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FOREWORD

ALISTAIR HODSON

It is a privilege to be the editor for the 2022 *Journal of the Australasian Tax Teachers Association*. This year we have had submitters from a number of jurisdictions. Several articles are from New Zealand and Australian authors, and we also have articles from Hong Kong and South Africa. In total there are nine articles in this issue.

The 33rd Annual ATTA Conference, originally scheduled to be held in 2021, was postponed until 2022 due to the devastating impact of COVID-19. A hybrid ATTA Symposium was held at the University of Canterbury (UC) in January 2021, with the Annual ATTA Conference hosted for the first time in a hybrid format by UC between 19 and 20 January 2022. The Conference theme was *The Future of Tax: More than Just Politics?*

There were five keynote addresses throughout the conference including one from The Hon Justice Sir William Young KNZM, recently retired Supreme Court Judge, whose contribution is presented first in this issue of *JATTA* and is based on his keynote address. Titled '*Looking back on the approaches of the courts to tax, after more than 24 years on the bench*', it provides an interesting insight into recent New Zealand tax administration and avoidance through a judicial lens. Justice Young's contribution is organised under the three headings of: care and management, the pre-assessment and challenge processes, and tax avoidance. Under the tax avoidance head, he reflects on the recent 4:1 decision of *Frucor Suntory Ltd v Commissioner of Inland Revenue* [2022] NZSC 13, a case that will engender robust discussion amongst the tax community for some time, not only on the application of section BG1 of the *Income Tax Act 2007* (NZ) (the general anti-avoidance provision), but also on the application of penalties for taking an abusive tax position. Given the disparate nature of the topics considered in his paper, Justice Young considers the identification of a theme may be a little artificial. These reservations notwithstanding, Justice Young discerns something of a thread which runs through what has happened – demystification. Justice Young's paper concludes that tax litigation has come to be treated in very much the same way as other litigation about money. The focus is on what, if anything, is owed. The parties, including the Commissioner, can approach tax disputes in the courts in a pragmatic way, settling, if they choose, on a basis that reflects the risks and benefits of litigation options. The courts have increasingly put to one side distracting procedural issues in order to better concentrate on whether tax is due and, if so, how much is owed. This same process of demystification has also been applied to tax avoidance.

The first two articles in this issue of the Journal are both tax education focused, relating to Australia's National Tax Clinic Program. A multi author, multi university article 'Work-integrated learning for international students: developing self-efficacy through the Australian National Tax Clinic Program' by Michelle Cull, John McLaren, Brett Freudenberg, Connie Vitale, Donovan Castelyn, Robert Whait, Ann Kayis-Kumar, Van Le and Annette Morgan considers the impact of the work-integrated learning experience as part of Australia's National Tax Clinic Program on the self-efficacy of international students studying in Australia. The nine authors make reflections on the program run by their respective university. The creation of tax clinics at 10 Australian universities is a relatively recent development in the establishment of a work-related learning experience for students. The authors' analysis has shown that the student experience at the tax clinics has had a positive impact on self-efficacy, particularly for international students. The study supports the need for authentic work integrated learning consulting experiences such as those offered by tax clinics to provide a stronger foundation for all students to transition from university study to professional work.

Robert Whait, Connie Vitale and Donovan Castelyn are the authors of the article 'Tax Clinics in Australia – the Road to Legitimacy'. They observe that tax clinics are now a recognised fixture of Australia's tax landscape. For this position to first be both attained and to continue, tax clinics needed to achieve legitimacy among several key stakeholders including taxpayers, professional bodies, university students, and the Australian Taxation Office and Federal Treasury. Tax clinics were established in Australian universities to fill a gap in the market by providing free services to those who cannot afford a tax agent. Students, under supervision, provide these services. This article evaluates the process undertaken by participants in the National Tax Clinic Program ('NTCP') to achieve legitimacy in Australia during their first year of operation while the NTCP was being trialled. The article demonstrates how tax clinics have adopted pragmatic, moral and cognitive strategies to attain legitimacy. The article also provides a brief history of tax clinics. This study inductively analyses articles submitted and published by each participating clinic in the 2020 special edition of the *Journal of Australian Taxation*. The study shows a reliance on pragmatic legitimacy which is easier to attain, but it is not as durable as moral or cognitive types of legitimacy. The authors conclude it may be wise for clinics to shift focus toward attaining moral and cognitive legitimacy by adopting relevant and appropriate strategies.

Jonathan Barrett's article debunks the myth of the Akaroa window tax. This article is an offshoot of a larger research project on taxes and the constitution of the built environment and focuses on the specific claim that a doors and window tax operated in the nascent township of Akaroa on Canterbury's Banks Peninsula (Horomaka). That claim

is based on an implausible presumption that France (Wīwī) established a sovereign colony, with its own fiscal system, in Akaroa between 1840 and 1845. Akaroa is a popular destination for locals and visitors, around one hour by car from Christchurch. Barrett refers to an article published in the *Columbia Journal of Tax Law*, a prestigious United States journal, that has reported how 'a missionary in the French colony of Akaroa would climb in and out of his "home" on his hands and knees in an attempt to minimise the size of the windows and doors.' A sceptical analysis of the claim that the French doors and windows tax applied in Akaroa demonstrates that the claim has no foundation. The missionary had made a joke about his humble accommodation. A considerable number of European style buildings would have been needed to make such a tax viable and the French never levied such a tax in their colonies. Besides, Akaroa was in fact never a French colony. Although the Columbia article focused on a particular fallacy, this article has far broader application to tax and the built environment, indeed to academic research in general.

Wilson Chow's article 'Entering a new era: Time for a holistic review and revamp of the tax system in Hong Kong?' addresses the recent evolution of the Hong Kong tax system, and the need, according to the author, for significant reform. Once aptly described as the 'Jurassic Park in the Pearl River Delta', the simple low-rate tax system in Hong Kong has also been said to be 'troublingly successful'. Hong Kong has had extraordinary success, with low rates of tax, the government usually operating at a surplus, and the populace appearing to be generally content with both the tax system and the balance of taxation and public spending. This article argues for a timely and holistic review of the tax system to prepare for and meet the challenges for a new era from now to and beyond 2047. The article sketches out the way forward for a modernised and more 'fit for purpose' system. Chow concludes that while the Hong Kong tax system 'ain't broke', it would be better, as an ancient unattributed quote says, to 'have not thy cloak to make when it begins to rain'!

Lisa Marriott's article 'Tax Principles and the Serious Hardship Provisions in Aotearoa New Zealand' analyses the serious hardship provisions contained in the *Tax Administration Act 1994* (NZ). The article reviews several cases where serious hardship has been claimed by taxpayers. The principles of administrative efficiency, equity and minimisation of tax distortions are used to frame the discussion. These principles were referred to by Labour's Hon David Parker, Minister of Revenue and Associate Minister of Finance, in the recently proposed Tax Principles Act. In determining that the serious hardship provisions meet none of the proposed principles, the article questions what impact a proposed *Tax Principles Act* will have on existing legislation that does not align with the proposed new Act. The article concludes that while there may be little disagreement that tax principles are an important component of tax design, they may be

of little benefit if not used to resolve potentially contentious components of existing legislation.

Pendency of cases plagues the Indian tax appeal system. A certain level of delay is understandable with respect to tax appeals. In India, tax cases can take anywhere between twelve to fourteen years to get decided if the appeals go all the way through to the Supreme Court, the last stage of appeal. In his article 'Pendency in the Indian Tax Appeal System' Sashi Mohan discusses the views of tax practitioners, former adjudicators, and retired tax officials regarding factors that influence the pendency of tax cases and recommendations on how to alleviate the problem in the context of the Indian tax appeal system. He concludes that pendency is a function of case volume, adjournments, delay in filling vacancies in the appellate fora, and a lack of tax expertise in courts. Case volume is further influenced by poor judiciousness of Income Tax Department ('ITD') officials, declining judiciousness and independence of some appellate authorities, strategies adopted by taxpayers, repetitive appeals, a dearth of accountability of appellate authorities and ITD officials, and the complexity as well as the uncertainty of law. Mohan discusses these factors in his article as well as suggesting various solutions to reduce pendency in tax appeals.

It is not only tax cases that have significant delays through India's judicial system. Recently it was reported in the media that India's longest running legal dispute has finally been settled, and by a judge who had not been born when it began more than 70 years ago. India's courts are currently sitting on a backlog of 50 million cases, with two pending cases dating back to 1952 and 1956.

Tax avoidance is an issue for any tax jurisdiction. It has various harmful effects, including a loss of revenue for governments but also the costs associated with identifying and judicially resolving an avoidance case. Teresa Pidduck, André Klopper, Tshephiso Malema and Michelle Kirsten's article 'Did New Zealand Get It Right? Lessons for the South African GAAR', seeks to make two contributions. First, the article analyses and compares the interpretation and application of the South African GAAR with those of the New Zealand GAAR with the aim to identify weaknesses in the South African GAAR and lessons that can be learnt from its New Zealand counterpart. Secondly, the article has applied the South African GAAR to the facts of three New Zealand tax avoidance cases (*Penny and Hooper*, *Ben Nevis* and *Frucor*) to further identify weaknesses in the South African GAAR, in order to propose amendments to improve its efficacy. While the New Zealand GAAR was used for comparative purposes, it is worth noting that the New Zealand GAAR itself is not without issue, and an embedded uncertainty remains. Some earlier New Zealand tax avoidance case law, and more recently *Frucor* reiterate the complexity in avoidance cases with regard to both the substantive tax and the imposition

of penalties. Similarly, reflecting on the delay in the *Frucor* Supreme Court decision results in an unavoidable sense of uncertainty for taxpayers and practitioners alike.

The final article, Steven Stern's 'Tax legislative Drafting: Superannuation Example: How Safe Is Your Pension?', fits well with the conference theme *The Future of Tax: More than Just Politics?* The success of legislation in effecting its purpose largely depends on the words drafters use to express their intention. Effective drafting requires the legislation to meet three essential criteria: transparency, accessibility and congruency. This article focuses on the Treasury Laws Amendment (Fair and Sustainable Superannuation) Bill 2016 (Cth) and associated legislation. Stern examines this legislation, and compares its objects and purposes, enunciated by the then Treasurer of the Commonwealth of Australia, The Hon Scott Morrison MP in his second reading speech. Stern concludes that the legislation fails to meet the three key criteria for effective drafting. Stern concludes that taking the politics out of tax reform requires the simplification of tax laws to make then comprehensible. Tax teachers who oversee the training of the next generation of tax practitioners are well placed to pursue this objective.

The articles presented in this volume reflect the breadth and variety of taxation research in Australasia.

I would like to thank the authors who submitted their articles for this edition of *JATTA*. The production of this volume would not have been possible without the efforts of so many who gave so willingly of their time. The peer reviewers who each anonymously provide exemplary guidance to authors in assisting them to strengthen their respective articles also deserves a special mention.

Alistair Hodson

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20 December 2022

LOOKING BACK ON THE APPROACHES OF THE COURTS TO TAX, AFTER MORE THAN 24 YEARS ON THE BENCH

THE HON JUSTICE WILLIAM YOUNG KNZM, JUDGE OF THE SUPREME COURT OF NEW ZEALAND

I OVERVIEW

I was appointed to the bench in late 1997. I retired as a full-time judge on 13 April 2022 but continue to sit as an acting-Judge. For the years preceding my appointment in 1997, tax advice and litigation formed an appreciable and, at times, significant part of my very general practice at the bar. In contradistinction, over the more than 24 years I have sat on the High Court, Court of Appeal and Supreme Court, tax litigation has made up a comparatively small proportion of the cases I have heard. In part this is because there is not a great deal of tax litigation. It is also a function of the way the New Zealand courts operate with all senior court judges required to be generalists. This has some advantages and disadvantages. For present purposes, what it means is that my awareness of the developments and changes in tax law is pretty much confined to what I have absorbed as a result of involvement in particular cases. Some of these cases have, however, been of some significance and they provide the basis for what follows.

In selecting topics to discuss, I have looked at areas of tax law where the approach of the courts to tax issues has evolved appreciably since I was appointed to the bench. That appointment coincided (at least broadly) with three significant events which have affected the development of the law of taxation and feature in the discussion which follows:

- In 1995, a new section 6A of the *Tax Administration Act 1994* (NZ) ('*TAA 1994*') came into effect. It charged the Commissioner with 'the care and management of the taxes covered by the Inland Revenue Acts'.[1]
- In 1996, new Parts 4A (dealing with pre-assessment dispute procedures) and 8A (dealing with challenges to assessments) of the *TAA 1994* were enacted. They came into effect for the 1997–98 tax year.[2]
- Tax returns which prompted the litigation leading to the Supreme Court judgment in *Ben Nevis Forestry Ventures Ltd v Commissioner of Inland Revenue*[3] were lodged in respect of the tax year ending 31 March 1997.

What follows is organised under the following headings:

- Care and management (Part II);

---

[1] *Tax Administration Amendment Act 1995* (NZ) s 4.

[2] *Tax Administration Amendment Act (No 2) 1996* (NZ) ss 11 and 42.

[3] *Ben Nevis Forestry Ventures Ltd v Commissioner of Inland Revenue* [2009] 2 NZLR 289.

- Pre-assessment and the challenge processes (Part III); and
- Tax avoidance (Part IV).

II CARE AND MANAGEMENT

In what I think was the first case involving tax which I heard as a judge (*Fairbrother v Commissioner of Inland Revenue*[4]), s 6A was in play. In issue was whether a taxpayer who was sued on an assessment could plead an agreement that the Commissioner would accept a lesser amount in satisfaction of the tax as assessed. A District Court Judge had struck out the defence and the taxpayer appealed. This apparently simple case raised an issue of some difficulty.

Traditionally the Commissioner had been seen as having no discretion as to the collection of taxes (other than as was specifically conferred by statute). So, in *Brierley Investments Ltd v Bouzaid*, a judgment delivered in 1993, Richardson J observed:[5]

> The income tax legislation proceeds on the premise that in the interests of the community the Commissioner is to ensure that the income of every taxpayer is assessed and the tax paid. The Commissioner cannot contract out of those obligations. No doubt, and as contemplated under the State Sector Act 1988 and the Public Finance Act 1989, resource limitations will at times affect the nature and extent of the investigation undertaken to quantify the statutorily imposed liability for tax and the efforts made to pursue recovery. But the Commissioner does not have a general dispensing power. He (or she) cannot opt out of the obligation to make the statutory judgment of the liability of every taxpayer under the Act.

This approach was construed broadly. Thus, the Commissioner stated:

> Final agreements must be in accordance with the law. Agreements cannot be finalised on "splitting the difference" on a global basis. All agreements must be on an issue by issue basis based on the law and the evidence available. Once signed, the agreement precludes the taxpayer from using the disputes process in relation to the issues finalised.
>
> …
>
> As the Commissioner is under a statutory obligation to assess and collect the correct amount of tax, it is inappropriate that the risks of litigation be factored into the final agreement. While litigation risk is an appropriate consideration in terms of commercial agreements, it is not appropriate in the context of finalising an agreement of taxation disputes. If the law is uncertain and there is only a 50/50 chance of the Courts taking one view or the other, it is not possible to simply give a taxpayer one-half of the advantage or disadvantage in recognition of the uncertainty. Agreements are based on the same statutory criteria as that for making other assessments. The process of final agreements should not be regarded as an opportunity for issuing an assessment that does not conform to legislation.
>
> …

---

4 *Fairbrother v Commissioner of Inland Revenue* [2000] 2 NZLR 211 (HC).

5 *Brierley Investments Ltd v Bouzaid* [1993] 3 NZLR 655 (CA) 659 (citation omitted).

> The ability of the taxpayer to pay the tax is not relevant in determining a taxpayer's tax liability, but may give rise to other administrative arrangements tailored to the taxpayer's circumstances. When the facts and law support issuing an assessment but the taxpayer will not be able to pay the tax, the assessment is still to be issued. The taxpayer should apply under the relevant sections of the Tax Administration Act 1994, ie, sections 176 and 177, for consideration to have the tax remitted or obtain an instalment payment arrangement.[6]

The information bulletin made no reference to *TAA 1994* s 6A. In its current form, this provides:

> **6A Commissioner's duty of care and management**
>
> *Care and management*
>
> (1) The Commissioner is charged with the care and management of the taxes covered by the Inland Revenue Acts and with such other functions as may be conferred on the Commissioner.
>
> *Highest net revenue practicable within the law*
>
> (2) In collecting the taxes committed to the Commissioner's charge, and despite anything in the Inland Revenue Acts, it is the duty of the Commissioner to collect over time the highest net revenue that is practicable within the law having regard to—
>
> (a) the resources available to the Commissioner; and
>
> (b) the importance of promoting compliance, especially voluntary compliance, by all persons with the Inland Revenue Acts; and
>
> (c) the compliance costs incurred by persons.

The expression 'care and management' had been taken from United Kingdom legislation. This provided that income tax should be 'under the care and management of the Commissioners'.[7] This was applied by Lord Diplock in the following way in the House of Lords decision in *Inland Revenue Commissioners v National Federation of Self-Employed and Small Businesses Ltd*:[8]

> In the exercise of these functions the board [of Inland Revenue] have a wide managerial discretion as to the best means of obtaining for the national exchequer from the taxes committed to their charge, the highest net return that is practicable having regard to the staff available to them and the cost of collection.

In my judgment in *Fairbrother*, I noted:

> [25] I accept that the very prescriptive and detailed drafting of the relief and remissions provisions of the Inland Revenue Acts can be regarded as pointing [against the appellant's argument]. If there is, indeed, a broad power vested in the

---

[6] Inland Revenue, *Tax Information Bulletin* (August 1998) 10(8) 4–5.

[7] *Taxes Management Act 1970* (UK) s 1.

[8] *Inland Revenue Commissioners v National Federation of Self-Employed and Small Businesses Ltd* [1982] AC 617 (HL) 636.

> Commissioner to settle tax liabilities on a commercial and pragmatic basis, there would be no need for these detailed provisions. So, prior to the introduction of s 6A, there was scope for an argument that the premise underlying these provisions was that the Commissioner was obliged (in the absence of explicit contrary statutory direction) to collect the right amount of tax. …
>
> [26] I have no doubt, however, that this issue has now been put beyond doubt by the introduction in 1995 of s 6A of the Tax Administration Act. The phrase "care and management" was borrowed from the United Kingdom legislation. As well, the specific terms of the duty imposed on the Commissioner to "collect over time the highest net revenue that is practicable within the law" created by [s 6A(2)] is very similar to the language employed by Lord Diplock in the *Small Businesses* case. [Section 6A(2)] makes it clear that this duty overrides anything else that might be explicit or implicit in the Inland Revenue Acts. In those circumstances, it seems to me that s 6A must be regarded as a statutory ratification of the approach adopted by the House of Lords in the *Small Businesses* case.
>
> [27] I note that s 6A is a direct sequel to the report of the Organisational Review of the Inland Revenue Department in April 1994. The review committee referred to the argument that the Commissioner was obliged to assess and collect all taxes that are due regardless of the resources and costs involved. In the opinion of the Review Committee this was "not a realistic objective". Reading s 6A in light of the terms of that report confirms my view that there is now no scope for an argument based on an absolute obligation to collect the right amount of tax.

As will be apparent, *Fairbrother* was a collection case, where the Commissioner had issued an assessment conforming with his view of the correct tax position, but a delegate had then, according to the appellant at least, agreed to a settlement. So, the related question whether s 6A permitted the Commissioner to *issue* an assessment which did not conform to his or her view of the correct tax position might be thought to have been open to at least some debate. This question arose acutely in the Trinity litigation.

Shortly before the High Court trial of the challenges to the assessments associated with that scheme, a number of documents associated with the set-up and operation of a company associated with the Trinity scheme were obtained by the Serious Fraud Office from the British Virgin Islands and made available to the Commissioner. When these documents surfaced and were shared with the taxpayers, some of them settled with the Commissioner on the basis of amended assessments. Those who did so came out of the litigation on far better terms than those who persisted with their challenges and lost. On the law as stated in the *Brierley Investments* case, it would not have been open to the Commissioner to have settled on the basis of amended assessments that did not reflect his or her view of the correct legal position. Relying on *Brierley Investments* and other cases, the appellants applied to the High Court Judge to recall his primary judgment and, when that application was dismissed, appealed to the Court of Appeal.

This aspect of the Trinity litigation raised an interesting issue as to what if anything the courts could have done if of the view that the settlement was improper. The Court dealt with this question in this way:[9]

> [18] [Counsel for the appellants] was not altogether clear on where a recall of the judgment would lead. He wished to be in a position to explore in more detail the circumstances in which the settlements occurred and the state of mind of the assessing officer who issued the amended assessments. But it was not obvious to us how such an exercise would result in a better outcome for the appellants unless, in some way, the Commissioner could be required to offer to the appellants the same terms as he settled on with the other taxpayers.
>
> [19] We have some difficulty with the logic of this. In the end the correctness or otherwise of the assessments affecting the appellants depends on judgments made by the courts and not the opinion of the Commissioner. The correctness of the assessments against the appellants was upheld by Venning J and, in the judgment which we are delivering simultaneously, we dismiss the appeal against that judgment. On this basis, the appellants' complaints do not go to the merits of the dispute between them and the Commissioner but rather to the appropriateness of the Commissioner's settlements with the other taxpayers. If it were the case that the Commissioner under-taxed the other taxpayers, why would this justify the courts requiring the Commissioner to under-tax the appellants? Indeed, we conclude that the whole issue is collateral to the merits of the dispute between the appellants and the Commissioner.

The appellants' argument, as summarised, envisaged judicial review proceedings. But as these remarks indicate, I have tended to be at least doubtful as to the utility of judicial review in this context and I will return later to the significance of s 6A in relation to judicial review. As it happened, the case did not formally determine what the courts should or could do if of the view that the settlements with the other taxpayers were improper. This is because, by 2007, when this case was decided, s 6A had been applied in a number of cases in addition to *Fairbrother*.[10] As the Court of Appeal noted:[11]

> These cases all support the view that the Commissioner may settle tax litigation on a basis which does not necessarily correspond to the Commissioner's view of the correct tax position.

III PRE-ASSESSMENT AND THE CHALLENGE PROCESSES

In 2009, I gave a paper titled 'Tax Disputes'.[12] It, like this paper, had a retrospective character. I began it by noting that when I was practising, "all I needed to know about the

---

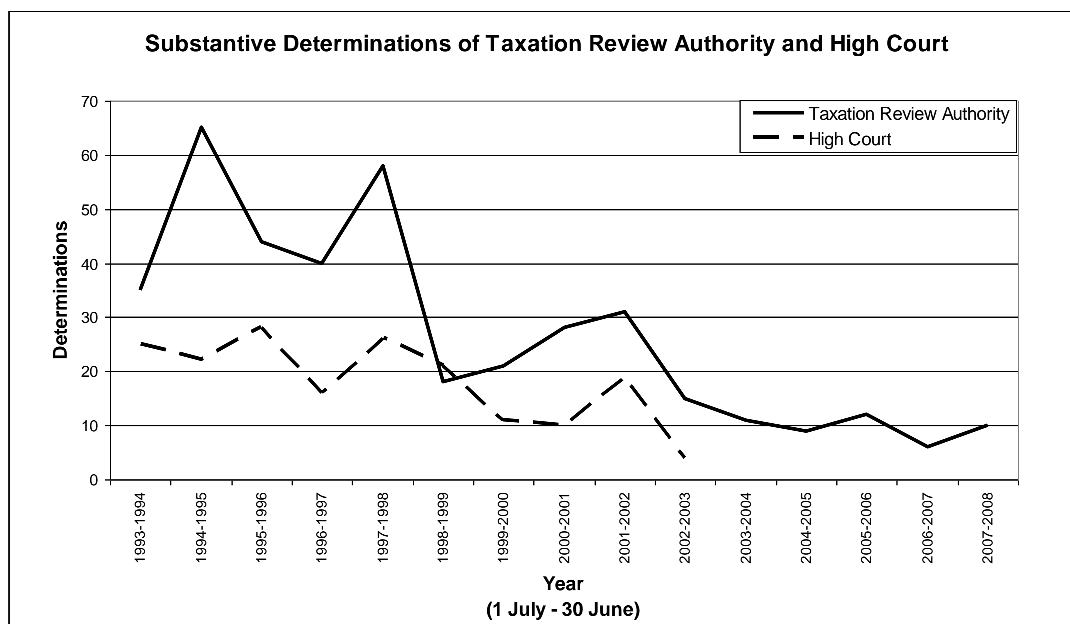
[9] *Accent Management Ltd v C of IR (No 2)* (2007) 23 NZTC 21,366 (CA).

[10] The other cases were *Chatham Islands Enterprise Trust v C of IR* [1999] 2 NZLR 388 (CA), *Auckland Gas Co Ltd v C of IR* [1999] 2 NZLR 409 (CA) and *Attorney-General v Steelfort Engineering Co Ltd* (1999) 1 NZCC ¶55-005 (CA).

[11] *Accent Management (No 2)* (n 9) [13].

[12] Sir William Young, 'Tax Disputes in New Zealand' (2009) 4 *Journal of the Australasian Tax Teachers Association* 1.

tax disputes resolution procedure could have been written on the back of an envelope"[13] and then reviewed the effect of the disputes resolution procedure introduced into the *TAA 1994* in 1996. The transition to the new regime was not entirely easy and my paper noted most of the tax disputes dealt with by the Courts at that time were about process. Associated with this, there had been a sharp decline in substantive determinations by the courts and Taxation Review Authority which I recorded in a graph:



A similar analysis through to 2013 is provided in a paper given by Glazebrook J to the ATTA Conference 9 years ago.[14] She also provided explanations for the decline in tax cases before the courts, particularly the ability to settle cases, the penalties and interest regimes and difficulties associated with the dispute resolution process. I had it in mind to carry this exercise through to the present but the factual data that would enable this is not readily accessible.

The impressions I am left with, however, are that:

(a) The large number of cases about process about which I commented in my 2009 paper were largely a function of teething difficulties with the new pre-assessment procedures and the complexities and arguments thrown up by major tax avoidance litigation involving the Trinity scheme and bank repo deals.

(b) The legal issues associated with the pre-assessment dispute procedure and the availability of judicial review have been resolved in ways that provide a context not particularly auspicious from the point of view of those minded to raise process issues.

---

[13] Ibid 1.

[14] Susan Glazebrook, 'Taxation Disputes in New Zealand' (Conference Paper, Australasian Tax Teachers Association Conference, 22 January 2013).

(c) There is currently little tax avoidance of the kind (for instance involving off-the-shelf structures) likely to result in litigation in the courts.

(d) A significant proportion of the disputes which do crystallise are settled commercially under the care and management power.

In what follows in this section, I will mention three cases which illustrate the second of the propositions just listed.

In issue in *Commissioner of Inland Revenue v Zentrum Holdings Ltd*[15] was whether, in an appeal against a Taxation Review Authority decision setting aside an assessment, it was open to the Commissioner to justify the assessment on the basis of a legal argument which had not previously been advanced. Standing in the way of the Commissioner doing so were two previous decisions of the Court of Appeal, *Commissioner of Inland Revenue v VH Farnsworth Ltd*[16] and *FB Duvall Ltd v Commissioner of Inland Revenue*.[17] These two cases were decided by reference to the *Inland Revenue Department Act 1974* (NZ). In issue was whether what had become known as the *Farnsworth* principle – that the Commissioner could not support an assessment on a basis not relied on prior to the dispute reaching the courts – was applicable to the dispute resolution process under the *TAA 1994*.

In *Zentrum*, the evidence exclusion rule in *TAA 1994* s 138G was not engaged as no disclosure notice had been given.

In rejecting the argument that the *Farnsworth* principle continued to apply, the Court reviewed the relevant provisions of *TAA 1994*, including s 138B, which provides for challenges to assessments, observing:[18]

> This section makes it clear that the nature of the challenge is an attack on the assessment itself rather than a consideration of the taxpayer's NOR. On this basis the current scheme differs from that considered in *Farnsworth*.

We later went on:

> [35] As noted, no disclosure notice was given in this case. Accordingly, the evidence exclusion rule provided for by s 138G did not apply. The existence of a specific evidence exclusion rule which applies only in specified circumstances rather suggests that outside those circumstances there is no comparable implied and absolute rule confining the parties to the positions formally taken in their NOPAs and NORs. Further – and perhaps more importantly – the existence of the discretion provided for by s 138G(2) to waive the evidence exclusion rule where a disclosure notice has been given is flatly inconsistent with the existence of such an implied and absolute rule.
>
> [36] Faced with s 138G, [counsel for the respondent] submitted that the parties are confined to their pre-assessment positions in all cases, save that where a

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15 *Commissioner of Inland Revenue v Zentrum Holdings Ltd* [2006] 1 NZLR 145 (CA).

16 *Commissioner of Inland Revenue v VH Farnsworth Ltd* [1984] 1 NZLR 428 (CA).

17 *FB Duvall Ltd v Commissioner of Inland Revenue* (2000) 19 NZTC 15,658 (CA).

18 *Zentrum* (n 15) [30].

> disclosure notice has been given the Authority or High Court has a limited discretion to permit expansion of grounds of assessment or challenge. On this basis the giving of a disclosure notice makes the subsequent procedures more, rather than less, flexible. The perversity of this result makes it clear to us that the approach contended for by [counsel for the respondent] was not intended by Parliament.
>
> [37] We are accordingly satisfied that the *Farnsworth* principle has no application under the new disputes process.

The continuing practical effect of *Zentrum* is limited by amendments to ss 89M and 89N. In most instances, these amendments require disclosure notices to be issued and thus s 138G to be triggered. But what it signals is that, in the absence of express legislative provision to the contrary, the courts can be expected to deal with tax disputes on their merits.

The other two cases I discuss in this section concern the availability of judicial review in relation to assessments. The first is the Court of Appeal decision in *Westpac Banking Corp v Commissioner of Inland Revenue*[19] and the second is the Supreme Court decision in *Tannadyce Investments Ltd v Commissioner of Inland Revenue*.[20]

TAA 1994 pt 8A provides for a challenge process under which the taxpayer may challenge an assessment either before the Taxation Review Authority or the High Court. The primarily relevant sections are ss 109 and 114, which relevantly provide:

> **109 Disputable decisions deemed correct except in proceedings**
>
> Except in … a challenge under Part 8A,—
>
> (a) no disputable decision may be disputed in a court or in any proceedings on any ground whatsoever; and
>
> (b) every disputable decision and, where relevant, all of its particulars are deemed to be, and are to be taken as being, correct in all respects.
>
> **114 Validity of assessments**
>
> An assessment made by the Commissioner is not invalidated—
>
> (a) through a failure to comply with a provision of this Act or another Inland Revenue Act; or
>
> (b) because the assessment is made wholly or partially in compliance with—
>
> (i) a direction or recommendation made by an authorised officer on matters relating to the assessment:
>
> (ii) a current policy or practice approved by the Commissioner that is applicable to matters relating to the assessment.

[19] *Westpac Banking Corp v Commissioner of Inland Revenue*, [2009] 2 NZLR 99.

[20] *Tannadyce Investments Ltd v Commissioner of Inland Revenue* [2012] 2 NZLR 153.

Understandably, the courts have always accepted that the correctness of a tax assessment should generally only be able to be challenged in objection or challenge proceedings.[21] But the courts were not willing to disavow the availability of judicial review in exceptional cases.[22] Thus, for some time, New Zealand appellate decisions supported the availability of judicial review of assessments which did not represent the genuine assessment of the Commissioner as to the tax position of the taxpayer.[23] And running through the cases was a refusal to treat *TAA 1994* ss 109 and 114 (and their precursors) as meaning what they say.

In respect of the broadly corresponding Australian legislative provisions at the time (ss 175, 175A and 177 of the *Income Tax Assessment Act 1936* (Cth)), in 2008 the High Court of Australia, in the *Futuris* case, confined judicial review to two circumstances: first, where what is said to be an assessment is not in truth an assessment; and secondly, where there has been conscious maladministration. These two concepts were, to some extent, run together, with both seen as not producing an assessment that is immune from judicial review.[24]

The availability of judicial review was considered by the Court of Appeal in relation to challenges under s BG 1 of the *Income Tax Act 1994* (NZ) to repo deals entered into by a number of banks including Westpac. In the case of Westpac, there were 10 such transactions. In relation to one (the First Data transaction), Westpac had obtained a binding ruling as to the non-applicability of s BG 1. There were differences of opinion within the Inland Revenue Department between the two sections primarily involved (Rulings and Corporates). Some years later, the Commissioner issued amended assessments in relation to the other nine transactions. Westpac responded with both challenge and judicial review proceedings. The judicial review proceedings were premised on the contention that there was an unacceptable inconsistency of approach between the amended assessments and the treatment of the First Data and some other similar transactions.

The approach we adopted was as follows:[25]

> [59] We think it appropriate to continue to apply the established principles as to judicial review in tax cases. We accept that judicial review is available where what purports to be an assessment is not an assessment. Associated with this, we accept that judicial review is available in exceptional cases and thus may be available in cases of conscious maladministration (as was recognised in *Futuris*). We can reconcile this with ss 109 and 114 on the basis that in such cases (that is, no genuine assessment or conscious maladministration) what is challenged is either not an assessment or, at the least, not the sort of assessment which the legislature had in mind in enacting

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21 *Commissioner of Inland Revenue v Lemmington Holdings Ltd* [1982] 1 NZLR 517 (CA); and *Miller v Commissioner of Inland Revenue* [1995] 3 NZLR 664 (CA).

22 *Miller v Commissioner of Inland Revenue* [2001] 3 NZLR 316 (PC), [18].

23 *Commissioner of Inland Revenue v Canterbury Frozen Meat Co Ltd* [1994] 2 NZLR 681 (CA).

24 *Commissioner of Taxation v Futuris Corp Ltd* (2008) 237 CLR 146.

25 *Westpac Banking Corp* (n 19) [59]-[64].

> those sections. On this basis we see the availability of judicial review as depending on the claimant establishing exceptional circumstances of a kind which results in the amended assessment falling outside the scope of ss 109 and 114 and thereby not engaging those sections.

We were, however, unenthusiastic about the appropriateness of judicial review both generally in tax cases and in relation to the case at hand:

> [60] … A taxpayer who seeks judicial review of an assessment might be thought to be disputing it and doing so in flat defiance of s 109(a). Section 109(b) deems an assessment to be "correct in all respects" which might be thought to necessarily extend to its validity. In the context of the present case, we have difficulty with reconciling the statutory requirement that the 1999 amended assessment be taken as "correct in all respects" with the proposition advanced by Westpac that it is none the less invalid and ineffective.
>
> [61] We also consider that the broad approach contended for by Westpac places too much emphasis on the assessment as an exercise of a statutory power of decision. An assessment should reflect the correct tax position and a taxpayer's liability to pay tax exists independently of the assessment. If the assessment is correct, it is hard to see why complaints about process should result in the taxpayer not paying tax on a correct basis. Where there are very large sums of tax at stake (as there are here), this raises fairness considerations in relation to other taxpayers who have met their liabilities for the tax year concerned. If the assessment is wrong, it can be corrected in later challenge proceedings. If it is correct, the tax should be paid. It is frankly difficult to see what is unfair in this approach.
>
> [62] Further, it is perfectly clear that allowing collateral challenge to assessments through judicial review can provide scope for gaming and diversionary behaviour.
>
> [63] In the past taxpayers going down the judicial review route have often sought to delay the statutory processes (whether prior to, or after, assessment) until the judicial review proceedings are completed; this on the ostensibly sensible ground that until the judicial review claim is determined it is premature to proceed with the statutory process. The response of the courts has been to require the review claim to be brought in the same proceedings as the challenge. But this is not necessarily an answer to the potential for judicial review to lead to delay, as illustrated by an unsuccessful attempt by Westpac in this case to have its validity cause of actions heard first.
>
> [64] Collateral challenge involves not just delay but also diversion of effort and resources. The challenge proceedings between Westpac and the Commissioner will be complex and will fully engage the attention and resources of the Commissioner and the Court. The validity cause of action involves an attempt by Westpac to turn the case back on to the Commissioner. If it goes to trial, considerable resources which might otherwise have been devoted to the primary issue between the parties will be diverted to an inquiry into the internal processes of IRD. This inquiry will throw up questions which are, on the one hand, difficult and nuanced (as to the subtleties of the differences of approach adopted by Rulings and Corporates) but, on the other, entirely irrelevant to whether Westpac owes the tax it has been assessed to pay, which in the end will turn on the Judge's approach to s BG 1.

When the issue was revisited by the Supreme Court in *Tannadyce Investments Ltd v Commissioner of Inland Revenue*,[26] the approach taken in *Westpac* came in for some criticism: from the minority, as too restrictive of judicial review, and, from the majority, as insufficiently deferential to ss 109 and 114.

The minority commented:

> [29] The judgment in *Westpac* did not, however, address the line of authority of the Court of Appeal and Privy Council under the 1976 Act's provisions, which has sought not only to give general priority to statutory challenges to assessments, but also to recognise that in some cases they will not address rule of law considerations as adequately as judicial review. As there is no significant change in the current statutory scheme or relevant provisions from that under the 1976 legislation, the Court of Appeal should not have approached the 1996 provisions as if they were new legislation.

But in contradistinction, the majority observed:[27]

> … we do not consider the *Westpac* Court, and hence the Court [of Appeal] in the present case, gave enough weight to the purpose of s 109, in particular when that section is considered against the availability of resort to the High Court when a challenge is made under Part 8A, and the breadth of a hearing authority's powers under that Part. We have already referred to the Court's strong inclination to read sections like s 109 in a way that preserves the availability of judicial review to deal, at least, with matters of vitiation which render the decision involved no decision in law at all. But that is not the right way to approach s 109 in its particular statutory context. By insisting that the statutory disputes and challenge processes be followed, as s 109 does, Parliament has not deprived taxpayers of the ability to have all their concerns about tax assessments determined by the High Court. The legislative policy evident in s 109 is not at odds with the right of citizens to have matters of legality determined by the High Court. There is therefore no reason to read down, on the premise of presumed parliamentary purpose, the clear and unequivocal words of s 109 and, in particular, its use of the words "on any ground whatsoever".

Judges who have favoured the availability of judicial review of tax decisions give considerable relevance to the public law character of the Commissioner's powers and associated rule of law considerations. By way of contrast, some of us who have resisted the availability of judicial review have tended to see tax disputes as primarily about whether tax is or is not owed, a question that can usually (and perhaps always) be appropriately addressed independently of inquiry into the propriety of the Commissioner's actions.

Contrary to the view expressed by the minority in *Tannadyce*, the Court in *Westpac* did rely on one feature of the current statutory framework which was not part of the 1976 legislative provisions applied in the Court of Appeal and Privy Council decisions referred to. This was *TAA 1994* s 6A. As is apparent from what I have earlier said, it was heavily relied on in *Accent Management* as validating assessments that did not necessarily reflect

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[26] *Tannadyce Investments* (n 20).

[27] Ibid [67].

the Commissioner's view of the tax position. This is not, in itself, a complete answer to the rule of law concerns of the minority, but it is of at least some relevance to the debate. Also of relevance is the point noted in both the *Accent Management* (recall) and *Westpac* cases that, if the Judge determining a challenge concludes that tax is owed, earlier procedural infelicities on the part of the Commissioner are unlikely to be of any practical moment.[28]

On the approach of the majority in *Tannadyce*, the conflicting approaches are resolved pragmatically, on the basis that the challenge procedure offers all opportunity required for fair challenge to an assessment.

IV TAX AVOIDANCE

A general anti-avoidance rule ('GAAR') of sorts was included in the *Land and Income Assessment Act 1891* (NZ)[29] and a more sophisticated version of this provision, recognisably a precursor to the current s BG 1, was introduced in 1900.[30] But, until the 1960s, anti-avoidance was largely left to the legislature.[31]

The fundamental problem with the application of the GAAR is that it sits extremely awkwardly in the highly prescriptive legislative context provided by the Income Tax Act. Orthodox statutory interpretation principles provide, at best, only limited assistance. Indeed, to my way of thinking orthodox statutory interpretation techniques were simply not up to the task of making sense of the overall (that is GAAR-inclusive) legislative scheme. I consider that this is illustrated by the twists and turns and associated incoherence and indeterminacy of some of the pre-*Ben Nevis* jurisprudence as to the application of the GAAR. It is also the point to which Lord Wilberforce was referring in *Mangin v Commissioner of Inland Revenue* when he commented:[32]

> It is because I believe that the limits of judicial interpretation, however liberal or common sense the process may be claimed to be, are passed when one comes to attempt to apply the New Zealand section to this present case that I cannot agree with the Board's decision. I think that we have here a rusty instrument which breaks in our hands and is no longer capable of repair.

Despite the apparently insoluble difficulties alluded to by Lord Wilberforce, the GAAR continued to be part of the New Zealand income tax system. Indeed, amendments made to it, starting in 1974, were indicative of a clear legislative purpose that the GAAR should continue to be used, perhaps more frequently and certainly more effectively.

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[28] *Accent Management Ltd (No 2)*, above n 9, at [18]–[19]; and *Westpac* (n 19) [61].

[29] There was an earlier anti-avoidance provision in relation to land tax in the *Land Tax Act 1878 (NZ)*.

[30] *Land and Income Assessment Act 1900* (NZ) s 82.

[31] The only case prior to the 1960s in which a precursor to s BG 1 was invoked was *Timaru Herald Co Ltd v Commissioner of Taxes* [1938] NZLR 978 (CA).

[32] *Mangin v Commissioner of Inland Revenue* [1971] NZLR 591 (PC), 603.

The subsequent history is well-known. It is, as well, the subject of a paper I gave in 2016[33] in which I reviewed in detail the jurisprudence leading up to, and including, *Ben Nevis* and *Penny v Commissioner of Inland Revenue* (*Penny and Hooper*).[34] I do not propose to repeat what I said in that paper.

The consistency of the approaches taken in *Ben Nevis* and *Penny and Hooper* and, most recently in *Frucor Suntory Ltd v Commissioner of Inland Revenue*[35] represent a break from the discontinuities that were a feature of the Privy Council tax avoidance jurisprudence, as discussed in my 2016 paper. The formulation of a single, overarching test[36] marks a change from the indeterminacy that characterised some of the earlier jurisprudence. Also, and more generally – and this is something which has been discussed by many commentators – *Ben Nevis* and *Penny and Hooper* (and now *Frucor* as well) exemplify something of an attitudinal change in relation to tax avoidance.

As is demonstrated by the difference between the majority and minority judgments in *Frucor*, particularly as to shortfall penalties, there remains scope for more than one view as to whether *Ben Nevis* represented a sharp discontinuity with the earlier jurisprudence (essentially the position adopted in the minority judgment) or, alternatively, was at least consistent with a well-established line of authority that the GAAR applied to contrived and artificial arrangements securing apparent tax advantages for taxpayers who had not suffered the economic burden which such advantages were meant to mitigate.[37]

V WHAT COMES OUT OF ALL THIS?

As will be apparent, I was personally involved as a judge in most of the cases I have discussed and, in other cases, judgments for which I had had primary responsibility came under scrutiny. This means that I have a reasonably good understanding of the minutiae of the issues involved. But this level of personal involvement means that I am not particularly well placed to assess the significance of what has happened. And, in any event, given the disparate nature of the topics I have considered, the identification of a theme may be a little artificial. But these reservations notwithstanding, I think that I can discern something of a thread which runs through what has happened – demystification.

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33 William Young, 'The Evolution of the Approach of the New Zealand Courts to Tax Avoidance' (2016) 11 *Journal of the Australasian Tax Teachers Association* 1.

34 *Penny v Commissioner of Inland Revenue* [2011] 1 NZLR 433 [*Penny and Hooper*].

35 *Frucor Suntory New Zealand Ltd v Commissioner of Inland Revenue* [2022] NZSC 13.

36 The majority in *Ben Nevis* formulated a two-stage test for tax avoidance. The first step is whether the use made of any specific provision/s was within the intended scope of the provision/s and the second is whether the taxpayer's use of the provision/s, viewed in light of the arrangement as a whole, was outside the contemplation of Parliament when it enacted the provision/s: see *Ben Nevis* (n 3) [107] per Tipping, McGrath and Gault JJ. With some explanation of, or perhaps adjustment to, the first step, this test was approved in *Frucor*.

37 The cases included *Challenge Corporation Ltd v Commissioner of Inland Revenue* [1986] 2 NZLR 513 (PC); *Commissioner of Inland Revenue v Auckland Harbour Board* [2001] 3 NZLR 289; and *Peterson v Commissioner of Inland Revenue* [2006] 2 NZLR 433.

Tax litigation has come to be treated in very much the same way as other litigation about money. The focus is on what, if anything, is owed. The parties, including the Commissioner, can approach tax disputes in the courts in a pragmatic way, settling, if they choose, on a basis that reflects the risks and benefits of litigation options. The courts likewise have increasingly put to one side distracting procedural issues in order to better concentrate on whether tax is due and, if so, how much is owed. And this same process of demystification has been applied to tax avoidance. The indeterminacy of some of the jurisprudence prior to *Ben Nevis* along with the twists and turns that the law had taken since the 1960s meant that the law was inaccessible to those without a deep knowledge of a significant number of cases. That is no longer the case, with *Ben Nevis*, *Penny and Hooper* and *Frucor* providing a coherent framework – collectively perhaps a single source of truth – within, or against, which most cases can be assessed.

WORK-INTEGRATED LEARNING FOR INTERNATIONAL STUDENTS: DEVELOPING SELF-EFFICACY THROUGH THE AUSTRALIAN NATIONAL TAX CLINIC PROGRAM

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ABSTRACT

This article considers the impact of the work-integrated learning ('WIL') experience as part of Australia's National Tax Clinic Program ('NTCP') on the self-efficacy of international students studying in Australia. Through a pre and post survey the results demonstrate that participation in the NTCP had a positive impact on the self-efficacy of international students to a larger extent than domestic students. The WIL experience substantially increased the confidence of international students in relation to applying taxation law, communication, teamwork, presenting ideas and taxation research. In addition, international students were more confident in achieving their career goals and understanding what is expected of them as a professional advisor. This study provides empirical evidence of the benefits of WIL for international students. The findings have implications for educational professionals as they design future degree courses which aim to improve both the student experience and employability outcomes of international students.

Keywords: accounting, consulting, international students, self-efficacy, tax clinic, work-integrated learning (WIL)

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I INTRODUCTION

The international student market is challenging for many countries around the world, with the globalisation of education through cross-border study increasing to 5.3 million students by 2017.[1] While Covid-19 has limited this market due to restrictions on travelling, countries are considering what the post-Covid international student market may look like. This includes how opportunities for work-integrated learning ('WIL') could provide an enhanced experience,[2] and improve international students' confidence to pursue their future careers.

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1 OECD, *Education at a Glance 2019: OECD Indicators* (OECD Publishing, 2019).

2 Craig Cameron and Anne Hewitt, *Facilitating student engagement with WIL: A risk management framework for studentships*. Final Report (ACEN, 2022).

Prior to the Covid-19 outbreak, international education was a major revenue source for Australia with international student revenue reaching $8.9 billion in 2018, representing almost a quarter of total university revenue.[3] Of the international students in Australia, almost 50% enrol in management and commerce programs,[4] with accounting students making up 10% of all international student enrolments in Bachelor level and above programs in 2019 (pre-Covid-19).[5]

In addition to the revenue that international students can provide to universities, they potentially provide a source of skilled migration to address skill shortages. Labour force demands in the accounting sector in Australia have exceeded supply for several years, and a skills shortage has largely been blamed on the unsuitability of candidates applying for the positions.[6] Thus, the effectiveness of domestic and international accounting students in meeting this skills shortage is questionable. This issue is expected to be exacerbated post Covid-19 as demand for accountants increases due to the heavy reliance on accounting professionals in supporting individuals and businesses manage the impacts of Covid-19 and aid in the nation's economic recovery.[7] While the Covid-19 pandemic saw unprecedented job losses across many sectors of the economy, the demand for accounting and finance professionals increased by close to 10% from February 2020 to February 2021[8] and there is an expectation that their workload will continue to increase in the future.[9] As part of this dynamic environment, increasing globalisation and technological advances have presented a new set of skills requirements that place greater emphasis on soft skills such as communication, critical thinking, problem solving, and organisation and time management.[10]

However, concerns have been raised as to whether international students have the confidence (self-efficacy) and skills to successfully transition to the work force. Previous research in Australia has indicated that many international students have not been

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[3] J Smyth, 'Australian business schools: will overseas students return?' *Financial Times* (London, 28 October 2020).

[4] Universities Australia, *Work Integrated Learning in Universities: Final Report* (Universities Australia, April 2019).

[5] Chartered Accountants ANZ and CPA Australia, *Inquiry into Australia's skilled migration program: part 1 of 2*, Submission 45 (27 February 2021).

[6] Department of Employment, *Labour Market Research – Accountants* (Commonwealth of Australia, 2017).

[7] Jotham Lian, 'No demand shortage: Predictions for the profession in 2021' *Accountants Daily* (Web Page, 14 January 2021) <https://www.accountantsdaily.com.au/regulation/15244-no-demand-shortage-predictions-for-the-profession-in-2021>.

[8] Australian Bureau of Statistics (ABS), *Labour Force, Australia, Detailed: May 2021* (Commonwealth of Australia, 2021).

[9] Tasha Levy, 'How COVID-19 has been impacting accountants across Australia' *Accountants Daily* (Web Page, 15 May 2020) <https://www.accountantsdaily.com.au/business/14365-how-covid-19-has-been-impacting-accountants-across-australia>.

[10] Deloitte Touche Tohmatsu, 'The path to prosperity: Why the future of work is human' *Deloitte Insights*. Building the Lucky Country #7 (2019).

provided sufficient opportunity to develop their employability skills while studying in Australia.[11] WIL is seen as a prime opportunity to develop students' employability,[12] and their self-efficacy to pursue their careers.[13] In its purest form, WIL involves students undertaking authentic activities where they engage directly with industry and/or the community as part of their formal learning and assessment in their degree studies, such as in a consulting type role.[14] WIL can help international students develop their communication and language skills, as well as increasing knowledge of their host country's workplace culture; all areas where international students have expressed a lack of confidence.[15]

A combination of labour market demands, employability outcomes of graduates and changing skills requirements of accounting professionals has placed more attention on the importance of WIL in improving student employability.[16] Further, the introduction of the government's 'Job-ready Graduates Package'[17] and changes to government funding of universities, which is now partially tied to graduates' employability outcomes[18] has led to greater interest in improving students' readiness for future work.

Part of this readiness for future work is a student's confidence, self-efficacy, which describes how strongly a person believes in their own general capabilities to face challenges, as well as to complete specific tasks.[19] Understanding a person's self-efficacy is important, as these beliefs can influence the ability to function and take on future challenges. WIL has been demonstrated to improve the self-efficacy of students involved.[20] A student's self-efficacy may play an important role in their preparing for work

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[11] Jill Blackmore et al, *Australian international graduates and the transition to employment* (Deakin University, 2014); Cate Gribble, 'Employment, work placements and work integrated learning of international students in Australia' (IEAA Research Digest No 2, International Education Association of Australia, June 2014); Dennis Murray, Jill Blackmore, Cate Gribble and Rebecca Hall, *Internships and work placement opportunities for international students in Victoria* (International Education Association of Australia, 2012).

[12] Bonnie Amelia Dean, Stephanie Perkiss, Milica Simic Misic and Karina Luzia, 'Transforming accounting curricula to enhance integrative learning' (2018) 60(3) *Accounting & Finance* 2301; Denise Jackson and Stephanie Meek, 'Embedding Work-integrated Learning into Accounting Education: The State of Play and Pathways to Future Implementation' (2021) 30(1) *Accounting Education* 63.

[13] Brett Freudenberg, Craig Cameron and Mark Brimble, 'The Importance of Self: Developing Students' Self Efficacy Through Work Integrated Learning' (2010) 17(10) *International Journal of Learning* 479.

[14] Denise Jackson, 'Students' and their supervisors' evaluations on professional identity in work placements' (2018) 12(2) *Vocations and Learning* 245; Jackson and Meek (n 12).

[15] Universities Australia (n 4).

[16] Dean, Perkiss, Milica Misic and Luzia (n 12); Jackson and Meek (n 12).

[17] Australian Government, *Job-ready Graduates Package* (Commonwealth of Australia, 2020).

[18] Australian Government, *Performance-based funding for the Commonwealth grant scheme* (Commonwealth of Australia, 2019).

[19] Albert Bandura, 'Self-Efficacy: Toward a Unifying Theory of Behavioral Change' (1977) 84(2) *Psychological Review* 191.

[20] Freudenberg, Cameron and Brimble (n 13).

in the real-world in that it allows students to see that they have the agency and perceived capability to manage their career choices.[21] With higher levels of self-efficacy, students can devote more effort toward career planning,[22] and this can be important in building the next generation of professionals.

However, there can be barriers for international students to undertake a WIL experience, such as visa restrictions, financial pressures, and perceived language difficulties.[23] For universities, the employability outcomes of international students are of growing importance, especially since these can impact on higher education institutions' rankings. Examples include the QS Graduate Employability Ranking as part of the QS World University Rankings[24] and the Global University Employability Ranking published by Times Higher Education.[25] However, it is questionable whether universities have adequate structures and resources in place to produce accounting graduates that are job ready.[26]

One recent WIL innovation implemented in Australia is the National Tax Clinic Program ('NTCP') which commenced in 2019. This saw ten Australian universities being funded by the Australian Federal Government to operate student tax clinics.[27] These clinics allow university tax students (under the supervision of tax professionals) to provide free tax advice, advocacy, and education to community members, and as such can be categorised as a 'consulting WIL'.[28] These community members can include low-income individuals, recent immigrants, recovering addicts, people returning to work and those operating micro businesses, many of whom would otherwise fall through the cracks in meeting their tax obligations.[29] The matters that students can assist clients with include completing tax returns, advising on proposed business activities, advocating on a client's behalf with the tax authority, and assistance with objections to tax assessments.

The present study seeks to determine the impact of this authentic WIL consulting experience on the self-efficacy of international students studying in Australia. It specifically considers the differences between domestic and international students and

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[21] Daniela Spanjaard, Tim Hall and Nicole Stegemann, 'Experiential Learning: Helping Students to Become 'Career Ready' (2018) 26 *Australasian Marketing Journal* 163.

[22] Ibid.

[23] Gribble (n 11).

[24] Quacquarelli Symonds Ltd, *In the QS World University Rankings: Graduate Employability Rankings* (2021).

[25] Times Higher Education Ltd, *Best universities for graduate jobs: Global University Employability Ranking 2020* (2021).

[26] Mark Brimble and Brett Freudenberg, 'Will WIL'ing work?' (2010) 28 *B-HERT Newsletter* 2.

[27] Donovan Castelyn, Stephanie Bruce and Annette Morgan, '2019 National Tax Clinic Project: Curtin University – Curtin Tax Clinic' (2020) 22(2) *Journal of Australian Taxation* 1.

[28] Jackson and Meek (n 12).

[29] Stuart Robert, [The Hon Stuart Robert MP Assistant Treasurer], Address to the Australasian Tax Teachers Association 31st Annual conference, Speech: Duxton Hotel, Perth, 16 January 2019.

makes an important contribution to the literature on the importance of WIL for international students' self-efficacy and employment prospects in accounting and taxation, with significant improvements found across several dimensions of self-efficacy. It also provides a practical contribution to the higher education sector, the profession, and policymakers by showcasing the benefits of a national WIL program in developing and preparing a diverse cohort of students to become the next generation of accounting and tax professionals.

This article commences with a review of the literature on WIL and tax clinics, followed by an examination of the role of WIL in developing self-efficacy and discussion about WIL and international students. An outline of the research methodology adopted in the study are then presented, followed by the research findings. The article ends with an overview of the limitations, possible future research, and contributions of the research for tertiary education before concluding.

II LITERATURE REVIEW AND THEORETICAL FRAMEWORK

To understand how the tax clinics may influence international students' self-efficacy, this section discusses WIL in terms of a tax clinic setting, followed by how WIL could influence self-efficacy, and then what the international student experience may be in this regard.

A *WIL AND TAX CLINICS*

University tax clinics provide a unique WIL opportunity to accounting and taxation students as they participate in organised activities that benefit the community. Such participation builds practical experience for students who may become future accountants and/or tax professionals as they have first-hand experience in tax research, accounting and taxation software, preparation of tax documentation, and most importantly, taxpayer interaction. The real-world aspect of tax clinics allows students to develop communication skills, problem solving skills, tax research skills, and social awareness.[30] Tax clinics have been offering services to low-income taxpayers in the United States since the 1990s and this has extended to other jurisdictions including Australia, Canada, and the United Kingdom.[31] Tax clinics have been reported to bridge the gap between academic preparation, the professional workplace and volunteerism[32] and have

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30 Susan E Anderson and Christine C Bauman, 'Low-income Taxpayer Clinics as a form of service learning' in BN Schwartz and JE Ketz (eds), *Advances in Accounting Education Teaching and Curriculum Innovations* (*Advances in Accounting Education, Vol. 6*) (Emerald Group Publishing Limited, 2004) 117-132.

31 Ann Kayis-Kumar, Jack Noone, Fiona Martin and Michael Walpole, 'Pro Bono Tax Clinics: An international comparison and framework for evidence-based evaluation' (2020) 49(2) *Australian Tax Review* 110.

32 C David Strupeck and Donna Whitten, 'Accounting service-learning experiences and the IRS volunteer income tax assistance programme: a teaching note' (2004) 13(1) *Accounting Education* 101; T Keith Fogg, 'History of Low-Income Taxpayer Clinics' (Research Paper No 2013-3005, Villanova Law/Public Policy, 2012).

found that helping those less fortunate, interacting with taxpayers, and applying the taxation legislation to be some of the major benefits of this WIL activity.[33]

The definition of WIL is broad and varies across universities, discipline areas and stages of study in terms of duration and scope. WIL activities can be for-credit or not-for-credit and include field trips, industry-based projects, internships, placements, service learning and simulations.[34] Common amongst all WIL programs and activities is the key objective to provide opportunities for students to gain 'hands-on experience in a real-world environment'.[35] Jackson and Meek review various emergent forms of WIL in accounting, referring to tax clinics as an example of a consulting arrangement.[36] Consulting involves 'students (individually or in teams) providing consultancy services and information to others, including other students, industry partners and community organisations'.[37]

In the Australian higher education sector, tax clinics require students to directly interact with members of the community, including low-income individuals and small business taxpayers, about matters relating to taxation including the meaning and operation of a tax law, lodgement of tax returns and business activity statements and tax debt, under the guidance of a tax professional.[38] Tax clinics also allow students to gain experience in important non-technical skills including conducting meetings, listening to client issues, note-taking, conducting research, time management, and working co-operatively with their peers and supervisor. Tax clinics are essentially a professional tax practice operating within a university.

Tax clinics benefit taxpayers who utilise the free service as well as the students who apply their theoretical knowledge in a practical way.[39] As a result, tax clinics provide substantial WIL benefits similar to the more well-known and established clinical experiences offered in law, medicine, nursing, and teaching.[40] The tax clinic experience also fills a gap in accounting programs, as while there is strong support for WIL in the accounting

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[33] Anderson and Bauman (n 30).

[34] Martin Smith et al, 'Career development learning: Maximising the contribution of work-integrated learning to the student experience (Australian Learning & Teaching Council: Final Project Report', University of Southern Queensland Wollongong (Report, 2009) <https://research.usq.edu.au/item/9z163/career-development-learning-maximising-the-contribution-of-work-integrated-learning-to-the-student-experience-final-project-report-june-2009>.

[35] Ly Thi Tran and Sri Soejatminah, 'Get foot in the door: International students' perceptions of work integrated learning' (2016) 64(3) *British Journal of Educational Studies* 337, 341.

[36] Jackson and Meek (n 12).

[37] WIL Innovation, 'Innovative Working Integrated Learning Models', *Australian Collaborative Education Network* (Web Page, 2018) <https://wil-innovation.acen.edu.au/>.

[38] Castelyn, Bruce and Morgan (n 27).

[39] Jotham Lian, 'Trial tax clinics a hit with community, educators' *Accountants Daily* (Web Page, 8 July 2019) <https://www.accountantsdaily.com.au/tax-compliance/13249-trial-tax-clinics-a-hit-with-community-educators>; Jackson and Meek (n 12).

[40] C Bauman, 'The IRS appeals process - case method and tax clinics' (2001) (August) *The Tax Adviser* 558.

discipline,[41] there remains a lack of focus on offering authentic WIL experiences in the accounting curriculum.[42] Successful examples of how WIL has been integrated into the curriculum, such as tax clinics, can prove useful to accounting educators by both highlighting the benefits for student employability and by providing a framework on which to base their student learning activities. The integration of tax clinics within the accounting and taxation curriculum also supports calls for more authentic, 'true' forms of WIL such as consulting, that goes beyond internships and simulations by engaging diverse student cohorts in formal interaction with the community and industry to effectively achieve graduate outcomes that meet the needs of the accounting profession.[43]

There is a large amount of literature demonstrating the benefits gained by students participating in WIL activities, as it can enhance student employability[44] and provide students with the generic skills needed to transition into, and function effectively in the workplace.[45] WIL has been found to build non-technical skills such as active listening, communication, emotional intelligence, negotiation, reasoning skills and team-building,[46]

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[41] Trevor Stanley and Jia Xu, 'Work-Integrated Learning in accountancy at Australian universities – forms, future role and challenges' (2019) 28(1) *Accounting Education* 1.

