Payroll tax de-grouping

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Abstract: Payroll tax legislation invariably includes "grouping" rules, the effect of which is to group related employer entities so that only one threshold for wages is available for the group. In recognition of the broad ambit of the grouping provisions, they are accompanied by provisions that allow the revenue authority to "de-group" employers. The purpose of this article is to take stock of the case law about the grouping provisions, and to suggest ways to assist practical compliance, principled decision-making and dispute resolution. The author also believes that it is important to consider group members' exposure to others' debts. The article discusses whether grouping and de-grouping amounts to taxation by discretion, with some suggestions concerning principled decision-making, recent case law about grouping and de-grouping, common taxpayer mistakes and misconceptions, whether the revenue authority asks the right questions when considering de-grouping applications, and recovery issues when part of the group fails.

Introduction

Payroll tax is of increasing importance in state budgets. Tax practitioners are seeing an increase in audits and adjustments. My experience is that businesses are surprised by the existence and reach of rules that group businesses, with the effect that only one threshold for wages is available for the group.

It is timely to take stock of the case law about the grouping provisions, and suggest ways to assist practical compliance, principled decision-making and dispute resolution. With mounting tax debt becoming an issue, it is also important to consider group members' exposure to others' debts. Topics covered include:

(1) whether grouping and de-grouping amounts to taxation by discretion, with some suggestions concerning principled decision-making;

(2) recent case law about grouping;

(3) recent case law about de-grouping;

(4) common taxpayer mistakes and misconceptions;

(5) whether the Commissioner asks the right questions when considering de-grouping applications. A couple of points have emerged from recent matters where the wrong emphasis seems to have been taken in asking questions about de-grouping; and

(6) recovery issues when part of the group fails.

An earlier version of this article was presented for The Tax Institute in July 2011 at the States' Taxation Conference. I have updated the article since then because of two developments. The first development is the decision of the Victorian Civil and Administrative Tribunal, *Liquid Rock Constructions Pty Ltd v Commissioner of State Revenue*,[1] which begins to solve one of the puzzles about the harmonised common employment grouping rules. Second, I mention the decision of the High Court in *Tasty Chicks.* As to the latter, I have not amended all references to the decisions below. The High Court's decision is on narrow administrative law grounds. Thus, what I have previously said about other aspects of the decisions of the New South Wales Court of Appeal and Gzell J largely stands.

The reason for grouping provisions

The system for payment and collection of payroll tax for a single employer (that is, one not grouped) in Queensland involves monthly payments calculated by applying the appropriate rate of payroll tax to the greater of zero and the amount equal to the total of taxable wages during the period, "less the periodic deduction" (s 20(1)(b) of the *Payroll Tax Act 1971* (Qld) (Qld Act)). (There is an annual reconciliation, but that does not affect the thrust of this explanation.)

The amount of the periodic deduction is worked out using complex formulae in s 17 Qld Act. The periodic deduction apportions the annual tax-free threshold across the year. The effect of that is that such a non-grouped employer, having taxable wages below a particular monetary threshold, might have a more or less significant deduction from the periodic payment of payroll tax, which then washed up at the end of the year.

While the mechanisms differ in detail, similar provisions apply elsewhere.[2]

Payroll tax was handed by the Commonwealth to the states in 1971 as a growth tax. In the mid-1970s, various states introduced grouping provisions. These grouping provisions were to overcome the possibility of the splitting of businesses, with the consequent possibility that each separate business might gain a deduction. As *Baxter*, *Artistic*, and other cases discussed below show, this remains an important consideration in the interpretation and application of the provisions.

In recognition of the broad ambit of the grouping provisions, they were accompanied by the introduction of provisions that allow the Commissioner to "de-group" employers.

Legislative provisions

I refer to the provisions in Queensland, with comparatives given by note.

General approach to the interpretation of the legislative provisions

In *Baxter v Chief Commissioner of Pay-roll Tax*,[3] Yeldham J said that the Part containing the grouping provisions was introduced in New South Wales in 1975 and that:

> "It is obviously designed to prevent the splitting of businesses, and to avoid other devices for the minimising of any liability for pay-roll tax."

His Honour went on to say:[4]

> "In construing s 16H it is necessary to keep firmly in mind that the grouping provisions to be found in Pt IVA cast an exceptionally wide net and potentially give rise to a great many unintended grouping situations. The provisions of s 16H(1) were intended to provide a balance against this to prevent injustice from being done in particular cases and hence, in my view, it should not be given a narrow construction."

The section referred to there, s 16H of the former NSW Act, is the equivalent of s 74 in Queensland, though detail differs.[5]

McPherson J came to the same view as Yeldham J as to the reason for the grouping provisions. See *John French Pty Ltd v Commissioner of Pay-roll Tax*.[6]

The NSW Court of Appeal has emphasised the importance of the Commissioner's power to de-group. In *Commissioner of Pay-roll Tax v RG Elsegood & Co Pty Ltd*, Hutley JA said:[7]

> "The judgment under appeal suggests harsh possibilities if the appeal is allowed. The legislature has itself recognized that the Commissioner needs an administrative discretion to exempt businesses which, according to the strict interpretation of the requirements for grouping, would be caught. This does not exempt the court from the burden of construing the words as they stand, but it does suggest that some of the fearful consequences envisaged by the respondents may not be real, in that the Commissioner will have power to alleviate them, and this limits the force of the argument from consequences."

Samuels JA concurred in those reasons. Mahoney JA came to the same view.[8] This suggests that some real scope must be given to the operation of the de-grouping rules, rather than simply starting with the proposition that entities are grouped, and laying any great weight upon the reasons (eg common control, common employees) that resulted in the grouping. Those reasons are a given, and they are the reason for the remedy.

In *Plummers Border Valley Orchards Pty Ltd v Commissioner of Taxes*,[9] Riley J said this of the legislative purpose of the de-grouping provision in the Northern Territory most closely related to that under discussion above:

> "The appellant complained that the Commissioner failed to consider the anti-avoidance purpose of grouping entities and failed to properly consider the concessionary nature of the exclusion provided for in s 17H of the Pay-roll Tax Act 1978. The effect of s 17H is to ameliorate any absurd or unjust operation of the grouping provisions of the Act and, it was submitted, should be approached accordingly. The section is 'intended to provide a balance" against unintended groupings and "to prevent injustice from being done in particular cases': *Baxter & Anor v Chief Commissioner of Pay–roll Tax* (1986) 7 NSWLR 122 at 131; 18 ATR 627 at 635; 86 ATC 4816 at 4823."

