

AVAILABILITY OF DECLARATORY RELIEF IN REVENUE LAW DISPUTES

PRESENTATION TO THE TAX BAR ASSOCIATION CPD PROGRAM

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A. Introduction

1. The decision in *Sandini v Commissioner of Taxation* [2017] FCA 287 (“*Sandini*”) is a recent example of declaratory relief having been sought and obtained in revenue litigation. Declaratory relief has become something of a *cause célèbre* among Australia’s tax lawyers over the past ten years or so.
2. In particular, this has been since the controversy generated by the decision of the Full Federal Court in *Commissioner of Taxation v Indoороopilly Children Services (Qld) Pty Ltd* (2007) 158 FCR 325 (“*Indooroopilly*”). More recently though the Chief Justice of the Federal Court, in the annual Melbourne University Law School Tax Lecture in 2014, raised the issue and highlighted the availability of declaratory relief in appropriate cases. But as McKerracher J demonstrated in *Sandini*, by referring to *Oil Basins Ltd v The Commonwealth* (1993) 178 CLR 643, declaratory relief in revenue litigation is not a new concept. There are, however, a number of features of the interaction between the pathway for review of taxation decisions provided by Part IVC of the *Taxation Administration Act 1953* (“**the TAA**”) and the circumstances in which declaratory relief might be thought to be suitable, that have the consequence that there will be many circumstances in which declaratory relief will not be available or will not be appropriate.
3. What I would like to do this evening first is to outline some of the history that has attended the topic of declaratory relief in tax cases in recent years.
4. Secondly, I will try to identify the core principles and potential pitfalls to be considered when determining whether declaratory relief is appropriate in any particular case.
5. Thirdly, I am going to suggest some examples of situations where declaratory relief might be appropriate. Of course, what I am doing is making general remarks only and each situation

will involve different facts – so my remarks should not be regarded as or relied on as advice applicable to any particular set of circumstances.

B. Recent history of declaratory relief in tax cases

6. Although it might be a stretch to call the introduction of the GST recent, it prompted a number of proceedings in which declaratory relief was sought, concerning the consequences for GST purposes of particular transactions.
7. So in *Marana Holdings Pty Ltd v Commissioner of Taxation* (2004) 55 ATR 161; [2004] FCA 233 the taxpayer sought (and failed to obtain) declarations to the effect that the sale and purchase of particular real estate was input taxed. It was agreed between the parties (as is recorded in the reasons given by the Full Federal Court in the decision on appeal (2004) 141 FCR 299) that the disposal of the proceeding by way of declaratory relief was appropriate.
8. *TAB Ltd v FCT* (2005) 59 ATR 430 is another example of a taxpayer seeking declaratory relief in a GST case. That case is notable for the reason that it involved an application for declaratory relief against the Commonwealth Commissioner of Taxation being sought in a State Supreme Court. Leaving aside cases where an assessment is on foot, which will give rise to difficulties as discussed below, the State Supreme Courts have jurisdiction through s 39B of the *Judiciary Act 1903* and s 4 of the *Jurisdiction of Courts (Cross Vesting) Act 1987* (“**the Cross-Vesting Act**”).
9. In particular s 39B(1A)(c) vests original jurisdiction in the Federal Court in any matter “arising under any laws made by the Parliaments” with the exception of criminal matters. In turn that jurisdiction is vested in the Supreme Courts by s 4 of the Cross-Vesting Act.
10. However, it needs to be borne in mind that a matter that is within the original jurisdiction of the Federal Court is a “special federal matter” within the meaning of s 3 of the Cross-Vesting Act. The effect of s 6 is that (as relevant to tax cases) the State court must transfer it to the Federal Court unless it makes an order on the basis that there are special reasons for the proceeding being determined in the State court. (This issue was identified recently in *Anglo American Investments Pty Ltd v Deputy Commissioner of Taxation* [2017] NSWCA 17 at [75] to [77]).
11. It is not clear whether any point about this issue was identified in the *TAB Ltd* decision but in any event, the parties may not have noted the issue or perhaps the parties both agreed that there were special circumstances. In that case there was no assessment on foot. Liability to

pay GST did not depend on the making of an assessment but on the calculation of a “net amount” owing under the GST Act. There was a process by which an assessment could be requested under the TAA, and that process if adopted gives rise to a reviewable decision once the assessment has issued. As I discuss below, once an assessment has issued it will often not be possible to proceed by way of an application for declaratory relief, at least without the agreement of the Commissioner and the Court.

