1 INTRODUCTION

The Victorian Parliament has inserted into the *Duties Act* 2000 (Vic) (*DA*) two general anti-avoidance rules, one directed at transfer duty avoidance (general duties rule) and the other at avoidance practices that are concerned with the land-rich provisions (land-rich rule). These rules draw on generally established and tested principles and terms employed in the income tax general anti-avoidance rule as contained in Pt IVA of the *Income Tax Assessment Act* 1936 (Cth) (*ITAA*). It is expected that these principles will be applied to define the legal scope and practical application of the new duties rules.

2 ELEMENTS OF THE NEW RULES

The general duties rule imposes duty on transactions in respect of which duty would have been chargeable under Ch 2 of the *DA* but for a tax avoidance scheme.1 On this formulation the rule applies where:

(a) there is a transaction;
(b) there is a tax avoidance scheme; and

(c) but for the tax avoidance scheme, duty would have been chargeable under Ch 2 on the relevant transaction.

So stated, it requires the making of a hypothesis as to what the liability to duty under a transaction apart from the impugned tax avoidance scheme would have been.

2.1 Transaction

The presence of a transaction in respect of which duty would have been chargeable is a condition precedent to the operation of the general duties rule.

The word transaction is not defined. In circumstances where there is no relevant antecedent state of affairs or a transaction by reference to which liability to duty could be assessed then arguably there would be no relevant transaction in respect of which duty would have been chargeable because none would have existed. On this reasoning, the general duties rule would only apply where there is a pre-existing arrangement from which the parties depart in favour of adopting the tax avoidance scheme. In other words, the presence of a pre-existing transaction provides the basis for the formation of the relevant hypothesis as to the transaction that would have been chargeable but for the impugned tax avoidance scheme.

This is an unduly restrictive analysis and courts may give a more generous interpretation to the word transaction to encompass possible options that could have been available to the affected taxpayer.

Other than the forgoing possible limitation, it is anticipated that little will turn on the scope of the word transaction because where a duty benefit has been obtained, one would expect that there would have existed a relevant
transaction in any particular case. It would be a question of fact as to what that transaction may be.

2.2 Tax Avoidance Scheme

The word scheme is defined in very broad terms by s69B(2) of the DA to include the whole or any part of a contract, arrangement, understanding, undertaking or promise and extends to unilateral plans, proposals and courses of action.

In view of the application of settled jurisprudence to the interpretation of the concept of a scheme in the context of income tax, it is submitted that the Victorian Supreme Court and ultimately the High Court would interpret the requirement of scheme under s69B(2) in the following manner:

(a) The Commissioner of State Revenue has significant discretion in the identification and particularisation of the relevant scheme by reference to which the general duties rule may be applied.

(b) Within a wider scheme which has been identified, the Commissioner may rely upon a narrower scheme as meeting the requirements of the general duties rule. This is subject to the following qualifications:

(i) That the decision to rely upon the narrower scheme does not cause embarrassment or surprise to the other side; and

(ii) That the circumstances are capable of standing on their own as a scheme within s69B without being robbed of all practical meaning.2

2.3 Duty Chargeable But For Scheme

The benefit that forms the subject of the general duties rule lies in the definition of tax avoidance. The expression tax avoidance is defined by
s69B(2) of the DA to mean the elimination, reduction or postponement of liability to transfer duty.

On this formulation, any duty gain howsoever described would fall within the scope of the concept of tax avoidance. Other than the reduction, elimination or postponement of liability to duty there would be no conceivable duty benefit.

The general duties rule imposes duty on a transaction in respect of which duty would have been chargeable but for a tax avoidance scheme. This requires the making of a hypothesis as to what may have taken place apart from the impugned scheme, a requirement which has to be satisfied by reference to relevant facts and evidence as to options reasonably available to the affected taxpayers.

