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1 Introduction

This paper follows a discussion paper delivered to TTI's Queensland Tax Forum in 2017, and draws heavily on that paper. Thanks are due to Harry Lakis and Damien Bourke, who co-authored that paper with me, and to Phil Magoffin, who co-presented that paper with Harry Lakis and me. Particular thanks are due to Harry Lakis for his on-going assistance in developing this paper. Thanks are also due to DJ Alexander, vacation clerk, for his assistance in putting this paper together.

The 2017 discussion paper considered various issues of concern with the payroll tax grouping regime, and commented on legislative options for reform.

Our purpose here today is somewhat similar, although here we are concerned with what can be achieved by administrative, rather than legislative, reform.

As the Payroll Tax Acts in each State are very similar, our primary reference here is to the Payroll Tax Act 1971 (Qld) ('Qld Act'). Similar provisions can be found in each of the Payroll Tax Acts of the other States and Territories, and one of the purposes of today's exercise is to identify differences in interpretation where the provisions are the same. However, in some cases, we identify differences between the Acts in each State and in those cases we have made express reference to the relevant provisions in the other States.

Much of the same analysis is necessary to identify and demonstrate the problems with the existing system, before considering options for administrative reform to alleviate those problems.

Unfortunately there have been very few payroll tax grouping matters that have been heard in a Court. Consequently much of the guidance in the application of the provisions arises out of review processes in administrative tribunals. Decisions from such tribunals do not have the standing of judicial authority.

In addition, the matters that are before a tribunal or a court are necessarily heard and determined based only on the facts and issues that are presented in the immediate case. The cases will often identify the matters that fall for grouping, or are denied exclusion, but may not assist in explaining what arrangements fall outside the grouping provisions, or qualify for exclusion orders.

2 A Short Outline of the Grouping Provisions' History

Payroll tax was transitioned from a Federal tax to a State tax in 1971. There were comments made in Queensland Hansard at the time, describing the known (but as yet not outlawed) minimisation structure of splitting employer entities.

Existing Victorian grouping reforms were subsequently adopted in 1975.

The grouping provisions, originally in ss.16A – 16I, were subsequently renumbered as ss.66 – 75 in the Qld Act.

The Queensland provisions were 'harmonised' with those in Victoria and NSW in 2008.

3 The Purpose of the Grouping Provisions

The cases describe an anti-avoidance purpose: to overcome the strategy of accessing the exemption threshold on multiple occasions, by splitting a payroll amongst separate entities carrying on purportedly separate businesses [see the often cited case of *Commissioner of Pay-Roll Tax v RG Elsegood & Co Pty Ltd* ('*RG Elsegood*').[1]

That 'anti-avoidance' purpose has been confirmed on numerous occasions: *Plummers Border Valley Orchids v Commissioner of Taxes (NT)* ('*Plummers*');[2] *Baxter & Anor v Chief Commissioner of Pay-roll Tax (NSW)* ('*Baxter*');[3] *Artistic Pty Ltd v Commissioner of State Revenue* ('*Artistic*');[4] *Tasty Chicks Pty Ltd & Ors v Chief Commissioner of State Revenue* ('*Tasty Chicks*').[5]

The cases have also recognised the very broad scope of the grouping provisions, said to be alleviated by the operation of the exclusion provisions (again, see *RG Elsegood*), although that mechanism for relief from grouping has itself been criticised - see *Muir Electrical Co Pty Ltd & Ors v Commissioner of State Revenue (Vic)* ('*Muir*').[6]

Ultimately the grouping provisions have been allowed to aggregate businesses that were never operated as one integrated payroll, and despite which remedial exclusion orders are often denied. See the analysis by Bond J in *Scott and Bird and Ors v Commissioner of State Revenue* ('*Scott and Bird*').[7] The provisions do this independently of any decision or determination of the Commissioner. No notice is required to a group member who then automatically becomes liable to pay – even though the assessment may only have been served on the "Designated Group Employer". While the group member would qualify as a 'taxpayer' who can object, in most cases the time limit to lodge an objection in respect of previous periods will have expired.

[1] [1983] 1 NSWLR 223 at 229-230.
[2] 2002 ATC 4530 at 4537.
[3] 1986 ATC 4816 at 4817.
[4] [2006] WASAT 39 at [98].
[5] [2009] NSWSC 1007 at [99].
[6] 2001 ATC 4386 at [14].
[7] [2016] QSC 132 at [27] – [28].

4 The Scope of the Grouping Provisions

Many of the scenarios that incur grouping squarely fulfil the perceived purpose as an anti-avoidance measure to aggregate payrolls amongst businesses that are purported to operate separately.

The provisions start to overreach when they deem grouping when there is nothing more than a mere common discretionary beneficiary amongst separate discretionary trusts.

In other scenarios, simple common elements will combine two seemingly separate groups, for example through common sets of directors, or shareholdings.

An alarming provision is found in s.72, which causes individuals (directors or shareholders) to be branded as "relevant entities", and to thereby become part of a payroll tax group by operation of the definitions in ss.74A-74G.

Some contended applications of the grouping provisions have thrown up absurd results that are unlikely to have been intended by the legislature. This is a basis to reject the absurd interpretation for a more reasonable one. The case that is most frequently cited in support of the proposition that Courts are entitled to approach the interpretation of legislation by taking into account the consequences of giving a particular meaning, is *Cooper Brookes (Wollongong) Pty Ltd v FCT* ('*Cooper Brookes*').[8]

[8] (1981) 147 CLR 297, at 320-321.

5 The Grouping Provisions – specific comments

5.1 The existence of a "business" is a pre-requisite

Section 66 extends the meaning of 'business' to include matters not usually within that meaning:

> *business includes any of the following, whether carried on by 1 person or 2 or more persons together –*
>
> ...
>
> *(d) the carrying on of a trust, including a dormant trust.*

That extended definition is then coupled with the common control provisions, which state that:

> *71(1) If a person or set of persons has a controlling interest in each of 2 businesses, the persons who carry on those businesses constitute a group.*
>
> *71(2) For this section, a person or set of persons has a controlling interest in a business if any of the following applies:*
>
> ...
>
> *(g) for a business carried on under a trust – the person or set of persons, whether or not as the trustee or beneficiary of another trust, is the beneficiary in respect of more than 50% of the value of the interests in the trust under which the business is carried on.*

Substituting the definition of business into section 71 gives us:

> *71(1) If a person or set of persons has a controlling interest in each of 2 [carryings on of a trust], the persons who carry on those [carryings on of a trust] constitute a group.*
>
> *71(2) For this section, a person or set of persons has a controlling interest in [the carrying on of a trust] if any of the following applies:*
>
> ...
>
> *(g) for [the carrying on of a trust] carried on under a trust – the person or set of persons, whether or not as the trustee or beneficiary of another trust, is the beneficiary in respect of more than 50% of the value of the interests in the trust under which [the carrying on of a trust] is carried on.*

As can be seen, this becomes somewhat recursive and difficult to apply. One approach to its interpretation is to recognise that it is the carrying on of the trust which is the business, and not the trust itself (particularly given a trust is not an entity in any event). Further, the persons which are grouped are the persons who carry on the businesses. As trusts are not persons, it is the trustees who are grouped. However, that is not the same thing as saying that the trust assets of the trustees form part of the group.

That suggests that the beneficially held assets of the trustee are susceptible to attack under the grouping provisions, but not the trust assets, unless those trust assets are employed in carrying on an actual business.

Sections 70 and 71 address entities that operate a "business". In the absence of a business, grouping should not arise under those sections.

The sections should go further and consider whether the business is an employer. The object of the provisions is only achieved if businesses that have employees are the subject of grouping.

In the *Can Barz* litigation[9] the grouping of a superannuation fund with other active entities created tension between the provisions of the *Superannuation Industry (Supervision) Act* 1993 (Cth) (notably ss. 62 and 67A as well as regulation 5.08) and the *Payroll Tax Act 1971* (Qld) (which imposes joint and several liability on group members). Hence the superannuation fund (which had never had a business or indeed 'employees') was sought to be made liable for a liability which had not been incurred for the specific purpose of providing retirement benefits for its members.

On the other hand, if there are three 'associated' (to use a neutral term) entities, only one of which has any employees, then there is no mischief if that employer/business is registered and pays its payroll tax liability, and in that case no grouping need occur.

The rationale for the provisions were summarised in the submission made by the appellant in *RG Elsegood* (and accepted by Mahoney JA):

> *"Tax relief was given by the Act to businesses employing less than a specified number of employees. Attempts have been made, or could be, made by larger businesses to obtain that relief by splitting their businesses into a number of smaller or separate businesses, employing no more than the specified number of employees. The remedy adopted by the statute to avoid that mischief was: to deny such relief to members of a 'group'; to provide for the employees of 'commonly controlled' businesses to be deemed to constitute a group to define 'group' for this purpose in wide terms so as hopefully to include all who might be involved in the avoidance of the purpose of the legislation; and to deal with such anomalies as might arise because of the wide terms of the definition of 'group' partly by specific provisions: s 16E is perhaps directed to this, at least in part; and partly by committing the Commissioner a discretion which he may exercise so as to remove such anomalies."*

5.2 What is the purpose of s.72 and ss.74A-74G?

Section 72 does not confine its operation to entities that operate a business. Why is that the case, and by what means does the provision operate to ensure that employees of "associated" businesses are all aggregated and treated as one payroll?