See also *Re Portaplant Australia Pty Ltd and Chief Commissioner of State Revenue*[10] summarising the law, and the general comments of the High Court of Australia in the recent decision of *Tasty Chicks Pty Ltd & Ors v Chief Commissioner of State Revenue (NSW)*.[11]

In the Revenue's appeal from the decision of the State Administrative Tribunal of Western Australia in *Artistic*,[12] the Commissioner unsuccessfully contended that the tribunal had wrongly taken into account as "irrelevant considerations" two factors, namely:[13]

(1) that there was no suggestion that the three entities were split into separate entities to avoid payroll tax; and

(2) that the application of the grouping provisions would impose a burden on a small business not imposed on competitors of a similar size.

These factors were said to have been taken into account by the tribunal in the context of its consideration of whether it was "just and reasonable" for a taxpayer not to be grouped. That phrase still occurs in WA. It is also necessary to deal with that phrase in Queensland for pre-harmonisation years, for example, under former s 69(7)(b) Qld Act (commonly controlled businesses) and former s 68(2) Qld Act (common employees). Perhaps what is said in that regard has an impact in relation to post-harmonisation language, where the Commissioner is empowered to take into account "any other matters the Commissioner considers relevant".[14] The Court of Appeal of the Supreme Court of Western Australia said:[15]

> "The expression 'just and reasonable' is an expression obviously calculated by the legislature to enable the Commissioner, and the Tribunal standing in his shoes, to consider a wide range of circumstances that may be relevant to the exercise of a discretion in respect of the grouping of taxpayers. Given the breadth of language employed by the legislature, the Commissioner must overcome a significant hurdle to establish that the matters referred to by the Tribunal are irrelevant."

The court then said that, if the businesses in question have been "split off from one larger business", that fact "would plainly be relevant to the exercise of the discretion in respect of grouping".[16] On one view, what the New South Wales Court of Appeal said in *Chief Commissioner of State Revenue v Tasty Chicks*[17] might be thought to conflict with the WA Court of Appeal's view, but it is not clear whether *Artistic* was cited to the New South Wales Court of Appeal. Following *Farrah Constructions v Say-Dee*,[18] an intermediate appellant court should follow a decision of another such court, unless persuaded that the earlier judgment is plainly wrong.

The WA Court of Appeal then noted that the Commissioner had "properly conceded, in the course of argument" that the range of considerations embraced by the expression "just and reasonable" included considerations personal to the prospective taxpayer.[19] The financial burden which would be imposed on such a taxpayer, in contrast to competitive businesses of the same size which were not subject to such a burden, were said to be "plainly just such a consideration".[19]

Conclusions as to disposition of decision-maker when approaching de-grouping

As we will see, the positive operation of the grouping provisions is very powerful and can lead to some surprising results.

The case law is plain that the legislative antidote to too exorbitant an operation of the positive grouping rules is the Commissioner's discretion to de-group. The legislature has committed the responsibility to the executive branch of government. When preparing this article, I was challenged to consider whether this meant that there was "taxation by discretion". A narrow and unsatisfactory answer would be that the breadth of taxation is positively determined without resort to administrative discretion, and that administrative discretion simply gives relief.

A more useful answer, however, is that the legislature relies on a principled application of the de-grouping provisions by the executive branch. Under the previous sub-heading, I have suggested the disposition which should inform that principled exercise of discretion.

To summarise, from the earliest de-grouping decisions, it has been recognised that the grouping provisions were "designed to prevent the splitting of businesses". The grouping provisions "cast an exceptionally wide net and potentially give rise to a great many unintended

grouping situations". The de-grouping provisions were thus "intended to provide a balance against this to prevent injustice from being done in particular cases and … should not be given a narrow construction".

The existence of the de-grouping provisions is significant in the interpretation of the positive grouping provisions because, even where there are "fearful consequences" of a particular interpretation of a grouping provision, "the Commissioner will have power to alleviate them".

It is relevant to take into account, under either the "just and reasonable" rubric, or I would suggest under the power to take into account "any other matters the Commissioner considers relevant", whether entities have been split to avoid payroll tax.[20]

You will see it suggested by some that, to enliven the de-grouping discretion, one has to look for some element of injustice, or an unintended consequence arising from grouping, by which the speaker in those cases truly means something exceptional and out of the ordinary. Such an approach often starts with the proposition that the positive grouping provision generally gets the grouping right.

I do not think that this is the correct disposition. One is not looking only for the absurd. One is looking for the administrative decision-maker to reach the correct or preferable decision, bearing in mind the "exceptionally wide net" of the positive grouping provisions, which "potentially give rise to a great many unintended grouping situations". That is the disposition which should inform principled decision-making in this area.

As we shall see below, this particularly comes to the fore following the broadening of the "relevant agreement" provisions after *The Muir Electrical Co Pty Ltd v Commissioner of State Revenue*.[21] These have been a game-changer.

Common employees

I have recently had a matter where, for years pre-harmonisation, grouping under former s 68 Qld Act was in issue.[22] The positive (grouping) provisions here were:

> "(1) For the purposes of this Act, where —
>
> (a) an employee of an employer or 2 or more employees of an employer performs or perform duties solely or mainly for or in connection with a business carried on by that employer and another person or other persons or by another person or other persons; or
>
> (b) an employer has, in respect of the employment of or the performance of duties by 1 or more of the employer's employees, an agreement, arrangement or undertaking (whether formal or informal, whether expressed or implied and whether or not the agreement, arrangement or undertaking includes provisions in respect of the supply of goods or services or goods and services) with another person or other persons relating to a business carried on by that other person or those other persons, whether alone or together with another person or other persons;
>
> that employer and —
>
> (c) each such other person; or
>
> (d) both or all of those other persons;
>
> constitute a group."