**Purpose Or Effect of Tax Avoidance**

The general duties rule applies to impugn a tax avoidance scheme being a scheme that directly or indirectly has tax avoidance:

(a) as its purpose or effect; or

(b) as one of its purposes or effects, provided that the purpose or effect of tax avoidance is not merely incidental to another purpose or effect of the scheme. Tax avoidance may be the effect of the scheme at the time when it was entered into or subsequently.

The general duties rule applies where tax avoidance is one of the purposes or effects and not necessarily the dominant purpose or effect.

Effectively, the first requirement that the scheme has tax avoidance as its purpose or effect is completely subsumed by the second. Provided the relevant tax avoidance purpose or effect is not merely incidental then the rule would apply. It is by no means clear what the expression ‘merely incidental’
means or how it can be used as a threshold condition to identify the transactions to which the rule is intended to apply. That expression is likely to take its meaning and content from a particular context and facts and it would be very difficult to formulate a general principle to determine what purpose or effect is merely incidental to other purposes or effects of the scheme.

The relevant purpose or effect is that of the scheme. This prescribes a purely objective test that would not permit a consideration of evidence of the subjective motivation or purpose of the particular scheme participants. This approach is consistent with that adopted by the Federal Court to the interpretation of Pt IVA.3

The general duties rule requires the ‘purpose or effect’ of a scheme to be the elimination, reduction or postponement of any person’s liability to pay transfer duty.4 This raises a question as to the meaning of the word ‘effect’ and its relationship to the word ‘purpose’.5

On one view, the use of the expression purpose or effect proceeds on the basis that there is a difference between the purpose and effect of a scheme.6 On this view, the purpose of the scheme looks to the actual driving force behind the scheme whereas the effect looks to the actual consequence, result or outcome of the scheme.7 It would follow that regardless of why, objectively, the scheme was entered into or carried out, if the scheme actually results in the reduction, elimination or postponement of liability to transfer duty then the rule would apply. The presence of commercial or non-tax considerations or influences would be irrelevant.

On this construction of the word ‘effect’, the first requirement of ‘purpose’ would be made completely redundant because the presence of some form of a transfer duty gain is a condition precedent to the application of the rule and yet the presence of such a gain would provide the impugned effect.8 This follows because a purpose to avoid liability to duty (by means of reduction,
elimination or postponement) is not enough unless the scheme actually results in a duty gain and hence would have the requisite impermissible effect.9

The alternative to the view that there is a difference between the purpose and effect of a scheme is to treat purpose as an element in assessing the effect of a scheme. On this view, the determination of the effect of the impugned scheme requires an examination of the consequences of the scheme and the objective purpose of the scheme. As noted, a mere purpose to avoid duty can never be enough unless the scheme has that effect.

It is submitted that the expression ‘purpose or effect’ should be interpreted and applied as a composite expression that requires a determination of the purpose and effect of the scheme.10 A mere tax effect without the impermissible tax avoidance purpose would not be enough and likewise a mere tax avoidance purpose without the impermissible tax effect would not be enough. It follows that the general duties rule would only apply where a scheme is tainted by a purpose of reducing, eliminating or postponing transfer duty that is not merely incidental and that the scheme actually or potentially has the effect of reducing, eliminating or postponing liability to transfer duty.

This is consistent with the broad scheme and policy of the legislation. In essence, purpose looks to the factors that explain why the scheme was entered into or carried out whilst effect looks to its consequences. Where s69B(1) of the DA refers to a scheme that has the relevant purpose or effect ‘whether the scheme had that effect at the time it was entered into, or only subsequently’, it is submitted that Parliament intended the rule to apply to a scheme that is tainted by a tax avoidance purpose at the time when it was entered into or carried out but has a delayed tax avoidance effect.
3 IMPOSITION OF DUTY UNDER THE NEW RULES

Once the terms of the general duties rule are satisfied then the rule proceeds to authorise the Commissioner to disregard the scheme and determine what duty would have been payable under Ch 2 of the DA ‘but for’ the scheme. The expression but for effectively requires a reassessment by reference to an alternative and essentially hypothetical state of affairs that did not exist in fact but that was reasonably expected in the circumstances. Effectively, the question would be:

If the affected taxpayer did not enter into or carry out the impugned scheme, what would a reasonable person expect the taxpayer to have done?