Properly understood, s.72 operates only to impose liability by association. In doing so, it arguably offends the principle of legality (while perhaps not directed at s.72, but in an analysis that must be of

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[9] *Can Barz Pty Ltd & Anor v Commissioner of State Revenue & Ors* [2016] QSC 59; *Scott and Bird & Ors v Commissioner of State Revenue* [2016] WSC 132; *Can Barz Pty Ltd & Anor v Commissioner of State Revenue* (No 2); *Scott and Bird & Ors v Commissioner of State Revenue (No 2)* [2016] QSC 181; *Can Barz Pty Ltd & Bird & Scott v Commissioner of State Revenue* [2016] QCA 142; *Commissioner of State Revenue v Can Barz Pty Ltd (No 2)* [2017] 2 Qd R 537.

universal relevance, see the discussion of Philippides JA in *Commissioner of State Revenue v Can Barz Pty Ltd & Anor*[10]].

That principle is so dominant that it operates without regard for the usual rule requiring some effect to be given to the offending provision.

To the contrary, in order to overcome the prohibitions imposed by the principle of legality, the words used in the legislation must be sufficient to show an intention to expressly override the principle. Section 72 could meet that threshold. Otherwise the scope of operation of s.72 should be read down by reference to the purpose of the provision and its context.

[10] [2016] QCA 323.

6 Exclusion Orders

6.1 The test for exclusion

In Queensland, the factors listed in s.74(3) cannot be elevated to the status where they replace the statutory test set out in s.74(2) - see *Boston Sales and Marketing Pty Limited v Chief Commissioner of State Revenue* ('*Boston Sales*').[11]

The scheme for making exclusion orders was considered by Bond J in *Scott and Bird and Ors v Commissioner of State Revenue* ('*Scott and Bird*').[12] In some respects it represents 'fresh eyes' looking at what practitioners may have thought was a settled scheme. What Bond J identifies is:

a. the discretion to issue an exclusion order is conferred in s.74(1);

b. the discretion is only enlivened if the Commissioner is satisfied as to the matters in s.74(2), namely independence and no connection between businesses;

c. if the discretion is enlivened, then the Commissioner must have regard to the matters in s.74(3); and

d. there will be some 'crossover' between the factors that must be considered in forming the 'evaluative judgment' as to whether the discretion in s.74(1) is enlivened, and then deciding whether the discretion in s.74(1) should be exercised.

Bond J rejects the taxpayer's submission that s.74(2) confers a discretion, and that s.74(3) comprises mandatory considerations for the exercise of that discretion. This rejection is said to follow the NSW Court of Appeal's decision in *Seovic Engineering Pty Ltd v Chief Commissioner of State Revenue* ('*Seovic*').[13]

What is confusing about that rejection is that the submission exactly aligns with the legislative scheme in NSW, where the exclusion order provisions bear a different formulation in the *Payroll Tax Act 2007* (NSW) ('*NSW Act*'). Section 79 of this act provides:

> *Section 79 Exclusion of persons from groups*
>
> *(1) The Chief Commissioner may, by order in writing, determine that a person who would, but for the determination, be a member of a group is not a member of the group.*
>
> *(2) The Chief Commissioner may only make such a determination if satisfied, having regard to the nature and degree of ownership and control of the businesses, the nature of the businesses and any other matters the Chief Commissioner considers relevant, that 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 that group.*
>
> ...

[11] [2014] NSWCATAD 139 at [23].
[12] [2016] QSC 132 at [39] – [42].
[13] [2015] NSWCA 242.

Effectively, the provisions in ss.74(2) and 74(3) of the Qld Act are found combined in s.79(2) of the NSW Act. By that formulation, the factors from s.74(3)[14] are expressly integrated into the precondition for the enlivening of the discretion in NSW.

In that respect the Queensland provisions/formulation should be contrasted (and perhaps distinguished) with the one that was analysed in *Seovic*. On that basis *Seovic* is not 'binding' on the Queensland court. However it is that distinction, and the fragmentation of the factors from the evaluative decision in Queensland, that arguably supports and permits the formulation advanced by Bond J in *Scott and Bird.*

Some commentators are critical of the analysis of the exclusion provisions in *Scott and Bird.* Irrespective, the case offers a construction of the provisions that must now be reconciled with the existing rulings and practices, reconciled or distinguished from *Seovic*, or the position should be clarified by legislative harmonisation/reform.

6.2 What if there is no business?

If there is no business then, reasonably, the submission can be made that exclusion cannot be denied - i.e. there can be no business with which to evaluate the existence of a connection or interdependence with another business. Support for this proposition may be found in the judgment of Bond J in *Scott and Bird*[15] - although in that case the existence of a deemed business, by operation of s.66, prevailed against the submission.

Although the trustee of a trust might be deemed to carry on a business (see s.66(d)), when it comes to evaluation under s.74 it is necessary to identify and evaluate a connection or interdependence that arises in the carrying on of that business (deemed or otherwise).

An alternative construction is that s. 74(2) cannot operate in the absence of a business. This construction supports the idea that is the 'deemed' business which must be compared with the businesses carried on by other members of the group.

Where the business is merely 'deemed', such as the carrying on of a trust, where the trust merely holds investments and does not conduct an actual business, it is the carrying on of the trust which must be compared with the businesses carried on by other members of the group.

In this context, the carrying on a trust would seem to involve no more than the making of decisions by the trustee of the trust.

Considering the 'independence', and 'connection' requirements separately, s. 74(2) can be read as follows:

> The commissioner may make an exclusion order only if the commissioner is satisfied a business carried on by the person:

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[14] of the QLD Act.

[15] *Scott and Bird & Ors v Commissioner of State Revenue* [2016] WSC 132 [2016] QSC 132 at [45], [52] and [53].

> (a) is carried on independently of a business carried on by any other member of the group: and
>
> (b) is not connected with the carrying on of a business carried on by any other member of the group

Paragraph (3)(a) requires the Commissioner to have regard to 'the nature and degree of ownership and control of the businesses carried on by the person and the other members of the group'. For this provision to be given meaning, it may be necessary to read in the word 'common' as follows:

> 'the nature and degree of **common** ownership and control of the businesses carried on by the person and the other members of the group'.

6.3 The problem with the exclusion provisions

Each state has a provision which allows for smaller groups to be subsumed into larger groups. These are found in s. 73(1) of *Payroll Tax Act 1971* (QLD), s. 26(1) of *Pay-roll Tax Assessment Act 2002* (WA) and in s. 74(1) of each other states and territories respective payroll tax act (*Payroll Tax Act 2007* (VIC), *Payroll Tax Act 2007* (NSW), *Payroll Tax Act 2011* (ACT), *Payroll Tax Act 2008* (TAS), *Payroll Tax Act 2009* (SA) and *Payroll Tax Act 2009* (NT)).

These provisions provide that if a person is a member of two or more groups, all the members of those groups form one larger group. The result of which is that 'supergroups' can be formed, as discussed later in this paper.

It is clear the grouping provisions have gone well beyond their intended purpose. In *Commissioner of Pay-roll Tax (N.S.W.) v. R.G. Elsegood & Co. Pty. Ltd.*[16] Mahoney JA summarises this purpose well:

> Tax relief was given by the Act to businesses employing less than a specified number of employees. Attempts have been, or could be, made by larger businesses to obtain that relief by splitting their businesses into a number of smaller or separate businesses, employing no more than the specified number of employees. The remedy adopted by the statute to avoid that mischief was: to deny such relief to members of a "group"; to provide for the employees of "commonly controlled" businesses to be deemed to constitute a "group"; to define "group" for this purpose in wide terms so as hopefully to include all who might be involved in the avoidance of the purpose of the legislation; and to deal with such anomalies as might arise because of the wide terms of the definition of "group" partly by specific provisions: s 16E is perhaps directed to this, at least in part; and partly by committing to the Commissioner a discretion which he may exercise so as to remove such anomalies. Section 16H was seen as giving such a discretion.

The reference to s. 16E is the exclusion provision of the repealed *Pay-roll Tax Act 1971* (NSW).

The courts have repeatedly expressed the view that the grouping provisions are too wide and the de-grouping provisions provide an avenue to alleviate the absurdity that results.[17]

Most recently in *Seovic*), Meagher JA stated:

> It may readily be accepted that the broad purpose of the power to exclude is to enable the Chief Commissioner to relieve against the unreasonable operation of the grouping provisions.

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[16] [1983] 1 NSWLR 223 at 229.
[17] See generally as to the following quotes: David W Marks "Payroll tax de-grouping" *The Tax Specialist* Vol 15(3).

In *Baxter* Yeldham J stated:

> In construing sec. 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 sec. 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.

In *RG Elsegood* Hutley JA stated:

> The judgment under appeal suggests harsh possibilities if the appeal is allowed. The legislature has itself recognised 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.

In *Plummers* Riley J stated:

> 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 s17H of the Pay-roll Tax Act. The effect of s17H is to ameliorate any absurd or unjust operation of the grouping provisions of the Act and, it was submitted, should be approached accordingly.

