AUSTRALIAN TAXATION OFFICE PRONOUNCEMENTS: WHY TAX ADVISERS NEED TO EXERCISE CAUTION

ALEXANDER FULLARTON* AND DALE PINTO#

Abstract

In the modern environment of complex taxation law there is ever-evolving legislation and interpretation. To maintain the high professional standards that are ethically and legally required, tax practitioners are obliged to engage in close scrutiny of the law to obtain a clear understanding. However, tax practitioners find it increasingly difficult to keep themselves informed while dealing with the pressures of their workloads. Therefore, to assist practitioners, professional bodies are constantly providing information and commentary about changes to statutory and case law. Further, the Australian Tax Office (ATO) issues its own interpretations, rulings and other such proclamations, to guide taxpayers and practitioners and assist in compliance. The authors' research suggests that the sometimes confusing and apparently convoluted legislative change and evolving case law are leading practitioners to become increasingly reliant on ATO rulings and advice rather than conducting their own legislative research and making their own interpretations of statutes.

This article argues that the practice of accepting ATO opinions without challenge can have extremely significant fiscal impacts on taxpayers and tax collections. It warns that tax practitioners should not always consider that the rulings, determinations and advice provided by the ATO give the greater clarity and certainty in the preparation and lodgement of taxation returns and the payment of tax that are sought by practitioners.

I INTRODUCTION

In the modern environment of complex taxation law there is ever-evolving legislation and interpretation. To maintain the high professional standards that are ethically and legally required, tax practitioners are obliged to engage in close scrutiny of the law to obtain a clear understanding. However, tax practitioners find it increasingly difficult to keep themselves informed while dealing with the pressures of their workloads. Therefore, to assist practitioners, professional bodies are constantly providing information and commentary about changes to statutory and case law. Further, the Australian Tax Office (ATO) issues its own interpretations,

* Adjunct Professor, Curtin Law School, Curtin University.
# Professor of Taxation Law, Curtin Law School, Curtin University.
This paper comments on research published in articles by Alexander Fullarton and Dale Pinto in the *New Zealand Journal of Taxation Law and Policy*. Alexander Robert Fullarton and Dale Anthony Mark Pinto, 'Tax Accounting for Livestock: Mother or Meat/Capital or Revenue' (2021) 27(1) *New Zealand Journal of Taxation Law and Policy* 39; 'The *Wade Case*: An Analysis' (2021) 27(2) *New Zealand Journal of Taxation Law and Policy* 121.

rulings and other such proclamations, to guide taxpayers and practitioners and assist in compliance.

The authors' research suggests that the sometimes confusing and apparently convoluted legislative change and evolving case law are leading practitioners to become increasingly reliant on ATO rulings and advice rather than conducting their own legislative research and making their own interpretations of statutes. This article argues that the practice of accepting ATO opinions without challenge can have extremely significant fiscal impacts on taxpayers and tax collections. It warns that tax practitioners should not always consider that the rulings, determinations and advice provided by the ATO give the greater clarity and certainty in the preparation and lodgement of taxation returns and the payment of tax that are sought by practitioners.

Tax agents are duty bound to take reasonable care to ensure that taxation laws are applied correctly to the circumstances in relation to which they are providing advice to a client,[1] and in that context this article asserts that agents should not accept that the ATO's view on a matter is unquestionably correct. Further, it is noted that, while the ATO provides guidance and views, their written advice usually contains a statement to the effect that they are for guidance only and may not be binding in a court. Their written opinions often include a specific disclaimer that states:

> If this advice turns out to be incorrect and you underpay your tax as a result, you will not have to pay a penalty. Nor will you have to pay interest on the underpayment provided you reasonably relied on the advice in good faith. However, even if you don't have to pay a penalty or interest, you will have to pay the correct amount of tax.[2]

Therefore, it is clear that the ATO assumes no responsibility to taxpayers or practitioners for misinterpretations or misapplications of the law. Taxpayers and their agents must make reasonable independent inquiry to ensure compliance and the correct payment of tax.

II LIABILITY FOR GIVING ADVICE

The authors examined an uncommon, but significant, business transaction that occurs in rural and remote Australia each year – the sale of a pastoral lease by a sole trader, partnership, or similar business structure. In the sale of a pastoral and farming property as a going concern, the ATO view is that *all* animals held in a business of primary production are considered to be trading stock, regardless of the function that they perform in that business. The impact of this is that all receipts from the sale of animals in conjunction with the sale of a primary production business are taxed as income according to ordinary concepts. Therefore, individual pastoralists,

---

1 Code of Professional Conduct *Tax Agent Services Act 2009* (Cth) s 30-10.

2 Letter from Alison Lendon, Deputy Commissioner of Taxation, to Alexander Fullarton, 6 November 2019. The following articles have a copy of the letter from the Deputy Commissioner of Taxation. Alexander Robert Fullarton and Dale Anthony Mark Pinto, 'Tax Accounting for Livestock: Mother or Meat/Capital or Revenue' (2021) 27(1) *New Zealand Journal of Taxation Law and Policy* 39; 'The *Wade Case*: An Analysis' (2021) 27(2) *New Zealand Journal of Taxation Law and Policy* 121.

graziers and farmers are denied the tax concessions that other business proprietors are granted on the sale of capital assets included in the transfer of their businesses.