[42] Gemma K Lewis, Belinda Williams, Stephen Allen, Beverly Goldfarb, Kevin Lyall, Rose Kling and Peta Statham, 'Developing an evaluation tool to provide a 360-degree reflection on work-integrated learning in accounting education' (2021) 30(6) *Accounting Education* 601.

[43] Jackson and Meek (n 12).

[44] Gay Crebert, Merrelyn Bates, Barry Bell, Carol-Joy Patrick and Vanda Cragnolini, 'Developing generic skills at university, during work placement and in employment: Graduates' perceptions' (2004) 23(2) *Higher Education Research & Development* 147; Greg Ryan, Susan Toohey and Chris Hughes, 'The purpose, value and structure of the practicum in higher education: a literature review' (1996) 31 *Higher Education* 355.

[45] Brett Freudenberg, Mark Brimble and Craig Cameron, 'WIL and generic skill development: The development of business students' generic skills through work-integrated learning' (2011) 12(2) *Asia-Pacific Journal of Cooperative Education* 79; Denise Jackson, 'Employability skill development in work-integrated learning: Barriers and best practice' (2015) 40(2) *Studies in Higher Education* 350; Marie Kavanagh and Lyndal Drennan, 'What Skills and Attributes Does an Accounting Graduate Need?' (2008) 48 *Accounting and Finance* 279.

[46] P Anderson and P Green, '(L)earning for employability, lessons for HE?' (Seminar Paper, University of Wolverhampton, 2006); Georgina Barton, Kay Hartwig and Anh Hai Le, 'International Students' Perceptions of Workplace Experiences in Australian Study Programs: A Large-Scale Survey' (2019) 23(2) *Journal of Studies in International Education* 248; Cate Gribble and N. McRae, 'Creating a climate for global WIL: Barriers to participation and strategies for enhancing international students' involvement in WIL in Canada and Australia'. In G Barton and K Hartwig (eds), *Professional Learning in the Work Place for International Students: Exploring theory and practice* (Springer, 2015) 35-56; Brenda Little and Lee Harvey, *Learning through work placements and beyond*. A report for HECSU and the Higher Education Academy's Work Placements Organisation Forum (Manchester, 2006); Emma Nicholls and Margaret Walsh, 'University of Wolverhampton case study: Embedding practical work-based modules into a traditionally, theoretical programme' (2007) 49(3) *Education & Training* 201.

and to improve technically oriented skills such as analysis, critical thinking and problem solving.[47] Also, WIL can improve the professional identity of those students involved.[48]

As a WIL activity, the tax clinic experience may offer many benefits,[49] and could build both the technical and non-technical skills of student participants. Related to this, it is expected that the tax clinic experience will assist in building students' self-efficacy,[50] as they have opportunities to interact with the public and be mentored by tax professionals as they solve actual taxation problems; an aspect which is explored in more detail next.

B *WIL and Self-efficacy*

How strongly a student believes in their own capabilities to complete task requirements (such as those required by a tax professional) may also influence their ability to function and consequently perform the tasks; this is known as 'self-efficacy'.[51] It follows that the way in which students approach their learning about the nature of professional work can be affected by how they perceive task requirements,[52] as well as the specific learning context in which they learn these.[53]

Self-efficacy can be considered as having two dimensions: general and task-specific. General self-efficacy refers to how one perceives their capabilities more generally, given a wide range of situations. Conversely, task-specific self-efficacy is concerned with perceptions of capabilities with regards to a specific domain or tasks.[54] Since WIL is an

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47 John Hattie, HW Marsh, James T Neill and Garry E Richards, 'Adventure education and Outward Bound: Out-of-Class Experiences That Make a Lasting Difference' (1997) 67(1) *Review of Educational Research* 43; Peter Reddy and Elisabeth Moores, 'Placement year academic benefit revisited: Effects of demographics, prior achievement and degree program' (2012) 17(2) *Teaching in Higher Education* 153.

48 Kristen MacDonald, Craig Cameron, Mark Brimble, Brett Freudenberg and Dianne English, 'Realizing the professional within: The effect of work integrated learning' (2014) 15(2) *Asia-Pacific Journal of Cooperative Education* 159.

49 Anderson and Bauman (n 30); J Gold, 'Funding for tax preparation needed for low-income taxpayers' (2002) July *Tax Notes* 439; NE Olson, 'Low-income taxpayer clinics: A challenge to tax professionals' (1998) *Exempt Organization Tax Review* 291; Janet Spragens and Nina Olson, 'Tax clinics: The new face of legal services' (18 September 2000) *Tax Notes* 1525.

50 Freudenberg, Cameron and Brimble (n 13).

51 Bandura, 'Self-Efficacy: Toward a Unifying Theory of Behavioral Change' (n 19).

52 Michelle Cull and Glenda Davis, 'Students' Perceptions of a Scaffolded Approach to Learning Financial Planning: An Empirical Study' (2013) 22(2) *Accounting Education: an international journal* 125; Linda English, Peter Luckett and Rosina Mladenovic, 'Encouraging a deep approach to learning through curriculum design' (2004) 13(4) *Accounting Education: an international journal* 461.

53 L Gow, D Kember and B Cooper, 'The teaching context and approaches to study of accountancy students' (1994) 9(1) *Issues in Accounting Education* 118.

54 Albert Bandura, *Self-Efficacy: The Exercise of Control* (WH Freeman, 1997).

'active and contextualised experience',[55] it can provide a fertile environment in which to improve self-efficacy.[56] As a result, it is expected that the tax clinic experience would enhance students' self-efficacy, especially in skills areas that are in high demand by the accounting profession.

WIL enables students to develop self-efficacy across all four categories of experiences: mastery, modelling, social persuasion, and self-awareness of physiological.[57] Through WIL experiences, such as those offered by the NTCP and examined in this study, students are provided with an opportunity to 'master' a skill by practising what they were taught in class.[58] Students are also exposed to modelling while they observe their supervisors or other students deal with difficult tasks, in addition to social persuasion when they receive feedback on their performance from supervisors and their peers.[59] In addition, self-awareness of their own physiological state when confronted with a particular task can be useful for students in improving their self-efficacy.[60]

Students can both develop and reflect on their self-efficacy by participating in a WIL program. This is important to improve accuracy of self-efficacy judgment[61] which can later become a substitute for external guidance.[62] Furthermore, as students increase their self-efficacy, they are more likely to take on more challenging goals.[63] Thus, WIL programs that provide mastery and vicarious experiences with opportunities for feedback and self-reflection can assist with students' appraisal of their own capabilities while also

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55 Belinda Mclennan and Shay Keating, *Work integrated learning (WIL) in Australian universities: the challenges of mainstreaming WIL*. ALTC NAGCAS National Symposium (ALTC, 2008).

56 Brimble and Freudenberg (n 26); David Edwards, 'Improving student achievement through industry placement', *Proceedings from International Conference on Engineering Education (ICEE)* (2007).

57 Albert Bandura, 'Self-Efficacy Mechanism in Human Agency' (1982) 37(2) *American Psychologist* 122; Sanjib Chowdhury, Megan Lee Endres and Thomas W Lanis, 'Preparing Students for Success in Team Work Environments: The Importance of Building Confidence' (2002) 14(3) *Journal of Managerial Issues* 346; Nava Subramaniam and Brett Freudenberg, 'Preparing Accounting Students for Success in the Professional Environment: Enhancing Self-Efficacy Through a Work Integrated Learning Program' (2007) 8(1) *Asia-Pacific Journal of Cooperative Education* 7; Robert Wood and Albert Bandura, 'Social Cognitive Theory of Organizational Management' (1989) 14(3) *Academy of Management Review* 361.

58 Mary L Tucker and Anne M McCarthy, 'Presentation Self-Efficacy: Increasing Communication Skills Through Service-Learning' (2001) 13(2) *Journal of Managerial Issues* 227. The broad influence on tax clinic students' self-efficacy has been reported in: Annette Morgan et al, 'Pro bono tax clinics: Aiding Australia's Tax Administration and Developing Students' Self-efficacy' (2022) 24(1) *Journal of Australian Taxation* 76.

59 Joyce K Fletcher, 'Self Esteem and Cooperative Education: A Theoretical Framework' (1990) 26(3) *Journal of Cooperative Education* 41; Wood and Bandura (n 57).

60 Wood and Bandura (n 57).

61 Tucker and McCarthy (n 58).

62 Bandura, *Self-Efficacy: The Exercise of Control* (n 54).

63 Barry J Zimmerman, Albert Bandura and Manuel Martinez-Pons, 'Self-motivation for academic attainment: The role of self-efficacy beliefs and personal goal setting' (1992) 29(3) *American Educational Research Journal* 663.

developing their self-efficacy and supporting them to become independent learners.[64] Further, feedback from supervisors on domain-specific knowledge as part of WIL can increase student self-efficacy.[65]

In a WIL study considering 21 measures of self-efficacy, students participating in a simulated WIL program have been found to improve in 20 of the 21 measures, with the largest improvement in the area of 'future employment'.[66] Keneley and Jackling found domestic and international students studying accounting in Australia to have different learning experiences;[67] with home country and culture also impacting on personal finance knowledge amongst university students.[68] It is possible that this may also influence the perceived self-efficacy of international students as they adjust to the Australian context. However, the ability of international students to assist clients from different cultural backgrounds, as provided by their WIL experience in a tax clinic, may be beneficial in improving the perceived self-efficacy of these students. Further, the importance of self-efficacy can be extended to students being able to successfully manage their career choice decisions,[69] especially since self-efficacy is known to influence future actions, including career choice.[70]

Career choice theories consider the interplay of self-efficacy with intrinsic motivation, career goals and social learning. For example, self-determination theory ('SDT') suggests that opportunities for learning, growth and challenge[71] such as those provided by WIL, may fulfill students' intrinsic motivation for autonomy and competence,[72] leading to improved perceived self-efficacy and corresponding motivation to pursue a career path. Further, higher self-efficacy is perceived when engaging in activities that impact people and are aligned with their value system,[73] and this may also apply to WIL activities. Social learning theory also suggests that the social environment of WIL may influence self-

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64 Marilyn Gist and Terence Mitchell, 'Self-Efficacy: A Theoretical Analysis of its Determinants and Malleability' (1992) 17(2) *Academy of Management Review* 183.

65 Richard K Coll, Mark Lay and Karsten E Zegwaard, 'The Influence of Cooperative Education on Student Self-Efficacy Towards Practical Science Skills' (2001) 36(2) *Journal of Cooperative Education* 58.

66 Freudenberg, Cameron and Brimble (n 13).

67 Monica Keneley and Beverley Jackling, 'The acquisition of generic skills of culturally-diverse student cohorts' (2011) 20(6) *Accounting Education* 605.

68 Michelle Cull and Diana Whitton, 'University Students' Financial Literacy Levels: Obstacles and Aids' (2011) 22(1) *Economic and Labour Relations Review* 99.

69 Spanjaard, Hall and Stegemann (n 21).

70 Bandura, 'Self-Efficacy Mechanism in Human Agency' (n 57).

71 Edward L Deci and Richard M Ryan, *Intrinsic Motivation and Self-determination in Human Behavior* (Plenum, 1985).

72 Ibid.

73 Chung-An Chen, Don-Yun Chen and Chengwei Xu, 'Applying Self Determination Theory to Understand Public Employee's Motivation for a Public Service Career: An East Asian Case (Taiwan)' (2018) 41(2) *Public Performance & Management Review* 365.

efficacy of students as they learn through the observation of clients, colleagues, and supervisors in a real-life professional environment.[74]

C *WIL AND INTERNATIONAL STUDENTS*

International students need additional help to be work ready upon graduation,[75] particularly in terms of developing key soft skills and becoming familiar with workplace culture in their host country, since many focus instead on acquiring technical skills and achieving high grades.[76] WIL can give international students valuable exposure to work-related activities relevant to their chosen profession.[77] Thus, WIL can provide an opportunity for international students to build their employability skills while also providing an area for universities to differentiate themselves in a highly competitive global labour market.[78] Further, the demands presented by globalisation and digital disruption now require accounting graduates to perform effectively across myriad work environments, countries, and cultures, with students who can demonstrate their ability to adapt to different work environments and cultures being in high demand.[79]

WIL is valued by international students and may assist in addressing the many challenges faced by international students in gaining employment.[80] Such challenges include limited local networks, lack of knowledge of the local labour market, and weak communication skills.[81] WIL is particularly important for international students who may lack confidence in key employability areas and who also struggle to find professionally relevant work experience opportunities in their host country.[82] In addition to the development of

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74 Dennis J Delprato and Bryan Midgley, 'Some fundamentals of B. F. Skinner's behaviorism' (1992) 47(11) *American Psychologist* 1507.

75 Carmela Briguglio and Robina Smith, 'Perceptions of Chinese students in an Australian university: are we meeting their needs?' (2012) 32(1) *Asia Pacific Journal of Education* 17; Cate Gribble, *International Employability Guide: Enhancing the Employability of International Graduates (A Guide for Australian Education Providers*) (International Education Association of Australia, 2015); 'Graduate Outlook 2015: The Report of the 2015 Graduate Outlook Survey: Perspectives on Graduate Recruitment', *Graduate Careers Australia* (Report, 2014) <https://www.graduatecareers.com.au/files/wp-content/uploads/2016/07/graduate-outlook-report-2015-final1.pdf>.

76 A Voninski and D Willox, *International Student Employability: A Guide for Australian Education Providers*. *Second Edition*. International Education Association of Australia (IEAA) (2020).

77 Carol-Joy Patrick et al, 'The WIL (Work Integrated Learning) report: A national scoping study [Final Report]', *Queensland University of Technology* (Report, 2008) <https://eprints.qut.edu.au/216185/>.

78 Blackmore et al (n 11).

79 Meredith Tharapos, Brendan T O'Connell, Steven Dellaportas and Ilias Basioudis, 'Are Accounting Academics Culturally Intelligent? An empirical investigation' (2019) 51(2) *British Accounting Review* 111.

80 Deloitte Access Economics Pty Ltd, *Growth and opportunity in Australian International Education* (2016).

81 Blackmore et al (n 11).

82 Patrick et al (n 77).

technical skills for international students, WIL can expose them to the cultural context of the work environment, as well as the ability to practice their language skills (if English is a second language). This insight to the work environment may address the deficiency of international students, as they can find it difficult to interact effectively in an Australian workplace.[83]

WIL, as part of an accounting degree experience at Australian universities, has been extensively researched;[84] however, many studies tend to treat students as a homogenous group, with little to distinguish between domestic and international student cohorts.[85] One study on Chinese students in Australia demonstrated how WIL assisted the development of Chinese students' English language, communication skills and cultural competence, as well as improving awareness of their professional identity.[86] WIL has also been found to improve international students' confidence in themselves as a professional practitioner.[87]

However, it appears there are low participations rates for international students in WIL experiences,[88] which is especially the case for postgraduate accounting students.[89] Of the literature that covers international students' WIL experiences, there has been much discussion of the barriers for international students participating in WIL. Two major issues centre around language barriers and limited understanding of local culture[90] which can make it difficult to place international students in a WIL activity.[91] Other factors include immigration status and the financial cost that can be involved, for example

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[83] Indra Abeysekera, 'Issues Relating to Designing a Work-Integrated Learning (WIL) Program in an Undergraduate Accounting Degree Program and Its Implications for the Curriculum' (2006) 7(1) *Asia-Pacific Journal of Cooperative Education* 7.

[84] Ibid; Tracey McDowall, Beverley Jackling and Riccardo Natoli, 'Relationships between Vocational Interests and Learning Approaches to Advance the Quality of Student Learning in Accounting' (2015) 24(6) *Accounting Education* 498; Bonnie Cord, Graham Bowrey, Graham Bowrey and Michael Clements, 'Accounting students' reflections on a regional internship program' (2010) 4(3) *Australasian Accounting Business and Finance Journal* 47.

[85] Gribble (n 11).

[86] Tien Cuong Nguyen, 'Work Integrated Learning: A Case Study of Chinese Students in an Australian University' (PhD Thesis, Victoria University, 2020).

[87] Ibid.

[88] Murray, Blackmore, Gribble and Hall (n 11).

[89] Gribble (n 11).

[90] Gribble (n 75); Thanh Pham, Dat Bao, Eisuke Saito and Raqib Chowdhury, 'Employability of international students: Strategies to enhance their experience on work integrated learning (WIL) programs' (2018) 9(1) *Journal of Teaching and Learning for Graduate Employability* 62.

[91] Cate Gribble, Mark Rahimi and Jill Blackmore, 'International Students and Post-study Employment: The Impact of University and Host Community Engagement on the Employment Outcomes of International Students in Australia' IL Tran and C Gomes (eds), International Student Connectedness and Identity. *Cultural Studies and Transdisciplinarity in Education*, vol 6. (Springer, 2017).

forgoing paid casual work to engage in the WIL.[92] However, poor communication has been identified as a central reason for international students not to engage with WIL.[93]

Similar issues apply to international students seeking work experience relevant to their field of study to improve career prospects,[94] or to secure graduate employment which is often sought by international students to remain in the host country after their studies have been completed.[95]

Often, the importance of work experience is not recognised, or offered early in the degree, which leaves international students with little time to prepare or engage in a WIL experience.[96] Further, some job placements (such as those in large banks and government departments) require students to have permanent residency or citizenship making it difficult for international students to obtain even part-time work in their host country.[97] Paid work experience, or placement opportunities for international students can also be limited due to student visa working conditions which restrict the number of hours that students are able to work,[98] while the cost of travel to industry workplaces can also make such experiences prohibitive.

Ensuring that a diverse range of students can access a form of WIL that suits their needs and prepares them for future work requires attention and must provide equitable outcomes for all students, particularly international students who are susceptible to exploitation in their urgency to gain relevant experience in Australia.[99] Despite the extant literature on WIL, until recent years there existed little empirical research that specifically examined the experiences of international students and WIL in accounting[100] or that compared the benefits of WIL between domestic and international students. A

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[92] Gribble (n 11).

[93] Patrick et al (n 77).

[94] Jean-Luc Cerdin and Marie Le Pargneux, 'Career and international assignment fit: Toward an integrative model of success' (2009) 48 *Human Resource Management* 5; Christopher Lawson, *Student voices: enhancing the experience of international students in Australia* (Australian Education International, 2012).

[95] Yehuda Baruch, Pawan S Budhwar and Naresh Khatri, 'Brain Drain: Inclination to stay abroad after studies' (2007) 42(1) *Journal of World Business* 99; Hessel Oosterbeek and Dinand Webbink, 'Does Studying Abroad Induce a Brain Drain?' (2011) 78 *Economica* 347; Thanh Pham and Denise Jackson, 'The need to develop graduate employability for a globalized world' in TLH Nghia, T Pham, M Tomlinson, K Medica and CD Thompson (eds), *Developing and Utilizing Employability Capitals: Graduates' Strategies across Labour Markets* (Routledge, 2020).

[96] Ross Smith, David Mackay, Dale Holt and Di Challis, 'Expanding the realm of best practices in cooperative industry-based learning in information systems and information technology: an inter-institutional investigation in Australian higher education information technology' (2008) 9(2) *Asia-Pacific Journal of Cooperative Education* 73.

[97] Lawson (n 94); Universities Australia (n 4).

[98] Cameron and Hewitt (n 2).

[99] Jackson (n 14); Jackson and Meek (n 12).

[100] Murray, Blackmore, Gribble and Hall (n 11); Patrick et al (n 77).

preliminary study has illustrated how an online WIL experience may not be as effective in developing international students' self-efficacy when compared to their domestic counterparts, especially in terms of their communication skills.[101] With the increasing pressure for international students to build their employability skills to be work-ready in a globalised environment,[102] there is a need for further research into the WIL experience of international students. This is especially the case in discipline areas such as accounting where placements are not a compulsory course requirement,[103] yet are an important curriculum priority to ensure students understand the realities of contemporary work in the profession.[104] Also, there are concerns about international students being able to successfully transition from their studies to industry,[105] and to acquire employability skills that are transferable across different countries and cultures.[106]

This study thus examines the extent to which WIL allows international students to develop their self-efficacy across key technical and soft skills areas required by accounting graduates and considers if there are differences in the development of self-efficacy between domestic and international students participating in the WIL experience across seven universities involved with the NTCP in Australia.

III RESEARCH METHODOLOGY

The underlying research questions for this study are:

> RQ1: Does WIL allow international students to develop their self-efficacy?
>
> RQ2: Are there differences in the development of self-efficacy between domestic and international students participating in WIL?

To address the research questions, this study employed a pre- and post-survey of students, to ascertain the influence, if any, of participating in the tax clinic experience, on their self-efficacy.

The survey was conducted at seven of the 10 universities involved in the NTCP during the first 18 months of operation, representing five different Australian states (New South Wales, Queensland, South Australia, Tasmania, Western Australia), with participating students nearing the end of their university studies and having completed the tax component of their degree.[107] Students are supervised by a tax professional, including tax

[101] Brett Freudenberg and Melissa Belle Isle, 'Confidence in a Pandemic: Students' Self-efficacy when Volunteering in an Online Tax Clinic' (2021) 27(4) *New Zealand Journal of Taxation Law and Policy* 279.

[102] Pham and Jackson (n 95).

[103] Stanley and Xu (n 41).

[104] Samantha Sin, Anna Reid and Alan Jones, 'An Exploration of Students' Conceptions of Accounting Work' (2012) 21(4) *Accounting Education* 323.

[105] Gribble (n 11); Cameron and Hewitt (n 2).

[106] Pham and Jackson (n 95).

[107] In 2021 the National Tax Clinic was expanded to 13 universities: 'National Tax Clinic program', *ATO* (Web Page, 13 April 2022) <https://www.ato.gov.au/general/gen/national-tax-clinic-program/>

agents and/or academic staff. Precise details of how each tax clinic is structured can be found in a special edition of the *Journal of Australian Taxation*.[108] While we acknowledge that there are some differences in the way that the tax clinics are structured, all tax clinics must meet the same requirements outlined by the government funding requirements.[109]

Both surveys were anonymous and completed voluntarily by students with their consent provided. Approval to conduct the study was received from the Human Research Ethics Committees for each of the participating universities.

The measurement of self-efficacy in prior work has focused on general self-efficacy, as well as task-specific dimensions. For this study, a 16-item measure of self-efficacy was adopted, comprising both general and task specific dimensions.[110] Table 2 provides the full set of self-efficacy dimensions used. While general dimensions have demonstrated valid associations with initiation and persistence in behaviour,[111] task-specific dimensions better predict performance of cognitive tasks.[112]

The 16 measures adopted in this study are derivate of other measures used in other studies but reduced in number from 21 to 16 to aid completion rates and be more precise.[113] The first three dimensions of the questionnaire were adapted from the Chen,

[108] Indra Abeysekera, 'National Tax Clinic Program Model Innovation' (2020) 22(2) *Journal of Australian Tax* 174; Castelyn, Bruce and Morgan (n 27); Brett Freudenberg, Colin Perryman, Kirstin Thomas and Melissa Belle Isle, 'Griffith Tax Clinic' (2020) 22(2) *Journal of Australian Taxation* 64; Sunita Jogarajan, Kate Fischer-Doherty and Julian Panetta, '2019 National Tax Clinic Project: Melbourne Law School Tax Clinic' (2020) 22(2) *Journal of Australian Taxation* 27; Ann Kayis-Kumar, Gordon Mackenzie and Michael Walpole, 'Interpersonal Collaborative Practice in Pro Bono Tax Clinics: A Case Study Approach' (2020) 22(2) *Journal of Australian Taxation* 49; Van Le and Tina Hoyer, '2019 National Tax Clinic Project: James Cook University Tax Clinic' (2020) 22(2) *Journal of Australian Taxation* 162; John McLaren, '2019 National Tax Clinic Project: University of Tasmania' (2020) 22(2) *Journal of Australian Taxation* 96; Ben Raines and Sonali Walpola, '2019 National Tax Clinic Project: The ANU Tax Clinic' (2020) 22(2) *Journal of Australian Taxation* 193; Connie Vitale and Michelle Cull, '2019 National Tax Clinic Project: Western Sydney University' (2020) 22(2) *Journal of Australian Taxation* 116 and Robert Whait, '2019 National Tax Clinic Project: UniSA Tax Clinic' (2020) 22(2) *Journal of Australian Taxation* 137.

[109] Robert (n 29).

[110] Rudolf J Bosscher, and Johannes H Smit, 'Confirmatory Factor Analysis of the General Self-Efficacy Scale' (1998) 36(3) *Behaviour Research & Therapy* 339; Gilad Chen and Stan Gully, 'Specific Self-Efficacy, General Self-Efficacy, and Self-Esteem: Are They Distinguishable Constructs?' (Proceedings, Annual Meeting of the Academy of Management, 1997); Andrea K Kirk and David F Brown, 'Latent Constructs of Proximal and Distal Motivation Predicting Performance Under Maximum Test Conditions' (2003) 88(1) *Journal of Applied Psychology* 40.

[111] Mark Sherer, James E Maddux, Blaise Mercandante and Steven Prentice-Dunn, 'The Self-Efficacy Scale: Construction and Validation' (1982) 51 (2) *Psychological Reports* 663.

[112] Alvin Y Wang and R Stephen Richarde, 'Global Versus Task-Specific Measures of Self-Efficacy' (1988) 38 *The Psychological Record* 533.

[113] Freudenberg, Cameron and Brimble (n 13).

Gully and Eden general self-efficacy scale,[114] which has been demonstrated to correlate more highly with motivational variables including goal orientation and performance.[115]

In terms of task-specific variables, thirteen dimensions were developed under the themes of 'Profession'; 'Communication', 'Team' and 'Problem Solving'. This was based on prior research that indicates these are attributes that industry is looking for in graduates.[116]

A *Participants*

Demographic details of student participants are summarised in Table 1. A total of 133 students completed surveys at the beginning of the semester and 94 at end of the semester. Since 214 students participated in one of the seven tax clinics during this time, the response rate for the pre-survey was 62%, and 44% for the post-survey. The lower response rate of the post-survey was partly due to Australia's Covid-19 restrictions coming into force when the post-survey was conducted. These restrictions forced some international students to leave Australia soon after completing their studies to return home. One of the initial observations that can be made is that the tax clinics appear to be a way to engage international students in a WIL experience given the proportion of them involved (approximately 40 to 50%).

There is similarity in the demographic characteristics of the beginning and end cohorts. For example, males account for approximately 37% of both beginning and end cohorts, and nearly two thirds of the students surveyed were aged between 20 – 30 years old. Half of the beginning survey participants were international students, which was slightly lower at 38% for the end survey. Less than half of the students have no prior professional work experience. The possible influence of various demographic features on the experience of students has been reported elsewhere.[117] Students participating in the program are in their final year and have previously completed a taxation law unit.

The purpose of this study is to assess whether the tax clinics involved in the NTCP are collectively improving the self-efficacy of international students in its current delivery. Each clinic delivers a WIL opportunity for students with consistency in terms of the tax work completed by students with taxpayers while under the supervision of tax professionals in a professional setting, meeting the same objectives outlined in the funding conditions of the NTCP. Course objectives across all universities in this study had the following common themes: analysing problems and the impact on stakeholders; applying appropriate research methods and accounting/taxation knowledge to solve

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[114] Gilad Chen, Stanley M Gully and Dov Eden, 'Validation of a New General Self-Efficacy Scale' (2001) 4(1) *Organizational Research Methods* 62.

[115] Ibid.

[116] Sharon Hayes, Brett Freudenberg and Deborah Delaney, 'Role of Tax Knowledge and Skills: What are the Graduate Skills Required by Small to Medium Accounting Firms' (2018) 13(1) *Journal of the Australasian Tax Teachers Association* 152.

[117] Michelle Cull, Csilla Skultety and Ryan Kumar, 'Factors Influencing the Motivation to Pursue a Career in Financial Planning' 2022) 8(1) *Financial Planning Research Journal* 40.

problems; using appropriate verbal and written communication methods to convey information; and working as part of a group of consultants to produce timely and professional work. Thus, it was expected that students' self-efficacy would improve across all 16 measures, given that the learning outcomes aligned with both general (e.g., managing time) and task-specific variables (classified under profession, communication, teamwork, and problem-solving).

Table 1: Demographics

Attribute		Beginning of tax clinic (n = 133)	Percent (Beginning) (n = 133)	End of tax clinic (n = 94)	Percent (End) (n = 94)
Gender	Male	49	36.84%	35	37.23%
	Female	84	63.16%	58	61.70%
	Not disclosed			1	1.06%
University	University 1	19	14.29%	13	13.83%
	University 2	34	25.56%	26	27.66%
	University 3	5	3.76%	7	7.45%
	University 4	16	12.03%	10	10.64%
	University 5	16	12.03%	15	15.96%
	University 6	30	22.56%	4	4.26%
	University 7	13	9.77%	19	20.21%
Age	<20 years	11	8.27%	6	6.38%
	20 – 30 years	84	63.16%	61	64.89%
	31 – 40 years	27	20.30%	21	22.34%
	>40 years	11	8.27%	6	6.38%
Nationality	Domestic	66	49.62%	58	61.70%
	International	67	50.38%	36	38.30%
Professional work experience	No	60	45.11%	38	40.43%
	Yes - less than 3 months	22	16.54%	17	18.09%
	Yes - 3 months but less than 6 months	12	9.02%	9	9.57%
	Yes - more than 6 months	39	29.32%	30	31.91%

Note: Some percentages may not add to 100 per cent due to rounding

Table 2: Self-Efficacy: International students vs domestic students

How "confident" are you in your ability to ...*	Domestic				International				All students			
	Mean Start (n = 66)	Mean End (n = 58)	Change in Mean	% Change	Mean Start (n = 67)	Mean End (n = 36)	Change in Mean	% Change	Mean Start (n = 133)	Mean End (n = 94)	Change in Mean	% Change
General												
... accomplish difficult tasks when faced with them.	3.62	3.76	0.14	4%	3.39	3.89	0.50	15%**	3.50	3.81	0.31	9%*
... perform quite well under pressure.	3.79	3.78	-0.01	0%	3.61	3.92	0.31	9%	3.70	3.83	0.13	4%
... to better manage time.	4.03	3.95	-0.08	-2%	3.84	4.11	0.27	7%	3.93	4.01	0.08	2%
Profession												
... begin a career in the Degree I am studying.	4.09	4.07	-0.02	0%	3.82	4.39	0.57	15%**	3.95	4.19	0.24	6%
... to achieve my career goals	3.80	3.86	0.06	2%	3.69	4.47##	0.78	21%***	3.74	4.10	0.36	10%**
... to understand what is expected of me as a professional advisor.	3.71	3.88	0.17	5%	3.61	4.22	0.61	17%**	3.66	4.01	0.35	10%**
Communication												
... to communicate with clients in an effective manner	3.50	4.05	0.55	16%**	3.45	3.92	0.47	14%	3.47	4.00	0.53	15%**
... structure and write an advice.	3.23	3.53	0.30	9%	3.42	3.81	0.39	11%	3.32	3.64	0.32	10%*
... to be clear when presenting my ideas.	3.52	3.78	0.26	7%	3.40	4.00	0.60	18%**	3.46	3.86	0.40	12%
... to communicate with colleagues in an effective manner	4.11	4.22	0.11	3%	3.81	4.36	0.55	14%**	3.95	4.28	0.33	8%**
Team												

… to coordinate tasks within my work group.	3.86	4.19	0.33	9%*	3.90	4.50	0.60	15%***	3.88	4.31	0.43	11%**
… to contribute ideas for a team result.	3.92	4.22	0.30	8%*	3.96	4.42	0.46	12%**	3.94	4.30	0.36	9%**
Problem solving												
… to research tax issues confidently.	3.72	3.97	0.25	7%	3.66	4.25	0.59	16%**	3.69	4.07	0.38	10%**
… use a range of software applications.	3.58	3.59	0.01	0%	3.61	3.83	0.22	6%	3.59	3.68	0.09	3%
… analyse topics to identify what information I need to produce a good result.	3.47	3.72	0.25	7%	3.70	4.14#	0.44	12%*	3.59	3.88	0.29	8%*
… critically evaluate the relevance, reliability, and authority of information I find so that I know what to use and what to discard.	3.59	3.62	0.03	1%	3.52	4.06#	0.54	15%**	3.56	3.79	0.23	6%
Overall average	**3.72**	**3.89**	**0.17**	**5%**	**3.65**	**4.14**	**0.49**	**13%**	**3.68**	**3.98**	**0.30**	**8%**

Likert scale, 0 = Not confident at all; 1 = A little confident; 2 = Slightly confident; 3 = Moderately confident; 4 = Quite confident; 5 = Very confident.

* $p < .05$. ** $p < .01$. *** $p < .001$.

# $p < .05$. ## $p < .01$. (international students *cf* domestic students)

IV FINDINGS AND RESULTS

A *Descriptive Overview of Improvement in Self-efficacy*

Table 2 provides the results of domestic, international, and total student responses to 16 self-efficacy dimensions, both at the beginning and the end of the WIL experience in the tax clinic. It also includes the percentage change in self-efficacy as indicated by how confident students were in their abilities for each dimension over the survey period. While the results indicate an 8% improvement in self-efficacy overall, international students demonstrated a much greater improvement in their total average self-efficacy figure (13%), than domestic students (5%).

While international students demonstrated a greater increase in confidence than domestic students across 15 of the 16 self-efficacy measures, international students also began with the lowest levels of confidence in their ability for almost all categories (except for teamwork and using a range of software and analysis of topics). The biggest difference in confidence between domestic and international students at the beginning of their time at the tax clinic was in relation to: '*accomplish difficult tasks when faced with them*' and '*communicate with colleagues in an effective manner*' where international students rated their confidence at least 20 points lower than domestic students. This lower self-efficacy of international students could explain in part their hesitation to engage in WIL generally;[118] although it appears that the tax clinics appeared to have facilitated their involvement regardless of this.

Interestingly, in addition to the largest growth in confidence when compared with domestic students, by the end of their time in the tax clinic, international students were also more confident than domestic students across all general self-efficacy measures, and all but one of the task-specific measures; being '*able to communicate with clients in an effective manner*'. While this measure did substantially increase for international students (14% increase) it may be that their communication with clients still needs to be improved, which may include issues with having English as a second language.[119] Interestingly, the measure of '*communicate with colleagues*' also increased (14%) for international students. This might indicate that internal office communication in the tax clinic environment greatly increased international students' self-efficacy in this regard, which is still an important skill to develop for accounting graduates.[120] The tax clinic environment provided opportunities for modelling and social persuasion. As one student said: 'Working alongside the other student advisers and supporting each other as well as working with a partner on the presentation and bouncing ideas off of each other really contributed to the improvement of my teamwork skills.'

Overall, this would tend to suggest that the WIL experience of the tax clinic provided international students a positive environment to improve their self-efficacy, in terms of both general and task specific measures, which is supported by the following student quote: 'This experience gives me a chance to enhance my confidence in the profession I would like to pursue in the future.'

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[118] Murray, Blackmore, Gribble and Hall (n 11).

[119] Gribble (n 75).

[120] Hayes, Freudenberg and Delaney (n 116).

The task-specific dimensions demonstrated generally a greater improvement than the general self-efficacy dimensions. For international students, the largest percentage improvement in confidence was '*achieve my career goals'* (21%), closely followed by '*to understand what is expected of me as a professional advisor*' (17%), '*to be clear when presenting my ideas*' (18%), '*to coordinate tasks within my work group*' (15%) and '*to research tax issues confidently'* (16%). Such large improvements in self-efficacy are pleasing to see, as they can provide greater perception of students' professional identity, as well as important skills required of a professional advisor. The results also demonstrate the strong influence that self-efficacy has on career choice and contributes to the literature on career choice theory, including SDT which suggests students are more likely to be motivated to achieve their career goals when they have built confidence around their ability to perform specific tasks.

When we consider domestic students, their greatest improvement was '*to communicate with clients in an effective manner*' (16%). This could demonstrate that maybe domestic students dominated or gained more from client meetings, which may be attributed to having English as a first language, which may be of assistance when advising on technical taxation matters: 'As a non-experienced, shy international student, I needed more practice and more opportunities for leading client meetings in order to overcome my nervousness and lack of confidence.' However, it did appear that international students thought their English skills improved: 'As a student that has English as secondary language this was extremely useful to improve my communication skills with clients.'

RQ1. WIL allows international students to develop their self-efficacy

The percentage improvement in the mean self-efficacy measures for international students participating in the tax clinic as presented in Table 2 suggests that WIL does allow international students to develop their self-efficacy. To determine whether these percentage improvements were statistically significant, an analysis of variance was conducted (ANOVA). ANOVA was considered appropriate, given that paired sample *t*-tests were not possible due to ethics restrictions around the way that data was collected. Further, in analysing the improvement in means for any one group (international students) an independent samples *t*-test would violate the assumption of independence as the same participants appear in both the beginning and the end time points. With more than 30 participants in each group, ANOVA is considered robust with little effect of any violation of the normality assumption, and as differences in group size do not exceed 1:1.5, ANOVA is robust against heterogenous variances.[121]

In addressing RQ1, the ANOVA found international students demonstrated statistically significant improvement across 11 of the 16 self-efficacy measures, at the 0.05, 0.01 and <.001 levels, as identified by the asterisks (*, **, ***) in Table 2. This included one general self-efficacy measure being '*accomplish difficult tasks when faced with them'*, $F(1, 101) = 7.28$, $p = .01$, $r^2 = .07$, and ten task-specific measures across profession (3), communication (2), team (2) and problem solving (3).

[121] Adelma Hills, *Foolproof Guide to Statistics using IBM SPSS* (Pearson, 2nd ed, 2011).

Statistically significant improvements were observed for international students across all three of the profession measures: '*begin a career in the Degree I am studying*', $F(1, 101) = 6.91$, $p = .01$, $r^2 = .06$; '*achieve my career goals*', $F(1, 101) = 15.31$, $p = .00$, $r^2 = .13$, and '*understand what is expected of me as a professional advisor*', $F(1, 101) = 9.16$, $p = .00$, $r^2 = .08$. This improved confidence in terms of professional identity provides international students with an improved basis for transitioning to their professional careers.

Two of the communication measures demonstrated significant improvements at the <.001 level: '*be clear when presenting my ideas*', $F(1, 101) = 7.02$, $p = .00$, $r^2 = .06$, and '*communicate with colleagues in an effective manner*', $F(1, 101) = 9.25$, $p = .00$, $r^2 = .08$. Statistically significant improvements in confidence for the team measures '*coordinate tasks within my work group*', $F(1, 101) = 10.90$, $p = .00$, $r^2 = .10$, and '*contribute ideas for a team result*', $F(1, 101) = 8.17$, $p = .01$, $r^2 = .07$, were also found for the international students as a result of the tax clinic experience. This supports social learning theory and suggests that the tax clinic context provided a positive team environment that allowed the international students to develop their self-efficacy through mastery, modelling and social persuasion.[122] International students expressed how they appreciated this:

> I had much chance to sit in front of clients, listening to my supervisor communicating with them and I also had [a] chance to ask questions…it was a precious experience for me to prepare and talk to client to get information independently.
>
> … I also learn how to portray professionalism and empathy in communicating to better understand clients' needs or issues during appointments. This is primarily due to the direct guidance and supervision working closely with tax practitioners, supervisors and distinguished Academics.

Also, the interaction with clients appeared to be important to international students and assisted students in developing techniques to improve their confidence: 'By meeting new people as a client and giving them an advice, I learnt a lot what to say appropriately and got more confident'.

Further, the international students significantly improved their confidence in problem solving across three measures: '*research tax issues confidently*', $F(1, 101) = 10.17$, $p = .00$, $r^2 = .09$; '*analyse topics to identify what information I need to produce a good result*', $F(1, 101) = 5.37$, $p = .02$, $r^2 = .05$, and '*critically evaluate the relevance, reliability and authority of information I find so that I know what to use and what to discard*' $F(1, 101) = 9.26$, $p = .00$, $r^2 = .08$. This development is demonstrated in the following student quote:

> As I did not have a deep knowledge of the tax law, I had to research about the topic in the Australian Master Tax Guide and other resources and then discuss with the client about his/her case. Through this process, I was able to improve my understanding of tax law at a deeper level and thus, developed my research skills.

The interaction with clients appeared to be an important part of this development: 'Each client had a different situation, which required students to apply suitable tax knowledge

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[122] Bandura, 'Self-Efficacy Mechanism in Human Agency' (n 57).

to solve the issues. This helped better understanding of the realistic aspect of tax law in the real life.'

While the ANOVA results show statistically significant improvements in confidence for international students across more than half of the self-efficacy measures, the measure that had the largest effect on confidence for international students was '*achieve my career goals'*. This supports the 21% improvement observed in Table 2. This would tend to suggest that international students having completed their WIL experience at the tax clinics would have greater confidence as they move to the next stage of their careers, which in parts relates to the context of having an experience of an Australian work environment: 'Constantly explaining areas of tax law to clients helped me improve my ability to communicate as I was not confident of communicating in a workplace where people predominantly spoke with an Australian accent.'

Therefore, in response to RQ1, these results demonstrate that the WIL tax clinic experience provided international students with an opportunity to substantially, and significantly, develop their self-efficacy across a wide range of measures.

RQ2. Differences in the development of self-efficacy between domestic and international students participating in WIL

The ANOVA performed in response to RQ1 (discussed above) to determine where international students showed significant improvements in self-efficacy due to WIL, was replicated for domestic students to allow for a comparison to be made between domestic and international students. Unlike international students, domestic students did not show any significant improvement in the general self-efficacy measures. However, domestic students did show statistically significant improvements in three of the task-specific self-efficacy measures. These were '*communicate with clients in an effective manner*', $F(1, 122) = 8.86$, $p = .00$, $r^2 = .07$; '*coordinate tasks within my work group'*, $F(1, 122) = 4.32$, $p = .04$, $r^2 = .03$, and '*contribute ideas for a team result*', $F(1, 122) = 4.2$, $p = .04$, $r^2 = .03$. These ANOVA results support the descriptive statistics in Table 2, with the most significant improvement for domestic students being in communicating with clients in an effective manner (16% improvement).

The results indicate that international students significantly improved their self-efficacy across more of the 16 measures (11) than domestic students did (3), with the increase for domestic students generally more modest. However, given that the mean confidence values of the self-efficacy measures at the beginning of the WIL experience were lower for international students than domestic students, an independent *t*-test was conducted on each of the self-efficacy measures for both the beginning and ending survey results to test for any significant differences between domestic and international student groups.

For the beginning survey, the *t*-test demonstrated no significant differences between domestic and international students for self-efficacy across all five categories (general, professional, communication, team and problem solving). However, supporting the higher growth results in Table 2 and indicated by the ANOVA results, the *t*-test on the end survey results (see Table 3) revealed statistically significant differences between domestic and international students for three areas of self-efficacy: '*achieve my career goals'* $t(92) = 3.167$, $p = .002$; '*analyse topics to identify what information is needed to produce a good result*' $t(92) = 2.124$, $p = .036$; and '*critically evaluate the relevance, reliability and authority of information*' $t(92) = 2.077$, $p = .041$. These items are marked

accordingly in Table 2 (#, ##) and summary results are presented in Table 3. Such findings support that the WIL experience at the tax clinic had a larger positive impact on the self-efficacy of international students than on domestic students, with the most significant difference shown in confidence in ability to '*achieve my career goals*'; the difference in means of 0.61, 95% CI[0.993, 0.227] representing a medium to large effect (r^2 = 0.098).[123] Given the concerns about international students' ability to be able to transition to careers in their host country this is a positive finding.[124]

Table 3: Results for Self-Efficacy of Domestic and International Students: End survey

I have confidence in my ability to:	Domestic students		International students		*t*(92)	*p*	r^2
	M	*SD*	*M*	*SD*			
... achieve my career goals	3.86	.981	4.47	.774	3.167	.002	0.098
... analyse topics to identify what information I need to produce a good result.	3.72	.970	4.14	.833	2.124	.036	0.047
... critically evaluate the relevance, reliability and authority of information I find so that I know what to use and what to discard.	3.62	1.105	4.06	.754	2.077	.041	0.045

Consequently, in terms of RQ2 there are demonstrable differences in the development of self-efficacy between domestic and international students participating in WIL, with the most significant differences suggesting that WIL resulted in larger improvements in self-efficacy across a wider range of measures for international students when compared with domestic students.

Overall, the participation of students at the tax clinics generally appeared to have a positive influence on their self-efficacy. Specifically, international students appear to have gained a greater increase in self-efficacy over several measures compared to their domestic counterparts. Thus, the tax clinics present rich learning environments for students and provide access to a meaningful WIL experience while also providing a positive contribution to the community.

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[123] Jacob Cohen, *Statistical Power Analysis for the Behavioral Sciences*. Revised edition. (Academic Press, 1977).

[124] Pham and Jackson (n 95).

B *Limitations and Future Research*

There are a number of limitations to this study that need to be acknowledged, including the potential for self-selection as highly motivated students may have been attracted to the opportunities provided by the tax clinic experience. Nevertheless, it should be recalled how the level of self-efficacy of international students were generally lower than domestic students at the beginning of their experience. Also, the self-efficacy measures are self-reported and as such may not be a totally accurate representation of the level of skills of the students. In self-reported survey research, common method bias can be a concern. To address the threat of common method bias in the current research, we employed Harman's single factor test which found the total variance extracted by a single factor to be 47.74%, falling just below the recommended threshold of 50%. While common method bias did not appear to be a significant factor in this research, it cannot be ruled out as a contributing factor. Furthermore, it was not possible to directly match students to pre and post surveys and the individual experience at the seven tax clinics may lead to different results.

Future research could consider whether the different modes used to conduct the tax clinics influences students' learning experience. Also, future research could try to measure more objectively the generic skills development of students when participating at the clinics. Given that Covid-19 restrictions meant some clinics had to operate in an online environment, future research might consider whether an online clinic affected the ability of international students to improve their communication skills and confidence for career progression.

A study could also consider the success of international students in securing professional work, and to what extent they perceived that their experience at the tax clinic contributed to this. A similar survey could be conducted in 3 - 5 years' time to measure the impact the tax clinics have on the self-efficacy of students, whether these are in their home country, host country or elsewhere. Moreover, it may be possible for tax clinics in other jurisdictions to conduct similar research to consider whether findings support that of the Australian experience.

V CONCLUSION

The creation of tax clinics at 10 Australian universities is a recent development in the establishment of a WIL experience for accounting students. The above analysis demonstrates that the student experience at the tax clinics has had a positive impact on self-efficacy, particularly for international students.

Overall, through measuring the self-efficacy of students across a range of key skills areas, the results provide evidence of the positive impact that a consulting form of WIL has on the employability skills of students and more specifically, international students, indicating that international students may have a lot to gain from this form of a WIL experience. Further, the study supports calls for more to be done to improve confidence

levels of international students around employability,[125] and for research that evaluates ways to embed WIL into accounting education and the corresponding impact on the employability of students from different backgrounds.[126] It also addresses the recommendation of Cameron and Hewitt that WIL offerings be designed to maximise access to international students.[127]

As borders begin to re-open in the aftermath of Covid-19, it is important for universities to ensure that their international students have not only the technical knowledge but also the work ready experiences to assist them transition to their chosen profession. This is especially the case for professions with a skill shortage, such as accounting. An important part of this transition is students' self-efficacy. This article has reported how international students in the NTCP had significantly greater growth compared to domestic students in several self-efficacy dimensions, including achieving career goals and communication skills. Such evidence can help support calls for professional bodies to encourage universities to support the development of WIL in the curriculum.[128] Moreover, this research contributes to self-determination theory by demonstrating how WIL can improve self-efficacy and subsequently provide strong motivation for students to pursue their career goals. Further, it contributes to social learning theory by illuminating the influential role of the social learning environment provided by WIL in improving self-efficacy, particularly for international students. These results reinforce the importance of WIL in improving the educational outcomes for students, including international students. Consideration should be given as to how more students, including international students, can be provided the opportunity to gain greater confidence and skill through WIL while studying. This study supports the need for authentic WIL consulting experiences such as those offered by the tax clinics to assist international students build their self-efficacy and improve their employability skills. Such experiences provide a stronger foundation for all students to transition from university study to professional work.

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125 Barton, Hartwig and Le (n 46).

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TAX CLINICS IN AUSTRALIA – THE ROAD TO LEGITIMACY

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ABSTRACT

Tax Clinics are a recent phenomenon in Australia although their heritage dates to the early 1960s in the United States of America. Notwithstanding the international reverence with which tax clinics have been associated, there has and remains a need for these initiatives to be legitimised domestically. To that end this article evaluates the process undertaken by participants in the National Tax Clinic Program ('NTCP') to achieve legitimacy in Australia during the first year of their operation in 2019 while the NTCP was being trialed. More specifically, the article responds to the research question: what legitimation strategies were employed by Australian tax clinics during the trial phase? The article engages inductive analysis to respond to the research question and analyses disclosures made by each NTCP participant in manuscripts published in a special issue of the *Journal of Australian Taxation*. The article clearly demonstrates how tax clinics have adopted pragmatic, moral and cognitive strategies to attain legitimacy and provides a series supporting practical examples. These examples show that clinics relied predominantly on pragmatic legitimacy strategies with moral and cognitive legitimacy strategies being employed to a lesser extent.

I INTRODUCTION

In 2018, Curtin University established Australia's first tax clinic.[1] This initiative was conceived with the dual purpose of (i) responding to the evolving demands placed on Australian tax and legal education, in recognition of the emerging needs of industry, and (ii) facilitating access to free and reliable tax advice for unrepresented taxpayers seeking to meet or comply with their tax-related affairs.[2] In response to the success of the Curtin initiative, the National Tax Clinic Program ('NTCP') trial was subsequently established in 2019 and enabled 10 (including Curtin University) academic institutions, State and Territory wide, to conduct a 12-month funded trial of the program.[3] The national trial was

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[1] Donovan Castelyn, Stephanie Bruce and Annette Morgan, '2019 National Tax Clinic Project: Curtin University – Curtin Tax Clinic' (2020) 22(2) *Journal of Australian Taxation* 1.

[2] Ibid 3.

[3] See, former Prime Minister, Scott Morrison, 'Keynote Address' (Speech, Australian Chamber of Commerce and Industry Annual Dinner, 28 November 2018). Relevantly, the Prime Minister announced the establishment of 'ten new tax clinics … to provide free assistance to small businesses and individuals with disputes with the ATO. These tax clinics will ensure small businesses in need have

ultimately deemed a success and the original 10 participants were granted a further two year's funding.[4] More recently, in mid-2021, the Australian Government sought to expand the initiative more broadly. While still confined to academic institutions, grants are now awarded on an open and competitive basis.[5] Tax clinics are now a recognised fixture of Australia's tax landscape. However, for this position to first, be attained and second, to continue, clinics needed to achieve legitimacy among several key stakeholders. These include(ed) but are not limited to; the taxpayers, professional bodies, university students and the internal university community and the government and its department such as the Australian Taxation Office ('ATO') and Federal Treasury.

Accordingly, it is the purpose of this article to evaluate the processes undertaken by the NTCP trial participants to achieve legitimacy in Australia. More specifically, the article will seek to respond to the research question, namely: What legitimation strategies were employed by Australian tax clinics during the trial phase? The article will engage with inductive analysis to respond to this question by analysing disclosures made by each NTCP trial participant in manuscripts published in a special issue of the *Journal of Australian Taxation*.[6]

The article will initially provide further background into the motivations for the NTCP and its comparative international initiatives. The article will then discuss the aspects of legitimacy theory pertinent to the paper and identify the initial and subsequent challenges participants in the NTCP needed to overcome. A discussion concerning the research methodology and critical observations will then follow prior to the article offering a series of concluding remarks.

II BACKGROUND AND LITERATURE

A *A Brief History of Tax Clinics*

Tax clinics globally are a recent phenomenon, though their origins date back to the late 1960s in the United States of America ('US').[7] Fogg recollects that the first test tax clinic was established at Harvard Law School in 1968 and supported by funding from the Internal Revenue Service ('IRS').[8] This initial program enabled law students from the Harvard Law School to assist taxpayers undergoing an office audit in the Boston District whereby students were permitted to accompany taxpayers as a 'witness,' but not as the

access to specialist advice from tax practitioners and students in the field on a pro bono basis.' See also, *Journal of Australian Taxation* (2020) 22(2) Special Edition on Tax Clinics for a comprehensive overview of clinics involved in the trial phase.

4 See Treasury, *Mid-Year Economic and Fiscal Outlook* (Report, December 2019) 283 <https://archive.budget.gov.au/2019-20/myefo/download/MYEFO_2019-20.pdf>.

5 'Archived Grant Opportunity View - GO4847', *Australian Government* (Web Page) <https://www.grants.gov.au/Go/Show?GoUuid=04bd4ff8-8251-4713-aafe-92ac41f55134>.

6 *Journal of Australian Taxation* (2020) 22(2) Special Edition on Tax Clinics.

7 Keith Fogg, 'Taxation with Representation: The Creation and Development of Low-Income Taxpayer Clinics' (2013) 67 *Tax Law* 5.

8 Ibid.

taxpayer's legal representative.[9] Throughout the 1970s and 1980s more universities opened tax clinics stipulating that the service was targeted at low-income taxpayers and supported by funds from the Department of Education.[10] In addition to the pedagogical motivations, a central theme of each clinic during this time, which admittedly persists to the present, is the provision of timely, accurate and reliable tax advice and/or representation to eligible low-income taxpayers.[11] Aptly, the tax clinical program in America is referred to as the Low-Income Tax Clinic ('LITC') program. By the late 1990s, tax clinics in the US were well established and benefited from matched national funding and a countrywide presence.[12]

LITCs have continued to operate in both the academic and non-academic domains with a particular focus on assisting low-income individuals who have a tax dispute with the IRS and providing education and outreach to individuals who speak English as a second language ('ESL').[13] Relevantly, the established aims of the program now include:

- providing pro bono representation on behalf of low-income taxpayers in tax disputes with the IRS, including audits, appeals, collection matters, and federal tax litigation;
- responding to IRS notices and correction of account problems;
- educating low income and ESL taxpayers about taxpayer rights and responsibilities; and,
- identifying and advocating for issues that impact low-income taxpayers.[14]

Australia is understood to be the first nation following the US to introduce a similar program. Moreover, as noted, Curtin University, under the leadership of Annette Morgan and Donovan Castelyn, is credited as the first tax clinic in Australia and subsequently the impetus for the NTCP trial. The NTCP parallels the LITCs in the US sharing similar philanthropic and pedagogical ideologies.[15] Notably, each participant in the Australian

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[9] Despite the well-intentioned motivations for this program, it was discontinued a mere 18 months later based on a perceived lack of benefit to the school and the service. See ibid 5.

[10] Ibid 3. Each clinic based their models on the previously established clinics focused on low-income taxpayers and providing practical skills to their enrolled university students.

[11] Internal Revenue Service, Office of the Assistant Commissioner, *Report on Legal Assistance Test Program* (Final Report, November 1978).

[12] Fogg (n 7) 23. See also, Restructuring and Reform Act of 1998 (RRA 98) which authorised $6.0 million in matching grants to the LITCs.

[13] The impact of the LITC program continues to expand. In the 2021 grant year, LITCs represented 19,413 taxpayers, educated 133,757 taxpayers and service providers, helped secure $5.8 million in refunds and decrease or correct $50 million in tax liabilities. Moreover, the LITC Program awarded over $12 million in grants to 130 organizations in 47 states and the District of Columbia with similar funding and assistance levels expected in 2022 and beyond. See, 'Low-Income Taxpayer Clinics 2022 Program Report', *Inland Revenue Service* (Report, January 2022) <https://www.irs.gov/pub/irs-pdf/p5066.pdf>.

[14] Ibid.

[15] Castelyn (n 1) 2.

program is required to deliver on the following for taxpayers who cannot afford representation:

- provide pro-bono advice, guidance and assistance on tax matters;
- represent clients on a pro bono basis in dealings with the ATO;
- create education activities in each Tax Clinic to improve understanding of the tax system;
- provide advocacy facilities to enable wider involvement in highlighting and reducing issues and problems in the tax system; and
- staff Tax Clinics with students undertaking relevant studies including accounting, law or dispute resolution.[16]

B *The Pathway to Legitimacy*

The discussion above demonstrates how tax clinics were established in Australian universities to fill a gap in the market by providing free services to those who cannot afford a tax agent. Students, under supervision, providing free tax services from within universities presents a new practice in Australia that must attain and maintain legitimacy for long term survival. Since their inception, the clinics have attracted attention from the tax profession who are concerned that clinics will be competing with their member firms by poaching clients. Therefore, it is important for clinics to demonstrate that they are achieving the objectives of the NTCP to attain and maintain legitimacy with the profession, as well as with several other stakeholders. Power discusses a range of stakeholders from which legitimacy for a new practice is sought such as clients, the non-client external world, and the internal world.[17] Following this, tax clinic client group stakeholders will comprise specific taxpayers seeking advice and services, members of the public receiving education, financial counsellors, and other referral sources. Non-client external groups stakeholders will comprise the Australian Taxation Office, Treasury, and the Tax Practitioners' Board, and the general community. Lastly, internal world stakeholders will comprise university students, other academics and the broader university community.

Suchman regards legitimacy as the 'generalized perception or assumption that the actions of an entity are desirable, proper or appropriate within a socially constructed system of norms, values, beliefs and definitions'.[18] Legitimacy is therefore a multifaceted concept.[19]

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[16] ATO (n 5) 8.

[17] Michael Power, 'Auditing and the Production of Legitimacy' (2003) 28(4) *Accounting, Organizations and Society* 379 cited in Brendan O'Dwyer, David Owen and Jeffrey Unerman, 'Seeking Legitimacy for New Assurance Forms: The Case of Assurance on Sustainability Reporting' (2011) 36(1) *Accounting, Organizations and Society* 31.

[18] Mark Suchman 'Managing legitimacy: strategic and institutional approaches' (1995) 20(3) *Academy of Management Review* 571, 572.

[19] See eg, Alex Bitektine, 'Toward a Theory of Social Judgements: The Case of Legitimacy, Reputation, and Status' (2011) 36(1) *Academy of Management Review* 151; Alex Bitektine and Patrick Haack, 'The 'Macro' and the 'Micro' of Legitimacy: Toward a Multilevel Theory of the Legitimacy Process' (2015) 40(1) *Academy of Management Review* 49; Noel Brown and Craig Deegan, 'The Public Disclosure of Environmental Performance Information – A Dual Test of Media Agenda Setting Theory and Legitimacy Theory' (1998) 29(1) *Accounting and Business Research* 21; Mohamed Chelli, Jacques Richard and

It is beyond the scope of this article to conduct an extensive evaluation of the literature concerned with legitimacy theory. It is however prudent for this article to explore, as a foundation for further analysis, the literature broadly concerning legitimacy with a particular emphasis on strategic and institutional approaches to developing relationships with stakeholders.[20]

The framework established by Suchman and subsequently endorsed and expanded upon by Tilling and Tilt,[21] O'Dwyer[22] and Deephouse et al,[23] will inform much of the subsequent discussion in this article.[24] To that end, the strategic approach emphasizes legitimacy as an operational resource instrumentally managed by organisations.[25] Whereas, institutional legitimacy emphasises the power of external, cultural and contextual factors in constructing organisations and the standards by which they are judged.[26] Each strand is further divided into pragmatic, moral and cognitive terms.

1 *Pragmatic Legitimacy*

Pragmatic legitimacy concerns self-interested and instrumental evaluations of new practices by external stakeholders.[27] There are three sub-types of pragmatic legitimacy. One is exchange legitimacy where the expected value of an organisation's activities is what ultimately determines its legitimacy.[28] Expressed in the alternative, stakeholders will legitimise a new practice by assessing the instrumental value that it provides and whether it meets their needs. Another is influence legitimacy which occurs when external stakeholders believe that they can shape the organisation providing the practice or the

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Sylvain Durocher, 'France's New Economic Regulations: Insights from Institutional Legitimacy Theory' (2014) 27(2) *Accounting, Auditing and Accountability Journal* 283; Craig Deegan, 'An Overview of Legitimacy Theory as Applied within the Social and Environmental Accounting Literature', in Jeffrey Unerman, Jan Bebbington and Brendan O'Dwyer (eds), *Sustainability Accounting and Accountability* (Routledge, 2008) 248; David Deephouse and Mark Suchman, 'Legitimacy in Organizational Institutionalism', in Royston Greenwood, Christine Oliver, Roy Suddaby and Kerstin Sahlin-Andersson (eds), *The SAGE Handbook of Organizational Institutionalism London* (Sage, 2008) 49.

[20] Suchman (n 18). For a comprehensive discussion surrounding the broader aspects of organisational legitimacy, see, Sanjaya Kuruppu, Markus Milne and Carol Tilt, 'Gaining, Maintaining and Repairing Organizational Legitimacy - When to Report and When not to Report' (2019) 32(7) *Accounting, Auditing & Accountability Journal* 2062.

[21] Matthew Tilling and Carol Tilt, 'The Edge of Legitimacy: Voluntary Social and Environmental Reporting in Rothmans' 1956 – 1999 Annual Reports' (2010) 23(1) *Accounting, Auditing and Accountability Journal* 55.

[22] O'Dwyer et al (n 17).

[23] David Deephouse, Jonathan Bundy, Leigh Plunkett Tost and Mark Suchman, 'Organizational Legitimacy: Six Key Questions' in Royston Greenwood, Christine Oliver, Thomas B Lawrence and Renate E Meyer (eds), *The SAGE Handbook of Organizational Institutionalism London* (Sage, 2017) 27.