12. Another GST case that was dealt with by way of declaratory relief, was that of Logan J in *Deputy Commissioner of Taxation v PM Developments Pty Ltd* [2008] FCA 1886. The case concerned a property development company that had gone into liquidation. The liquidator had sought a private ruling to the effect that he was not personally liable for GST on the sale of property sold by the company post liquidation. The Commissioner had ruled that he was. The liquidator approached the Federal Court seeking *inter alia* a declaration that he was not personally liable for the GST. The issue was important primarily not because of the GST outcome but because of the issue of whether the liquidator personally was liable on the basis that he was making the supply, or whether the GST was a cost or expense of the liquidation to be paid in accordance with the priorities required under the *Corporations Act*.
13. Logan J had no difficulty in concluding that there was a justiciable “matter”; he identified the fact that the Federal Court had jurisdiction (in circumstances where an assessment was not issued) under s 39B and went on to consider whether or not the jurisdiction to grant declaratory relief should be exercised. He pointed to the ability to request an assessment, the availability of review proceedings pursuant to Part IVC of the TAA, and the relevant “conclusive evidence” provisions that are engaged where an assessment is produced and tendered in proceedings other than Part IVC proceedings. Those matters gave rise to:

“[A]n expectation on the part of the Parliament ... that, insofar as exercise of the judicial power of the Commonwealth is called for to resolve a Commonwealth revenue law controversy, that will ordinarily occur in this Court (initially on a taxation appeal or alternatively on an appeal on a question of law from the AAT ...”

14. Nevertheless in that case, the court was prepared in the exercise of discretion to make the declaration sought. The issue raised was important; there was no evidentiary controversy; the Commissioner does not appear to have submitted that the proceeding was unsuitable for declaratory relief and he had not sought to issue an assessment to the liquidator and to tender it. Moreover, Logan J noted the matter was one that was always going to end up in the Federal Court, save that if it did so following an objection, then there would be delays and

expenses that would have reduced the funds available for distribution to creditors (the principal creditor being the Commissioner).

15. It is not clear from the decision whether the Commissioner in that case had expressly conceded that the matter was suitable for declaratory relief if he were to lose on the substantive tax issue, but it is clear that he didn't say the matter was unsuitable. That may have been because the Full Court of the Federal Court had been very critical of the Commissioner in another private ruling case the previous year, in which it had suggested that the Commissioner himself should have approached the court seeking declaratory relief.
16. That case was *Indooroopilly*. The issue was whether an issue of shares to the trustee of a discretionary trust gave rise to a "fringe benefit" within the meaning of s 136(1) of the *Fringe Benefits Tax Assessment Act*. The taxpayer sought a private ruling that it did not, and its position was supported by a number of first instance decisions of the Federal Court that the Commissioner thought were wrong, and contrary a public ruling, but which for various reasons had not been appealed. One of those decisions was that of Kiefel J in a case called *Essenbourne Pty Ltd v FCT* [2002] FCA 1577. The Commissioner ruled adversely, notwithstanding the *Essenbourne* decision. In his reasons for ruling, he dealt with the decision as follows:

"Whilst Kiefel J's views in the *Essenbourne* case [2002] FCA 1577 about the proper interpretation of the definition of a fringe benefit in the fringe benefits tax law are contrary to the views expressed in Taxation Ruling TR 1999/5, the Commissioner has determined that as the *Essenbourne* case is not an appropriate vehicle to test the issue with the Full Federal Court, the views expressed in TR 1999/5 will remain the ATO position."

17. In the appeal, the Commissioner made a submission that he was not compelled to follow *Essenbourne* and the other single judge decisions that he thought were wrong. That prompted some fairly vigorous judicial criticism about the executive branch of government ignoring the law as stated by the judicial branch of government. But more relevantly for today's purposes, the submission led Edmonds J (with whom Allsop and Stone JJ agreed) to say that:

"[F]aced with the ruling application, in my opinion, it was incumbent on the Commissioner, having taken the view that findings of fact precluded him from appealing *Essenbourne* ... either to follow the construction embraced in those cases

or seek a declaration from the Court as to the proper construction and apply that construction in the ruling.”