The Commissioner may then make an assessment or reassessment by reference to the reasonably expected alternative identified.

The land rich rule contains further provisions to facilitate the making of an assessment. In making a determination under s89I of the DA, the Commissioner may:

(a) deem a company or unit trust scheme to be a landholder of a particular class;

(b) deem a landholder or the trustee of a unit trust scheme to hold land and determine the extent of that landholding;

(c) deem a landholder to be land-rich;

(d) deem a relevant acquisition to have been made by any person and determine the extent of that interest; and

(e) determine the value of any land.

It is trite to note that the Commissioner must make these determinations in accordance with law and it is critical that such determinations are founded upon relevant facts that justify such a determination. In other words, such
determinations are only open to facilitate the making of an assessment by reference to the reasonably expected alternative course of action that the taxpayer would have undertaken but for the impugned scheme.

4 POTENTIALLY AFFECTED ARRANGEMENTS

The kind of arrangements to which the general duties rule and land-rich rule could apply include:

(a) The grant of a long term lease to one entity and the grant of an option over the remainder to a related entity, with the lease and option being contained in separate agreements specifically to avoid the potential operation of s7(1)(b)(v) of the DA.

(b) Where a Victorian company’s only asset is land in Victoria with an unencumbered value of less than $1,000,000, transferring all the company’s shares to a prospective purchaser of the land (with appropriate indemnities from the vendor regarding the company’s past liabilities) instead of transferring the land itself.

(c) Granting to one entity an interest in relevant fixtures before transferring to a related entity the land on which the fixtures are located.11 Leaving aside the general duties rule, this option continues to be available following the enactment of new s22A of the DA.

5 APPLICATION OF DOCTRINE OF FISCAL NULLITY?

The UK common law doctrine of fiscal nullity operates to see though a series of individual transactions and characterises the overall arrangement by reference to the end result of the series as a whole rather than to each individual transaction considered. In order for the operation of the doctrine to be triggered:
(a) there must be a pre-ordained series of transactions or one single composite transaction. This composite transaction may or may not include the achievement of a legitimate commercial or business end; and

(b) there must be steps inserted which have no commercial or business purpose apart from the avoidance of liability to tax, not no business effect.

If those ingredients exist, the inserted steps are to be disregarded for fiscal purposes and the court must then look at the end result.12

In John v FCT, the High Court referred to the doctrine of fiscal nullity as ‘essentially a principle arising from the construction of the statute’.13 The Court’s view was that the doctrine does not apply to the ITAA because the Act already contains a general anti-avoidance provision.14 By parity of reasoning, it is submitted that the existence of transfer duty and land-rich duty general anti-avoidance provisions in the DA means that the doctrine does not apply to these two duties. The application of the doctrine of fiscal nullity to other duties under the Act and to stamp duty in jurisdictions without duties general anti-avoidance rules remains to be determined.15

6 CONCLUSIONS

The introduction of the general duties rule and the land-rich rule is likely to create uncertainty in the operation of the law and pose a significant challenge to practitioners seeking to advise on transfer duty and land-rich duty in Victoria. The rules must be considered on every occasion where advice is provided on the potential imposition of the relevant duties.

The greatest challenge facing Victorian courts is to determine the boundaries of the general duties rule and land-rich rule. The rules contain very broad
concepts and low thresholds to ensure a very broad and arguably indeterminate operation. Such a broad operation must be reconciled with perceived legislative intention and policy. Under a literal interpretation of the rules, a transaction may be impugned even though it may be commercial in every respect except for a purpose or effect of reducing or postponing liability to transfer duty or land-rich duty.
Notes

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1 DA s69B.
4 DA s69B(1).
5 The observations made here apply equally to the land-rich rule.
8 Victoria, Parliamentary Debates, Legislative Assembly, 2 June 2004, 53 (Robert Clark, Member for Box Hill).
9 Sections 69B and 69C of the DA.