140 C.L.R. 314 and Cridland v. Federal Commissioner of Taxation (1977) 140 C.L.R. 330. In the last of these cases (judgment being delivered in August 1977), the Court comprised Barwick C.J, Stephen, Mason, Jacobs and Aickin JJ, with Mason J. delivering a judgment in which the other judges concurred.

Cridland concerned a wholly "artificial" transaction in which thousands of university students, on payment of \$1 each, became entitled to the benefits of primary production averaging of income, in virtue of being beneficiaries of a trust which carried on a business of primary production. Mason J said, at pp 337-8,

“Although the very restricted operation conceded to s. 260 by the course of judicial decision and the generality of the language in which the section is expressed stand in high contrast, the construction of the section is now settled. It is therefore a source of some surprise that it continues to be relied upon

when its defects and deficiencies have been apparent for so long. More than twenty years ago Kitto J. said in Federal Commissioner of Taxation v. Newton: “Section 260 is a difficult provision, inherited from earlier legislation, and long overdue for reform by someone who will take the trouble to analyse his ideas and define his intentions with precision before putting pen to paper.” This message, despite its clarity, seems not to have reached its intended destination.

It was recently decided in Mullens v. Federal Commissioner of Taxation that even if a transaction has been entered into for the purpose of diminishing a taxpayer’s liability to tax by securing to the taxpayer a benefit or advantage conferred by a specific provision of the Income Tax Assessment Act, e.g. an allowable deduction, which but for the transaction would not have accrued to the taxpayer, the transaction will not be caught by s. 260 if it satisfies the provision in question.

The decision in the Mullens Case and the passages from the judgments to which I have referred show that the principle which underlies the Keighery Case is not as narrow as the primary judge supposed it to be. It is not confined to cases in which the Act offers two alternative bases of taxation; it proceeds on the footing that the taxpayer is entitled to create a situation by entry into a transaction which will attract tax consequences for which the Act makes specific provision and that the validity of the transaction is not affected by s. 260 merely because the tax consequences which it attracts are advantageous to the taxpayer and he enters into the transaction deliberately with a view to gaining that advantage.

The distinction drawn by Lord Denning in Newton v. Federal Commissioner of Taxation, between arrangements implemented in a particular way so as to avoid tax and transactions capable of explanation by reference to ordinary business or family dealing has not been regarded as the expression of a universal or exclusive criterion of operation of s. 260. Lord Denning’s observations were applied neither in the Mullens Case nor in the subsequent case of Slutzkin v. Federal Commissioner of Taxation.

The transactions into which the appellant entered in the present case by acquiring income units in the trust funds in question were not, I should have thought, transactions ordinarily entered into by university students. Nor could they be accounted as ordinary family or business dealings. They were explicable only by reference to a desire to attract the averaging provisions of the statute and the taxation advantage which they conferred. But these considerations cannot, in light of the recent authorities, prevail over the circumstance that the appellant has entered into transactions to which the specific provisions of the Act apply, thereby producing the legal consequences which they express.

As I have mentioned, Cridland was a decision of five members of the Court and the leading judgment was delivered by Mason J., not Sir Garfield Barwick. There is no doubt that the Barwick Court, very experienced in income taxation law, approached issues of tax avoidance differently from the High Court following the retirement of Sir Garfield Barwick. However, even at the time Cridland was decided, several matters had come before the High Court in which there was evident a tendency to expand the notion of income according to ordinary concepts and usages as brought to tax as assessable income under subsection 25 (1) of the 1936 Act. In London Australia Investment Company Ltd v. Federal Commissioner of Taxation (1977) 138 C.L.R. 106, the Chief Justice dissenting, Gibbs and Jacobs JJ decided that gains made by an investment company on the sale of shares purchased for their dividend yield were income, because the buying and selling of shares was done as part of the business of the company. In Federal Commissioner of Taxation v. St Hubert's Island Pty Ltd (in liquidation) (1978) 138 C.L.R. 210, Mason, Jacobs and Murphy JJ, Stephen and Aickin JJ dissenting, decided that certain land was "trading stock", there being features which gave the enterprise in question the character of one in which the taxpayer was engaged in the business of trading in land, even though the acquisition of the land was a single, isolated transaction. These two decisions were criticized at the time, as being inconsistent with long established authority and principle. However, they did not yet constitute a change of the tide of decision on income taxation in the High Court. Nonetheless they were an intimation of things to come. When the tide did change, a few years later, the course of decisions in the High Court, having began to move against the taxpayer, has continued further and further in that direction.