Former s 68(1)(a) Qld Act resembles post-harmonisation s 70(1) Qld Act. The limitation is that the "employer" must carry on business with the other person who is to be grouped.[23] See, for example, *Chief Commissioner of State Revenue v Tasty Chicks*.[24]

Former s 68(1)(b) Qld Act is substantially the same as the former s 9A(1A)(c) Vic Act considered by the Victorian Court of Appeal in *The Muir Electrical Co Pty Ltd v Commissioner of State Revenue* (2001) 4 VR 70.[25]

The following quote from *The Muir Electrical Co Pty Ltd v Commissioner of State Revenue* seems apposite:[26]

> "Returning to the facts of the present case, it cannot be said that the supplemental deed is an agreement in respect of the performance of duties by one or more of Muir's employees. It is an agreement for the provision of services by Muirs, leaving Muirs free to choose how it will provide those services. It was not denied on behalf of the respondent that the provision of the services could be sub-contracted to another company, nor was it suggested that the agreement was a sham or that it did not represent the true agreement between the parties."

Not surprisingly, this was followed by Gzell J in *Tasty Chicks Pty Ltd v Chief Commissioner of State Revenue*[27] and, in his so doing, was approved by the New South Wales Court of Appeal.[28]

The Victorian legislature addressed the issue in 2003, as we shall see.

Broadening of provisions post-harmonisation

With harmonisation, Queensland introduced s 70(2), which provides:[29]

> "If 1 or more employees of an employer are employed solely or mainly to perform duties in connection with 1 or more businesses carried on by 1 or more other persons, the employer and each of those other persons constitute a group."

Again, there is a substantial threshold here of "solely or mainly". This provision need not detain us.

Post-Muir Electrical re-write of "relevant agreement" provision

The extract of former s 68 Qld Act above includes, as former s 68(1)(b), a provision which is of a type that I will refer to as a "relevant agreement" provision. The key to that provision was that the relevant agreement had to be "in respect of the employment of or the performance of duties by" the employer's employee. Thus, an arrangement under which services were offered by a central service company to a number of franchisees (where no particular employee duties are prescribed) could comfortably be seen as not caught by such a provision.

Following the 2001 Victorian Court of Appeal decision in *Muir Electrical* (mentioned above), Victoria amended its "relevant agreement" provision and, on harmonisation, other states have followed. The provisions in Queensland are in s 70(3) and (4):[30]

"Even where there are 'fearful consequences' … 'the Commissioner will have power to alleviate them'."

"(3) If 1 or more employees of an employer perform duties —

(a) in connection with 1 or more business carried on by 1 or more other persons; and

(b) in connection with, or in fulfilment of the employer's obligation under, a relevant agreement;

the employer and each of those other persons constitute a group.

(4) In this section —

relevant agreement means an agreement, arrangement or undertaking for services to be provided to 1 or more of the other persons in connection with the business or those businesses carried on by the other person or persons —

(a) whether the agreement, arrangement or undertaking is formal or informal, express or implied; and

(b) whether or not the agreement, arrangement or undertaking provides for duties to be performed by the employees or states the duties to be performed by the employees or states the duties to be performed by them."

The move to broaden the relevant agreement provisions following *Muir Electrical* began in Victoria with s 19 of the *State Taxation Acts (Miscellaneous Amendments) Act 2003*, which amended former s 9A Vic Act. The difficulty with this amendment is that, on one reading, it essentially groups the entire world.

When this article was presented in July 2011, I deliberately included this provocative example:

(1) read broadly, an audit firm, which provides services to a company under its audit retainer, will be grouped with that company because the audit firm has employees who perform duties in connection with the business carried on by the company;

(2) as the audit firm will have a number of clients, each of those clients is a sub-group with the audit firm, which sub-groups are subsumed into a larger group by provisions such as s 74 Qld Act;

(3) if that audit firm also does trust account audits for, say, law firms and letting agents, this would draw into that large group each of the law firms, each of the letting agents, and presumably each of the clients of the law firms and letting agents; and

(4) thus, if an international audit firm audits an international bank, literally the entire world is drawn into one large group.

As expected, this example given by me at a conference attended by Revenue officers and private practitioners elicited differing views. The effects of a broad interpretation of these provisions have since been drawn to the attention of the Victorian Civil and Administrative Appeals Tribunal in *Liquid Rock Constructions Pty Ltd v Commissioner of State Revenue*.[31]

The comments of Deputy President Macnamara in *Liquid Rock* are significant, and may solve this puzzle for the Revenue and taxpayers. The Deputy President posed an example of:[32]

"... a company providing accountancy services and a company providing gardening services. On a regular basis an employee of the gardening service company attends the premises occupied by the accountancy company, the employee mows the lawn, weeds the flower beds and performs other functions in the garden as requested by the accountancy company's office manager. This is done pursuant to an on-going contract or arrangement between the accountancy company and the gardening company. One would not imagine that this would lead the two companies to be grouped subject only to the Commissioner's discretionary power to de-group. The question would be why? Is there some analytical explanation beyond what Doyle CJ described as 'an element of impression'?"

Deputy President Macnamara then pointed out that the Victorian provision, upon which harmonised provisions were based, required that there be:[33]

"Duties performed in connection with or in fulfilment of the employer's obligation under an agreement, arrangement or undertaking for the provision of services …"

The Deputy President then reasoned that the gardening and accountancy businesses in his example would not be grouped because:[34]

"... whilst the gardening employee would be furnishing services in connection with the conduct or business of the accounting company to enable it to provide an acceptable face to its clients and the public generally, he would not be performing duties. Parliament has deliberately chosen a different phrase referring to the performance of duties in the one place and the provision of services in another to cater for this sort of distinction."

Without wishing to go into the more complex facts before the Victorian Civil and Administrative Tribunal in that case, it is sufficient to note how the Deputy President applied that reasoning, both under the former and present Victorian provisions about common employment:[35]

"In my view someone in Ms Asvestas' situation will be regarded as supplying services to LRP in the circumstances described in the evidence. *She would not be regarded as performing duties for or in connection with its business unless there is at least some power on the part of LRP to direct her as to the manner of the performance of those alleged duties.* The evidence in this case was that it was entirely at the discretion of LRC and its controllers Mr De Spirito and Mr Malone as to whether the particular work would be done and exactly how it would be done, that is, whether immediately, some hours later this afternoon or perhaps only next week. *It would be going too far I think to suggest that the relevant paragraph requires a relationship of such a nature that one could regard Ms Asvestas as being not only an employee of LRC but also LRF before the paragraph could operate;* but I am clear that the present situation falls outside what is contemplated ..." (emphasis added)

This is a significant judgment — all the more significant because of the standing of the Deputy President and his experience in payroll tax matters. The remaining difficulties are also apparent from the judgment. No bright line test is given, as is evident from the concluding sentence in the passage.