[24] Suchman (n 18).

[25] Kuruppu, Milne and Tilt (n 20) 2065.

[26] Ibid.

[27] Suchman (n 18) 571.

[28] Kuruppu, Milne and Tilt (n 20) 2065.

practice itself.[29] Influence legitimacy may also be achieved where the new practice appeals to a stakeholder's broader set of interests beyond their own.[30] The final type of pragmatic legitimacy is dispositional legitimacy which is concerned with the character of organisations providing the practice and the belief that they are acting in stakeholders' best interests.[31] With respect to tax clinics, stakeholders may be looking for various needs to be satisfied or outcomes to be achieved with legitimacy being difficult to attain or maintain if these needs are not met or the outcomes are not achieved.

2 *Moral Legitimacy*

Moral legitimacy is concerned with approval based on whether the new practice is perceived as right or wrong according to whether it achieves certain social outcomes and increases social welfare.[32] As with pragmatic legitimacy, various sub types of moral legitimacy exist.[33] Consequential and procedural kinds of moral legitimacy are achieved by stakeholders' assessing what the new practice achieves and whether those achievements align with socially acceptable techniques and procedures.[34] These are objectively assessed from the external stakeholder's point of view. Personal legitimacy can be achieved through evaluation of the individuals involved in the new practice.[35] This determination concerns the individual's status, reputation or charisma. Similarly, structural legitimacy can be achieved by assessing the administrative and physical practices and whether those can be regarded as appropriate for that new practice.[36] With respect to tax clinics, helping vulnerable taxpayers who cannot afford tax services and who need it may be regarded as the right thing to do, but legitimacy may dissipate if this goal is not achieved. Selecting appropriate clients to serve and students to serve them using an appropriate clinic model and an appropriately experienced and qualified supervisor would also be relevant aspects to consider. A charismatic or well-regarded supervisor would also assist with attaining and maintaining moral legitimacy.

3 *Cognitive Legitimacy*

Pragmatic and moral legitimacy are congruent to the extent that they both concern discursive evaluations from external stakeholders which can be in the form of engagement through action or dialogue, whereas cognitive legitimacy moves beyond discursive evaluations and is established by the new practice objectively being the most appropriate way to achieve a desired outcome or meet a particular need.[37] This can be

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[29] Ibid.

[30] Suchman (n 18) 578 - 579.

[31] Kuruppu, Milne and Tilt (n 20) 2065.

[32] Suchman (n 18) 585.

[33] Ibid; O'Dwyer et al (n 17) and Deephouse et al (n 23) 33.

[34] Ibid.

[35] Ibid.

[36] Ibid.

[37] Suchman (n 18) 571.

demonstrated by providing plausible arguments for the new practice's existence, referred to as comprehensible legitimacy,[38] or through the need for the new practice essentially being self-evident or as commonly espoused, 'taken for grantedness'.[39] The self-evident appropriateness or taken for grantedness of tax clinics to meet the needs to taxpayers who cannot comply with their tax affairs on their own and do not have the means to pay for appropriate help might be regarded as the ultimate form of legitimacy, but if this cannot be attained, continually arguing for their existence in a comprehensible and persuasive manner would be appropriate to attain and maintain this type of legitimacy.

4 *Strategies and Practices to Attain and Maintain Legitimacy*

A new practice may seek to achieve or rely on many types of legitimacy. It is also recognised that the implementation of strategies and practices can achieve more than one type of legitimacy.[40] Ruef and Scott however acknowledge several conflicts when seeking to achieve multiple legitimacies.[41] For example, moral legitimacy's concern with outcomes is clearly related to the pragmatic legitimacy's focus in instrumental exchange such that a practice that is judged poorly with respect to its outcomes are also likely to be assessed poorly with respect to the value of any exchanges with stakeholders.[42] In contrast, a new practice that is assessed positively with respect to doing the right thing and achieving social welfare may be assessed poorly with respect to pragmatic legitimacy due to some stakeholders observing poor or even reduced value from it.[43]

Some types of legitimacy are easier to attain but are harder to maintain while others are harder to attain but are more durable once they have been attained.[44] For example, pragmatic legitimacy is regarded as the easiest to attain but the least durable due to its emphasis on short term material incentives and its greater exposure to changes in perceptions of external audiences.[45] In contrast, cognitive legitimacy is the hardest to

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[38] O'Dwyer et al (n 17) and Deephouse et al (n 23) 33.

[39] Ibid.

[40] Derick Brinkerhoff, 'Organisational Legitimacy, Capacity and Capacity Development' (Discussion Paper No 58A) (June 2005) 1.

[41] Martin Ruef and Richard Scott, 'A Multidimensional Model of Organizational Legitimacy: Hospital Survival in Changing Institutional Environments' (1998) 43(4) *Administrative Science Quarterly* 877.

[42] See further, Adriana Burlea-Schiopoiu and Ion Popa, 'Legitimacy Theory' in Samuel O Idowu, Nicholas Capaldi, Liangrong Zu and Ananda das Gupta (eds), *Encyclopedia of Corporate Social Responsibility* (Springer, 2013) 1579. See also, Pablo Archel, Javier Husillos, Carlos Larrinaga and Crawford Bradford Spence, 'Social Disclosure, Legitimacy Theory and the Role of the State' (2009) 22(8) *Accounting, Auditing & Accountability Journal* 1284.

[43] Brinkerhoff (n 40) 5.

[44] Ruef and Scott (n 41) 880.

[45] O'Dwyer et al (n 17) 35 and Deephouse et al (n 23) 33. See also, Matthew Tilling, 'Some Thoughts on Legitimacy Theory in Social and Environmental Accounting' (2004) 24(2) *Social and Environmental Accountability Journal* 1.

attain but has longer-term orientation and is easier to maintain.[46] Moreover, failure to obtain and maintain moral legitimacy can undermine the preservation of any pragmatic or cognitive legitimacy.[47] Cognitive legitimacy evolves slowly as it is often the product of constituents' cumulative experiences.[48] With respect to tax clinics, legitimacy would have had to have been achieved quickly – especially since the trial period was initially for one year and a competitive grant process was to follow a couple of years after. Therefore, a heavy reliance on pragmatic and moral legitimacy instead of cognitive legitimacy is expected during the NTCP trial period. If that is the case, gaining cognitive legitimacy in the long term would be beneficial and recommended.

Three broad strategies have emerged from the literature which may assist in achieving one or more types of the legitimacies discussed above. These include, *conform*, *selection* or *manipulation strategies*.[49] *Conform strategies* are adopted by a new practice to comply with and acquiesce to institutional pressures.[50] Ordinarily, legitimacy would be achieved through reference to how a new practice has relied on or incorporated established and respected models, practices and standards.[51] *Selection strategies* reduce the extent to which conformity is necessary, either by selecting partial or symbolic compliance or selecting an industry that has matching institutional pressures.[52] Karlsson and Middleton note that: '[s]election strategies often involve adhering to institutional pressures but exerting influence regarding which to adapt to – for example, selecting the customer segment to target or in which industry to act, or choosing to please the owners at the expense of conforming to tax laws'.[53] *Selection strategies* can also involve suppressing non-conformity, either by using symbolic conformity or simply by not informing others about the real aim and actions of the organisation. *Manipulation strategies* involve active engagement in trying to change an institution or alter the surrounding environment.[54] These strategies seek to persuade stakeholders about the value of the practice, the merit

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[46] See further, Markus Milne and Dennis Pattern, 'Securing Organizational Legitimacy - An Experimental Decision Case Examining the Impact of Environmental Disclosures' (2002) 15(3) *Accounting, Auditing & Accountability Journal* 372.

[47] Dare John Olateju, Olakunle Abraham Olateju, Seyi Vincent Adeoye and Idris Suleiman Ilyas, 'A Critical Review of the Application of the Legitimacy Theory to Corporate Social Responsibility' (2021) 9(3) *International Journal of Managerial Studies and Research* 1.

[48] Rajesh Kumar and TK Das, 'Interpreter Legitimacy in the Alliance Development Process' (2007) 44(8) *Journal of Management Studies* 1425.

[49] Tomas Karlsson and Karen Williams Middleton, 'Strategies for Creating New Venture Legitimacy' (2015) 29(6) *Industry and Higher Education Journal* 469.

[50] Ibid 471.

[51] Ibid. See also, Howard Aldrich and Marlene Fiol, 'Fools Rush In? The Institutional Context of Industry Creation' (1994) 19(4) *Academy of Management Review* 645; Arthur Stinchcombe, 'Social Structure and Social Organization' in James March (ed), *Handbook of Organizations* (Rand McNally, 1965) 142.

[52] Karlsson and Middleton (n 49) 472.

[53] Ibid.

[54] Ibid.

of the morals that it will achieve and by constructing a narrative about the practice that enhances understanding about it.[55]

Against this background the article will now discuss how tax clinics have achieved legitimacy and through what means. First by reviewing the research undertaken and then by exploring and commenting on the results.

III Method

This section discusses the research methodology and analysis undertaken by the authors with respect to the data collection and its analysis.

A *Data Collection*

As noted, this study chiefly considers the manuscripts published in the 2020 special edition of the *Journal of Australian Taxation.*[56] Accordingly, data collection was reasonably linear and consisted of one article from each of the ten clinics participating in the NTCP trial as follows (alphabetical order) (collectively, 'the Articles'):

- Australian National University ('ANU')[57]
- Curtin University ('Curtin')[58]
- Charles Darwin University ('CDU')[59]
- Griffith University ('Griffith')[60]
- James Cook University ('JCU')[61]
- Melbourne University ('MLB')[62]
- University of New South Wales ('UNSW')[63]
- University of South Australia ('UniSA')[64]

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55 O'Dwyer et al (n 17) 36 and Deephouse et al (n 23) 33.

56 2020 *Journal of Australian Taxation* Volume 22, Issue 2. See <https://www.jausttax.com.au/volume-22-issue-2>.

57 Ben Raines and Sonali Walpola, '2019 National Tax Clinic Project: The ANU Tax Clinic' (2020) 22(2) *Journal of Australian Taxation* 193.

58 Castelyn (n 1).

59 Indra Abeysekera, 'National Tax Clinic Program in the Northern Territory, Australia: A Project Model Innovation' (2020) 22(2) *Journal of Australian Taxation* 174.

60 Brett Freudenberg, Colin Perryman, Kristin Thomas and Melissa Belle Isle, 'The Griffith Tax Clinic' (2020) 22(2) *Journal of Australian Taxation* 64.

61 Van Le and Tina Hoyer, '2019 National Tax Clinic Project: James Cook University Tax Clinic' (2020) 22(2) *Journal of Australian Taxation* 162.

62 Sunita Jogarajan, Kate Fischer-Doherty and Julian Panetta, '2019 National Tax Clinic Project: Melbourne Law School Tax Clinic' (2020) 22(2) *Journal of Australian Taxation* 27.

63 Ann Kayis-Kumar, Gordon Mackenzie and Michael Walpole, 'Interprofessional Collaborative Practice in Pro Bono Tax Clinics: A Case Study Approach' (2020) 22(2) *Journal of Australian Taxation* 49.

64 Robert B Whait, '2019 National Tax Clinic Project: UniSA Tax Clinic' 2020 22(2) *Journal of Australian Taxation* 137.

- University of Tasmania ('UTas')[65]
- Western Sydney University ('WSU').[66]

These articles comprise a complete and representative data set since each clinic participating in the NTCP trial contributed an article to the special issue, the articles were written to achieve a common objective using a similar method and were based on a template provided by one of the clinic academics. The common objective is evidenced by the special issue guest editor who wrote:[67]

> Each article in this special edition is written by the tax academics and tax clinic staff engaged in each of their tax clinics, with each article discussing the unique operating structures used in order to comply with the requirements of the Australian Government.
>
> Each contribution in this issue portrays how each Tax Clinic has put into practical operation these guidelines and provides insight into how this initiative has greatly enhanced access to our tax system for Australian taxpayers.

The template provided on which all articles were based recommended that each article should contain an introduction followed by a discussion of the clinic design including details of the clinic model, the level and type of student involvement, and the level and type of client involvement. The template also recommended that a discussion regarding the research methodology follow and suggested that a reflective case study approach be used based on reflections from the academic authors involved in establishing their clinic, as well as comments from student and client interviews and questionnaires that were conducted. In a manner consistent with the method, the template recommended discussion of the academic author's reflections and observations on the key challenges, key learning experiences for themselves and students and key client experiences. Recommendations and conclusions based on the academic's reflections were suggested as the final section in the template. Critically, the template specified that the purpose of each article was to provide key observations from the 2019 experience of conducting a tax clinic. The articles covered the same time period having focused on each clinic's establishment during 2019, except for UniSA Tax Clinic's article since UniSA joined the program late resulting in its trial period being offset from the other clinics by 6 months.

Even though the articles were written with a common objective, method, and based on a suggested template structure, limitations may result from authors deviating from the structure and objective at various points. For example, some authors chose to include a literature review in their article. Authors may also have been reluctant to discuss some aspects lest they offend their employers, colleagues and/or the Australian Tax Office ('ATO'). Notwithstanding these limitations, these articles currently represent the best available data to study the formation of tax clinics in Australia. Indeed, how the fledgling

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[65] John McLaren, '2019 National Tax Clinic Project: The University of Tasmania Tax Clinic' (2020) 22(2) *Journal of Australian Taxation* 96.

[66] Connie Vitale and Michelle Cull, '2019 National Tax Clinic Pilot Project: Western Sydney University' (2020) 22(2) *Journal of Australian Taxation* 116.

[67] Michael Blissenden, 'Foreword' (2020) 22(2) *Journal of Australian Taxation* i.

NTCP attained and maintained legitimacy can help current and future clinics attain and maintain legitimacy by informing them through the analysis herein reported. The analysis reported herein can also inform stakeholders about the objectives of the NTCP and how each clinic aims to meet those objectives. The special issue presents a unique opportunity to study all the 10 clinics in the trial phase of the program while they were being established and seeking support from the various stakeholders. The limitations in the data are also mitigated to a certain extent by the theoretical lens used to inform the analysis since it focuses the analysis onto specific aspects.

B *Data Analysis*

The analytical method employed in this study may be referred to as inductive analysis.[68] Inductive analysis is a broad term used to denote methods that involve one or more detailed readings of data to 'derive concepts, themes or a model through interpretations'.[69] The process is inductive since it allows the research findings to emerge from the data in contrast to deductive methods which might constrain the data due to their focus on testing a hypothesis or due to the need to adhere to a strict method.[70] Inductive analysis also allows for voluminous data to be reduced, managed and displayed to facilitate the drawing of conclusions that are relevant to the research question or objective.[71] In this study, text-based data in the form of the Articles was analysed to allow themes, trends and patterns to emerge. Since this study's objective is concerned with legitimacy of tax clinics, the data was subsequently analysed via that lens by categorising the data into the types of legitimacy and the strategy relevant to achieving it.

Thomas provides a five-step process for coding data in an inductive manner.[72] In summary, this process involves preparing and formatting the raw data, closely reading the data, creating categories in upper and lower levels, reducing overlap and redundancy, and revising and refining the categories until the researchers are satisfied. This process was followed during this study. The Articles used in this study are freely available and can be downloaded from the journal's website. The authors obtained a Microsoft Word version of the edition in a single document and separated each article into its own document. Each article was then imported into *NVivo* and given a title based on the university clinic being discussed in each paper. Various nodes were developed based on the contents of each article. The highest level of nodes (parent nodes) were titled 'challenges', 'models', 'successes', 'university setting', and 'who benefits'. After developing the first nodes, one author coded themes to them. Initial coding was undertaken on the paper produced by JCU. Data regarding each clinic's marketing strategies (Table 1 below)

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[68] David Thomas, 'A General Inductive Approach for Analyzing Qualitative Evaluation Data' (2006) 27(2) *American Journal of Evaluation* 237.

[69] Ibid 238.

[70] Ibid.

[71] Matthew Miles and Michael Huberman, *Qualitative Data Analysis* (Sage, 2nd ed, 1994).

[72] Ibid 73.

and student recruitment characteristics (Table 2 below) was also drawn from the Articles and collated in *NVivo* as described above.

Qualitative research ought to be conducted in a trustworthy manner that is credible, transferable, dependable, and confirmable.[73] Trustworthiness in this study was achieved by independent parallel coding[74] where a second author undertook identical analysis on JCU's article to gain a mutual understanding and reflection regarding coding to nodes and developing new nodes. The nodes developed from parallel coding of the JCU article were compared and discussed by two of the authors leading to an agreed upon set of nodes for further analysis. The remainder of the papers were then divided among the same two authors and were coded independently; however, one author checked all the coding for appropriateness to the relevant node. After the coding was completed, nodes were categorised into legitimacy types based on the text allocated to each node. Further, a legitimacy strategy was identified for each type. The data within each node was then mined to identify relevant legitimacy types and the strategies to attain that type. Challenges to attaining and maintaining legitimacy were also identified.

Coding in *NVivo* generally requires the researchers to agree on a coding unit, either a word, sentence or paragraph, which enables analysis based on the amount of text devoted to that theme. Since this research is concerned with broad themes that emerge from each of the Articles, it was not necessary to settle on a coding unit. Instead, the authors coded text in sentences or paragraphs based on convenience, however ultimately whole paragraphs irrespective of their size were coded so that the coded parts could be seen in context. The results of the analysis described herein are discussed below. Where relevant and necessary, the manuscript supporting the results will be identified.

IV RESULTS AND DISCUSSION

The commentary in this section is segmented into three components which parallel the *NVivo* coding and separation into legitimacy types and strategies. Accordingly pragmatic legitimacy will be discussed first followed by moral legitimacy and then cognitive legitimacy. Within each component, the authors will address the identified research question by discussing the legitimation strategies used by clinics separately for each stakeholder.

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[73] Yvonna Lincoln and Egon Guba, *Naturalistic Inquiry* (Sage, 1985).

[74] Ibid.

A *Pragmatic Legitimacy*

As discussed above, pragmatic legitimacy is concerned with self-interested and instrumental evaluations of new practices by external stakeholders. This can be achieved via *conform strategies* that show how the new practice meets stakeholders' needs and provides instrumental value, or *selection strategies* that identify and attract stakeholders who value the types of exchanges that the new practice provides, or via *manipulation strategies* that attempt to persuade stakeholders that the new practice has value for them.[75] This section will discuss how the clinics achieved this type of legitimacy in view of all stakeholders as well as the following identified stakeholders: The ATO, Treasury and the Federal Government, the profession, clients, students, and universities.

1 *All Stakeholders*

Securing client demand, to be discussed further below, is also an important *conform strategy* for all other stakeholders since it demonstrates the practical need for tax clinic services. Two clinics specifically noted that it was difficult to anticipate or predict client demand (Curtin, UniSA), one clinic mentioned the difficulty of attracting clients at the beginning of their clinic's operation (Griffith) and two clinics noted the difficulty in predicting client demand for outreach services (UniSA, JCU). A particularly difficult period mentioned by two clinics is the first half of the year where tax is not foremost in peoples' minds (UTas, UniSA).

2 *The ATO, Treasury and the Federal Government*

The principal concern for these stakeholders and indeed the pathway to legitimacy is ensuring that tax clinics deliver on providing the services expected of them as specified in the NTCP guidelines.[76] One *conform strategy* used by each clinic to attain pragmatic legitimacy with policy stakeholders was to report various statistics to their stakeholders. Although this reporting was required by the NTCP, it demonstrates to the stakeholders that the clinics are operating successfully, are providing value and are meeting the program's objectives, although this remains contingent on whether clinics are selecting appropriate clients as discussed below. Other key performance indicators were developed for feedback to those managing clinics and for reporting to various stakeholders as the need arose.

3 *Clients*

Vulnerable clients are perhaps the group that most directly benefits from each clinic's activities. Clients in theory can be viewed on an individual level or as a collective. One *conform strategy* used by each clinic to attain pragmatic legitimacy with clients was to demonstrate an understanding of the taxation laws to clients. This was primarily achieved through engaging clients in seminars or direct compliance or advisory work and students through immersive learning. Forty percent of clinics stated that members of the community that attended seminars hosted by clinics increased their tax literacy by

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[75] Suchman (n 18).

[76] This notion is concurrent with the finical concept of ROI (return on investment). Notably, as the federal government invested $100,000 into each clinic, it was prudent to demonstrate a return.

obtaining general tax information on a variety of small business and individual tax matters (UniSA, UTas, WSU, ANU). Twenty percent of the clinics highlighted a high level of attendance at the seminars; with over 100 (UniSA) and 123 (UTas). One clinic noted that clients who came to the clinic for services had their tax affairs dealt with which may not otherwise have occurred since time and money were barriers to fulfilling their obligations (UniSA). Fifty percent of the clinics highlighted that numerous clients took advantage of the opportunity to be brought up to date with their tax affairs or have some tax matter dealt with (UTas, CDU, JCU, WSU, UniSA). Thirty percent of clinics mentioned that the advice and assistance they received whilst having their tax affairs dealt with increased their tax literacy and empowered them to try completing their tax on their own in future (JCU, Griffith, MLB). Additionally, 30% of clinics stated that clients were grateful for the assistance provided to them (Griffith, MLB, WSU) and 40% of clinics mentioned that clients provided positive feedback about the services provided (UniSA, JCU, MLB, WSU). Twenty percent of clinics serviced regional and remote areas (Curtin, JCU), and one clinic took their outreach to the suburbs (UniSA).

Specific examples of instrumental value (consistent with a *conform strategy*) received by clients' participation was provided by two clinics (20%) which included the following:

- a reduction in a taxpayer's debt and the implementation of a payment plan for the remainder of the debt (Curtin);
- $10,000 in debt waived for a refugee (MLB);
- approximate value of work performed for clients totalling $318,150 (Curtin);
- approximately $1,400,000 in debt was corrected or written off (Curtin);
- the value of pro-bono contributions by industry partners totalling more than $100,000 for the preparation of 585 income tax returns and/or business activity statements (Curtin).

Since clinics provide free services, vulnerable clients only need to invest their time to come away from the clinics with a positive exchange. Evidence of the positive exchange is also provided by specific feedback comments. For example, one clinic, WSU, asked clients, '[w]hat were your original expectations of the Tax Clinic and how did your visit to the Tax Clinic compare?' Clients reported that their expectations were met and, in some cases, exceeded. Overall, the client experience was positive and each client who has visited the clinic had their tax issues satisfactorily resolved.

Vulnerable taxpayers support for clinics was recognised through customer surveys, emails and open expressions of relief. The ATO recognised the work of the clinics through more tax awareness evident in the community and contributions made to change systemic issues in the current tax system. Universities support the program for the positive impact to their reputation, the student experience resulting in improved graduate employability, and a successful work integrated learning (WIL) program. While this is a great result, challenges concerning managing client expectations around the responsiveness of government departments can erode pragmatic legitimacy gains. Outreach to the suburbs or remote and regional areas carries risks that there may not be much client demand when going there leading to perceptions of tax clinics being a solution without a problem.

4 *Students*

Students are another group that received substantial direct benefits from participation in the clinic. One clinic reported that their students believed that their involvement was

rewarding (Griffith), another clinic reported that students' feedback was immensely positive (ANU), a third clinic mentioned that students were grateful to be part of the clinic with feedback on a 5-point Likert scale demonstrating that students agreed or strongly agreed that participation was a valuable learning experience that provided insight into the profession (WSU). Students at Melbourne University 'appreciated the opportunity to present their research to ATO staff and felt like they were making a difference with their work'. Overall, 80% of clinics reported positive student experiences, evidenced in many ways. Twenty percent of clinics reported student feedback from 2019 was universally positive (ANU, JCU), 20% reported that students were unanimously positive regarding their clinic experience (MLB, WSU). One clinic stated that students' pro bono work ethic had been awoken (UniSA).

Thirty percent of the tax clinics referred to more specific benefits which included the knowledge, skills and experience gained of both a technical and soft skill nature leading to enhanced employability (WSU, MLB, Curtin). Forty percent of clinics positively highlighted technical skills developed including the improvement of tax technical knowledge, legal skills and research skills (Griffith, MLB, UniSA, WSU) and one tax clinic mentioned the linking of those skills with practice (Curtin). Some clinics stated how skills were developed, for example 20% mentioned soft skill development through written and oral communication skills (ANU, WSU), 10% mentioned empathic skills (WSU), 20% mentioned interviewing skills and approaches (WSU, MLB) and one clinic mentioned working with clients (Griffith). Another clinic highlighted leadership skills for students returning as mentors (UTas), 20% highlighted pro bono ethic (WSU, UniSA) and 30% highlighted the students' development as professionals (ANU, Griffith, WSU).

One clinic stated other miscellaneous benefits included forming relationships with tax professionals volunteering in the clinic (ANU) which directly led to employment opportunities with the mentors and beyond (ANU). Twenty percent of the clinics stated that on a practical level, the time students spend in the clinic [under the supervision of registered tax agents] contributes towards the Tax Practitioners Board ('TPB') education requirements for students to become a registered Tax Agent (WSU, UTas).

One clinic used a reflective journal as an assessment task which demonstrated to the academic staff that the students are enjoying the experience whilst developing their transferable and employability skills. Receiving this type of feedback from students makes for a rewarding experience for an academic (WSU). In addition, all students felt supported by their academic supervisor and would recommend participating at the Tax Clinic to fellow students (WSU). The *conform strategies* are also evidenced by students' support of the program expressed in various social media posts and feedback to supervisors thanking the clinics for work experience and their opportunity to help the vulnerable clients in their community. These positive exchanges contribute to narratives about the clinic that can be broadcast to students more broadly thereby creating legitimacy within the student body which encourages further participation.

In a similar manner to clients, there are challenges in attaining pragmatic legitimacy with students as evidenced by the difficulty in obtaining student participants in non-teaching weeks and getting volunteer students to commit for a whole semester.

Pragmatic legitimacy is also achieved by *selection strategies* geared toward identifying and attracting constituents who value the types of exchanges the new practice can

provide. Marketing is central to attaining this type of legitimacy and it dominates the discussion below. Marketing can also be viewed in the context of a *manipulation strategy* as well through it attempting to persuade stakeholders regarding the value of clinics. The primary means to attract clients to clinics was via numerous forms of marketing. Twenty percent of clinics regarded marketing as a way of raising awareness of the clinics generally among the public (ANU, Griffith) while 30% of clinics focused on targeting specific client types (ANU, WSU, JCU). One clinic mentioned that the community needed to be aware of how to apply for assistance (Griffith). Clinics tried many ways of marketing with some being more successful than others as discussed below. The marketing strategies adopted by each university are summarised in Table 1. The data for this table was collated in *NVivo* from the Articles as discussed in the method above.

Table 1: Marketing strategies

	Social Media	Print Media	Radio / TV	Media Releases	Clinic Website	Staff / Student Notices	Flyers / brochures	Banners / signs / posters	Seminars	Extant Relationships	Letterbox drops and visits	Special event (launch day)
ANU	x	x	x		x		x	x		x		
CDU	x	x	x	x	x		x	x			x	
Curtin	x	x	x		x							
Griffith	x	x	x	x	x					x	x	
JCU					x							
MLB	x				x	x		x			x	
UNSW					x							
UniSA	x	x	x	x	x	x	x	x	x		x	x
UTas					x							
WSU		x	x	x	x	x	x	x	x			x

Additionally, the ATO promoted the clinics via its own website and through the small business news bulletin that it emails to those that subscribe to it. This has not been included in the above table since this was an ATO initiative. The NTCP also partnered with Financial Counselling Australia which increased the number of taxpayers assisted by the clinics.

One clinic stated that social media was effective partly because it started several months prior to a clinic opening (ANU). Social media has broad reach, is inexpensive and it is possible to get statistics on hits but is potentially reliant on an algorithm and can be cancelled at the whim of the platform (Facebook). Another clinic mentioned that mentors and community partners recommended better targeting of the intended clientele (ANU), but did not mention how to do that and what that involves. One clinic stated that although not listed above, word of mouth was regarded as the most 'relevant' way to promote their clinic (Curtin). One clinic shared that seminars doubled as a marketing tool to increase the awareness of clinics in the community as well as educating the public about tax matters (UniSA). They were often poorly attended leading to few clients arising from them, but took significant time and effort to develop, market and operate meaning that their value as a marketing strategy was limited (UniSA).

Another example of a *selection strategy* was to attract clients within the respective university communities. Most clinics (70%) are centred around one or more university campuses with a few providing outreach to additional locations which created challenges with securing client demand as discussed above. For example, Charles Darwin University which provided services at shopping centres in the Northern Territory in addition to its university campus, Curtin University serviced the entire state of Western Australia with the clinic travelling to Broome in August and Albany in October, and James Cooke University serviced North Queensland and conducted mobile 'pop-up' clinics in the North Queensland towns of Ayr, Ingham and Cairns at special times unspecified. While UniSA's clinic was mainly centred in the Adelaide CBD, it operated at Hackham West Community Centre (about 1 hour by car south of Adelaide) every Wednesday from August to October 2019.

Challenges with marketing and not attracting as many of the right type of clients will create problems for legitimacy. Seventy percent of clinics mentioned that marketing was challenging, although some clinics expanded on the issue in their articles more than others and experienced different specific issues. These generally centred on attempts to direct the marketing toward clients who meet the clinics' criteria. In addition to this, the discussion indicates that marketing could have been improved overall, for example, one clinic said that marketing could have been more effectively targeted toward intended clients (ANU) rather than simply raising awareness.

Factors that impeded marketing varied. Apart from the general lack of community awareness of the clinic project mentioned by two clinics as being a general hurdle to overcome (ANU, Curtin), these two clinics also experienced skepticism from stakeholders which exacerbated the problem. Another challenge, which directly impacts on legitimacy, is that clinics' marketing efforts inevitably draws attention from the tax profession raising concerns about poaching clients. One clinic, WSU, was asked directly by *Accountants Daily* whether clinics were taking work away from accountants. The response, which is consistent with a *selection strategy* for attaining and maintaining legitimacy, follows:

> I think there is some stigma that this was set up to take work away from accountants and this is definitely not about that … It needs to be clear that we are not trying to take work away from other accountants, where this is clearly designed to providing services for unrepresented, low-income taxpayers that are individuals, sole traders or partnerships.

One clinic acknowledged that hampering efforts to overcome marketing challenges was marketing that was poorly coordinated due to it being ad-hoc involving disparate groups from different internal divisions (Griffith). Another clinic (UniSA) found it difficult to communicate a clear message, for example: stakeholders interpreting 'individuals' to not include small businesses. Also creating challenges is the need for clinics to comply with their institutional marketing protocols and guidelines when undergoing any marketing practices. This meant that clinics were not necessarily free to market their services in the manner they wished. University marketing practices are geared toward attracting students for education, not clients to receive free professional services. Two clinics mentioned that deficient marketing meant that the group that clinics were supposed to help, i.e., those in the community who could not afford a tax agent, was not sufficiently reached (JCU, UniSA).

One clinic stated that the marketing challenges were mitigated by having more time for marketing prior to the operation of a university's second clinic (ANU). Another suggested allowing networks to grow and developing lists of contacts that are updated regularly assisted with marketing (Griffith) whilst UniSA suggested leveraging off existing partnerships (UniSA). Three clinics mitigated marketing challenges by having academics act through their own initiative by distributing leaflets (Griffith, UniSA) drafting media releases and using social media etc (Griffith) and directly approaching community groups (Griffith; UniSA; CDU).

One clinic highlighted that a further marketing challenge was the inability or unwillingness of marketing departments to adapt marketing strategies when it was clear that they were not effective (UniSA). The quick establishment time imposed on all participating universities meant that systems to track the effectiveness of marketing strategies were not in place when clinics first opened (such as the case with UniSA) but were developed during the first semester. These systems remain rudimentary and require further work. It might be appropriate for clinics to collectively adopt a more global marketing strategy, although clinics that rely solely on referrals from external organisations and/or are in highly populated areas may not regard that as a priority.

One clinic implied that traditional advertising tends to not be successful. For example, UniSA conducted over 10 radio interviews, although it is difficult to evaluate as indicated above. Marketers advised that the clinic is not 'sexy' enough to advertise on its own. Instead, there needs to be a carrier message in the form of a current, topic tax issue that affects many people to grab their attention, then tack on a message about the clinics at the end. The same clinic (UniSA) recommended more systematic evaluation of marketing strategy effectiveness and amending the strategy accordingly.

Thirty percent of clinics sought to service a more remote area away from their main office, but in some cases, securing client demand was problematic. For CDU, operating beyond Darwin was an imperative since the Northern Territory has low population density over a wide geographic area. To service this population, CDU opened up mobile clinics at various shopping centres in the Northern Territory. Other clinics also sought to service broader geographical areas. JCU established pop-up clinics in Northern Queensland and UniSA established a secondary clinic in Hackham West, a southern suburb of Adelaide. Curtin also travelled to remoter locations in Western Australia. CDU paid for advertisements in local newspapers to foreshadow their arrival in these areas in the hope of securing demand. UniSA no longer operates in Hackham West, instead, it offers a remote service via telephone or video conferencing which enables it to service the entire state in a flexible manner. One clinic (JCU) stated that the marketing that was undertaken was generally ineffective in some way or less effective than it could have been for operating their pop-up (mobile) clinics. Clinic operations in more populated areas fared better and were more likely to have stable demand. The issue for clinics in less densely populated areas is the extent to which they rely on the university community for clients versus attempting to grow more community awareness and clients from that.

The above discussion highlights the challenges faced but also the importance of marketing strategies to clinics in securing clients. These strategies also inform potential students who are interested in becoming a tax professional after graduation. Strategies to increase awareness of clinics in the community is another objective that requires a means of

evaluation with respect to how much has awareness spread and what are the most effective means to increase it?

5 *The Profession*

Discussion about the profession can be divided into discussion about the specific firms and practitioners within them that provide pro bono assistance to clinics and discussion about the profession more broadly. Firms that provide pro bono assistance are the easiest to attain pragmatic legitimacy since they exchange directly with the clinics that they support whereas the broader profession exchanges with clinics in a more distance, indirect manner.

(a) *Firms Providing Pro Bono Support*

Due to firms providing pro bono support being directly involved and exchanging with clinics, the main legitimation strategies are *conform strategies*. Thirty percent of clinics refer to pro bono practitioners' direct interaction within their clinics and the value they obtain via these exchanges. Some pro bono practitioners saw value in participating and helping clinics due to development opportunities for staff, especially those who were new to the profession, marketing opportunities for their firm due to the publicity that participation and being associated with the clinic provides and through observing and assessing student volunteers for recruitment (JCU). Pro bono practitioners appreciated being included as part of the clinic (ANU) and provided positive feedback about it (JCU).

Various skills among the staff providing pro bono assistance were enhanced and developed including leadership skills through mentoring students, listening, communication and empathy skills due to the challenging situations the clinic's clients present that staff of the pro bono firms are not generally exposed to (MLB). Staff from pro bono firms that assisted clinics viewed their employers in a more favourable light (MLB). Pro bono practitioners do not need to be the direct beneficiaries of the exchange to see instrumental value that the clinics provide. Instead, they can see value for the profession more generally by observing how clinics provide students with the 'opportunity to advance their practical skills in applying the law and improve them as prospective legal practitioners and employees' (MLB).

(b) *The Broader Profession*

The profession more broadly cannot obtain such direct exchanges and cannot see the benefits to them unless they are directly involved. This is reflected in the difficulty in getting pro bono help at times (JCU) and comments from one clinic that they would like to see engagement with industry (ie the profession) improve (Griffith).

6 *Universities*

Positive exchanges from students' participation also creates pragmatic legitimacy for tax clinics in the eyes of the university since universities are interested in student welfare, satisfaction and learning outcomes.

B ***Moral Legitimacy***

Moral legitimacy is attained by the practice being perceived as the right thing to achieve certain social outcomes and increase societal welfare. As discussed above, moral legitimacy can be attained via *conform strategies* that show how the new practice has achieved the socially desirable outcomes, or *selection strategies* that involve selecting

social welfare criteria and objectives that appeal to stakeholders, or *manipulation strategies* that persuade stakeholders regarding the merit of the social welfare objectives that the new practice will achieve.[77] There were several challenges that needed to be addressed to ensure that socially desirable outcomes were attained. Clinics needed to attract appropriate clients and serve them with an open, non-judgmental client mindset. Students also needed to be recruited and provided with a true work experience setting, a challenge that arises since we cannot control the level of client demand or the issues they will present. This section discusses the strategies clinics used to obtain moral legitimacy with all stakeholders, firms providing pro bono support, clients and students. Some *selection strategies* regarding clients and students will also influence legitimacy for other stakeholders who assess whether clients and students are selected using morally appropriately criteria.

1 *All Stakeholders*

A clear *conform strategy* for all stakeholders was for clinics to produce reports that collate and summarise data regarding how each clinic has achieved its social objectives. *Selection strategies* are evident in appeals and references to the NTCP goals and objectives. The criteria set by the NTCP specifically mentioned assisting vulnerable taxpayers. It was assumed that stakeholders for whom the moral criteria would be appealing existed. Vulnerability was not specifically defined leaving this to the discretion of the individual clinics. Therefore, clinics were required to develop criteria for client recruitment as will be discussed further below.

2 *Firms Providing Pro Bono Support*

Practitioners who engage in pro bono work can directly see the social good that the clinic that they are involved with creates. Such a *conform strategy* led to those firms supporting clinics partly because of it and two clinics (20%) shared examples of this. At James Cook University, a firm regarded its involvement as an opportunity to engage in a 'social justice project in the North Queensland community'. At Melbourne University, another firm participated out of 'a desire to assist vulnerable taxpayers and teach and mentor students'. It was reported by 20% of clinics that practitioners found providing pro bono services 'rewarding' (JCU, MLB), but the nature of the reward was often not specified. One clinic reported that clinics gave firms an opportunity to 'do meaningful work' (MLB). Pro bono practitioners in one clinic (JCU) were somewhat reluctant to do some of the base level work required to help vulnerable taxpayers comply with their tax obligations since they felt their time was better spent on complex cases and on student learning and support.

3 *Clients*

Moral *conform strategies* for clients would focus on social outcomes that they receive. Thirty per cent of clinics highlighted that clients reported that their mental wellbeing improved from knowledge gained and being assisted with their tax affairs (UniSA, WSU, MLB) with one clinic further adding that having their debts reduced and other disputes

[77] Suchman (n 18).

resolved also aided this improvement (MLB). This clinic also advised that clients expressly stated that they were less stressed about tax after their visit to the Clinic (MLB).

Moral *selection strategies* for clients (and other stakeholders such as the profession) would focus on appropriate criteria for their selection. There were no specific client eligibility criteria mandated by the ATO, only that services were to be for clients who were deemed to need the program to address a perceived gap in the market.[78] This broad criterion was foundational to the clinics' formation since they were not intended to compete with the profession, but it led to some variety in the target client market with lack of representation due to taxpayers being unable to afford it as the common denominator across all clinics. Twenty percent of clinics (Curtin, UniSA) also stated that a condition be that the taxpayer be an Australian resident (or permanent or temporary resident), but some latitude may have been given depending on circumstances. Twenty percent of clinics clarified that in practical terms, each client was assessed on its own merits with some (UniSA, Curtin) having a clause in the client service agreement to stop providing services if it became clear that the client was not eligible. Only ANU restricted services to individuals without business item schedules, but that was later lifted. MLB only serviced small business if they were in a dispute with the ATO or requiring establishment information. UniSA could not restrict help to individuals since a tax help centre had already been established on campus and a point of differentiation was required to ensure sufficient work for students to gain experience with.

Some clinics imposed income based limits, but others based vulnerability on more qualitative or situational factors. For example, ANU limited clients' pre-tax family income to $60,000 later increasing that to $80,000 assessed on an individual basis. MLB used the tax help criteria for individuals with annual income of less than $60,000 or with low financial literacy or with a non-English speaking background. WSU imposed a limit of $2 million in turnover for small businesses in line with the 2016 small business tax concessions threshold.[79] Even though that threshold was later increased to $10 million in the 2017 financial year WSU kept the limit at $2 million.

Attaining and retaining moral legitimacy requires *selection strategy* to identify which areas to serve based on appropriate moral criteria which were generally based on a reasonable density of vulnerable clients who required free tax services. Clinics achieved mixed success in providing outreach services due to the lack of client demand and challenges in scheduling clients for the time that clinics were present in these locations.

In practical terms, from a geographical standpoint, each clinic served clients in its own state since it was clear from the NTCP that each state was to have a clinic to serve it. Nevertheless, it was theoretically possible for clinics to serve clients outside their state, although this was not commonly done. To avoid confusion, some clinics clarified their geographical limits, particularly in states that had more than one clinic. Only 20% of clinics (ANU, JCU) imposed territory-based criteria by limiting services to the ACT and North Queensland residents respectively with ANU removing that limitation later. The

[78] ATO, 'National Tax Clinic Trial' (Grant Guidelines, 2019).

[79] *Income Tax Assessment Act 1997* (Cth) s 328-110.

only clinics that are in close geographic proximity are UNSW and WSU, but UNSW obtains clients solely from financial counsellors while WSU obtains clients from financial counsellors and other more general sources. Evidently, all clinics ensured that their services were provided to the target market thereby re-enforcing the *conform strategy* of moral legitimacy.

4 *Students*

Conform strategies for attaining moral legitimacy are evidenced by students from one tax clinic stating that they experienced an improved sense of community, belonging and inclusivity, and a sense of pride and purpose through their service to the clinic (Curtin). All but one student from a second tax clinic also agreed that being part of the Tax Clinic helped to develop their interest in doing pro bono work in the future (WSU). *Selection strategies* for attaining legitimacy include the criteria and method to recruit students with the characteristics of eligible students, as determined by each clinic, shown in Table 2. The data for this table was collated in *NVivo* from the Articles as discussed in the method above.

Table 2: Student recruitment characteristics

	Post Graduate	**Under Graduate**	**Business Student**	**Law Student**	**GPA**	**Internship/WIL Enrolled Unit**	**Volunteers**	**Completed or enrolled in a Taxation Law Unit**	**Second to third year of study**	**EOI, CV and Interview required**
ANU	x	x				x		x	x	x
CDU	x		x				x	x		
Curtin		x	x	x			x	x	x	x
Griffith		x	x	x	x	x	x	x	x	x
JCU		x	x	x		x		x		x
MLB	x			x		x		x		x
UNSW	x	x	x	x		x	x	x		
UniSA	x	x			x	x	x	x		x
UTas	x	x				x	x	x	x	
WSU		x	x		x	x		x	x	x

Overall, the clinics allowed both postgraduate and undergraduate students to assist in the clinic with eight of the 10 clinics stipulating that the students must have completed or be currently enrolled in an introductory taxation law unit. These eligibility criteria support the statement made by Andrew Mills[80] that the tax clinics 'will also give tax law and accounting students practical experience of dealing with clients in a real-life setting'. Supporting this notion, most of the tax clinics required students to apply for their positions via the submission of an Expression of Interest and Curriculum Vitae which was followed up by an interview with the Tax Clinic Manager/Director. Curtin University and Charles Darwin University did not require the students to be enrolled in a unit whilst volunteering at the clinic. CDU had six students undertaking a Master of Professional Accounting course who had completed the taxation course unit volunteering in the teaching clinic. Whereas Curtin insisted on an appropriate course of study with volunteers 'which demonstrated an ability to work both autonomously, collaboratively, and in a customer or other client-focused environment' more relevant than prior tax-related experience. Most students participated in the clinic for the duration of their enrolment in the relevant unit.

C *Cognitive Legitimacy*

Cognitive legitimacy is concerned with the practice being regarded as the most appropriate and acceptable way to achieve an outcome. As with the other types of legitimacy, *conform*, *selection* and *manipulation strategies* can be used to attain this type of legitimacy. *Conform strategies* involve showing how the new practice has adopted or been influenced by existing respected practices, models or standards while *selection strategies* involve selecting an appropriate certification, model or standard for the new

[80] Andrew Mills, the then Second Commissioner, ATO, 'Tax in a Changing World' (Speech, Australasian Tax Teachers' Association 31st Annual Conference, Perth, 17 January 2019).

practice and *manipulation strategies* involve enhancing understanding or comprehensibility by constructing narratives about the practice or having other organisations copy identical or similar methods of conducting the new practice.[81] Having the appropriateness of the new practice being regarded as self-evident and its existence taken for granted are other *manipulation strategies*.[82] There were far fewer cognitive legitimacy strategies employed by clinics, therefore this section does not discuss them with reference to any specific stakeholder. Rather, it is likely that the few cognitive strategies would be relevant to all stakeholders.

A cognitive *conform strategy* can involve showing how the new practice has copied established and respected models and standards. Individual clinics attained legitimacy by following the successfully tested 'Curtin' model. Choosing this option not only provided the implementation of already established policies and procedures it also assisted to encourage the support of the university legal team and allowed the clinic to open up on very short notice. Other clinics chose not to follow the same model as this was not a stipulation of the grant guidelines, opting to utilise some of the 'Curtin' resources, for example the client agreement and the student participation deed. The clinics choosing not to utilise the same model in essence did not use the *conform strategy* of legitimacy.

A cognitive *selection strategy* may involve selecting a 'certification or standard that can be applied to the practice'. The NTCP specified that the clinics should at a minimum include the supervision of a tax professional however did not mandate how that supervision was to be performed and what type of tax professional was to provide it. Twenty percent of clinics chose to identify tax professionals as full-time academics who were also registered tax agents (Curtin, WSU), where three tax clinics employed tax academics that were not registered tax agents (CDU, UTas, MLB). Another option adapted by two clinics was to hire external tax agents (Griffith, UNSW) and two other tax clinics hired external tax professionals who were not registered tax agents (ANU, UniSA). Pro bono services were also provided to 40% of clinics by tax agents or legal professionals (Curtin, JCU, MLB, UNSW) to supplement current expertise in the clinic. Maintaining the minimum standard of having a tax professional available highlights a cognitive *selection strategy*.

Cognitive legitimacy can also be attained by it being *taken for granted* that it is an acceptable or natural approach to effect collective action, i.e. the need for the practice is essentially self-evident. This was most observed by the willingness of each of the clinic universities to establish a clinic and the success of each university in doing so.

V CONCLUSION AND CONTINUATION

This study has considered the fledgling NTCP program through the lens of legitimacy theory. Since the NTCP's provision of free tax advice, education, and representation and additionally is a new type of service, it needs to attain and maintain legitimacy in the eyes of stakeholders to survive in the long term. This study inductively analysed articles submitted and published by each participating clinic in the *Journal of Australian Taxation*

[81] Suchman (n 18)

[82] Ibid.

special issue[83] to determine what legitimation strategies were adopted by the 10 clinics that participated in the NTCP trial.

Pragmatic legitimacy was the predominant form of legitimacy that clinics attained by demonstrating the value that clinics provide to stakeholders. Policy stakeholders such as the ATO, Federal Treasury and the Federal Government received value though the success of the program in meeting its objectives as demonstrated via reports provided to them. Clients received value in getting their taxes done and the associated relief while students received value through skills developed and the relationships formed with the profession. Significant effort was expended on marketing strategies to convey the value that clinics provide. Tax firms providing pro bono support saw these benefits directly while assisting clinics.

Attaining moral legitimacy involved ensuring that stakeholders were aware that the clinics were achieving its social objectives as well as having morally appropriate criteria to select and recruit clients and students and select the geographical location to provide outreach services. Attaining cognitive legitimacy involved conforming to a well-regarded and successful model of practice such as the Curtin model (as the first Australian tax clinic) as well as its policies and procedures and selecting appropriate people with qualifications and experience to supervise students and serve clients.

The study shows a reliance on pragmatic legitimacy which is easier to attain, but it is not as durable as moral or cognitive types of legitimacy. It may be wise for clinics to shift focus toward attaining moral and cognitive legitimacy by adopting relevant and appropriate strategies. In this way, clinics' legitimacy to provide free tax services will be 'taken for granted' and regarded as the 'self-evident' solution to assist taxpayers who cannot afford to get help from the profession. Further research could be undertaken with stakeholders to determine what strategies would be most effective in achieving legitimacy from their perspective. Further research could also determine how legitimacy strategies of clinics participating in the NTCP evolve over time.

[83] *Journal of Australian Taxation* (n 6).

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WĪWĪ I AOTEAROA: THE MYTH OF THE AKAROA WINDOW TAX

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ABSTRACT

An article published in the *Columbia Journal of Tax Law*, a prestigious United States journal, reported that 'a missionary in the French colony of Akaroa described how he would climb in and out of his "home" on his hands and knees in an attempt to minimize the size of windows and doors'. Based on this anecdote, the author of the articles sought to demonstrate the folly of the French doors and windows tax (*contribution des portes et fenêtres*).

This article debunks the myth of the Akaroa window tax. It also questions presumptions about the historical impact of taxes, in particular window taxes, on the built environment. The article also reflects on why researchers may perpetuate myths, despite their implausibility.

Key words: window tax, colonial taxes, tax myths, taxes' determinative power

I INTRODUCTION

It is common for tax commentators to attribute a determinative power to taxes in shaping the built environment.[1] A tax on bricks, for example, might encourage avoidance, such as the use of extra-large or tile bricks as a building material. Therefore, if we encounter walls that include extra-large or tile bricks, we may assume that the use of the abnormal building material was determined by the brick tax. Indeed, the proposition that the use of extra-large bricks was caused by a brick tax is commonly encountered.[2] However, Robin Lucas's in-depth analysis of the United Kingdom brick tax (1784-1850) concludes there is no evidence to support the contention that the introduction of extra-large and tiled bricks 'was in any way related to the tax on bricks'.[3] This conclusion does not imply that the brick tax had no impact on architectural design but its effects were likely to have been localised and a less important determinant of design than, say, technological developments or production and transport costs.

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1 See eg, Meredith R Conway, 'And You May Ask Yourself, What Is That Beautiful House: How Tax Laws Distort Behavior Through the Lens of Architecture' (2019) 10(2) *Columbia Journal of Tax Law* 165; Michael Keen and Joel Slemrod, *Rebellion, Rascals, and Revenue: Tax Follies and Wisdom Through the Ages* (Princeton University Press, 2021).

2 See eg, 'The Brick Tax of 1784' *Tax Fitness* (Blog Post, 5 January 2018) <https://taxfitness.com.au/Blog/brick-tax-1784>.

3 See Robin Lucas, 'The Tax on Bricks and Tiles, 1784-1850: its Application to the Country at large and, in particular, to the County of Norfolk' (1997) 13 *Construction History* 29, 51.

Generally, tax is just one consideration in choosing building materials, and more generally influencing how people build. Following Rowan Moore, far more important factors include: 'weather, pollution, vegetation, furnishing, maintenance, decay, taste, property prices, laws, freedoms and restrictions of access and use, sentiment, symbol, association, perception, traffic, density, customs, mood, activity, fear, clothes, food, technology, seismic conditions, artificial and natural light'.[4]

This article, which is an offshoot of a larger research project on taxes and the constitution of the built environment,[5] focuses on the specific claim that a doors and window tax operated in the nascent township of Akaroa on Canterbury's Banks Peninsula (Horomaka).[6] That claim is based on an implausible presumption that France (Wīwī)[7] established a sovereign colony, with its own fiscal system, in Akaroa between 1840 and 1845.[8] This article debunks the myth of the Akaroa window tax. It also questions presumptions about the historical impact of taxes, in particular window taxes, on the built environment. The article also reflects on why researchers may perpetuate myths, despite their implausibility.

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[4] See Rowan Moore, *Why We Build* (Picador, 2012) 391.

[5] See in particular, Jonathan Barrett, 'Tax Determinism and the Cityscape: A Skeptical Approach' (2022) 75(2) *Tax Law Review* 271.

[6] In his circumnavigation of New Zealand, James Cook mistook the peninsula to be an island and named it 'Banks's Island', after his botanist, Joseph Banks. See 'James Cook sights Banks "Island"', *Ministry of Culture and Heritage* (Web Page, 6 October 2020) <https://nzhistory.govt.nz/james-cook-sights-banks-island>. Cook does not appear to have made contact with *tangata whenua* (people of the land); they would presumably have corrected his errors, both as to geography and pre-existing nomenclature.

[7] While the Māori denotation of France as 'Wīwī' and its people as 'Ngā iwi Wīwī' may attract puerile amusement, there is no indication that Māori intended anything derogatory in identifying a country and nation in a particular way because they often heard the utterance 'oui, oui' (yes, yes). Other countries' names in te reo Māori, however, are usually transliterations of the English names.

[8] The name 'Akaroa' is Kāi Tahu Māori for 'Long Harbour', which would be spelled 'Whangaroa' in standard Māori. See AW Reed, *Māori Place Names, Their Meanings and Origins* (Reed, 4th ed, 2016) 15. (This article uses Kāi Tahu dialect spellings, where appropriate, unless quoting.) See also Gordon Ogilvie, *Banks Peninsula – Cradle of Canterbury* (Government Printer, 2007); Louis J Vangioni (with supplementary notes by DJC Pringle), 'Old Maori place names around Akaroa Harbour', Christchurch Libraries (Report, 1967) <https://christchurchcitylibraries.com/Heritage/Publications/Akaroa/OldMaoriPlaceNames/Vangioni-1967.pdf>. Older texts also refer to a previous name 'Wangoolou': see eg, 'Maori History of Banks Peninsula' in HC Jacobson, *Tales of Banks Peninsula* (Akaroa Mail Office, 1914) <http://nzetc.victoria.ac.nz/tm/scholarly/tei-JacTale.html>. Since there is no "l" sound in Māori, this may simply be "Whangaroa" misheard by European ears. See 'Maori Names', *Akaroa Mail and Banks Peninsula Advertiser* (online, 11 December 1906) 2 <https://paperspast.natlib.govt.nz/newspapers/AMBPA19061211.2.15>. Keith Lyons notes: 'Errors were common in the recording of Maori names when explorers and whalers charted the area in the early 19th century. Many names were lost, and those that survived were often corrupted. Hakaroa, Wongaloor, Wageroa and Woonaloa were all given as variants of Akaroa'. See Keith Lyons, 'The French at d'Akaroa' (1992) 15 *New Zealand Geographic* 26.

Part II identifies some common claims about taxes and their power to determine the shape of the built environment. Sceptical counterarguments are presented, which do not necessarily fully rebut determinative presumptions, but are sufficient to destabilise them.

Part III unpacks Meredith Conway's claim that French colonists levied a window tax in Akaroa. I do not intend to impugn the general quality of Conway's scholarship or, indeed, any of the research questioned in this article. In relation to the mythical Akaroa doors and window tax, I have had access to sources which a US researcher could not reasonably be expected to be privy or consult. By way of comparison, this article makes good faith statements about *te reo* Māori (Māori language), made from a *tauiwi* (non-Māori) perspective – these may reveal my own ignorance.

Part IV reflects on implausible claims about taxes and places them in the broad context of contemporary research. It considers why researchers, including leading tax academics, may perpetuate 'urban myths' or otherwise fail to engage with them critically.

Conclusions are then drawn.

II Do Taxes Determine the Built Environment?

Much of what is commonly accepted about taxes and their power to determine the built environment is unfounded, and is repeated without critique or scepticism. An example is the presumption that Greek houses are often left incomplete to avoid property taxes. Michael Keen and Joel Slemrod claim '[i]n Greece, there is a 60 percent tax reduction for unfinished buildings, the predictable result being a glut of half-done buildings'.[9] Kurt Kohlstedt debunks this myth and explains that the exposed rebar allows owners to add more floors over time.[10]

Taxes on building materials have some impact on the built environment but these effects, especially if they are deleterious and unforeseen, may be exaggerated or misattributed. The window tax is the locus classicus. It is commonly identified as the cause of the immiseration of urbanised working people, even though less than 15 percent of houses in the UK were subject to the tax at the time of its abolition.[11] However, a glass tax ran

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9 Keen and Slemrod (n 1) 201. The authors do not provide evidence to support their claim.

10 Kurt Kohlstedt, 'Vernacular Economics: How Building Codes & Tax Shape Regional Architecture' 99%Invisible (Blog Post, 22 January 2018) <https://99percentinvisible.org/article/vernacular-economics-building-codes-taxes-shape-regional-architecture>. See also 'Do Greeks evade taxes by not finishing their houses?' *[SKEPTICS]* (Blog Post) <https://skeptics.stackexchange.com/questions/27662/do-greeks-evade-taxes-by-not-finishing-their-houses>. An exemption is provided under the Municipal Real Estate Duty in respect of buildings under construction. But this exemption lapses after the earlier of seven years or the building being used. See 'Greek real estate taxation: a brief summary' *PWC* (Web Page, May 2018) <https://www.pwc.com/gr/en/publications/greek-thought-leadership/greek-real-estate-taxation-summary-2019.html>.

11 Using data from Ludlow, a small provincial town, Wallace Oates and Robert Schwab demonstrate that the excess burden of the tax caused the number of windows in buildings to bunch below the threshold of the tax. See Wallace E Oates and Robert M Schwab, 'The Window Tax: A Case Study in Excess Burden' (2015) 29(1) *Journal of Economic Perspectives* 163. Their model is plausible but it is questionable whether it can be extrapolated to the rapidly expanding industrial cities of the time. Furthermore, they do not take into account the effects of the glass tax on new buildings. See, however, Thomas Piketty,

parallel with the window tax.[12] The latter may have been a more important financial consideration for speculative developers, since they would have needed to bear the cost of the glass tax upfront. Indeed, one medical report attributed windowless accommodation to the glass tax, rather than the window tax.[13] There can be no doubt that the window tax exacerbated insalubrious living conditions,[14] but it did not cause them.[15]

People flocked to Britain's industrial cities at unprecedented rates in the early nineteenth century.[16] Overcrowding and poor health outcomes were inevitable, whatever taxes might have been levied. Indeed, George Orwell observed the squalor and misery in industrial cities, such as Manchester, almost a century after the window tax had been abolished.[17] However speculative and unscientific a counterfactual exercise may be, we may ask whether, in the absence of the window tax, the urbanised working poor would have experienced similar health outcomes. The glass tax would still have applied but, far more importantly, the massive influx of people into the industrial cities ensured overcrowding and exploitation in an unchecked capitalist economy, with laissez-faire government.[18] These appalling conditions continued long after the abolition of the window and glass taxes, and, despite some slum clearance programs,[19] did not

Top Incomes in France in the Twentieth Century: Inequality and Redistribution, 1901-1998 (Seth Ackerman, trans, Harvard University Press, 2018) 499 on the disproportionate increase in the number of doors and windows relative to the increase in the French population during the nineteenth century when a doors and windows tax operated.

12 See Hugh Tait, *Five Thousand Years of Glass* (British Museum, 1991) 186.

13 See '*The Duty on Glass*' (22 February 1845) 1(112) *Lancet* 214-5, doi:10.1016/s0140-6736(02)70996-3. While the absence of fresh air and sunlight is obviously unhealthy, some medical reports of the time misunderstood the aetiology of diseases associated with overcrowding. Cholera, eg, was thought be transmitted by miasma (bad smells), rather than infected water. See Ajesh Kannadan, 'History of the Miasma Theory of Disease', (2018) 16 *ESSAI* doi: <https://dc.cod.edu/essai/vol16/iss1/18>.

14 See Commissioners for Inquiry into the State of Large Towns and Populous Districts, *First and Second Reports of the Commissioners for Inquiry into the State of Large Towns and Populous Districts, vol 2 Part 2* (William Clowes & Sons, 1845) 201.

15 Large, existing houses with many windows may have been subdivided into cramped accommodation for multiple families. Since the tax was calculated per building, its impact would have been felt disproportionately by these poor tenants. This is likely to have led to blocking up of windows by landlords seeking to reduce overheads.

16 See eg, Romola J Davenport, 'Urbanization and mortality in Britain, c. 1800–50' (2020) 73(2) *Economic History Review* 455.

17 See George Orwell, *The Road to Wigan Pier* (Victor Gollancz, 1937). On the squalid conditions of Manchester of the 1840s, see generally, Friedrich Engels, *The Condition of the Working Class in England in 1844* (Allen & Unwin, 1920).

18 In 1800, London was the only British city with a population in excess of 100,000; by 1850, there were nine. See JFC Harrison, *The Common People: A History from the Norman Conquest to the Present* (Fontana, 1984) 227.

19 See generally, Anthony S Wohl, *The Eternal Slum Housing and Social Policy in Victorian London* (Routledge, 1977). Local councils also played a major role in building decent social housing. See 'The History of Council Housing', UWE (Report, 2008) <https://fet.uwe.ac.uk/conweb/house_ages/council_housing/print.htm>. As late as 1962, there were

significantly change before the Attlee government (1945-51) sought to combat the 'Five Giant Evils' – want, disease, ignorance, squalor and idleness – as identified in the UK's Beveridge Report.[20]

Generally, my research indicates that, contrary to usual claims about, for example, the width of Amsterdam's canal-side house,[21] the impact of taxes on the built environment is secondary, minimal or mythical. The specific focus of this paper lies with adducing evidence available in Aotearoa New Zealand to identify a canard about a French doors and windows tax in Akaroa, and to fully debunk it.