18. The subsequent controversy that followed was, in my view, surprising. The Commissioner was faced with an application for a ruling that he did not wish to give but which would be consistent with the decided cases. There was an applicant who would, logically, have been a contradictor had the Commissioner sought declaratory relief. There was dispute between the applicant and the Commissioner as to whether the decided cases were wrong, and as to how the Commissioner was required to rule. Those circumstances, in my view, gave rise to a “matter” in the sense of the existence of a justiciable controversy, the existence of which is necessary for jurisdiction to arise. And s 39B(1A)(a) of the *Judiciary Act* vests original jurisdiction in the Federal Court in any matter in which the Commonwealth is seeking a declaration (and as noted above s39B(1A)(c) gives original jurisdiction in any matters arising under any laws made by the Parliament other than particular criminal matters).
19. In those unusual circumstances it is hard to see, in my view, how the issue gave rise to the controversy that it did. Probably a large part of the heat in the ensuing debate related to the court’s criticism of the Commissioner as representing the executive branch of government. But three judges of the Federal Court had agreed that the Commissioner should have sought a declaration.
20. In any event, in June 2007 the Honourable Daryl Davies QC, formerly a judge of the Federal Court, published an article in the Tax Institute’s journal *Taxation in Australia*. The article referred to the decision in *Indooroopilly*, and specifically in relation to the issue of declaratory relief. It said this:

“With due respect to his Honour, [referring to Edmonds J] it would have been entirely inappropriate for the Commissioner at any stage to seek a declaration from the Court as to the proper construction of s 136(1). The Court is not empowered to give advisory opinions on matters of law and the Commissioner is not empowered to seek one.”
21. The Commissioner subsequently released legal advice from the Solicitor-General, and other counsel, on the issue of whether he could have sought declaratory relief, the purport of which was that normally, private rulings or the issue of assessments should be used to test interpretations of the law.

22. Edmonds J was not inclined to let Mr Davies' views or the Commissioner's legal advice go without a response. He referred to them in a paper given in 2008 at the Annual Conference of the Australian Tax Teachers' Association titled "Recent Tax Litigation: A View from the Bench". In that paper (a copy of which available on Austlii) Edmonds J set out the Commissioner's legal advice at some length and wrote:

"With the benefit of hindsight, I would accept that it would not usually be appropriate, nor able, for the Commissioner to seek to use declaratory proceedings to resolve disputes for the reasons advanced in the joint opinion. On the other hand, I do not regard the background circumstances to the *Indooroopilly* ruling ... as providing a 'usual' context or environment."

23. As I have said, much of the controversy following *Indooroopilly* related to the criticism of the Commissioner for not following single judge decisions of the Federal Court. The topic of the scope for declaratory relief in revenue cases seems to have been given little consideration in the next few years although, as I have mentioned, Logan J had no difficulty with the view that declaratory relief was available in *PM Developments*. That of course was an application by a taxpayer and not the Commissioner.
24. The topic gained attention again in 2014 when Allsop CJ, who had agreed with Edmonds J in *Indooroopilly*, but by then had become Chief Justice, drew attention to the potential for declaratory relief in revenue cases in the annual tax lecture given at the Melbourne Law School. The topic was then picked up by the Commissioner in a speech to the Tax Bar Association here, a couple of months later, in November 2014.
25. Speaking about declaratory relief, the Commissioner said:

"We acknowledge that there are benefits in using declaratory proceedings to try and resolve ambiguous points of law, without the need to go through an expensive litigation process. We do work with taxpayers to jointly use declaratory proceedings, where appropriate, although this is not commonplace.

We think that there are some types of disputes where seeking declaratory orders are appropriate. For example, for discreet questions dealing with elections and withholding issues. We also think there is scope to use declaratory proceedings before assessment, to try and resolve disputes earlier."