Let me return to my example of the listed company, its audit firm, law firms, letting agents and international banks. I have provocatively asked whether these provisions now group the whole world.

I am sure that *Liquid Rock*, decided since this example was publicly discussed, will be cited as an answer in all the clear cases. But the absence of a bright line test remains a concern. For, as we shall see, even if my example is even arguably correct, this may have curious results under the new collection provisions, which make each group member liable for the payroll tax of all other group members.

I was not the first to point out the difficulty with the post-harmonisation relevant agreement provisions.[36] Once the breadth of the post-harmonisation relevant agreement provisions is explained to a court or tribunal, it will be a short step for that court or tribunal to de-group *if* there is power. However, see below.

This rather suggests that a realistic attitude to de-grouping will also follow at an administrative point. It shows the difficulty for the revenue authority when the

legislation has a "fuzzy" focus, and draws too many in to the net.

Practical operation of old and new de-grouping provisions

A deal of my work still involves pre-harmonisation payroll tax. That is a function of the extent of look-back on audit, and of the fact that cases take some time to percolate through the system. I therefore have a perspective of the development of these provisions. I trust, therefore, that you will bear with me as I work through old and new de-grouping provisions, again using Queensland as a base for comparison.

De-grouping operation of former s 68(2) Qld Act

Former s 68(2) Qld Act read:

> **"Grouping where employees used in another business**
>
> …
>
> (2) Where the commissioner is satisfied, having regard to the nature and degree of the duties referred to in subsection (1) and to any other matters that the commissioner considers relevant, that it would not be just and reasonable to include as a member of a group a person or persons carrying on a business, the commissioner may, by order in writing served on that person or those persons, exclude the person or persons from the group."

The subsection directs the Commissioner's attention to two specific factors, "and any other factors that the Commissioner considers relevant". The phrase "just and reasonable" is dealt with above.

De-grouping operation under former s 69(7) Qld Act

Former s 69(7) Qld Act provided:

> **"Grouping of commonly controlled businesses**
>
> …
>
> (7) Where the commissioner is satisfied, having regard to the nature and degree of ownership or control of businesses that constitute a group and to any other matters that the commissioner considers relevant, that —
>
> (a) a business carried on by a member of that group is carried on substantially independently of and is not substantially connected with the carrying on of a business carried on by any other member of that group; and
>
> (b) it is just and reasonable that the first mentioned member be excluded from that group;
>
> the commissioner may, by order in writing served on the first mentioned member, exclude that member from that group."

Modern de-grouping provision on harmonisation

The provisions of interest here are s 74(2) and (3) Qld Act:

> "(2) The commissioner may make an exclusion order only if the commissioner is satisfied a business carried on by the person is carried on independently of, and is not connected with the carrying on of, a business carried on by any other member of the group.
>
> (3) For deciding whether to make an exclusion order, the commissioner must have regard to:
>
> (a) the nature and degree of ownership and control of the businesses carried on by the person and the other members of the group; and
>
> (b) the nature of the businesses; and
>
> (c) any other matters the commissioner considers relevant."

The changes thus wrought in Queensland on harmonisation were:

(1) to extend to grouping under common employee cases some of the factors previously only expressly relevant to common control cases;

(2) to reorder those factors in the de-grouping provision, so that there would now be an argument as to whether the factors in s 74(3) in some way add content, not previously present, to the consideration of independence and connection;

(3) to substitute for the test for "just and reasonable that the [group member] be excluded" a requirement that the Commissioner must have regard to "any other matters the Commissioner considers relevant"; and

(d) to delete the concept of "substantial".

Nevertheless, something can be learned from the past treatment of provisions like former ss 68(2) and 69(7) Qld Act.

Relevance of nature and degree of ownership

The commencing words of former s 69(7) Qld Act refer to two matters to which the Commissioner is to have regard when evaluating the matters mentioned in paras (a) and (b). As noted above, the re-ordering of these provisions in the present s 74 Qld Act does raise a question as to how those factors are to be evaluated, and as to whether they are additional substantive hurdles or simply matters that must be evaluated in reaching the state of satisfaction required by s 74(2) Qld Act. To me, it is the latter, so that the analysis of cases about former s 69(7) Qld Act is a useful exercise, as is an analysis of cases about those provisions interstate which were analogues of that former Queensland provision.

The Commissioner is not required to be satisfied of anything mentioned in the commencing words, but takes those matters into consideration when evaluating the matters mentioned in paras (a) and (b). See the lengthy passage in *Commissioner of State Taxation (WA) v Scotford Cameron & Middleton Pty Ltd*.[37]

Common ownership cannot, alone, oust the power to de-group which is conferred, but it is a factor to be taken into account.[38]

As McPherson J said in *John French Pty Ltd v Commissioner of Pay-roll Tax*:[39]

> "Because ownership or control are among the factors which operate to produce a group under ss. 16B to 16D, a number of the reported cases emphasise that such factors alone are not sufficient to prevent exclusion pursuant to s. 16H: see *Mead Packaging (Aust.) Pty. Ltd v. Commissioner of Pay–roll Tax* ..."

And yet practitioners repeatedly see cases where the primary decision-maker has relied entirely on the ownership and control without going to the next necessary stage of making the required evaluation as to whether the primary decision-maker is "satisfied a business carried on by the person is carried on independently of, and is not connected with the carrying on of, a business carried on by any other member of the group" (s 74(2) Qld Act). This is an old error which recurs.

Where the degree of ownership is at the minimum level for grouping to have operated, one can discount the "degree of ownership" as a significant factor in favour of maintaining the group.[40]

In the context of the then equivalent WA de-grouping rule, it has been said that there is a difference between a mere capacity to control and actual control.[41] This difference is relevant to assessing the degree and nature of common ownership because, if one person is a silent partner, simply protecting their investment in a passive way, and the other is an active participant, the Commissioner is obliged to

take that into account when assessing the "nature and degree of ... control".