The doors and windows tax (*contribution des portes et fenêtres*) was one of the French national taxes that became known as 'the four old ladies' (*les quatre vielles*) because they were essentially unchanged between 1792 and 1914. The other taxes were: the real estate tax (*contribution foncière*), the business-licence tax (*contribution des patentes*), and the personal property tax (*contribution personelle-mobilière*).[22] In the sprawling French empire, '[t]he system of taxation [was] supposed to be based largely on that of the mother country'.[23] However, according to Edwin Seligman,

> the colonial tax systems resemble those of the mother country primarily in the fact that by far the greater part of the revenue comes from indirect taxation. But so far as direct taxes are concerned the colonies differ in many respects not only from the mother country, but also from each other.[24]

And so, while *les quatre vielles* may have formed the notional basis for direct imperial taxation in broadest principle, '[of] these four taxes, *that on doors and windows is entirely lacking in the colonies*'.[25] Since Seligman wrote in 1900, it is remotely possible that the doors and windows tax had been introduced in the colonies but was discontinued or had not yet been introduced. This possibility is sufficiently unlikely to be implausible;[26] in relation to Akaroa, it is an impossibility because the settlement was never a French colony.

60,000 slum or unfit houses in Manchester, 80,000 in Liverpool, and 97,000 in Glasgow. See Andrew O'Hagan, 'At the Hunterian' (4 November 2021) 43(21) *London Review of Books* 18.

[20] See 'The Beveridge Report: "The Way to Freedom from Want"', *National Archives* (Report, 1942) <https://www.nationalarchives.gov.uk/pathways/citizenship/brave_new_world/transcripts/freedom.htm>.

[21] See eg, Keen and Slemrod (n 1) 201.

[22] See Piketty (n 11) 228-9.

[23] See Edwin RA Seligman, 'The French Colonial Fiscal System' (1900) 3(1) *Publications of the American Economic Association* 21, 29.

[24] Ibid.

[25] Ibid (emphasis added).

[26] With the notable exception of Algiers (1830), French colonial expansion generally took place from the 1880s. The infrastructure simply did not exist in most colonial outposts to justify a doors and window tax until the twentieth century. Because of its mix of indigenous people and French settlers, with concomitant specific taxes being levied on a cultural basis, it is reasonable to assume that a doors and windows tax was never raised in Algiers. See ibid, 31.

III THE MYTH OF THE AKAROA DOORS AND WINDOW TAX

Kāi Tahu, the most populous southern *iwi*,[27] have occupied Te Waipounamu (the South Island) for some 800 years,[28] although population density has always been far lower than that of Te Ika a Māui (the North Island).[29] Nevertheless, according to Louis Vangioni, Akaroa 'was once the home of hundreds of Maoris [but] … When the French settlers arrived [in 1840] their numbers [Māori] had been terribly reduced, first by the horrible Kai huanga feud, [30] and finally by Te Rauparaha's raids'.[31]

George Hempelman, a whaler of German origin, was one of first Europeans to establish a permanent presence on Banks Peninsula (Horomaka). Hempelman claimed to have bought almost the entire the peninsula from certain Māori chiefs in 1837, and, indeed, pursued this claim until his death in 1880.[32] In 1838, another whaler, the French captain Jean-François Langlois, purportedly bought the peninsula for Fr1000 (£40) from chiefs living around Ōhinehou (later Port Cooper and, now, Lyttleton). He paid a deposit of Fr150 (£6) in kind (one woollen overcoat, six pairs of cloth trousers, 12 oilskin hats, two pairs of shoes, a pistol, two red woollen shirts and one oilskin coat).[33] Rather than occupy the land, Langlois returned to France to raise finance, which was achieved through the formation of the Nanto-Bordelaise Company, a firm akin to the London-based New Zealand Company.

Kāi Tahu did not acknowledge Langlois's deed, which was written in French. Whatever the deed purported, it was not perfected.[34] The Nanto-Bordelaise Company recognised that Langlois's failure to complete the hypothetical purchase of the peninsula by occupation, and sent him back to acquire new deeds,[35] accompanied by settlers to occupy the land. The first European settlers arrived in 1840, under the protection and control of

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[27] It is usual to refer to the three southern *iwi* (Waitaha, Kāti Mamoe and Kāi Tahu) as 'Kāi Tahu whānui'. See 'Tāngata Whenua', *Otago Museum* (Pamphlet).

[28] See 'Ngāi Tahu – the iwi', *Ngāi Tahu* (Web Page, 1997) <https://ngaitahu.iwi.nz/ngai-tahu/>.

[29] See LDB Heenan, 'The Changing South Island Maori Population' (1996) 22(2) *New Zealand Geographer* 125.

[30] See 'Waikākahi', *Christchurch City Libraries* (Web Page, 2021) <https://my.christchurchcitylibraries.com/ti-kouka-whenua/waikakahi/>.

[31] Vangioni (n 8) 2. On Te Rauparaha, see 'Te Rauparaha', *Christchurch City Libraries* (Web Page, 2021) <https://my.christchurchcitylibraries.com/ti-kouka-whenua/te-rauparaha/>.

[32] See 'No. 3. – George Hempelman and his Purchase of Akaroa' in Jacobson (n 8) 55-71.

[33] Peter Tremewan, *French Akaroa* (University of Canterbury Press, 1990) 7. See also Peter Tremewan, 'Kai Tahu Land Sales to Captain Langlois and the Nanto-Bordelaise Company on Banks Peninsula WAI 27 doc T3', *Ministry of Justice* (Web Page, May 1989) <https://forms.justice.govt.nz/search/Documents/WT/wt_DOC_94788171/Wai%2027%2C%20T003.pdf>.

[34] 'The Ngai Tahu Ancillary Claims Report 1995', *Waitangi Tribunal* (Report, 1995) 96 <https://ngaitahu.iwi.nz/wp-content/uploads/2018/04/LandReport.pdf>.

[35] See Peter Tremewan, 'The French Alternative to the Treaty of Waitangi' (1992) 26(1) *New Zealand Journal of History* 99, 100.

the French Navy in the form of the corvette *L'Aube*, captained by Charles Lavaud.[36] The reported number of French settlers varies – it is usually stated to be 53. Additionally, six (or sometimes 12) German settlers came with them. Once they realised that less land was available for settlement than had been promised, the French persuaded the Germans to settle at nearby Takamatua, which was promptly renamed German Bay, before reverting to its indigenous name during World War 1.

Conway evidently presumes that a doors and windows tax was levied in Akaroa. She argues '[s]imilar tax avoidance behaviors [blocking up of windows and doors] were observed in France as those observed in England.'[37] It is reasonable to assume that some avoidance occurred, although Thomas Piketty observes that, between 1822 and 1876, the number of taxable doors and windows in France increased by 80 percent, despite a population growth of only 20 percent.[38] It is, however, difficult to convey how different the architecture of Europe was from much of that of the nascent colony in New Zealand. An American visitor to Akaroa in 1845, for example, described various houses as 'not as good as a New England hogpen', 'a hut no better than a coal pit' and 'a farmhouse [that] would vie in elegance with a New England coal pit hut'.[39] The idea that a doors and windows tax might be applied to these humble shelters is fanciful. Such a tax requires a critical density of buildings that actually incorporate doors and windows.

Before the 1850s, much of New Zealand's settler architecture was provisional and housing was often similar to poor rural shelter in Britain.[40] Furthermore, construction of many early European homes was commonly dependent on *mātauranga* (knowledge) Māori, in particular, building knowledge and skills. Peter Tremewan describes Tripe's hut as being:

> made up of a number of wooden posts, which supported walls made from a lattice-work of bamboo (probably toitoi) and a roof of rushes (wiwi). It had no windows and only a small door that they had to crawl through. Furniture was limited to matting beds. This sounds very much like a Maori whare [house] and may be explained by the fact that they had with them a Maori convert from the North Island.[41]

Despite the differences between early settler shelter in New Zealand and European urban buildings, Conway recounts the story of 'a missionary in the French colony of Akaroa … [who] would climb in and out of his 'home' on his hands and knees in an attempt to minimize the size of windows and doors.'[42] Setting to one side the logical fallacy that

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[36] See 'Lavaud, Charles Francois' in AH McLintock (ed), *An Encyclopaedia of New Zealand* (1966) Te Ara – the Encyclopedia of New Zealand (Web Page) <http://www.TeAra.govt.nz/en/1966/lavaud-charles-francois>.

[37] See Conway (n 1) 181.

[38] See Piketty (n 11) 499.

[39] Quoted by Tremewan, *French Akaroa* (n 33) 197.

[40] Early settler dwellings were commonly made from wattle and daub or cob construction with rush thatch roofs made from *raupō* (reeds). See Geoff Mew and Adrian Humphris, *Raupo to Deco: Wellington Styles and Architects 1840-1940* (Steele Roberts, 2014) 25.

[41] See Tremewan, *French Akaroa* (n 33) 139.

[42] See Conway (n 1) 181.

climbing in and out on his hands and knees might reduce the size of the windows and doors, Jean-André Tripe,[43] the Marist missionary in question, was clearly joking. Conway relies on Thomas Buick's 1928 history of Akaroa.[44] Buick wrote of the missionary's basic shelter 'to avoid the door and window tax' is *his droll explanation* of the fact that it had but one opening for entrance and exit, through which he was compelled to crawl on his hands and knees.'[45]

French investors may have sponsored the Akaroa settlement, and the French navy may have partly policed it but France did not gain sovereignty over a single square foot of New Zealand territory. Having signed Te Tiriti o Waitangi (the Treaty of Waitangi) with numerous Māori *rangatira* (chiefs) starting on 6 January 1840, Britain claimed the entire New Zealand archipelago before the Lavaud-led mission arrived in New Zealand.[46] Under customary international law,[47] all of New Zealand was, then, a British colony.[48] British annexation of the territory may have been hastened by fears of the French claiming sovereignty over the South Island,[49] but such a claim was never made and the French did not openly dispute British sovereignty.

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43 Tripe arrived in Akaroa 1840 to pursue what was clearly 'a difficult mission' and left frustrated in 1842. See 'New Zealand Marist History', *Society of Mary New Zealand* (Web Page) <https://www.sm.org.nz/about/nz-province/new-zealand-marist-history/>.

44 See T Lindsay Buick, *The French at Akaroa: An Adventure in Colonization 1866-1938* (Board of Māori Ethnological Research, 1928).

45 Ibid 151 (emphasis added).

46 When Lavaud arrived at Akaroa, he discovered a police magistrate's court had been established. See Tremewan (n 33) 97. Indicating the *entente cordiale* that prevailed in Akaroa, Charles Barrington Robertson, the magistrate, shared a house with the impressively named Pierre Joseph Sainte-Croix Croquet de Belligny, the Nanto-Bordelaise Company's representative. See ibid 151.

47 In European conceptions, sovereignty could be gained by conquest or cession. See Lord Lugard, 'The Basis of the Claim for Colonies' (1936) 15(1) *International Affairs* 3, 3. In this scheme, the Treaty of Waitangi was an act of cession. While *rangatira* at Waitangi and elsewhere, most likely accepted the British Crown's exclusive right to police Europeans in the territory, it is generally believed that they did not cede something like Westphalian sovereignty. See generally, Claudia Orange, *The Treaty of Waitangi* (Bridget Williams Books, 2nd ed, 2003).

48 For a discussion of the different proposals for colonisation, see generally, Tremewan, 'The French Alternative to the Treaty of Waitangi' (n 35). Tremewan counterfactually asks: 'Would the Banks Peninsula and South Island Maori have been better off if the French rather than the British had succeeded in imposing colonial rule on the South Island?' Dave Armstrong's stage play *Le Sud,* used the idea of a francophone South Island to critique Anglo values. See eg, Thomson, Rebecca, 'South Island colonised by French? Quelle horreur!' *The Wellingtonian* (online, 19 August 2009) <https://www.stuff.co.nz/dominion-post/news/local-papers/the-wellingtonian/2699797/South-Island-colonised-by-French-Quelle-horreur>. Perhaps, New Caledonia can provide an indication of how a French-ruled Te Waipounamu might look like today – an overseas department, struggling with the question of independence. See eg, 'France keeps New Caledonia independence referendum on track' *RNZ* (Web Page, 3 November 2021) <https://www.rnz.co.nz/international/pacific-news/454873/france-keeps-new-caledonia-independence-referendum-on-track>.

49 While this explanation may seem believable, its veracity is questionable. See eg, Tremewan, *French Akaroa* (n 33) xvi, n 4. Concerns about French colonisation may, however, had prompted some of the Māori chiefs to sign a treaty with the British Crown. See Dame Claudia Orange, "'This Country Is Ours.

The French were, however, permitted to exercise a degree of autonomy in Akaroa between 1840 and 1845, notably to ensure order among the French settlers and visiting French whalers.[50] Lavaud used fines imposed on French settlers convicted of selling liquor illegally to fund public works projects,[51] but these fines cannot be seen as taxes in a normal understanding. Generally, it is implausible to think that the licence granted to Lavaud to police the Francophone settlers and whalers might have extended to French taxes being levied in sovereign British territory.

In 1840, Britain annexed a territory larger than the mother country in which Europeans were massively outnumbered by Māori.[52] In the early years of the colony, *tikanga* Māori (crudely translated as customary practices) applied in non-urban areas and remains part of the New Zealand common law, subject to the meeting of certain criteria.[53] In this context of nominal control but limited practical ability to effectuate power, it is understandable that the colonial government should allow the French navy to temporarily exercise discipline over the French in Akaroa. This paradigm manifestation of pragmatism was greatly attributable to the relationships Lavaud established, firstly, with Lieutenant-Governor Hobson,[54] and, then with the local police magistrates.[55] During this period, Lavaud neither claimed nor denied French sovereignty over the territory, and the British, in Nelsonian fashion, appear to have turned a blind eye to what could have

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We Are the Governor'" *The Dominion Post* (Wellington, 4 February 2021) 17. Orange does not explain why Māori might have preferred British to French intervention. However, it is possible that the sanguinary encounter between Marion du Fresne's French expedition and Māori in the Bay of Islands in 1772 was relevant. See 'Marion du Fresne arrives in Bay of Islands', *Ministry of Culture and Heritage* (Web Page, 6 November 2020) <https://nzhistory.govt.nz/marion-du-fresne-arrives-in-the-bay-of-islands>.

[50] According to Tremewan, *French Akaroa* (n 33) xix, 'French people were judged by a French court of justice and French bylaws were enforced'. However, the law was administered by officers of the French navy (ibid 206). And so, it is not certain that French law was applied to the letter – the administrators were, after all, sailors, not lawyers – or whether discipline was applied in a pragmatic way to ensure order in the Francophone part of the settlement.

[51] See ibid 212. Tremewen does not record the amount of the fines.

[52] In 1840, the 80,000 Māori population outnumbered non-Māori in a ratio of 40 to 1. By 1850, numbers for the two groups were roughly equal. In 1901, the Māori population had fallen to 46,000 and the number of non-Māori had increased to 770,000. See Claudia Orange, 'Treaty of Waitangi – Dishonouring the treaty – 1860 to 1880', *Te Ara – the Encyclopedia of New Zealand* (Web Page) <http://www.TeAra.govt.nz/en/graph/36364/maori-and-european-population-numbers-1840-1881>.

[53] See Sir Geoffrey Palmer, *Law – Legal history*, *Te Ara – the Encyclopedia of New Zealand* (Web Page) <http://www.TeAra.govt.nz/en/law/page-1>.

[54] According to rumour, Lavaud became enamoured with Eliza Hobson, the Lieutenant-Governor's wife and therefore lingered in the Bay of Islands as their guest longer than he might. See Tremewan, 'The French Alternative to the Treaty of Waitangi' (n 35) 95. The story that France lost the opportunity to claim sovereignty over Te Waipounamu because of Lavaud's *amour fou* for Eliza Hobson is worthy of Guy de Maupassant. Unfortunately for myth-peddlers, Lavaud had already resigned himself to British sovereignty claims before he met the Hobsons.

[55] See ibid 206-21.

become a cause for belligerence. In 1845, however, Willoughby Shortland, Hobson's gubernatorial successor, unequivocally asserted British sovereignty over all of New Zealand from the time of the Treaty of Waitangi. The French navy departed, leaving the French settlers to unequivocal British control. Many of the Akaroa settlers promptly naturalised as British citizens.[56]

Notwithstanding the brief period of cooperative policing, there is no evidence of the formation and maintenance of a civil law enclave within a common law country, akin to Louisiana or Québec;[57] rather, the colonial government allowed French naval officers to maintain order over a small number of their fellow countrymen in an embryonic British colony. The *English Laws Act 1858* (NZ) declared that the Laws of England 'so far as applicable to the circumstances of the Colony' had been in force since 14 January 1840. No traces of French law can be found in New Zealand law, including tax laws, as a consequence of the Akaroa settlement.

Between 1833 and 1840, New Zealand was administered as a dependency of New South Wales, a British colony. Consequently, imports, notably alcohol and sugar, were taxable under British legislation.[58] The *Customs Act 1841* (NZ) introduced New Zealand's first taxes,[59] and, until the 1860s, customs duties were the only national taxes.[60] Local property taxes (rates) were also raised to fund infrastructure in new settlements, but the national tax base only expanded to include stamp duties[61] in order to fund colonial belligerence against Māori.[62] The British did not levy a window tax in New Zealand; indeed, the lack of windows in many pre-1850 settlements would have rendered such a tax pointless.

In June 1849, the New Zealand Company bought the Nanto-Bordelaise Company's interests in Banks Peninsula for £4,500. *An Encyclopedia of New Zealand* reported in 1966 '[t]oday, apart from a few French street names, there remains little to show Akaroa's origin as a French settlement'. Rue Lavaud is one of the surviving names. These remnants (or new names) may have tourist value, but few truly French buildings exist or, indeed, were ever built in Akaroa. According to Christchurch City Council:

> The fact that Akaroa was founded by settlers sent out by a French colonising company has misled some into thinking that Akaroa today has a French character. But the 19th

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56 See eg, the schedule to the *Naturalization Act 1853* (NZ). More German than French family names appear in the schedules to the naturalisation Acts.

57 See eg, Thomas E Carbonneau, 'Survival of Civil Law in North America: The Case of Louisiana' (1992) 84 *Law Librarians Journal* 171.

58 See *Customs Act 1833* (UK).

59 A Sub-Collector of Customs was appointed for Akaroa in February 1843. This appointment represented a direct challenge to French control over its nationals in or visiting the settlement. However, in the prevailing spirit of cooperation and avoidance of conflict, 'there is no record of any French ship being fined and certainly none was seized'. See Tremewan, *French Akaroa* (n 33) 216-7.

60 See also *Customs Act 1846* (NZ) and *Customs Act 1858* (NZ).

61 See *Stamp Duties Act 1866* (NZ).

62 See Paul Goldsmith, 'Taxes – Taxation – 1840 to the 1880s', *Te Ara - the Encyclopedia of New Zealand* (11 March 2010) <http://www.TeAra.govt.nz/en/taxes/page-1>.

and early 20th century buildings that set Akaroa's character are of a "Colonial Vernacular" style that owes more to British than to French precedents.[63]

IV REFLECTIONS

Conway's response to Tripe's joke indicates a predisposition to presuming a power of taxes to determine the design of buildings, notwithstanding a wealth of evidence that either contradicts or minimises that power. She is not alone, however, in her apparent lack of appropriate scepticism in the face of appealing anecdote. Ole Rekdal observes:

> Many of the messages presented in respectable scientific publications are, in fact, based on various forms of rumors. Some of these rumors appear so frequently, and in such complex, colorful, and entertaining ways that we can think of them as academic urban legends. The explanation for this phenomenon is usually that authors have lazily, sloppily, or fraudulently employed sources, and peer reviewers and editors have not discovered these weaknesses in the manuscripts during evaluation.[64]

Rekdal adds:

> The digital revolution has provided us with marvelous weapons for exposing and cutting down the prevalence rates of rumors and urban legends in academia. The problem is that the same devices can also be used for other purposes, such as contributing to … the 'Lazy author syndrome': throwing a few keywords into a database to come up with an impressive list of references which at first glance cannot easily be exposed as secondary, irrelevant, unreliable, or sources not even read by the author.[65]

In the neoliberal university,[66] researchers have become 'publish or perish entrepreneurs' who may be tempted to cut corners to promote their careers.[67] Nevertheless, reliance on insubstantial, if ostensibly attractive sources, is much older than the neoliberal university and digital technology. As people, we tend to believe the narratives that are most compelling to us, whether they are told by Gospellists or online influencers. As the popular historian Yuval Noah Harari observes, '[t]he truly unique trait of *Sapiens* is our ability to

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[63] John Wilson and Louise Beaumont, 'A Report Prepared for: Keri Davis-Miller Planner, City Plan Team Christchurch City Council', *Christchurch City Council* (Report, June 2009) 5 <https://ccc.govt.nz/assets/Documents/The-Council/Plans-Strategies-Policies-Bylaws/Plans/district-plan/banks-peninsula/AkaroaHistoricalOverview-part-1.pdf>.

[64] See Ole Bjørn Rekdal, 'Academic urban legends' (2014) 44(4) *Social Studies of Science* 638, 638.

[65] See ibid 651.

[66] On the features of the neoliberal university, see eg, Sheila Slaughter and Gary Rhoades, 'The Neo-Liberal University' (2000) 6 *New Labor Forum* 73.

[67] See Mark Bauerlein, Mohamed Gad-el-Hak, Wayne Grody, Bill McKelvey and Stanley W Trimble, 'We Must Stop the Avalanche of Low-Quality Research', *The Chronicle of Higher Education* (13 June 2010) <https://www.chronicle.com/article/we-must-stop-the-avalanche-of-low-quality-research/>.

create and believe fiction. All other animals use their communication system to describe reality. We use our communication system to create new realities'.[68]

'Maslow's hammer' refers to the cognitive bias we have towards the familiar, and so, to the person with a hammer, every problem presents as a nail.[69] Perhaps, for some tax specialists, every social problem can be remedied by a tax. Conversely, when a tax is present in a social context, it may be presumed to be the principal determinant of human behaviour. Oates and Schwab, for example, are plausible in arguing that the window tax caused bunching,[70] but their sample of a small provincial town does not necessarily reflect the national experience of the tax, particularly in the great industrial cities. Furthermore, their study does not take into account the potential influence of the glass tax or the massive migration into the metropoles. Less rigorous research than theirs repeats myths without critical scrutiny or insight.

This part of the article identifies certain ways in which research into tax and the built environment is inadequate.

A *Missing or Circular Evidence*

In the 1962 edition of an occupational health and diseases text, Donald Hunter observes '[t]he *window tax* … still served to discourage proper lighting and ventilation' so that architects were 'naturally encouraged' to design structures with as few windows as possible.[71] Hunter does not provide evidence to support his claim. Certainly, carpenters and bricklayers would have been engaged to block up windows but were architects really involved in designing new structures with fewer windows for tax avoidance purposes? Relevant evidence is not readily available; nevertheless, Kenneth Clute relies on Hunter to support his statements about the window tax.[72] Andrew Glantz then uses Clute to support his assertion that 'recent discourse on the unintended adverse side effects legislation can pose on health point to the Window Tax as an example with terrible consequences'.[73] Both Keen and Slemrod, and Oates and Wallace rely on Glantz to support

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68 Interview with Arik Gabbai, 'What Makes Humans Different? Fiction and Cooperation' *Smithsonian Magazine* (online, February 2015) <https://www.smithsonianmag.com/arts-culture/what-makes-humans-different-fiction-and-cooperation-180953986/>.

69 See 'Maslow's hammer in integrative medicine: one size will never fit all' (2020) 7(3) *Advances in Integrative Medicine* 119 doi:10.1016/j.aimed.2020.07.002.

70 See generally, Oates and Schwab (n 11).

71 See Donald Hunter, *The Diseases of Occupations* (Little, Brown, 3rd ed, 1962) 87. The current edition of the text does not refer to the window tax. Hunter places the window tax in the context of massive and rapid urbanisation, but does not mention the glass tax which, to reiterate, would have presented significant upfront costs for speculative developers.

72 See Kenneth F Clute, 'Law and Health: Some Current Challenges' (1972) 50(1) *Milbank Quarterly* 7, 27.

73 See Andrew E Glantz, 'A Tax on Light and Air: Impact of the Window Duty on Tax Administration and Architecture, 1696-1851' (2008) 15(2) *Penn History Review* 18, 33-4. Glantz's analysis is thorough and generally plausible; it is also particularly indebted to Stephen Dowell, *A History of Taxation and Taxes in England: from the Earliest Times to the Present Day* (Vol. 3, 1884) and WR Ward, *The Administration of the Window and Assessed Taxes, 1696-1798* 67(265) *English Historical Review* 522 (1952).

certain of their statements about the window tax. It is not submitted that the evidence is false but it follows a chain that is not reliably anchored in unimpeachable evidence.

Mansard roofs are recessive roofs that are punctuated by windows. Although design of the mansard roof is usually attributed to François Mansart (1598-1666), it was probably first used by Pierre Lescot (c1500-1570) as a French response to Italian Renaissance Classicism.[74] Despite its French origins, the mansard roof has become ubiquitous, and for good reasons. Restrictions have long been imposed on the height of the walls of urban buildings, first for utilitarian reasons (at a time before lifts), second to promote hygiene (access to sunshine for other buildings and the streets), and third for aesthetic reasons.[75] The mansard roof permits compliance with each of these requirements. While utilitarian reasons became less relevant after the invention of the lift, access to light became more pressing with the emergence of technology that allowed taller buildings.[76] Along with their aesthetic appeal, their amenability to planning ordinances explains why mansard roofs are so common.

Evidence is persuasive that mansard roofs became popular in France because they suited ordinances restricting the height of buildings.[77] Social goals, such as restricting the height of buildings need to be mandatory. If wealthy people have the opportunity to choose to pay a tax in order to build higher, such social objectives can be rendered nugatory.[78] Nevertheless, some commentators insist that the French restrictions on building height were imposed through taxes, and the mansard roof was a tax avoidance scheme.

According to Conway, '[d]uring the reign of Napoleon, French property taxes were partially based on the number of floors a property has. The number of floors is counted based on all floors below the roofline (hence the name "roof tax").'[79] There is, however,

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[74] See 'Lescot, Pierre (c.1500/10–78) French Architect' in James Stevens Curl and Susan Wilson (eds), *A Dictionary of Architecture and Landscape Architecture* (online, 3rd ed, 2015) <https://www-oxfordreference-com.helicon.vuw.ac.nz/view/10.1093/acref/9780198606789.001.0001/acref-9780198606789-e-3318?rskey=GgGM4m&result=1>.

[75] See Robert Anderson Pope, 'A Discussion of the Controlling Principles of Building Height Limitations for Great Cities' (1915) 6(2) *Town Planning Review* 125, 133.

[76] See eg, the mansard roofs of many buildings around Central Park in New York.

[77] According to Simon Texier, an ordinance of 1667 limited the height of apartment blocks to 48 feet (14.63 metres) – measured to the cornice; from 1784, this limit was increased to 54 feet (17.54 metres). See Simon Texier, *Paris Panorama de l'Architecture de l'Antiquité à Nos Jours* (Parigrame, 2012) 66. A fifth floor could therefore be accommodated, while complying with the height limit. Ibid, 80.

[78] For example, the Chinese government has imposed a restriction on skyscraper height. See eg, Sandy Li, 'China bans super skyscrapers, putting a ceiling over new buildings that exceed 500 metres, citing safety concerns', *South China Morning Post* (online, 7 July 2021) <https://www.scmp.com/business/article/3140178/china-bans-super-skyscrapers-putting-ceiling-over-new-buildings-exceed-500>. Such a restriction could not be achieved through a plausible tax. The buildings affected tended to be billionaires' vanity projects. Demonstrating that they could incur a tax and still build higher would have enhanced their status further.

[79] See Conway (n 1) 183 (footnote omitted). Conway cites Richard V Francaviglia, *Main Street Revisited: Time, Space, and Image Building in Small-Town America* (University of Iowa Press, 1996) 28 in support

no obvious evidence that such a roof tax was ever levied in France.[80] Conway cites an article by Karen Powell.[81] But Powell's statement about the existence of a roof tax is unreliable.[82] Her cited authority for the possible existence of the elusive tax is a 'toolkit' written by David Robinson. Without providing any supporting evidence, Robinson states '[t]he tax-evading Mansard roof is perfect example of the way the property tax system can affect the behaviour of builders and the look of cities'.[83] Akin to buildings without foundations, researchers here have structured arguments that have no evidential basis.

The real estate tax (*contribution foncière*) was based on the estimated rental value of land and buildings.[84] The number of floors would have been one factor in estimating rental value but location, for example, would have been a far more important determinant of notional rental value.[85]

B *The Distorting Lens of the Present*

We have a tendency to view historical arrangements through the distorting lens of the present. Two examples of this distortion are the way we form presumptions about the window tax from existing buildings, and another the exaggeration of French influence in New Zealand.

1 *Existing Buildings*

Contemporary discussions of the window tax often include a photograph of a particular building with occluded windows to prove the folly of the window tax.[86] In reality, the buildings with blocked-up windows that exacerbated the misery of the urban poor have long gone, removed either through slum clearance or the Blitz. The handsome residence in the ubiquitous photograph is the last building of a Classical Revival terrace that was clearly built for the fashionable and wealthy of Southampton; that explains its longevity.

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of her argument. But Francaviglia provides no evidence of a tax and besides is most interested in the aesthetics of the mansard roof.

80 Texier makes no mention of property taxes influencing the design of apartments in Paris at any time. Jean-Édouard Colliard and Claire Montialoux do not include a roof tax in their brief history of French taxation but do, of course, refer to the real estate tax (*contribution foncière*). See Jean-Édouard Colliard and Claire Montialoux, *Une brève histoire de l'impôt* (2007) 1(1) *Regards croisés sur l'économie* 56 doi: 10.3917/rce.001.0056.

81 See Karen E Powell, *A Historical Perspective on Montanan Property Tax: 25 Years of Statewide Appraisal and Appeal Practice* (2009) 70 *Montana Law Review* 21, 23.

82 See ibid, 23, nn 14 and 15.

83 See David Robinson, *The Councilor's Toolkit #4*, *Laurentian University* (Web Page, 12 April 2004) <http://inord.laurentian.ca/4_04/Councillors%20Toolkit%204b.htm>.

84 See Piketty (n 11) 228-9.

85 See eg, Rotimi Boluwatife Abidoye and Albert PC Chan, 'Critical determinants of residential property value: professionals' perspective' (2016) 14(3) *Journal of Facilities Management* 283.

86 See eg, Madsen Pirie, 'The Window Tax', *Adam Smith Institute* (Blog Post, 24 July 2019) <https://www.adamsmith.org/blog/the-window-tax>. Ironically, Adam Smith broadly approved of the window tax, subject to a critique of inequitable treatment of rural and urban properties. See Adam Smith, *An Inquiry into the Wealth of Nations* (Encyclopaedia Britannica, 1952) 361-2.

Why does it have blocked-up windows? Being at the end of the terrace, it could be for security reasons. Blank windows are a common architectural feature, used to promote symmetry, particularly in the neo-Classical style that dominated civic buildings and the private dwellings of the wealthy in the nineteenth century. Blank windows may also hide staircases or partition walls. Many explanations can be adduced for blank windows in the houses of the nineteenth century wealthy, which may have more recently been converted into commercial premises or divided into apartments, but the window tax presents as the least likely explanation for occluded windows in buildings, such as those of the Southampton terrace. It is pertinent to consider why, 170 years after the abolition of the window tax, the owners of such a landmark building have not restored or introduced glass.

Many buildings designed and constructed after the window tax was repealed may include blank windows. This fact may lend itself to myth-making. Creating 'proof' of a mythical New Zealand window tax could be constructed on the following lines. Since the *English Laws Act 1858* (NZ) provided that English statutes applied in New Zealand from 1840, and the window tax was not repealed until 1851, it may be concluded that the window tax applied in New Zealand between 1840 and 1851. Photographs of bricked-up windows of old buildings in central Dunedin provides 'evidence' of the existence of the New Zealand window tax. In fact, the photographs only prove that some windows in Dunedin, which was not founded until 1848, have been bricked-up. No window tax was levied in early colonial New Zealand; such as tax would have been pointless until a critical mass of European-style buildings had been built.

2 *French Influence in New Zealand*

Far fewer French settlers came to colonial New Zealand than German immigrants. For example, in 1842, invited by the New Zealand Company and sponsored by Count Ranzau of Mecklenburg, 140 Germans immigrated to the Nelson region, and were joined by a further 200 in 1844. In 1886, there were more than 5000 German settlers in New Zealand. Indeed, 'Germans were the largest continental European ethnic group to settle in New Zealand before 1914. They made a transitory contribution to the early cultural landscape … with their steep roofed Lutheran churches … However, they soon adopted the way of other pioneer farmers'.[87] Following anti-German sentiment during World War I, 'the rural Germans and their descendants became "submerged groups", absorbed in language, dress, and occupation'.[88] Because of this submersion, today, we typically overlook the not insignificant German immigration to New Zealand.

Although a handful of churches with distinctive Lutheran steeples still exist or have been replicated, fire is an effective eraser of New Zealand's wooden buildings that might otherwise provide markers of culture. What is the relevance of German immigration to this article? Without familiarity with Moutere in the Nelson region, one is unlikely to appreciate that Germans, after Anglo-Celts, were the most significant European settlers in

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[87] See IH Burnley, 'German Immigration and Settlement in New Zealand 1842-1914' (1973) 29(1) *New Zealand Geographer* 45, 62.

[88] See ibid.

post-Treaty New Zealand. In contrast, the tiny French settlement at Akaroa, which could only plausibly be described as a 'French village' between 1840 and 1845 attracts disproportionate attention, partly because of the advertising puff of property developers and tourism promoters. In this regard, the Christchurch City Council notes:

> although most overseas visitors to Akaroa continue to see it as a delightful place with a special, distinctive character, few of them accept the claim still made ignorantly by some locals that it is a French village. In a *Lonely Planet* guide we read that while Akaroa is undeniably a picturesque place "the Gallic pretence can sometimes be a tad forced". A writer in the *Guardian* noted in 2005 that "[i]t soon becomes clear that any direct French influence on Akaroa ended long ago.[89]

Perhaps 'fake news' about a non-existent tax is appropriate for much mythologised Akaroa.

V CONCLUSION

This article has focused on a particular fallacious proposition published in a prestigious US tax journal but has far broader application to tax and the built environment, indeed to academic research in general. A sceptical analysis of the claim that the French doors and windows tax applied in Akaroa demonstrates that the claim has no foundation. The missionary Tripe made a joke about his humble accommodation. A doors and windows tax would have needed a considerable number of European-style buildings to be viable. This explains why the French did not levy such a tax in their colonies. Even if they had, Akaroa was never a French colony. In short, Ngā Iwi Wīwī no more introduced a doors and windows tax to Akaroa than they did the guillotine.

[89] 'Akaroa Heritage Overview: Section 7 Change and Growth 1950 to 2009' (Report) *Christchurch City Council* 158 <https://www.ccc.govt.nz/assets/Documents/The-Council/Plans-Strategies-Policies-Bylaws/Plans/district-plan/banks-peninsula/AkaroaHistoricalOverview-part-2.pdf>.

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ENTERING A NEW ERA: TIME FOR A HOLISTIC REVIEW AND REVAMP OF THE TAX SYSTEM IN HONG KONG?

WILSON CHOW*

ABSTRACT

Its simple and low-rate tax system has helped Hong Kong to become a flourishing economy in the world post World War II and to get through challenges and crises over the last two decades. This article argues, however, that the time has come with forces from within and outside, locally, regionally and internationally, economically, socially and politically, individually and collectively, testing Hong Kong's not-yet-broken tax system to its limits and calls for a timely and research-informed, comprehensive and substantive review and reform to be applied to the regime.

Keywords*:* Tax policy, tax system, review and reform, Hong Kong

I INTRODUCTION

Once aptly described as the 'Jurassic Park in the Pearl River Delta',[1] the simple and low-rate tax system in Hong Kong has also been said to be 'troublingly successful'.[2] The Hong Kong income tax system as we know it today dates from the 1940s when the *Inland Revenue Ordinance* cap 112 (Hong Kong) ('*IRO*'), the key and only income tax law even for now in Hong Kong, was first enacted on 3 May 1947 with its origin from the *War Revenue Ordinance 1940* (Hong Kong).[3] It has helped Hong Kong to become a flourishing economy in the post-WWII world.[4] Based upon and contained within a common law tradition and framework, the system is still running well; but its unreformed age is showing. Since 1997 it has operated within a Special Administrative Region of the People's Republic of China ('PRC'), the latter being a civil law jurisdiction.

The system has endured and come through such challenges as the global financial crisis and the severe acute respiratory syndrome ('SARS') over the last two decades, with no comprehensive and substantive reforms having been applied to the regime itself since it was established. However, the local economic and social conditions underlying its original

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1 Andrew Halkyard, 'The Hong Kong Tax Paradox or Why Jurassic Park Exists in the Pearl River Delta' (1998) 8 *Revenue Law Journal* 1.

2 Michael Littlewood, *Taxation without Representation: The History of Hong Kong's Troubling Successful Tax System* (Hong Kong University Press, 2010).

3 See ibid 5.

4 Ibid 2.

design have changed over the years and will continue to change. In addition, the plea for enhanced international tax cooperation, typically through the work of the Organisation for Economic Cooperation and Development ('OECD'), attributed mainly to the continuing growth of globalization, international trade and e-commerce, is growing louder. More recently the aftermath of substantial domestic social unrest with a series of events sparked off by an amendment bill regarding extradition proposed by the Hong Kong government in 2019 has amplified changes already underway in the demographics of Hong Kong, coupled with subtle twists and turns in the PRC's approach towards Hong Kong and the unprecedented public health risks associated with COVID-19. These factors have had, and will continue to have, an impact on the economy and society in Hong Kong, as well as regionally and internationally. In essence, they are testing Hong Kong's not-yet-broken tax system to its limits. The call for timely and research-informed responses to review, reform and develop a tax system that will address the domestic challenges and be more convergent with, rather than isolated and divergent from, the PRC and other international counterparts, has been intensifying.[5]

Part II of this article gives an account of the tax system in Hong Kong and the legislative changes made to it over the last decade.[6] Part III and IV, with respective references to local, regional and international contexts, put forth arguments for a timely and holistic review of the system to prepare for and meet the challenges for a new era from now to and beyond 2047, the initial 'expiry' (or primary review) date of the innovative 'one-country, two systems' regime.[7] This article will conclude, in Part V, by sketching out the way forward for a modernised and more 'fit-for-purpose' system. It would be better, as an ancient unattributed quote says, 'have not thy cloak to make when it begins to rain'!

II THE HONG KONG TAX SYSTEM

A *The 'troublingly successful' 'Jurassic Park in the Pearl River Delta'*

The Appendix contains a table that matches the key features of the Hong Kong tax system against a simplified tax matrix.[8] The system is best known for being 'simple' because of the following features. First, it has only one level of taxation which means that once a corporation is chargeable to tax, its after-tax profits distributed to its shareholders as dividends are not subject to tax again.[9] Second, it has only one single jurisdiction to tax and that is territorial source which means that offshore profits and income are generally

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5 See eg, YY Butt and Patrick Ho, The Changing Role of Hong Kong Taxation in Fiscal Policy in the Last Thirty Years and its Prospective Future' (2021) 25(1) *Asia-Pacific Journal of Taxation* 19; Stefano Mariani, 'Trajectories for the Development of the Inland Revenue Ordinance in Hong Kong' (2021) 25(2) *Asia-Pacific Journal of Taxation* 21, 25-31

6 See also Butt and Ho (n 5) that made a similar attempt over a longer period of time with a slightly different emphasis.

7 See Part IV A.

8 The author first encountered this as a teaching and learning tool used by Professor Andrew Halkyard at the Faculty of Law, The University of Hong Kong, more than a decade ago.

9 *Inland Revenue Ordinance* cap 112 (Hong Kong) ('*IRO*') s 26(a).

exempt from Hong Kong taxes, regardless of the domicile or residence of the person.[10] Third, it does not have any general income tax but instead, three separate and distinct taxes on: trading, business and profession income; income for the use of immovable property; and employment and office income.[11] Nevertheless, an individual having income from other than from just employment or office may elect for personal assessment by which he or she will be assessed on his or her aggregate income from various sources and enjoy favourable concessionary deductions and personal allowances as if he or she only earned employment or office income.[12] Last but not least, it does not have any indirect taxes or capital gains tax except to the extent and in the form of stamp duty, which is a duty on certain prescribed instruments for giving effect to certain transactions involving immovable property and company shares.[13] The tax base is therefore very narrow.

Apart from being 'simple', the system has relatively low tax rates. The standard rates for income taxes are set at 15% and 16.5% for individuals and corporations respectively.[14] Assessable profits from the trade, profession or business up to HK$2,000,000 (about AU$270,500) are subject to only 50% of the applicable standard rate.[15] Progressive tax rates from 2% to 17% apply to the net chargeable employment and office income,[16] subject to the maximum of having the standard rate charged on the whole of the net assessable income as reduced by allowable concessionary deductions.[17] According to the 2020-21 Annual Report of the Inland Revenue Department ('IRD') , for the year of assessment 2019-20, only 1.3% of salaries tax payers were charged at the standard rate but they contributed 35.7% of the final salaries tax assessed. Given its simplicity and low tax rates (and burden), it is not surprising that comparatively few tax incentives have been made available in Hong Kong.

Stamp duty is levied on prescribed chargeable documents, typically on the amount or value of the consideration[18] except a fixed duty of HK$5 (about AU$0.93) is payable on a duplicate of a chargeable document. [19] *Ad valorem* duty rates are generally low, notably at 0.26% on contract notes for sale and purchase of Hong Kong shares.[20] In contrast, *ad valorem* stamp duty rates on chargeable instruments on transactions involving residential

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[10] Ibid ss 5, 8 and 14.

[11] Ibid.

[12] Ibid ss 41 and 42.

[13] *Stamp Duty Ordinance* (Hong Kong) cap 117 ('*SDO*').

[14] *IRO* (n 9) schs 1 and 8.

[15] Ibid schs 8A and 8B.

[16] Ibid sch 2.

[17] Ibid s 13(2).

[18] *SDO* (n 13) sch 1.

[19] Ibid head 4.

[20] Ibid head 2(1).

immovable property in Hong Kong can be as high as at 15% [21] unless the purchaser (or transferee or assignee) is a Hong Kong permanent resident acting on his or her behalf without beneficially owning another residential property in Hong Kong.[22] If the purchaser (or transferee or assignee) of the residential property is a non-Hong Kong permanent resident, the transaction attracts an additional buyers' stamp duty at the rate of 15%.[23] A subsequent quick disposal of the residential property will be subject to the special stamp duty at a rate of 10%, 15% or 20%, depending on the length of the holding period such that a shorter period of ownership attracts a higher duty rate.[24]

Save and except perhaps with the current stamp duty regime on residential properties in Hong Kong serving its specific purposes to curb speculation in the property market and to stabilise property prices,[25] a tax system of those features listed out above is an outliner and should probably have become 'extinct' by now. The system has been, however, 'troublingly successful'.[26] It has been 'successful' as it witnessed the rise of an economy from a fishing village to an international financial centre, accumulating vast fiscal reserves despite the exceptionally light levy of taxes.[27] Such success may have been attributed to the revenue brought by premiums charged by the government for 'leasing' land to property developers (including sales of lease and lease-conversion fees), [28] as well as the relatively low public spending.[29]

Meanwhile, the success is 'troubling' because firstly, judged by axiomatic criteria, the system is considered 'grossly flawed' as being 'inherently inequitable' permitting 'avoidance and evasion of kinds' and on a 'scandalous' scale.[30] For example, with regards to the benefits in kind, a residential unit provided rent-free by the employer, only a notional benefit called "rental value" will be added to the chargeable income of the employee, such rental value being calculated at 10% of the net income of the employee after deducting outgoings and expenses excluding self-education expenses, for a residential unit provided rent-free by the employer, irrespective of how much the unit

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21 Ibid heads 1(1) and 1(1A), pt 1 of scale 1.

22 Ibid s 29BB.

23 Ibid sch 1, heads 1(1AAB) and 1(1C).

24 Ibid heads 1(1AA) and 1(1B).

25 See further Jianlin Chen, 'The Yet-to-Be Effective but Effective Tax: Hong Kong's Buyer's Stamp Duty as a Critical Case Study of Legislation by Press Release' (2014) 10 *University of Pennsylvania East Asia Law Review* 1, 18-26 for an introduction of those measures.

26 Littlewood (n 2).

27 Ibid 2.

28 Ibid 16 and 205. See further Richard Cullen and Antonietta Wong, 'How History Has Shaped the Hong Kong Revenue Regime' in Noland Sharkey (ed), *Taxation in ASEAN and China* (Routledge, 2012).

29 Littlewood (n 2) 2.

30 Ibid.

actually costs.[31] Secondly, having been an 'undemocratic' government, the Hong Kong approaches to light taxation and a low level of public spending has appeared to enjoy greater popularity and support than those in most democracies.[32] People in Hong Kong ostensibly have been tolerant of such a low level of public expenditure, given that most of them are hardly taxed at all.[33] Further, as illustrated below, it appears systematically difficult to increase taxes, to increase the progressivity of its tax system and to increase public spending or to operate at a deficit.[34] Such a tax system, functioning tangentially with the phenomena described above, might possibly be found instructive to other jurisdictions, not least to those 'democracies' which have been struggling between casting an appropriate tax burden and voters' preference.[35]

B *'If it ain't broke, don't fix it'*

This expression is often quoted to explain the lack of motivation in carrying out any significant or wholesale review and reform of the tax system in Hong Kong. The Annual Reports of the IRD, from 2010/11 to 2021/22,[36] provide a snapshot of the key legislative changes over the last decade or so, from April 2010 to March 2022, [37] to the two major tax statutes in Hong Kong, the *IRO* and *Stamp Duty Ordinance* (Hong Kong) cap 117 ('*SDO*'). Evidently, the two major tax laws have both grown thicker and more complex over the years.

Regarding the IRO, the most noticeable feature over the course probably is the annual cut of the tax bill by a certain percentage subject to a ceiling while marginal tax bands for individual taxpayers has become more in number and wider apart, the lowest being 2% for the first HK$50,000 (about AU$9,265) of one's net chargeable income. Such tax concession typically applies to salaries tax and tax under personal assessment and occasionally, profits tax. For example, the reduction for the year of assessment 2021/22 applicable to all three taxes mentioned is 100%, subject to a ceiling of HK$10,000 (about AU$1,853) per case. This has taken, in estimate, a further 2.01 million individual taxpayers and 151,000 tax-paying businesses out of the tax net for that tax year, with the total public revenue forgone amounting to about HK$14.3 billion (about AU$2.65

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31 *IRO* (n 9) ss 9(1)(b) and 9(2). See also generally Inland Revenue Departmental Interpretation and Practice Notes (DIPN) No 16, and specifically DIPN Nos 38 and 41 <https://www.ird.gov.hk/eng/ppr/dip.htm>.

32 Littlewood (n 2) 2-3.

33 Ibid 2.

34 Ibid 3.

35 Ibid.

36 'Annual Report', *Inland Revenue Department* (Web Page, 12 December 2022) <https://www.ird.gov.hk/eng/ppr/are.htm>.

37 Interested readers may contact the author for a detailed table summarising those changes, which intends to serve as an initial step to continue Littlewood's treatise (n 2) which gives a historical account of the regime up to 2009/10.

billion).[38] This annual tax cut has seemingly become a convention and normal practice of the Hong Kong government not only in addition to or in lieu of relieving individuals and businesses from tax burden in the midst of any unfavourable economic situation, but also during years of fiscal surplus when, perhaps, the government had more money than it reckoned how to spend.[39] By any standards, this kind of 'habitual' annual tax cut is beyond imagination but 'something beguilingly attractive in Hong Kong's successes'[40] that other jurisdictions might find it interesting to investigate and explore.

Moreover, allowances and concessionary deductions are more favourable, typically with a policy reason behind. The following examples can all be considered to attempt to address the emerging, if not already emerged, ageing population[41] in Hong Kong: increase in child allowance to encourage giving births, increase in allowances for maintaining and residing with parents and grandparents, as well as increase in the maximum deduction of elderly residential care expenses to encourage the younger generation to take care of their elderly rather than 'abandoning' them in public institutions, increase in the maximum deduction for mandatory contributions to the Mandatory Provident Fund, premiums for voluntary health insurance and deferred annuity policies to mobilise the middle-aged group to plan ahead for their retirement life.

For businesses, the system now has two tiers of profits tax rates of which only half of the normal rate is applicable to the first HK$2,000,000 (about AU$370,225) of assessable profits. Small and medium enterprises should particularly welcome and be benefited by this initiative. There are also far more tax incentives and concessions than before, targeting special categories of businesses including, for examples, Islamic bonds, insurance businesses, aircraft and ship leasing, innovation and technology start-ups, acquisition of intellectual property rights, research and development, as well as fund management businesses. All these link to the current and future positioning of Hong Kong as the global financial, transportation, innovation and technology centre.

On the other hand, changes to the *SDO* over the last decade seem to have taken a different course. Said to be aimed at curbing the skyrocketing residential property price, the last decade saw the increase in the maximum ad valorem stamp duty rate from 3.75% to 4.25%, then to 8.5% and now at a flat rate at 15% unless an exception applies, among which the most relevant ones concern either a purchase by a Hong Kong permanent resident acting on his or her own behalf without beneficially owning another residential property in Hong Kong or a transfer between closely related individuals. On top of the ad valorem stamp duty, two additional types of duty have been introduced, both applicable to residential property transactions. The first is special stamp duty, the enhanced version of which is currently set at a maximum rate of 20% for quick disposal within 6 months after acquisition unless an exception applies, which includes, again, a transaction between

[38] 'News Archive', *Inland Revenue Department* (Web Page, 6 April 2022) <https://www.ird.gov.hk/eng/ppr/archives/22040601.htm>.

[39] See further Littlewood (n 2) 285-6.

[40] Ibid (n 2) 286.

[41] This issue will be elaborated below in Part III.

closely related individuals. The other one is buyer's stamp duty at the rate of 15% unless, for example, the purchaser is a Hong Kong permanent resident acting on his or her behalf. While relief is provided for individuals buying their new residence first and disposing of the previous one later, payment of duty can no longer be deferred. The mischief of buying more than one residential property under one single instrument has, after a court decision, been addressed and managed by further legislative amendments. Stamp duty on non-residential property transactions has also been subject to changes, first by bringing forth the time for stamp duty charge to the agreement for sale, instead of as was the case previously on the conveyance on sales, followed by doubling the ad valorem duty rates to a maximum of 8.5% when the flat rate of 15% was introduced to residential property transactions. It is only most recently that the rates have been reduced back to the original scale with a maximum rate at 4.25% while the duty rate on contract notes for sale and purchase of Hong Kong shares has increased to 0.26% in aggregate.

Other than those highlighted above, an earlier attempt in 2006 to introduce a goods and services tax ('GST') did not come to fruition. It has been suggested that it was essentially for lack of support of the representatives of the business sector that the proposal saw its failure.[42] Indeed, history has been repeating itself since 1947 in various attempts to radically reform the tax system in Hong Kong by introducing, for instance, a normal income tax to replace the schedular system, a tax on dividends and a sales tax.[43] Indeed, the business interests and elites seem to have played a significant role in shaping (and keeping intact) the tax system in Hong Kong, irrespective of the twists in political developments and the varying extent of democratisation in post-1997 Hong Kong.

The latest proposal of a vacancy tax targeting newly completed flats for domestic use being left unsold and not rented out for more than six months in a year had also been shelved. This proposal took the form of amending the *Rating Ordinance* (Hong Kong) cap 116 with the introduction of special rates which is defined under the bill to mean 'a tax chargeable on' such applicable tenement. Rates, in Chinese literally meaning 'payment for the Hong Kong Police' and used to support the police force and other public services in the old days, can be considered an indirect tax on landed property. They are charged at a percentage, currently at 5%, of the rateable value which is the estimated annual rental value of a landed property at a designated valuation reference date, assuming that the property was then vacant and to let. Both the owner and the occupier are liable for rates but in the absence of any agreement to the contrary, liability for rates rests with the occupier.

The Rating (Amendment) Bill was gazetted on 13 September 2019 with a Bills Committee formed on 8 May 2020. After two meetings of the Bills Committee in June and further consideration of the Housing Committee in July 2020, the Transport and Housing Bureau announced the withdrawal of the Bill on 19 October 2020, saying that views of the members at the Bills Committee were very divergent and there had been strong and

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[42] Littlewood (n 2) 274 and Jingyi Wang and Wilson Chow, 'Capital Gains Tax with Hong Kong Characteristics: Desirability, Feasibility and Design' (2018) 48 *Hong Kong Law Journal* 555, 564. See further generally Littlewood (n 2) 251-75.

[43] Ibid 106, 159-60, 188-9 and 237-40. See further generally: ibid 210.

differing views in the community, taking into account the then economic situation as well.[44]

As will be elaborated in Section 4.1 below, expansion of public expenditure is generally restricted. It has indeed been the case well before 1997 and is consistent with 'positive non-interventionism' which, since 2005, has also been known as 'big market, small government'.[45] Changes in stamp duty excepted, the above account is an affirmation of such adherence to the doctrines in tax policy and reform. The pattern of ad hoc responses and changes suggest that any major and more systemic tax reform is not an easy mission in Hong Kong, let alone the old saying that there is never a good time to introduce a new tax: as when times are tough, it is necessary to stimulate the economy instead of burdening it with new taxes; yet when the economy is recovering and booming, new taxes are just not needed.[46]

1 Stress Test from within

Nonetheless, the system has been, is, and will be, subject to stress tests internally.[47] From Figure 1 below, the financial year 2020-21 saw the largest ever fiscal deficit in Hong Kong. The larger-than-expected deficit was said to be mainly due to the government's expenditure related to the COVID-19 relief measures.[48]

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[44] The Government of Hong Kong SAR, 'Government decides to withdraw Bills for introducing Special Rates on unsold first-hand units and franchised taxis' (Press Release, 19 October 2020) <https://www.info.gov.hk/gia/general/202010/19/P2020101900708.htm>. See further Legislative Council of the Hong Kong SAR, *Bills Committee on Rating (Amendment) Bill 2019* <https://www.legco.gov.hk/yr19-20/english/bc/bc02/general/bc02.htm>.

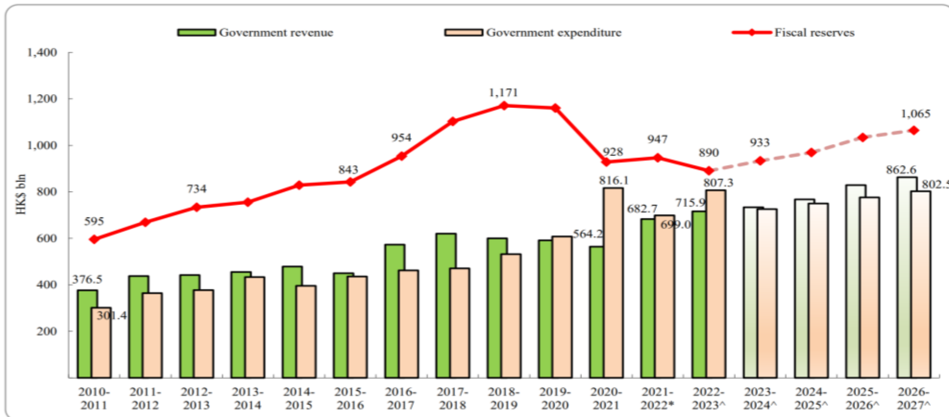
[45] '"Big market, small government" a key policy', *news.gov.hk* (Web Page, 19 September 2006) <https://www.news.gov.hk/isd/ebulletin/en/category/administration/060919/html/060919en03004.htm>. See further Lau Siu Kai, 'Basic Law may see some needed changes after 2047', *China Daily Hong Kong* (online, 8 August 2022) <https://www.chinadailyhk.com/article/284561>.

[46] Littlewood (n 2) 286.

[47] See eg, Wang and Chow (n 42) 557-63.

[48] See 'Past budgets', Financial Secretary (Web Page, 22 February 2023) <https://www.budget.gov.hk/2023/chi/previous.html>.

Figure 1 – Trend of government revenue, expenditure and fiscal reserves[(1)]



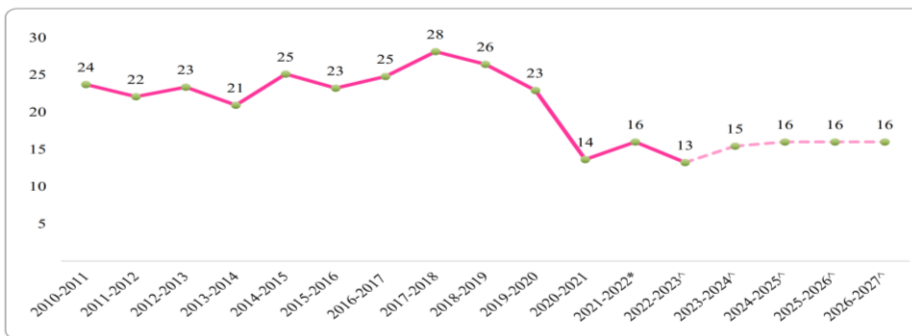
Notes: (*) Revised estimate.
(^) Estimate/forecast.
(1) Government revenue and expenditure do not include issuance and principal repayment of green bonds issued under the Government Green Bond ("GGB") Programme. Following the offering of the inaugural tranche of green bond in 2019, issuance under the GGB Programme amounted to HK$7.8 billion, HK$19.3 billion and HK$35.1 billion over 2019-2020 to 2021-2022 fiscal years respectively, and planned annual issuance during 2023-2024 to 2025-2026 is also set at HK$35.1 billion. Meanwhile, annual principal repayment of green bonds over 2024-2025 to 2026-2027 would range from HK$7.1 billion to HK$29.7 billion.

Data sources: 2022-2023 Budget speech and The Treasury (various years).

Source: Research Office, Legislative Council Secretariat, Research Brief (Issue 1, 2022/23)

Figure 2 below shows the surge in the fiscal deficit resulting in a rapid decline in the government's fiscal reserves. The current level of fiscal reserves dwindled sharply from 23 months in 2019-2020. It is indeed close to the level in 2003-2004 when Hong Kong was hit by the SARS pandemic. It is estimated to reach its record low in the financial year 2022-23 and will maintain at more or less the current level for the following four years.

Figure 2 – Fiscal reserves as number of months of government expenditure



Notes: (*) Revised estimate.
(^) Estimate/forecast.

Data sources: 2022-2023 Budget Speech and The Treasury (various years).

Source: Research Office, Legislative Council Secretariat, Research Brief (Issue 1, 2022/23)

The sharp fall in revenue from land premium contributed partly to the deficit. According to the data from the Lands Department, it was just HK$53.6 billion (about AU$9.93 billion) in 2020/21. The 2021-22 Budget estimated land premium to be HK$97.6 billion (about

AU$18.08 billion) [49] but at the end of the financial year, again according to the Lands Department, it was just HK$94.377 billion (about AU$17.48 billion), with the sale of one single piece of land at the New Central Harbourfront near the Star Ferry terminal on Hong Kong Island contributing HK$50.8 billion (about AU$9.41 billion).[50] While the latest Budget expects an increase in the land premiums, no successful sale has been concluded during the first two months of the new financial year.

Regarding revenue collected via tax, it seems from the table below that salaries tax and stamp duty have coped with the recent situation relatively better. However, the narrow tax base remains a concern; inequality and the absence of distributive justice caused by the system persist.[51]

Figure 1 Revenue collected by tax type

Type of tax	2017-18 ($m)	2018-19 ($m)	2019-20 ($m)	2020-21 ($m)
Profits tax -				
Corporations	133,459.3	160,833.2	149,427.5	**129,489.7**
Unincorporated businesses	5,640.9	5,786.5	6,472.8	**6,050.0**
Salaries tax	60,838.8	60,145.9	50,412.4	**75,027.3**
Property tax	3,447.8	3,624.4	2,806.5	**3,957.2**
Personal assessment	5,342.5	5,963.1	4,999.8	**6,293.7**
Total earnings & profits tax	**208,729.3**	**236,353.1**	**214,119.0**	**220,817.9**
Estate duty	31.3	88.7	53.6	**7.4**
Stamp duty	95,172.8	79,978.7	67,198.0	**89,044.6**
Betting duty	21,959.1	22,194.4	22,012.2	**20,877.1**
Business registration fees	2,726.7	2,826.7	189.6	**73.0**
Total revenue collected	**328,619.2**	**341,441.6**	**303,572.4**	**330,820.0**
% change over previous year	**13.2%**	**3.9%**	**-11.1%**	**9.0%**

Source: IRD 2020-21 Annual Report

For instance, the poverty situation continues to be worrying while the overheated real estate market has remained an unresolved long-term problem.[52] Poverty is defined with reference to monthly household income. Poor households are households with income below the poverty line which is drawn up for each group of households of the same size, defined as 50% of the median monthly household income (before policy intervention) of that household size group.[53] The Government used to refer to the poverty rate, which represents the ratio of poor population (meaning the number of persons living in the poor

[49] Research Office, Legislative Council Secretariat, *Research Brief* (Issue 3, 2021/22): <https://www.legco.gov.hk/research-publications/english/2021rb03-the-2021-2022-budget-20210407-e.pdf>.

[50] Lands Department, 'Land Sale Records' (Web Page, 2021) <https://www.landsd.gov.hk/en/resources/land-info-stat/land-sale/land-sale-records.html>.

[51] Yan Xu, 'Distributive Justice and Income Taxation – Is Hong Kong Special?' (Conference Paper, Australasian Tax Teachers Association (ATTA) Conference, 19-20 January 2022).

