OPINION

APPLICATION OF PRECEDENT TO TAX CASES

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ADVICE

APPLICATION OF PRECEDENT TO TAX CASES

1. We are asked to advise the Australian Tax Office on issues concerned with the rule of law and application of precedent in relation to the handling of tax cases.

2. The Inspector General of Taxation is currently reviewing the Tax Office's management of litigation. It is anticipated that the Inspector General's report will place heavy emphasis on views expressed by Justice McHugh in his speech at the Australian Bar Association Conference, '*Tensions between the Executive and the Judiciary*', in July 2002. In his speech, McHugh J referred to the tension between the executive and the judiciary. He referred to an earlier paper by Professor Pearce that gave examples of Departments refusing to follow judicial or tribunal decisions. The judge said:

> No doubt an Executive agency is entitled to disregard a decision where it is truly in conflict with another decision that it thinks is correct. It may sometimes also be justifiable to refuse to follow a decision that is the subject of appeal. But that has problems. Judicial decisions are not provisional rulings until confirmed by the ultimate appellate court in the system. Until set aside, they represent the law and should be followed. Moreover, the Executive can run into serious legal problems where it continues to enforce legislation that a court has ruled invalid. Even more difficult to justify is the refusal to follow a ruling that is not the subject of appeal merely because the agency regards it as wrong and will test it at the next opportunity.

3. We are instructed that the Inspector General is likely to recommend in his report that the Commissioner should administer tax laws consistently with court decisions in relation to all similar taxpayer cases until and unless the law is changed by Parliament. The view seems to be that this applies equally to "quasi judicial" decisions of the Administrative Appeals Tribunal.

4. We are asked whether we agree with the strict views of McHugh J, and for guidance on how to resolve tensions in this area between administration of the tax law and respect for the rule of law.

Consideration

5. The issues raised involve principally questions of appropriate behaviour, rather than strict law. They arise across government, and are not confined to the area of tax law. The circumstances of each case may vary and we do not consider that absolute rules are generally appropriate. At best, we consider that some broad principles can be identified that can be used to guide conduct in this area.

6. The position of government bodies is different from private parties, in the sense that they are responsible for administration of a law across the board. This means that issues of consistency arise. However, we do not consider that this prevents an agency like the ATO from challenging earlier judicial decisions. Issues of consistency and fair administration can be addressed in ways other than a rigid adherence to previous judicial decisions.

7. The first point we make is that the law is not authoritatively settled in any particular case until final orders are made. Nevertheless, where the law is generally settled as a result of a prior decision of an appellate court, it will not usually be appropriate to resist dealing with another matter covered by the decision on the basis of that authority. This, however is a matter of good administration rather than strict law, and there may be circumstances where a challenge to a decision is appropriate. Where there is not an appellate court decision, there is greater opportunity to challenge a decision although, in extreme cases, even an earlier High Court decision can be the subject of challenge in the High Court..

8. A decision by the High Court or a Full Court is authoritative, in the sense that it will be followed by other judges unless it is overturned. Single judges or tribunals are not free to depart from such decisions and hence it would usually be inappropriate and unwise for an administrative decision-maker to adopt a contrary interpretation. If an appeal is still on foot, such as an outstanding High Court appeal, the most appropriate approach may be to delay finalising a matter until the High Court or Full Court decision is available. It is recognised that this will not always be possible.

9. In the case of single judge decisions, the position is a little different. While a single judge is not obliged by the doctrine of precedent to follow the decision of another single judge, he or she will usually do so unless he or she considers it to be 'clearly wrong'. This is done as a matter of judicial comity.

10. However, an administrative tribunal will normally be expected to follow a single judge decision that has interpreted a statutory provision (*FCT v Salenger* (1988) 19 FCR 378, 387-8). It follows that an administrative decision-maker who did not follow a single judge decision would be likely to find his or her decision overturned on merits review by the administrative tribunal. There is, therefore, clearly a risk in deciding not to follow even a single judge decision, unless that decision is the subject of an appeal. However, if advice has been obtained that suggests that an earlier tribunal or single judge decision is wrong, that in our view provides a basis on which to challenge that decision. The real issue in that situation is how to deal with cases affected by that view pending an opportunity to test the issue in court.

11. We consider there is clearly a difference in this regard between a settled interpretation not subject to appeal and a recent interpretation that is subject to appeal or where there is a clearly announced intention to seek a suitable vehicle to test the issue further.

12. In a previous advice the Solicitor-General has expressed the following views which we reproduce here (amended not to refer to the specific matter under consideration):