7 Can/should the power to exclude extend to smaller groups?

As discussed below, 'supergroups' are created by a combination of the discretionary trust provisions and the 'group of groups' provision.

If the exclusion provision is applied to members of supergroups, the Commissioner must be satisfied that the business is carried on independently of "any other member of the group".[18] If the supergroup consists of hundreds, or hundreds of thousands, of members, this becomes impossible in practice.

A question for consideration is whether the exclusion power can be applied at the small group, or sub-group, level.

7.1 Relevant authorities

The question of which group was relevant was considered by Meagher JA in *Tasty Chicks*[19] Meagher JA suggests the 'group of groups' provision from the now repealed *Pay-Roll Tax Act 1971* (NSW) does not cause smaller groups to cease to exist. In this case, the de-grouping provisions were applied to the smaller groups rather than the larger.

Tasty Chicks applied s 16C[20] which no longer exists in harmonised legislation. This section provides that the Commissioner can only split groups that were formed by ways listed in the section (which do not include larger groups formed by subsumed smaller groups).

Meagher JA said:

> 50 Before considering those arguments it is necessary to identify the relevant "group". Section 16K of the Administration Act provides that if a person is a member of two or more primary groups, the members of all the groups together constitute a primary group. The effect of s 16K, which applied in the second and third periods, is that Tasty Chicks and Angelo Transport were members of the larger primary group comprised of M&J Chickens and any entities in smaller primary groups of which M&J Chickens was also a member. **Section 16K does not in terms provide that on its application, the smaller primary groups cease to be groups and s 16L provides that a person may be a member of more than one primary group.**
>
> However, s 16C(1) states that a determination under s 16B may only be made in respect of a person who would, but for the determination, be a member of a group arising under s 106H. Accordingly, the question whether s 16C(3) applies must be determined by reference to the smaller primary groups comprised of Tasty Chicks and M&J Chickens and Angelo Transport and M&J Chickens. (emphasis added)

The relevant sections provided, at the time:

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[18] Section 74(2) *Payroll Tax Act 1971* (QLD).

[19] [2012] NSWCA 181 at [50]. The matter was reconsidered by the NSW Court of Appeal following the decision of the High Court [2011] HCA 41

[20] *Pay-Roll Tax Act 1971* (NSW).

16B:

16B Exclusion of persons from groups

(1) The Chief Commissioner may, by order in writing, determine that a person who would, but for the determination, be a member of a group is not a member of the group.

...

16C:

16C Grounds for excluding persons from group

(1) A determination may be made by the Chief Commissioner under section 16B in respect of the following persons only:

(a) a person who would, but for the determination, be a member of a group arising under section 106H (Primary groups arising from the use of common employees) of the Taxation Administration Act 1996,

(b) a person who carries on a business as trustee of a trust and would, but for the determination, be a member of a group arising under section 106I (Primary groups of commonly controlled businesses) of the Taxation Administration Act 1996,

(c) a person who would, but for the determination, be a member of a group arising under section 106IA (Primary groups arising from tracing of interests in corporations) of the Taxation Administration Act 1996.

16K Smaller primary groups subsumed by larger groups

If a person is a member of 2 or more primary groups, the members of all the groups together constitute a primary group.

16L Grouping provisions to operate independently

The fact that a person is not a member of a primary group constituted under a provision of this Part does not prevent that person from being a member of a primary group constituted under another provision of this Part.

Additionally, in *Seovic*, the Civil and Administrative Tribunal of New South Wales allowed de-grouping at the smaller group level. However, this decision was later overturned by the Appeal Panel.

[10] The applicants objected to the Chief Commissioner's assessments on the basis that there was a failure to exercise the discretion under s 79(1) to exclude one or more of them from the smaller groups. An exercise of that discretion in relation to one of the applicants would have had the effect of dissolving the larger group. Those objections were disallowed.

[11] The applicants applied to the Administrative Decisions Tribunal under s 96 of the Taxation Administration Act 1996 (NSW) for an administrative review of the Commissioner's decisions... By its decision delivered on 30 April 2014 the Tribunal (constituted by Senior Member Verick) concluded that the Chief Commissioner had erred in not

> exercising the discretion under s 79 to exclude Exell from each of the smaller groups constituted by s 71(2), which also would have de-grouped the larger group constituted by s 74(1). The Tribunal remitted the matter to the Chief Commissioner "to exercise his discretion under s 79 of the Act to de-group Exell from Civil + Exell and Engineering + Exell groups": *Seovic Civil Engineering Pty Ltd v Chief Cmr of State Revenue* [2014] NSWCATAD 52 at [44].

Baxter is the only authority where the exclusion provisions were successfully applied to exclude a sub-group from a larger group (without assistance from the former provisions discussed in *Tasty Chicks*).

In *Baxter* Valga Pty. Ltd. (Valga) was grouped with W.A. Baxter & Co. (Baxter) (group 1). Valga was grouped with Paul Paroz Brett & Assoc. (Paul Pauroz) (group 2). Gemmi Pass Pty. Ltd. (Gemmi) was grouped with Paul Paroz (group 3).

These three groups were combined by common members into one larger group (group 6).

The Commissioner conceded that Valga was carried on independently of Paul Paroz and Gemmi, and Baxter was carried on independently of Gemmi and Paul Paroz.

The exclusion provision in Queensland and all other states and territories required a member of a group to prove that it is substantially[21] independent of "any other member of the group".

The Commissioner argued that this required a member of a group to prove that it is substantially independent of each other member of the group to be excluded from that group. This interpretation would mean that Valga and Baxter could not be excluded from group 6 because they could not prove that they were independent of each other (but could prove that they were both individually substantially independent of Gemmi and Paul Paroz).[22]

The taxpayer in *Baxter* argued that if the members of a sub-group could prove to be substantially independent of each other member in a larger group (each member not in the sub-group but in the larger group) then that sub-group could be excluded from the larger group. This approach would dissolve the larger group into smaller groups. This would allow Valga and Baxter (together as group 1) to separate from the larger group 6.[23]

In response to the taxpayer's submission, the Commissioner argued that the sub-groups cease to exist, so the approach would result in resurrecting the sub-groups. The plaintiff argued that the approach does not resurrect any sub-group – it simply excludes two members of a group, leaving the larger group with less members and the new excluded members as a new group.[24]

Yeldham J agreed with the taxpayer's approach.

> I see no reason, either in principle or in the language used in the relevant section, why the latter cannot be construed, with the aid of sec. 21(b) of the Interpretation Act 1897, so as, for example, to remove two members from a group of

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[21] 'substantially' has since been deleted from the relevant provision.

[22] To clarify, Valga and Baxter could each prove that they were independent of 2 out of 3 of the other group members. The Commissioner argued that they needed to be independent of 3 out of 3 of the other group members to be excluded.

[23] To clarify, Valga and Baxter can each prove to be substantially independent of each member of group 6 that are not a member of the original group 1 (whose members are Valga and Baxter). Following the approach argued by the taxpayer, this would allow group 1 to separate from group 6, dissolving group 6 into two separate sub-groups (being the original group 1 and group 3).

[24] However, in effect, the approach does create two groups that were the same as two of the original sub-groups. The taxpayer argued that sub-groups did not need to be resurrected to achieve this.

> four. Such a result has logic and common sense on its side and would permit, in a case like the present, an absurd and plainly unintended consequence to be avoided. By treating words in the singular as including those in the plural sec. 16H(1) can, and in my opinion should, be construed as follows:
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> ``Where the Chief Commissioner is satisfied, having regard to the nature and degree of ownership or control of the businesses, the nature of the businesses and any other matters that he considers relevant, that businesses carried on by members of a group are carried on substantially independently of, and are not substantially connected with the carrying on of a business or businesses of **another member or other members of that group**, the Chief Commissioner may, by order in writing served on those first mentioned members, exclude them from that group." (emphasis added)

This decision, allowed members a sub-group to together be excluded from a larger group if each member of the sub-group could prove to be substantially independent of each member of the larger group not in the sub-group. However the way Yeldham J construed the exclusion provision could raise an interpretation in other circumstances.[25] The phrase "another member or other members of that group" supports an interpretation that a member of a group (or multiple members together as a sub-group) could be excluded from a group if they prove to be substantially independent of only one other member of that group. This would allow members of a group to easily become excluded from a group. However, such an interpretation is relying on a version of the legislation construed by Yeldham J and used in a way not used in *Baxter*.

However, this seems to be the only authority in Australia that takes this view. All other cases interpret the phrase "any other member of the group" as "each member of the group". For example in Port Augusta Medical Centre Pty Ltd v Commissioner Of State Taxation ('*Port Augusta*'),[26] Kourakis J states at 111:

> The finding of a substantial connection and dependence between PAMC and the incorporated medical practices is sufficient to deny the application of s 18I of the Act because it means that PAMC cannot show that it is not relevantly related to "any other member" of the group. Nonetheless in order to determine all of the issues raised on this appeal I turn next to the connections between PAMC on the one hand and Vay and Guyram on the other.

Here, Kourakis J decided that a lack of independence between one member of a group from another defeats a claim of exclusion from that group.