In 1978 the influence of Sir Garfield was not dead. McCormack v. Federal Commissioner of Taxation (1979) 143 C.L.R. 284 (a case concerning section 26(a) and the onus of proof), the well known decision of Federal Commissioner of Taxation v. Everett (1980) 143 C.L.R. 440 (allowing as effective for income taxation purposes an assignment of a share of a solicitors partnership) and Federal Commissioner of Taxation v. Westraders Pty Ltd (1980) 144 C.L.R. 55 (a case in which the taxpayer successfully used the trading stock provisions of the 1936 Act to create a deduction for income tax purposes where no economic loss or outgoing was suffered by the taxpayer) were decisions which the High Court would not now make. Many taxpayers took advantage of the decision in Everett which was overcome by amendment to the 1936 Act. The decision in Westraders was also reversed by retrospective legislation.

The Gibbs Court

Sir Harry Gibbs became Chief Justice on 12 February 1981. In the first months Sir Harry was Chief Justice there were notable decisions in favour of the Commissioner. Sir Harry was not always the man who writes articles in the daily press deploring the state of the income tax law.

In Cooper Brooks (Wollongong) Pty Ltd v Federal Commissioner of Taxation (1981)147 C.L.R.297, a Court comprising the Chief Justice and Stephen, Mason, Aickin and Wilson JJ, by a majority, Aickin J dissenting, repaired what it considered to be a “mistake” in the drafting of a highly technical and complex “anti avoidance” provision of those sections of the 1936 Act which dealt with the carry forward of company losses, by reading a reference in those provisions to another company as

being a reference to the company that was to take the losses into account. Mason and Wilson JJ. said that a literal construction of the provisions would produce a “capricious and irrational operation” of the anti avoidance provision, and that the Court (I suppose any court) could ignore the literal meaning of the statute and give it an effect which the Court did not consider capricious and irrational.

The Gibbs High Court considered two cases regarding deductions in relation to costs of maintaining a home study. The taxpayers were Ken Handley, of the New South Wales Bar, and Neil Forsyth, a leading barrister at the Victorian Bar: Handley v. Federal Commissioner of Taxation (1981) 148 C.L.R. 82 and Federal Commissioner of Taxation v. Forsyth (1981) 148 C.L.R. 203. A

majority, comprising Mason, Murphy and Wilson JJ, Stephen and Aickin JJ dissenting, decided the deductions should not be allowed, Murphy J. on the grounds that the outgoings were “domestic” in character, Mason and Wilson JJ., adopting a restrictive construction of subsection 51(1) of the 1936 Act, on the ground that, because of the “essential character” of the outgoings, the outgoings were not incurred in gaining or producing assessable income and were not necessarily incurred in carrying on the profession of barrister. These decisions appeared to many at the time to be wrong in principle as being based on an unduly narrow understanding of the provision which provides generally for the deductibility of outgoings (and losses) incurred in the derivation of assessable income. Nevertheless, this understanding of subsection 51(1) seems to be current orthodoxy, as is evident in the decision of the Gleeson High Court in Federal Commissioner of Taxation v Payne (2000) 202 C.L.R. 93, disallowing to a taxpayer the costs of travelling between two places at which the taxpayer derived assessable income.

The decision in Whitfords Beach (Federal Commissioner of Taxation v. Whitfords Beach Pty Ltd (1982) 150 C.L.R. 355) was a surprise to those who practised income taxation law. I was in Court on St Patrick's Day 1982 and heard the judgment. The Commissioner's appeal was allowed. A case of an enterprising realization of a capital asset was treated by the Gibbs High Court as involving the deviation of income assessable under section 25 of the 1936 Act. The burden of the reasoning of the majority (including the Chief Justice) was that the complexity of the process of realization of the parcel of land by rezoning, subdivision, construction of roads, etc and sale by allotments, constituted a business.