In their publications,[3] the authors challenge that opinion and argue that animals used for breeding or other purposes are not trading stock, but rather should be considered as capital assets used for the purposes of manufacture.[4] They argue that the word all is not contained in s 995 of the *Income Tax Assessment Act 1997* (*ITAA 1997*), and they note that the ATO relies on the decision in *Federal Commissioner of Taxation v Wade* (the 'Wade Case')[5] to validate its opinion. They find that the ATO's reliance on the decision in the Wade Case for support may be somewhat problematic.[6]

The authors argue that there *is* a distinction between breeding animals and livestock produced for sale, and that such animals should be accounted for and taxed accordingly.[7] The authors' research has established that, while the ATO view is correct, it is based on a false premise and might fail if challenged in court. However, it appears that tax professionals have generally accepted the ATO view without challenge for over 70 years and have been advising their clients accordingly. It is the authors' view that, if the matter were to be challenged and taxpayers were found to have been overpaying tax, then the caveat contained in the ATO advice might place the liability on the professionals providing the advice to the taxpayer and not on the ATO.

III THE WADE CASE STUDY

To consolidate their argument, the authors have examined the evidence presented to the High Court in the Wade Case.[8] Their publications look at the ATO advice that all animals held in a business of primary production are trading stock, and the basis on which the ATO holds that belief. They find that, while the ATO advice is correct, the basis for that view is not.

The ATO's view is that it:

> considers that the definition of live stock in section 995-1 of the *Income Tax Assessment Act 1997* includes all animals in a primary production business for the reason that the majority ruling of Dixon and Fullagar JJ in the High Court Decision of *Federal Commissioner of Taxation v Wade* (1951) 84 CLR 105 (Wade's Case) provides [that] 'The definition of trading stock brings "live stock" within s 36(1). There is a definition of livestock which, by inference, makes it clear that all animals are to be included case of a business of primary production. Notwithstanding, therefore, the taxpayer's claim that the destruction and replacement of 110 head of his dairy herd is a capital transaction it is clear enough that for the purposes of s 36(1) the cattle fall within the expression of "trading stock".'[9]

---

[3] Alexander Robert Fullarton and Dale Anthony Mark Pinto, 'Tax Accounting for Livestock: Mother or Meat/Capital or Revenue' (2021) 27(1) *New Zealand Journal of Taxation Law and Policy* 39; 'The *Wade Case*: An Analysis' (2021) 27(2) *New Zealand Journal of Taxation Law and Policy* 121.

[4] Ibid, 'Tax Accounting for Livestock' (n 3) 67.

[5] (1951) 84 CLR 105.

[6] Fullarton and Pinto, 'The *Wade Case*: An Analysis' (n 1).

[7] Fullarton and Pinto, 'Tax Accounting for Livestock' (n 3) 47.

[8] Alexander Fullarton and Dale Pinto 'The Foundations of the *Wade Case*' (n 3).

[9] Lendon (n 2).

Despite the fact that, intuitively, stud bulls, cows, rams and ewes as well as dairy cattle, mustering horses and dogs might be considered, and valued, as aids to manufacture rather than as trading stock held for the purposes of sale, the matter appears to have been unchallenged for over 70 years. It appears that retiring pastoralists, graziers and farmers have remitted income tax on the basis that the proceeds of the sale of their stock in conjunction with the sale of their properties is income according to ordinary concepts, or a trading profit rather than a capital gain. Consequently, the authors argue, these taxpayers have over-remitted tax on the basis of advice provided by their tax advisers, accountants and other professionals.