Recent de-grouping case

Port Augusta Medical Centre Pty Ltd v Commissioner of State Taxation[42] is yet another "facts case" about de-grouping. The de-grouping provision relied on there (former s18I SA Act) has some similarity to former s 69(7) Qld Act. It includes as an express relevant consideration of the nature of the businesses,[43] and it omits a reference to it being "just and reasonable" to exclude.

Peek J[44] not surprisingly approves the statement of Rath J in *Mead Packaging*.[45] And his Honour approves of the proposition that a particular business, to be de-grouped under this provision, must show substantial independence and to be not substantially connected, as against each other member of the group, to be let out.[46]

Peek J's comments[47] as to there being a substantial connection between PAMC Pty Ltd[48] on the one hand, and each of Vay Pty Ltd and Guyram Pty Ltd on the other hand, owing to profit distribution, are somewhat difficult to understand outside the individualistic structure adopted by the doctors in this case. The situation would be different where operating income (where a profit is made) does not flow between members of the group that conduct businesses, but rather to investing entities.[49]

Approach to former s 69(7)(a) and (b) Qld Act

In an oft-cited passage, Rath J said in *Mead Packaging (Aust) Pty Ltd v Commissioner of Pay-roll Tax (NSW)*:[50]

> "Section 16H(1) requires two findings to be made, namely (1) that a business carried on by the plaintiff (as a member of a group) is carried on substantially independently of a business carried on by any other member of that group; and (2) that the business is not substantially connected with the carrying on of the business carried on by the other member of the group. The first limb appears to relate to the independence of the businesses, and requires an examination of the connection between the business activities. The second limb appears to relate to connection in management. At all events the composite expression used in the subsection requires a consideration of the businesses and their control, and a finding of substantial independence and substantial absence of connection."

The Full Court of Queensland in *John French Pty Ltd v Commissioner of Pay-roll Tax*[51] has questioned whether the division in focus between the first and second limb is correct, but has said that both the business and management must be considered:[52]

> "I am not altogether convinced that the distinction suggested by His Honour between the first and second limbs of s. 16H(1) is readily apparent, but an examination of both business activities and management is clearly justified as part of the inquiry directed by the section."

The same concern had earlier been expressed by the Victorian Taxation Board of Review in *Case* PR/8/80,[53] where Chairman RL Gilbert considered the case on the basis that "connection" connoted something more than management. He pointed out what was required to show a relevant connection:[54]

> "To show the 'connection' required by s 9A calls for something that would go to show a continuous course of active and substantial relationship in a business or commercial sense between the 'carrying on' of the businesses of the parties in question such as to deny that they were 'carried on' independently of each other and to affirm that they were 'carried on' in the necessary 'connection' with each other."

In *Denham Constructions Pty Ltd v Chief Commissioner of State Revenue*,[55] Studdert J, having noted the issue raised by McPherson J in *John French*, nevertheless preferred Rath J's approach.

Rath J and Studdert J's decisions were followed by Riley J in the Northern Territory Supreme Court in *Plummers Border Valley Orchards Pty Ltd v Commissioner of Taxes*.[56]

In *Denham Constructions Pty Ltd v Chief Commissioner of State Revenue*,[57] Studdert J rejected the contention that "management" in the formulation of Rath J was restricted to day-to-day management. With respect, the word "management" does not appear in the statute, and this gloss upon a gloss heralds danger. The question is whether a business carried on is substantially connected with the carrying on of another business. It is plainly relevant to consider whether those involved with one business have day-to-day management of the other business, or have permitted day-to-day management to an active partner. This is something to be considered.

While the mere fact that businesses are different is not decisive in terms of independence,[58] one can nevertheless look at differences in the various businesses. Under pre-harmonisation provisions, this was implicit, and it is now explicit by provisions such as s 74(3)(b) Qld Act. Extreme examples make the point, as in *Re Artistic Pty Ltd v Commissioner of State Revenue* (hairdressing salons de-grouped from electrical contractors).[59] But examples like that present rarely to courts and experience in this field is that, usually, this factor is simply one of many taken into account.

Some focus must also be given to the alleged "connection" in a case. It is only a connection *in the carrying on of the business* which is relevant.[60]

Content of "substantially"

In the pre-harmonisation provision in Queensland (former s 69(7)), the wording used required an evaluation of whether there was *substantial* independence and no *substantial* connection, in the relevant sense. Post-harmonisation provisions do not use the word "substantially". Nevertheless, it is perhaps instructive to look back at the pre-harmonisation wording before considering whether this change makes a difference.

There has been some judicial exposition of "substantially independent of". In *Commissioner of Stamps v Rivington Farms Pty Ltd*, it is said:[61]

> "I point out that in the Shorter Oxford English Dictionary the phrase 'independent of' is said to equal 'independently of' or 'without regard to or irrespective of.' I suppose that in s. 18i one could substitute for the words 'substantially independently of' the words 'substantially without regard to' and give the words the same meaning."

In *Plummers Border Valley Orchards Pty Ltd v Commissioner of Taxes*, Riley J said:[62]

> "The word 'substantially' does not have a fixed meaning. What is required to demonstrate that a business is 'not substantially connected' with another business is a matter of fact and degree to be considered in all of the circumstances. It calls for the exercise of judgment. The connection must be actual and of substance. It must not be minimal yet need not be total."

Studdert J had to deal with the correctness of the NSW pay-roll tax ruling, apparently applied by the Revenue in their decision-making in *Denham Constructions Pty Ltd v Chief Commissioner of State Revenue*.[63] The passage in the ruling spoke of the elements of substantial independence and substantial absence of connection.

While a taxpayer might contend that the ruling considered in *Denham* sets the bar too low in favour of the Revenue, it was nevertheless there held correct to say that: "... if the member of the group satisfies the defendant that any connections are no

more than casual, irregular or occasional occurrences the discretion may be enlivened". I do not understand Studdert J as attempting to say that those words in the ruling replace the words of the statute.