Thus, within the first year after Sir Harry became Chief Justice, the Gibbs High Court was establishing itself as a Court which favoured the Commissioner. Each of the matters decided by the Gibbs High Court, which I have mentioned, I venture to suggest, would have been decided the other way by Sir Garfield Barwick. As I have mentioned, appeals to the High Court were now by special leave, which was being given less and less frequently. The criticisms of the Barwick High Court (as advanced by Marr) that it nourished tax avoidance, made the Gibbs High Court shy of income tax appeals and increasingly reluctant to intervene for the taxpayer. We begin to see many volumes of the Commonwealth Law Reports without a tax case.

In 1984, the High Court, comprising the Chief Justice and Murphy, Wilson, Brennan, Deane and Dawson JJ, upheld the constitutional validity of the Taxation (Unpaid Company Tax – Vendors) Act 1982 and the Taxation (Unpaid Company Tax – Promoters) Act 1982. These enactments are remarkable for their careless drafting and unfair provisions. I have little doubt that a High Court which considered these enactments to be unjust could have found reason enough to invalidate them. But the

Gibbs High Court (as it existed in 1984) was determined to distance itself from any possibility of an allegation that it was not “tough on tax avoidance”. Remember these were the days of the witch hunts for “tax avoiders”: the Painters and Dockers Royal Commission had been transformed into a crusade against tax avoidance; Neil Forsyth was about to be prosecuted for giving honest advice to clients who sought to minimize their tax by “artificial means”; Part IVA was fresh on the statute books and weak Bar Councils were passing “ethical rules” inhibiting the giving of tax advice.

The Mason Court

Sir Anthony Mason became Chief Justice on 6 February 1987. He had been a member of the Court for almost 15 years. In his swearing in as Chief Justice (1987) 162 C.L.R. x, he spoke of the limitations of judicial power:

“Our courts have an obligation to shape principles of law that are suited to the conditions and circumstances of Australian society and lead to decisions that are just and fair. In discharging that obligation judges do not exercise unlimited freedom of choice or the freedom of choice that is inherent in the legislative and the political process.”

At the end of his tenure as Chief Justice many would doubt that his High Court had well and truly discharged the obligation so expressed.

Sir Anthony was Acting Chief Justice when he sat with Wilson, Brennan, Deane and Dawson JJ to decide Federal Commissioner of Taxation v The Myer Emporium Ltd (1987) 163 C.L.R. 199. The issue decided by the High Court was whether a lump sum received for the assignment of interest due or to become due on a loan for more than seven years was income or assessable under section 26(a) of the 1936 Act. The taxpayer had been successful in both Courts below. The transaction which gave rise to the loan and subsequent assignment was part of a tax minimization plan. The

decision of the Court to allow the Commissioner's appeal was based upon a very broad notion of income. The Court, referring to Whitfords Beach, said, at pp 209 – 210, that “if the circumstances of a transaction are such as to give rise to the inference that the taxpayer's intention or purpose in entering into a transaction was to make a profit or gain, the profit or gain will be income”. This dictum appears to eliminate any distinction between capital and income: every business transaction is entered into with the purpose or intention of profit making.

The distinction between a gain on income account and a gain capital account depends primarily upon the nature of the transaction giving rise to the gain, not the intention or purpose of the taxpayer. In truth, the High Court in the Myer Emporium case was determined to stop what it saw as tax avoidance. After Cridland, section 260 could not be called in aid. But the Court was prepared to stretch the notion of income to do the job.

The next case to come to the Mason High Court involving tax avoidance was John v. Federal Commissioner of Taxation(1989) 166 C.L.R. 417. The case concerned a Curran's case scheme. See Curran v. Federal Commissioner of Taxation (1974) 131 C.L.R. 409. In John, the Court refused to revive section 260 and decided that the doctrine of “fiscal nullity”, which briefly flourished in the United Kingdom, was not appropriate to be adopted in the construction of the 1936 Act. Instead, the Court simply overruled Curran's case, which had been decided by Barwick C.J., Menzies and Gibbs JJ., Stephen J. dissenting.