26. By this time of course, not only had Allsop J become Allsop CJ but a different individual was the Commissioner of Taxation. Both the Federal Court and the ATO by now seemed to be alive to the possibilities that declaratory relief might offer.
27. The reference to declaratory proceedings having utility before assessment is important because, as I will come to below, once there is an assessment it will - at least in the absence of agreement – often be difficult to obtain declaratory relief. Indeed at a practical level the Commissioner’s agreement and co-operation will often be required, even before an assessment issues, because of the possibility that the Commissioner might simply issue an assessment and seek to tender it and rely on the applicable conclusive evidence provisions (e.g. s 177 of the *Income Tax Assessment Act 1936* and now s 350-10 of Schedule 1 to the TAA).
28. But continuing on with the history for the moment, it is worth noting that in October 2016 all of the existing practice notes for specialist lists in the Federal Court were revoked. That included Tax-1, which had been applicable since August 2011 and made no mention whatsoever of declaratory proceedings in revenue cases.
29. The revised Tax-1 came out on 25 October 2016 and addressed specifically the possibility of declaratory relief.
30. Paragraph 4.4 of the Practice Note is as follows:
- “Declaratory Orders
- 4.4 Declaratory relief may be brought in the circumstances prescribed by s 21 of the Federal Court Act and r 8.03 of the Federal Court Rules. Such relief may be appropriate, but is not limited to, circumstances where the facts are agreed or are not in dispute.”
31. So the situation now seems to be that not only has the *Indooroopilly* controversy been resolved, but both the Commissioner and the Federal Court have said publicly that declaratory relief is available in appropriate cases.
32. I now want to refer briefly to some of the core principles, the manner of proceeding and the potential pitfalls to be considered when considering declaratory relief.

C. Principles and pitfalls regarding declaratory relief

33. As I have already mentioned, s 39B(1A)(c) of the *Judiciary Act* confers original jurisdiction on the Federal Court in respect of any matter “arising under any laws made by the Parliament” other than certain criminal matters. This is a conferral of very broad jurisdiction and while in some cases there may be an issue as to its scope, this is unlikely to be the case in Commonwealth Taxation disputes.
34. Section 21 of the *Federal Court Act* in turn confers jurisdiction to make binding declarations, in relation to civil proceedings in which the court has original jurisdiction. That would include applications for declarations in tax disputes.
35. Where a party seeks declaratory relief, the proceeding has to be commenced by an originating application, which is required to state the declarations sought: see Rule 8.03 of the *Federal Court Rules*. The originating application in these circumstances is required to be supported by an affidavit, which is required both by paragraph 4.3 of the Tax-1 Practice Note, and also by Rule 8.05(b) of the *Federal Court Rules*. Rule 8.05(b), in circumstances where an applicant seeks relief that does not include damages, contemplates an affidavit or a statement of claim. However, paragraph 4.3 of the Practice Note requires an affidavit.
36. I doubt whether an affidavit ought to be required in all cases. In many cases it might be more appropriate for the parties to file pleadings. In any event, the rule does not say what the affidavit has to contain.
37. Depending on the circumstances of the case, the affidavit could depose to:
- (a) the facts relied on to justify the grant of declaratory relief;
 - (b) the fact that the parties are agreed on the facts relevant to the application, or in any event that particular facts are not in dispute;
 - (c) the circumstances of the history of the dispute, including the facts relevant to justify the conclusion that there is a “matter” suitable for disposition by way of declaratory relief; and/or
 - (d) in some cases, potentially, the affidavit could give a short outline of the background to the dispute and identify facts relevant to how the applicant seeks to have the dispute managed by the court (such as, for example, by exhibiting a draft statement of claim where the applicant wishes to proceed by way of pleadings).