7.2 Relevant provisions

As discussed elsewhere in this paper, exclusion orders (Qld) and orders that a person is not a member of a group (Vic and NSW) are permitted by section 74 (Qld) and section 79 (Vic and NSW). In each case, the power applies to exclude a person from a group, or to determine that a person is not a member of a group.

Accepting that the requirement is that the business carried on by the person be independent of, and not connected to, a business carried on by any other member of the group, the question becomes: what is the group? If the group is the broader group formed after merger of all smaller groups with

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[25] Any other interpretation could only be obiter as it was not decisive in *Baxter*.
[26] [2012] SASCFC 7.

common members, then application of the provision becomes very difficult. If, however, the provision can be applied at the small group level, then its application may be simpler.

Section 68 (Qld), or section 69 (Vic and NSW) suggests that a group is constituted by all the persons or bodies forming a 'group that is not part of any larger group'.

The explanatory memoranda for the 'group of groups' provision in most States[27] explain that the smaller groups cease to exist.

Section 68 may be taken to suggest that the exclusion provision is to be applied to that larger group. An alternative proposition is that the exclusion provision can be applied at either level, so that the term 'group', which is applied for the purposes of the balance of the legislation, is that group which remains after application of the exclusion provision.

Interpretation of the provisions is not assisted by the recursive use of 'group' in section 68 and section 69. The recursion problem is even greater in Vic and NSW, where s. 67 defines 'group' to mean:

> a group constituted under this Part, but does not include any member of the group in respect of whom a determination under Division 4 is in force.

An aid to interpretation is provided by section 79(4), which appears in each Act, other than Queensland and Western Australia.

Section 79(4) of the *Payroll Tax Act 2009* (NSW)[28] states:

> (4) This section **extends** to a group constituted by reason of section 74 (Smaller groups subsumed by larger groups). [emphasis added]

The use of the word 'extends' implies that s. 79 can otherwise be applied at the smaller group level. If it were intended that the provision could be applied only at the level of the larger group, it would have been more appropriate to say 'applies' rather than 'extends'.

The Explanatory Memorandum to the Northern Territory Payroll Tax Bill 2009 comments on the scope of s. 79(4). It states:

> Subclause (4) provides that a determination that a person is not a member of a group **can** be made in relation to a larger group (that is, a group where smaller groups have been subsumed into a larger group under clause 74 of this Bill). [emphasis added]

Again, the reference to 'can', rather than 'can only' suggests that the provision merely provides for an extension of the power to larger groups, such that it can also be applied to smaller groups.

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[27] Victoria: Clause 74 Payroll Tax Bill 2007 Explanatory Memorandum, New South Wales: Clause 74 Payroll Tax Bill 2007 Explanatory Note, Tasmania: Clause 74 Payrole [sic] Tax Bill 2008 Notes on Clauses, Northern Territory: Clause 74 Payroll Tax Bill 2009 Explanatory Statement and Western Australia: Clause 36 Pay-Roll Tax Assessment Bill 2001 Explanatory Memorandum.

[28] Section 79(4) of the Payroll Tax Acts of Victoria, Australian Capital Territory, Tasmania, Northern Territory and South Australia are identically worded.

7.3 Conclusion on interpretation

Having regard to the dearth of authority on the question, and having regard to the aid to understanding provided by s. 79(4), it is suggested that it is open to the Commissioners to administer the exclusion provisions on a sub-group basis.

8 Other questions of approach

8.1 The Old 'Just and Reasonable' Test

Prior to the harmonisation reforms in 2008, s. 71(3) of the Queensland Act provided "[w]here the commissioner is satisfied ... 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 ... exclude them from that one group" (emphasis added). This 'just and reasonable' test is not included in the harmonised legislation.

For example, in *Artistic*[29] Artistic Pty Ltd was excluded from a group because it was obvious that it did not attempt to split its businesses to gain the benefit of multiple payroll tax free thresholds.

In *Seovic* the Chief Commissioner originally grouped Excell and Civil and Excell and Engineering. These two groups were then joined into one larger group.

The applicants objected to the assessment, and attempted to exclude one of the members from a sub-group which would in effect dissolve the larger group. The basis of the objection was that a general 'just and reasonableness' test should be used to assess whether a person could be excluded from a group. Meagher JA concluded that no such test now exists.[30]

8.2 Discretions must be exercised reasonably

The High Court has observed that where a statutory power is conferred the legislature is taken to intend that the discretion is to be exercised reasonably and justly [see, e.g., *Minister for Immigration and Citizenship v SZIAI* (2009)[31] ; *Kruger v The Commonwealth*[32]].

In *Minister for Immigration and Citizenship v Li* (2013)[33], the High Court had occasion to discuss the concept of unreasonableness as a ground of review. Unreasonableness will be found where, by reference to the scope and purpose of the statute, a decision maker has committed a particular error in reasoning, given disproportionate weight to some factor, or reasoned illogically or irrationally – such that the decision may be ultra vires and void.

8.3 Prohibition for corporate groups

What is the policy reason for denying exclusion orders for members of a corporate group? See s.74(4).

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[29] [2008] WASCA 24 at [20]-[23].
[30] at [16]-[23].
[31] 83 ALJR 1123 at 1127 [15]-[16].
[32] (1997) 190 CLR 1 of 36.
[33] 249 CLR 332 at [63] – [76].

If corporations otherwise meet the test of their businesses not being connected and being carried on independently, then why can't they also apply for exclusion from a group?

As this is a legislative, rather than administrative matter, we do not consider the point further here.

8.4 A logical methodology

The administration of the Commissioner's discretion to issue exclusion orders should follow a logical approach that lends itself to objective evaluation (for advisers) and implementation (for the Commissioner).

A suggested logical approach is as follows:

a. The first question should be: what is the incident/factor that is alleged to reflect the disqualifying connection or interdependence between the businesses?

b. The next question should be: is the incident/factor that is alleged to reflect the disqualifying connection or interdependence between the businesses insignificant, or is it 'substantial';

c. The next question should be: is the existence of that incident/factor attributable to:

    a. the nature and degree of ownership AND control;

    b. the nature of the businesses;

    c. other matters (reasonably) considered relevant.

8.5 What is 'substantial'

Although the word "substantial" was removed in the latest version of the exclusion provisions, the cases have always required a degree of materiality, which has been read as amounting to the requirement for a *substantial* connection or interdependence - see Pagone J in *GTS Industries Pty Limited v Commissioner of State Revenue*[34], and *Lombard Farms Pty Ltd v Chief Commissioner of State Revenue* (*'Lombard'*).[35]

The cases have also supported that the materiality should be measured by examining the effect that the connection or interdependence has on the business, or more precisely the effect that removing the connection or interdependence would have [see *Lombard*].

For example, an analysis would look at the effect on the viability of the business if:

[34] [2004] VCAT 21.
[35] [2013] NSWADTAP 42 at [50]-[51].

a. an inter-entity loan was called up, determined not by reference to the scale of the loan, but to the capacity of the debtor to repay [see *Crusher Holdings Pty Ltd v Commissioner of Taxes (NT)*[36], and *Lombard Farms* (on remission back)].[37]

b. if there is a particular connection of custom or supply, then whether it is at arm's length, or whether it is readily interchangeable and that supply can readily be obtained from someone else without affecting the viability of the business.

8.6 The Factor of Ownership 'and' Control

First and foremost, the mere existence of any common ownership element cannot itself be invoked to deny exclusion. In other words, the factor that caused grouping in the first place cannot later, of itself, be relied upon to deny exclusion.

The degree of ownership and control must not be insignificant – if a mere fifty-one percent co-ownership causes grouping to arise, then something more substantive must exist to qualify as a relevant degree of ownership and control to deny exclusion – provided the logical methodology outlined above is also applied.

Certainly the deeming provisions found in the grouping provisions should be ignored when considering the *actual* ownership and control of businesses. For example, where there may be a "set of persons" deemed to control numerous entities and businesses, if in fact the *actual* control is exercised by sub-groups or individuals distinct from that entire "set" – then the actual reality must prevail [see *Commissioner of State Taxation (WA) v Scotford Cameron & Middleton Pty Ltd*].[38]

It cannot be ignored that the analysis is as to ownership AND control of the business, not ownership OR control of the business. In addition, applying the logical methodology outlined above, the identified connection or interdependence itself must be explained by the existence and extent of ownership and control.

Ownership and control must not be a mere potential or theoretical factor, but must be shown to be the actual factor that led to the connection or interdependence between the businesses.

8.7 Nature of the Businesses

This factor looks at the complementary (or otherwise) nature of the activities carried on by the businesses seeking to be excluded from each other.

Cases have shown that if businesses are disparate in nature, then they are entitled to be excluded, even if they have common ownership and control. Examples include:

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[36] (1994) 29 ATR 156.
[37] [2014] NSWCATAD 132.
[38] 81 ATC 4576 at 4578.

a. a prawn farm and an ice-cream shop [see *Commissioner of Payroll Tax v John French Motors*].[39]

b. a hairdresser and an electrician [see *Artistic*[40]].

c. a building contractor and a hotel [see *Shadforth Lythgo* QCAT 12 April 2016].

Generally, businesses of disparate/non-complimentary nature should be excluded, irrespective of their ownership and control.