Fletcher v Federal Commissioner of Taxation (1991) 173 C.L.R. 1

concerned a tax avoidance scheme. The history of the litigation was complex. A partnership of which the taxpayer was a member incurred interest on moneys

borrowed to acquire an annuity, the annual amount of which, for some years, would not exceed the annual interest on those borrowed moneys. The Court said that, if a consideration of the whole of the circumstances of the incurring of an outgoing reveals that a disproportion between the outgoing and relevant assessable income is “essentially to be explained by reference to the independent pursuit of some other objective, and that only part of the outgoing can be characterized by reference to the actual or expected production of assessable income, apportionment of the outgoing between the pursuit of assessable income and the pursuit of that other objective will be necessary”. This highly generalized language tends to conceal the real reason for decision, namely that, if the Court thinks the taxpayer incurred an outgoing in a tax avoidance scheme the taxpayer will be denied the whole or part of the outgoing. The taxpayer’s tax avoidance purpose in incurring the outgoing was treated as reason to deny the deduction otherwise allowable within the general words of subsection 51 (1) of the 1936 Act.

Deputy Federal Commissioner of Taxation v Richard Walter Pty Ltd (1995) 183

C.L.R. 168 is not really a “tax avoidance” case, although the assessments in issue were made under Part IVA. It concerns those provisions of the 1936 Act which are intended to prevent collateral attack upon assessments. The current income taxation legislation contains kindred provisions. Section 175 provided that the validity of an assessment shall not be affected by reason that any provision of the Assessment Act had not been complied with. Section 177 provided that a notice of assessment or a copy of a notice of assessment, purporting to be made under the hand of certain officers, is conclusive evidence of its due making and that it is correct in every particular, except in proceedings for an appeal under the Assessment Act. Many taxpayers believe (and one may suppose that some, at least, have good grounds for so

believing) that officers of the Commissioner unfairly or in bad faith when multiple assessments are issued to the same taxpayer on different bases, but essentially bringing to tax the same income, or multiple assessments are issued on alternative bases to different taxpayers in respect of the same income. The High Court upheld this practice of the Commissioner. See also Federal Commissioner of Taxation v. Prestige Motors Pty Ltd (1994) 181 C.L.R. and Federal Commissioner of Taxation v. A.N.Z. Savings Bank Ltd. (1994) 181 C.L.R. 466, where the High Court reversed decisions by the Full Court of the Federal Court on procedural matters.

In Federal Commissioner of Taxation v. Peabody (1994) 181 C.L.R.359, the Full Bench of the High Court considered Part IVA. The Commissioner's appeal was dismissed. But the basis for that decision was that it would not have been expected that the taxpayer would have obtained the "tax benefit" in the year of income identified by the Commissioner. The taxpayer's victory may have been Pyrrhic.

The Brennan Court

Sir Gerard Brennan was sworn in as Chief Justice on 21 April 1995.

In 1996, the Spotless Services case was decided by the High Court. (See Federal Commissioner of Taxation v. Spotless Services Pty Ltd (1996) 186 C.L.R. 404).

Let me remind you of the facts. The Spotless companies had \$40 million of surplus funds for short term investment. They placed the funds on short term deposit with an institution in the Cook Islands at a rate of interest some 4.5 per cent less than that available on bank deposits in Australia. The Cook Islands levied no tax upon the income, save for a 5 per cent withholding tax. The companies said they were not subject to income tax in Australia because the interest income derived in the Cook

Islands was not exempt in the Cook Islands and, under paragraph 23(q) of the 1936 Act, that interest income was exempt from tax in Australia. The Commissioner applied Part IVA. The taxpayers were successful at first instance and on appeal to the Full Court of the Federal Court. The High Court made it clear at the outset that Part IVA is to be construed and applied according to its terms, not under the influence of “muffled echoes of old arguments” concerning other legislation. The Court described as a “false dichotomy” references to, on the one hand, “a rational commercial decision” and, on the other, “the obtaining of a tax benefit as the dominant purpose of the taxpayers in making the investment”.