The authors investigated the reported decision in the Wade Case and concluded that:

> Based solely on the reported decision of the Wade Case, [the authors] found that sufficient doubt existed to suggest the Commissioner's view might not be reliably supported by the decision of the Wade Case. Instead, the reported decision supported the argument that some animals held in a business of primary production, such as horses and dogs used for mustering, stud stock used for breeding, or animals used for the production of animal products, such as milk or wool, are of a capital nature and should be treated accordingly for taxation purposes.[10]

Subsequently, the authors' research looked beyond the reported decision of the Wade Case[11] and found that hearings before the Commonwealth Taxation Board of Review and an earlier case heard by the High Court provide evidence and background that is not presented in the authorised case reports.[12] They suggest that the reasons given by Dixon and Fullagar JJ for their decision may have been taken out of context by the ATO. They note that:

> Dixon and Fullagar JJ accepted the concept that the cattle were to be considered trading stock, and therefore of a revenue nature, irrespective of the role that they played in the business. They also noted that Kitto J was reluctant to accept that principle, but focused instead on the concept of insurance recoveries and the costs of repairs to support his decision.
>
> Fullarton and Pinto also pointed to a number of relevant previous cases that were not considered by the High Court. Without supporting documentation other than the report published in the *Commonwealth Law Reports* it could not be concluded whether their Honours were aware of those cases, or whether they had been omitted from either the evidence or the reported decisions.[13]

Therefore, the authors argue that, while the ATO considers that the main decision of the High Court was focused on animals held in a business of primary production, and from this infers that all animals are held as trading stock regardless of their role in that business, the Wade Case was focused on the assessment of monies paid to a taxpayer in compensation for a loss. Wade had been compensated for the loss and replacement of his assets, and that is the primary matter

---

[10] Alexander Fullarton and Dale Pinto 'The Foundations of the *Wade Case*' (n 3).

[11] Alexander Fullarton and Dale Pinto 'The Foundations of the *Wade Case*' (n 3).

[12] *Wade v Commissioner of Taxation*, Commonwealth Taxation Board of Review No. 2. (1950) No M37/1950. Note: The matter is also reported as (1950) 1 CTBR (NS) Case 77, 335; and (1950) 1TBRD Case 72, 273: and in John Angus Lancaster Gunn and Richard Esmond O'Neill (eds), *Commonwealth Taxation Board of Review Decisions (New Series)* (Butterworth and Co, 1952) 1; (1 CTBR (NS)).

[13] Alexander Fullarton and Dale Pinto 'The Foundations of the *Wade Case*' (n 3). Cases considered by Fullarton and Pinto are contained in pages 134-7.

addressed by the court. That those assets happened to be dairy cows and not a milking shed or some other assets is not specifically relevant to the decision, but what was relevant was the assessment of the surplus funds of £130 left over from the compensation received by Wade and the cost of purchasing the replacement cows. The authors argue that the judges' comments as to the classification of the lost assets (dairy cows) are *obiter dictum* rather than central to the matter decided, and might not be regarded as legal precedent in subsequent cases.

The authors found that a 1927 case considered by the High Court concerning the classification of livestock had held that ewe weaners were not trading stock as they were held for the purposes of breeding, and that the proceeds of the sale of such ewe weaners were not assessable income.[14] That decision is in direct conflict with the inference that all animals held in a business of primary production are trading stock and not capital assets. Therefore, the authors conducted an investigation into why the 1927 decision in *Robinson v Federal Commissioner of Taxation* was different to the judges' supporting statements in the Wade Case of 1951.

It was found that s 17 of the *Income Tax Assessment Act 1922*, in force until 1936, expressly excluded livestock which, in the opinion of the Commissioner, Assistant Commissioner or Deputy Commissioner, were ordinarily used as beasts of burden or as working beasts or for breeding purposes. However, s 17 had been deliberately repealed, to bring all animals into the Live Stock Trading Schedule for assessment for income tax, on the recommendation of the Royal Commission on Taxation 1932-34.[15] Therefore, it is the repeal of that legislation which renders all animals held in a business of primary production trading stock, not the decision of the Wade Case. The ATO view may be correct, but it is based on the wrong reasons.

The authors point to that flaw in the ATO's published view to draw the attention of tax professionals and academics to the need to conduct diligent research in giving advice to taxpayers. It this case, it might be said that the ATO 'got lucky', but the advice clearly contains the caveat that it is not to be relied on, other than to indemnify taxpayers from penalties and interest if the advice is incorrect, and therefore the responsibility lies entirely on the giver of the advice and not the ATO. The authors further suggest that if this particular advice might be successfully challenged – the matter decided was the assessment of insurance recoveries and not the classification of animals – then, given the number of rulings, opinions and determinations issued by the ATO, there are almost certainly others that would fail under intense scrutiny and challenge. This highlights that a failure to carry out reasonable investigations may result in false beliefs and cause considerable fiscal damage to taxpayers. Failure to take note of the ATO's caveat could leave tax professionals liable to claims of negligence.

IV FINAL OBSERVATIONS

The authors make the following observations as to the conduct and findings of their research:

> The definition of livestock as trading stock, and therefore as products for sale rather than capital assets used as aids to manufacture, is a matter of legislation not case law.

[14] *Robinson v Federal Commissioner of Taxation* [1927] HCA 8; (1927) 39 CLR 297.
[15] *Royal Commission on Taxation* (Third Report, 12 April 1934) 135.