[52] See eg, Wang and Chow (n 42) 559-61.

[53] 'Poverty Situation', *Census and Statistics Department* (Web Page, 2022) <https://www.censtatd.gov.hk/en/scode461.html#section8>.

households) to total population living in domestic households,[54] with intervention of recurrent cash only, including cash-based benefits recurrently provided by the Government to individual households, such as social security benefits and education allowances in cash. From 2019 onwards, it refers to the rate after intervention of all measures including one-off measures and non-cash benefits provided with means tests such as the provision of public rental housing by the Government. Behind this rosier comparison, the public expenditure on relieving poverty has increased.[55]

Generally, public expenditure has been ever increasing, more noticeably in social welfare and health care since 2017-18.[56] Among other social issues, housing has always been one of the biggest concerns. To illustrate, Hong Kong housing prices have had an index between 170 and 190 over the last three and a half years, with July 1997 as the base period with an index of 100, according to a weekly index based on contract prices in transactions of a major property agency group that monitors variations in residential property.

The need for additional resources will intensify, particularly in light of the increasing costs for housing, the ageing population that refers to a shift in the distribution of population towards older ages with an increase in the population's mean and median ages, a decline in the proportion of the population composed of children, and a rise in the proportion of the population composed of elderly, and hence the increasing demand for medical care and social welfare. High expectations are said to have been expressed by the PRC government on the new Chief Executive of Hong Kong and his 'cabinet' in solving social problems including housing.[57] Some of the recent amendments to the IRO as sketched out above have supported this call. The forecast made in 2017 projected an elderly dependency ratio of 529 in mid-2046. The latest forecast shows the ratio at 569 in 2049, as reflected in the table below. This means that it is estimated to have, by 2049, 569 persons aged 65 and over per 1,000 persons who are within working age of 15-64, close to 57%.

According to the government statistics in August 2021,[58] the provisional estimate of the Hong Kong population was just below 7.4 million (7,394,700) at mid-2021, representing a decrease of over 87,000 (87,100) or 1.2% from 7.48 million (7,481,800) at mid-2020. The population decrease comprised a natural decrease (i.e. deaths surpassing births) and net outflow of Hong Kong residents. Over the same period, there was a net outflow of 89,200 other Hong Kong residents. The Hong Kong government attributed this mainly to

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[54] Ibid.

[55] Ibid.

[56] Secretary for Financial Services and the Treasury, '2022-23 Budget – Briefing for Legislative Council' (Report, 25 February 2021) <https://www.budget.gov.hk/2021/eng/pdf/2021_2022_SFST_Briefing_to_LegCo_25022021_en.pdf>.

[57] See further Wallis Wang, 'Beijing has high expectations – especially on housing', *The Standard* (Hong Kong, 20 June 2022) 1.

[58] Government of Hong Kong SAR, 'Mid-year population for 2021' (Press Release, 12 August 2021) <https://www.info.gov.hk/gia/general/202108/12/P2021081200387.htm>.

the continued impact of COVID-19, stringent border control and quarantine measures in place in Hong Kong and other places around the world, resulting in severe interruption of international travel, such that Hong Kong residents who had left Hong Kong before the pandemic may have chosen to remain outside Hong Kong or cannot return to Hong Kong. Those figures as at the end of 2021 were revised to just over 7.4 million (7,403,100), 23,600 or 0.3%, partly due to a net outflow of just 27,300 residents.[59] Despite the categorical dismissal by the government of the idea, what might have also contributed to the net outflow but not mentioned is the aftermaths of the social unrest in Hong Kong in 2019 leading to another brain-drain from here. Comparison of enrolment figures from the Education Bureau reveals that over 30,000 students withdrew from Hong Kong schools between October 2020 and September 2021.[60] They may just go abroad for further studies but whether they would return, and if so, how many of them would do so, remain uncertain. Indeed, a survey reported by the Hong Kong Institute of Asia-Pacific Studies, Chinese University of Hong Kong, over a course of five years from September 2017 to September 2021 has revealed that there has been an increase from 34% to around 42 to 43% of respondents would leave Hong Kong if there exists an opportunity to do so. Among those who would leave for elsewhere, more than one-third have somehow been preparing or have prepared to do so.[61]

The COVID-19 epidemic and the strategies, controls and measures taken by Hong Kong may just add more uncertainties as to how long it will take for the local economy to recover, the extent of its recovery and hence how all these may impact on the overall fiscal situation of the place. Hong Kong may well have passed the peak of the fifth wave of the pandemic, it has not yet returned to full normality prior to the first experience of the infectious disease in the midst of the rebound of the fifth wave. While it is undeniable that we are living in the 'new normal' and we must learn how to live up to it, it takes time, and sometimes pain, to adapt to the rather fluctuating and evolving situation with all possible variants and mutants, apart from the possible discovery and spread of another highly infectious and life-threatening disease.

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[59] Government of Hong Kong SAR, 'Summary results of 2021 Population Census and Year-end Population Estimate for 2021' (Press Release, 28 February 2022) <https://www.info.gov.hk/gia/general/202202/28/P2022022800462.htm>.

[60] William Yiu, 'More than 30,000 students quit Hong Kong schools, with campuses in high-income areas taking hardest knocks', *South China Morning Post* (online, 3 June 2022) <https://www.scmp.com/news/hong-kong/education/article/3180243/over-30000-students-quit-hong-kong-schools-campuses-high>.

[61] Hong Kong Institute of Asia-Pacific Studies, 'The Chinese University of Hong Kong's survey on Hong Kong as a livable city', (Report [in Chinese], 2021) <http://www.hkiaps.cuhk.edu.hk/wd/ni/20211020-110804_1.pdf>.

2 External Forces

(a) *The China Factor: Continuing autonomy or increasing integration*

Hong Kong is a special administrative region under the PRC. While it enjoys a high degree of autonomy administratively, Hong Kong has been subject to the (re)exercise of sovereignty by the PRC since July 1997. *Basic Law of the Hong Kong Special Administrative Region of the People's Republic of China* art 5 ('*Basic Law*'), the mini-constitution of the Hong Kong, preserves its prevailing system and way of life for at least 50 years from 1 July 1997 by providing that the PRC's socialist system and policies shall not be practised in Hong Kong during the period. So far as public finance and the tax system are concerned, the *Basic Law* arts 106 to 108 allow independence of Hong Kong subject to certain caveats including avoiding deficits, keeping the budget commensurate with the growth rate of its gross domestic product, as well as taking the low tax policy as reference. Such independence is given despite the fundamentally different tax systems Hong Kong and its sovereign state respectively have, as shown in the simplified tax matrix in the Appendix. On the other hand, the provisions not just provide a 'fiscal firewall' separating Hong Kong's public finances from those of the PRC, they grant constitutional, or quasi-constitutional, status to the 'low tax policy' and restrict public spending not to increase beyond the growth rate of its gross domestic product even without a deficit.[62]

It is now half-way through to the earliest 'expiry' date of the guarantee set at 2047. More recently, the 14th five-year plan of the PRC 2021-2025 seems to lay more emphasis on 'sovereignty', 'national security' and 'integration' with regards to the inter-relationship between the PRC and Hong Kong. In particular, with a specific aim to maintain the long-term prosperity and stability of Hong Kong and Macau, Article LXI of the plan provides that:

> We will fully and accurately implement the guiding principles of 'one country, two systems', 'Hong Kong people governing Hong Kong', 'Macau people governing Macau', and a high degree of autonomy. We will adhere to Hong Kong and Macau being governed in accordance with the law, uphold the constitutional order of the Special Administrative Regions (SARs) specified in the Constitution and the Basic Law. We will put into practice *the central government's overall jurisdiction* of the SARs, and implement the legal system and enforcement mechanisms of the SARs for *safeguarding national security*, and we will defend the *nation's sovereignty, security, and development interests, as well as the overall social stability of the SARs*. We will resolutely prevent and check external forces from interfering in Hong Kong and Macau affairs, support Hong Kong and Macau in consolidating and enhancing their competitive advantages, and *better integrate them into the overall development of the country*. [*Emphasis added*]

These thematic phrases have become more visible and apparent after the social unrest in 2019, leading to, inter alia, the enactment of the National Security Law and the so-called 'improved' electoral system to ensure patriots are administering Hong Kong. The latest election of the Legislative Council has its lowest-ever voter turnout, probably the

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62 Littlewood (n 2) 244-8.

narrowest-ever political spectrum, albeit with the largest-ever number of seats returnable from direct and indirect elections. Most recently, Hong Kong has also seen the highest-ever number of votes from the Election Committee in support of its next Chief Executive but, for the first time ever, in a one-horse race. Another illustration may well be the Hong Kong's choice of approach in combating and tackling COVID-19 that is more aligned with the PRC's strategies, from vaccination campaigns, social distancing requirements to travel restrictions. The Hong Kong government has been unprecedentedly firm despite repeated calls from the business representatives for earlier and wider relaxation of those measures in order to resume normal business activities.

Public law scholars and columnists hold divergent views on the sustainability of the 'one country, two systems' framework beyond 2047, despite what the PRC officials have repeatedly said and reassured.[63] It may be too early to speculate whether such 'integration' would and could, in time, spill over to the tax system in Hong Kong. While Hong Kong may not be another special economic zone for which the PRC provides location-specific tax incentives, on no account, however, should the China factor be overlooked with respect to how the Hong Kong system might have to change in the following decade or so. Indeed, the expectation from the PRC on the Hong Kong government to counter and solve social problems, as well as to integrate with the bigger part, has hinted the latter to likely expand its role in all aspects, economic, social, and people's livelihood, and to provide necessary impetus for its integration in the overall development of the former. As such, the *Basic Law* art 107 which stipulates that Hong Kong 'should follow the principle of keeping expenditure within the limits of revenues in drawing up its budget, and strive to achieve a fiscal balance, avoid deficits and keep the budget commensurate with the growth rate of its gross domestic product' may no longer be appropriate. Rephrasing of the article to allow the financial flexibility to the Hong Kong government to, for instance, widen its tax base or engage in other major and fundamental tax review and reform is clearly within the ambit of the PRC and may not be far from too remote.[64]

(b) *Regional Competition: The Lion City versus the Fragrant Port*

The two rivals, Singapore and Hong Kong, have long engaged in fierce but rather healthy competition for the most dominant 'mid-shore', as distinguished from 'offshore',[65] financial centre serving as the global gateway to Asia. The simplified tax matrix in Table 1 of the Appendix compares and highlights the key differences between these two taxing jurisdictions. Noticeably, Singapore does have estate duty and GST and it taxes, on top of

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63 For example, compare and contrast Alex Lo, 'Hong Kong is already living past 2047', *South China Morning Post* (online, 8 June 2022) <http://www.scmp.com/comment/opinion/article/3180905/hong-kong-already-living-past-2047>; Albert Chen, 『「一國兩制」的可持續性』 "The sustainability of 'One Country, Two Systems'" (in Chinese), *Ming Pao* (online, 20 June 2022) <https://news.mingpao.com/pns/觀點/article/20220620/s00012/1655662922468/陳弘毅-「一國兩制」的可持續性>.

64 Lau (n 46).

65 See eg, Joe Cheung and Chris Burton, 'Is Midshore the new Offshore', *IFC Economic Report* (Spring/Summer 2019) 41.

its source base, on a remittance basis, namely offshore profits of Singaporean resident companies in some circumstances. It has been, on the other hand, proactive in increasing its attractiveness for activities such as fund management and wealth planning. In 2020, Singapore leapfrogged Hong Kong, just marginally, for the first time in a global jurisdiction ranking survey, which asked 620 corporate services executives to rate the importance of various financial centres.[66] On the other hand, the Hong Kong government has responded with a series of favourable tax policies to further promote the place as a wealth management centre and family office hubs.[67] Would the 'success' of Singapore despite having such other taxes as GST and estate duty and a broader tax base including taxing remittances provide insights to how Hong Kong could reshape its tax system to meet challenges ahead?[68]

While the recent disruption since 2019 of the local economy might have made Hong Kong slightly more unfavourable, the tie and connection between the PRC and Hong Kong are something that Singapore does not, will not and cannot, have. Despite the social unrest and the COVID-19, PRC money has been flowing into the Hong Kong Stock Exchange, an example of which is a report of such investment through the Shanghai-Hong Kong and Shenzhen-Hong Kong connect programmes.[69] A survey conducted by Hong Kong's Private Wealth Management Association ('PWMA') and KPMG China has revealed that the contribution to Hong Kong's estimated private wealth from PRC individuals would increase from just 35% in 2019 to 51% by 2026.[70] Would the increased integration with the PRC offer Hong Kong a larger edge, allowing room even for some fundamental tax reform to modernise the system instead of competing with providing more tax incentives alone?

(c) *International Tax Arena: Cooperation or isolation*

Given its source-based tax system, international tax for a long time had not attracted much attention in Hong Kong despite the existence of a legislative provision for the making of double taxation agreements ('DTAs')[71] and the unprecedented arrangement with the PRC to prevent double taxation of income in 1998, which was subsequently replaced by a comprehensive agreement in 2007.

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[66] 'Is Singapore nudging ahead of Hong Kong as Asia's preferred financial hub?', *Vistra Insights* (Web Page, 2 November 2020) <https://www.vistra.com/insights/singapore-nudging-ahead-hong-kong-asias-preferred-financial-hub>.

[67] See further, Financial Secretary, Hong Kong SAR, *Budget Speech 2020-21* [61]-[62]; *Budget Speech 2021-22* [86]-[88]; *Budget Speech 2022-23* [82]. See 'Past budgets' (n 48).

[68] See further Mariani (n 5) 26-9.

[69] Yiyang Wei and Denise Jia, 'Chinese Mainland Cash Floods Into Hong Kong Stock Market', *Caixin Global* (online, 20 January 2021) <https://www.caixinglobal.com/2021-01-20/chinese-mainland-cash-floods-into-hong-kong-stock-market-101652920.html>.

[70] PWMA and KPMG, *Hong Kong Private Wealth Management Report 2021* <https://www.pwma.org.hk/wp-content/uploads/2021/10/Hong-Kong-Private-Wealth-Management-Report-2021-English.pdf>.

[71] *IRO* (n 9) s 49.

Hong Kong now has 45 DTAs with its major trading partners, [72] in addition to several limited agreements for the avoidance of double taxation of shipping income and airline income. Generally, a DTA provides certainty to investors on the taxing rights of the contracting parties, helps investors to better assess their potential tax liabilities on economic activities, and provides an added incentive for overseas companies to do business in Hong Kong, and likewise, for Hong Kong companies to do business overseas.[73] The year 2010 was the watershed year for the treaty network of Hong Kong. Hong Kong was at that time at the edge of being 'blacklisted' by the OECD as a tax haven and during that year a dozen such DTAs were signed. This achievement represents the product of rounds of negotiations and hard work, implementing what the then Financial Secretary announced in the 2009-10 Budget to align Hong Kong's exchange of tax information arrangements with international standards. The expanded network enables Hong Kong to serve as a safe harbour for investors more effectively without carrying the stigma of 'tax haven'. Other than the exchange of information article in DTAs, Hong Kong has seven other disrete Tax Information Exchange Agreements to date, with the first of its kind being with the US, followed by Denmark, Faroes, Greenland, Iceland, Norway and Sweden. Further, Table 4 in the Appendix lists out other legislative changes over the last decade have also highlighted Hong Kong as one of the international tax rule-takers in enhancing international tax cooperation, specifically with regards to exchange of tax information and related matters.[74]

Lately, the Two Pillars under BEPS 2.0 of the OECD pose another round of challenges to the Hong Kong tax system.[75] Essentially, Pillar One deals with tax challenges arising from digitalisation and the increasingly digitalised economy. It seeks to, among other things, expand the taxing rights of market/user jurisdictions where there is an "active and sustained participation of a business in the economy of that jurisdiction through activities in, or remotely directed at, that jurisdiction". To follow suit may mean necessary amendments to the Hong Kong charging provision on profits tax which currently requires, inter alia, carrying on a trade or business in Hong Kong. Further or alternatively, it may take the form of additions to the existing list of dutiable commodities, which comprises liquor, tobacco, hydrocarbon oil and methyl alcohol,[76] or the introduction of a new tax akin to GST. Pillar Two, intends to subject multinational enterprises ('MNEs') to a minimum 15% corporate tax rate globally. According to the OECD, Hong Kong has an effective corporate tax rate below this minimum rate while, for comparison, PRC and

[72] 'Comprehensive Double Taxation Agreements concluded' (Web Page, 8 November 2022) <https://www.ird.gov.hk/eng/tax/dta_inc.htm>. See further Julien Chaisse and Xueliang Ji, 'Rethinking Hong Kong's Tax Agreements: Challenges of Transparency, Harmonisation and Global Tax Reform' (2021) 51 *Hong Kong Law Journal* 405.

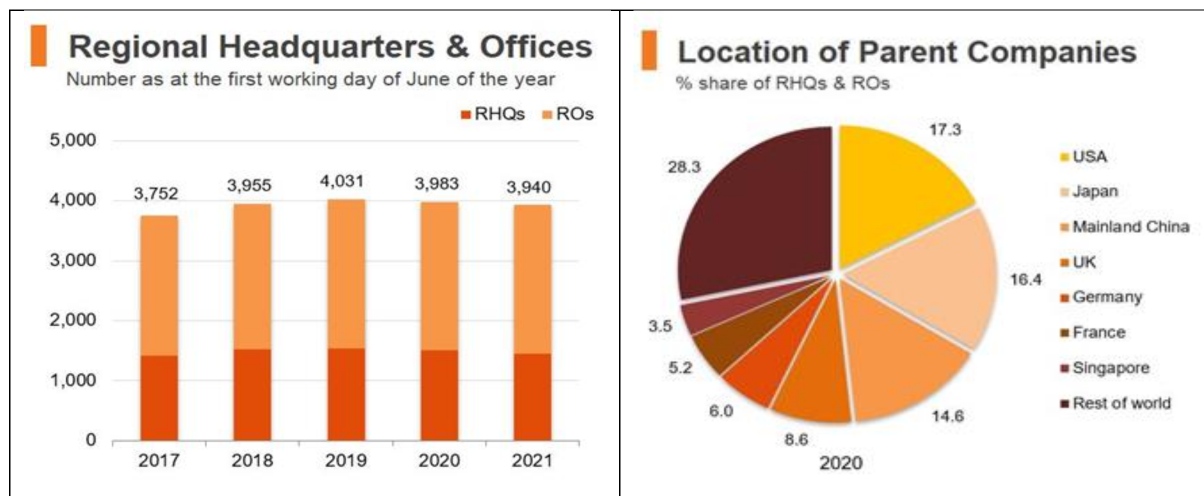
[73] 'Double Taxation Relief', *IRD* (Web Page, 2017) <https://www.ird.gov.hk/eng/pol/dta.htm>.

[74] See further Jingyi Wang, 'Global Development of Information Exchange: Rule-maker versus Rule-taker in International Tax Law' (2019) 49 *Hong Kong Law Journal* 951.

[75] See Christina Allen, 'Jurisdictional Taxing Rights under Model Conventions' (Conference Paper, ATTA Conference, 19-20 January 2022) for a historical account and a summary of both BEPS and BEPS 2.0.

[76] *Dutiable Commodities Ordinance* (Hong Kong) cap 109.

Singapore have theirs over 20% and 15% respectively.[77] It is understood that the Hong Kong government plans to implement, inter alia, the global minimum effective tax rate and considers introducing a domestic minimum top-up tax with regard to MNEs with global turnover of €750 million euros (about AU$1,177 million) to ensure that their effective tax rates reach the global minimum effective tax rate of 15% so as to safeguard Hong Kong's taxing rights.



Source: HKTDC Research

More than two decades post-1997, Hong Kong remains a popular gateway for regional headquarters or offices of MNEs, as the figures above show. On the other hand, the European Union ('EU') in October 2021 announced, again, the inclusion of Hong Kong in its watchlist on tax co-operation as it considered that the non-taxation of certain foreign sourced passive income in Hong Kong might lead to situations of "double non-taxation". In response, the Hong Kong government has committed to amend the *IRO* to target corporations, particularly those with no substantial economic activities in Hong Kong, that make use of passive income to evade tax across the borders.

While Hong Kong's attitude to remain a norm-taker in international tax rules seems evident, to what extent its continuously playing this role would impact on the MNE's choice of the place as their regional hubs is less than certain. What may seem even more uncertain is the PRC's approach towards the Two Pillars. The PRC has risen from a norm-taker to a norm-shaker in the international arena, especially in the shaping of BEPS 1.0, but its stance towards BEPS 2.0 seems to have been ambivalent, especially with regards to Pillar Two.[78] With the rise of the PRC as one of the world-leading powers, we have also seen, from time to time, a propagandistic war of words in the media between its spokesmen and the West's over all sorts of issues, political, social and economic. Would such divergence of views on a number of other matters spill over into the debate about international tax policy or there would be more convergence on tax matters because of

[77] *Corporate Tax Statistics* (OECD, 3rd ed, 2021).

[78] Jingyan Li, 'China's Rising (and the United States' Declining) Influence in Global Tax Governance? Some Observations' (2021) 75 *Bulletin for International Taxation* 1.

commonly shared economic interests? How would the PRC's role in the playing out in the next steps of BEPS 2.0 and beyond affect the positioning of Hong Kong?

III CONCLUSION: 'HAVE NOT THY CLOAK TO MAKE WHEN IT BEGINS TO RAIN'

The simple and low-rate tax system in Hong Kong has a remarkable track record of standing against the tide at various difficult times. It clearly 'ain't broke'. Nevertheless, it has long been considered outdated and inequitable. The last decade or so has seen the continuation of the rather reactive and piece-meal approach in legislative amendments. Such changes have made the tax codes grow significantly in volume and, in a way, complicated the system. On the other hand, no initiative to broaden the narrow tax base has succeeded in modernising the system and keeping it in pace with the changing socio-economic conditions in Hong Kong which have become drastically different from what they were underlying the original design of the system. Internal issues such as an ageing population, increasing costs of housing and demand for medical care and social welfare will only intensify in the years ahead, pressing for further increases in public expenditure and subjecting the system to a stress test. The recent socio-political events in Hong Kong, magnified by the socio-economic impact caused by the pandemic, have added fuel to the fire, draining the level of fiscal reserve with uncertainty over how long it will take to recover.

The external factors pose more questions than they answer. The PRC's balance in its approach and attitude towards Hong Kong in its broader sense of integration and national security as a sovereign state on the one hand, while seeing Hong Kong as a major gateway for global investment on the other hand, cannot be neglected. Its tug of war with the West, in particular the US, in the political and economic arenas may influence how it stands with respect to global tax governance, which in turn may have an impact on the positioning and (re)action of Hong Kong in the international trend of tax cooperation. The sustainable challenge from, if not success of, Singapore as a long-time economic rival in the region, will have to be borne in mind and, in some ways, may be worth appropriate referencing. This article argues that all these forces combined, internal and external, justify the need for a comprehensive review of and, where appropriate, wholesale changes to the tax system in Hong Kong, some of which may be more pressing timing-wise than the others.

Options have been raised over the years, from reviving and reforming the suspended estate duty[79] to rejuvenation of the discussion on the GST[80] and the vacancy tax withdrawn, from a capital gains tax with Hong Kong characteristics[81] to reimagining territoriality or even putting it to its end and expanding the tax schedules,[82] just to

[79] See eg, Andrew Halkyard and Wilson Chow, 'The Death of Estate Duty? The Case for Retention and Reform' (2004) 8 *Asia-Pacific Journal of Taxation* 48.

[80] See eg, Adrian Sawyer, 'New Zealand's Successful Experience Introducing GST: Informative Guidance for Hong Kong' (2013) 43 *Hong Kong Law Journal* 161.

[81] See eg, Wang and Chow (n 42); Butt and Ho (n 5).

[82] See Mariani (n 5) 25-31.

reiterate a few. Experience tells that any proposal to alter the fundamentals of the Hong Kong tax system will unavoidably attract arguments against it, more often than not, from the business and professional sectors. However, the recent approach adopted by the Hong Kong government in combating and controlling the impact of COVID-19, seemingly in alignment with the PRC strategies, has tipped the balance more towards maintaining public health and not overloading public hospitals as paramount even at the price of less expeditious economic recovery, contrary to the usual voices from the business and professional sectors. Could this be an indicator that we may be entering into an era under the 'new normal' when a larger scale of review and reform of the Hong Kong tax system can take off?

How would the general public perceive and respond to any fundamental changes to the Hong Kong tax system? The ordinary people in Hong Kong can tolerate the opulent paying much less tax than the latter would elsewhere because they mostly pay hardly any. The public view was overwhelmingly negative towards GST when it was proposed. However, researchers have also shown that Hong Kong people would be more receptive to tax reform that would address the unfairness in the tax system and/or improve their living conditions[83] and that they would agree to pay higher taxes if that would result in better public services.[84] Indeed, no strong public sentiment against the increase in *ad valorem* stamp duty and the introduction of Special Stamp Duty and Buyers Stamp Duty was evident. Those measures aim at stabilising property prices with available exceptions favourable to Hong Kong permanent residents who are genuinely acquiring their only property for self-use.

In no circumstances will tax reform be as straightforward as one would like to see. Any proposal, standalone or a combination of options, requires careful design and analysis, gauging expert and public opinion from all stakeholders. All these steps take time and effort. Accordingly, prompt action trumps. Continued and extended delay is not, however, recommended. While the Hong Kong tax system 'ain't broke', it would be better to 'have not thy cloak to make when it begins to rain'.

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APPENDIX

Table – A simplified tax matrix

Country Features	HKSAR	PRC	Singapore
Level of Tax	1	2	1
Jurisdiction to Tax	Territorial source	Residence and source	Territorial source [and on remittance]
Tax Rate	Relatively low [except stamp duty on land property transaction]	Medium	Low to medium
Income Tax	Similar to a schedular system [except personal assessment]	Income tax on individuals and enterprises	Income tax on individuals and companies
Tax on Capital	No	Yes; as income	No
Indirect Taxes	No	Yes	Yes
Tax Incentives	Not many	Many	Many

Tax Principles and the Serious Hardship Provisions in Aotearoa New Zealand

Lisa Marriott*

Abstract

This article analyses the serious hardship provisions in the *Tax Administration Act 1994* (NZ). The article reviews several cases where serious hardship has been claimed by taxpayers. The principles of administrative efficiency, equity and minimisation of tax distortions are used to frame the discussion. These principles are selected for analytical purposes as they were recently proposed by the Aotearoa New Zealand Revenue and Associate Finance Minister to underpin a proposed *Tax Principles Act*. In determining that the serious hardship provisions meet none of the proposed principles, the article questions what impact a proposed *Tax Principles Act* will have on existing legislation that does not align with the proposed new Act. It concludes that while there is likely to be little disagreement that tax principles are an important component of tax design, they may be of little benefit if not used to resolve potentially contentious components of existing legislation.

I Introduction

Aotearoa New Zealand (NZ) Revenue and Associate Finance Minister, David Parker, recently proposed introducing a *Tax Principles Act*.[1] If introduced, the Act will outline detailed tax principles and officials will report against those principles. The suggested principles are horizontal equity, vertical equity, administrative efficiency, and minimisation of economic tax distortions.

Few would disagree that adopting a principles-based approach to all aspects of taxation is desirable. However, the proposal generates several questions including: what is the impact on existing components of the taxation regime that may not align with the agreed upon principles? Will they change or does a principles-based approach allow recognition of anomalies alone? This article takes just one example of this: the provisions that allow for tax to be written off when a taxpayer suffers from serious hardship. The research applies the principles of equity, administrative efficiency and minimisation of tax distortions to this one, relatively small, component of the tax legislation. The study aims to assess if this regime meets the principles and what this may mean if a *Tax Principles Act* is introduced.

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[1] Minister David Parker, 'Shining a light on unfairness in our tax system' (Speech, Victoria University of Wellington, 26 April 2022).

In NZ taxpayers may request financial relief if they can demonstrate that recovery of outstanding tax would place the taxpayer in serious hardship.[2] In 2016 the NZ High Court confirmed a two-step approach for hardship applications.[3] The Commissioner of Inland Revenue ('CIR') must first determine whether the payment of tax would result in serious hardship for the taxpayer. Once that determination has been made, the CIR may consider the taxpayer's compliance history.

It is not possible to obtain detailed information on cases where the serious hardship provisions have been used to provide tax relief. Therefore, this research provides an in-depth analysis of two reported tax cases where the serious hardship provisions have been thoroughly analysed in the courts. Reported case law typically involves taxpayers who are challenging an Inland Revenue ('IR') decision to disallow a serious hardship claim to write off outstanding tax. The two main cases discussed in this study are *P v Commissioner of Inland Revenue*[4] and *Singh v Commissioner of Inland Revenue.*[5] In addition to these two detailed cases, the key features of several additional cases are highlighted to provide greater insight on the use of the serious hardship provisions.

This study queries the fairness that exists with the serious hardship provisions. With reference to fairness, most individual taxpayers do not have the opportunity to request relief of their tax obligations, as the tax due is deducted at source. While they may be able to demonstrate serious hardship from paying this tax, these taxpayers do not have the same right to apply for this to be written off, as the serious hardship provisions only apply to 'outstanding tax'.

The two case studies used in this study for illustrative purposes provide an indication of the inefficiency of the serious hardship provisions. Multiple cases, reviews, judicial reviews and appeals take place in providing for the natural justice of the taxpayers. Both cases took over 10 years to resolve. Most of the other cases reviewed also took lengthy periods to resolve. During this time, the taxpayer gains the time value of money from non-payment of tax obligations.

With relevance to minimising tax distortions, the serious hardship provisions write off penalties and interest along with the tax. The proportions of interest, penalties and tax written off in 2019/20 for serious hardship were 11%, 14% and 72% for interest, penalties and tax, respectively.[6] While the amounts written off under the serious hardship provisions are relatively small compared to those written off under other circumstances such as insolvency or being uneconomic to pursue, these write-offs provide few incentives to encourage taxpayer compliance.[7] The provisions also challenge the deterrence impact of the serious hardship provisions. While it appears that most of the debt written off

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2 *Tax Administration Act 1994* (NZ) s 177 ('*TAA 1994*').

3 *Singh v Commissioner of Inland Revenue* [2016] NZHC 3001 ('Singh [2016]').

4 *P and Commissioner of Inland Revenue* [2015] NZHC 2293 ('P [2015]').

5 *Singh v The Commissioner of Inland Revenue* [2017] NZCA 506 ('Singh [2017]').

6 Response to *Official Information Act 1982* (NZ) request (Inland Revenue, 12 October 2021).

7 Ibid.

relates to penalties and interest, these penalties and interest exist to deter non-compliance: either specific non-compliance of a taxpayer or general compliance of all taxpayers. The deterrent effect is diluted when taxpayers can engage in non-compliant behaviour and, if detected, claim serious hardship to avoid compliance.

This article argues that the serious hardship provisions are unlikely to meet the desired principles proposed by Minister Parker. This then raises the question of what consequential action a *Tax Principles Act* may provoke. This is not a question that this study can address. However, the question is a relevant consideration for those tasked with drafting and implementing the *Tax Principles Act*.

The article commences in section two with a brief discussion of some of the literature that has discussed the principles highlighted by Minister Parker, to provide a conceptual framework for the discussion later in the article. This section also incorporates the relevant legislation. The following section comprises three parts, all discussing cases where serious hardship has been claimed. The first two sections each discuss a specific case in depth, while the third provides a synopsis of 12 additional cases. A discussion follows in section four, highlighting how this provision challenges the principles mentioned by Minister Parker. The article concludes in section five.

II BACKGROUND

There are two parts to this section. The first engages in a brief discussion on the theoretical concept of fairness to reflect the balance that must be achieved in tax between deterring potentially non-compliant taxpayers, while ensuring that procedural justice is maintained. This is relevant for considering horizontal and vertical equity, as well as administrative efficiency and minimising distortions. The second part of this section outlines the legislation relating to the serious hardship provisions.

A *Fairness and Punishment*

Fairness underpins most theories of justice, although fairness is not always framed in the same way. For example, Rawls' theory of justice as fairness conceptualises how social institutions allocate rights, duties and advantages.[8] Of particular relevance to this study is the opposite, which is the allocation of disadvantages or burdens, such as paying one's tax. Rawls proposes two principles of justice: concern for equal liberty and the difference principle. The latter is relevant to this study, as the difference principle promotes the concept that inequality in distribution is permissible, if it improves the situation of those who are least advantaged. There is no data to indicate who benefits from the serious hardship provisions. IR advise they cannot provide this information, so the only data that can be used to gauge who benefits from the serious hardship regime is from reported cases. The two case studies outlined in depth in section three have high income-earning taxpayer defendants. The other cases also do not appear to have low-income taxpayer

[8] John Rawls, *A Theory of Justice* (Oxford University Press, rev ed, 1999).

defendants, notwithstanding the claims of serious hardship that are common across all the cases.

Rawls also discusses fair equality of opportunity. This has relevance to the current study as not all taxpayers have the same opportunity to have their serious hardship taken into consideration when paying taxes. Rawls proposes that factors such as social position should not impact on elements of deservingness, as these are not deserving in the first instance. Consequentially, Rawls argues that individuals do not deserve benefits that flow from these factors.[9] In arguing that fairness must result from non-arbitrary grounds, factors such as having more resources should not result in preferential treatment.

Rawls writes that 'no official should have discretionary power to inflict penalties whenever he thinks it for the benefit of society'.[10] However, the converse argument raises the question of whether officials should have discretionary power not to apply penalties when it may benefit an individual and not society. When taxpayers have tax, penalties or interest written off, this benefits only the individual and is to the detriment of society.

Rawls argues that outcomes must not only be efficient, they must also be just.[11] Rawls pursues this argument by claiming that equality of opportunity must also be present to achieve just outcomes.[12] Specifically, Rawls claims that people 'require a formal equality of opportunity whereby all have at least the same legal rights of access to all advantaged social positions'.[13] This challenges the current serious hardship provisions, as all taxpayers do not have the same opportunity to apply for the advantage of relief.

Walzer's 'spheres of justice' provides another lens. Walzer suggests that we should consider all allocations of benefits or burdens to consider whether distributions are fair. That is, some arrangement of different allocations of advantages and disadvantages may appear unfair, but when viewed in aggregate may result in a just outcome.[14] Of relevance to this study is that the cases discussed in the following section indicate the presence of advantage alongside preferential treatment when it comes to paying tax. Walzer's approach to equity can be used to assess whether taxpayers who benefit from the serious hardship provisions are likely to avoid overall advantage.

Nozick proposes a theory of entitlement, where past circumstances or events may create different entitlements. In Nozick's theory, justice is determined by whether entitlements are met, rather than by a chosen end-state or a measure such as need or merit. Thus, Nozick's theory of entitlement focuses on how the distribution occurs, rather than what the distribution is. This theory supports a retributive view of punishment incorporating

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9 David Mapel, *Social Justice Reconsidered: The problem of appropriate precision in a theory of justice* (University of Illinois Press, 1989).

10 Michael Walzer, *Spheres of Justice: A defense of pluralism and equality* (Basic Books, 1983).

11 John Rawls, 'Distributive Justice: Some addenda' (1968) 13 *Natural Law Forum* 51, 57.

12 Ibid 57.

13 Ibid.

14 Walzer (n 10)

proportionality of responsibility and harm as factors in the sentencing process.[15] Nozick proposes that final outcomes cannot determine if justice is achieved, rather the process by which the outcomes are produced is also relevant.[16]

When considering theories of punishment, typically these combine the elements of retribution, restitution, deterrence, incapacitation and rehabilitation. When considering non-compliance with tax, restitution and deterrence are the most relevant factors. Incapacitation and rehabilitation primarily apply to criminal behaviour and are less relevant for economic non-compliance. Retribution has some relevance, but primarily in signalling that punishment is justified when it is deserved.[17]

Restitution requires putting right the wrong. In the case of tax, this requires the taxpayer to meet their tax obligations, which typically would include the core tax alongside penalties and interest. The objective of restitution is to compensate for any loss and to ensure that the non-compliant individual does not obtain an advantage that compliant taxpayers do not.[18] In the case of non-payment of tax obligations, society suffers from fewer services or higher taxes, when taxes are not paid by those who owe them.

Deterrence comprises two components. Specific deterrence is intended to deter an individual who has been non-compliant from engaging in similar behaviour and general deterrence is intended to deter other individuals who may behave in a similar manner. While the tax system comprises penalties for non-compliance, most taxpayers are compliant. Importantly, penalties are only effective as a deterrent to the extent that non-compliant taxpayers believe that there is a likelihood of both being detected and incurring a penalty.[19]

The rational choice view of deterrence suggests that compliance will increase if the costs of offending outweigh the benefits: 'if judges can make the "costs" of an offence more onerous than the derived benefits, individuals will be deterred from committing offences'.[20] However, there is evidence that challenges this.[21] Notwithstanding the uncertainty of the impact of punishment as a real deterrent to non-compliance, it is still generally accepted to be important to signal to compliant taxpayers that non-compliant taxpayers will not be advantaged from their non-compliance. These are all important considerations to ensure administrative efficiency and minimise distortion of behaviour from the tax regime.

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[15] Robert Nozick, *Anarchy, State, and Utopia* (Blackwell Publishers, 1974).

[16] John E Roemer and Alain Trannoy, 'Equality of Opportunity' (Cowles Foundation Discussion Paper No 1921, Cowles Foundation for Research in Economics, Yale University, 2013).

[17] G Hall, *Sentencing Law and Practice* (LexisNexis, 2004).

[18] Ibid.

[19] Ministry of Justice, *Sentencing Policy and Guidelines: A Discussion Paper* (Ministry of Justice, 1997).

[20] K Varma and A Doob, 'Deterring Economic Crimes: The case of tax evasion' (1998) 40(2) *Canadian Journal of Criminology* 165, 167.

[21] M Bagaric, T Alexander and A Pathinayake, 'The Fallacy of General Deterrence and the Futility of Imprisoning Offenders for Tax Fraud' (2011) 26 *Australian Tax Forum* 511.

B *Serious Hardship*

TAA 1994 subpart 2B covers 'care and management' of the tax system. Among the duties outlined in this subpart are, the responsibility of every Minister and every officer of any government agency responsible for the collection of tax, to 'at all times use their best endeavours to protect the integrity of the tax system'. Under *TAA 1994* s 6A, the Commissioner is charged with the care and management of the taxes covered by the Inland Revenue Acts. As part of these functions, the Commissioner must 'collect over time the highest net revenue that is practicable within the law' having regard to:

(a) The resources available to the Commissioner; and
(b) The importance of promoting compliance, especially voluntary compliance, by all persons with the Inland Revenue Acts; and
(c) The compliance costs incurred by persons.[22]

TAA 1994 s 177A outlines how to apply the serious hardship provisions. This is outlined below:

(a) For the purposes of section 176, recovery of outstanding tax would place a taxpayer, being natural person, in serious hardship;
(b) For the purposes of section 177, the Commissioner may accept the taxpayer's request for financial relief on the basis of a claim that recovery of the taxpayer's outstanding tax or a relief company's outstanding tax would place the taxpayer, being a natural person, in serious hardship;
(c) For the purposes of section 177B, an instalment arrangement entered into by a taxpayer or a relief company would place the taxpayer, being a natural person, in serious hardship;
(d) For the purposes of section 177C (write-off of tax by the CIR), recovery of the outstanding tax would place the taxpayer, being a natural person, in serious hardship.[23]

The legislation continues to explain that the Commissioner makes a decision under this section by determining whether financial information, after allowing for payment of the outstanding tax, shows that the taxpayer would likely have significant financial difficulties because:

(a) The taxpayer or their dependant has a serious illness:
(b) The taxpayer would likely be unable to meet:
    i. Minimum living expenses estimated according to normal community standards of cost and quality;
    ii. The cost of medical treatment for an illness or injury of the taxpayer, or of their dependant;
    iii. The cost of education for their dependant:

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[22] *TAA 1994* (n 2) s 6A.

[23] Ibid s 177A(1).

(c) Other factors that the Commissioner thinks relevant would likely arise.[24]

The legislation is clear that 'compliance with, and non-compliance with, tax obligations must not be considered by the Commissioner when making a decision under this section'.[25] However, the Commissioner is not required to write off the outstanding tax if recovery of the outstanding tax would place the taxpayer in serious hardship.[26]

Amounts written off due to serious hardship are relatively small, as shown in Table 1, totalling NZ$142.2 million over the three-year period. Over the same period, 41,801 taxpayers had debts written off due to serious hardship, with an average debt per customer with a debt written off of NZ$3,402. Table 1 shows a downward trend of overall tax debt written off due to serious hardship and average debt per customer written off due to serious hardship.

Table 1: Serious hardship[27]

Financial Year (June-July)	**2017/18**	**2018/19**	**2019/20**	**Total**
Tax debt written off due to serious hardship	NZ$62.1 million	NZ$440.9 million	NZ$39.2 million	NZ$142.2 million
Number of taxpayers who had debts written off due to serious hardship	15,459	12,406	13,936	41,801
Average debt per customer written off due to serious hardship	NZ$4,017	NZ$3,297	NZ$2,813	NZ$3,402

III EXAMPLES OF SERIOUS HARDSHIP

This section comprises three parts. The first two provide a more in-depth discussion on two cases where the serious hardship provisions have been considered under application for judicial review. These cases are *P v Commissioner of Inland Revenue* and *Singh v Commissioner of Inland Revenue.* The third part of this section provides detail on several other cases reported in an application for judicial review, where the Commissioner has declined an application for tax relief because of serious hardship.

A *P v Commissioner of Inland Revenue*

When *P v Commissioner of Inland Revenue* was heard at the High Court in 2015, Mr P was described as a self-employed professional aged 75 years of age. Details were provided on

[24] Ibid s 177A(2).

[25] Ibid s 177A(3).

[26] Ibid s 177C(1BA).

[27] Response to *Official Information Act* request (Inland Revenue, 25 August 2021).

various illnesses that he had suffered over the last few years.[28] P had applied for judicial review of the Commissioner's decision to not write off P's tax debt of NZ$470,577.90 on the grounds of serious hardship under *TAA 1994* s 177. This case had a history going back 12 years. At the time of the application for judicial review, NZ$1,198,247.80 of tax debt had already been written off on two prior occasions.

In 2003, P had applied for tax relief because of his ill health and was granted relief of payment of his tax due of NZ$343,185.80. An instalment arrangement was entered into for the balance of NZ$184,000. In 2008, the Commissioner wrote off a further NZ$855,062, relating to goods and services tax (GST), income tax and pay-as-you-earn ('PAYE'), again based on P's health. At that time, NZ$253,000 tax remained outstanding. At the time of the second write-off, the case reports that the Commissioner anticipated that P 'would endeavour to bring his tax affairs under control by selling one of the two properties that P owned with his wife: their home and a beach property'.[29] This did not occur, and P increased his mortgage commitments to make the tax payment.

After the 2008 arrangements, P again fell into arrears with his 2009 provisional tax payments and 'continued to accrue tax debts since then'.[30] A third application for relief based on serious hardship followed in 2012. This was refused by the Commissioner and the taxpayer commenced judicial review proceedings. The Commissioner then reviewed her decision and provided a new decision, which also declined the application. P commenced further judicial review proceedings, heard in 2014. At this review, it was found that the Commissioner had not properly applied the law, as she had failed to consider P's financial circumstances as at the date of the application for relief. The claim was that while P had equity in assets that could be used to pay his creditors, this might not be the case at the date of the application.

P submitted a new application, at which time the total outstanding debt was NZ$470,577.90, of which NZ$124,445.30 was assessed tax for PAYE and GST. In considering the new application, IR analysis showed that if P was required to make payments towards his outstanding tax, that would be likely to place him in serious hardship. However, they also found that he had equity in a property that could be used to pay outstanding tax. IR calculated that P could pay approximately a quarter of the outstanding tax debt.[31]

The case notes reflect that P had suffered from ill health for several years, which had reduced his income. However, the case also notes that his 'income has remained significantly higher than most taxpayers who pay their tax'.[32] P's taxable income for the years 2005 to 2014 is outlined in Table 2:

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28 *P* [2015] (n 4).

29 Ibid [5].

30 Ibid [6].

31 Ibid [12]. Calculated as half the net equity in the property, as the property was jointly owned with P's wife.

32 Ibid [14].

Table 2: P's taxable income (2005-2014)[33]

Year	Income
2005	NZ$243,068.47
2006	NZ$227,385.23
2007	NZ$281,143.64
2008	NZ$215,888.98
2009	NZ$182,378.65
2010	NZ$132,014.00
2011	NZ$347,046.03
2012	NZ$94,742.10
2013	NZ$76,647.24
2014	NZ$91,550.14

The case notes write: '[n]otwithstanding previous relief, you have failed to structure your affairs so that you can live within your means'.[34] It was also noted that the applicant failed to comply with his tax obligations when he had a higher income: 'despite his ongoing health issues, in the year to March 2011 the applicant had a better year financially. He had a taxable self-employed income of NZ$331,986 and could have made up some of his arrears'. However, he made no payments towards his 2010 income tax and only ever paid NZ$246.19 towards his 2011 tax.[35] Analysis of P's financial arrangements was described as showing that he was 'actually insolvent, in that you would be unable to pay all of your debts as and when they fall due, when payment of on-going tax is taken into account'.[36] While the taxpayer had offered to set aside 30% of income to ensure future tax obligations would be met, the IR official noted that the bank would be entitled to those funds if P fell behind in his debt servicing.

P's 'poor compliance' was noted along with his 'failure to structure your affairs so you can live within your means notwithstanding being provided with relief on two previous occasions'.[37] Instead, provision of further financial relief was not seen as appropriate to protect the integrity of the tax system and to promote compliance. Bankruptcy proceedings were proposed.[38]

33 Ibid [51].

34 Ibid [14].

35 Ibid [51].

36 Ibid [14].

37 Ibid.

38 Ibid.

The substance of the case relates to a change of legislation that occurred after P's original application for consideration of serious hardship, and his resubmission of that request after the Commissioner's first review. In the pre-2014 hardship provisions it was not possible for the Commissioner to bankrupt a taxpayer who met the definition of a person who would be placed in serious hardship if that person had to pay their outstanding tax. This position changed after 30 June 2014, and the Commissioner was permitted to choose whether to bankrupt or write off the tax.[39]

P argued 'the serious hardship he suffered and continues to suffer is merely a continuation of the reasons which justified the writing off of tax on earlier occasions'.[40] Therefore, it was claimed that it is not a question of his having failed to take advantage of several opportunities to adjust his affairs to meet his tax obligations but of his inability to meet his continuing obligations. The court agreed with P that the legislation had changed, but ultimately decided that the outcome for P would have remained unchanged despite the change in legislation.

B *Singh v Commissioner of Inland Revenue*

The *Singh v Commissioner of Inland Revenue* case has an equally long timeframe as the previous case. The case started in 2008 when Mr Singh voluntarily disclosed to the Commissioner the sale and purchase of 16 properties between October 2002 and January 2004.[41] An investigation followed, which found that Mr and Mrs Singh had bought and sold 39 properties, with an aggregate value over NZ$8 million, when the period was extended to March 2007.[42] The Singh's claimed they were not aware that the property dealing resulted in taxable income. The Singh's provided few of the records requested by IR, but in 2009 the Singh's agreed to the tax adjustments for the income years 2003-2007. In 2010 the Singhs' accountant suggested the Singhs would offer a lump sum payment of NZ$150,000, but this did not occur. [43]

In February 2011, the Commissioner obtained judgements against the Singhs for NZ$574,105.77 and NZ$619,730.45, respectively.[44] These amounts related to unpaid income tax and GST, overpaid family assistance benefits, plus interest and penalties for gross carelessness.[45] Further information provided resulted in the Commissioner reducing the amounts owed by around NZ$200,000.

The Commissioner commenced bankruptcy proceedings in 2012. The taxpayers filed a notice of intention to oppose the application, claiming they would be able to repay the

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[39] Ibid [49].

[40] Ibid [22].

[41] *Singh* [2016] (n 3) [6].

[42] *Singh* [2017] (n 5).

[43] Ibid [6].

[44] Ibid [7].

[45] Ibid.

outstanding debt given time. The Court was asked to approve an instalment arrangement with monthly payments of NZ$5,000. However, five years after this claim was made 'only NZ$1,200 was paid'.[46]

In January 2014, a formal request was made for financial relief on the basis that the Singhs were in serious financial hardship. The request was for the entire debt to be written off. In response to this the Commissioner offered to accept a payment of NZ$649,482 and write off the balance. The debt was then around NZ$1.75 million.[47] A second request for financial relief followed in September, with the claim that their financial position had deteriorated since the previous request. Mr Singh offered to pay NZ$30,000 'which could be offered in full and final settlement of the combined debt'.[48] This was declined as discrepancies were found in the financial information provided by the taxpayers. One example provided was 'the amount required to service the mortgage on the property owned by the Singhs' family trust, disregarding all other living expenses, was more than their declared combined income'.[49] The case notes record that 'The Commissioner concluded that the information provided in support of the request for financial relief did not reflect the true position'.[50]

A third request for financial relief was made in January 2015, where the taxpayers offered to pay NZ$56,000 plus NZ$400 per month for 36 months (a total of NZ$70,400 or roughly 4% of the debt that existed in January 2014) or alternatively to write off the entire amount of the debt. The Commissioner declined this offer and bankruptcy proceedings were set for March 2015. A fourth request for relief was made in March 2015, which was also declined. The Singhs filed for judicial review and the Commissioner agreed to review the situation for the fifth time.

During this investigation, it was noted that the Singhs' declared income was NZ$5,012, but monthly home loan payments were NZ$4,859, leaving them only NZ$153 for their living costs. Their statement also suggested they were supporting their two adult children. However, the investigation had found no evidence of living expenses, and was advised that one adult son was paying for the Singhs' living costs. Further investigation of the spending did not support this claim.[51] IR again declined to provide the taxpayers with tax relief. The taxpayers then reinstated their judicial review proceedings.

During the review of the decisions, other factors were discovered and the conclusion was reached that 'Mr and Mrs Singh have continued to suppress their income for tax purposes'.[52] The case notes observe that in previous applications for hardship relief, IR were unable to determine whether they were in hardship, as their expenses exceeded

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[46] Ibid [8].

[47] Ibid [11].

[48] Ibid [12].

[49] Ibid [13].

[50] Ibid.

[51] Ibid [22].

[52] Ibid [26].

their declared income, a situation that continued at the time of the case. Hence, IR concluded that income had not been declared for review purposes or returned for tax purposes.[53]

The judicial review was dismissed at the High Court and the taxpayers appealed. The subsequent appeal was also dismissed.

C *Other Examples of Serious Hardship*

As requests for tax relief because of serious hardship generally only become visible when taxpayers engage in court action, such as through a judicial review, it is not possible to comment with any accuracy on the extent to which cases such as the two outlined in the previous sub-sections are representative of other cases involving serious hardship. Twelve additional cases are briefly outlined in Table 3 for the purposes of balance.[54] All the following cases resulted from judicial review applications or other requests for the courts to review decisions made by the Commissioner.

Table 3: Cases where serious hardship relief is requested

Year	Case Name	Outstanding Tax	Tax Type (where known)	Other information from case notes
2002	*Singh*[55]	NZ$84,473.94	Income tax	• Taxpayer had filed 'numerous tax returns on behalf of both himself and his clients seeking refunds to which neither he nor they were entitled'. • Taxpayer kept refunds. • Case states: 'Debtor's offending encompassed a vast array of activities, many of which were devious in the extreme'.[56] • Case states: 'Commissioner has reasonable cause to suspect that Mr Singh has secreted other

[53] Ibid.

[54] A search was undertaken on 7 June 2022 in Wolters Kluwer CCH IntelliConnect using the search protocols 'serious hardship' and 'Inland Revenue' from 1 January 2000. This returned 215 results. Most of these were not cases; instead they were Standard Practice Statements, other Tax Updates or tax advice from Inland Revenue (e.g. Agents Answers), Bills or commentary that included discussion of the serious hardship provisions. Cases were only included when they were relevant to serious hardship. Some cases, for example, focused on instalment arrangements, rather than serious hardship.

[55] *Re Singh; ex parte Commissioner of Inland Revenue (No 2)* (2002) 20 NZTC 17,943.

[56] Ibid [25].

				funds away in the name of third parties'.[57] • Order for adjudication made.
2004	*Raynel*[58]	NZ$28,134.78	Income tax, GST, PAYE	• Taxpayer noted to have a poor record of compliance with tax obligations and a pattern of new entities being established immediately on the collapse of predecessors. • Payments had not been made to IR when funds were available. • IR were taking steps against Raynel since May 2000. Taxpayer continued to trade. • Case was dismissed.
2004	*Tyrell*[59]	NZ$330,000	Income tax	• No evidence provided by taxpayer that she had attempted to explore ways to repay outstanding tax. • Case states: 'It appears evident that a deliberate decision to divert these funds for personal use was made'.[60] • Application to set aside bankruptcy notice refused.
2004	*Marra*[61]	NZ$360,000	Income tax	• Part of the Digitech tax avoidance scheme (in the mid-1990s). • Losses claimed were subsequently disallowed. • Failed to demonstrate serious hardship as financial difficulties had arisen solely from his tax liability. • Commissioner successfully applied to adjudicate the taxpayer bankrupt.

[57] Ibid [46].

[58] *Raynel v Commissioner of Inland Revenue* (2004) 21 NZTC 18,583 ('*Raynel*').

[59] *Re Tyrell; ex parte Commissioner of Inland Revenue* (2004) 21 NZTC 18,542.

[60] Ibid [13].

[61] *Re Marra; ex parte Commissioner of Inland Revenue* (2004) 21 NZTC 18,494.

2005	*Clarke*[62]	NZ$581,461.49 and NZ$865,118.23	Income tax	• Taxpayer submitted tax returns showing losses 1994-1999, but tax losses were subsequently disallowed. • Case refers to the presence of a family trust and 'assets that have disappeared during 2000'. • Case was dismissed.
2005	*W*[63]	NZ$443,722.56	Income tax, GST	• Taxpayer was a barrister. • Late income tax payments dating back to 1990; unpaid tax 1997-1999; returns not filed 2003-2004. • GST paid late in seven six-month periods from 1993; unpaid in 11 six-month periods from 1994. • CIR directed to reconsider application.
2005	*McLean*[64]	NZ$234,066.65	Income tax	• Taxpayer was a real estate agent. • Tax was owing due to participation in Digitech/Salisbury tax avoidance scheme (1994-95). • Losses claimed were subsequently disallowed. • Taxpayer had alienated assets into trusts.
2004	*Gilchrist*[65]	NZ$45,000 and NZ$200,000+	GST, other	• Taxpayers were trustees of a trust that owed GST of NZ$45,000. • Case states: 'Other arrears of tax obligations of Mr Gilchrist and associated trusts …owe more than NZ$200,000 in tax arrears'.

[62] *Clarke v Commissioner of Inland Revenue, Money v Commissioner of Inland Revenue* (2005) 22 NZTC 19,165 ('*Clarke*'). The tax losses that were subsequently disallowed resulted from an investment scheme (Digi-Tech, Salisbury) that was related to taking an abusive tax position or evasion or similar [at 24].

[63] *W v Commissioner of Inland Revenue* (2005) 22 NZTC 19,602 ('W').

[64] *McLean v Commissioner of Inland Revenue* (2005) 22 NZTC 19,231.

[65] *Gilchrist v Commissioner of Inland Revenue* (2004) CIV-2993-054-862, High Court, Palmerston North ('*Gilchrist*').

				• Taxpayer made unsuccessful appeal against decision to reject instalment arrangement.
2010	*Larmer*[66]	NZ$175,641.68	Income tax, GST	• Met the criteria for serious hardship for 2000-2003, but not for the subsequent tax years.
2011	*Kea*[67]	NZ$532,653.28	Income tax	• Taxpayer was a management consultant. • Filed tax returns but did not pay tax for period 2003-2010. • Property was owned in a trust (where taxpayer was settlor, trustee and discretionary beneficiary). Judicial review application dismissed.
2012	*Ali*[68]	NZ$266,291	Income tax	• Taxpayers were buying and selling properties and had equity of NZ$700,000 in a property. • Case concerns assessments for years ended 2004 and 2006. • Application for judicial review dismissed.
2015	*Russell*[69]	NZ$5,692,665.90	Income tax	• Well known NZ tax case. • Outstanding tax amount was for the period 1985 to 2000 based on a scheme he devised that had the effect of reducing and avoiding tax. • Debt increased to over NZ$350 million by 2015. • Commissioner's appeal to strike out proceedings granted.

There are some common themes that can be identified from the cases in Table 3. Many of these have had multiple reviews and negotiations that have been ongoing for years. However, from the outset, the outcome of many cases appeared likely to be bankruptcy of the taxpayer and any collection of outstanding funds was unlikely. Several of the cases

[66] *Larmer v Commissioner of Inland Revenue* (2010) 24 NZTC 24,016 ('*Larmer*').

[67] *Kea v Commissioner of Inland Revenue* (2011) 25 NZTC 20-084 ('*Kea*').

[68] *Ali v Commissioner of Inland Revenue* (2012) 25 NZTC 20-121.

[69] *Russell v Commissioner of Inland Revenue* (2015) 27 NZTC 22-003.

involved blatant non-compliant behaviour, with participation in tax avoidance schemes presenting as a recurring fact.

IV DISCUSSION

This article does not suggest that the Commissioner is wilfully writing off tax without making a reasonable attempt to collect it. At some level it is the opposite, as in many situations it appears that the Commissioner invests considerable time and resource into processes that appear unlikely to ever result in a revenue-positive outcome. While in some cases this may be needed to ensure natural justice is present, in the cases outlined above, the resource intensive processes are exacerbated by the serious hardship provisions. This section discusses the issues that arise from the cases outlined above and questions whether the serious hardship provisions meet the criteria expected of good tax policy and, specifically, those highlighted recently by Minister Parker.

A *Administrative Efficiency*

The cases outlined in section three show that many cases take a lengthy period to resolve, such as the cases involved in the Digitech tax avoidance scheme from the mid-1990s. In some cases, this was over 10 years. In the *Singh* case, it was 13 years between the transactions and the judicial review hearing, during which time almost no tax was paid and at the end of the proceedings it appeared that no tax would be paid as the assets were held in trusts. Bankruptcy appeared inevitable, but this was probably inevitable from the time the initial disclosure of unpaid tax was made. Instead, the processes permitted the bankruptcy to be delayed for at least 10 years, as the taxpayer requested multiple reviews.

For all the cases outlined above (i.e., those in Table 3, as well as *Singh* and *P*) the taxpayer has the benefit of the use of money that is unpaid, or the use of assets where these have been purchased. Conversely, the state did not have the use of these funds to be used for the benefit of society for either a potentially long period of time, or at all. The outcome of many of the cases discussed in section three was bankruptcy for the taxpayer, resulting in the tax, interest and penalties permanently written off, after many years of resource intensive reviews. One could argue that the taxpayers in most of the cases outlined above had little to lose by engaging IR in drawn-out proceedings. Some of the taxpayers were clearly persistent in their demands for tax relief, with little to act as a deterrent.

In *P v Commissioner of Inland Revenue,* where bankruptcy was not a consideration, interest and penalties were written off on two occasions. In other cases where taxpayers were negotiating, again interest and penalties were often the components that appeared to be negotiable. From the perspective of administrative efficiency, imposing penalties and interest, only to subsequently write them off if a taxpayer claims they will suffer from serious hardship if they must pay those taxes, is inefficient.

B *Fairness*

There are few other areas in society where people can claim they cannot afford to pay their debts, and this should afford them preferential treatment. This creates a challenge for horizontal equity if all debtors to the state are the same, as tax debtors are not treated in the same way as, for example, welfare debtors or those owing other fines.

An illustrative example is Legal Aid in NZ. Individuals may apply to have their Legal Aid written off under circumstances that are similar, but not identical, to those outlined in the tax legislation, i.e., inability to meet basic living expenses, inability to meet medical costs, or the presence of a serious illness or injury. Note, however, the difference with reference to living expenses. To qualify for Legal Aid write-off the applicant must demonstrate they cannot 'meet basic living expenses'.[70] For tax purposes the person must show they are unlikely to meet 'minimum living expenses estimated according to normal community standards of cost and quality', that is, 'normal' standards, rather than 'basic living expenses'.

It is unclear what minimum living expenses estimated according to normal community standards of cost and quality look like. However, it is probably safe to assume that it includes some basic food items and accommodation. In NZ, need for Government hardship assistance is high, and in recent times people reporting insufficient income have increased.[71] Government spending on additional hardship assistance increased from NZ$78.3 million in the quarter to March 2017 to NZ$238.8 million in the quarter to March 2022: an increase of over 200%.[72] This represents 647,571 hardship assistance payments in the most recent quarter.[73] The majority of these grants were for food (363,888).

Living costs for those in the lowest-income households (which includes beneficiaries and superannuitants) have been rising faster than those across all households over the past five years.[74] The Household Living Cost Index for beneficiary households increased by 3.9% over the year to September 2021 and the Salvation Army forecast this to increase to 6% by the end of 2021. Any increases in benefits were therefore absorbed in increased costs of living. This is visible in the hundreds of thousands of food grants paid out by the Ministry of Social Development.[75] However, beneficiaries or superannuitants who have government transfers as their only sources of income cannot apply for serious hardship. They may be suffering from ill health or unable to meet minimum living expenses according to normal community standards, but the serious hardship provisions do not apply to them. Conversely the serious hardship provisions were successfully applied (twice) in the case of *P v Commissioner of Inland Revenue,* to a high-income earner.