38. As to the requirement for a “matter”, as we know from *Sandini* and *PM Developments*, there needs to be a judiciable controversy.
39. Where there is a tax dispute, this is often likely to be the case - whether it be as to which of alternative constructions of the legislation is correct in relation to a given set of facts, or indeed in circumstances where one side or the other contends for particular facts that are said to have a particular consequence arising under the taxation legislation.
40. The requirement for a “matter”, or a justiciable controversy, has the consequence that there must be a right, duty or liability to be established by the determination: the authorities are referred to in *Sandini* at [29]-[31] and for further reading, there is a paper written by the former Chief Justice of the High Court, when he was a member of the Federal Court, French J titled “Declarations – Homer Simpson’s Remedy – Is there anything they cannot do?” dated 30 November 2007 which is available on Austlii. That paper, which is not written with tax disputes in mind, contains a thorough discursus of the principles applicable to declaratory relief generally.
41. Concomitantly with the requirement for a “matter” it is also well established that declaratory relief must be directed to determining actual legal controversies and not to answering questions about abstract or hypothetical issues. Declarations should not be made in respect of an assumed or hypothetical state of facts: see *Ainsworth v Criminal Justice Commission* (1992) 175 CLR 564 at 581-2 per Mason CJ, Dawson, Toohey and Gaudron JJ; *Bass v Permanent Trustee Company Limited* (1999) 198 CLR 334 (“**Bass**”) at 355-357 per Gleeson CJ, Gaudron, McHugh, Gummow, Hayne and Callinan JJ and see per Kirby J at 370-1.
42. In this respect Jacobs J (with whom McTiernan ACJ agreed) in *University of New South Wales v Moorhouse* (1975) 133 CLR 1 said at 24:
- “A declaration of right based on facts found in the particular case can certainly be made but it is not possible to make a declaration of right which amounts to a conclusion of fact from a hypothetical or assumed state of facts and thereby to enunciate or declare a rule of apparently general application as though it were a declaration of applicable law...”
43. This principle has been explained by pointing out that where there is no “*real legal controversy*” between the parties a claim for declaratory relief should be summarily

dismissed: see per Ormiston JA, with whom Tadgell JA agreed, in *C.E. Heath Casualty & General Insurance v Pyramid Building Society (in liquidation)* [1997] 2 VR 256 at 260.

44. However the requirement for a real legal controversy, and the principle that a Court should not make declarations based on assumed or hypothetical statements of fact, does not mean that that the court cannot make a declaration about the legal consequences of events that have not yet occurred, provided that there are actual facts found that justify it.
45. In *Bass* the first issue was whether the State of New South Wales was a “person” to whom the prohibition on misleading or deceptive conduct in then s 52 of the *Trade Practices Act* applied. The matter came up to the High Court on appeal from a decision answering preliminary questions that had been framed during the course of interlocutory disputes. The High Court held that that issue could be determined by reference only to the statement of claim: in effect, dealing with the issue as on a demurrer.
46. However, issues as to whether the legislation applied to other respondents – which depended on factual matters such as whether they were acting as agents for the State – were not able to be determined in circumstances where there were no facts found or agreed. In explaining why, the High Court reasoned by analogy to the principles applicable to declaratory relief. The principal judgment refers to the need for an “established or agreed situation” and the need for a “real question”. At 356 the joint reasons explained that the jurisdiction to deal with real questions:
- [I]ncludes the power to declare that conduct which has not yet taken place will not be in breach of a contract or a law and such a declaration will not be hypothetical in the relevant sense. Barwick CJ pointed this out in *The Commonwealth v Sterling Nicholas Duty Free Pty Ltd* (1972) 126 CLR 297 at 305.”
47. Therefore provided that one can identify a “real question”; and that may arise from agreed facts, provided that they are not simply assumed or hypothetical. The issue will not necessarily be hypothetical even if the contemplated transaction has not yet taken place. *Sterling Nicholas* concerned whether duty free goods could lawfully be sold to customers in Sydney, prior to them boarding international flights, and delivered to them at the airport, or whether doing so would amount to supplying goods within the airport which was not permitted under a particular provision of the *Airports (Business Concessions) Act*. There was no doubt that the duty free operator in fact intended – subject to the outcome of the application for declaratory relief – to sell goods duty free in that manner. Barwick CJ

dissented and was prepared to make a declaration in favour of the taxpayer; as was Windeyer J. Menzies J (with whom McTiernan J agreed) held that the declarations should not have been made but said at 311 that “the declarations of the kind sought could, in a proper case, have been made”. Owen J thought that there was substance in the argument that the case was unsuitable for declaratory relief but did not need to decide the point.

48. In any event, the dissenting dicta of Barwick CJ was picked up by six members of the High Court in *Bass*.
49. The issue that immediately comes to mind in the context of tax disputes, of whether a declaration as to an event that has not taken place can be made, is whether a declaration that a proposed transaction will not attract Part IVA could be made.
50. That issue could probably be the subject of a discrete seminar in itself. I do want to say something about it and I will shortly. But before I turn to that topic, I want to suggest some other circumstances in which – obviously depending on the facts of each case – declaratory relief might be viable. By declaratory relief I am talking about issuing a discrete proceeding in the Federal Court seeking as the only remedy, a declaration – I am not referring to the practice that is sometimes adopted of framing for determination, preliminary or discrete questions.