The Court said

“tax laws are one part of the legal order within which commerce is fostered and protected. Another part is Part IV of the Trade Practices Act 1974 (Cth) which regulates or proscribes certain restrictive trade practices. In this broad sense, “[t] axes are what we pay for civilized society”, including the conduct of commerce as an important element of that society”.

It is not unexpected that a court, philosophically or ideologically so motivated, should decide for the Commissioner, overturning the conclusions of fact below. Probably, however, one should not complain that the Court revealed the true basis for its decision, rather than concealing its social or political motivation behind the application of highly generalized, even meaningless, statements of legal principle. There is an irony of the Spotless decision that, if the taxpayer companies had received the same interest rate in the Cook Islands as in Australia (and thus derived even more exempt income), the conclusion that Part IVA was applicable would have been more difficult to reach. One doubts, however, that any obstacle would have deterred the Brennan High Court from ensuring the taxpayer companies did not get the benefit of the exemption expressly granted by section 23 (q).

There was one other decision of the Brennan High Court which might be thought to concern a “tax avoidance” transaction: Federal Commissioner of Taxation v. Orica Ltd (1998) 194 C.L.R 500. The taxpayer company had liabilities under debenture trust deeds. It arranged for another, unrelated, company to assume those liabilities in consideration for a capital payment. In its profit and loss account the taxpayer company disclosed, under the heading “Extraordinary Profit”, an amount of \$36.4 million, being the difference between the principal outstanding under the debenture trust deeds at the time of the assumption agreement and the amount paid to the assumption party. Under the Myer Emporium reasoning the amount of the extraordinary profit was not income (except in the opinion of the Chief Justice), nor was it assessable as a profit from the carrying on or carrying out of a profit making undertaking or scheme. However, a majority (Gummow and Callinan JJ. dissenting) gave to the words of section 160M a very broad construction and, thus, found that the extraordinary profit was an assessable capital gain. The reasons of the dissentients are more persuasive and consistent with authority and principle than are the reasons of the majority.

During the tenure of Sir Gerard Brennan as Chief Justice, the flow of tax appeals became a trickle. On looking through the Commonwealth Law Reports one cannot escape the conviction that the Court found other matters more interesting. On my count, of the cases reported in the 12 volumes of the Commonwealth Law Reports during the tenure of Sir Gerard Brennan as Chief Justice, there were five income tax appeals taken by the High Court, including the two I have mentioned. The other three were also appeals where the Commissioner was granted special leave. In no case was a taxpayer granted special leave. In two of those other three matters the Commissioner’s appeal was dismissed and in the third it was allowed.

The Gleeson High Court

Anthony Murray Gleeson was sworn in as Chief Justice on 22 May 1998.

The work of his Court is already reported in more than 20 volumes of the Commonwealth Law reports. On my count (including Hart's case which has not yet found its way into the Commonwealth Law Reports) there are only nine matters in which the Court has taken appeals which primarily involve the construction of the income taxation legislation of the Commonwealth.

One of these matters was Steele v Deputy Federal Commissioner of Taxation (1999) 197 C.L.R. 459. It is a rare case of a taxpayer's appeal, which was allowed. There was no such case while Sir Gerard Brennan was Chief Justice and no other, so far, in the tenure of Gleeson C.J. In this case, interest incurred by the taxpayer upon a borrowing used to purchase land upon which she intended to build and operate a motel, a plan which did not come to fruition, was disallowed. The decision below was plainly wrong and in serious disconformity with long established authority and the plain words of the statute. It was said that the borrowing to build the motel was an "affair of capital" and interest was, therefore, not deductible. There are many difficulties with that reasoning. It is a sufficient connection between the incurrence of periodical interest on borrowed moneys and the derivation of assessable income that the borrowed moneys are applied to acquire an asset which is intended to be used to derive assessable income at some time.