The word "substantially" was also explained as following by Martin CJ in *Crusher Holdings Pty Ltd v Commissioner of Taxes (NT)*:[64]

> "The word 'substantial', or, as here, 'substantially', is not only susceptible to ambiguity, it is a word calculated to conceal a lack of precision; per Deane J *Tillmanns Butcheries Pty Ltd v Australasian Meat Industry Employees' Union* (1979) 42 FLR 331 at 348. It calls for the exercise of judgment."

It is, for example, noteworthy that in *John French*,[65] the common use of offices, board rooms and professional accountants was not thought to be substantial connection (McPherson J and Campbell CJ concurring). It is useful to see how readily such trifling points are discounted by the court.

Absence of the word "substantially"

The only state in which the word "substantially" persists is Western Australia, in the de-grouping provision concerning commonly controlled businesses (s 32(3) WA Act). The question is whether deletion of the word "substantially", from the criteria formerly used in deciding some de-grouping applications, makes a difference.

To begin, to read a word into a statute, where the word is absent, and particularly where it appears that a deliberate decision has been made to omit the word, would be a large step.[66]

We have seen above in *Rivington* that the phrase "independently of" meant "without regard to or irrespective of". That does not mean that the businesses have no interaction. In Queensland, ruling PTA 031.2 attempts to encapsulate the matter this way:[67]

> "The Commissioner must be satisfied that:
>
> (a) there is not a continuous course of active and significant relationship, in a business or commercial sense, between the carrying on of the employer's business and the carrying on of businesses conducted by any other member of the group and
>
> (b) the connections which do exist are no more than casual, irregular or occasional occurrences."

While there is much to be said for that explanation of the current law in that ruling, it does nothing to address what must surely be an unintended consequence: that essentially everyone in commerce is grouped because of the post-*Muir Electrical* relevant agreement provision. In the example I have given above, an audit engagement is usually for a term of years, which could hardly be said to be casual, irregular or occasional. With the other interconnections that I pointed to in the example above, potentially everyone in commerce is pulled in, with apparently no way of being let out.

Liquid Rock, above, only begins to show us a way out of this potentially wide reading of the positive grouping rules. To me, this argues, contrary to *RG Elsegood*, for the positive grouping provision to be read down.

> "… in the move to harmonisation with a common de-grouping provision, something has been lost."

Must de-group, where otherwise satisfied

The word "may" in the resuming words in former s 69(7) Qld Act does not confer a discretion. It confers a power that must be exercised if the satisfaction which conditions it attains.[68] The same must apply with the harmonised de-grouping provision.

Grouping of groups

Former s 71 Qld Act

Former s 71 Qld Act sufficiently explains itself as to its positive operation by its heading: "Smaller groups subsumed into larger groups". The provision is perhaps best visualised in its positive operation by considering the matter in terms of Venn diagrams and set theory.

In the simplest case, where there are two sets with a common member sitting at the intersection of the sets, the two sets (we will call them "groups") are treated as one large group and it is no longer valid to think of any of the members of either of the two smaller sets as being members of the smaller groups (former s 71(1) and (2) Qld Act).

McPherson J explained the matter simply in *John French Pty Ltd v Commissioner of Pay-roll Tax*:[69]

> "The function of this section is not primarily to constitute groups, but to combine them, or, to use the description found in the marginal note to the section, to ensure that 'smaller groups [are] subsumed into larger groups'."

Former s 71(3) Qld Act then provides the Commissioner with a discretion:

> "(3) Where the commissioner is satisfied, having regard to any matters that the commissioner considers relevant, that it would not be just and reasonable to include as members of one group the members of two or more groups, the commissioner may, by order in writing served on the person or persons who are members of those groups, exclude them from that one group."

As to "just and reasonable", see above.

Unfortunately, in the move to harmonisation with a common de-grouping provision, something has been lost here.

Operation of harmonised provision

Under the pre-harmonisation provision, the de-grouping order excluded from the large group members of two or more groups. This then allowed the Commissioner to deal with the de-grouped smaller groups individually.

Under the harmonised provision, the only method of de-grouping available (for example, under s 74 Qld Act) is through the same set of tests mentioned above concerning a business being carried on by the person independently of, and in a way which is not connected with the carrying on of, a business carried on by *any other* member of the group. Thus, it is not sufficient that a member of one sub-group show that it is independent of and not connected with all of the other businesses within that sub-group. It is not even valid, because of Queensland s 68, to think in

those terms. Rather, once the larger group is formed, the only road to exclusion for an individual member is to show, as against every member of every subsumed group in the larger group, that the particular business satisfies the test.

One occasionally sees contentions to the opposite effect, but I consider that the view put here is the better view.

Assisting practical compliance

One point that is perhaps useful to consider is mistakes one sees and misconceptions. I am not saying that these mistakes or misconceptions are made or held by those practising in this field. It is, however, rather the mistakes and misconceptions one sees time and again when matters arrive on one's desk.

Perhaps it is best to list these with brief comments:

(1) that the Commissioner should not have "grouped" the entities. It is trite to us that the legislation groups, and that it is then a matter of applying for the exercise of an administrative discretion for de-grouping, where that discretion is available. However, as we see below in relation to a significant development in debt collecting, this does mean that the taxpayer should now be more alive than ever to ensure that possible grouping is identified, and the Commissioner's view on the possible grouping and on de-grouping be obtained at an early point. Otherwise, absent a de-grouping order, each member of a group can be jointly and severally liable for the payroll tax debts of any member of the group;

(2) a variant on this is that sometimes it is suggested that the grouping provisions are anti-avoidance provisions which do not apply where there is no attempt to split businesses. That again is to misunderstand the positive operation of the grouping provisions, which operate without regard to such factors, as against the discretion to de-group where that has been said to be a relevant consideration. This is particularly worrying in light of the extended breadth now of the "relevant agreement" provisions to do with common employees, where the potential application of the provisions is quite large;

(3) a further variant of the first — that the business can put off raising a matter with the Commissioner on the grounds that the Commissioner would (so it is said) inevitably de-group a particular business when asked. Again, because of the provisions concerning joint and several liability for payroll tax, this is something that can never be put off;