The purpose and object of the payroll tax grouping provisions, and the exclusion provisions, are not to outlaw and discourage the creation of a portfolio of disparate businesses, where those businesses could never have operated in conjunction by one employer.

8.8 Cross-jurisdictional issues

I understand that, quite properly, each State seeks only to impose payroll tax on its own citizens.

Let us assume that Qld Co, NSW Co, and NSW Trust are grouped. NSW Trust does not have any employees and does not operate a business in the usual meaning of the word. Neither Qld Co nor NSW Co has a payroll sufficient to meet the threshold individually, but collectively the threshold is met in each State.

Wages paid by Qld Co are taxable in Qld, but not NSW, as discussed in PTA 039.1. Further, Qld Co registers for payroll tax in Queensland, while NSW Co registers in NSW. NSW Trust does not register in either jurisdiction, as it is not an employer.

However, as a result of grouping, Qld Co's payroll tax liability will be calculated, at least in part, by reference to the payroll of NSW Co, as NSW Co's wages cause the group's wages to exceed the threshold.

If NSW Co fails to pay its payroll tax, then NSW Trust may be called upon to pay the tax under section 81 of the NSW Act. However, I understand that Qld Co will not be, presumably on the basis that requiring Qld Co to pay a tax liability of NSW Co would not be 'for the peace, order and good government' of NSW, so that it would be beyond NSW's constitutional reach.

On the other hand, if Qld Co fails to pay its payroll tax, then neither NSW Co nor NSW Trust will be called upon for payment.

As a result, in a cross-jurisdictional context, the grouping provisions are used to determine the *amount* of liability, but do not finally determine *who* is liable. In this limited context, the provisions serve their purpose as anti-avoidance provisions (as only one threshold is claimed by the group), without unfairly imposing liability on an entity for the actions of another entity. This may be suggested as a reasonable objective for the provisions more generally.

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[39] (1984) 14 ATR 228 at 236.

[40] at 8053.

8.9 The Public Ruling - PTA 031

The Queensland, NSW and Victorian versions of PTA 031 open with the statement

> '[Part 4 of the Payroll Tax Act] provides for the grouping of two or more employers. The effect of grouping is that only one payroll tax deduction can be claimed for each group.'

If this statement were correct, this presentation would be unnecessary.

Recognising that the statement is intended to summarise a set of complex provisions in a couple of sentences, a more accurate sentence might be

> [Part 4 of the Payroll Tax Act] provides for the grouping of two or more persons. The effect of grouping is that only one payroll tax deduction can be claimed for each group of persons, and that each member of the group is liable for the payroll tax obligations of each other member.

The NSW and Victorian Rulings then include the following statement:

> To avoid anomalies which may arise from the strict application of the grouping provisions, s. 79 of the Act provides that an **employer** that is grouped may apply...to be excluded from the group.

The Queensland ruling also refers to an order excluding an 'employer'.

For example, the first sentence under the heading 'Ruling' in the NSW and Victorian Rulings states:

> In order to be granted an exclusion from a group, the applicant **employer** must satisfy the [Chief] Commissioner that...

The equivalent sentence in the Queensland Ruling states:

> In order for an **employer** to be granted an exclusion from a group, the Commissioner must be satisfied that...

The Victorian SRO has issued a separate document which sets out in some detail how the provisions operate, although again, the extent of the operation of the provisions is not clear to the casual reader, particularly in relation to the formation of 'supergroups', discussed below. Given the complexity of the provisions, explaining their operation is certainly a difficult task.

Each of these rulings assume that 'employers' apply for exclusion from grouping. However, the provisions refer to 'persons'. While the provisions require that the persons be carrying on business in order to be considered for exclusion, the extended definition of 'business' will apply for this purpose, so that an entity which is not carrying on an actual business may be excluded. However, there is no requirement that the person seeking exemption be an employer.

I leave it for consideration whether:

- the rulings require amendment to reflect the way in which the grouping provisions are approached by the Commissioners; or
- the way in which the grouping provisions are approached by the Commissioners should be amended to reflect the rulings

9 Supergroups

9.1 Getting the band together

It is worthwhile considering a specific example of the operation of the provisions. In making the following points, I recognise that this is not the way in which the provisions are administered, and I am not suggesting that the Commissioners have sought to impose payroll tax obligations in the way described below. Rather, the point of the following is whether that non-imposition can be put on a sound basis, and if so, what consequences would that have when that basis is applied consistently to all entities.

A standard discretionary trust produced in the last 30 or 40 years typically contains one or more of the following catch-all beneficiary clauses:

> Any trust or company in which any beneficiary has a beneficial interest [whether direct or indirect]
>
> ...
>
> Any person who has made a donation of $2 or more to [CHARITY].

While these clauses are becoming less common, due to increasing recognition not only of the issue described here, but also FIRB requirements, and other related issues, you would expect to find at least one of these clauses in perhaps 50%, if not 75%, of discretionary trusts in Australia.

A standard discretionary trust will typically also include more specific beneficiary clauses which include entire extended family groups as secondary or tertiary beneficiaries. Very commonly, at least one member of the broad beneficiary class will hold a portfolio of shares in Australian public companies, meaning that each of those Australian public companies is a beneficiary of the trust.

Considering next the definition of 'controlling interest', any person who may benefit from a discretionary trust is taken to be a beneficiary in respect of more than 50% of the value of the interests in the trust,[41] and is taken in turn to have a controlling interest in the (deemed) business carried on under the trust.[42]

As a result, most discretionary trusts will be controlled by one or more Australian public companies.

Next we consider section 71(1), which provides that:

> If a person or set of persons has a controlling interest in each of 2 businesses, the persons who carry on those businesses constitute a group

An Australian public company which is a beneficiary of multiple trusts will cause those trusts to be grouped together.

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[41] Qld section 71(6).

[42] QLd section 71(2)(g).

Each trust in the group may itself be associated with its own 'groupies' - various entities and individuals who might be genuinely thought of as associates or related persons. The trust may therefore be grouped with those entities.

The groups will then be joined together to create a large group of trusts and their 'groupies'.

Those groups of trusts which then be grouped together to form a larger group with any groups which have common members. For example, for the group of trusts which collectively include Rio Tinto as a beneficiary, it is likely that at least one of those trusts will also have the Commonwealth Bank as a beneficiary. As a result, the collection of trusts and groupies connected by Rio Tinto will be joined with the collection of trusts and groupies connected by Commonwealth Bank.

The process will snowball so that most trusts in Australia will form part of a single group, which will also include each of their groupies.

So far, the snowball does not include the public companies themselves. However, many, if not all, public companies will have at least one employee who works part-time for the public company, and also works part time for an entity in the supergroup. As a result, the public company and the entity will be grouped under the common employee provisions. As the group consisting of the public company and the entity will have a common member with the supergroup, that group will also join the supergroup.

The supergroup will thus include most small to medium enterprises in Australia, and, most likely, every major public company in Australia.

None of this has required the exercise of any discretions – it happens simply by the operation of law, as currently interpreted.

9.2 Breaking up the band

9.2.1 Can the Commissioner make an exclusion order without specific consideration of the entities?

At present, 'supergroups' are ignored by the Commissioner as a matter of practice. While this is commendable and appropriate, it begs the question of the legislative basis upon which this occurs. As has been discussed, groups do not depend for their existence upon the making of a decision by the Commissioner (see *Smeaton Grange Holdings Pty Ltd v Chief Commissioner of State Revenue*[43] discussed below), although exclusion orders do require the exercise of a specific discretion.

The question is therefore whether the Commissioner's current practice can be put on a sound legislative footing, and if so, whether that sound footing might also solve some of the other problems with the grouping regime.

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[43] (2016) 104 ATR 58.

Many of the problems with the grouping provisions could be resolved if the Commissioner were able to exclude persons from groups by reference to categories of persons, rather than by reference to individual persons.

In order for a general exclusion to be made, the Commissioner would, at the least, have to consider the matters set out section 74(2) and 74(3).

A simple form of order might look something like the following:

> A trust which is grouped with another trust *solely* because both trusts have a common beneficiary is the subject of an exclusion order from the group constituting the two trusts where the common beneficiary is not a default beneficiary of the trust, and has not received any distributions from the trust.

In the event that the Commissioner discovers that this exclusion order has caused an entity to be excluded from a group in circumstances in which the Commissioner forms the view that the entity ought not to be excluded, it is open to the Commissioner to revoke the exclusion order.

A similar order might be useful in the case of companies grouped because they happen to have a common employee – namely someone with two part-time jobs.

9.2.2 The sub-group issue

As discussed above, it is reasonable to suggest that the exclusion order can be applied at the smaller group, or sub-group, level. If that proposition is accepted, then the practicalities of making exclusion orders will be greatly simplified.

If an exclusion order can apply only if an entity can be separated from each other member of the broader group, then no trusts will be able to leave this group, as they will all be connected with another member of the group, being their groupies.

If, however, exclusion orders can be applied on a sub-group basis, then the trust might be able to be broken out of the broader group of trusts which it has no relation to – although given the sheer size of the supergroup, this may prove difficult in practice. However, if it can be done, then the group will shrink back down to consist only of the trust and its groupies. Similarly, the major public company should be able to disassociate itself fairly easily with the entities with which it is grouped as a result of the common employee provisions – but only on a sub-group basis. At the supergroup level, the public company would have to show it was not associated with each and every entity in the supergroup – a practically impossible task.