It is the operation and repeal of s 17 which determines the classification, not the decision in the Wade Case. If a challenge to the ATO view was to be determined on the evidence of the report in the Wade Case, reasonable evidence would need to be submitted to the court (such as accurate accounting and animal breeding records) to show that trading livestock were segregated from breeding livestock, and it would be argued that the Wade Case primarily considered the assessment of insurance and compensation monies as ordinary income. Taxpayers might then successfully argue that the proceeds of the sale of their breeding stock should be taxed according to the capital gains tax provisions and not as income according to ordinary concepts.

Section 17 was repealed on the recommendation of the Ferguson Royal Commission, but the reason given by the Royal Commission was not the same as that given to Parliament for the repeal. The Royal Commission report points to the difficulty in separating a sheep (a capital asset) from its wool (a revenue asset). The explanatory memorandum accompanying the Bill recommended the repeal of s 17 as a matter of simplicity.

Parliamentarians might instead have amended the Bill to add a sub-section to ensure that sheep were sold 'off-shears' (that is, s 17 would apply to shorn sheep but not to those 'in wool'). Taxpayers might then have been able to classify their animals as plant, providing they were shorn. That amendment would have addressed the Royal Commission's concern without removing s 17 entirely. The *Income Tax Assessment Act 1997* could be amended to clarify the matter addressed by the authors, and the argument that breeding stock should be considered as plant rather than as goods for sale could be settled. The findings of this research validate the current ATO view, but do not settle the core argument that retiring pastoralists, farmers and graziers are being deprived of capital gains tax concessions, to which other business proprietors are entitled, on the disposal of their businesses.

The interest in this point of tax law shown by the accounting profession has been rather low. Despite several approaches to members of the Institute of Public Accountants generally and individual approaches to rural and urban tax agents, only 110 respondents were willing to participate in this research. The matter was generally of little or no interest to urban practices, few of which have clients who might be impacted by the ATO view. The number of taxpayers in Western Australia engaged in disposing of pastoral properties averaged just ten per year over the past 20 years. No investigation was made as to farmers' views. The lack of volume of transactions might explain the general lack of awareness of and interest in this issue by taxation practitioners.

A key observation goes to the root of this research – had Wade's accountant been aware of the repeal of s 17 then he might have disclosed the disposal and purchase of replacement dairy cows in Wade's 1948 income tax return, instead of appending a note disclosing the transactions. Had the assessing clerk been aware of the repeal of s 17 then he might have advised Wade at the point of amendment and the reason. Had the Crown solicitor been aware of the repeal of s 17 then the fact might have been presented to the Commonwealth Taxation Review Board and Wade's appeal would have been dismissed.

Had Kitto J been advised of the repeal of s 17 then he may not have had:

> … some difficulty in accepting the view that the fact that dairy cattle, which are not trading stock according to ordinary concepts, are required [to be] by force of a definition to be taken into account under ss 28 and 32 of the *Income Tax Assessment Act* 1936-1947 (Cth) as trading stock.[16]

There are many historical reasons, not least the social and economic upheavals of The Great Depression and World War Two in the years between 1934 and 1948, which may have caused the repeal of s 17 and the impact on the application of income tax on primary producers. However, the key lesson from this research is that reliance on memory, or the opinions of others not qualified to conduct legal research and provide legal advice as to legislation, can lead to very expensive outcomes for the courts, administrators and taxpayers.

Perhaps all of those involved relied on what had been the legislation the last time they had had to address the matter – just after the Great Depression, and 'before the war'. Times and the legislation had changed but they did not know that. The authors suggest that it is hard to judge whether they ought to have known in 1951, but in 2022, those professionals and academics engaged in providing taxation law advice for remuneration are ethically and legally bound to ensure they have a sound knowledge of the legislation, and they should not rely on the opinions or views of others. That caveat certainly applies to advice or opinions given by the ATO, which points to doubt in relying on such advice or opinions.

The authors also note the opinion of McNab, who casts doubt on the value of private rulings as in a number of cases the Courts have failed to give effect to them. He suggests that events occurring after the ruling is issued, such as changes in corporate structure or legislation, can render the ruling superfluous. He further suggests that sometimes the cost of applying for a private ruling can outweigh the benefits to the taxpayer relying on the ruling.

However, he does also point to:

> The key benefit of such a ruling is found in s 357-60 [ITAA 1997] which states that "a ruling" "binds the Commissioner" in relation to "you". If it applies to you, and you rely on it by acting (or omitting to act) in accordance with it, the Commissioner is then unable to increase your tax liability in relation to the subject-matter of the ruling, or apply penalties and interest if there is a later disagreement. This certainty can be valuable.[17]

[16] Wade Case 114.
[17] Paul McNab 'Private Rulings: Are they worth it?' (2022) 57(1) *Taxation in Australia* 38,39.