Most of the cases outlined above appeared to involve higher income earners. This is assumed on the basis that tax liabilities were significant, such as NZ$581,461 and

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70 Ministry of Justice, 'Application for Write off/Exemption' (Web Page, 2022) <https://www.justice.govt.nz/assets/Documents/Forms/WO-Application-Editable-PDF-Final-29-01-2021.pdf>.

71 Salvation Army, *State of the Nation* (Salvation Army Social Policy & Parliamentary Unit, 2022).

72 Ministry of Social Development, *Benefit Fact Sheets: Snapshot – March 2022 Quarter* (Report, 2022) <https://www.msd.govt.nz/documents/about-msd-and-our-work/publications-resources/statistics/benefit/2022/benefit-fact-sheets-snapshot-march-2022.pdf>.

73 Ibid.

74 Salvation Army (n 71) 25.

75 Ibid 26.

NZ$865,118 in income tax owing in *Clarke*; or Kea who owed NZ$532,653 in income tax.[76] Various justifications were provided in the cases for why the taxation was not paid when it was due. However, an important consideration when income tax is outstanding, is that the income has been earned. One example of justification was in *P v Commissioner of Inland Revenue* when P claimed his illness had limited his ability to pay tax. A taxpayer may be in a position of serious hardship if they are suffering from illness.[77] However, in several years his illness did not appear to impact on his income earning ability, just his ability to pay his tax obligations.

Most taxpayers are compliant or have limited options not to pay their taxes.[78] This fact challenges vertical equity as taxpayers do not have the same ability to apply for tax relief if they are suffering from serious hardship. Only those who do not have tax deducted at source may make this claim. Moreover, only those who do not have tax deducted at source obtain the benefit of not paying on time and can take advantage of the time value of money.

Walzer argues that not all allocations of benefits or burdens must be equal to be fair. Instead, we should look to the overall allocation to assess whether fairness has been breached. It is difficult to argue that the taxpayers considered in this article have not benefited overall from the tax position adopted. While bankruptcy was looking like it would be the outcome for many, this was likely to have been the result from the time the tax debt was incurred. Some taxpayers do not even have to incur the burden of public awareness of their non-compliance, as taxpayers such as 'P' (in *P v Commissioner of Inland Revenue*) benefit further from name suppression.

A particular concern about the application of the serious hardship provisions is the lack of transparency on who benefits from them. Except for the small number of cases that are reported, and the aggregate total of funds written off due to serious hardship, little is known about who benefits from the provisions. There may be Te Tiriti of Waitangi (Treaty of Waitangi) concerns to the extent that only certain 'types' of taxpayers are benefiting from these provisions. However, in the absence of transparency, that must remain as conjecture.

What is known is that those who do not benefit are wage and salary earners who have PAYE deducted at source. Therefore, those who may be able to benefit from the serious hardship provisions include those who are self-employed, earn income from other untaxed sources or run a business. In some of the cases outlined in the previous section, GST comprised part of the outstanding tax.[79] In these cases, the taxpayer has charged their customer for GST but not paid it to IR as required. It appears anomalous that the taxpayer

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[76] *Clarke* (n 62); *Kea* (n 67).

[77] *TAA 1994* (n 2) s 177A(2)(a).

[78] Inland Revenue report that 89.9% of tax payments from customers were on time in 2020/21. Inland Revenue, *Annual Report Te Tari Taake Pūrongo ā-Tau 2021* (Inland Revenue, 2021) 10.

[79] *Raynel* (n 58); *W* (n 63); and *Larmer* (n 66).

should then claim serious hardship when they have retained funds they did not have a legal right to retain.

In some of the cases outlined in Table 3, there were clear suggestions of dishonest behaviour: engagement in tax avoidance schemes or deliberately alienating assets. However, it is this dishonest behaviour that is then afforded preferential treatment if tax relief is available, when it is not available to compliant taxpayers.

C *Minimisation of Tax Distortions – Deterrence*

Discretion and leniency are both desirable, albeit within limits. As noted by Freedman and Vella 'to operate efficiently and effectively revenue authorities require discretion, but processes must be in place to keep discretion in check'.[80] The operationalisation of discretion should not result in the unintended consequence that it deters others from complying.

One question that arises from the above cases is why no prosecutions are taking place in the cases where taxpayers had misrepresented their circumstances. The Commissioner may prosecute criminal non-compliance. While not all the activity outlined above could be considered criminal, there is some activity that is, such as false representations to the Commissioner (including by concealment of or failure to provide relevant information); misuse of revenue held in trust, such as GST; false refund claims; or non-filing of returns when due with intent to evade assessment and payment of liabilities.[81]

Reference to IR's prosecution guidelines indicates that 'prosecution is one way the Commissioner of Inland Revenue protects the integrity of the tax and social policy systems'.[82] Prosecution is described as 'an enforcement activity, usually of last resort, applied in conformity with the Solicitor-General's Prosecution Guidelines …against those who refuse to comply with their tax or social policy obligations'.[83] The guidelines explicitly identify the intended deterrent effect, with reference to the sanction of criminal conviction and punishment assuring compliant taxpayers that the Commissioner will take enforcement action against non-compliers.

Two tests must be satisfied for a prosecution to proceed: there must be sufficient evidence to provide a reasonable prospect of conviction; and the public interest test must be met. It is the second of these that is of most interest as, in the cases outlined above, there was no suggestion of inadequate evidence supporting the cases. Alongside the Solicitor-General's public interest considerations, which apply to all IR cases, the Commissioner

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[80] Judith Freedman and John Vella, 'HMRC's Management of the U.K. Tax System: The Boundaries of Legitimate Discretion' in Chris Evans, Judith Freedman and Rick Krever (eds), *The Delicate Balance – Tax Discretion and the Rule of Law* (IBFD, 2011).

[81] Inland Revenue, 'The types of non-compliance that may result in a decision to prosecute' (Web Page, 2022) <https://www.taxtechnical.ird.govt.nz/en/about/our-prosecution-guidelines>.

[82] Inland Revenue, 'Introduction' (Web Page, 2022) <https://www.taxtechnical.ird.govt.nz/en/about/our-prosecution-guidelines>.

[83] Ibid.

considers several revenue-specific factors.[84] These factors favour prosecution and include:

- Conformity with IR compliance strategies, especially current risk factors;
- A history of non-compliance;
- The degree of non-compliance;
- Loss to the revenue;
- Damage to the integrity of the Revenue, e.g., attempts to undermine the administration of the Revenue Acts;
- Misuse of corporate entities for a criminal tax purpose, e.g., phoenixing or using multiple entities to facilitate GST fraud;
- Organised and systematic attacks on the tax or social policy systems.[85]

IR also documents factors that work against prosecution. There are two, both of which relate to the availability of alternatives. These are:

- The availability of effective alternatives, e.g., where a defaulter has made good the losses to the Revenue, has paid any interest, and the educational / compliance / integrity/ deterrence aspect is met by assessment of a suitable civil penalty; or
- Where alternatives to prosecution are available and a prosecution, though still justifiable, would consume resources that could be better used elsewhere.

As noted in *Raynel*, 'if the public interest in collecting taxes would be better served by a compromise agreement with the taxpayer than by the exercise of the range of enforcement powers available to the Commissioner, such a compromise was regarded as being within the broad managerial discretion of the Commissioner'.[86] IR take relatively few prosecutions: 50 in 2020/21.[87] While prosecution may not be ideal in many of the cases discussed in this article, there are other actions that could be taken, for example taking a decision on insolvency at an earlier date, where a company is involved. This could avoid the protracted court cases that absorb IR resources. Moreover, this would align with the Commissioner's duty to maximise the recovery of outstanding tax under the *TAA 1994*.[88]

In *P v Commissioner of Inland Revenue,* it appears that there was no follow up to ensure the sale of the property as proposed. Furthermore, there appeared to be little by way of assessment of expenditure, otherwise it would have been apparent that the taxpayer's spending would have resulted in an inability to meet his tax obligations. To the extent that a taxpayer receives the benefit of tax write-off due to serious hardship, some further

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[84] Crown Law, 'Solicitor-General Prosecution Guidelines' (Web Page, 2022) <https://www.crownlaw.govt.nz/assets/Uploads/Prosecution-Guidelines/ProsecutionGuidelines2013.pdf>.

[85] Inland Revenue, 'The Commissioner's Public Interest Factors' (Web Page, 2022) <https://www.taxtechnical.ird.govt.nz/en/about/our-prosecution-guidelines>.

[86] *Raynel* (n 5858) [4].

[87] Inland Revenue, *Annual Report Te Tari Taake Pūrongo ā-Tau 2021* (Inland Revenue, 2021).

[88] *TAA 1994* (n 2) s 176.

action should follow to ensure that the taxpayer becomes compliant. In the absence of this, there is unlikely to be any deterrence from the write-off. It is important that there is at least some disadvantage for those who are recklessly non-compliant and then claim serious hardship to avoid tax obligations.

Several taxpayers argued that the Commissioner breached his/her duty under *TAA 1994* s 176 to maximise the recovery of outstanding tax from a taxpayer, by declining to reduce the taxpayer's obligation due to serious hardship.[89] This argument was that the Commissioner would achieve a greater recovery from negotiating with the taxpayer than would be possible in a bankruptcy. To the extent this argument was entertained, it impacts on deterrence.

The serious hardship provisions appear unlikely to meet any of the principles outlined by the Minister. They are not horizontally equitable as all those suffering from hardship cannot take advantage of the serious hardship provisions. They are not vertically equitable, as the provisions are only available to those who have unpaid tax obligations. From the cases examined, economic distortions exist as deterrence is not present when those who decide not to be compliant can potentially benefit from the serious hardship provisions. Furthermore, compliance, or non-compliance is not a factor considered in the first stages of deciding whether financial relief is available.[90] Therefore, taxpayers can be deliberately non-compliant and still apply for tax relief.

V CONCLUSION

In reviewing the serious hardship provisions in the *TAA 1994*, the article questions the extent to which these meet desirable principles in a tax system. The article concludes that those most likely to be suffering from serious hardship are unlikely to be able to take advantage of the provisions and they breach both vertical and horizontal equity. An examination of the case law leads to the conclusion that the serious hardship provisions, at least in some cases, generate administrative inefficiency, with lengthy times for resolution and considerable investment of time and resources into cases where there is unlikely to be a successful collection of tax revenue.

In finding that the provisions do not meet these principles, the question then arises of what will happen to such practices if Minister Parker's proposed *Tax Principles Act* is implemented. Will it result in change so that the legislation has greater alignment with the principles, or does it instead provide for visibility of statutory anomalies? Either of these is likely to be of benefit.

A key limitation of this study is access to data. As explained, there is no visibility on how frequently the serious hardship provisions are used. While we know approximately 14,000 taxpayers per year have debt written off due to serious hardship, we do not know the proportion of serious hardship claims that are accepted or declined. We also do not have insight into IR's internal processes that guide decision making for the serious

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[89] See *Raynel* (n 58) or *Gilchrist* (n 655).

[90] *TAA 1994* (n 2) s 177A(3).

hardship provisions.[91] This restricts further in-depth analysis on the operationalisation of the serious hardship provisions.

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PENDENCY IN THE INDIAN TAX APPEAL SYSTEM

SA MOHAN*

ABSTRACT

Pendency of cases plagues the Indian tax appeal system. Tax cases take anywhere between twelve to fourteen years to get decided if the appeals go all the way to the Supreme Court, the last stage of appeal. This article discusses the views of tax practitioners, former adjudicators, and retired tax officials regarding factors that influence the pendency of tax cases and recommendations on how to alleviate the problem in the context of the Indian tax appeal system.[1] For example, pendency is primarily dependent on case volume, adjournments, delays in filling vacancies in the appellate fora, and uneven tax expertise among adjudicators. While this article discusses pendency issues in India, many of the issues discussed would be relevant to other developing countries and some issues may be pertinent to developed nations also.

Key words: pendency, tax appeals, Indian tax appeal system

I INTRODUCTION

In India, the first level of appeal for taxpayers is before the Commissioner of Income Tax (Appeals) ('CIT(A)'), a quasi-judicial authority staffed by an Income Tax Department ('ITD') official of the rank of a commissioner.[2] The CIT(A), despite being an ITD official, is expected to be independent in so far as their appellate function is concerned.[3] An appeal from the CIT(A) lies before the Income Tax Appellate Tribunal ('ITAT'), which is independent of the ITD and is the second level of appeal for taxpayers and the first level of appeal for the ITD, both against orders of the CIT(A).[4] Unlike the CIT(A) appellate authority, which is staffed by a senior official of the ITD, the ITAT falls under the Ministry of Law and Justice, which is independent of the Ministry of Finance, to which the ITD and the Central Board of Direct Taxes ('CBDT') report.[5] The CBDT is the apex decision making body in India for income tax matters and oversees the ITD. Rulings of the ITAT can be

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1 The author is grateful to the interviewees for their time and thoughts. The views of interviewees are their personal views and do not represent the views of any of the organisations the interviewees worked for in the past. The author is also grateful to an anonymous reviewer for their comments and feedback and to the Editors of the Journal of the Australasian Tax Teachers Association for their support during the article submission process.

2 Deloitte, 'Reducing income tax disputes in India: A way forward' (Deloitte Tax Policy Paper 6, February 2020) ('*Deloitte Tax Policy Paper*').

3 Interview with AA, a former ITAT adjudicator and a retired High Court Judge (Author, online, March 2021).

4 *Deloitte Tax Policy Paper* (n 2).

5 Mukesh Butani, *Tax dispute resolution: Challenges and opportunities for India* (LexisNexis, 1st ed, 2016).

appealed to a jurisdictional High Court, whose decisions can be appealed to the Supreme Court of India, the highest court of the land.[6]

The judicial system in India is known for its inefficient disposal of cases, at least as measured by the time taken by the system to adjudicate cases.[7] In the tax appeal system, the lower judiciary (i.e., fora below the level of High Courts) is replaced by the CIT(A) and the ITAT, quasi-judicial institutions that are structured more along the lines of administrative courts. The functional expertise of the CIT(A) and the ITAT leads to relatively faster adjudication of cases. For example, the CIT(A) takes one to two years on average to adjudicate appeals,[8] while the ITAT takes one to three years on average to adjudicate appeals.[9] The average time taken by High Courts that handle a large portion of the tax appeals, such as the Delhi, Bombay, Madras, and Calcutta High Courts, to dispose of tax cases is over five years.[10] The average pendency in the Supreme Court has been estimated to be around three years.[11] Pendency is therefore more acute at the High Court and the Supreme Court levels.[12] Overall, the 'tax litigation process in India could take 12-14 years (if appeals go up to the Supreme Court) to resolve a tax dispute'.[13]

In this article, the pendency of tax appeals is discussed qualitatively using data from interviews, articles, and reports. Pendency is defined as the 'quality, state, or condition of being pending or continuing undecided'.[14] In the context of this article, pendency refers to the number of cases or appeals pending before the income tax appellate fora in India.[15] A lesser pendency of appeals indicates a more efficient income tax appellate system and vice-versa. This article provides a brief description of the research methodology, followed by a discussion of factors contributing to the pendency of tax appeals. The article concludes with some recommendations for reducing the pendency of tax appeals in India.

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[6] *Deloitte Tax Policy Paper* (n 2).

[7] Harish Narasappa, 'The long, expensive road to justice', *India Today* (online, 27 April 2016) <https://www.indiatoday.in/magazine/cover-story/story/20160509-judicial-system-judiciary-cji-law-cases-the-long-expensive-road-to-justice-828810-2016-04-27>.

[8] *Deloitte Tax Policy Paper* (n 2).

[9] Interview with J, a former ITD official and a retired ITAT adjudicator (Author, online, January 2021); Interview with Q, a tax lawyer practitioner (Author, online, February 2021).

[10] Economic Division, Department of Economic Affairs, Ministry of Finance, *Economic survey 2017-18 Volume II* (Annual Report, Oxford University Press, 30 March 2018) ('*Economic Survey 2017-2018*').

[11] Narasappa (n 7).

[12] Interview with S, a tax accountant practitioner (Author, Online, February 2021).

[13] *Deloitte Tax Policy Paper* (n 2) 7.

[14] Henry Campbell Black, *Black's Law Dictionary* (Thomson Reuters, 10th ed, 2014) 1314.

[15] Gagan Gandhi, 'How To Reduce The Pendency?', *LiveLaw.in* (Opinion, 26 August 2020) <https://www.livelaw.in/columns/how-to-reduce-the-pendency-161988>. 'Pendency refers to the long-pending backlog of the cases in all the Judiciary levels, i.e., The Supreme Court, the High Court, and the District or Subordinate courts'. Ibid.

II RESEARCH METHODOLOGY

This research primarily refers to confidential interviews conducted by the author with former tax officials, tax practitioners, including practising tax lawyers and chartered accountants, and retired adjudicators, including former ITAT adjudicating members, retired High Court judges, and a former Supreme Court judge. More specifically, the 31 interviewees comprise three former High Court judges, eight former ITAT adjudicators, two retired CBDT members, seven former ITD officials, seven tax lawyer practitioners, six tax accountant practitioners, and four tax practitioners with both legal and accountancy qualifications. All interviewees have more than 10 years of experience, with more than three quarters having at least 25 years of experience.

Interviews are the most appropriate data collection method for conducting in-depth research into the views of tax professionals regarding the income tax appellate system in India. All of the interviews were conducted between December 2020 and June 2021 and involved participants located in Bangalore, Chennai, New Delhi, Kolkata, Mumbai, and Hyderabad. The interviews were transcribed verbatim and were coded and analysed qualitatively using NVivo. Semi-structured interviews were used to understand the views of interviewees as this approach allows a researcher to steer an interview in a direction that balances the objectives of the interviewer and the research with the desire of interview participants to share their thoughts. Semi-structured interviews include 'prepared questioning guided by identified themes in a consistent and systematic manner' and are 'interposed with probes designed to elicit more elaborate responses'.[16] The broad themes of the interview guide help researchers direct the interview without influencing participants with direct questions, while the probes help interviewees gather their thoughts and recount details.[17]

III PENDENCY OF APPEALS

Pendency of cases within the judicial system is a major problem in India, with around 40 million cases pending at various levels of the judiciary.[18] Tax cases fare better, relatively. As per a former ITD official, who retired as an ITAT adjudicating member, pendency at the CIT(A) level adds up to around two years of the caseload before that forum.[19] Further, as of February 2020, around 88,000 cases were pending before the ITAT,[20] i.e., less than two years of the ITAT's pre-pandemic appeal disposal rate, given that the ITAT disposed of

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16 Sandy Q Qu and John Dumay, 'The Qualitative Research Interview' (2011) 8(3) *Qualitative Research in Accounting & Management* 238, 246.

17 Ibid 246-47.

18 'National Judicial Data Grid', *NJDG* (Web Page) <https://njdg.ecourts.gov.in/njdgnew/index.php>.

19 Interview with J (n 9).

20 Press Trust of India, '88,000 appeals pending before Income Tax Appellate Tribunal: Chairman', *Business Standard* (online, 26 February 2020) <https://www.business-standard.com/article/pti-stories/88-000-appeals-pending-before-income-tax-appellate-tribunal-chairman-120022601297_1.html>.

around 50,000 appeals in 2019-20.[21] A retired ITAT adjudicator and a senior tax lawyer noted that appeals are heard at the ITAT between six months and three years, depending on the complexity of a case and the location of the bench where an appeal is pending.[22] For example, pendency is more in locations such as Mumbai and New Delhi as cases pending before the Mumbai and Delhi benches add up to a little less than half of the ITAT's total pendency.[23] Still, the ITAT and the CIT(A) are better placed than the judiciary with respect to the pendency of appeals and the time frame for their adjudication. The judiciary disposes of around 10 million cases per year, meaning that its pendency of 40 million cases amounts to around four years of its annual disposal rate,[24] twice that of both the CIT(A) and the ITAT.

Pendency depends on factors such as case volume, adjournments, tax expertise in the appellate fora, the number of vacancies in these fora, and time taken to fill such vacancies. These factors are discussed below, along with other aspects that contribute to pendency of tax appeals.

A *High Case Volume*

One of the reasons for the large pendency of tax cases is the high volume of appeals filed,[25] many of which, according to some tax practitioners, should never have been filed to begin with.[26] A retired member of the CBDT remarked that the ITD routinely files appeals against orders of the CIT(A) and the ITAT and sometimes even against decisions of High Courts.[27] Interviewees note that the ITD files two to three times the number of appeals filed by taxpayers,[28] i.e., around 70-80% of all appeals filed.[29] A retired Chief Commissioner of the ITD said that 50% of the appeals filed by the ITD would be infructuous,[30] and data shows that the ITD does lose a majority of its appeals.[31] Some add

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[21] Letter from Justice Pradeep P Bhatt (President, Income Tax Appellate Tribunal) to Author, 8 June 2021.

[22] Interview with J (n 9); Interview with Q (n 99).

[23] Press Trust of India, '88,000 appeals pending before Income Tax Appellate Tribunal: Chairman' (n 20).

[24] National Judicial Data Grid (n 18).

[25] Interview with M, a former ITAT adjudicator (Author, online, January 2021); Interview with S (n 12).

[26] Interview with U, a tax lawyer practitioner (Author, online, February 2021); Interview with W, a retired ITAT adjudicator (Author, Online, February 2021); Interview with AG, a tax lawyer practitioner (Author, online, April 2021).

[27] Interview with A, a former ITD official and a retired CBDT member (Author, online, December 2020).

[28] Interview with N, a retired ITD official (Author, online, January 2021).

[29] Interview with V, a tax accountant practitioner (Author, Online, February 2021); Interview with Q (n 9); Interview with U (n 26); Interview with Y, a tax accountant practitioner (Author, online, March 2021).

[30] Interview with N (n 28). A retired ITAT adjudicator agreed. Interview with W (n 26).

[31] Interview with AG (n 26); Interview with U (n 26); *Deloitte Tax Policy Paper* (n 2) 12.

that taxpayers also contribute to the pendency of cases by filing meritless appeals or by strategically keeping appeals pending.[32]

The following sub-sections discuss certain aspects that contribute to the high case volume in the income tax appellate system. These include lack of judiciousness of ITD officials, the declining judiciousness of the CIT(A), the declining independence of the ITAT, declining judicial discipline, poor accountability within the tax system, taxpayer strategies, repetitive appeals, and the complexity of tax law.

1 *Lack of Judiciousness of ITD Officials*

Income tax officials' fear of audit and inquiry as well as their overzealousness in collecting taxes and their disregard for precedent contribute to the lack of judiciousness of officials.

(a) *Fear of Audit and Inquiry*

ITD officials often file meritless appeals to avoid being questioned by the ITD or the Accountant General[33] for not filing an appeal against a decision in favour of a taxpayer or to avoid being accused in a vigilance investigation for not appealing such decisions.[34] The fear of audit and inquiry contributes to ITD officials filing appeals almost mechanically,[35] leaving taxpayers to fight them out.[36] For example, ITD officials are particularly insistent on filing appeals when a case involves a large tax demand.[37] This is to avoid a remark from an internal ITD audit or an external Accountant General audit that significant revenue was lost due to ITD officials not filing further appeals in such cases.[38] Consequently, finality is not reached in several cases due to ITD officials not accepting an adverse appellate order until the case is decided by the jurisdictional High Court or, sometimes, by the Supreme Court of India.[39]

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32 Interview with B, a former ITD official and a retired ITAT adjudicator (Author, online, December 2020); Interview with J (n 9); Interview with H, a tax accountant practitioner (Author, online, January 2021); Interview with M (n 25).

33 The Accountant General of India is part of the institution of the Comptroller and Auditor General (CAG) of India, which is a constitutional authority that was established under Article 148 of the Constitution of India.

34 Interview with AG (n 26); Interview with N (n 28); Interview with T, a tax lawyer practitioner (Author, online, February 2021).

35 Interview with N (n 28); Interview with A (n 277). A senior tax lawyer noted that 'as far as [the income tax] department is concerned, nobody wants to say, I won't file an appeal'. Interview with AG (n 26).

36 Ibid.

37 Interview with B (n 322).

38 Ibid.

39 Interview with H (n 32).

(b) *Overzealousness*

Another reason for the filing of meritless appeals by the ITD is the overzealousness, colloquially referred to as 'revenue-mindedness', of ITD officials to assess tax even when there is no legal basis for an assessment.[40] A senior tax lawyer said that, in one case, the ITD raised a tax demand by retroactively applying a law enacted on 1 April 2014 on the guise of the law being clarificatory and persisted with the appeal all the way to the Supreme Court, despite the High Court dismissing the appeal and noting that the law applied prospectively.[41]

Tax practitioners further note that unfair reopening of tax assessments results in the proliferation of litigation,[42] adding that in some cases, 'assessments are reopened only to meet the [revenue] target'.[43] More specifically, practitioners argue that the pressure on tax officials to meet revenue targets results in overzealous tax demands, which taxpayers dispute by filing appeals.[44] Only after protracted litigation do taxpayers secure relief from the appellate fora.[45] Tax officials sometimes even admit to tax demands being made to meet revenue targets and ask taxpayers to instead seek relief in the appellate fora,[46] leading to unnecessary litigation.

Revenue targets seek to hold officials accountable and are used as a performance metric, for example, to determine promotions and career prospects.[47] However, such targets appear to have unintended and undesired consequences in many cases. Senior practitioners assert that, in some cases, 'just to meet revenue targets, … extreme positions are taken by the [ITD]',[48] and that such extreme positions 'will only promote more litigation'.[49] Consequently, practitioners believe that in the absence of unreasonable revenue targets, income tax officials will not have an incentive to take extreme positions and make overzealous tax demands.[50]

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[40] Interview with AG (n 266).

[41] Ibid.

[42] Interview with Z, a tax accountant practitioner (Author, online, March 2021); Interview with AC, a retired ITD official (Author, Online, March 2021); Interview with AG (n 26).

[43] Interview with AG (n 266).

[44] Interview with E, a tax practitioner (Author, online, January 2021); Interview with P, a tax practitioner (Author, Online, February 2021).

[45] Interview with Z (n 42).

[46] Interview with E (n 44); Interview with P (n 444).

[47] Interview with AF, a tax lawyer practitioner (Author, online, April 2021).

[48] Interview with AG (n 266).

[49] Interview with Y (n 29).

[50] Interview with AG (n 26).

(c) *Disregard for Precedent*

The revenue-mindedness of ITD officials to file appeals despite contrary law or precedent also contributes to the filing of meritless appeals. A retired Chief Commissioner of the ITD explained that many ITD officials do not 'understand what a question of law is' and 'even if they understand, they don't want to really follow [the law]'.[51] For example, a former ITAT adjudicator, who retired as a High Court judge, said that in almost every appeal, the ITD argues that 'the findings of [the] tribunal are … perverse, in a mechanical way'.[52] A senior tax practitioner added that officials 'would virtually appeal … everything', because they disregard 'judicial precedents', leading to a 'lot of appeals … being gathered at the ITAT'.[53] Thus, most of the tax appeals filed by the ITD involve issues that have already been decided by the jurisdictional High Court or the Supreme Court, and should not have been filed.[54] The ITD consequently loses such appeals, especially those that disregard Supreme Court precedent.[55]

The following sub-sections consider the prevalence of judiciousness within the appellate fora, the degree of independence of the appellate fora from the government, adherence to judicial discipline within the appellate fora, and the stage at which finality of law is attained.

2 *Declining Judiciousness of the CIT(A)*

The declining independence of appellate authorities is said to contribute to a lack of judiciousness and promote unnecessary litigation, further contributing to the pendency of appeals. The doctrine of separation of powers mandates that the executive and the judiciary should be independent of one another,[56] lest litigants lose faith in an appellate authority that is not independent of the government. A paucity of such faith may result in litigants appealing unfavourable decisions from an appellate authority that is generally perceived to be biased.[57]

For instance, in the 1980s and the 1990s, the CIT(A) was perceived to be judicious.[58] In those days, CIT(A) authorities were knowledgeable and dispassionate and followed the

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51 Interview with N (n 28).

52 Interview with AA (n 3).

53 Interview with K, a tax accountant practitioner (Author, online, January 2021).

54 Interview with T (n 34); Interview with N (n 28).

55 Interview with AD, a retired ITAT adjudicator (Author, online, April 2021).

56 *Rojer Mathew v South Indian Bank Limited* [2020] 6 SCC 1 (Supreme Court of India) ('*Rojer Mathew*'); *Madras Bar Association v Union of India* [2020] SCC Online SC 962 (27 November 2020) (Supreme Court of India) ('*Madras Bar Association 2020*').

57 Interview with M (n 25). The former ITAT adjudicator cited the example of the CIT(A) being perceived as biased in favour of the ITD, leading to taxpayers routinely appealing the CIT(A)'s orders.

58 Interview with Q (n 9).

principles of natural justice.[59] Unfortunately, that perception no longer dominates.[60] Most tax practitioners and retired ITAT adjudicators and even some retired ITD officials feel that the CIT(A), more so in the recent past, tends to err in favour of the ITD despite being an independent authority in so far as their quasi-judicial function is concerned.[61] For example, a senior tax lawyer claimed that some CIT(A) authorities refuse to give relief to taxpayers and instead ask taxpayers to get relief from the ITAT.[62] Also, a senior tax accountant argued that CIT(A) 'authorities now view themselves as an extension of the [tax] assessment authority'.[63]

Moreover, some retired ITAT adjudicators and retired ITD officials note that if there is no jurisdictional High Court precedent on a point of law but instead two conflicting non-jurisdictional High Court views exist, one favouring taxpayers and the other favouring the ITD, CIT(A) authorities generally 'tend to favour the revenue'.[64] Tax practitioners agree that the CIT(A) does not usually adopt precedent favouring taxpayers unless the precedent is that of the jurisdictional High Court or the Supreme Court.[65] Even when there is no conflict among High Court decisions, the CIT(A) generally ignores decisions in favour of the taxpayers.[66]

The CIT(A) is reluctant to deny relief to the ITD when there is no binding precedent[67] despite settled law that when there are two views possible, the view in favour of the taxpayer should be adopted by quasi-judicial authorities such as the CIT(A).[68] The CIT(A) tends to err in favour of the ITD when such interpretation is feasible,[69] even if relief to

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59 Interview with V (n 2929); Interview with W (n 26).

60 Interview with Q (n 9).

61 Interview with B (n 32); Interview with C, a former ITD official and a retired CBDT member (Author, online, December 2020); Interview with E (n 44); Interview with F, a tax lawyer practitioner (Author, online, January 2021); Interview with L, a tax practitioner (Author, online, January 2021); Interview with M (n 25); Interview with N (n 28); Interview with P (n 444); Interview with V (n 29); Interview with Z (n 42); Interview with AD (n 55); Interview with AF (n 47).

62 Interview with Q (n 99).

63 Interview with V (n 29).

64 Interview with J (n 9); Interview with C (n 61); Interview with M (n 25); Interview with AD (n 55). In India, the ITD is colloquially referred to as the 'revenue' (department).

65 Interview with H (n 32).

66 Interview with N (n 28).

67 Interview with J (n 9).

68 *Dalmia Power Ltd. v Assistant Commissioner of Income-Tax*, [2019] 265 Taxman 37 (Madras High Court, India). The Madras High Court observed: "it is settled law that while dealing with the taxing provision, when two interpretations are possible, the Court would interpret the provisions in favour of the taxpayer and against the revenue. In cases of doubt or dispute, the construction should be made in favour of the taxpayer and against the revenue." Ibid. Interview with AD (n 55).

69 Interview with P (n 44).

taxpayers is due, because CIT(A) authorities like to 'play [it] safe'[70] to avoid being suspected by the ITD for inappropriately favouring taxpayers.[71] A senior tax practitioner remarked that 'in the recent years, there has been a fear' among CIT(A) authorities that if relief is given to taxpayers, the CIT(A) would be 'singled out for investigation for corruption'.[72] A senior tax practitioner concluded that the CIT(A) 'is now an institution more for the comfort of the department'.[73]

The waning objectivity and lower judiciousness of the CIT(A) may help the ITD win more appeals at that level but subsequently results in a proliferation of taxpayer appeals at the level of the ITAT, adding to the case volume and the concomitant pendency of tax appeals.

3 *Declining Independence of the ITAT*

Taxpayers consider the ITAT to be an independent appellate forum and the first level within the tax system where taxpayers can secure some justice.[74] The Supreme Court has repeatedly intervened to protect the independence of tribunals such as the ITAT from the government.[75] Most recently, in response to the Government of India's Tribunal, Appellate Tribunal and other Authorities (Qualifications, Experience and other Conditions of Service of Members) Rules, 2017 under *Finance Act 2017* (India) s 184, which changed the composition of the committee to select tribunal adjudicators, the Supreme Court remarked that the rule changes sought to 'keep the judiciary away' from the selection of tribunal adjudicators and struck down the rules as being violative of the doctrine of separation of powers.[76] The Supreme Court also struck down the government's recent rules to reduce the tenure of ITAT adjudicators from that of a permanent position until superannuation of the adjudicators at the age of 62 to, first, a three-year term, and thereafter, a four-year term.[77]

A tax lawyer commented that, of late, the government appears to be influencing the adjudicative functioning of the ITAT to achieve a favourable result in appeals of particular

70 Interview with L (n 611); Interview with C (n 61).

71 Interview with M (n 25).

72 Interview with V (n 29).

73 Interview with Y (n 29).

74 Interview with T (n 34).

75 *L Chandra Kumar v Union of India* [1997] 3 SCC 261 (Supreme Court of India); *Rojer Mathew* (n 56); *Madras Bar Association 2020* (n 56); *Madras Bar Association v Union of India* [2021] SC Writ Petition (Civil) No 502 of 2021 (14 July 2021) (Supreme Court of India) ('*Madras Bar Association 2021*').

76 *Rojer Mathew* (n 56).

77 *Madras Bar Association 2020* (n 56); *Madras Bar Association 2021* (n 75). The rules referred to above are from the Tribunal, Appellate Tribunal and other Authorities (Qualifications, Experience and other Conditions of Service of Members) Rules, 2020, and the Tribunal Reforms (Rationalisation and Conditions of Service) Ordinance, 2021 (specifically, section 184(1), introduced as an amendment to the *Finance Act 2017* (India)).

interest.[78] And some former ITAT adjudicators claim that the government does not want an independent ITAT.[79] In this context, a senior tax lawyer argued that 'the government does not realise … that having an un-independent or an executive tribunal … is self-defeating'.[80] An un-independent ITAT would result in more appeals to the High Courts,[81] further increasing the pendency of tax appeals, as the wait to be heard in the High Courts is even longer.[82]

4 *Declining Judicial Discipline*

Explaining the importance of judicial discipline at the level of High Courts in the context of highlighting the value of certainty in tax law, a senior practitioner said that:

> [T]here was a … good practice in the [past] … where, if a particular High Court had taken a view, other High Courts would generally follow [that view] …, unless there was some strong reservation …. But now, everybody says, who's this … [judge] to tell me? I know the law better …. … I will take my own view, I'm, I'm not bound by it. Why? Because it's my ego at stake versus his. Otherwise, there was a certain comity, you know, that, look, some judge has taken a view, it's not an absurd view, it's a plausible view, it's a possible view, let's follow … [that view in the interest of] uniformity. We are dealing with a central statute, not a state statute. It will have effect … across state borders, let's have uniformity.[83]

The senior practitioner added that a lack of judicial discipline implies a lack of certainty.[84]

The ITAT also suffers from judicial indiscipline.[85] A former ITAT adjudicator and retired High Court judge remarked that, given the importance of certainty, ITAT benches should adhere to the principle of judicial discipline by following the rulings of other benches.[86] Declining judicial discipline adversely impacts the certainty of law and fosters litigation.

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78 Interview with AF (n 47).

79 Interview with X, a former ITAT adjudicator and a retired High Court Judge (Author, online, March 2021); Interview with AA (n 3); Interview with AD (n 555).

80 Interview with AG (n 26).

81 Ibid.

82 Most appeals are decided by the ITAT within three years while the High Courts may take more than five years to decide appeals. Interview with J (n 9); Interview with Q (n 9); *Economic Survey 2017-2018* (n 10).

83 Interview with P (n 44).

84 Ibid.

85 Interview with R, a tax practitioner (Author, Online, January 2021); Interview with T (n 34); Interview with AC (n 42); Interview with N (n 28).

86 Interview with X (n 79).

Another reason for the high pendency of appeals is the leniency that High Courts show in admitting appeals.[87] In theory, High Courts can only admit appeals involving substantial questions of law.[88] In *Sir Chunilal V Mehta & Sons Ltd v The Century Spinning & Mfg Co Ltd*, the Supreme Court laid down criteria for differentiating between substantial questions of law and other questions of law.[89] However, interviewees claim that High Courts liberally admit issues that would not qualify as substantial questions of law, leading to the proliferation of appeals before the High Courts.[90] A retired ITAT adjudicator remarked: 'When in doubt whether a substantial question of law arises or not in a case, the judge would be inclined to admit' the corresponding appeal.[91] This is particularly true of tax appeals as most judges are not well-versed in tax and tax cases form a small minority of their cause list.[92] Liberal admission of non-substantial questions of law results in finality of the contested points of law being postponed and the proliferation of appeals before the High Courts.

The sub-section below describes the dearth of accountability within the tax system, for example, lack of accountability of ITD officials for filing meritless appeals as well as poor accountability of adjudicators for not deciding appeals within a pre-specified time frame.

5 *Poor Accountability within the Tax System*

Tax practitioners, retired ITAT adjudicators, and retired ITD officials argue that there appears to be little accountability within the ITD for filing meritless appeals.[93] Within the ITD, there is said to be a fallacy that filing an appeal does not cost the ITD anything, leading to officials mechanically or routinely filing appeals even where there is no merit.[94] The issue of accountability persists from the level of the assessing officer,[95] who files the appeal, to that of the Chief Commissioner, who either directs or approves the filing of appeals by the ITD.

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87 Interview with Y (n 29); Interview with AD (n 55).

88 *Sir Chunilal V Mehta & Sons Ltd v The Century Spinning & Mfg Co Ltd* [1962] 1962 AIR 1314 (Supreme Court of India); Interview with AB, a former High Court judge and a retired Supreme Court judge (Author, online, March 2021).

89 *Sir Chunilal V Mehta & Sons Ltd* (n 88); Interview with AB (n 88).

90 Interview with Y (n 29); Interview with AD (n 55); Interview with N (n 28).

91 Interview with AD (n 55).

92 Ibid.

93 Interview with M (n 25); Interview with P (n 444); Interview with AD (n 55); Interview with AE, a retired ITAT adjudicator (Author, online, April 2021); Interview with AG (n 266).

94 Interview with N (n 28); Interview with Y (n 29).

95 The 'assessing officer' is the ITD official who makes the original tax assessment in a matter that is on appeal.

Moreover, there is no accountability at the level of the CIT(A) for deciding appeals on time.[96] As there is no time limit imposed on the CIT(A) to adjudicate appeals, sometimes, adjudication may take more than three years, and in a few cases, more than six years.[97] Similarly, there appears to be no accountability within the higher appellate fora, i.e., the ITAT and the courts, to the litigants for deciding appeals within a pre-specified time frame.[98] This contributes to pendency. For example, there are over 90,000 cases pending for more than three decades and over 240,000 cases pending for more than two decades before High Courts.[99] Also, more than a million cases have been pending for more than a decade.[100]

Another reason for the filing of meritless appeals by the ITD in many cases,[101] and by the taxpayers in some cases,[102] is that litigants in India rarely pay costs when they lose an appeal.[103] When litigants do pay costs, usually, only nominal court costs are levied on the losing party rather than the full cost of representation, for example, lawyers' fees.[104] Therefore, the Indian legal system does not hold litigants accountable for filing meritless appeals.

The next sub-section looks at other reasons for taxpayers filing infructuous appeals as well as strategies and actions of taxpayers and their counsel that add to the pendency of matters.

6 *Taxpayer Strategies*

Taxpayers try to overcome precedent by distinguishing, sometimes innovatively, the facts in a case from that of the case establishing the precedent.[105] A senior lawyer pointed out that tax practitioners are paid handsomely to transform even a question of law into a mixed question of fact and law, which is the art of the practice of law.[106] Moreover, a

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96 Interview with Q (n 9).

97 Ibid.

98 Shailesh Gandhi, 'India's huge backlog of court cases is a disgrace – but Covid-19 has provided solutions', *Scroll.in* (Web Page, 28 June 2021) <https://scroll.in/article/998458/indias-huge-backlog-of-court-cases-is-a-disgrace-but-covid-19-has-provided-solutions>.

99 Madan B Lokur, 'What Is Stopping Our Justice System From Tackling the Cases Pending Before Courts?', *The Wire* (online, 12 May 2021) <https://thewire.in/law/india-judiciary-pending-cases-supreme-court>.

100 Ibid.

101 Interview with AG (n 26); Interview with U (n 26); Interview with W (n 26); Interview with N (n 28).

102 Interview with B (n 322); Interview with P (n 44).

103 Interview with AG (n 266); Interview with A (n 277).

104 Interview with A (n 27); Interview with AC (n 42).

105 Interview with W (n 26); Interview with E (n 44).

106 Interview with G, a tax lawyer practitioner (Author, online, January 2021).

former ITD official, who retired as an ITAT adjudicator, argued that taxpayers also file meritless appeals.[107] The retired ITAT adjudicator remarked that some taxpayers try their luck before the ITAT should they be partly unsuccessful before the CIT(A),[108] adding that, 'even if the taxpayer doesn't want to … prolong litigation', their counsel would file an appeal to 'test his luck before the tribunal'.[109] Another former ITD official, who retired as an ITAT adjudicator, said that, in some cases, taxpayers may appeal due to lack of clarity on whether accepting an unfavourable income tax assessment would lead to penalty or prosecution.[110] To counter the threat of penalty and prosecution, taxpayers may file meritless appeals and defer that risk.[111]

Another strategy that taxpayers sometimes adopt is to keep appeals pending before the ITAT by taking adjournments until a High Court passes a judgement in a different case that constitutes favourable precedent to their case.[112] Taxpayers may also keep a matter pending in the hope that the government may launch a dispute resolution scheme that would offer favourable terms for settling a tax appeal that a taxpayer would otherwise have lost.[113] Furthermore, taxpayers who are unable to pay the tax due may file an appeal to secure time to pay the demand as an appeal requires taxpayers to deposit only 20% of the tax owed.[114]

The sub-section below explains some reasons behind the so called 'repetitive appeals', and the impact of repetitive appeals on the volume as well as the pendency of tax appeals.

7 *Repetitive Appeals*

A former ITD official, who retired as an ITAT adjudicator, claimed that around 50% of the tax appeals filed would be repetitive appeals.[115] Repetitive appeals occur when the ITD files appeals involving the same point of law in multiple cases, sometimes, despite legal precedent disfavouring the ITD on that point.[116] In some cases, the ITD may not follow even binding High Court precedent and may continue to file appeals until the Supreme

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[107] Interview with B (n 32).

[108] Ibid.

[109] Ibid.

[110] Interview with J (n 9).

[111] Ibid.

[112] Ibid.

[113] Interview with M (n 25); Interview with H (n 322).

[114] Ibid.

[115] Interview with J (n 9). Another retired ITAT adjudicator concurred. Interview with AE (n 93).

[116] Interview with J (n 9); Interview with T (n 344); Interview with X (n 79).

Court finds against the ITD.[117] This process may take many years.[118] A senior practitioner noted that even when the CBDT accepts a High Court judgement, that decision is not passed down to all ITD officials, resulting in repetitive appeals being filed against even accepted points of law.[119]

Meanwhile, the ITD official makes assessments against the taxpayer even if there is an ITAT order or sometimes a High Court judgement in favour of the taxpayer, leading to the taxpayers disputing such assessments and filing repetitive appeals.[120] Interestingly, *Income Tax Act 1961* (India) ('*ITA 1961*') s 158A offers taxpayers a means to avoid repetitive appeals if they agree to ultimately be bound by the decision of a High Court or the Supreme Court on the point of law disputed in their assessment.[121] However, taxpayers do not appear to opt for this provision, and the ITD does not appear to encourage taxpayers to opt for section 158A either.[122]

8 *Tax Law Complexity*

Senior tax practitioners argue that the complexity of and the uncertainty in tax law contribute to the high volume of cases,[123] and former ITAT adjudicators agree.[124] A tax practitioner said that 'if the laws were simpler', they would lose their 'bread and butter'.[125] A reason for the complexity of law may be poor drafting of tax laws.[126] Also, as a retired ITAT adjudicator suggested, the complexity introduced by frequent amendments may lead to ambiguity in the interpretation of the law and result in its misapplication.[127] For example, tax 'laws are so difficult that even for the judges and lawyers, [it is] difficult to find the correct position of the law' in some situations.[128] A former ITD official, who retired as an ITAT adjudicator, concurred, adding that, sometimes, tax provisions are so

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117 Interview with J (n 9); Interview with T (n 34); Interview with V (n 29).

118 Interview with J (n 9).

119 Interview with Q (n 9).

120 Interview with J (n 9); Interview with S (n 12); Interview with T (n 34).

121 Interview with J (n 9).

122 Ibid.

123 Interview with V (n 29); Interview with L (n 611); Interview with E (n 444).

124 Interview with M (n 25); Interview with W (n 26).

125 Interview with V (n 29).

126 Interview with A (n 277); Interview with AA (n 3).

127 Interview with AE (n 93). A tax practitioner agreed that frequent amendments to tax law contribute to the complexity of and the ambiguity in the tax law. Interview with G (n 10606).

128 Interview with AE (n 93).

complex that ITD officials are unable to understand such provisions properly,[129] resulting in tax disputes.

In this context, a former ITAT adjudicator, who retired as a High Court judge, proposed that 'certainty is more important than simplicity'.[130] Referring to the propensity of the ITD to amend the *ITA 1961* in response to an unfavourable decision of the High Court or the Supreme Court, a former High Court and retired Supreme Court judge said that:

> [If] every time a [judicial] decision … [is published], you amend the [Income Tax] Act, … what is left of the original section is probably not what the original framers thought of. So, there should be more of certainty. If you want to make the tax system effective, what is necessary is that it should be clear, it should be transparent, and [it should be] certain. Otherwise, the taxpayer … [will get] confused, leading to all sorts of litigation.[131]

Senior tax practitioners advise that certainty in tax law 'is valued by a business more than anything else'[132] and agree that 'stability in the law' is 'essential'.[133] However, as a retired ITD official noted, in some cases, the ITD 'needlessly' makes 'amendments where none were required'.[134] A senior tax lawyer agreed and said that 'more than complexity, it is … the frequent changes' which cause more litigation.[135] The senior lawyer gave an example of the finance bill proposing 'a slew of amendments to the *Income Tax Act*' every year.[136]

Tax practitioners also suggest that pendency is partly due to inefficiencies in the Indian tax appeal system.[137] Both taxpayers and the ITD contribute to such inefficiencies. Some of these inefficiencies, including frequent and often unnecessary adjournments granted in tax appeal cases, are discussed below.

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[129] Interview with J (n 9).

[130] Interview with AA (n 3).

[131] Interview with AB (n 88). A former ITD official, who retired as an ITAT adjudicator, and a tax practitioner concurred. Interview with J (n 9); Interview with H (n 32).

[132] Interview with P (n 44).

[133] Interview with Y (n 29). A retired ITAT adjudicator concurred. Interview with AD (n 55).

[134] Interview with N (n 28). A retired ITAT adjudicator agreed and noted that 'frequent tinkering with the [*Income Tax*] *Act* [deprives] the modicum of stability'. Interview with AE (n 93). The retired adjudicator concluded that such frequent 'amendments destabilize the [adjudicatory] system'.

[135] Interview with U (n 26).

[136] Ibid.

[137] Interview with F (n 61); Interview with E (n 44).

B *Adjournments*

A senior tax practitioner noted that delays are sometimes caused due to the 'lethargy' amongst both the ITD and tax practitioners[138] to adjourn matters without good reason. The government has tried to reduce the pendency of cases at the level of the CIT(A) and the ITAT by increasing the number of CIT(A) authorities and the number of ITAT benches,[139] but does not appear to have tried to improve the appellate system's efficiency, for example, by limiting, via law, adjournments.

Adjournments contribute significantly to the pendency of cases.[140] Interestingly, while former ITD officials claim that taxpayers are guilty of taking a lot of adjournments,[141] tax practitioners hold the ITD responsible for taking unnecessary adjournments.[142] Retired ITAT adjudicators are divided on who is more to blame for taking adjournments.[143] A former ITAT adjudicator, who retired as a High Court judge, noted that 'in every case, one party knows that he's going to win … [while the] other party knows [that] he is wrong and he is going to lose'.[144] The retired High Court judge added that 'it is [in] the interest of the losing party to prolong … [the matter] as long as possible'.[145] Regardless, the end result is that litigation is needlessly prolonged and the time of the appellate fora and the non-adjourning party and their counsel is wasted.

Sometimes, adjournments may be taken by a party to shop for a bench of their choice.[146] A retired ITAT adjudicator remarked that earlier, 'know thy law' used to be the rule, but now, 'know thy judges' appears to be the practice, with litigants taking repeated adjournments until a favourable bench hears the appeal.[147] Tax practitioners and retired ITAT adjudicators also note that, at times, the bench itself may prefer to adjourn the case, for example, in long or complex matters.[148] Moreover, adjudicators are generally lenient in granting adjournments,[149] resulting in some fora such as the ITAT issuing instructions

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138 Interview with U (n 26).

139 Interview with A (n 27).

140 Interview with M (n 25).

141 Interview with J (n 9).

142 Interview with AF (n 47).

143 A retired ITAT adjudicator and a former tax practitioner held the ITD responsible for taking adjournments. Interview with W (n 26). But a retired ITAT adjudicator and former ITD official held taxpayers responsible, claiming that taxpayers use adjournments as a strategy. Interview with J (n 9).

144 Interview with X (n 79).

145 Ibid.

146 Interview with V (n 29); Interview with AD (n 555); Interview with AE (n 93); Interview with AF (n 47).

147 Interview with AE (n 93).

148 Interview with W (n 266); Interview with S (n 12).

149 Interview with M (n 25).

to adjudicators that adjournments should not be given in old matters so as to ensure that such cases do not remain pending on the ITAT's docket.[150] Retired ITAT adjudicators suggest that granting of adjournments should be the exception, not the norm.[151] And a retired Supreme Court and former High Court judge advised that courts should be strict, not liberal, in granting adjournments and that adjournments have 'become a disease'.[152]

The next two sections discuss the impact of inadequate tax expertise in courts and the delay in filling vacancies in the appellate fora on the pendency of appeals in the tax system.

C *Inadequate Tax Expertise in Courts*

Retired ITAT adjudicators say that most High Court judges are not well-versed with taxation, necessitating such judges having to familiarise themselves with the subject.[153] For example, a former ITAT adjudicator, who retired as a High Court judge, remarked that a simple matter that is decided 'in 10 minutes in the tribunal … may take three hours in the High Court' because the ITAT is a specialist tax forum, whereas High Court judges are generalists.[154] Therefore, unfamiliarity with tax law may lead to slower adjudication of tax appeals at the level of the High Court, adding to the pendency of tax cases in High Courts. Also, as noted previously, inadequate tax expertise in High Courts often leads to judges admitting tax appeals that do not satisfy the requirement laid down by the Supreme Court that only appeals raising substantial questions of law should be admitted by the High Courts, adding to the pendency.[155]

D *Delay in Filling Vacancies*

Another reason for the pendency of cases in appellate fora is that the government does not promptly fill vacancies in the ITAT, the High Courts, and the Supreme Court.[156] For example, less than 700 of the sanctioned strength of 1080 High Court judges were in place as of May 2021.[157] The Supreme Court has expressed concern regarding dilatory filling of

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150 Interview with T (n 34).

151 Interview with AD (n 55); Interview with AE (n 93).

152 Interview with AB (n 88).

153 Interview with AD (n 55); Interview with AA (n 3).

154 Interview with AA (n 3).

155 Interview with Y (n 29); Interview with AD (n 55).

156 Interview with S (n 122).

157 Madan B Lokur, 'Why Is it So Hard to Fill up the Judicial Vacancies in Our Courts?', *The Wire* (online, 11 May 2021) <https://thewire.in/law/india-judge-vacancies-justice-delivery>.

vacancies in the tribunals[158] and the courts.[159] As a senior practitioner remarked, unless the vacancies in the ITAT and the courts are filled up, pendency will remain a problem.[160] In India, ITAT and High Court adjudicators retire at the age of 62, whereas Supreme Court judges retire at the age of 65. However, the government does not plan recruitment in advance based on the known retirement dates of adjudicators.[161] A senior practitioner noted that 'the process of search, interview, and appointment … takes its own time of at least one to two years, during which time the institution suffers due to the vacancy not being filled up'.[162]

In this context, the Supreme Court made the following observations in a recent case:

> The tribunals which are constituted as an alternative mechanism for speedy resolution of disputes have become non-functional due to the large number of posts which are kept unfilled for a long period of time. Tribunals have become ineffective vehicles of administration of justice, resulting in complete denial of access to justice to the litigant public. … This Court is aghast to note that some tribunals are on the verge of closure due to the absence of … [adjudicators].[163]

The Court explained below the impact of vacancies in tribunals such as the ITAT:

> Existence of large number of vacancies … and the inordinate delay caused in filling them up has resulted in emasculation of the tribunals. The main reason for tribunalisation, which is to provide speedy justice, is not achieved as tribunals are wilting under the unbearable weight of the exploding docket.[164]

The above discussion therefore describes factors that contribute to the pendency of appeals in the Indian tax appeal system. The following section explores some of the recommendations of interviewees to reduce the pendency of cases in the appellate system.

IV RECOMMENDATIONS

Recommendations to reduce the pendency of tax appeals include suggestions of interviewees with regard to decreasing the case volume, enhancing the judiciousness of appellate authorities, improving accountability within the tax system, reducing the

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158 *Madras Bar Association 2021* (n 75).

159 Press Trust of India, '"Give Fixed Time Frame": Supreme Court to Centre on Judge Appointments', *NDTV* (News Report, 16 April 2021) <https://www.ndtv.com/india-news/supreme-court-asks-centre-to-give-fixed-time-frame-on-judge-appointments-2414798>.

160 Interview with S (n 12).

161 Ibid.

162 Ibid.

163 *Madras Bar Association 2021* (n 75) 68.

164 Ibid 76.

uncertainty in tax law, and making the appellate system more efficient by reducing vacancies, improving expertise, limiting adjournments, and improving the productivity of tax hearings.

A *Case Volume*

Interviewees, including retired ITAT adjudicators and judges, tax practitioners, and retired ITD officials, suggest ways and means to reduce the pendency of cases. For example, most interviewees agree that a simple way to dispose of a lot of appeals quickly and reduce the pendency is to bunch tax appeals involving the same point of law and then decide the common issue of law so that all of the corresponding appeals are resolved simultaneously.[165] While bunching of appeals is done sometimes, the initiative depends on the judge involved and there is no systematic process that tags appeals on the same point of law and hears them together. Such tagging may require the implementation of an e-filing system to code and track similar matters. High Courts have already begun transitioning to e-filing systems to adapt to the SARS-CoV-2 pandemic.[166] The ITAT also transitioned to an e-filing system in June 2021.[167] These implementations are expected to facilitate the bunching of tax appeals and reduce pendency.

B *Judiciousness*

An obvious requirement and a mandate of any judicial system is the issuance of speaking orders, i.e., decisions that clearly document the reasoning behind the conclusion arrived at in the case. This mandate is unfortunately not met in a number of tax cases in India. Interviewees recommend better training of appellate authorities to ensure judiciousness and promote speaking orders.[168] For example, CIT(A) authorities may need to be trained to be judicious as their previous role would have involved maximising tax collection for the ITD in an administrative, not a judicial role.[169] Tax practitioners agree with this recommendation.[170]

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165 Interview with AG (n 26); Interview with AB (n 88); Interview with AE (n 93); Interview with S (n 1212).

166 ANI, 'Delhi High Court Inaugurates E-Filing Facility for Applications, Replies', *NDTV* (News Report, 14 June 2020) <https://www.ndtv.com/delhi-news/delhi-high-court-inaugurates-e-filing-facility-for-online-filing-of-applications-replies-2245922>. The pandemic refers to the SARS-CoV-2 pandemic that manifested in 2020.

167 Income Tax Appellate Tribunal, *Launching of e-Filing Portal of Income Tax Appellate Tribunal* (4 June 2021).

168 Interview with B (n 32); Interview with N (n 28); Interview with W (n 26).

169 Interview with N (n 28); Interview with Q (n 9).

170 Interview with K (n 53); Interview with Q (n 9).

On a different note, tax practitioners recommend the appointment of adjudicators of good quality solely based on merit.[171] Such adjudicators would pass speaking orders and may do so efficiently, resulting in fewer appeals arising against their decisions as well as facilitating a reduction in the pendency of appeals. A few tax practitioners suggest that delivery of justice today is dependent on the person meting out the justice and propose the institution of a system to ensure justice regardless of the person judging the case.[172] For example, rigorous processes and safeguards may enable the development of such a system.

Tax practitioners also recommend that revenue targets for ITD officials be done away with to stem unreasonable tax demands and improve the judiciousness of assessments, which would consequently reduce unnecessary litigation.[173] As most of the income tax revenue is collected through tax deduction at source and advance tax collected from taxpayers,[174] doing away with revenue targets may be feasible. For example, tax assessments can perhaps be used more as an audit and deterrence mechanism so that income tax officials are focused on identifying and penalising tax evasion as opposed to simply collecting revenue. If the audit mechanism is rigorous and the deterrence effective, tax collection may automatically improve through regular advance tax collections and tax deductions at source. To ensure that income tax officials properly audit tax returns, tax officials can be assessed on whether errors in the returns have been identified and whether new errors have been introduced by an assessment. These tax assessments can then be independently audited by internal or external audit teams.

C *Tax Law*

Tax practitioners also suggest making tax law less ambiguous so that interpretation of the tax law is consistent and certain.[175] Certainty has been said to be more important than simplicity.[176] A former ITAT adjudicator, who retired as a High Court judge, noted that if 'certainty is there, there'll be no further appeals'.[177] One way to improve certainty is for the ITD to identify test cases and petition for their resolution at the level of the High Court

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[171] Interview with T (n 34); Interview with L (n 61); Interview with AA (n 2); Interview with AD (n 55); Interview with AF (n 477).

[172] Interview with R (n 85).

[173] Interview with AF (n 477); Interview with AG (n 26); Interview with T (n 34).

[174] Depending on the method of calculation, between 82% to 90% of the income and corporate tax revenue is collected via advance tax and tax deduction at source ('TDS'). Sunil Jain, 'Tax raids, and not just on Tapsee Pannu, are a bad idea', *Financial Express* (online, 8 March 2021) <https://www.financialexpress.com/opinion/tax-raids-and-not-just-on-tapsee-pannu-are-a-bad-idea/2208659/>. A former ITD official, who retired as an ITAT adjudicator, similarly noted that 'almost 70 to 80% of the taxes are collected' through advance tax and TDS and that tax assessments contribute to only 10% of the revenue. Interview with J (n 9).

[175] Interview with H (n 32); Interview with AB (n 88); Interview with U (n 266).

[176] Interview with AA (n 3).

[177] Interview with X (n 79).

or the Supreme Court so that interpretation of the law is clear.[178] This can stop the proliferation of appeals on issues covered by the test case.

Certainty can also be improved via strict adherence to precedent by lower authorities.[179] And when High Courts interpret a point of law differently, the Supreme Court can immediately resolve the conflict of law to stem the proliferation of litigation.[180] On the other hand, when there is no conflict, the Supreme Court could let reasonable High Court judgements stand instead of the highest court of the land sitting as a court of first appeal against High Court decisions.[181] This will lead to finality of litigated issues being realised sooner, resulting in reduced litigation and lesser pendency.[182]

Some tax practitioners also recommend that tax law be made simpler,[183] but others believe that tax is inherently a complex subject and that even in OECD countries with well-developed and fairly stable tax systems, tax law remains complicated.[184] However, most tax practitioners agree that amendments to tax law should be made judiciously and sparingly to preserve the certainty of tax law and reduce litigation that would otherwise arise from such amendments.[185]

D *Accountability*

Practitioners and retired ITD officials also recommend the imposition of costs on litigants who file meritless or frivolous appeals.[186] Such court costs are one way to hold litigants accountable.[187] Courts could also award the cost of representation incurred by the winning litigant, apart from court costs, to suitably compensate the respondent who finally prevails.

[178] Ibid.

[179] Interview with K (n 533).

[180] Interview with R (n 85).

[181] Interview with AG (n 266); Interview with F (n 611). Some feel that tax is not a subject that needs to be decided at the Supreme Court and only cases involving constitutional issues should be taken up by the Supreme Court as such issues merit the Court's review. Interview with Y (n 29).

[182] Interview with AG (n 26).

[183] Interview with L (n 611); Interview with U (n 26). One way to simplify tax law is to reduce the number of deductions to further socio-economic objectives, for example, incentives or benefits to certain industries, by offering such incentives or benefits as grants instead. Interview with P (n 44); Interview with S (n 12); Interview with U (n 26); Interview with AC (n 42). But some argue that tax law should be used to meet socio-economic goals. Interview with R (n 85).

[184] Interview with D, a retired ITD official (Author, online, December 2020); Interview with H (n 32); Interview with AC (n 42).