Further, if a particular groupie can, via an exclusion order, be broken out of the smaller group of entities to which it belongs, then it will also be separated from the supergroup.

For example, if A, which forms part of the supergroup, is grouped with B, B will then join the supergroup. If the exclusion order rules are applied only at the larger group level, B will need to show that it should be excluded from each other member of the supergroup. If, instead, the exclusion order is applied at the sub-group level, B need only demonstrate that it should be excluded from the group comprising A and B, as a result of which B would leave the supergroup.

On the assumption that B was not otherwise part of the supergroup, this seems an eminently fair outcome.

9.2.3 Multiple applications of the 'group of groups' rule

An alternative solution to the supergroup is the interpretation of the 'group of groups' rule. If the rule is limited to a single application, rather than being applied many times in succession, then the supergroup will not build up to its ultimate size, meaning that exclusion orders would not be necessary.

It is open to the Commissioners to issue a ruling setting out a view of the group of groups rule in this context.

9.2.4 The 'Smeaton Grange' solution

A partial solution which seemed to be available for a short time arose from the decision of White J in the Federal Court in Smeaton Grange.

White J decided, consistent with the decision of the Full Federal Court in *Ramsden*, that a beneficiary could disclaim their interest in a trust, and that such a disclaimer would be effective at law, and operate retrospectively.

That decision was overturned by the Full Federal Court. The reason given was that the scheme of the legislation should be considered based on the facts as they stood at the relevant time.[44]

The comment in Ramsden that '[a]t law an effective disclaimer operates retrospectively, and not merely from the time of disclaimer, was noted by Sackville AJA (who gave the majority opinion), but seems to have considered to be obiter.[45] Instead, Sackville AJA found that *'it does not alter the analysis to say that if the Disclaimers had retrospective effect it was by 'operation of law''*.[46]

My purpose here is not to consider the correctness of the decision of the Full Federal Court. Rather, I would like to focus on a key statement made by Sackville AJA in the course of his reasoning[47]:

> ...the legislative scheme can only be given effect if the existence and composition of any group of which the employer forms part can be determined at the same time as the employer becomes liable to pay payroll tax to the Chief Commissioner. It is at that point, if the employer does not discharge its liability, that group members become jointly and severally liable to pay the Chief Commissioner the amount of payroll tax the employer has failed to pay. It is also at that point that the Chief Commissioner can enforce the group members' liability. **The legislative scheme would be unworkable unless the determination of group membership in accordance with s 72 of the Payroll Tax Act can be undertaken by reference to the legal relationships as they exist between the different parties at the time the employer's liability to pay payroll tax arises.** That determination must be made on the basis of the facts as they exist at the relevant time. [emphasis added]

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[44] see paragraph 143.
[45] see paragraphs 120-121.
[46] see paragraph 150.
[47] at paragraph 143.

I agree with this statement entirely (leaving aside the question of whether those legal relationships are retrospectively affected by a later disclaimer). The legislation is unworkable unless a determination of group membership can be undertaken by reference to the legal relationships as they exist at the time.

The extension of the grouping provisions to beneficiaries of discretionary trusts makes the operation of the legislation unworkable. If an employer cannot know whether it is grouped with another employer, it cannot properly comply with its payroll tax obligations.

In the absence of fraud, you will know, or should be able to find out, whether you are a director or shareholder of a company. You will also know, if you are the director of a trustee company, who the beneficiaries of that trust are. However, a mere beneficiary of a trust does not have that information and nor does the trustee of another trust which may be grouped with the first trust without their knowledge.

Accordingly, the interpretation adopted by Sackville AJA, rather than saving the payroll tax legislation from unworkability, leads directly to an unworkable situation in which liabilities will be uncovered years after the fact, and which **could not** have been known by the taxpayer, even assuming access to the best legal advice, in the absence of the critical information that a trust existed with a wide beneficiary clause.

This unworkability becomes clearer in the context of 'supergroups'. The Commissioners do not seek to apply the payroll tax legislation to supergroups. Instead, we proceed on a 'don't ask, don't tell' basis. An neither the OSR, nor the taxpayer, are aware of the full web of discretionary trusts which lead to the supergroup, payroll tax is assessed only on the basis of relationships which are known. In the case of retrospective assessments, this may occur on the basis of information which the Commissioner, but not the taxpayer, is able to access, using the Commissioner's information gathering powers.

However, whatever assessment is issued is almost certainly wrong, having regard to the legislative scheme. In order to break up the supergroup, the Commissioner must exercise a positive discretion. In the absence of that discretion, the group exists, whether or not the parties, or the Commissioner, know about it.

9.2.5 A practical approach?

The question of whether a discretionary beneficiary of a trust should be treated as controlling that trust also arises in the foreign purchaser surcharge context for stamp duty, at least in NSW and Victoria. The question does not arise in Queensland, as only default beneficiaries are deemed to control the trust for stamp duty purposes in Queensland.

The Victorian legislation provides

> 3B What is a substantial interest in a trust estate for the purposes of the definition of foreign trust?
>
> (1) For the purposes of the definition of foreign trust in section 3(1), a person has a substantial interest in the trust estate of a trust if—
>
> (a) the person has a beneficial interest of more than 50% of the capital of the estate of the trust; or

(b) the Commissioner has made a determination under section 3D in respect of the person.

(2) If, under the terms of a trust, a trustee has a power or discretion as to the distribution of the capital of the trust estate to a person or a member of a class of person, any such person is taken to have a beneficial interest in the maximum percentage of the capital of the trust estate that the trustee is empowered to distribute to that person.

Other than being limited to capital distributions, rather than income and capital distributions, this definition has the same effect as the Payroll Tax Act definition.

While NSW takes the approach that this provision can be dealt with via the Smeaton Grange approach, Victoria takes a more liberal approach which does not necessarily require amendments of trust deeds.

The Victorian SRO includes this statement on its website

> Family trusts are predominantly discretionary in nature. These trusts will often have a wide class of family members as general beneficiaries, which may include foreign persons who are not intended to benefit from the trust. As such, in interpreting trust deeds of this nature, the Commissioner will adopt a practical approach so that trusts that have foreign beneficiaries who have not and who are, based on available information, unlikely in the future to receive any distributions, will not be considered a foreign trust.
>
> In adopting a practical approach, the Commissioner will consider the following factors:
>
> > Any intention (manifest or implied) of the settlor and/or trustee to vest any capital or income in the foreign person(s),
> >
> > The relationship or connection between the foreign persons and the person(s) for whom the trust was established,
> >
> > The likelihood of the foreign person(s) receiving or benefiting from any of the capital or income of the trust, having regard to any historical distributions of income and/or capital, and
> >
> > Any other relevant information available to the Commissioner.

Notwithstanding that the provisions refer only to capital distributions, the statement refers to both income and capital, which seems reasonable given the purpose of the statement.

It is also noteworthy that the Commissioner does not accept that the foreign persons are not beneficiaries of the trust – instead the Commissioner takes the view that the trust is not a foreign trust. Implicitly, the trust is not controlled by the foreign beneficiaries.

Applying the same approach to payroll tax would suggest that trusts should not be treated as being controlled by beneficiaries who have not, and would not be expected to, receive distributions under the trust. This would drastically reduce the scope of the grouping provisions as they relate to discretionary trusts, and would effectively break up the supergroups without need for policy changes or legislative intervention.

It would also separate some of the 'groupies' from their trusts, where there was no reasonable expectation of receiving a distribution.

The approach might apply, for example, where a trustee has made a family trust election for income tax purposes. While it is still possible for the trustee to distribute amounts to persons outside the family group, albeit with an additional tax cost (family trust distribution tax), for practical purposes, however, it is reasonable to assume that only persons within the family group are likely to receive distributions of either income or capital from the trust.

Application of this approach to payroll tax would go a long way towards 'breaking up the band'. While a note of caution should be issued as to how this would operate in practice, keeping in mind the statement in *Smeaton Grange* that it would be 'unworkable' if we did not know which entities constituted a group., it seems that this approach would give rise to less uncertainty, rather than more, if it breaks up the supergroups.

Where there is residual uncertainty, the Commissioner might be approached for their views. A reasonable rule of thumb might suggest that an absence of uncertainty due to an absence of knowledge of the existence of the trust in question might strongly suggest that the trusts should not be treated as associated.

10 Joint Liability of Group Entities

10.1 Liability to be construed in context

First, the preceding discussion points are relevant context, and the implementation of those factors should operate to remove numerous entities from alleged groups, for example:

a. if they have no employees (although this proposition may require overrule of *Scott and Bird*);

b. if they do not even operate a business (noting however the 'deemed' business that may arise for a trust by operation of s.66);

c. if there is no substantial connection or interdependence between the businesses;

d. if the businesses that are carried on are plainly disparate in their nature;

e. if, irrespective of ownership, the businesses are separately controlled; and

f. if the degree of common ownership is slim.

The interpretation and implementation of the grouping provisions and the exclusion provisions consistent with their purpose and object will mean that there are fewer entities found to exist in any group in the first place.