(4) that, in de-grouping, it is simply necessary to run evidence about the independence of a given business from the businesses of a number of the group members. This was never the case, but it has become even more critical now that the de-grouping discretion for smaller groups subsumed into a larger group has changed. Now it is necessary to run evidence (as it almost certainly was wise to do in the past) about independence from every member in the large group. This can be a time-consuming and costly process, and obviously for each additional group member considered, there is an increasing risk of failure in that enterprise; and

(5) as to the forum in which the de-grouping discretion should be reviewed. Unfortunately, this error recurs despite the long lessons of the past. For example, *Conte Mechanical and Electrical Services Pty Ltd v Commissioner of State Revenue*[70] is the latest example of a taxpayer not appreciating the effect of the rule in *Avon Downs* in a court (absent special provision in the appeal rules — see note). Where it is possible to seek merits review in another place such as a tribunal, the taxpayer must go there. If no merits review is available, the taxpayer should reconcile itself to the long odds of overturning a de-grouping decision on error of law.[71]

Recovery issues when part of the group fails – post-harmonisation

There are rules everywhere which are similar to s 51A Qld Act:

> **"Joint and Several Liability of Group Members**
>
> (1) This section applies if a member of a group fails to pay an amount the member is required to pay under this Act in respect of a period.
>
> (2) Every member of the group is liable jointly and severally to pay the amount, whether or not the member was an employer during the period to which the amount relates.
>
> (3) This section is subject to ss 34(2) and 42(2)."

The exceptions there relate to a liability of a relevant group employer to pay, respectively, the designated group employer's annual liability for the financial year and the designated group employer's final liability for the period on the return date for lodgment of the designated group employer's final return.

It would seem that Queensland s 51A is there to catch a situation where there is no designated group employer, either by voluntary designation by the taxpayers or through the process of designation by the Commissioner. Elsewhere, harmonised provisions such as s 81 NSW Act seem to cover the field.[72]

This has enormous consequences, which I will simply list:

(1) where persons are grouped, but it was not obvious that they should have been grouped (for example, if all franchisees of a particular chain are grouped) and there is no relief yet from grouping by a de-grouping order — each franchisee is responsible for each other's liability for payroll tax and for the franchisor's liability for payroll tax. That would make most small businesses insolvent;

(2) as highlighted above, the post-*Muir Electrical* amendment to the relevant agreement provisions mean that, literally read, all of commerce in Australia is drawn into one large group. Because of the narrowing of the de-grouping provisions by, for example, the withdrawal of the word "substantially", there is no obvious way out of grouping for most long-term service relationships, such as audit engagements, letting engagements and retainers. This means that there is something additional for directors of unrelated companies to have to concern themselves with when signing a solvency declaration;

(3) this presents good opportunities for the Commissioner to go debt collecting in a way that does not necessarily involve him later in preference proceedings against a liquidator. The Commissioner can go after an apparently solvent member of the group, leaving that solvent member of the group to prove in any liquidation or administration of other group members for the right of indemnity; and

(4) you will, I think, increasingly see the use of garnishee notices,[73] directed to remaining, apparently solvent, members of groups, to gain a jump on unsecured creditors. One wonders whether the experiment with the Crown giving up its priority in debt collecting three and four decades ago was worthwhile.

Those are the emerging trends I see in debt collecting. With the mounting payroll tax liabilities one sees, owing to better directed audited activities, this is going to be a real focus of future discussions with revenue authorities.

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This article was originally presented at The Tax Institute's 11th Annual States' Taxation Conference, held in Melbourne on 28–29 July 2011.

References

1 [2011] VCAT 2164.

2 *Payroll Tax Act 2007* (NSW) (NSW Act), ss 8 and 9 and see the Schedules; *Payroll Tax Act 2007* (Vic) (Vic Act), ss 8 and 9 and see the Schedules; *Payroll Tax Act 2009* (SA) (SA Act), ss 8 and 9 and see the Schedules; *Payroll Tax Act 2008* (Tas) (Tas Act), ss 8 and 9 and see the Schedules; *Payroll Tax Act* (NT) (NT Act), ss 8 and 9 and see the Schedules: *Payroll Tax Act 2011* (ACT) (ACT Act), ss 8 and 9 and see the Schedules; *Pay-roll Tax Act 2002* (WA) (WA Act), s 26.

3 (1986) 7 NSWLR 122 at 124D.

4 (1986) 7 NSWLR 122 at 131F-G.

5 Former s 16H NSW Act provided relief where there was grouping owing to the common employee rules in former s 16C. The grouping provisions for common employees are now: s 71 NSW Act; s 71 Vic Act; s 71 SA Act; s 31 WA Act; s 70 Qld Act; s 71 Tas Act; s 71 NT Act; and s 71 ACT Act. The de-grouping provisions are now: s 79 NSW Act; s 79 Vic Act; s 79 SA Act; s 38 WA Act; s 74 Qld Act; s 79 Tas Act; s 79 NT Act; and s 79 ACT Act.

6 [1984] 1 Qd R 125 at 132, ll.17-22.

7 [1983] 1 NSWLR 223 at 225E.

8 [1983] 1 NSWLR 223 at 229E-G.

9 (2002) 50 ATR 162 at [37].

10 (2008) 71 ATR 500 at [20]-[24].

11 2011 ATC ¶20-283 at [8].

12 The decision of the tribunal is reported as *Artistic Pty Ltd v Commissioner of State Revenue* (2006) 62 ATR 372 (Deputy President Chaney). The decision of the Western Australian Court of Appeal is reported as *Commissioner of State Revenue (WA) v Artistic Pty Ltd* 2008 ATC ¶20-004 (Martin CJ, Buss JA and Newnes AJA).

13 (2006) 62 ATR 372 at [19].

14 For example, s 74(3)(c) Qld Act.

15 2008 ATC ¶20-004 at [21].

16 2008 ATC ¶20-004 at [22].

17 2010 ATC ¶20-233 at [47]-[48].

18 (2007) 230 CLR 89 [135].

19 2008 ATC ¶20-004 at [23].

20 A contrary suggestion in *Chief Commissioner of State Revenue v Tasty Chicks* (NSW Court of Appeal), does not sit easily with the doctrine of precedent in Australia established by the High Court in *Farrah Constructions v Say-Dee*, as noted above. The decision of the NSW Court of Appeal is out of step with the WA Court of Appeal in *Artistic*. This is discussed more fully above.