In Federal Commission of Taxation v. Montgomery (1999) 198 C.L.R. 639 the taxpayer was a member of Freehills, who received an inducement payment from the landlord of a city building to relocate to that building. The High Court, by a majority, the Chief Justice, McHugh and Callinan JJ dissenting, held the receipt was income, according ordinary concepts, on the ground that it arose from a singular adventure in the nature of trade, undertaken in the course of a wider business activity. The decision was very evenly balanced. The dissentients may well have formed a majority, if, for example Heydon J. had been on the Court instead of Gaudron J. The dissentients remarked, at p 649, that the principles stated in the Myer Emporium case are “ not without their difficulties of application”.

Deputy Federal Commissioner of Taxation v Woodhams (2000 199 C.L.R. 370 was a case involving those provisions of the 1936 Act which impose upon directors of companies a liability for an amount of PAYE tax which the company has deducted, but has failed to remit to the Commissioner. The Court found for the Commissioner and reversed the decision of the Victorian Court of Appeal. Federal Commissioner of Taxation v. Scully (2000) 201 C.L.R. 148, concerned the construction of section 27B (1) of the 1936 Act. The Commissioner was the successful appellant.

Federal Commissioner of Taxation v. Sara Lee Household and Body Care (Australia) Pty Ltd (2000) 199 C.L.R. 520, concerned the construction of section 160 U of the 1936 Act. The Commissioner prevailed and the decision of the Federal Court was reversed. In Federal Commissioner of Taxation v Ryan (2000) 201 C.L.R. 109, the High Court decided that a “nil assessment” was not an assessment at all, and again the Commissioner prevailed and the Federal Court was reversed.

In Federal Commissioner of Taxation v Payne (200) 202 C.L.R. 93, the High Court decided that the costs incurred by a taxpayer of travelling between two places where the taxpayer derived assessable income were not deductible because those costs were not incurred “in the course of” gaining or producing assessable income. Again the Federal Court was reversed. It should be said that the words “in the course of” do not appear in subsection 51(1), which requires, instead, that the expenditure “in” gaining or producing assessable income is deductible.

I now come to the two decisions of the Gleeson High Court where it may be thought there was an issue of “tax avoidance”. The first is Federal Commissioner of Taxation v. Consolidated Press Holdings Ltd (2001) 207 C.L.R. 235. The case involved the application of Part IVA in relation to two matters. The first matter involved the question whether the Commissioner had been correct to disallow the deduction of interest on certain borrowings by the taxpayer. The High Court held that the Commissioner was correct. In doing so, the Court observed that it was “both possible and appropriate to attribute the purpose of a professional advisor to the taxpayer”. The High Court also held that a person could enter into or carry out a “scheme” for the dominant purpose of obtaining a tax benefit where that purpose was consistent with the pursuit of a commercial gain in the course of carrying on a business. The Court was again distracted by talk of “false dichotomies”. The second matter was whether the taxpayer company had engaged in “dividend stripping” within the meaning of Part IVA. Here the tax payers arguments prevailed and it was held that “dividend stripping” in its common acceptance or meaning was to be understood as a transaction the dominant purpose of which was “tax avoidance”, rather than a “normal commercial transaction”.

The decision of the High Court in Federal Commissioner of Taxation v. Hart, given on 27 May 2004, is not yet reported in the Commonwealth Law Reports. The taxpayers borrowed money under what was called a “split loan facility”, applied part to a private or domestic purpose, the acquisition of a residence for themselves, and applied the balance to the acquisition of another residence, which they let for the purpose of gaining or producing assessable income. The loan agreement provided for the borrower to direct the application of the whole of the periodical payments under the loan agreement to the satisfaction of that part of the loan used for private or domestic purposes. Interest on the balance of the loan was allowed to accrue and be capitalised and compounded. In the Federal Court, it was decided that the “tax benefit” for the purposes of Part IVA, upon which the Commissioner relied in assessing the taxpayers, was that, but for the split loan facility, the taxpayers would have made monthly payments of principal and interest so that interest was spread rateably over the total of the borrowed moneys in the proportion the moneys were used to purchase the respective assets. The Chief Justice and McHugh J. accepted that conclusion about a tax benefit. The split loan facility they concluded, “depended entirely for its efficacy” on tax benefits. They relied upon the reasoning in the Spotless case. Gummow and Hayne JJ. wrote a long joint judgment. They said, at p.18 of the judgment,

“There is no basis to be found in the words used in Part IVA for the introduction of some criterion additional to those identified in the Act itself. There is no reference to a scheme having some commercial or other coherence”.

