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‘Backpacker tax’ offends Australia-UK double taxation treaty

Melita Parker reports on *Addy v Federal Commissioner of Taxation* (2021) 95 ALJR 911 [2021] HCA 34

The High Court has unanimously rejected a narrow interpretation of a non-discrimination clause in a bilateral tax treaty. In doing so it drew support from interpretive principles applicable to treaties and to OECD model commentaries. The decision suggests that non-discrimination clauses, at least in international agreements, may prohibit discrimination on the basis of a consequence flowing from the protected characteristic.

Background

Ms Addy is a British national. She arrived in Australia in August 2015 on a working holiday visa. Between August 2015 and May 2017, Ms Addy worked as a waiter in Sydney. She was an Australian resident for taxation purposes.

The new Pt III of Sch 7 to the *Income Tax Rates Act 1986* (Cth) (Rates Act) came into effect on 1 January 2017. It provided that a flat rate of tax of 15 per cent would be applied to the first $37,000 of an individual's 'working holiday taxable income'. At the same time, Pt I of Sch 7 to the Rates Act provided that an Australian national was entitled to a tax-free threshold of $18,200 and then a tax rate of 19 per cent for the first $37,000 earned.

On 20 December 2017, the commissioner of taxation issued Ms Addy with an amended notice of assessment for the 2017 income year which applied Pt III of Sch 7 to Ms Addy's assessable income after 1 January 2017. Ms Addy objected to the assessment, relevantly, on the ground that the application of Pt III of Sch 7 to her assessable income contravened Art 25(1) of the snappily titled *Convention between the Government of Australia and the Government of the United Kingdom of Great Britain and Northern Ireland for the Avoidance of Double Taxation and the Prevention of Fiscal Evasion with respect to Taxes on Income and on Capital Gains* (convention).

The convention

Art 25 of the convention provides:

> Nationals of a Contracting State shall not be subjected in the other Contracting State to any taxation or any requirement connected therewith, which is other or more burdensome than the taxation and connection requirements to which nationals of that other State in the same circumstances, in particular with respect to residence, are or may be subjected.

The convention was incorporated into Australian domestic law on 17 December 2003.

Proceedings

Ms Addy commenced proceedings in the Federal Court which allowed her appeal against the commissioner's decision. An appeal by the commissioner to the Full Court was allowed by majority. Ms Addy was granted special leave to appeal to the High Court.

The commissioner's argument in the High Court

The commissioner argued that a different rate was applied to Ms Addy because of her visa type, not her nationality (at [17]). Ms Addy was not in the 'same circumstances' as an Australian national because she was earning working holiday income which an Australian national could never earn (at [17]). As a consequence, the commissioner argued, Art 25(1) was not engaged.

The High Court's reasoning

In a single judgment of Kiefel CJ, Gageler, Gordon, Edelman and Gleeson JJ, the High Court allowed Ms Addy's appeal.

The court described the principles of interpretation which applied to tax treaties as 'well settled' (at [23]). While the text of the convention was the 'starting point' and has 'primacy in the interpretation process', it was 'mandatory' that the court consider the 'context, object and purpose' of the treaty, 'consistent with the general principle that international instruments should be interpreted in a more liberal manner than would be adopted if the court was required to construe exclusively domestic legislation' (at [23]).

The court started from the position that in cases alleging discrimination, the circumstances of the person alleged to have suffered discrimination and those which are related to the 'prohibited ground' are to be excluded from the circumstances of the comparator (at [30]). The 'prohibited ground' extended beyond Ms Addy's nationality to her visa status because that was a characteristic which 'depended on her nationality' (at [28]). The court later referred to the visa status as a 'consequence flowing from the protected characteristic' (at [31]). On this basis, the court rejected the commissioner's submission that there was no available comparator (at [30]).

The court noted that the convention was one of a number of international treaties that Australia has concluded based on the Model Tax Convention on Income and on Capital published by the OECD. The court stated that the commentaries prepared by the OECD to accompany the model conventions which were available at the time Australia and the United Kingdom made the convention could be used in interpreting Art 25 (at [32]). The court left open for another day whether commentaries prepared since the convention was made could be used in the interpretation but noted, in any event, that they were not inconsistent with the construction adopted (at [35]).

The court drew particular support from two aspects of the commentary. The first explained that the expression 'in the same circumstances' refers to 'taxpayers…placed from the point of view of the application of the ordinary taxation laws and regulations, in substantially similar circumstances both in law and fact' (at [32]). The second explained the effect of Art 25 as 'when a tax is imposed on nationals and foreigners in the same circumstances, it must be in the same form as regards both the basis of charge and the method of assessment, its rate must be the same…' (at [32]).

The court found that an Australian national deriving the same income from the same source as Ms Addy would be taxed at a lower rate in accordance with Pt 1 of Sch 7 (at [31]). The application of Sch 7, Pt III to Ms Addy was, as a result, a contravention of Art 25(1) of the convention. BN