[185] Interview with AG (n 26); Interview with AF (n 47).

[186] Interview with AG (n 266); Interview with AC (n 42).

[187] Interview with AG (n 26).

Also, adjudicators, all the way from the CIT(A) to High Court judges, should be held accountable for delivering orders within a pre-specified time frame. One way to ensure this is to mandate hearing of matters chronologically in the order they are filed, instead of allowing litigants with influence and resources to leapfrog appeals that had been filed much earlier.[188]

E *Adjournments*

Former ITD officials, tax practitioners, retired ITAT adjudicators, and former judges agree that repeated and unnecessary adjournments are a major problem in the tax system.[189] As noted earlier, a former High Court and retired Supreme Court judge remarked that adjournments have become a disease.[190] Some interviewees propose that the number of adjournments given should be limited, for example, not more than three adjournments,[191] and even those should be given in exceptional circumstances when genuine reasons are furnished.[192]

F *Tax Expertise*

Another suggestion from a senior lawyer, a retired ITAT adjudicator, and a retired High Court judge is to improve the efficiency of High Courts by appointing meritorious ITAT adjudicators as High Court judges and leveraging the former's rich tax expertise to better filter out appeals by admitting only matters that raise a substantial question of law.[193] Introducing tax expertise into the benches of High Courts may also shorten the duration of hearings because judges who have tax expertise can quickly grasp and rule on tax issues.[194]

G *Tax Hearings*

In this context, some interviewees propose fixing the duration of arguments made by tax practitioners in a hearing to limit the duration of the overall hearing.[195] This limitation has been suggested because lawyers are known to sometimes read out past judgments

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188 Interview with B (n 32); Interview with Q (n 9).

189 Interview with N (n 28).

190 Interview with AB (n 88).

191 Interview with D (n 184); Interview with L (n 61); Interview with T (n 34).

192 Interview with AD (n 55); Interview with AE (n 933); Interview with AB (n 88).

193 Interview with Q (n 9); Interview with AA (n 3); Interview with AD (n 55).

194 Ibid; Interview with AA (n 3).

195 Interview with B (n 32); Interview with T (n 34).

cover to cover instead of simply citing the relevant facts and the points of law from those cases.[196]

H *Vacancies*

A recent opinion piece by a former Central Information Commissioner of India suggests that if the legal system were to operate with vacancies of no more than 5%, there would be no pendency, or even negative pendency of cases within the legal system.[197] While vacancies should be filled without delay, care should be taken to fill the vacancies with adjudicators who are both experienced in the subject and unimpeachable in character, as flawed appointments may only further impair the certainty and the fairness of adjudication.[198]

V Conclusion

Pendency is a function of high case volume, adjournments, delay in filling vacancies in the appellate fora, and inadequate tax expertise in courts. Case volume is influenced by poor judiciousness of ITD officials, declining judiciousness and independence of some appellate authorities, strategies adopted by taxpayers, repetitive appeals, a dearth of accountability of appellate authorities and ITD officials, and the complexity as well as the uncertainty of law.

A dearth of judiciousness of ITD officials is a significant cause of meritless appeals filed by the ITD. Similarly, the perception that CIT(A) authorities are not judicious leads to taxpayers increasingly filing appeals against the CIT(A)'s orders. For example, the CIT(A) and ITD officials not adhering to judicial precedent reflects poorly on their judiciousness. The paucity of judiciousness within the ITD also leads to repetitive appeals being filed by the ITD as well as the taxpayers. Unfortunately, there is no mechanism to hold either ITD officials or appellate adjudicators accountable for their actions or their delay in acting. All of these factors promote high case volume and pendency within the Indian tax appeal system.

Further, strategies adopted by taxpayers and their representatives in the appellate fora as well as the complexity and uncertainty of tax law add to the case volume and pendency. Pendency is also exacerbated by frequent and unnecessary adjournments sought by both ITD officials and taxpayers, and sometimes facilitated by appellate adjudicators. The delay in filling the vacant posts of adjudicators in the ITAT and the courts as well as inadequate tax expertise on High Court benches also adversely impacts pendency within the tax system.

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[196] Interview with X (n 79).

[197] Shailesh Gandhi (n 98).

[198] Interview with U (n 26); Interview with AA (n 3).

The simplest solutions to reduce pendency include bunching cases involving simple points of law and deciding them together, avoiding repetitive appeals by seeking clarity on a point of law from a High Court or the Supreme Court, ensuring that no more than 5% of adjudicator posts are vacant at each level of adjudication, imposing a limit on the number of adjournments given in a case, and eliminating revenue targets within the ITD. Other long-term solutions include improving the quality of appointments of adjudicators and providing better and periodical training to adjudicators to improve their subject matter knowledge and judiciousness, and instituting systems to hold the adjudicators and ITD officials accountable. Last but not least, ensuring the certainty of both judicial and statutory law cannot only help reduce litigation but also ultimately reduce the need for more adjudicators in the tax system.

This research is mostly based on interviews of lawyer and accountant practitioners, retired ITD officials, former ITAT adjudicators, and retired judges. Other sources include news articles, case law, and reports. As this article is based on a limited number of interviews, the details referred to from the interviews are not conclusive but only indicative. The interviews also do not constitute a random sample and the interview sample is not representative of the groups of tax practitioners, retired ITD officials, former ITAT adjudicators, or retired judges.

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DID NEW ZEALAND GET IT RIGHT? LESSONS FOR THE SOUTH AFRICAN GAAR

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ABSTRACT

Tax avoidance has various harmful effects, one of which is the loss of revenue for governments. While an effective general anti-avoidance rule ('GAAR') may be instrumental in mitigating this risk, there is still uncertainty as to the effectiveness of the current South African GAAR and whether the latest amendments, in 2006, adequately addressed the weaknesses identified in its predecessor. This uncertainty is compounded by the fact that the current South African GAAR has never been subject to judicial enquiry in its entirety. This article seeks to identify potential weaknesses and improvements to the interpretation and application of the South African GAAR through comparison to its New Zealand counterpart.

Keywords: GAAR, general anti-avoidance rule, avoidance, tax, tax avoidance

I INTRODUCTION

Tax avoidance is defined by the Organisation for Economic Co-operation and Development ('OECD') as the arrangement of a taxpayer's affairs with the intention of reducing the taxpayer's tax liability in a legal manner but in contradiction to the law that the arrangement purports to follow.[1] One of the harmful effects of tax avoidance is the loss of tax revenue for governments;[2] it is estimated that the amount of tax revenue lost due to tax avoidance in a single year worldwide could cover the cost of fully vaccinating the world population more than three times against COVID-19.[3] In response to the harmful effects of tax avoidance, governments tend to impose three main anti-avoidance measures: general anti-avoidance rules ('GAARs'), common law, and specific anti-

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1 'Glossary of Tax Terms', *OECD* (Web Page) <https://www.oecd.org/ctp/glossaryoftaxterms.htm>.

2 'Discussion Paper on Tax Avoidance and Section 103 of the Income Tax Act, 1962', *SARS* (Report, November 2005) <https://www.ftomasek.com/DiscussionPaperGAAR20051103.pdf>.

3 *The State of Tax Justice 2021* (Report, November 2021) ('*State of Tax Justice* Report') <https://www.globaltaxjustice.org/sites/default/files/State_of_Tax_Justice_Report_2021_ENGLISH_15-11-2021_v13b.pdf>.

avoidance rules.[4] Some governments use only non-legislative measures such as common law, but South Africa uses all three methods to curb impermissible tax avoidance.[5] The South African GAAR has been the subject of criticism since it was first introduced,[6] and this criticism is compounded by the lack of judicial guidance on the interpretation and application of the GAAR. The South African GAAR contains four elements that must be present for an 'impermissible tax avoidance arrangement'[7] to exist. These are that:

- an arrangement must be present;
- the arrangement must result in a tax benefit;
- the sole or main purpose of the arrangement must have been to obtain a tax benefit; and
- one of the tainted elements must be present.

It should be noted that in order for an arrangement to fall foul of the South African GAAR, all four requirements must be met. While the New Zealand GAAR also encompasses inquiries into an arrangement, the tax motive and the purpose, there is no separate fourth requirement for an inquiry into the 'tainted elements' as in the South African GAAR.

In March 2021 South Africa saw the case of *ABSA and Another v CSARS*[8] ('*ABSA Bank*') as the first reported case on the South African GAAR, fifteen years after its most recent amendment[9] – it remains questionable whether these amendments were sufficient to improve its efficacy after the GAAR was not successfully applied. The amendment to the South African GAAR aimed to address the weaknesses that had been identified and to improve the effectiveness of the GAAR by making changes to existing law.[10]

In summary, the taxpayer (ABSA) had purchased preference shares in a South African entity, which entitled ABSA to receive dividends that were free of tax when declared. These preference shares were invested back-to-back in an offshore trust. The resultant effect of a Double Tax Agreement between South Africa and Brazil was that the dividends received were tax free in both South Africa and Brazil. However, ABSA contended that it was unaware of the intermediation of other entities and the trust and therefore that it could not have participated in an impermissible tax avoidance arrangement. In *ABSA*

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4 AW Oguttu, 'International Tax Law: Offshore Tax Avoidance in South Africa' (2015) 133(2) *South African Law Journal* 456.

5 TM Pidduck, 'The Sasol Oil Case – Would the Present South African GAAR Stand up to the Rigours of the Court?' (2020) 34(3) *South African Journal of Accounting Research* 254 ('Sasol Oil').

6 SARS (n 2).

7 *Income Tax Act 58 of 1962* (South Africa) (*ITA 1962*') s 80A.

8 *ABSA v CSARS* [2019/21825] [2021] ZAGPPHC 127 ('*ABSA Bank*').

9 It is submitted that it is not unusual for a GAAR to remain untested for some time after amendment. For example, the Australian GAAR remained untested for eight years before it was presented before the courts. T Calvert and J Dabner, 'GAARs in Australia and South Africa: Mutual Lessons' (2012) 7(1) *Journal of the Australasian Tax Teachers Association* 53, 56.

10 SARS (n 2). The weaknesses identified included those relating to administrative provisions and, after a number of failures in the courts, those relating to the abnormality and purpose requirements contained in the previous South African GAAR.

Bank, the Court was required to decide whether or not the taxpayer had participated as a 'party' in an 'arrangement', as contemplated in section 80L of the *Income Tax Act 1962* (South Africa) ('*ITA 1962*'), and in deciding that the taxpayer was not party to an arrangement, the Court held that participating in an impermissible arrangement requires a taxpayer to act with volition.[11] The South African GAAR therefore failed on the basis that the taxpayer in *ABSA Bank* had no prior knowledge of and did not wittingly participate in an arrangement to avoid tax.[12] There was brief consideration of the tax benefit requirement but no consideration of the other two requirements of the South African GAAR, being the sole or main purpose requirement and the presence of one or more of the so-called 'tainted elements' (the fourth and final requirement of the South African GAAR, as discussed in section D, below).

As a result of the lack of judicial interpretation on the application and interpretation of the South African GAAR, this article seeks to make two contributions. First, the article analyses and compares the interpretation and application of the South African GAAR with those of the New Zealand GAAR, with the aim of identifying weaknesses in the South African GAAR and lessons that can be learnt from its counterpart in New Zealand. Second, the article applies the South African GAAR to the facts of cases from New Zealand, with the aim of identifying nuances that are only facilitated when practical application occurs. This is particularly relevant in that the South African GAAR has not been subject to judicial interpretation and application in its entirety to date. This second practical component facilitates greater depth of analysis and triangulation across multiple cases in order to make recommendations for improving the South African GAAR.

A multi-method qualitative research design and methodology are undertaken for the purposes of this study in the form of a 'structured pre-emptive analysis'.[13] Structured pre-emptive analysis employs a combination of doctrinal and reform-oriented research methodologies:[14] the doctrinal aspect of the research involves a critical and conceptual analysis of the two GAARs, while the reform-oriented aspect involves an intensive evaluation of the adequacy of the South African GAAR, with the objective of recommending changes.[15] A combination of these approaches facilitates an analysis of convergences between the findings of the doctrinal and reform-oriented research in the form of triangulation, to strengthen validity.[16] Given that this approach is appropriate when legislation has not yet been subject to judicial inquiry, it is justified for the purposes of this study, as there are parts of the South African GAAR that have never been subject to

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11 *ABSA Bank* (n 8) 39.

12 In contrast to 'volition' as contained in the ABSA judgment, for the purposes of the New Zealand GAAR, a taxpayer may still be a party to an arrangement without having knowledge of the intricacies of the tax avoidance steps. Refer to 'A Arrangement' for further discussion and analysis.

13 TM Pidduck, 'Tax Research Methodology for Untested Legislation: An Exemplar for the Tax Scholar' (2019) 33(3) *South African Journal of Accounting Research* 205.

14 Ibid.

15 Ibid

16 Ibid.

judicial enquiry.[17] Further, in order to address the subjectivity and bias that may be involved in selecting the case law, predefined criteria in the form of purposeful maximal sampling is used.[18] In terms of this criteria, preference is given to cases brought before the Supreme Court of New Zealand and the Court of Appeal, given that the decisions of these two Courts set judicial precedent.[19] The cases selected are *Penny v Commissioner of Inland Revenue*[20] ('*Penny and Hooper*'), *Ben Nevis Forestry Ventures Ltd v Commissioner of Inland Revenue*[21] ('*Ben Nevis*') and *Commissioner of Inland Revenue v Frucor Suntory New Zealand Limited*[22] ('*Frucor*'). Admittedly, it may be considered difficult to generalise the outcome of a study that uses cases, but it is argued that the outcome is symptomatic of what is going on more generally.[23]

This article is presented in five parts. Following this introduction, Part II commences with an analysis and comparison of the South African and New Zealand GAARs, with a particular focus on the differences between them. Part II also highlights potential weaknesses of the South African GAAR that may be addressed by lessons learnt from its counterpart in New Zealand. In Part III, the key findings and outcomes of the application of the South African GAAR to the selected cases are discussed. Part IV contains recommendations for improving the efficacy of the south African GAAR, and concluding comments are made in Part V.

II ANALYSIS AND COMPARISON OF THE GAARS

The current South African GAAR is contained in *ITA 1962* ss 80A to 80L and was first introduced in 1941, followed by its latest amendments in 1996 and 2006.[24] The 2006 amendments to the South African GAAR aimed to address the weaknesses identified in order to improve its efficacy.[25] The weaknesses identified by the South African Revenue

[17] Ibid.

[18] W Creswell and JD Creswell, *Research Design: Qualitative, Quantitative, and Mixed Method Approaches* (Sage Publications, 5th ed, 2018).

[19] Ministry of Justice, 'Our New Zealand Court System: Overview of the Appeals Process' *Ministry of Justice* (Web Page, 2021) <https://www.justice.govt.nz/assets/Documents/Publications/our-nz-court-system.pdf>.

[20] *Penny v Commissioner of Inland Revenue* [2011] NZSC 95 ('*Penny and Hooper*').

[21] *Ben Nevis Forestry Ventures Ltd v Commissioner of Inland Revenue* [2008] NZSC 115 ('*Ben Nevis*').

[22] *Frucor Suntory New Zealand Limited v Commissioner of Inland Revenue* [2022] NZSC 113 ('*Frucor*'). It should be noted that the Supreme Court judgment for *Frucor* was only made available on 30 September 2022, despite the Court's having heard the case more than twelve months prior. It is standard practice for the Supreme Court to release judgments within six months of the hearing date (refer *Senior Courts Act 2016* (NZ) s 170(3).

[23] R Gomm, M Hammersley and P Foster, *Case Study Method: Key Issues, Key Texts* (Sage Publications, 2000).

[24] *Revenue Laws Amendment Act 36 of 1996* (South Africa); *Revenue Laws Amendment Act 20 of 2006* (South Africa).

[25] SARS (n 2).

Service ('SARS') are listed below.

- It was not an effective deterrent to impermissible tax avoidance due to its failure to stand up to the rigors of the courts. The inconsistency and ineffectiveness of the South African GAAR resulted in significant time and resources being required to identify and prevent avoidance schemes.
- There were fundamental weaknesses within the abnormality requirement, such as hijacked techniques' – initially developed for *bona fide* business purposes – becoming commercially acceptable when widely used.
- The purpose requirement could only be met if it was proven that the sole or main purpose of a transaction was to obtain a tax benefit, where 'main' had been construed to mean 'predominant', excluding any transactions for which the tax benefit was not the 'predominant' purpose.
- Procedural and administrative issues existed, such as uncertainty relating to the scope of the previous GAAR and whether it could only be applied to a transaction as a whole or to individual steps within a transaction.[26]

Since its amendment in 2006, the South African GAAR, has referred to 'impermissible tax avoidance arrangement(s)', whereas its counterpart, the New Zealand GAAR, refers to 'tax avoidance arrangements'. The South African GAAR contains four elements that must be present for an 'impermissible tax avoidance arrangement' to exist.

- An arrangement must be present.
- The arrangement must result in a tax benefit.
- The sole or main purpose of the arrangement must have been to obtain a tax benefit.
- At least one of the tainted elements must be present. (The transaction was carried out in a manner not normally employed, was lacking in commercial substance, created rights or obligations not normally arising between parties dealing at arm's length, or resulted directly or indirectly in the misuse or abuse of the *ITA 1962*.)

New Zealand lays claim to having legislated the first GAAR in the world, as part of the *Land Tax Act 1878* (NZ).[27] The New Zealand GAAR also later underwent several amendments, which resulted in the current GAAR found in section BG 1 of the *Income Tax Act of 2007* ('*ITA 2007*') – which is supported by definitions in section YA 1 and GA 1.[28] The New Zealand GAAR contains three elements that must be present for a 'tax avoidance arrangement' to exist. Per *ITA 2007* s BG 1, these are:

- the presence of an arrangement;
- the arrangement's having tax avoidance as its purpose or effect, or as one of its purposes or effects; and

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26 Ibid.

27 C Elliffe, 'Policy Forum: New Zealand's General Anti-Avoidance Rule (GAAR) – A Triumph of Flexibility over Certainty' (2014) 62(1) *Canadian Tax Journal* 147; J Tretola 'Comparing the New Zealand and Australian GAAR' (2018) 25(1) *Revenue Law Journal* 1.

28 *Income Tax Act 2007* (NZ) s YA ('*ITA 2007*').

- the tax avoidance purpose or effect's being more than merely incidental.[29]

Section YA 1 defines these terms as follows:

- 'Arrangement' is a 'contract, plan or understanding, whether enforceable or unenforceable, including all steps and transactions by which it is carried into effect.'
- Tax avoidance includes the direct or indirect altering of any income tax; the relief of any person from a lability (or potential or prospective liability) to income tax; or the avoidance, postponement or reduction of income tax liability (or potential or prospective liability).
- 'Tax avoidance arrangement' is an arrangement that has tax avoidance as its purpose or effect, or as one of its purposes or effects provided such purpose or effect is not merely incidental.

A comparison of the two GAARs reveals that both have three requirements, namely an arrangement, a tax benefit or tax avoidance, and an inquiry into the purpose of the arrangement. The South African GAAR, however, contains an additional fourth requirement, while the New Zealand GAAR only contains the three already mentioned. The additional requirement in the South African GAAR is in the form of the so-called tainted elements requirement, which must be present before an arrangement falls foul of the GAAR. It is submitted that the additional fourth requirement and the lengthier nature of the South African GAAR makes it more prescriptive, which may inhibit its successful application when presented before the courts. Conversely, the interpretation of the New Zealand GAAR has been left to the courts in determining whether an arrangement falls foul of the GAAR.[30]

A *Arrangement*

The first requirement for the provisions of both GAARs to apply is the presence of an arrangement. The definitions of arrangement in both jurisdictions are considered to be sufficiently wide to include all actions that may be undertaken to achieve a specific purpose or effect.[31]

Notwithstanding the above similarities between the arrangement requirements of the two GAARs, in *Peterson v Commissioner of Inland Revenue*[32] ('*Peterson*'), the Privy Council

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[29] Ibid s BG 1.

[30] J Cassidy, 'The Duke of Westminster Should Be "Very Careful When He Crosses the Road" in New Zealand: The Role of the New Zealand Anti-Avoidance Rule' (2012) (1) *New Zealand Law Review* 1.

[31] *Meyerowitz v Commissioner for Inland Revenue* [1963] 25 SATC 287 [A]; *BNZ Investments Ltd v CIR* [2009] 24 NZTC 23,582 [HC] ('*BNZ*').

[32] *Peterson v Commissioner of Inland Revenue* [2006] 3 NZLR 433 ('*Peterson*'). This case involved the taxpayer's forming a syndicate to finance the production of feature films within New Zealand that high-rate taxpayers financed, obtaining significant tax advantages through depreciation allowances on the cost of the investment and funding the production of feature films with money borrowed under a non-recourse loan agreement: at [9]. *Peterson* ran counter to the decision made in *CIR v BNZ Investments*

did not spend time defining an arrangement but rather focused on determining whether the taxpayers were parties to the arrangement. The Privy Council noted:

> Their Lordships do not consider that the arrangement requires a consensus or meeting of minds; the taxpayer need not be a party to the arrangement and in their view he need not be privy to its details either.[33]

The principle established in *Peterson*, as well as in *Russell v Commissioner of Inland Revenue*,[34] may be compared to the judgment in *ABSA Bank* relating to the South African GAAR, as the following was held by Sutherland ADJP:

> The section requires a taxpayer to participate or take part. Such conduct requires volition. A taxpayer has to be, not merely present, but participating in the arrangement.[35]

This comparison indicates a weakness in the South African GAAR, as taxpayers may use 'ignorance' as defence to avoid application of the South African GAAR. The efficacy of the South African GAAR may be improved by following a similar approach to New Zealand's in not requiring taxpayers to have prior knowledge or to act with volition.

B *Tax Benefit*

The second requirement of the South African GAAR is the presence of a tax benefit resulting from the arrangement. *ITA 1962* s 1 defines 'tax benefit' as the 'avoidance, postponement or reduction of any liability for tax', while section 80L defines 'tax' as 'any tax, levy or duty imposed by the Income Tax Act or any act administered by the Commissioner'.[36] The Court held in *Smith v Commissioner for Inland Revenue* ('*Smith*')[37]

Ltd [2001] 20 NZTC 17,103 which was a Court of Appeal case where there was initially a requirement that there had been a contract, agreement, plan or understanding to which the taxpayer was a participant, as well as a consensus between the taxpayer and others as to what the result of the arrangement would be. Therefore, the taxpayer did not have to know all the details of an arrangement and the resultant tax avoidance but needed to at least have a broad appreciation of the overall effect. In *BNZ*, Thomas J argued that the definition of 'arrangement' did not require conscious involvement or awareness of the tax avoidance. In *Peterson*, it was held that an arrangement does not require a consensus or the meeting of minds and that a taxpayer neither needs to be party to an arrangement nor has to bear knowledge of the arrangement's details to be affected by it.

[33] Ibid 34.

[34] *Russell v CIR* [2010] 24 NZTC 24,463 ('*Russell*'). In this case, Wylie J reiterated the understanding of consensus with regard to a taxpayer's being party to an arrangement when stating: 'In effect, Mr Russell provided consensus, although I doubt this is a necessary ingredient of any arrangement.' Ibid (102).

[35] *ABSA Bank* (n 8) 39.

[36] *ITA 1962* (n 7) ss 1, 80L.

[37] *Smith v Commissioner for Inland Revenue* [1964] 26 SATC 1 ('*Smith*'). This case involved the taxpayer's establishing a trust to which the taxpayer became a trustee and on whose behalf the taxpayer rendered services. The taxpayer did not receive a salary from the trust for such services, and the net effect of the transactions was the transfer of virtually all income received by the trust to the taxpayer's own account for 'living expenses' for the taxpayer and his family. In the context of tax benefit, it needed to be

that tax benefit in the context of the South African GAAR refers to getting out of the way of, escaping or preventing an anticipated rather than an accrued or existing tax liability. A 'but for' test was also developed in *Smith* and was subsequently applied in *Commissioner for Inland Revenue v Louw*[38] to assist in determining the existence of a tax benefit by asking whether the taxpayer would have suffered tax 'but for' the arrangement.[39]

The second step in applying the New Zealand GAAR involves determining whether the arrangement has a tax avoidance purpose or effect. *ITA 2007* s YA 1 defines 'tax avoidance' as an arrangement that:

> (a) directly or indirectly alters the incidence of any income tax,
>
> (b) directly or indirectly relieves a person from a liability to pay income tax or from the potential or prospective liability to pay any future income tax
>
> (c) directly or indirectly avoids, postpones or reduces any liability to income tax or any potential or prospective liability to future income tax.[40]

This statutory definition of tax avoidance has been criticised for using broad terms that virtually include every possible transaction that reduces tax.[41] Furthermore, paragraphs (a) and (b) of this definition are said to introduce ambiguity, as they could refer to an accrued or a potential liability.[42]

The statutory definitions of 'tax benefit' and 'tax avoidance' seen in the South African and the New Zealand GAAR, respectively, contain similar wording, which indicates that both definitions are intended to apply to arrangements that have the effect of avoiding an anticipated or a prospective, rather than an accrued, liability.[43] It was, however, not the intention of New Zealand's Parliament to provide an exhaustive definition of tax avoidance, and as such, the courts in New Zealand have introduced judicial doctrines which do not require an extensive analysis of the statutory definition before the New Zealand GAAR can be applied.[44] This was illustrated in *Ben Nevis*, where the Supreme Court of New Zealand merely referred to the statutory definition of tax avoidance and

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determined whether these amounts received by the trust could have been regarded as a scheme to avoid income tax by the taxpayer, as contemplated in the previous South African GAAR: ibid [30].

38 *Commissioner for Inland Revenue v Louw* [1983] 45 SATC 113 [A] ('*Louw*'); *Smith* (n 38).

39 In *Louw*, a partnership was converted into a company through an allotment of shares against which the partners' loan accounts were credited, which were free of interest and not taxable in the hands of the directors. The loans were large sums of money amounting to more than double the combined salaries and dividend payouts and were thus considered abnormal.

40 *ITA 2007* (n 28) s YA 1.

41 M Littlewood, 'Tax Avoidance, the Rule of Law and the New Zealand Supreme Court' (2011) (1) *New Zealand Law Review* 263.

42 Ibid.

43 *Commissioner for Inland Revenue v King* [1947] 14 SATC 184 (A); Littlewood, 'Tax Avoidance' (n 43).

44 Cassidy (n 30).

focused on developing a parliamentary contemplation test[45] to assist in determining the presence of tax avoidance.[46]

The parliamentary contemplation test is a two-step process that is adopted in determining the existence of tax avoidance as follows:[47]

- The first step considers the taxpayer's use of the specific provisions of the legislation and whether those provisions have been used in a manner that is consistent with Parliament's intended scope.
- The second step considers the specific provision when viewed in the context of the arrangement as a whole and whether it is apparent that the specific provision has been used in a manner which could not have been within Parliament's contemplation and purpose when it enacted that provision.

In addition to the parliamentary contemplation test, the Court held in *Ben Nevis* that the economic and commercial reality of transactions may also be significant in the test for tax avoidance and considered the following a list of factors that may be relevant in determining the commercial reality of an arrangement and whether the arrangement is 'artificial' or 'contrived':[48]

- the manner in which the arrangement was carried out,
- the role of all the relevant parties and their relationships,
- the economic and commercial effect of documents and transactions,
- the duration of the arrangement,
- the nature and extent of the financial consequences for the taxpayer, and
- the circularity of cash flows.[49]

The above list only serves as guidance to taxpayers as to what will be considered by the courts and is not intended to be exhaustive.[50]

A comparison of the two GAARs reveals that the factors considered by the New Zealand courts in addition to the parliamentary contemplation test are comparable in some

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[45] The parliamentary contemplation test was introduced in *Ben Nevis* but was only applied for the first time in *Penny and Hooper*. Through an analysis of *Penny and Hooper*, it is evident that, while the parliamentary contemplation test provides solid guidance with regards to factors indicating tax avoidance, it is not as straightforward as it appears. The Supreme Court was the only court that unanimously decided in favour of Inland Revenue. *Penny and Hooper*, along with earlier tax avoidance cases (*BNZ, Peterson*) demonstrates the difficulty the courts face when assessing avoidance cases.

[46] T Hwong and J Li, 'GAAR in Action: An Empirical Study of the Transaction Types and Judicial Attributes in Australia, Canada and New Zealand' (2020) 68(2) *Canadian Tax Journal* 539.

[47] Elliffe (n 27).

[48] Cassidy (n 30).

[49] 'Interpretation Statement: Tax Avoidance and the Interpretation of Sections BG 1 and GA 1 of the *Income Tax Act 2007*', *Inland Revenue* (Report, 13 June 2013) <https://www.taxtechnical.ird.govt.nz/-/media/project/ir/tt/pdfs/interpretation-statements/is1301.pdf?la=en> ('Interpretation Statement: BG 1 and GA 1 of the *Income Tax Act 2007*').

[50] C Elliffe and JM Cameron, 'The Test for Tax Avoidance in New Zealand: A Judicial Sea-Change' (2010) (16) *New Zealand Business Law Quarterly* 440.

respects to the so-called 'tainted elements' and the indicators of lack of commercial substance contained in the South African GAAR (these elements and indicators are discussed in section D, below). However, some of the factors seen in New Zealand are not contained in the South African GAAR, and it is submitted that the efficacy of the South African GAAR may be improved by the incorporation of these factors into the current tainted elements. Further comparison reveals that while the New Zealand GAAR considers these factors as part of the test for tax avoidance, the South African GAAR contains the tainted elements and indicators as a separate fourth requirement which results in a lengthier and more onerous GAAR. It is also submitted that having the tainted elements as a separate requirement creates a weakness in the South African GAAR, since the courts may fail to successfully apply the GAAR to transactions that result in a tax benefit if at least one of the tainted elements is not met. Therefore, the South African GAAR may be improved by including the tainted elements and the indicators of lack of commercial substance as part of the inquiry of the tax benefit requirement or in a manner that is similar to that of the parliamentary contemplation test as applied in New Zealand.

C *Sole or Main Purpose*

The third requirement of both GAARs involves an inquiry into the purpose of an arrangement. The South African GAAR requires that the sole or main purpose of the arrangement must be to obtain a tax benefit, while the New Zealand GAAR requires the arrangement to have a tax avoidance purpose or effect. In applying the New Zealand GAAR, once it has been determined that the arrangement has a tax avoidance purpose or effect, it must be considered whether that purpose or effect is more than merely incidental.[51]

In the South African GAAR, the sole or main purpose requirement is retained from its predecessor, and therefore, the judicial precedent set under the previous GAAR can be extended to understanding the sole or main purpose requirement in the context of the current GAAR.[52] *ITA 1962* s 80G allows the Commissioner to make a rebuttable presumption that the sole or main purpose requirement of the arrangement was to obtain a tax benefit, unless the taxpayer produces affirmative and conclusive evidence to the contrary.[53] Some commentators are of the view that the evidence produced by the taxpayer to this effect may not be accompanied by the taxpayer's stated intentions or assertions, making this an objective assessment,[54] but notwithstanding these views, South African courts illustrated in *Secretary for Inland Revenue v Gallagher*[55] and in *Secretary for*

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51 Tretola, 'Comparing the New Zealand and Australian GAAR' (n 30).

52 AP de Koker and RC Williams, *Silke on South African Income Tax* (LexisNexis, 2021); TM Pidduck, 'The South African General Anti-Tax Avoidance Rule Lessons from the First World: A Case Law Approach' (PhD Thesis, Rhodes University, 2017) ('ZA GAAR').

53 Ibid.

54 de Koker and Williams (n 52).

55 *Secretary for Inland Revenue v Gallagher* [1978] 40 SATC 39 [A]. This case involved taxpayers who sought short-term investments with the aim of yielding the highest returns. This particular short-term

Inland Revenue v Geustyn Forsyth and Joubert[56] ('*Geustyn*') that the sole or main purpose requirement is a subjective test which requires the courts to take cognisance of the taxpayer's stated intention. These opposing views create a weakness in the South African GAAR, as there is uncertainty regarding the application of this requirement due to its use of wording that is similar to that of its predecessor.[57]

In the context of the New Zealand GAAR, the words 'purpose' and 'effect' are said to pose an interpretive difficulty, as they are not defined in the *ITA 2007*.[58] They were interpreted in *Ashton v Commissioner of Inland Revenue*,[59] where it was held that they are intended to refer to the end result achieved by an arrangement and not to the motive of the taxpayer. Although the courts in New Zealand see this as a subjective test, the presence of some objective factors is likely to inform the court's decision; for example, the Supreme Court considered a statement made by the taxpayer in *Ben Nevis* when determining the purpose of the arrangement.[60]

It is evident that there are opposing views in both the South African and New Zealand jurisdictions regarding whether the test for purpose is objective or subjective, and further guidance is required. It is submitted that clarifying that the sole or main purpose requirement is an objective test may go some way in improving the efficacy of the South African GAAR and in reducing ambiguity in its interpretation.

The concept of 'merely incidental' is not defined in the *ITA 2007*, but it was held in

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investment involved the proposed floating of shares, where a private company is converted to a public company by issuing shares to the public as a form of financing instead of using company funds to fund the company's expansion. The intention of the taxpayers was considered, and it was determined that the investment (made in the Cook Islands) was chosen for its high returns and was chosen over other alternatives, but when calculating the return on investment, it became evident that the tax consequences were a 'consideration'. The interest rate in the Cook Islands was lower than that offered in Australia, with the only significant difference in returns being that which resulted from the tax consequences.

[56] *Secretary for Inland Revenue v Geustyn Forsyth and Joubert* [1971] 3 ALL SA 540 [A] ('*Geustyn*'). This case involved an unlimited liability company that took over a partnership, where the three former partners became the sole directors who each held equal shares in the company. Each former director was employed by the company at an annual salary of ZAR10,000, and a payment of ZAR240,000 in respect of goodwill was payable to the partnership. No service contracts were signed with the former partners, nor was there any form of guarantee for the payment of the goodwill. The ZAR240,000 goodwill payment was credited to loan accounts of each partner in equal shares. Each partner received an annual salary lower than the agreed upon amount of ZAR10,000, and ZAR29,136 would have been payable by the company in normal tax. The Secretary for Inland Revenue applied the South African GAAR at the time and allocated the company's taxable income to the former partners in equal shares, resulting overall in no taxable income being reflected on the company's assessment.

[57] Pidduck, 'ZA GAAR' (n 52).

[58] C Atkinson, 'General Anti-Avoidance Rules: Exploring the Balance between the Taxpayer's Need for Certainty and the Government's Need to Prevent Tax Avoidance' (2012) 14(1) *Journal of Australian Taxation* 1.

[59] *Ashton v Commissioner of Inland Revenue* [1975] 2 NZLR 717 [PC].

[60] *Ben Nevis* (n 21).

Challenge Corporation Ltd v Commissioner of Inland Revenue[61] that a tax avoidance purpose would be considered merely incidental if it arose as a concomitant of a non-tax avoidance purpose or effect. Consequently, tax avoidance must arise naturally, without artificiality or contrivance, since artificiality and contrivance are likely to indicate that the tax avoidance purpose or effect is more than merely incidental.[62]

The 'merely incidental' requirement of the New Zealand GAAR may be contrasted with the 'sole or main purpose' requirement of the South African GAAR: the words 'merely incidental' in the New Zealand GAAR create a lower threshold for purpose, since the tax avoidance purpose need only be more than incidental. This indicates that it may be easier for arrangements with a dual purpose to fall foul of the New Zealand GAAR, even if the tax avoidance purpose is not the main or dominant purpose. In South Africa, the Court considered an arrangement that served a dual purpose in *Commissioner for Inland Revenue v Conhage (Pty) Ltd*[63] ('*Conhage*') and held that a taxpayer may choose a transaction which attracts the least amount of tax. This principle reveals a weakness in the South African GAAR, because following *Conhage*, taxpayers argued that merely referring to a commercial purpose was sufficient to prevent the Commissioner from successfully applying the GAAR.[64] This comparison indicates the possibility of improving the efficacy of the South African GAAR by including a 'merely incidental' test as opposed to the more onerous sole or main purpose test.

D *Tainted Elements*

The fourth and final requirement of the South African GAAR is for the arrangement to be characterised by at least one of the four tainted elements contained in *ITA 1962* s 80A. The Commissioner may rely on the non-exhaustive list of guidelines and definitions contained in *ITA 1962* ss 80C to 80E when proving that an arrangement is tainted by one of these elements.[65] In comparison, the New Zealand GAAR does not structurally have a fourth requirement, as the factors that may be considered comparable to the tainted elements in the South African GAAR are considered part of the parliamentary contemplation test in the New Zealand GAAR. It is submitted that the additional requirement contained in the South African GAAR makes it more prescriptive, which may limit its successful application. It is therefore also submitted that considering the additional factors as part of the parliamentary contemplation test is more effective and that the South African GAAR

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61 *Challenge Corporation Ltd v Commissioner of Inland Revenue* [1986] 2 NZLR 513.

62 Inland Revenue, 'Interpretation Statement: BG 1 and GA 1 of the *Income Tax Act 2007*' (n 53).

63 *Commissioner for Inland Revenue v Conhage (Pty) Ltd* [1999] [4] SA 1149 ('*Conhage*'). This case involved a sale and leaseback of a manufacturing plant and equipment. The Commissioner contended that there was no real intention for ownership to pass, even though the parties had thought the agreements sufficient to procure the tax benefits. Ibid [3].

64 SARS (n 2).

65 BT Kujinga, 'A Comparative Analysis of the Efficacy of the General Anti-Avoidance Rule as a Measure Against Impermissible Income Tax Avoidance in South Africa' (LLD Thesis, University of Pretoria, 2013) 111.

may be improved by following a similar approach in including the tainted elements as part of the tax benefit requirement. The tainted elements are discussed individually below but are summarised as follows:

- abnormality,
- lack of commercial substance,
- the creation of non-arm's length rights and obligations, and
- misuse or abuse of the *ITA 1962*.[66]

1 *Abnormality*

Despite receiving criticism under the South African GAAR's predecessor, the abnormality element is still a requirement of the current GAAR, meaning that the current GAAR may have likewise inherited some of its predecessor's weaknesses.[67] The weakness identified in the abnormality element is that transactions cease to be abnormal if they become commercially acceptable, as more taxpayers enter into similar transactions, resulting in the inefficacy of the GAAR.[68] Furthermore, contrary to its predecessor, the current test for abnormality is intended to be an objective rather than a subjective assessment.[69]

With the exception of the *Income Tax Case* 1712 [2000] 63 SATC 499,[70] where it was held that the abnormality element requires a comparison between a normal transaction and a transaction entered into for *bona fide* business purposes, there is currently no guidance on what constitutes a normal transaction, and this could lead to inconsistent judicial decisions that undermine the efficacy of the GAAR.

The abnormality requirement of the South African GAAR may be comparable to considering the manner in which an arrangement is carried out in the context of the New Zealand GAAR. Considering the manner in which an arrangement is carried out assists in determining what is achieved economically and commercially with the arrangement by examining the particular way it is structured and whether it has features that differ from usual commercial practice.[71] Given the lack of guidance regarding the application of the abnormality element in the South African GAAR, it is submitted that considering the manner in which a transaction is carried out may improve the efficacy of the South African GAAR by providing guidance on the application of the abnormality element.

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[66] T Calvert, 'An Analysis of the 2006 Amendments to the General Anti-Avoidance Rule: A Case Law Approach' (MCom Mini Dissertation, North West University, 2011) 28-29.

[67] SARS (n 2).

[68] Ibid.

[69] de Koker and Williams (n 52).

[70] *Income Tax Case* 1712 [2000] 63 SATC 499. This case involved a lease of tank containers with a view to sub-lease them. The rentals payable within the first two years made up the bulk of the total rental payment, and it was found that the transaction was abnormal due to the uneven spread of rental payments and the resultant excessively high tax deductions in the first two years.

[71] *BNZ* (n 31).

2 *Lack of Commercial Substance*

Lack of commercial substance applies to transactions entered into in a business context. It is generally defined in *ITA 1962* s 80C(1) as an avoidance arrangement that results in a significant tax benefit without having a significant effect on the business risks or net cash flows of the parties involved.[72] However, the *ITA 1962* does not provide any guidance on what constitutes a 'significant effect upon business risks or net cash flows' or a 'significant tax benefit' and as a result, a level of subjectivity may therefore arise when interpreting this definition.

The general test for lack of commercial substance per the South African GAAR may be considered similar in some respect to the nature and extent of financial consequences for the taxpayer, as well as transactions where the investor incurs no risk, in the context of the New Zealand GAAR. Unlike the South African GAAR, the factors contained in the New Zealand GAAR, such as the test for the nature and extent of financial consequences for the taxpayer and transactions where investors incur no risk, do not contain terms such as 'significant business risks' or 'significant tax benefit'. It is submitted therefore that the test used in New Zealand GAAR is preferable and should be adopted for the South African GAAR, as it is simpler and thus leaves it to the courts to determine whether the financial consequences suffered by the taxpayer are ones that can be expected from such an arrangement, without referring to problematic terms such as 'significant'.

ITA 1962 s 80C(2) contains a list of factors that are indicative of an arrangement that lacks commercial substance.[73] The list is non-exhaustive, and the factors given are intended to serve as guidelines when determining whether an arrangement lacks commercial substance. These indicators are discussed individually below:

(a) *Substance over Form*

The *ITA 1962* does not provide any guidance for determining whether an arrangement's legal substance differs from its legal form. While this indicator is derived from the common law doctrine of substance over form, in the context of the GAAR it is intended to be given a wider meaning.[74] The common law substance over form test determines whether the legal form of an arrangement is consistent with the true intentions of the parties to that arrangement and whether the risks and rewards are consistent with those that can be expected from the arrangement.[75] The recent case of *Sasol Oil v CSARS*[76] applied the previous South African GAAR, and the judgment in this case indicates that determining whether the substance of a transaction differs from its legal form is

[72] *ITA 1962* (n 7) s 80C(1).

[73] Ibid s 80C(2).

[74] National Treasury, 'Explanatory Memorandum on the Revenue Laws Amendment Bill' (Explanatory Memorandum, National Treasury, 2006).

[75] de Koker and Williams (n 52).

[76] *Sasol Oil v CSARS* [2018] ZASC 153 [A].

subjective.[77] The subjectivity involved in this test creates uncertainty regarding the application of the South African GAAR.[78]

(b) *Round-trip Financing*

This involves the deceptive use of funds in a circular manner between parties to an arrangement.[79] Round-trip financing is defined in *ITA 1962* s 80D, and the definition includes words such as 'among', 'between', 'reduce', 'offset', 'eliminate' and 'significant business risk'.[80] These terms have neither been defined in the *ITA 1962*, nor have they been judicially interpreted, which could raise uncertainties regarding the correct interpretations and applications thereof.

Considering the circularity of cash flows within an arrangement in the context of the New Zealand GAAR may be considered similar to the round-trip financing indicator of lack of commercial substance in the South African GAAR. However, for the purposes of the South African GAAR, an arrangement can only be tainted by the presence of round-trip financing if it meets the requirements listed in *ITA 1962* ss 80D(1)(a) and 80D(1)(b), while the New Zealand GAAR does not include a prescribed list of requirements that need to be met before the circularity of cash flows is considered present in an arrangement. It is submitted that to improve the efficacy of the GAAR, South Africa should follow an approach similar to New Zealand's in not providing a prescriptive definition of round-trip financing, leaving it to the courts to determine whether a transaction is tainted by this indicator's presence.

(c) *Accommodating or Tax-indifferent Parties*

The presence of an accommodating or tax-indifferent party within an arrangement is another indicator of an arrangement that lacks commercial substance. The use of accommodating or tax-indifferent parties within an arrangement is usually intended to defeat the balance between tax deductibility in the hands of one party and taxable income in the hands of another.[81]

In addition, section 80E(3)(b) excludes a foreign business establishment in terms of *ITA 1962* s 9D(1) from being a tax-indifferent party.[82] *ITA 1962* s 9D is an anti-avoidance section that requires the income of a resident to include a proportional amount of a foreign company's net income where that foreign company is controlled by the resident.[83] The exclusion of foreign business establishments from the definition of accommodating or tax-indifferent parties is problematic, because the use of Controlled Foreign Companies in the context of multinational enterprises is not unusual and creates the opportunity for

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[77] Pidduck, 'Sasol Oil Case' (n 5).

[78] Ibid.

[79] Kujinga (n 65).

[80] *ITA 1962* (n 7) s 80D.

[81] SARS (n 2).

[82] *ITA 1962* (n 7) ss 9D(1), 80E(3)(b).

[83] Ibid s 9D.

multinational enterprises to use these entities in such a way as to comply with *ITA 1962* s 9D but avoid tax.[84]

The accommodating or tax-indifferent parties indicator may be considered similar to considering the roles of all relevant parties and their relationships with the taxpayer in the context of the New Zealand GAAR. This factor from the New Zealand GAAR was considered in *BNZ Investments Ltd v CIR*,[85] where a tax benefit was split between unrelated parties. A comparison of the two GAARs reveals that the South African GAAR contains a prescriptive definition for an accommodating or tax-indifferent party, while the New Zealand GAAR leaves it to the courts to ascertain the roles of all relevant parties to an arrangement. It is submitted that the test used for the purposes of the New Zealand GAAR is less restrictive and may be adopted to improve the efficacy of the South African GAAR.

(d) *Offsetting or Cancelling Effects*

The presence or inclusion of elements that have the effect of offsetting or cancelling each other is an indicator contained in *ITA 1962* s 80C(2)(b)(iii), which uses words that have neither been defined nor interpreted by the courts, such as 'offsetting each other' and 'cancelling each other'.[86] It is submitted that defining these words may provide guidance on how they should be applied in the context of the GAAR.

3 *Rights or Obligations Not at Arm's Length*

ITA 1962 s 80A(c)(i) provides a third tainted element that must be considered in any context.[87] The section provides that an avoidance arrangement would be tainted if it had created rights and obligations not normally created between parties dealing at arm's length; however, the *ITA 1962* does not provide any guidance on how the concept of 'arm's length' should be interpreted in the context of the GAAR. The section also contains words such as 'normal', which are not defined. The concept of 'arm's length' was considered in *Geustyn*[88] in determining what unconnected persons would have agreed upon in the same situation. The efficacy of the South African GAAR may be improved by defining the concepts of 'arm's length' and 'normal'.

4 *Misuse or Abuse of the Act*

The 'misuse or abuse' element was not present in the South African GAAR's predecessor, and thus, the terms are neither defined in the *ITA 1962*, nor have they been interpreted by the courts. Consequently, uncertainty is created in the interpretation and application of this provision. While the South African GAAR makes use of a separate requirement for

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[84] Pidduck, 'Sasol Oil Case' (n 5).

[85] *BNZ* (n 31).

[86] *ITA 1962* (n 7) s 80C(2)(b)(iii).

[87] Ibid s 80A(c)(i).

[88] *Geustyn* (n 61).

the tainted element of misuse or abuse of the Act, which results in a lengthier and more complex GAAR, the New Zealand GAAR includes consideration for misuse of the legislation as part of the parliamentary contemplation test by considering whether a specific provision has been used in a manner that is consistent with Parliament's contemplation and purpose when Parliament enacted that provision.[89] It is submitted that the misuse or abuse of the Act element in the South African GAAR should form part of the tax benefit requirement.

In the next part of this article, the South African GAAR is applied to the facts of New Zealand cases with the aim of identifying nuances that are only facilitated when practical application occurs.

III APPLICATION OF THE SOUTH AFRICAN GAAR TO NEW ZEALAND CASES

Before the South African GAAR is applied to the selected New Zealand cases in order to identify further weaknesses, the facts of the cases are briefly discussed below.

A *Penny and Hooper*

Mr Penny and Mr Hooper were two orthopaedic surgeons who each practiced in their own separate capacity, and all of the income generated by their respective practices was personal income. Shortly after the personal income tax rate in New Zealand increased from 33% to 39% on 1 April 2000, the taxpayers adopted a structure to reduce their personal incomes. Each sold his practice – from which each earned substantial income – to a different incorporated company and became an employee of the company as well as the company's sole director. Although each of the taxpayers had different circumstances, both had common features: a company registration of which the taxpayers were the sole directors and the fact that the shares of each company were held by a family trust.

The Commissioner of Inland Revenue contended that the actions of Penny and Hooper amounted to tax avoidance and subsequently made assessments increasing the taxable income of the taxpayers for the tax years ending 31 March 2002, 2003 and 2004 by an amount equal to the difference between the salaries actually paid and what the Commissioner assessed as commercially realistic salaries for their services. The Commissioner contended that the actions considered were the creation of the company-trust structures, together with the reduced incomes, in totality and the cumulative effect thereof.[90] After investigations by the Commissioner began, Hooper and Penny declared larger salaries, reflecting the actual salaries earned, to avoid any penalties going forward if the Commissioner's view prevailed.

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89 Elliffe and Cameron, 'Test for Tax Avoidance' (n 50).

90 Ibid 12.

B *Ben Nevis*

The taxpayers in *Ben Nevis* were investors in a 50-year forestry investment syndicate that was involved in the development of a forest that was expected to be harvested in 2048. The taxpayers entered into a license agreement for the occupation of the land to be used for the development of the forest. Part of this agreement required the taxpayers to pay a license premium per hectare as well as an insurance premium at the end of the agreed license period to protect the taxpayers in the event of a shortfall in the net proceeds from the sale of the forest. The taxpayers claimed annual tax deductions for the insurance premiums and the license premium, amortised over a period of 50 years, even though the actual cash flows were only set to take effect in 2047.[91] The Commissioner argued that the taxpayers had taken an abusive tax position and that the GAAR was applicable.

C *Frucor*

In *Frucor*, Danone Asia Pty (Ltd) subscribed for equity shares in Frucor Suntory New Zealand Limited; however, this subscription was effectively structured as a loan from Deutsche Bank in order for Frucor to obtain a tax benefit in the form of tax-deductible interest. The loan was structured in an artificial and contrived manner, where the interest was, in substance, repayment of principal and interest to Deutsche Bank. During September 2020, the New Zealand Court of Appeal ruled in favour of the Commissioner and found that the arrangement entered into was a tax avoidance arrangement to obtain a tax benefit through the interest deductions claimed by Frucor when the arrangement should have been treated as an equity subscription. Both parties (Frucor and the Commissioner) appealed to the Supreme Court, and during September 2022, Frucor's appeal on the tax avoidance was dismissed. As a result, the arrangement remains subject to the provisions of *ITA 2007* s BG 1.[92]

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[91] Ibid.

[92] The Supreme Court did, however, allow the Commissioner's cross-appeal on the shortfall penalties. See (n 23).

D *Application of the GAAR*

The South African GAAR was applied to the facts of the above three cases, and the findings are summarised using the framework in Table 1 below.

Table 1: Framework for applying the GAAR to the facts of the court cases

Framework	***Penny***		***Ben Nevis***	***Frucor***
	Penny	**Hooper**		
1 – Is there an arrangement?	Yes	Yes	*	Yes
2 – Does the transaction/operation/scheme result in a tax benefit?	Yes	Yes	Yes	Yes
3 – Is the sole or main purpose to obtain such a tax benefit?	Yes	*	Yes	*

** Indicates that significant doubt exists as to the efficacy of the South African GAAR for this component of the GAAR.*

Based on the application of the South African GAAR to the above court cases, the following weaknesses were identified that may render the South African GAAR an ineffective deterrent to impermissible avoidance arrangements:

1 *Arrangement*

It is likely that an arrangement was present in all three cases. However, the arrangement in *Ben Nevis* included the incorporation of an insurance company (CSI Insurance) in the British Virgin Islands to which the insurance premiums were to be paid by the taxpayers at the end of the license agreement. The taxpayers in *Ben Nevis* argued that because they were not aware of the contents of CSI Insurance's business plan, they were not party to this step of the arrangement. In light of *ABSA Bank*, this reveals a weakness in the South African GAAR in instances where the Commissioner decides to apply the GAAR to steps within an arrangement, as taxpayers may argue that they were not aware of the particular step that is considered contrary to the GAAR by the Commissioner. It is submitted that the definition of a party to an arrangement should be amended to ensure that a taxpayer cannot use ignorance as a defence against the South African GAAR.

2 *Sole or Main Purpose*

It likely that the sole or main purpose of the arrangements in all three cases was to obtain a tax benefit. However, the following evidence was provided by the relevant taxpayers:

- The stated intention of the taxpayers, Hooper and Penny, was evident from *Penny and Hooper* when it was noted that both taxpayers said under cross-examination that the restructuring of their practices was 'because of a concern about exposure to medical negligence claims which might not be covered by the accident compensation scheme'. However, Penny only reduced his income (income from the practice compared to the salary he earned from the company) once the tax rate

changed in 2000, and therefore, the objective factors did not support Penny's stated intention.

- The stated intention of the taxpayers in *Ben Nevis* was evident from a statement made by Dr Muir, who was responsible for designing the arrangement, regarding the incorporation of CSI Insurance:[93] '… the real benefits of the deal are the tax concessions that can be obtained now by the investors and the foundation. One of the conditions required to gain the tax relief is that the insurance must be in place. The actual outcome of the deal in 50 years' time is not considered material.' The objective factor that supported this stated intention was the fact that the financial services company that assisted in incorporating CSI Insurance advertised its own services as providing clients with opportunities to 'reduce, defer and avoid taxes',[94] and Muir was aware of this fact.
- Frucor argued that its stated intention for the arrangement was the legitimate refinancing of a subsidiary in New Zealand. Stanley Marcello Jr, the Senior Director of Tax for Danone North America, gave several objective factors in support of this stated intention, suggesting several reasons why the transaction may have been entered into (apart from achieving the tax benefit).[95] These reasons were cash accumulation/retention benefits, future expanded capital base, Singaporean tax treatment, lower fixed interest rate funding for Frucor, local currency funding and an improved debt/equity ratio for Frucor. The purpose of the arrangement was, however, confirmed by Danone in a document stating that the point of the scheme was to allow Danone Asia Pty Ltd to finance the purchase of Frucor in a manner that would entitle it to tax credits.[96]

On a balance of probabilities, it is likely that the objective effect did not support the stated intention of the taxpayers, as is evident in the three cases discussed above. Nevertheless, in light of *Conhage*, if the taxpayers were able to provide a commercial reason for entering into the arrangements, this would have resulted in the sole or main purpose requirements' not being met. The efficacy of the South African GAAR may be improved by following the New Zealand approach, where the tax benefit must have been just one of the purposes, provided it is not merely incidental. This would place the Commissioner in a more favourable position, as it is submitted that if the taxpayers in the three cases discussed above had been able to provide other objective factors in support of their subjective intents, the South African GAAR may not have been applicable to these arrangements.

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93 *Ben Nevis* (n 21) 136.

94 Ibid 139.

95 *Commissioner of Inland Revenue v Frucor Suntory New Zealand Limited* [2020] NZCA 383.

96 *Frucor* (n 22) 41. The judgment in the Supreme Court contrasted with that of the High Court with regard to economic substance, as can be noted at 77: 'It follows that, contrary to the finding of fact in the High Court, the purpose of the arrangement was not to alter, by increasing, the debt/equity ratio of Danone. In substance its effect and purpose [were] quite the reverse.'

3 *Tainted Elements*

(a) *Lack of Commercial Substance*

While it is submitted that it is likely that the taxpayers in all three cases were able to obtain significant tax benefits without incurring significant business risks, it cannot be said with absolute certainty that the tax benefits obtained were significant and that there was no significant effect upon the investors' business risks, as the word 'significant' is not defined in the South African GAAR.

Nevertheless, it is evident in *Penny and Hooper* that the reduction of salaries enabled the companies to distribute the profits by way of dividends to the family trusts, avoiding payment of the highest personal tax rate (for the taxpayers) and that these dividends were then used by the trust for the taxpayers' family purposes, including benefiting Penny through loans and Hooper through funding the family home and holiday home. Therefore, the arrangement had an effect on the taxpayers' net cash flows, as they did not receive all of the income that they would have received had they not entered into the arrangement. There was an effect on the net cash flows for the taxpayers. This reveals a potential weakness in the South African GAAR, as a taxpayer may exercise indirect control over funds or cash flows even where direct control is not immediately apparent. In this case, it may have been through influence over the decisions made by trustees or even through influence over the use of the funds when received by the beneficiaries of the trust. This weakness may be addressed if the GAAR were to consider whether the taxpayer has direct or indirect control over the funds (even if the amounts were not received by the taxpayer), the relationships between the taxpayer and the recipients of the funds, or how the funds are applied.

While the taxpayers both restructured their personal income affairs, it should be noted that Penny had established the company-trust structure several years prior to the increase in the tax rates, and subsequently limited his income from the company when the tax rate increase took place. In contrast, Hooper restructured his practice shortly after the tax rate change. As per Table 1, above, it is noted in *Penny and Hooper* that there is significant doubt regarding the efficacy of the South African GAAR and the lack of commercial substance tainted element requirement when applied to this case and Penny's circumstances. This uncertainty is not necessarily limited to the timeframe in which the tax rate change took place; rather, the commercial benefit is probably the effect of the tax benefit[97] (tax rate change) alongside the annual fixing of low salaries.

In *Ben Nevis,* the insurance company used (incorporated in the British Virgin Islands) had no office, telephone line, employees or stationery.[98] These factors may be considered for the purposes of lack of commercial substance, drawing the substance of the insurer into question as part of the arrangement. In the context of the South African GAAR, the factors

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[97] By virtue of *ITA 1962* (n 7) s 80C(1), a taxpayer may not use the tax benefits derived to justify the commercial substance of an arrangement.

[98] *Ben Nevis* (n 21) [134].

mentioned above may have been considered for the purposes of business risk, but it is uncertain if it would have met the 'no significant effect on the business risks' requirement.

(b) *Round-trip Financing*

The arrangements in *Ben Nevis* and *Frucor* included an element of reciprocity, as there was a transfer of funds between parties that resulted in tax benefits. However, in *Penny and Hooper*, it is uncertain whether the transfer of the funds by the trust to the beneficiaries, and not the taxpayers, would be considered a reciprocal action. The Court in *Penny and Hooper* held that Penny and Hooper could be expected to control the trusts, even though neither of them was a trustee of the relevant trust, as it is expected that the trustees chosen by them would act according to their instructions, meaning that Penny and Hooper were in fact in control of the funds.[99] This reveals a weakness in the current South African GAAR, as it does not consider the role of all relevant parties to the arrangement when considering the existence of round-trip financing. The efficacy of the South African GAAR may be improved by considering the role of all relevant parties and any relationship that they may have.

(c) *Accommodating or Tax-indifferent Parties*

According to the strict definition of an accommodating or tax-indifferent party, as contained in *ITA 1962* s 80E(1), a taxpayer is considered an accommodating or tax-indifferent party if the amount derived by that party is not subject to normal tax.[100]
In all three cases, it is likely that the amounts were subject to normal tax, even though they were taxed at lower rates. In *Penny and Hooper*, prior to the restructuring, Penny and Hooper should have been subject to tax at the maximum individual tax rate of 39% on a significant portion of their generated income. However, as a result of the restructuring, the income of the trusts was taxed at 33% on the retained earnings (or, if distributed, the rate of the individual beneficiaries). Therefore, it is evident that Penny, Hooper, the companies, the trusts and the beneficiaries were subject to normal tax albeit at differing rates in certain instances. Furthermore, in *Ben Nevis*, CSI Insurance was incorporated in the British Virgin Islands, which is considered a well-known tax haven, indicating that the insurance company effectively transferred its tax advantage of being subject to tax at a lower rate on the insurance premiums to the taxpayers.[101] In addition, in *Frucor*, a similar trend was identified, where the accommodating party (the company incorporated in Singapore) was subject to normal tax, albeit at a lower rate. This reveals an additional weakness in the current GAAR: where a party is subject to normal tax on amounts earned (just at a reduced rate), the party(ies) would not be considered accommodating or tax-indifferent parties in South Africa.

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[99] *Penny and Hooper* (n 20) 35.

[100] *ITA 1962* (n 7) s 80E(1).

[101] Will Fitzgibbon, 'Tax Havens: British Virgin Islands Corruption Scandal Threatens its Dependable Tax Haven Reputation', *ICIJ* (Web Page, 26 January 2021) <www.icij.org>.

(d) *Offsetting or Cancelling Effects*

Certain offsetting and cancelling elements can likely be identified in all three cases. However, in *Ben Nevis*, the 'risks' incurred by the taxpayers were effectively offset by the insurance arrangement entered into with CSI Insurance in exchange for insurance premiums. The nature of an insurance arrangement is inherently offsetting, as the risk incurred by one party is taken over by another in exchange for premiums. Analysis of this case in the context of the South African GAAR reveals that contracts such as those for insurance may inherently contain features that fall foul of the GAAR. In *Frucor*, further weaknesses in the South African GAAR were identified, as the forward purchase agreements, convertible notes and share buy-backs present in this case may also be considered inherently offsetting due to the nature of these transactions. The scope of the South African GAAR may be extended beyond the legislature's intention by including arrangements that contain elements that are inherently offsetting and may unfairly prejudice taxpayers who enter into arrangements where these elements are present. Therefore, the efficacy of the South African GAAR may be improved by allowing for the discretion of the judiciary in a manner that more closely resembles that of the parliamentary contemplation test, following a similar approach as New Zealand where the interpretation of this indicator is left to the courts as opposed to the application of the prescriptive list that is currently employed.

Although it is evident that the two GAARs contain similarities, the applications thereof are different. Section IV of this study includes recommendations to improve the efficacy of the South African GAAR based on the lessons learnt from the New Zealand GAAR.