That will alleviate the jeopardy of joint liability affecting an entity that should not reasonably even be treated as a member of a group.

10.2 Joint liability Under s.34(2) and s.42(2)

Joint liability for grouped entities is primarily imposed by s.34(2) for annual liability, and s.42(2) for final liability.

Both provisions refer to "every relevant group *employer*" as being made liable.

Applying basic rules of statutory interpretation, and considering the text, context and purpose, those sub-sections have a pre-condition, namely that the group member be also an "employer".

10.3 The scope of s.51A

In Queensland, section 51A is expressly made subject to the primary provisions in s.34(2) and s.42(2). As mentioned above, those provisions confine liability to group members who are also employers and s.51A must be construed in light of the express provision: that it is subject to s.34(2) and s.42(2).

Section 51A(2) only operates to eliminate the possible argument, that an entity which is now an employer was not an employer during the period to which the liability amount relates.

Section 51A cannot overcome the fundamental legal principle that a law cannot invoke a punishment upon person for the liability or offence of someone else.

The principle of legality will not permit the tax liability of one employer to be recovered from someone who has no connection to that liability.

The provision does not contain wording such as will suffice to repel the principle of legality [see Philippides J A in *Commissioner of State Revenue v Can Barz Pty Ltd & Anor* [2016] QCA 323].

10.4 Dual use

As described above, the purpose of the provisions is to prevent avoidance of payroll tax by subdividing businesses. It is therefore relevant to consider to what extent the provisions serve that purpose.

In this respect, the provisions, as presently drafted, perform two functions:

a. They deny access to multiple tax free thresholds to employers who carry on related businesses

b. They impose joint and several liability upon all members of the group. In doing this, they define a 'group' which includes those employers, together with numerous other persons and entities, including those which do not carry on a business, and which have never had employees.

It may be suggested that only the first function serves the purpose of the provisions. To be generous to the drafters, it may also be suggested that the deeming provisions which expand the group to include non-employers, and persons who do not carry on businesses, serve the purpose of allowing those persons to be used as 'links' in a chain which allows other businesses to be added to the group. Breaking those links can be addressed not only by reform, but also by the manner in which the provisions are administered.

Even accepting that it is appropriate to use 'links in a chain', the provisions go far beyond what might be considered reasonable. In particular, the suggestion that all beneficiaries of a discretionary trust control that trust flies in the face of common sense and practice, particularly in cases where the beneficiary has never had a distribution made to it, and is not even aware of the existence or terms of the trust.

The second function of the provisions, however, does not serve the purpose of the provisions at all. The purpose of the provisions is sufficiently served by denying each business a separate entitlement to the benefit of the payroll tax threshold. Once that purpose has been served, it is appropriate to consider whether the same set of provisions should be applied in determining who should be liable to pay the resulting tax. This is particularly relevant if it is accepted that non-employers and persons who do not conduct businesses are legitimately included in the group only as links in a chain – the justification for them being additionally subject to personal liability is quite different, and not in any way related to the purpose of the provisions.

The situation may be contrasted with the income tax consolidation provisions, which also impose joint and several liability in many circumstances. In the case of the consolidations provisions:

a. The head company elects into those provisions – in the absence of an election, the provisions do not apply.

b. The provisions are limited to genuine company groups and do not extend to unrelated third parties.

c. The companies within the group benefit from the provisions, as they simplify the tax treatment of company groups, and allow intra-group transactions to be ignored.

d. When the provisions apply, it becomes difficult to separate out the liabilities of each entity.

None of those considerations is relevant to payroll tax.

a. Payroll tax grouping is not voluntary

b. The provisions extend well beyond genuine company groups, including to non-employers (subject to the remarks above) and persons who do not carry on businesses at all

c. No company benefits from payroll tax grouping.

d. it is very straightforward to work out the liability which each employer would otherwise have incurred had the threshold been unavailable.

10.5 Administrative solutions

The administrative options available here are rather simpler than those in relation to the question of which entities constitute a group.

The decision whether to pursue a particular individual or entity for the payment of payroll tax which remains unpaid by another entity rests with the Commissioner. It is open to the Commissioner not to choose to pursue particular individuals or entities.

It is further open to the Commissioner to outline a policy, founded in the power of general administration, as to circumstances in which individuals or entities will not be pursued for the payroll tax debts of others.

I suggest that an element of such a policy should include a consideration of the 'links in a chain' principle – that while an individual or entity might be appropriately included in a group to prevent the avoidance of payroll tax by accessing of multiple thresholds by multiple employers, there is a separate question for consideration as to whether it is appropriate to pursue the 'links in a chain' who are not employers, and are not in a position to influence whether or not the tax is paid.

11 Legislative options for reform

While our purpose today is to discuss administrative options, set out below, for completeness, are several legislative options. To the extent that similar outcomes can be achieved by the administrative approaches suggested above, that is to be commended.

Legislative options which may be considered in relation to the breadth of the provisions include:

a. Limiting the 'control' provisions relating to beneficiaries of discretionary trusts to default beneficiaries of those trusts, and perhaps to beneficiaries to whom a distribution has actually been made. This would eliminate 'accidental' groups which result simply from a wide beneficiary definition commonly used in family discretionary trusts.

b. Removing the provision by which unrelated groups are joined together by the simple presence of a common member.

c. Expanding the use of the de-grouping provisions, so that they focus on ensuring that the only businesses which are grouped are those which are obviously related, and could (and should) have been conducted more practically under a single umbrella. A 'similar business test' may be a good starting point here. If the businesses being conducted are not similar in nature, there is no reason to think that they have been separated simply to avoid payroll tax. Under this approach, florists would be immediately de-grouped from hotels. This option which may be given effect statutorily, or by changes in administrative practice.

Options which relate to the 'dual use' of the grouping provisions include:

a. Providing that the liability of each member of the group is no greater than their individual liability would have been had the threshold not been available at all. This strikes a balance between ensuring that parties are not incentivised to avoid payroll tax, and ensuring that 'innocent' parties are not subject to payroll tax obligations over which they have no control.

b. Restricting the operation of the joint and several liability provisions to actual employers who conduct businesses, and excluding non-employers and those who do not conduct businesses. If the State still considers it appropriate to pierce the corporate veil in relation to directors of companies which fail to comply with their payroll tax obligations, that could be done in a clear and specific manner, such that those directors are liable only for the obligations of companies which they direct. At present, 'back door' liability is imposed on directors, not only in relation to companies which they control, but also in relation to entirely unrelated companies over which they have no control.

c. Removing the joint and several liability provisions altogether.

12 Employment agency provisions

12.1 The Employment Agency regime

An emerging payroll tax 'risk' area is the scope of the employment agent regime.

Division 1B of the *Payroll Tax Act 1971* (Qld)[48] takes an employment agent to be an employer[49] and a service provider to be an employee[50] under an employment agent contract. The amount paid[51] to the service provider is deemed to be wages by the employment agent[52] and therefore could be subject to payroll tax under s 9.[53]

Section 13G provides a definition of when Division 1B applies:

> (1) An **employment agency contract** is a contract under which a person (an **employment agent**) procures the services of another person (a **service provider**) for a client of the employment agent.
>
> (2) However, a contract is not an employment agency contract if it is, or results in the creation of, a contract of employment between the service provider and the client.
>
> (3) Subsection (1) applies to a contract whether it is formal or informal, express or implied.
>
> (4) For this section—
>
> **contract** includes agreement, arrangement and undertaking.

Some States structure their provisions differently but all have the same key elements.

The regime therefore applies to a 'labour hire' arrangement where a person (the employment agent) contracts with another (the client) for the provision of labour where there is no agreement between the worker (on-hired worker) and the end client. It requires a contract:

a. under which
b. a person procures the services of another person
c. for a client of the person
d. not being a contract of employment between that other and the client.

Where the provisions apply, the employment agent is taken to be the employer and the on-hired worker is taken to be the employee. Any amounts paid or payable under the employment agent contract are then taken to be wages, so the employment agent is liable to payroll tax on those amounts.

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[48] Division 8 *Payroll Tax Act 2007* (NSW); Part 3 *Payroll Tax Act 2009* (VIC); Division 3.8 *Payroll Tax Act 2011* (ACT); Division 2A, Subdivision 7 *Pay-Roll Tax Assessment Act 2002* (WA); Division 8 *Payroll Tax Act 2008* (TAS); Division 8 *Payroll Tax Act 2009* (NT); Division 8 *Payroll Tax Act 2009* (SA).
[49] Section 13H *Payroll Tax Act 1971* (QLD).
[50] Section 13I *Payroll Tax Act 1971* (QLD).
[51] Or payable – s 13J *Payroll Tax Act 1971* (QLD).
[52] Sections 13J(1) (also any value provided to the service provider or a superannuation contribution).
[53] Under s13J(2)(b) the client can give the employment agent a declaration that the amount paid is not wages by the employment agent.

Where an employment agency contract exists it would be expected that the agent's duties would not extend to the following:

a. instructing the worker in performing the work
b. supervising the worker whilst performing work
c. reviewing the work performed by the worker
d. bearing financial riskier the work performed by the worker
e. being responsible for rectification.

The provisions were traditionally thought to only apply to 'true' labour hire arrangements.

