



FEDERAL FISCAL RELATIONS AFTER *VANDERSTOCK*

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Outline of Victorian Legislation

- . Victorian Parliament sought to impose fee on the use of zero and low-emission vehicles (ZLEVs)
- . Imposed on registered proprietor in relation to use of vehicle on Victorian public roads
- . 2 or 2.5c per kilometre during financial year
- . It is a tax on an act of consumption (destruction by use, in the case of a non-food item)(Barwick CJ in *Dickenson's Arcade*)
- . It is a 'true' tax on consumption - ie on the act of consumption
- . People often refer to taxes like GST (ie a sales tax) as consumption taxes but strictly speaking they are not - because they are not imposed on an act of consumption
- . This tax was imposed on an act of consumption - based on the use of the vehicle
- . Extremely rare - partly because difficult to collect, relies on an individual's honesty
- . Taxes usually imposed at an earlier stage ie production, manufacture, distribution, sale

Outline of the Constitutional Challenge to the Legislation

- . Argued to be an excise and prohibited to the states - s90 Commonwealth *Constitution* prohibits states from levying customs and excise duties
- . High Court has interpreted the meaning of 'excise duty' for more than 120 years, many areas of disagreement and uncertainty
- . Little evidence in the Convention Debates regarding what Founding Fathers intended word to mean, not defined in the *Constitution*
- . In any event, importance of what Founding Fathers intended words or sections to mean in terms of constitutional interpretation today a matter of significant conjecture
- . Orthodox view is that answers to constitutional questions not found 'in attempting to attribute some collective subjective intention to all or any of those who participated in the Convention Debates' (*New South Wales v Commonwealth (WorkChoices Case)*(2006) 229 CLR 1, 97 (five members of the High Court))

Outline of the Constitutional Challenge to the Legislation

- . At first, High Court limited the meaning of excise to taxes on production or manufacture of goods (*Peterswald v Bartley*, 1903)
- . Based on reserved powers type reasoning, read down broad Commonwealth powers (and, by implication) read limitations on state power narrowly to preserve states' power - an approach rejected by the High Court in 1920 in the classic *Engineers'* decision
- . In *Commonwealth Oil Refineries* (1926) High Court extended definition of excise to taxes on distribution and sale, and two members indicated a consumption tax could be an excise
- . In *Matthews v Chicory Marketing Board* (1938) Dixon J stated a consumption tax could be an excise, referring to Sir William Blackstone's definition of excise which could include consumption taxes, Latham CJ similar
- . Privy Council decision on Canadian *Constitution* - some thought it meant a consumption tax could not be an excise, based on distinction direct/indirect taxation, which has no Australian equivalent
- . Dixon J altered his view, accepted consumption tax not an excise (*Parton v Milk Board*)(at the time, PC decisions binding)
- . Dixon J also stated s 90 designed to give Commonwealth real control over the taxation of commodities as an instrument of power over the economy

Outline of the Constitutional Challenge to the Legislation

- . High Court defined excise to exclude a consumption tax in *Bolton v Madsen* (1963)
- . *Dickenson's Arcade Pty Ltd v Tasmania* (1974) - four members of High Court said a consumption tax was not an excise, based on *Parton* and *Bolton*
- . Two of those expressly doubted correctness of it, but felt duty bound to accept previous case law
- . Barwick CJ (dissenting) no logical reason for confining excise duties to those imposed prior to consumption
- . Questioned whether PC had really found a consumption tax could not be an excise
- . High Court's approach to interpretation of s 90 evolving - during 1960s and 1970s, highly formalistic criterion of liability approach - open to easy subterfuge by clever drafting, 'backdating devices'
- . 1980s and since - practical approach preferred - whether in substance it is a tax on goods
- . In 1990s High Court accepted view of Dixon J in *Parton* - object of s 90 was to give Commonwealth real control over the taxation of commodities (*Capital Duplicators No2, Ha*)

Anomaly in the Law Prior to *Vanderstock*

- . Orthodoxy is that s 90 designed to give Commonwealth real control over taxation of commodities
- BUT Commonwealth had no control over taxes imposed on consumption of commodities
- . Orthodoxy is that s 90 concerned with substance rather than form
- BUT if states imposed taxes at consumption stage, rather than retail stage or earlier stage, could easily circumvent s90
- . Mismatch between accepted purpose of provision, and how it was being interpreted
- . States could impede implementation of Commonwealth economic policy, where taxation is a leading tool at Commonwealth's disposal ie to encourage or discourage particular economic activity
- . Commonwealth has no direct constitutional control over the economy yet most would agree Commonwealth has prime responsibility for management of Australian economy

Majority in *Vanderstock* - Anomaly Removed

- . No accepted meaning of excise at federation
- . Some early HC authority suggesting consumption tax could be an excise, Dixon J believed it - Australian law sidetracked by what it was believed PC decision required (at a time when High Court bound by PC decisions)
- . Re-confirmed (as had *Capital Duplicators No2* and *Ha*) that purpose of s 90 to give Commonwealth real control over the taxation of commodities
- . Majority accepted existing position anomalous - tax on consumption will increase cost of those goods to consumers and generally depress demand for them - 'intuitively obvious'
- . 2 questions in terms of s 90 validity (a) whether fee was a tax on goods - whether fee related to production, manufacture, distribution, sale or consumption of goods, and (b) whether tax affected goods as subjects of manufacture/production/articles of commerce - whether likely to reduce demand for the goods
- . ZLEV clearly a tax on goods based on use of vehicle - a consumption tax - invalid due to s 90 *Constitution*