21 (2001) 4 VR 70.

22 At time of writing, the Queensland Civil and Administrative Tribunal's decision is reserved, so I say nothing about the matter other than that it provoked much reflection on these rules.

23 S 71(1) NSW Act; s 71(1) Vic Act; s 71(1) SA Act; s 71(1) Tas Act; s 71(1) NT Act; s 71(1) ACT Act; and the first limb of s 31(1) WA Act.

24 2010 ATC ¶20-233 at [47]-[48], [58].

25 Indeed, there was a deal of litigation in this matter, in the Victorian Civil and Administrative Tribunal, Trial Division, and later on a different subsection in *Commissioner of State Revenue v The Muir Electrical Co Pty Ltd* (2003) 8 VR 200.

26 (2001) 4 VR 70 at [12].

27 2009 ATC ¶20-132 at [104].

28 2010 ATC ¶20-233 at [65]-[69].

29 S 71(2) NSW Act; s 71(2) Vic Act; s 71(2) SA Act; s 71(2) Tas Act; s 71(2) NT Act; s 71(2) ACT Act; and the second limb of s 31(1) WA Act.

30 S 71(3) and (4) NSW Act; s 71(3) and (4) Vic Act; s 71(3) and (4) SA Act; s 71(3) and (4) Tas Act; s 71(3) and (4) NT Act; s 71(3) and (4) ACT Act; and s 31(2) and (3) WA Act. The WA provision is slightly differently worded, and seems to hark back to the language in Queensland pre-harmonisation.

31 [2011] VCAT 2164 at [37].

32 [2011] VCAT 2164 at [56].

33 [2011] VCAT 2164 at [58].

34 [2011] VCAT 2164 at [60].

35 [2011] VCAT 2164 at [62].

36 C Furnell, "Payroll tax grouping in Victoria on the basis of employee use", (2011) 45(8) *Taxation in Australia* 467-471.

37 (1981) 12 ATR 406 at 410.8-411.5 (Burt CJ, Kennedy J concurring, Wickham J coming to the same conclusion for reasons which are, in substance, the same at 409.5).

38 *Commissioner of Stamps v Rivington Farms Pty Ltd* (1981) 28 SASR 169 at 174-175 (Mitchell J). See, to the same effect, *Plummers Border Valley Orchards Pty Ltd v Commissioner of Taxes* (2002) 50 ATR 162 at [15], per Riley J, as to both ownership and control.

39 [1984] 1 Qd R 125 at 141, l.10.

40 *Mead Packaging (Aust) Pty Ltd v Commissioner of Pay-roll Tax (NSW)* (1978) 8 ATR 477 at 487, ll.33-35.

41 *Commissioner of State Taxation (WA) v Scotford Cameron & Middleton Pty Ltd* (1981) 12 ATR 406 at 410.3 (Wickham J), 411 l.35 (Burt CJ, Kennedy J concurring).

42 [2011] SASC 31.

43 It is difficult to tell now, but this serves to highlight what was said in *John French Pty Ltd v Commissioner of Pay-roll Tax* [1984] 1 Qd R 125 at 140.3 about the contrasting Queensland provision. McPherson J pointed out that the Queensland provision focused on the *carrying on* of businesses, rather than the businesses themselves. I have been unable to ascertain whether this difference was introduced in South Australia in 1988 as a result of *John French.*

44 [2011] SASC 31 at [31].

45 Extracted at [0]..

46 [2011] SASC 31 at [34]-[37], citing *John French*.

47 [2011] SASC 31 at [45]-[49].

48 His Honour's abbreviation for the appellant's name.

49 See ruling PTA 017.2.

50 (1978) 8 ATR 477 at 486.7.

51 [1984] 1 Qd R 125 at 141, ll.32-35.

52 McPherson J, WB Campbell CJ concurring, Matthews J not deciding.

53 (1981) 12 ATR 198 at 204.6-205.5.

54 (1981) 12 ATR 198 at 205.

55 (1998) 40 ATR 416 at 424.

56 (2002) 50 ATR 162 at [16]-[17].

57 (1998) 40 ATR 416 at 425.5.

58 *Ballarat Brewing Co Ltd v Commissioner of Pay-roll Tax (Vic)* (1979) 10 ATR 228 at 236, about l.47 (Gray J).

59 (2006) 62 ATR 372.

60 *Commissioner of State Taxation (WA) v Scotford Cameron & Middleton Pty Ltd* (1981) 12 ATR 406 at 412 (Burt CJ, Kennedy concurring).

61 (1981) 28 SASR 169 at 175 (Mitchell J).

62 (2002) 50 ATR 162 at [18].

63 (1998) 40 ATR 416 at 424.5.

64 (1994) 117 FLR 485 at 497.6.

65 [1984] 1 Qd R 125 at 143.

66 *Westpac v CSD* [1994] 2 Qd R 212 at 218.2, 224.7 (QCA).

67 Ruling PTA 031.2 at para 9.

68 Paraphrasing Burt CJ in *Phil Winkless Pty Ltd & Max Winkless (WA) Pty Ltd v Commissioner of State Taxation (WA)* (1986) 17 ATR 982 at 983, ll.45-48.

69 [1984] 1 Qd R 125 at 135, ll.32-35.

70 [2011] VSC 104.

71 Since this article was presented in July 2011, the High Court of Australia has set aside the decision of the New South Wales Court of Appeal, in a judgment reported as *Tasty Chicks Pty Ltd v Chief Commissioner of State Revenue (NSW)* 2011 ATC ¶20-283. Below, the difference between the New South Wales Court of Appeal and Gzell J concerned the particular significance to be accorded to the appeal provisions in the *Taxation Administration Act 1996* (NSW). Whether the result will be permitted to persist is another matter, but there is no word on any proposed amendment to the *Taxation Administration Act 1996*. The application of the HCA's decision of other states' administration laws is untested. See C Bevan, "Merits review of state tax decisions by a court", (2011) 46(6) *Taxation in Australia* 245, for one view.

72 See also s 7 WA Act.

73 Decided since this article was presented in July 2011, *Lis-Con Concrete Constructions Pty Ltd v Commissioner of State Revenue* [2011] QSC 363 (de Jersey CJ) is an example of a garnishee notice having been served.