> In the present case, however, there is some justification for declining to follow the Full Court's approach to the construction of the definition. The decision was not one of the ultimate appellate court. An appeal to the High Court having been precluded solely on the ground that the matter was not a suitable vehicle to consider the construction issue, it should be open to seek to bring before that Court another case which does not have such problems. If (the agency) were to regard itself as obliged to follow the decision, its ability to generate such a test case would be severely restricted.
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> (The agency) is obliged to comply with the law (this obligation can generally be enforced through judicial review mechanisms, and is reflected in cl.4 of the APS Code of Conduct, set out in reg.7 of the Public Service Regulations made under the *Public Service Act 1922*). The Act also provides that one of its functions is "to make determinations accurately and quickly in relation to claims and requests" made to it under the Act. More generally, neither the Commonwealth nor (the agency) should exploit their position by simply refusing to follow judicial authorities so as to force claimants through multiple levels of review and appeal in order to maintain their entitlements under the Act. A comparison may be drawn with the model litigant principles applicable to the conduct of litigation by the Commonwealth, which require the• Commonwealth to avoid unnecessary delay and to pay legitimate claims without litigation, and prevent the Commonwealth from taking advantage of claimants who lack the resources to litigate a legitimate claim.
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> However, such obligations do not necessarily mandate adherence in all circumstances to any decision of an intermediate appellate court. If this were the case, a Department administering a particular statute could be bound for all time (subject only to clarification by legislative amendment) by a decision of a lower court as to the construction of that statute, because an appeal was not or could not be pursued (for example, where the relevant Department was not a party to the proceedings before the lower court). An administrator is not part of the judicial hierarchy, and is not bound by the doctrines of precedent as is a lower court. Accordingly, in appropriate circumstances, it would be legitimate for (the agency) to depart from existing judicial decisions in order to produce a further test case seeking to overturn those decisions and uphold (the agency's) view as to the correct legal position.
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> …
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> In the present case, it is important that the High Court has not yet considered the relevant construction issue on its merits, nor has it indicated that the issue is not of sufficient general importance to attract a grant of special leave to appeal in a suitable case…. **Acting on the basis of legal advice that the reasoning of the Full Court is incorrect, we consider that (the agency) is justified in regarding the legal position as unsettled until such time as it has been considered by the High Court**.
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> If it does adopt such a position, however, it should do so openly, by disclosing to the relevant claimant that its decision may be contrary to (the case in issue), that it has taken the view (on the basis of legal advice) that the approach adopted in that case is incorrect, and indicating that it is prepared to contest the matter on appeal by challenging the correctness of it. If this is the only basis on which (the agency) proposes

> to resist payment of a claim, it would be practically essential, in our view, for the claimant to be given some form of indemnity covering his or her costs of taking or defending any appeals (this could be done either by agreeing to a costs order against it in any event, or through an applicable legal aid scheme). (The agency) must avoid any suggestion that its position will result in an undue burden or prejudice to individual claimants in particular cases who are forced into the courts in order to maintain their entitlement under the Act.
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> (The agency) should also be aware that it if adopts such an approach, placing express reliance on counsel's opinion as to the correctness of the decision in issue, it may not be entitled to rely on any privilege (including legal professional privilege) to resist the disclosure of the opinion in subsequent merits review or judicial review proceedings. For example, the opinion might be regarded as "relevant to the review of the decision" for the purposes of s 37 of the *Administrative Appeals Tribunal Act 197*5 (note that s 37(3) expressly overrides any privilege in such circumstances).
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> Provided that the above circumstances are present, we do not consider that such a course of action by (the agency) would expose it to any liability in tort, such as for misfeasance in public office (see *Northern Territory v Mengel* (1996)185 CLR 307), even if it were ultimately established that the decision made was contrary to the Act.
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> Such an approach would not set (the agency) above the law. The rule of law is maintained by the amenability of each administrative decision made to correction by the courts on the grounds of legal error. Although there is a strong likelihood that the Administrative Appeals Tribunal, the Federal Court at first instance and even the Full Court of the Federal Court will overturn decisions which are not in accordance with the construction adopted in the decision in issue, it is open to argue for the alternative construction throughout the appeals process so as to preserve its rights to argue the construction issue if and when the matter reaches the High Court. (our emphasis)

13. We consider that, in order to resist accusations that the ATO is disregarding judicial decisions contrary to the rule of law, it is important that, if the ATO considers that a decision is wrong, it should as soon as possible put those affected on notice of this view. It should only seek to challenge an earlier decision where it has legal advice to the effect that the decision is wrong. To avoid criticism it will also normally be appropriate, if the ATO launches a challenge to the earlier decision, to fund or organise suitable assistance to bring a test case. Pending the outcome of such a decision, other taxpayers affected should be informed of the proposed course of action.

14. We note that ATO Rulings, and Parliamentary Inquiries into Tax Rulings (see especially the 1987 Senate Report on Income Tax Rulings, pp. no.217/1987) recognised that the Commissioner may wish to argue in future litigation that an

interpretation in a ruling is correct despite an earlier judicial decision. We see no problem with this provided that the Commissioner is open about his intentions.

15. The position is, however, quite different where the law has been administered for a period of time on the basis of a judicial interpretation and the Commissioner subsequently decides that that interpretation is wrong or that it is prejudicial to the revenue. In that situation it is far more difficult to justify seeking to overturn the established interpretation on which the law has been administered and a taxpayer's liability determined. See recent remarks by the Victorian Court of Appeal in *Smith v Transport Accident Commission* [2005] VSCA 251, esp [18],[41],[45].To act in this way can be seen as disadvantaging one group of taxpayers over another. It, therefore, seems important, in our opinion, that a challenge to a decision considered wrong as a matter of law should occur as soon as possible after the particular decision, and that the Commissioner publicly indicate that he considers that the decision is wrong as a matter of law and that he will be seeking an opportunity to have the matter reviewed. He should normally take steps to generate and fund a test case on the point. In this way the model litigant obligations are met.

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