D. Possible circumstances where declaratory relief may be appropriate

51. The first point to make is that where an assessment is already on foot, it will generally be inappropriate to issue proceedings for declarations. Declaratory relief is a discretionary remedy. In circumstances where the law provides alternative sources of remedies, such as by way of the objection and appeal/review process under Part IVC of the TAA, the court might well refuse relief, especially if the Commissioner were to object to an applicant seeking a declaration.
52. Indeed the Commissioner might seek to tender the assessment, which would in most cases preclude any possibility of declaratory relief due to the application of the applicable conclusive evidence provision.
53. The second point is that declaratory relief will be more likely to be regarded as an appropriate way to proceed where both parties are agreed that proceeding in that manner is appropriate.

54. However, absence of agreement of itself does not mean that a court would refuse to hear an application for declaratory relief.

55. I will now try and outline a number of examples of circumstances in which proceeding by way of declaratory relief *might* be an appropriate course. I say might, because each case will turn on the actual facts and these examples are only hypothetical examples with incomplete facts.

C.1 Example – taxpayers in losses

56. One possible situation where it occurs to me that declaratory relief might be appropriate is in cases where, for example, a taxpayer is in a loss situation in any event. Taxpayers cannot object to “nil” assessments unless they wish to increase them. However one can envisage circumstances where it might be desirable to have the tax treatment of a particular issue determined such as where, for example, there is a dispute about a deduction but even if the taxpayer wins, there would still not be an assessment that tax is payable.

57. For example, where major infrastructure is being built issues may arise about characterisation of certain expenses, but the taxpayer entity undertaking the project may be in losses. Certainty as to the tax treatment may be desirable to enable regulatory disclosures to be made or to raise funds. Declaratory relief might be a fruitful avenue.

C.2 Example – withholding obligations

58. These are not generally assessed – the obligation to withhold either arises or it doesn’t. It may be in the interests of either or both of the payer and the payee to obtain clarity about the payer’s entitlement (or obligation) to withhold.

C.3 Example – characterisation of instruments as debt or equity

59. Self-explanatory - as Gareth Redenbach has suggested, issues of whether payments are frankable or not arise.

C.4 Example – application of Part IVA (or other anti-avoidance provisions)

60. The Commissioner very often will decline to rule on the application of Part IVA. Where the facts of a proposed transaction are known, the application of Part IVA to the transaction might be an example of a situation in which declaratory relief might be appropriate as

mentioned above. It is to be borne in mind that whether the “purpose” test in s 177D is based on objective facts.

C.5 Example – conduct by ATO officers

61. From time to time it may be appropriate to seek declarations to the effect that ATO officers are (or are not) permitted or required to take certain steps. A recent example arose in the UK, in which the Supreme Court of the United Kingdom considered whether officers of Her Majesty’s Revenue and Customs had breached non-disclosure obligations applying to them under the *Commissioners for Revenue and Customs Act 2005*. The decision is *R (on the application of Ingeneous Media Holdings plc) v Commissioners for Her Majesty’s Revenue and Customs* [2016] UKSC 54.

C.6 Example – valuation issues

62. Valuation issues often arise at the pre-assessment stage. These can include not only what the value of an asset or service is, but how it should be valued. Resolving such disputes pre-assessment has the potential in some cases to materially reduce the complexity and issues involved in subsequent disputes, even if the matter then proceeds through the process of objections and litigation. That is, resolving the issue by declaratory relief has the potential to take a large part of the dispute “off the table” earlier and may assist in achieving a settlement prior to time consuming and expensive litigation processes. The same may apply in a transfer pricing dispute to ascertaining what are the relevant “arm’s length conditions” that might be expected to operate between independent entities: cf s 815-125 of the *Income Tax Assessment Act 1997* (Cth).

Overall – declaratory relief has its place in tax litigation and may be useful to dispose of or narrow disputes. It offers flexibility in the process that the Part IVC process may not allow. It is likely to be most helpful where both sides to the dispute are agreeable as to proceeding by way of declaratory relief. Depending on the circumstances it may be appropriate for the Commissioner, or for the taxpayer, to be the applicant.

Happy to take questions.