Four recent cases have changed the scope of the definition of an employment agency contract; CXC Consulting Pty Ltd & Ors v Commissioner of State Revenue,[54] Freelance Global Ltd v Chief Commissioner of State Revenue,[55] UNSW Global Pty Ltd v Chief Commissioner of State Revenue[56] and H R C Hotel Services Pty Ltd v Chief Commissioner of State Revenue.[57]

Unlike what many had previously understood – that under an employment agency contract the worker would typically be under the day to day direction of the client, not the agent – it seems that there is a risk that such a contract will exist where a business is contracted to produce a particular 'result' and uses subcontractors to perform some of the services under the contract.

12.2Employment Agency Contracts

In *CXC Consulting Pty Ltd & Ors v Commissioner of State Revenue*, CXC Consulting acted as an intermediary between users of IT services and IT providers. CXC Consulting controlled the day-to-day activities of the IT workers and facilitated the engagement and payment processes. The court found that CXC Consulting 'procured' the services of the subcontracted IT providers. As a result, Ginnane J assessed the payments from CXC Consultants to the IT contractors as wages and therefore subject to payroll tax. Payments to the IT contractors were found to be wages even where the IT contractors engaged with CXC Consulting through an interposed entity such as a family company or trust.

In *Freelance Global Ltd v Chief Commissioner of State Revenue*, Freelance Global operated similarly to CXC Consulting as an intermediary between service providers and clients. White J held that 'procure' means:

> "...more than facilitate or enable and requires that the employment agent cause the services of a contract worker (or service provider) to be provided to the employment agent's client, with the expenditure of care or effort by the employment agent. I do not accept that this can only be done if the employment agent recruits the contract worker or service provider for the client."[58]

[54] [2013] VSC 492.
[55] [2014] NSWSC 127.
[56] [2016] NSWSC 1852.
[57] [2018] NSWSC 820.
[58] *Freelance Global Ltd v Chief Commissioner of State Revenue* [2014] NSWSC 127 at [115].

White J decided that the employment agency provisions are not restricted to labour hire and employment agent firms, on the basis that if that were the case there would be no need for the Act to define what an 'employment agent' is:

> "I do not consider that the fact that the activities of employment agents or labour hire firms was an intended focus of the provisions justifies the conclusion that it was the only intended focus of the provisions such that the word "procure" should be construed as applying only to the activities of employment agents or labour hire entities in sourcing, vetting and supplying persons to clients. Freelance carries on the last activity, that is, supplying persons' services to clients on Freelance's behalf. It procures those services by arranging or causing the performance of work by the contractors for the client to occur through the contracts it enters into with its clients and the business structure provided to its contractors."[59]

However, *UNSW Global Pty Ltd v Chief Commissioner of State Revenue* may rein in the increasing breadth of the provisions. UNSW Global provided an independent contractor business by supplying expert opinions to solicitors from a list of experts it kept on retainer. The court explained that the provisions only apply when the worker becomes part of the client's workforce.[60] The court held that an independent contractor carries on his or her own business and is therefore not part of the client's workforce.

It remains to be seen to what extent this critical 'workforce' distinction will be uniformly adopted by the Commissioners on an administrative basis, thereby simplifying the operation of the provisions.

More recently, in *H R C Hotel Services Pty Ltd v Chief Commissioner of State Revenue* the court focused on the word 'for' in s 37(1) of the *Payroll Tax Act 2007* (NSW) (the equivalent of s 13G of the Queensland Act). The issue was whether sub-contracted workers of H R C Hotel Services were contracted 'for' its own use or 'for' the client (as is required in the definition of employment agency contracts). The court highlighted that it was necessary for H R C Hotel Services to sub-contract the additional workers to complete its contract with the client. Also, the service providers were integrated into the hotels' day-to-day businesses and were indistinguishable from actual employees. The court held, because of these two features, that H R C Hotel Services procured the service providers 'for' the client.

In light of these cases, for an employment agent to 'procure' the services of a service provider 'for' a client:

a. the service provider must become a part of the workforce of the client; and
b. the procurement of the service provider must be a necessity for the employment agent to fulfil its contract with the client.

12.3 Employment agency rulings

For completeness, I observe that there are four harmonised tax rulings in relation to employment agency contracts; Revenue Ruling No. PTA 026 Version 2: Employment Agency Contracts -

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[59] Ibid at [152].
[60] Ibid at [63].

Declaration by exempt clients,[61] Revenue Ruling No. PTA 027: Employment Agency Contracts Chain of on-hire, Revenue Ruling No. PTA 028: Employment Agency Contracts- Workers on-hired to government and Revenue Ruling No. PTA 029: Recruitment Agencies / Placement Agencies / Job Placement Agencies.

Not all of these rulings have been adopted by all of the harmonised jurisdictions, as set out in Appendix 1. Formal adoption of the rulings by each remaining jurisdiction may improve administration of the provisions.

[61] However, Revenue Ruling No. PTA 026 Version 2 was not adopted in Queensland.

13 Appendix 1 – Payroll tax rulings

(Source: https://www.payrolltax.gov.au/revenue)

Number	Description	Qld	NSW	ACT	Vic	Tas	SA	NT	WA
PTA011	Allowances and Reimbursements	✓	✓	✓	✓	✓	✓	✓	✓
PTA031	Commissioner's discretion to exclude from a group	✓	✓	✓	✓	✓	✓	✓	✓#
PTA018	Contractor Deductions	✓	✓	✓	✓	✓	✓	✓	x
PTA007	Contractor Provisions – Door-to-Door Sale of Goods	✓	✓	x	✓	✓	✓	✓	x
PTA020	Contractors – 180-day Exemption	✓	✓	x	✓	✓	✓	✓	x
PTA035v2	Contractors - 90-Day Exemption	✓	✓	x	✓	✓	✓	✓	x
PTA019	Contractors – Labour and Non-Labour Components	✓	✓	✓	✓	✓	✓	✓	x

PTA033	Contractors - Services ancillary to the supply of goods	✓	✓	x	✓	✓	✓	✓	x
PTA022	Contractors – Services Not Ordinarily Required	✓	✓	✓	✓	✓	✓	✓	x
PTA014	Contractors – What constitutes a day's work?	✓	✓	✓	✓	✓	✓	✓	x
PTA023	Contractors Engaging Others	✓	✓	x	✓	✓	✓	✓	x
PTA034	Contributions to the Construction Industry Long Service Leave and Redundancy Funds	✓	✓	x	✓	✓	x	✓	x
PTA038	Determining whether a worker is an employee	✓	✓	✓	✓	✓	✓	✓	x
PTA028	Employment Agency Contract – Workers on-hired to government	✓	✓	x	✓	✓	✓	✓	x
PTA027	Employment Agency Contracts – Chain of on-hire	x	✓	x	✓	✓	✓	x	x

PTA026v2	Employment Agency Contracts – Declaration by exempt clients	✓	✓	x	✓	✓	✓	✓	x
PTA005v2	Exempt Allowances: Motor Vehicle and Accommodation	✓	✓	✓	✓	✓	✓	✓	✓
PTA021	Exemption for Contractors Ordinarily Rendering Services to the Public	✓	✓	✓	✓	✓	✓	✓	x
PTA012	Exemptions for maternity and adoption leave pay	✓	✓	✓	✓	✓	✓	✓	✓
PTA013v2	Fees paid to golf professionals by golf clubs	✓	✓	x	✓	✓	✓	✓	x
PTA003	Fringe Benefits	✓	✓		✓	✓	✓	✓	x
PTA003v2	Fringe Benefits			✓					
PTA017	Grouping of Professional Practices and Administration Businesses	✓	✓	✓	✓	✓	✓	✓	✓

PTA008	GST Considerations for the Calculation of Payroll Tax Liability	✓	✓	✓	✓	✓	✓	✓	✓
PTA025	Motor vehicle allowance paid to real estate salespersons	✓	✓	x	✓	✓	✓	✓	x
PTA024	Overnight accommodation allowances paid to truck drivers	✓	✓	x	✓	✓	✓	✓	✓
PTA037	Paid Parental Leave	✓	✓	✓	✓	✓	✓	✓	✓
PTA036v2	Payroll Tax – Interest and Penalty Tax	x	✓	x	✓	✓	✓	x	x
PTA006	Payroll Tax exemption for payments to owner-drivers	✓	✓	✓	✓	✓	✓	✓	x
PTA032	Payroll tax exemption for schools	✓	✓	x	✓	✓	x	x	x
PTA039	Payroll Tax Nexus Provisions .	✓	✓	✓	✓	✓	✓	✓	✓

PTA030	Penalty Charges under Superannuation Guarantee Charge	✓	✓	x	✓	✓	✓	✓	x
PTA016	Profit Distributions and Loan Accounts	✓	✓	✓	✓	✓	x	x	✓
PTA029	Recruitment Agencies / Placement Agencies / Job Placement Agencies	✓	✓	x	✓	✓	✓	✓	✓
PTA004	Termination Payments	✓	✓	✓	✓	✓	✓	✓	✓
PTA010	Wage subsidies	✓	✓	✓	✓	✓	✓	✓	✓
PTA015	Workers' Compensation Payments	✓	✓	✓	✓	✓	✓	✓	✓