Their Honours emphasised that what the Act requires is that the person, or one of the persons, who entered into or carried out any part of the scheme did so for the purpose of enabling the relevant taxpayer (alone or with others) to obtain a tax benefit in connection with the scheme. They also said:

“Whether considering what is a “scheme”, or considering other provisions of Part IVA, it is necessary to eschew arguments that proceed from unstated premises about choice or the drawing of false dichotomies between “rational commercial decisions” and obtaining a “tax benefit”.

Callinan J set out at length the Explanatory Memorandum for Part IVA in which it was said the provision was directed against tax avoidance arrangements that are “blatant, artificial or contrived”. His Honour construed the legislation by reference to the terms of the Explanatory Memorandum. Nonetheless, he concluded Part IVA was applicable.

CONCLUSIONS

I would like to attempt some conclusions.

First, the Barwick High Court was a taxpayer’s court in that taxpayers were successful appellants as often as was the Commissioner. The Gleeson High Court is a Commissioner’s Court. In the last 10 years there is only one case reported in the Commonwealth Law Reports or, as far as I am aware, anywhere else, in which a taxpayer has obtained special leave to appeal and has been successful on the appeal. The Commissioner is overwhelmingly successful in the High Court and, further, the overwhelming majority of matters in which special leave to appeal is granted are for appeals by the Commissioner. In the past 10 years the general anti avoidance provisions of Part IVA have been construed and applied in a way that is at odds with their stated purpose in the Explanatory Memorandum, the notion of income has been

broadened almost to the point of obliterating the distinction between income and capital and the criterion of deductibility in subsection 51 (1) (and its successor provision in the 1997 Act) has been narrowed to the disadvantage of taxpayers.

No doubt a Judge of the High Court, were he here tonight, would take the defence: I simply apply the law. This explanation does not take sufficient account of the facts, even if it is more properly rendered: I believe I simply apply the law. George Elliot said of one of her characters that she “was a well intentioned woman knowing little of her own motivations”. A Court constituted as is the Gleeson High Court, in the social circumstances of Australia in 2005, is not likely to reach the same conclusions on finely balanced issues of principle as a Court constituted by men of individualistic outlook who reached maturity before the Second World War. One should be under no illusions: personal character and social attitudes have a large influence on judicial decisions, as much as on political decisions. The Gleeson High Court will not risk the controversy that attended the taxation decisions of the Barwick High Court. But it is deeper than that: in matters of income tax everyone thinks he pays too much tax and everyone else pays too little! The public are thus better satisfied with a state of affairs where there is a construction of the income taxation legislation which ensures that there is the least opportunity for any person to so arrange his affairs that he minimizes his liability to tax. I believe that the Gleeson High Court begins from a philosophic and moral position that is the opposite of the position espoused by Sir Garfield Barwick.

I have read the more recent decisions of the High Court on taxation matters carefully to try to understand them as best one can. I am struck that the Court, as now constituted, does not demonstrate the confident understanding of business and commercial operations that was a feature of the Barwick High Court. Furthermore, the Court's judgments on Part IVA are characterized at once by an arid, literal construction of the statute and a shallow cleverness about "false dichotomies", etc. I have no doubt that the approach to the construction of Part IVA which has been embraced by the Gleeson High Court will see that provision employed by the Commissioner to inhibit and disrupt ordinary business and commercial transactions and will lead to uncertainty and unfairness in the administration of income taxation legislation, to the disadvantage of individual taxpayers and the whole community.

May I add one last matter. It is evident, I believe, that the Gleeson High Court has unleashed a monster by its approach to Part IVA. But it did not create the monster. Parliament did that. A general "anti-avoidance" provision is probably (as Sir Garfield Barwick said) based upon fundamentally flawed notions. Either the provision will be completely ineffective or it will give to the Commissioner excessive powers.

12 April 2005.