IV RECOMMENDATIONS

The doctrinal analysis and the reform-oriented research undertaken in sections II and III, respectively, have identified weaknesses that exist in the South African GAAR. As a result of the analysis and triangulation of the findings, it is submitted that the following recommendations may contribute to improving the efficacy of the South African GAAR:

- An approach similar to New Zealand's may be followed by not requiring a taxpayer to be party to an arrangement, meaning that prior knowledge and volition are not required from the taxpayer in identifying an arrangement.
- An approach similar to New Zealand's may be followed by requiring a purpose that is more than merely incidental instead of the current sole or main purpose requirement. It is further submitted that the inquiry into the purpose of an arrangement should be an objective test which is not affected by the taxpayer's stated intention.
- An approach similar to New Zealand's may be followed by considering the tainted elements as part of the tax benefit requirement; this may improve the efficacy of the South African GAAR, as only three requirements would need to be met instead of the current four.
- The exclusion of foreign business establishments from the 'accommodating or tax indifferent party' element of the current South African GAAR should be repealed, as the use of one or more controlled foreign companies in a multinational enterprise context is not unusual, and the use of controlled foreign companies may result in this element's not being applicable.

- The definition of an accommodating or tax-indifferent party should be amended to include parties that are subject to tax at a lower rate.
- The role of all relevant parties should be considered, as well as any relationship that they may have, in order to address the weakness identified under the round-trip financing indicator.
- Additional factors should be incorporated into the tainted elements, thereby allowing courts to consider more characteristics of an arrangement so as to draw an accurate conclusion based on the parliamentary contemplation test for the purposes of the tax benefit requirement. These factors may include those relating to:
    - transactions that have no commercial purpose;[102] and
    - transactions where the investor faces no risk.
- Consideration should be given to defining undefined terms to increase certainty and to ensure a consistent application of the South African GAAR.

V CONCLUSION

The tax lost due to cross-border tax avoidance alone in a single year could cover the cost of fully vaccinating the world's entire population against COVID-19 more than three times.[103] Therefore, it is imperative for countries to equip themselves with effective measures to combat impermissible tax avoidance. While the South African GAAR may be used as a defence against tax avoidance schemes, it has not yet been subjected to judicial inquiry to its full extent since its amendment in 2006, and it can therefore not be concluded whether or not the GAAR is an effective deterrent to impermissible tax avoidance arrangements.

This article has made two contributions to improving the efficacy of the South African GAAR, using lessons from New Zealand. Firstly, it has analysed and compared the interpretation of the South African GAAR with New Zealand's, with the aim to identify weaknesses in the South African GAAR and lessons that can be learnt from its New Zealand counterpart. Secondly, the article has applied the South African GAAR to the facts of three New Zealand court cases to further identify weaknesses in the South African GAAR, in order to propose amendments to improve its efficacy. While the New Zealand GAAR was used for comparative purposes, it is worth noting that the New Zealand GAAR itself is not without issue, and an embedded uncertainty remains. Cases from as early as *BNZ*, until *Frucor* reiterate the complexity in avoidance cases. Similarly, reflecting on the delay in the *Frucor* decision results in an unavoidable sense of uncertainty.

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[102] This factor considers whether an arrangement has a commercial and non-tax avoidance purpose, even though the arrangement is not precluded from being a tax avoidance arrangement merely because a taxpayer is able to refer to a commercial reason for entering into it. Considering whether a transaction has a commercial purpose is not directly relevant to the parliamentary contemplation test but rather assists in understanding the arrangement. See Inland Revenue, 'Interpretation Statement: BG 1 and GA 1 of the *Income Tax Act 2007*' (n 53).

[103] *State of Tax Justice* (n 3).

This article has followed a structured pre-emptive analysis by first analysing the South African GAAR using doctrinal analysis and then applying the GAAR to the facts of selected case law, using a reform-oriented approach. Only the facts that were considered in the judgments have been applied; consequently, this may constitute a limitation, as the facts that were not included in the judgments have not been considered.

The selected research design and methodology used in this article involves the use of a case or cases. While this can prove to be a limitation, as it may be difficult to generalise the outcome of a study that uses this approach, the case or cases investigated in such a study may be representative of what occurs within a larger system or society.[104]

The comparison performed between South Africa's and New Zealand's GAARs has revealed that guidance should be provided in order to address the uncertainties in the interpretation and application of the South African GAAR, so as to prevent inconsistencies that may limit its efficacy. In addition, the South African GAAR should be consolidated into a three-part enquiry instead of the current four-part enquiry, which may be achieved by considering the tainted elements as part of the tax benefit requirement instead of as a separate fourth requirement that makes the South African GAAR more onerous to apply. Finally, the sole or main purpose requirement should be amended so that it need not be the sole or main purpose to avoid tax but rather just one of the purposes, provided that the tax avoidance was not merely incidental.

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Tax Legislative Drafting – A Superannuation Example: How Safe Is Your Pension?

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Abstract

Statutory interpretation is an important aspect of teaching law and its practice. The Australian Government funds a nation-wide Tax Clinic Program. This program allows university students enrolled in tax-related courses to provide services to eligible taxpayers on their tax affairs. Eligible taxpayers may be unrepresented individuals, small business, not-for-profit organisations, or charitable institutions. The services may be advice, representation, and general support for taxpayers. Students provide the services under the supervision of qualified clinic managers and tax practitioners. Interpretation and application of Australian tax legislation is highly relevant to the provision of the services, and highlights the importance of skilful legislative drafting in plain English, which avoids jargon, and expresses the law concisely and definitively. Taxpayers should not need to consult cross-referenced provisions in multiple Acts and a plethora of subordinate statutory instruments.

This article examines superannuation-related legislation introduced by the then Treasurer of the Commonwealth of Australia, The Hon Scott Morrison MP, which commenced on 1 July 2017. The article highlights some difficulties inherent in this legislation due to its departure from legislative drafting standards and indicates the consequences for tax clinics and their clients.

I Introduction

The success of legislation in effecting its purpose largely depends on the words drafters use to express their intention. Rational drafters will be attentive to the probable effect of their choice of words upon the legislation's intended audience. Effective drafting requires the legislation to meet three essential criteria: transparency, accessibility, and congruency.

First, drafters should use words with well-defined and universally accepted meanings to the legislation's intended audience. This quality has been referred to as transparency.[1] Second, drafters should ensure their legislation is accessible to the legislation's intended audience. People to whom legislation is directed should be able to be apply this legislation

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1 Colin S Diver, 'The Optimal Precision of Administrative Rules' (1983) 93(1) *Yale Law Journal* 65, 129.

to concrete situations without excessive difficulty or effort. This quality has been referred to as accessibility.[2] Third, drafters should aim for the legislation's substantive content to produce the desired behaviour. The legislation should be 'congruent' with its underlying policy objective. This quality has been referred to as congruency.[3]

This article focuses on the *Treasury Laws Amendment (Fair and Sustainable Superannuation) Bill 2016* and associated legislation which, on Wednesday, 9 November 2016, the then Treasurer of the Commonwealth of Australia, The Hon Scott Morrison MP, moved in the House of Representatives be read a second time. With effect from 1 July 2017, this legislation amended the *Income Tax Assessment Act 1997* (Cth) ('*ITAA 1997'*) and the *Taxation Administration Act 1953* (Cth) ('*TAA 1953'*).

An examination of this legislation compared with its objects and purposes stated by Morrison in his second reading speech shows that it fails to meet any of the three key criteria specified above.

The legislation fails the transparency criteria. It is expressed in so much jargon. The legislation fails the accessibility criterion. It is contained in multiple Acts and a plethora of regulations in language which is hard to decipher. The legislation fails the congruency criterion. It lends itself towards the expropriation of beneficiaries' pensions by superannuation fund trustees notwithstanding that any such outcome may conflict with Morrison's stated objective of tax neutrality or confer financial benefits on superannuation funds at the expense of beneficiaries irrespective of any tax considerations. An example would be the unlocking of the pension capital through the commutation of pensions as part of a trend towards pension financialisation advantaging private financial institutions. [4]

This legislation seems to have all the defects described by the High Court of Australia in *Hepples v Federal Commissioner of Taxation.*[5] There it was said of the *Income Tax Assessment Act 1936* (Cth) ('*ITAA 1936'*) s 160M(6) and (7)[6] and the provisions to which they were related, as then in operation, that they were 'extraordinarily complex', 'obscure, if not bewildering, both to the taxpayer … and to the lawyer who is called upon to interpret them;[7] having been 'drafted with such obscurity that even those used to interpreting the utterances of the Delphic oracle might falter in seeking to elicit a sensible meaning from

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[2] Ibid.

[3] Ibid.

[4] Ray Broomhill, Monica Costa, Siobhan Austen and Rhonda Sharp, "What Went Wrong With Super? Financialisation and Australia's Retirement Income System" (2021) 87 *Journal of Australian Political Economy* 71, 88-9.

[5] (1991) 173 CLR 492.

[6] On the improvement brought about by the simplification of the Capital Gains Tax provisions in *the Income Tax Administration Act 1997* (Cth) ('*ITAA 1997*') which superseded the former provisions in the *ITAA 1936*, see Matthew Wallace, Geoffrey Hart and Chris Evans, 'An evaluation of the contribution of Justice Hill to the provisions for the taxing of capital gains in Australia' (2013) 28 *Australian Tax Forum* 123.

[7] *Hepples v Federal Commissioner of Taxation* (1991) 173 CLR 497 per Mason CJ.

its terms', with a 'result' which 'is so absurd that it is difficult to believe that Parliament intended it';[8] being 'couched in terms which … are unduly labyrinthine' for those 'seeking for some consistent policy or approach, if such is to be found';[9] and that in respect of the then *ITAA 1936*:

> In circumstances where the heavy burden of legal costs is likely to constitute an insurmountable obstacle … successive administrations have allowed the Act to become a legislative jungle in which even the non-specialist lawyer and accountant are likely to lose their way in the search to identify the provisions relevant to a particular case [where] in respect of a commonplace transaction … it could not realistically be suggested that there would be any difficulty at all in plainly expressing a legislative intent.[10]

The defective nature of the former tax legislation illustrated by this kind of adverse commentary by the High Court of Australia, as enunciated in *Hepples v Federal Commissioner of Taxation*,[11] seems to have continued as an unfortunate feature of the 2017 legislation.

II BACKGROUND

The pension and other rights which beneficiaries are entitled to under superannuation schemes are given in return for many years of work. Membership of a superannuation scheme is compulsory for most employees in Australia. Employees are compelled to contribute to the scheme out of their pay. Employer contributions into the superannuation scheme are deferred wage and salary payments which usually only become available to employees after their retirement.[12] These many millions of employees cannot be expected to decipher the kind of jargon in the legislation which commenced on 1 July 2017 spread over pages and pages of amendments to multiple Acts, such as the *ITAA 1997*, the *TAA 1953*, the *Superannuation Industry (Supervision) Act 1993* (Cth), and manifold regulations and other instruments made under those Acts.

The future of tax must be more than just politics. The Parliament must focus on whether years' ahead political statements regarding the anticipated impact of tax bills will in fact be realised. Tax considerations, as contrasted with unlocking pension capital through the commutation of pensions as part of a trend towards pension financialisation advantaging private financial institutions, [13] required a different approach by Morrison. Morrison should have introduced a short clear concise legislative amendment centred on one Act,

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[8] Ibid 546 per McHugh J.

[9] Ibid 521 per Toohey J.

[10] Ibid 511 per Deane J.

[11] (1991) 173 CLR 492.

[12] Lord Browne-Wilkinson, 'Equity and its Relevance to Superannuation Schemes Today' in M Scott Donald and Lisa Butler Beatty (eds), *The Evolving Role of Trust in Superannuation* (The Federation Press, 2017) 58, 60.

[13] Broomhill et al (n 4) 88-9.

namely, the *ITAA 1997*, in plain English simply to provide that pre-1 July 2017 tax-free superannuation income stream earnings above the prescribed cap become assessable income after 1 July 2017.

The Australian Financial Review asserts that Australia is left with 'a creaking tax system that imposes even more of a drag on the Australian economy' and calls for politics to be taken 'out of the way of tax reform',[14] and for government to 'spread the burden, and do less economic damage'.[15] The higher the standard of legislative drafting in respect of the tax law, the less there should be any economic damage. Legislative drafting standards in respect of tax law also impacts upon the teaching of tax. Tax must be taught in the context of the legislation in which the tax law is drafted. This result arises from the intrinsic connection between the teaching and practice of tax. This intrinsic connection can be illustrated by reference to the Australian Government-funded National Tax Clinic Program ('NTCP').

The Australian Government funds universities across Australia to run a NTCP. Pursuant to the NTCP there are tax clinics in every state and territory of the Commonwealth of Australia. The Australian Taxation Office ('ATO') supports this initiative, but the tax clinics operate independently. The NTCP taxpayers who may not be able to afford professional advice and representation with their tax affairs. This program is available to eligible individuals, small businesses, not-for-profit organisations, and charities. Sessions are offered via phone or web conferencing, as well as face-to-face in some locations. Students studying tax-related courses provide free tax advice and support under the supervision of qualified clinic managers.[16]

Universities overseeing the supervision of students providing services to eligible persons in the NTCP therefore have an interest in ensuring that the tax legislation meets such essential legislative drafting criteria as transparency, accessibility, and congruency.

III WHAT IS THIS ARTICLE'S THEME?

The theme of this article is there cannot be meaningful tax law unless the tax legislation is transparent, accessible, and congruent, so as for example to be comprehensible to taxpayers. Pursuant to this theme, this article maintains that the package of superannuation legislation introduced by Morrison which took effect on 1 July 2017 should have been provided in one Act to prescribe that pre-1 July 2017 tax-free superannuation income stream earnings above the specified cap become assessable income after 1 July 2017. Using this legislation as an example, the article maintains that taking the politics out of tax reform requires the simplification of the tax laws to make this legislation transparent, accessible, and congruent, becoming comprehensible to users

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[14] The FAR View, 'Take the politics out of the way of tax reform' *Australian Financial Review* (Sydney, 16 September 2021) 42.

[15] Ibid.

[16] 'National Tax Clinic program', *ATO* (Web Page, 13 April 2022) <https://www.ato.gov.au/General/Gen/National-Tax-Clinic-program/>.

such as tax students. To this end, Parliament must focus on the substantive content of proposed tax legislation. Treasurers should facilitate Parliament's capacity to focus on whether proposed tax legislation meets such legislative drafting standards as transparency, accessibility, and congruency. A focus on these standards must be ahead of how such measures are to be represented to the media in a way which would maximise a Government's political prospects or advance a Government's standing with private financial institutions seeking to unlock pension capital through the commutation of pensions as part of a trend towards pension financialisation which advantages these private financial institutions.[17].

Tax teachers oversee the training of the next generation of tax practitioners. To this end, tax teachers provide practical training to complement classroom teaching. In so doing, the importance of pursuing this objective of transparent, accessible, and congruent tax legislation should readily emerge. Consistent with the importance of practical training in university tax courses to prepare students for work as tax practitioners, there is recognition in the courts of how the work of academics can help courts in handing down their decisions, particularly at the appellate level with what has been termed 'practical legal scholarship'. [18]

IV EQUITY, TAX AND AUSTRALIAN SUPERANNUATION

An examination of what is necessary to establish a balanced, comprehensive, and multidimensional understanding of what equity means in the Australian superannuation system has identified a comprehensive series of regressive superannuation tax concessions as the recommended area for improvement so that the inequity can be redressed.[19]

A *Tax Treatment of Australian Superannuation*

Robert Carling describes superannuation tax concessions as being excessively generous to high income earners.[20]

1 *Impact of Tax Concessions*

Given the long-term trend towards increasing income inequality in Australia, it has been contended that there are convincing arguments towards an emphasis in retirement policies that distribute income more equally. Consequently, a case has been put forward that there is merit in Australia's superannuation system being complemented by a fully funded government run defined benefits scheme. A comprehensive review of this nature

[17] Broomhill et al (n 4) 88-9.

[18] Lord Burrows, 'Lionel Cohen Lecture 2021: Judges and Academics and the Endless Road to Unattainable Perfection', *The Supreme Court* (Web Page, 2021) <https://www.supremecourt.uk/docs/lionel-cohen-lecture-2021-lord-burrows.pdf>.

[19] John Harrison, 'Pursuing Equity in the Australian Superannuation System' (PhD Thesis, The University of Adelaide, 2021).

[20] Robert Carling, 'How should super be taxed' (2016) 32(3) *Policy* 13.

would incorporate a review of the tax concessions and their negative effect on the Australian government's budgetary position. [21]

The better-off retirees benefitting from the generous taxation advantages attached to Australia's superannuation system are said together with the private superannuation industry with its massive investments, the financial adviser industry and associated lobby organisations to constitute a plethora of 'vested' 'well-resourced interests'. These interests, it has been said, 'can be expected to resist any large-scale winding back of the current, financialised aspects of the system' with its inherent inequities.[22]

2 *The Tax Institute Approach*

The Tax Institute ('TTI') has described the legislative provisions introduced by Morrison which have taken effect from 1 July 2017 as being 'designed to *restrict* the amount of contributions that are made to a *concessionally taxed* environment' [emphasis added] where the 'transfer balance cap' ('TBC') imposed in respect of the 'transfer balance account' ('TBA') operating in respect of account based superannuation income streams are quarantined from, say, the defined benefit income cap which operates in respect of defined benefit pensions, so that pensioners 'whose pension balance is reduced because of market forces (for example, COVID-19 pandemic-related) will not be able to top up their pension if they have fully utilised their TBA, whereas a member whose pension balance has performed well can end up with a pension account balance that exceeds their TBC'.[23]

Among the reforms canvassed by TTI to those rules in respect of the TBC is, instead of resulting in compulsory commutation, 'subjecting excessive amounts to personal income tax'.[24] TTI states that the 'complex array of caps, thresholds and concessionary measures needs a rethink' being 'not sustainable in the long term' and 'the cause of many taxpayers inadvertently breaching the caps or the rules, with severe consequences in terms of their retirement savings or penalties'.[25] The resultant merging by superannuation fund trustees of very different accounts and caps appears to be sourced in the absence of the high level of data management required for the 2017 legislation to operate where the ATO is dependent upon what superannuation funds report.[26]

3 *This Article's Contention*

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[21] Rami Hanegbi, 'Australia's superannuation system: A critical analysis' (2010) 25 *Australian Tax Forum* 303.

[22] Broomhill et al (n 4) 88-9.

[23] The Tax Institute ('TTI'), 'Design of a Sustainable Superannuation System' (2022) 57(1) *Taxation in Australia* 19, 22 and 24.

[24] Ibid 28.

[25] Ibid 27-8.

[26] Ibid 24-5. See also 'Managing your transfer balance account', *ATO* (Web Page, 6 December 2022) <https://www.ato.gov.au/individuals/super/in-detail/withdrawing-and-using-your-super/transfer-balance-account/?page=3>.

This article contends that when one examines the actual words of the 2017 legislation, the explanatory memorandum and Morrison's second reading speech on the legislation's purpose and object, this legislation is designed to 'cap' the tax concessions on superannuation. It is not designed to 'cap' superannuation itself irrespective of the tax ramifications. This contrast is relevant to current reports of there being more complex legislation being canvassed to 'cap' how much money a superannuation fund beneficiary may continue leaving in a superannuation accumulation account so as to continue receiving 'a generous concessional tax rate of 15 per cent on earnings and contributions, well below the top marginal income tax rate of 45 per cent'.[27] In accordance with what TTI submits, a more sensible course would simply be to subject any such excessive amount to personal income tax, rather than purport to compel commutation of any such excessive superannuation.

B *Issues of Equity and Tax in Respect of Superannuation*

On Wednesday, 9 November 2016, Morrison moved in the House of Representatives that the *Treasury Laws Amendment (Fair and Sustainable Superannuation) Bill 2016* be read a second time. *Acts Interpretation Act 1901* (Cth) s 15AB provides for consideration in the interpretation of a provision of an Act to be given to ministerial second reading speeches.

1 *Morrison's Second Reading Speech*

In his second reading speech, Morrison told Parliament that: 'As our population ages, it is simply not sustainable to have ever increasing earnings generated from very high superannuation balances being completely tax-free.' He added that, from 1 July 2017, there would be a '$1.6 million cap on the total amount of superannuation a person can transfer into the retirement phase where earnings are tax-free'. Morrison explained that the intention of this legislation is to achieve tax neutrality by neutralizing any advantage an individual receives from having an excess above $1.6 million – as indexed over time in line with the consumer price index – in the designated capital in retirement-phase superannuation accounts which otherwise would have continued to be tax-free after 1 July 2017.[28]

Morrison further told Parliament that to ensure people did not transfer excess amounts into the tax-free earnings retirement phase, a tax was to be imposed on the earnings of retirement phase transfers that exceed the transfer balance cap. The $1.6 million transfer balance cap was around twice the level at which access to the age pension ceases on account of an individual's assets—not including the family home. This illustrated that the transfer balance cap had been set at a level to support retirement income streams well above that provided by the age pension. Over time, the transfer balance cap would index in $100,000 increments in line with the consumer price index, just like the age pension

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[27] Michael Read, 'Threat to Super Tax Breaks' *Australian Financial Review* (Sydney, 19-20 November 2022) 27.

[28] Ibid.

assets threshold. It was estimated that less than 1% of superannuation fund members would be affected by the transfer balance cap in 2017-18.[29]

V HOW RELEVANT LEGISLATIVE PROVISIONS OPERATE IN SUMMARY

A *Key Contention*

It is contended that, because requirements for commutation of pensions in the 2017 legislation operate within the ambit of securing tax neutrality, an assertion is wrong such as that any non-commutable lifetime pension must be included towards counting whether the transfer value cap has been exceeded for the purposes of triggering the compulsory commutation of any superannuation 'financial product until the superannuant is below the cap irrespective of whether the pension was assessable for income tax prior to 1 July 2017' and irrespective of whether the pension continues to be assessable for income tax after 1 July 2017.

1 *Problems in the Drafting of the Legislation*

Reference to some key features of the legislation will be followed by turning to address several key aspects in respect of its operation to demonstrate how the legislation's drafting has resulted in some significant defects when seeking to determine the extent and identify the targets of its practical application. Whereas the major provisions in the principal Act are clear, the drafting of much of the prolix subsidiary legislation obscures a non-commutable lifetime pension being unable to be included in the count towards whether the transfer value cap has been exceeded for the purposes of triggering the compulsory commutation of any superannuation 'financial product'. The prescribed ambit of the legislation is to impose a cap on earnings in the retirement phase of superannuation whose earnings are tax exempt; the prescribed object of the legislation is to limit the total amount of an individual's superannuation income streams that receive an earnings tax exemption; and the applicable Act's operational provisions prescribe that defined benefit lifetime pensions that are subject to commutation restrictions cannot result in excess transfer balance for the purposes of calculating whether a 'superannuation interest' must be commuted; instead any such excess is taxed.

2 *Importance of Hierarchy in Statutory Interpretation*

The prescribed statutory object when combined with the prescribed statutory ambit and the applicable Act's key operational provisions impacts on the interpretation of the remainder of the Act and of any pertinent subordinate legislation. Consequently, not every provision in every piece of legislation is to be given the same authority irrespective of whether it is in an Act or in subordinate legislation and irrespective of whether it enunciates the statutory object or purpose of the legislation or is there to achieve that object or purpose. Administrators must not quote the terms of such subordinate legislation out of context so as to pursue contrary objects and purposes. There is a

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[29] Ibid 3383.

hierarchy in legislation. At its apex are the provisions in an Act which prescribe its statutory object or purpose. Administrative action, whether in performance of a duty or exercise of a power, must conform to the scope and purposes of the relevant Act as it cannot be for an illegitimate purpose.[30] When one turns to addressing in detail the actual terms of the operative provisions in the 2017 legislation, it is clear that those operative provisions are within the prescribed ambit of this legislation and consistent with the legislation's prescribed statutory object.

3 *A Superannuant with Different Kinds of Superannuation Income Streams*

What happens if a superannuant has a combination of superannuation income streams, say, defined benefit income streams and account-based income streams? A non-commutable lifetime pension is subject to tax instead of commutation. Its value therefore is not included in determining whether the 'transfer value cap' has been exceeded on the value of those superannuation income streams which are not a 'capped defined benefit income stream', above which "transfer value cap", those other superannuation income streams are to be commuted.[31]

4 *Impact of Commutation*

The complexity inherent in the 2017 legislation seems to derive from the commutation of pensions being a central feature, rather than by contrast with what TTI canvasses simply 'subjecting excessive amounts to personal income tax' in respect of the Transfer Balance Cap rules.[32]

5 *Excess Transfer Balance Tax*

ITAA 1997 s 294.230 titled 'Excess transfer balance tax' neutralises any 'excess transfer balance' earnings tax exemptions on 'retirement phase' income streams that result in an 'excess transfer balance' by providing for a liability to pay an 'excess transfer balance tax' imposed by the *Superannuation (Excess Transfer Balance Tax) Imposition Act 2016* (Cth) in respect of any such 'excess transfer balance' earnings during a continuous period of more than one day during which at the end of the day there is an 'excess transfer balance'.

B *Application of the Legislation*

Having summarised some key features of the legislation, we shall now turn to its operation in respect of several key aspects. These key aspects are not intended to be exhaustive. What they demonstrate is how the legislation's drafting has resulted in some significant defects when seeking to determine the extent and identify the targets of its practical application.

1 *Exposure of Superannuation Fund Trustees*

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[30] *Commonwealth v AJL20* (2021) 273 CLR 43 [129] per Edelman J.

[31] For example, *ITAA 1997* (n 6) s 194.120.

[32] TTI (n 23) 28.

To protect the superannuation funds from litigation, the legislative drafter would have had to ensure that any commutation authority issued by the Federal Commissioner of Taxation to the superannuation funds is not outside the legislation's lawful ambit within the overriding terms of the principal Act and the Commonwealth's legislative powers. Otherwise, the superannuation fund trustees become exposed to litigation through such a claim as that the trustees' 'commutations' of pensions are at the direction of the Commissioner. The prohibition against acting under dictation, enunciated in *R v Stepney Corporation*[33] applies to superannuation fund trustees.[34]

2 *An Exception for Commutation*

Non-commutable defined benefit lifetime pensions inherently are not commutable. Therefore, how does the 2017 legislation operate in relation to defined benefit pensions that may be commutable?

It will be recalled that the ambit of the legislation is set out in *ITAA 1997* s 294.1. This ambit is prescribed as imposing a cap on the total amount which a superannuation fund beneficiary can transfer into the retirement phase of superannuation where earnings are exempt from taxation. This ambit is expressed to include: 'Division 136 in Schedule 1 to the Taxation Administration Act 1953 which contains rules about excess transfer balance determinations and commutation authorities'. Accordingly, the provisions prevent flooding of a 'transfer balance account' with monies that should not be there. This 'flooding' would leave no room for the monies which should be there (so as not to create exposure to the making of a wrong claim that there supposedly is some 'excess' in the superannuant beneficiary's 'transfer balance account'. Such an excess then becomes of a kind that superannuation fund trustees must commute as supposedly in excess of the beneficiary's 'transfer value cap'. The requisite quarantine prevents lumping altogether such different kinds of pensions and superannuation income streams as:

- non-commutable lifetime pensions regardless of when they commence funded by the elements untaxed in the fund, usually from governmental consolidated revenue. All of this kind of pension inherently could not attract the tax concessions thereby continuing to be assessable income after 1 July 2017. This pension therefore cannot result in an 'excess transfer balance' (for example, *ITAA 1997* s 294.120). This kind of pension therefore is not to be counted in determining whether the pensioner has exceeded the 'defined benefit income cap' (for example, s 303.2);
- non-commutable lifetime pensions regardless of when they commence funded from other than elements untaxed in the fund. Being non-commutable lifetime pensions, this kind of pension cannot result in an 'excess transfer balance' (for example, *ITAA 1997* s 294.120). However, any part of such a pension whose funding source is in contributions into the fund taxed at concessional rates counts towards whether the pensioner has exceeded the 'defined benefit income cap'. The result is 50% of any such

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[33] [1902] 1 KB 317.

[34] M Scott Donald, 'Beneficiary, Investor, Citizen: Characterising Australia's Super Fund Participants' in M Scott Donald and Lisa Butler Beatty (eds), *The Evolving Role of Trust in Superannuation* (The Federation Press, 2017) 48.

excess is included in the pensioner's assessable income to neutralise the tax concessions above the tax-free cap (for example, *ITAA 1997* s 303.2);

- lifetime annuities that existed prior to 1 July 2017, lifetime expectancy pensions and annuities that existed prior to 1 July 2017 and market-linked pensions and annuities that existed prior to 1 July 2017 (for example, *ITAA 1936* s 294.130). These pensions and annuities are not non-commutable lifetime pensions. These pensions and annuities therefore may be counted towards whether a superannuant beneficiary has exceeded not only the 'defined benefit income cap' but also the 'transfer balance cap'. However, provided that the superannuant beneficiary does not have any account based income streams, generally (because the presumption is that 'defined benefit income' should not have to be commuted), a lifetime annuity that existed prior to 1 July 2017, a lifetime expectancy pension or annuity that existed prior to 1 July 2017 and a market-linked pension or annuity that existed prior to 1 July 2017 will only be relevant in determining whether the superannuant beneficiary has exceeded the 'defined benefit income cap'. Such an excess results in 50% of any such excess in respect of income from a concessional tax source over the 'defined benefit income cap' being included in the superannuant beneficiary's assessable income to neutralise the concessional tax treatment in respect of the excess; and
- lifetime annuities that commenced after 1 July 2017, lifetime expectancy pensions and annuities that commenced after 1 July 2017 and market-linked pensions and annuities that commenced after 1 July 2017 (eg, *ITAA 1936* s 294.130, and all other account-based income streams regardless of when they commence. All these pensions, annuities and income streams are to be counted in a superannuant beneficiary's 'transfer balance account' to determine whether the superannuant beneficiary has exceeded the 'transfer balance cap'. Thereupon the superannuant beneficiary becomes liable to pay 'excess transfer balance tax' in respect of the 'excess' over the 'transfer balance cap' for every day on which the 'excess' has not been commuted.

Each of such different kinds of pensions and income streams must be properly identified, putting each of them into the correct category. Otherwise, the consequence is a far wider impact on the workforce and retirees than the relatively small number of high earners envisaged. This much wider impact arises through the merging by superannuation fund trustees of very different accounts and caps. This kind of merger appears to be sourced in the absence of the high level of data management required for the 2017 legislation to operate[35] where the ATO is dependent upon what superannuation funds report.[36]

There are further provisions which address what happens if there is a capped defined benefit income stream which does not involve the payment of non-commutable lifetime pensions. *TAA 1953* sch 1, s 136.80(2) provides for an exception to the mandatory operation of a 'commutation authority' in the case of any 'capped defined benefit income stream'. A 'capped defined benefit income stream' includes lifetime annuities that existed prior to 1 July 2017, lifetime expectancy pensions and annuities that existed prior to 1 July 2017 and market-linked pensions and annuities that existed prior to 1 July 2017 (for

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35 TTI (n 23) 24-5.

36 Ibid.

example, *ITAA 1936* s 294.130). In the case of such pre-1 July 2017 superannuation 'financial products', as an alternative to commutation 50% of the payments representing elements taxed in the fund at concessional rates in excess of the 'defined benefit income cap' are to be subject to tax in accordance with such legislation as *ITAA 1936* sub-div 303-A.[37]

3 *What is a 'capped defined benefit income stream'?*

The answer is that we do not always know what is a 'capped defined benefit income stream' where such a stream is not a non-commutable lifetime pension. In respect of a market-linked pension, the inclusion of operational provisions in what is supposed to be a definition, which operational provisions prescribed by regulation seem linked to lifetimes rather than the market, creates issues as to whether such a regulation can operate to produce a conflicting result to what would be realised by the ordinary and natural meaning of the term 'market-linked pension'.

There are major unnecessary complexities associated with the meaning of 'capped defined benefit income stream'. Provisions, such as ITAA 1997 s 294.130, which incorporate other material are undesirable. Members of the public must go from source to source before being able to identify the law on the crucial subject of the meaning of 'capped defined benefit income stream'. There is also uncertainty on which instrument they should consult.[38]

Set out below is why the inclusion in the definition of 'market-linked pension' of a range of operational provisions set out in regulations should not override the ordinary and natural meaning of the term where there is an inherent conflict between a pension necessarily lasting a lifetime and being linked to a market given the inherent uncertainties of any such linkage. This analysis is also germane as to whether subordinate legislation such as regulations can override the key statutory provisions in an Act which prescribe the Act's ambit (for example, *ITAA 1997* s 294.1, the Act's object (for example, *ITAA 1997* s 294.5), and how the Act must operate (for example, *ITAA 1997* s 194.120).

4 *Incorporation by Reference*

Where an Act contains a reference to a short title that is or was provided by law for the citation of another Act as originally enacted, or another Act as amended, then the reference is to be construed as a reference to that other Act as originally enacted and as amended from time to time. Where that other Act has been repealed and re-enacted, with or without modifications, the reference is to be construed as including a reference to the re-enacted Act as originally enacted and as amended from time to time. If a provision of the other Act is repealed and re-enacted (including where the other Act is repealed and re-enacted), with or without modifications, a reference to the repealed provision extends to any corresponding re-enacted provision (whether or not the re-enacted provision has

[37] 'Transfer balance cap - capped defined benefit income streams', *ATO* (Web Page, 15 September 2022) <https://www.ato.gov.au/>.

[38] Cf Dennis Pearce and Stephen Argument, *Delegated Legislation* (LexisNexis Butterworths Australia, 5th ed, 2017) 412.

the same number as the repealed provision as provided for by the *AIA 1901*.[39] Where an Act confers a power to make regulations, then, unless the contrary intention appears, the rules in respect of incorporation by reference applies to the regulations as if the regulations were an Act.[40]

When, as with the meaning of 'capped defined benefit income stream' defined in *ITAA 1997* s 294.130, there is incorporation by reference through designating by reference many multiple Acts and regulations, there are additional undesirable problems. Members of the public are subjected to the problem of going to another source before being able to identify the law on a topic. They may also be unsure which instrument they should consult, particularly where delegated or subordinate legislation, such as regulations, are incorporated by reference in an Act. This uncertainty as to which delegated or subordinate legislation the public should go to for ascertaining the law is particularly an issue where the delegated or subordinate legislation is incorporated by reference on a from time-to-time basis.[41] Such uncertainty can impact even on lawyers.

Regulations may, unless the contrary intention appears, make provision in relation to a matter on which the regulations are authorised or required to make by applying, adopting or incorporating, with or without modification, the provisions of an Act or of regulations, as in force at a particular time or as in force from time to time.[42] However, unless the contrary intention appears, regulations may not make provision in relation to a matter by applying, adopting or incorporating any matter contained in other regulations as in force or existing from time to time.[43]

The common law presumption was that, in the absence of an indication that a reference to another piece of legislation was to be ambulatory, the reference was taken to be to the legislation in the form it took at the date the reference to the legislation was made.[44] Subsequent amendments were not to be taken into account.[45] So *Workers' Compensation Act 1926-1942* (NSW) s 10(2) and (7) were incorporated as part of section 124 (3) in the terms in which they were expressed at the time when such a latter sub-section was enacted and were to be applied in its operation without regard to amendments thereto made subsequent to its enactment.[46] The *Companies Ordinance 1931* (ACT) adopted with modifications the company legislation of New South Wales in force at its commencement.

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39 *Acts Interpretation Act 1901* (Cth) s 10 ('*AIA 1901*').

40 *Legislation Act 1901* (Cth) s 13(1).

41 For example, Pearce and Argument (n 38) 412.

42 *Legislation Act 1901* (Cth) s 14(1).

43 Ibid s 14(2).

44 Dennis Pearce, *Statutory Interpretation in Australia* (LexisNexis Butterworths Australia, 9th ed, 2019) 68.

45 *Commissioner for Government Transport (NSW) v Deacon* (1957) 97 CLR 535, 546 per Dixon CJ, McTiernan, Fullagar, Kitto and Taylor JJ.; *Re Universal Distributing Co Ltd (in liq)* (1933) 48 CLR 171, 173 per Dixon J.

46 *Commissioner for Government Transport (NSW) v Deacon* (1957) 97 CLR 535.

Subsection 19(4) of the Ordinance provided that the practice and procedure so far as they were not regulated by rules of the High Court should accord, as nearly as could be, to the practice and procedure of the Supreme Court of New South Wales under the rules made pursuant to the *Companies Act 1899* (NSW). This provision was held to refer to the rules which existed at the time when the Ordinance was made. This provision was held not to refer to whatever rules might have been made from time to time after the commencement of the Ordinance.[47]

Such an outcome was rarely wished by legislators. Therefore, it tended to be incorporation by reference to other legislation to be read as a reference to that other legislation as amended or as in force from time to time.

The problem is further compounded where, as with the meaning of 'capped defined benefit income stream' defined in *ITAA 1997* s 294.130 there is incorporation by reference, and what is incorporated, is a definition. It can be an inversion of the ordinary approach to seek to interpret a definition by reference to provisions in which the defined term is being used.[48] In the case of the meaning of 'capped defined benefit income stream', its meaning cannot be ascertained without referring to the prolix and detailed provisions in multiple sets of regulations in which the term is used.

Context or subject matter may modify in a particular provision the prima facie meaning of a defined term. Context or subject matter cannot modify or affect in any way the statutory definition itself. It is only the statutory definition itself as prescribed in the legislation that is incorporated by reference that is relevant for the purposes of interpreting the legislation which has incorporated by reference the statutory definition. Other references to what is contained in the legislation from where the statutory definition has been incorporated by reference should not be considered for the purposes of arriving at an interpretation of provisions containing the statutory definition. The incorporation of a definition of a particular term stands upon a different footing from the incorporation of a section. The meaning of a section may be ascertainable only by a consideration of other sections with which it is associated. By contrast, it is the definition with determines meaning. The provisions in which the statutory definition appears do not determine the meaning of that definition.[49]

If an Act brings into itself by reference a clause in an earlier piece of legislation, the legal effect is to write the clause down just as if it had been written into the Act itself as a provision in the Act. From then there is no occasion to refer to the earlier piece of legislation at all. The clause is to be dealt with as if it were in the Act itself.[50] This outcome is by contrast to such a position as that where a single section of an Act of Parliament is introduced into another Act, it must be read in the sense which it bore in the original Act from which it is taken. Consequently, it is perfectly legitimate to refer to all the rest of that

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[47] *Re Universal Distributing Co Ltd (in liq)* (1933) 48 CLR 171.

[48] Pearce (n 44) 298.

[49] Ibid 300.

[50] *In re Wood's Estate, Ex parte, Her Majesty's Commissioners of Works and Buildings* (1886) 31 Ch D 607, 615-16 per Lord Esher MR.

Act to ascertain what the section means, though those other sections are not incorporated in the new Act.[51]

What of *ITAA 1997* s 294.130(1) incorporates by reference are the provisions of the specified sub-regulations of the *Superannuation Industry (Supervision) Regulations 1994* and of the *Retirement Savings Accounts Regulations 1997* as in operation when subsection 294.130(1) commenced. Any subsequent amendments to or repeal of such a sub-regulation is irrelevant. Given that the meaning of 'capped defined benefit income stream' is crucial in such contexts as where a superannuation income stream provider may choose not to commute,[52] an issue may arise as to the extent to which the prolixity contained in the sub-regulations can be referred to in ascertaining the meaning of this crucial term 'capped defined benefit income stream'. For example, a market-linked pension necessarily must be linked to the market. The notion that a market-linked pension can only be provided in accordance with such rules and standards that operate by reference to any such market-linked pension being required to last a lifetime seems fundamentally in conflict with the very essence of a market-linked pension. Accordingly, an issue might arise as to whether such a rule or standard in subordinate legislation might be held to be operational, instead of being definitional for the purposes of the relevant Act, so therefore not being able to change the ordinary accepted essential meaning of a 'market linked pension' as used by an Act of Parliament. *ITAA 1997* sub-s 294.130(1) seems to demarcate, on the one hand, a 'lifetime pension', a 'lifetime annuity', a 'life expectancy pension', a 'life expectancy annuity' from, on the other hand, a 'market-linked pension'. This demarcation arises as a 'market-linked pension' inherently is linked to the market and not to a lifetime or life expectancy. Regulations may be unable to prescribe operational provisions inconsistent with the essence of a market-linked pension prescribed by *ITAA 1997* sub-s 294.130(1).

Whatever the prolixity in the commutation provisions of *TAA 1953* sch 1 div 136 and relevant regulations, such as those made under section 294.140 do, no such provision is able to override the express terms of the ambit of the *ITAA 1997* prescribed by section 294.1 and expressed to extend to Division 136, section 295.1 prescribing the Object of the relevant legislation and section 294.120 prescribing that, in respect of non-commutable lifetime pensions, any resultant 'excess' is to be quarantined to be accounted for by taxation and not by commutation of superannuation interests.

5 *Trustee Choice Whether to Commute a Beneficiary's Pension*

The 2017 legislation provides for the superannuation fund trustee, and not the pensioner beneficiary, to choose not to commute any 'excess' defined benefit pension in a superannuation income stream. It provides that despite the requirement for commutation on superannuation income stream providers, if the specified superannuation income stream is a capped defined benefit income stream, the superannuation income stream

[51] *Mayor, Aldermen and Burgesses of the Borough of Portsmouth v Smith* (1885) 10 App Cas 364, 371 per Lord Blackburn.

[52] Schedule 1 to the *Tax Administration Act 1953* s 136.80 ('*TAA 1953*').

provider may choose not to comply with the commutation authority.[53] In relation to such financial products as a 'lifetime annuity', a 'life expectancy pension', a 'life expectancy annuity', a 'market-linked pension', a 'market linked annuity'; and a 'market linked pension Retirement Savings Account' whether or not such a financial product is a 'capped defined benefit income stream', thereby conferring a choice on the superannuation income stream provider whether or not to comply with a commutation authority, turns on whether such a financial product was purchased before 1 July 2017.[54] Superannuation funds therefore have an interest in ensuring that the legislation is interpreted and applied so as to be within the Commonwealth's legislative powers where such a financial product is purchased after 1 July 2017.

6 *No Provision for Compensation on 'Just Terms'*

The legislative drafting seems to have confused a Commonwealth Act with respect to Taxation with a law with respect to the acquisition of property. The legislation can be applied as if it were for the compulsory acquisition by trustees of their beneficiaries' property without there being any provision in this legislation for the beneficiaries to be given compensation on 'just terms'. Where a beneficiary, so as not to incur tax related liabilities, seeks the Federal Commissioner of Taxation to authorise a superannuation fund trustee to release his or her 'superannuation interests', provisions such as to the *TAA 1953* sch 1 ss 131-60 and 135-80 of make the Commonwealth liable to pay compensation on 'just terms' to superannuation fund trustees for loss to the fund of such a 'superannuation interest'. By contrast, there is no provision in this legislation for beneficiary pensioners to be given compensation on 'just terms'.

As intimated above, *TAA 1953* sch 1, s 136.80 does not make provision for 'just terms' to the superannuation funds where a commutation authority has been issued in relation to a broad range of financial products purchased from the fund after 30 June 2017. There, the superannuation fund does not have a choice on whether to commute the financial product. Consequently, the superannuation funds can also have an interest in the lack of a provision for 'just terms'.

AIA 1901 s 15A provides:

> Every Act shall be read and construed subject to the Constitution, and so as not to exceed the legislative power of the Commonwealth, to the intent that where any enactment thereof would, but for this section, have been construed as being in excess of that power, it shall nevertheless be a valid enactment to the extent to which it is not in excess of that power.

Donald Duval argues that '[t]he Constitution … does not give the Commonwealth Parliament power to legislate in respect of superannuation.'[55] In so far as compulsory 'commutation' is concerned, the 2017 legislation can validly operate only within such

53 Ibid s 136.80(2).

54 *ITAA 1997* (n 6) s 294.130(1).

55 Donald Duval, 'The Objectives of Superannuation Supervisory Legislation' in M Scott Donald and Lisa Butler Beatty (eds), *The Evolving Role of Trust in Superannuation* (The Federation Press, 2017) 12.

provisions in the *Constitution* as those which provide for the Commonwealth Parliament to have power to make laws for the acquisition of property on just terms for any purpose in respect of which the Commonwealth Parliament has power to make laws.

The Commonwealth Parliament has, subject to the *Constitution*, power to make laws for the peace, order and good governance of the Commonwealth with respect to '[t]he acquisition of property on just terms from any State or person for any purpose in respect of which the Parliament has power to make laws'.[56]

This constitutional protection is significant. It is regarded as a constitutional guarantee of property rights.[57] It has been stated that: 'There have been more decisions relating to s 51(xxxi) over the years than has been the case with the other express rights.'[58]

A law of the Commonwealth with respect to the acquisition of property must make provision for 'just terms'. An individual or a State affected by Commonwealth Government interferences with their proprietary rights must not be left without just recompense.[59] 'Just terms' involved full and adequate compensation for the compulsory taking. [60]

A pension is 'property'. Entitlement to a pension is property. This entitlement is to receive a pension at the designated rate. This right is an accrued right. This accrued right cannot be divested by any act of the Government.[61] There is a close relationship between salaries and pensions, both being remuneration benefits.[62] Money value does not provide for 'just terms' where it does not recognise the inherent real value of a pension. Payment of a 'price' that represented merely the money value of the expropriated property without provision for account to be taken of any special loss suffered by an owner does not provide a just measure of compensation and therefore does not satisfy the constitutional requirement of just terms.[63] Just terms requires that the acquisition legislation must ensure full compensation for what is lost.[64] There must be an assessment of compensation

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[56] *Australian Constitution* s 51(xxxi).

[57] Australian Law Reform Commission, *Traditional Rights and Freedoms: Encroachments by Commonwealth Laws* (Report No 129, December 2015) 185 [7.33].

[58] James Stellios, *Zines' The High Court and the Constitution* (The Federation Press, 6th ed, 2015) 620.

[59] *Bank of New South Wales v The Commonwealth of Australia* (1948) 76 CLR 1, 349-50 per Dixon J.

[60] *Johnston Pear & Kingham & the Offset Printing Co Pty Ltd v Commonwealth* (1943) 67 CLR 314 at 322-3 per Latham CJ.

[61] *Greville v Williams* (1906) 4 CLR 694 at 705 and 706 per Griffith CJ; 710-711, and 714 per O'Connor J, and Barton J concurring at 707.

[62] *Austin v The Commonwealth of Australia* (2003) 215 CLR 195, 261 per Gaudron, Gummow and Hayne JJ.

[63] *Johnston Pear* (n 60) 322-3 per Latham CJ.

[64] *Smith v ANL Limited* (2000) 204 CLR 493, 501 per Gleeson CJ.

in an appropriate way.[65] There must be a fair and just standard of compensation.[66] There must be an award approximately equivalent to the loss.[67]

It might be argued that a pensioner may invest the commutation amount in an accumulation account with a superannuation fund. It is therefore relevant that ‘property’ for the purposes of section 51(xxxi) extends beyond those interests that are designated as proprietary or as tangible or intangible property extending to coverage of innominate and anomalous interests including possession for an indefinite period.[68] The requirement for ‘just terms’ extends to a law which provides for the compulsory acquisition of property by non-Commonwealth bodies and other persons, such as by a private superannuation fund trustee. The property need not be acquired by the Commonwealth itself. It is immaterial whether the acquisition is to be made by the Commonwealth or by some other body authorized by the Commonwealth legislation to acquire the property. ‘Acquisition’ includes a requirement for the disposal of property to a non-Commonwealth body, such as a requirement to dispose of a beneficial interest in a private superannuation fund.[69]

A vested cause of action under the general law, such as a cause of action against a superannuation fund trustee in respect of its obligation to pay pensions, is ‘property’ for the purposes of section 51(xxxi). There is an ‘acquisition’ of this ‘property’ by reason of the purported extinguishment of a beneficiary’s pre-existing legally enforceable claim against a superannuation fund trustee in respect of the beneficiary’s rights for the superannuation fund trustee to continue paying the beneficiary a pension in accordance with the terms of the beneficiary’s purchase of this pension from the superannuation fund trustee. The beneficiary purportedly is to be forced to forego any right to ongoing performance of the superannuation fund trustee’s obligations to the beneficiary with respect to the payment of the beneficiary’s pension because of the purported extinguishment. By reason of this purported extinguishment, there is to be some identifiable and measurable countervailing benefit or advantage accruing to some other person, such as the superannuation fund, because of the purported extinguishment of the beneficiary’s cause of action against the superannuation fund trustee.[70]

A law for the expropriation of a pension is not a law with respect to ‘taxation’ thereby coming within section 51(ii) of the Commonwealth Parliament’s powers to make laws under the *Constitution*. The essence of a tax is that there is an exaction, levy, contribution, duty, or charge. A tax commonly takes the form of the imposition of an obligation to pay

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65 Ibid 557 per Callinan J.

66 Ibid 513 per Gaudron and Gummow JJ.

67 Ibid 531 per Kirby J.

68 *Minister of State for the Army v Dalziel* (1944) 68 CLR 261.

69 *P J Maggenis Pty Ltd v The Commonwealth of Australia* (1949) 80 CLR 382.

70 *Georgiadis v Australian and Overseas Telecommunications Corporation* (1994) 179 CLR 297. Michael Duffy, “Is a Cause of Action in Property a Castle? Statutory Choses in Action and s 51(xxxi) of the *Constitution*” (2018) 42 *Melbourne University Law Review* 1.

money. The compulsory substitution of one cause of action against a superannuation fund trustee for another cause of action against the superannuation fund trustee or the compulsory reduction in the value of a chose of action against a superannuation fund trustee is not 'taxation'.[71]

In administering legislation, Commonwealth officers have a duty, wherever relevant, to form an opinion as to how to apply that legislation in particular circumstances or to particular persons so that any such application would not be invalid as outside the legislative powers of the Commonwealth Parliament. Commonwealth officers must have regard to the constitutional restraints on the Commonwealth's legislative powers in making administrative decisions which purport to apply Commonwealth legislation. This duty extends to a tribunal, such as the Administrative Appeals Tribunal, reviewing any such administrative decision on its merits. A tribunal exercises administrative powers, not judicial powers, where, of necessity, the tribunal forms an opinion on the constitutional validity of how the administration of Commonwealth legislation has impacted upon a person seeking review of a relevant administrative decision. The tribunal's determination of such an issue is a necessary incident of reviewing a reviewable decision. In that regard, the tribunal does not determine the question of the legislation's constitutional validity. Instead, the tribunal determines whether the legislation's application by a Commonwealth officer to a particular person in particular circumstances in making a reviewable decision is a valid application of any such legislation, so that the tribunal interprets the legislation having regard to the constitutional limitations on the Commonwealth's legislative powers.[72]

A tribunal that is not a court and that is invested with non-judicial power correspondingly has authority – in the exercise of non-judicial power – to make up its mind and decide, in the sense of forming an opinion, about the limits of its own jurisdiction for the purpose of moulding its conduct to accord with the law.[73] A Commonwealth officer, such as the Federal Commissioner of Taxation, and a tribunal reviewing a decision of a Commonwealth officer, such as the Administrative Appeals Tribunal, has a duty to ensure that the Commonwealth's legislative powers are not exceeded. The formation of an opinion in that regard while making or reviewing an administrative decision is not an authoritative binding decision on the constitutional validity of any legislation.[74] The Federal Commissioner of Taxation, and the Administrative Appeals Tribunal must administer Commonwealth legislation to read and construe the legislation not to exceed the legislative power of the Commonwealth.[75]

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71 *Health Insurance Commission v Peverill* (1994) 179 CLR 226, 237-8 per Mason CJ, Deane and Gaudron JJ.

72 *Walsh v Commissioner of Taxation* [2012] AATA 451 (18 July 2012).

73 *Citta Hobart Pty Ltd v Cawthorn* (2022) 96 ALJR 476 [24] per Kiefel CJ, Gageler, Keane, Gordon, Steward and Gleeson JJ.

74 Ibid [62]-[65] per Edelman J.

75 *AIA 1901* s 15A.

As intimated above, the application of *Constitution* s 51(xxxi) to any compulsory commutation of a 'superannuation interest' is evidenced by such provisions as of Schedule 1 to the *TAA 1953* sch 1, ss 131-60 and 135-80. These provisions make the Commonwealth liable to pay compensation on 'just terms' to superannuation fund trustees for the loss to the fund of any 'superannuation interest' where a superannuant beneficiary chooses to seek the 'release' of any of his or her 'superannuation interests' from a superannuation fund. A superannuant beneficiary might seek such a 'release' so as not to incur tax or any other liabilities pertaining to the operation of the taxation laws.

An administrator exercising administrative powers inherently must interpret and apply relevant legislation in a way that is consistent with its constitutional validity. The interpretation and application of legislation in a way that is consistent with its constitutional validity is an essential part of the administrator moulding the administrative conduct according to law wherever a question of constitutional validity is relevant to administrative decision-making. An issue of constitutional validity can arise wherever it pertains to a question of whether legislation before the administrator can validly apply under the Constitution in particular circumstances or to a particular person or persons. This required approach is distinct from purporting to rule on the constitutional validity of the legislation which would involve an exercise of the judicial power of the Commonwealth not vested in an administrator.[76]

It is important to correctly demarcate what is a constitutional question from what is one of statutory interpretation. The constitutional question is whether the statutory authority conferred on the Executive is within the competence of the Parliament as contrasted with the statutory question whether the administrative action in question is authorised by the statute. If, on its proper construction, the statute complies with the constitutional limitation, without any need to read it down to save its validity, any complaint respecting the exercise of power thereunder in each case does not raise a constitutional question, as distinct from a question of the exercise of statutory power.[77]

An administrative law issue must not be confused with a constitutional law issue. The constitutional question is limited to whether an Act of Parliament is within the constitutional powers of the Parliament which has enacted the Act. Issues pertaining to whether directions, regulations or other subordinate legislation made under an Act would, if made by the Act be constitutional, do not raise a constitutional matter but an administrative law matter whose resolution involves an exercise of statutory interpretation as to whether the subordinate legislation is *ultra vires* the Act under which it is purported to have been made.[78]

A constitutional challenge to the State of Victoria's lockdown directions was misconceived because constitutional challenges can only be brought to an Act of Parliament and not to

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[76] *Walsh v Commissioner of Taxation* [2012] AATA 451.

[77] *AJL20* (n 30) [43] per Kiefel CJ, Gageler, Keane and Steward JJ.

[78] *Palmer v Western Australia* (2021) 272 CLR 505.

subordinate legislation whose purported operation within the terms of an authorising Act is a matter of statutory interpretation and of administrative law.[79]

Accordingly, any regulations would be inoperative as a matter of statutory interpretation and administrative law which might purport to provide for the compulsory commutation of beneficiaries' 'superannuation interests' where there is no provision for the beneficiaries to receive compensation on 'just terms'.

VI CONCLUSION

This article has set out to illustrate how what is presented in politically motivated statements by Commonwealth Treasurers, such as Morrison; for example, the achievement of tax neutrality, are countered by prolix legislation of the kind introduced into Parliament which commenced on 1 July 2017, whose implementation seems to serve rather a different objective of pension financialisation.[80]

Pension commutation conflicts with the prescribed ambit, object, and key operational provisions in the principal Act. For example, this conflict can be illustrated by reference to such key provisions as *ITAA 1997* s 294.1 (ambit), s 294.5 (object) and s 294.120 (operation). Consequently, any 'excess' must be brought to account by taxation and not by any compulsory commutation of a 'superannuation interest'.

A possible avenue for future research is how the analysis in this article may impact upon a present proposal for complex legislation to 'cap' how much money a superannuation fund beneficiary may continue leaving in a superannuation accumulation account so as to continue receiving 'a generous concessional tax rate of 15 per cent on earnings and contributions, well below the top marginal income tax rate of 45 per cent'.[81] If tax neutrality is the objective rather than financialisation of superannuation interests,[82] it would be preferable to proceed in accordance with what TTI proposes so that, instead of any excess resulting in compulsory commutation of a 'superannuation interest', 'subjecting excessive amounts to personal income tax'.[83]

The requirement to interpret and apply Commonwealth legislation to keep its operation within the constitutional limits on the Commonwealth's legislative powers, given such requirements for there to be provision in Commonwealth legislation for compensation on 'just terms' in Commonwealth 'laws … with respect to ... [t]he acquisition of property',[84] makes it important for there to be a focus on the Commonwealth legislating 'with respect

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[79] *Cotterill v Romanes (*2021) 360 FLR 341; [2021] VSC 498 (17 August 2021).

[80] Broomhill et al (n 4) 88-9.

[81] Read (n 28) 27.

[82] Broomhill et al (n 4) 88-9.

[83] TTI (n 23) 28.

[84] *Australian Constitution* s 51(xxxi).

to … Taxation'.[85] Instead of any excess resulting in compulsory commutation of a 'superannuation interest', 'subjecting excessive amounts to personal income tax'.[86]

Another potentially fruitful avenue for further research is to ascertain the influence of the private superannuation funds on the emphasis in the 2017 legislation on 'commutation' of superannuation, given such considerations as that:

1. An examination of what is necessary to establish a balanced, comprehensive, and multidimensional understanding of what equity means in the Australian superannuation system has identified a comprehensive series of regressive superannuation tax concessions as the recommended area for improvement so that the inequity can be redressed.[87]
2. Given the long-term trend towards increasing income inequality in Australia, it has been contended that there are convincing arguments towards an emphasis in retirement policies that distribute income more equally. Consequently, a case has been put forward that there is merit in Australia's superannuation system being complemented by a fully funded government run defined benefits scheme. A comprehensive review of this nature would incorporate a review of the tax concessions and their negative effect on the Australian government's budgetary position.[88]

The limitations of the analysis that so far has been made in this area seem to derive from, first, the prolixity and incomprehensibility of so much of the potentially relevant legislation with all the jargon that is there; second, the relevant legislation being contained in such a plethora of so many legislative instruments, cross-referencing to each other, instead of in one Act; third, the dearth of direct case authorities; fourth, there being relatively few academic articles on the subject; fifth, there being almost no discussion of, or attention to, the issues by the financial services industry, including consumer advocates; and, sixth, the lack of information in the public arena as to how superannuation funds are calculating the monies that they credit and debit to their beneficiaries' transfer balance accounts which the superannuation funds report to the ATO.

Pertinent to university tax clinics is that the High Court of Australia has over the past two years made it clear that challenging a regulation as being outside the legislative powers of either the Commonwealth Parliament or the Parliament of a State is a matter of administrative law within the ordinary jurisdiction of a relevant Federal or State court or tribunal, as contrasted with attracting the High Court's jurisdiction as having arisen under the *Constitution* or involving its interpretation.[89] The assistance by tax students in tax clinics with respect to such everyday matters as client applications for review to the Administrative Appeals Tribunal provides useful training. A client's application for review

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[85] Ibid s 51(ii).

[86] TTI (n 23) 28.

[87] Harrison (n 19).

[88] Hanegbi (n 21) 303.

[89] *Palmer* (n 78) and *AJL20* (n 30) [43] per Kiefel CJ, Gageler, Keane and Steward JJ.

of a decision by the Federal Commissioner of Taxation to issue an 'excess transfer balance determination' is within the Administrative Appeals Tribunal's jurisdiction.[90] It is such an 'excess transfer balance determination', if not overturned by the Tribunal, which becomes the basis of a subsequent 'commutation authority' for a superannuation fund trustee to 'commute' the client's pension.

Analysis of the kind conducted in this article might usefully be a central focus of tax teachers. The teaching of tax inherently relates to its practice. Effective tax laws are an essential tool of the tax practitioner. The maintenance of acceptable drafting standards with respect to the tax laws therefore should concern all tax teachers. In analysing some key features of Morrison's 2017 superannuation-related legislation, this article has sought to demonstrate the importance of legislative drafting standards to there being effective tax laws. An examination of the 2017 legislation compared with its objects and purposes as enunciated by Morrison in his second reading speech shows, in accordance with what is set out at the start of this article, and in the subsequent analysis, that it fails to meet any of three essential key criteria.

The legislation fails the transparency criteria being expressed in so much jargon that one needs the equivalent of a foreign language dictionary to begin obtaining any sense or meaning to it. The legislation fails the accessible criterion being contained in multiple Acts and a plethora of regulations in language which is hard to decipher. The legislation fails the congruent criterion in lending itself towards the expropriation of beneficiaries' pensions by superannuation fund trustees notwithstanding such an outcome often conflicts with Morrison's proclaimed object of tax neutrality.

The contrast between, on the one hand, what Morrison introduced into Parliament enacted as law commencing from 1 July 2017 with, instead, on the other hand, what should have been a short clear concise legislative amendment centred on one Act, namely, the *ITAA 1997*, in plain English simply to provide that pre-1 July 2017 tax-free superannuation income stream earnings above the prescribed cap become assessable income after 1 July 2017, should illustrate the importance of how the future of tax must be more than just politics. Taking the politics out of tax reform requires the simplification of the tax laws to make them comprehensible.

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[90] *TAA 1953* (n 52) sch 1, s 136.15; ibid pt IVC; *Citta Hobart* (n 73) [24] per Kiefel CJ, Gageler, Keane, Gordon, Steward and Gleeson JJ; [62]-[65] per Edelman J; and *Walsh v Commissioner of Taxation* [2012] AATA 451 (18 July 2012).

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