Minority – Gordon, Edelman and Steward JJ

- Gordon J agreed no established view of excise as at federation
- . Disagreed that section designed to give Cth real control over taxation of commodities (ie rejects majority view in (at least) *Capital Duplicators No2* and *Ha*), orthodoxy since 1949's *Parton*
- . Cannot be assumed tax on consumption will depress demand for goods
- . Claimed majority's position would 'radically affect' states' ability to raise revenue: [401](?)
- . Existing VFI would worsen: 'it was about the Commonwealth policy having most of the power to tax and the power to decide how that money is spent, but the states knowing what spending is needed, when and how': [401](?)
- . Claims economic effects of tax imposed at consumption 'materially different' from those imposed at prior time
- . Accuses majority of 'amending' the *Constitution*: [204](?)

Edelman J and Steward J

- . Claimed his suggested restraints on s 90 were 'to support a functioning federation in which state spending powers are supported by states revenue raising powers': [453](had to be imposed directly on supply side of market, have an effect on market for the sale of goods actually taxed, not another market)
- . Claims his suggested restraints (limiting s 90 to exclude consumption taxes) were part of the 'settlement' in *Ha* and *Capital Duplicators (No2)*: [461]; Steward J referred to notions 'journey had ended' in *Ha*: [708]
- . As a result of majority decision, taxes that had never been thought to be excises such as payroll tax, industrial taxes, taxes on sale of a business could be excises: [451, 473, 480, 481, 672, 677]
- . Claimed majority decision involved 'neglect of constitutional structure, neglect of constitutional text, neglect of contemporary understanding, neglect of history, neglect of political choice, neglect of economics, neglect of principle, neglect of precedent, neglect of authority, and neglect of future': [613]
- . Believes there was a view of the meaning of excise at the time of federation (quoting one founding father and an Accounts Committee from Victoria at the time): [630]; Steward J agrees - it was *Peterswald* view (1904)
- . Steward J disagrees purpose of s90 to give Cth control over taxation of commodities, refers to 'pursuit of absolute federal control' as more of an issue than erosion of economic union caused by excluding cons taxes from s90: [801]

Reflections on the Decision

- . purpose of s 90 to give Cth real control over taxation of commodities - accepted since 1949, re-affirmed by HC *Capital Duplicators No 2* and *Ha* - dissenting justices still refuse to accept; logic of this is s 90 must extend to consumption taxes
- . Claims that *Ha* reflected a 'settlement' or 'end of journey' (court in *Ha* expressly left open whether a consumption tax was an excise or not), dissenters did not accept majority position in *Ha* regarding purpose of s 90 - 'settlement'(?)
- . Clearly a consumption tax affects the overall price of goods to the consumer
- . Claims amount is too small to change behaviour AND fears for the future if this state tax is invalidated - consistency?
- . Founding Fathers - *New South Wales v Commonwealth* (2006) 229 CLR 1, 97: 'to pursue the identification of ... the framers' intention, much more often than not, is to pursue a mirage ... the answer to (whether a measure is constitutional or not) is NOT to be found in attempting to attribute some collective subjective intention to all or any of those who participated in the Convention Debates' (five justices)(emphasis added); cf Craven 'Original Intent and the Australian Constitution - Coming Soon to a Court Near You?' (1990) 1 *PLR* 166; (1992)18 *MULR* 874, 894: 'in the interpretation of the Australian Constitution ... the search for the intentions of those who framed the document is paramount'
- . Use of concept of 'directness' discredited in other areas of constitutional law (eg s 92 *Cole v Whitfield* (1988) 165 CLR 360 rejecting the direct/indirect distinction as 'unsatisfactory' (401)(all members of the Court) and not helpful here - because it lends itself to easy evasion; Barry Gordon 'What is an Excise Duty? Nineteenth Century Literature and the Australian Constitution' (1989) 11(1) *History of Economics Review* 22, 31: 'by the 1890s informed students of public finance were well aware of the ambiguities surrounding the terms 'direct' and 'indirect'. Their writings suggested ... that the inclusion of such terms in the constitution ... was not ... recommended'.

The World Has Changed Since our *Constitution* Was Drafted but our Written *Constitution* (Largely) Has Not

- . 'growth of national identity results in corresponding growth in the area of activities which have an Australian rather than a local flavour. Thus, the complexity and values of a modern national society result in a need for co-ordination and integration of ways and means of planning for that complexity and reflecting those values. Inquiries on a national scale are necessary and likewise planning on a national scale must be carried out. Moreover, the complexities of society, with its various inter-related needs, requires co-ordination of services designed to meet those needs' (*Victoria v Cth and Hayden* (1975) 134 CLR 338, 412 (Jacobs J)).
- . 'that the Cth would, as time went on, enter progressively, directly or indirectly, into fields that had formerly been occupied by the states was from an early date seen as likely to occur' (*Victoria v Commonwealth* (1971) 122 CLR 353, 396 (Windeyer J))
- . Sir Anthony Mason notes the founding fathers intended to give new Cth Parlt all powers necessary to conduct affairs of nation, *Constitution* intended to enshrine flexible mix federal/state power and not to set a certain view of federalism that existed in 1890s: 'words of the *Constitution* have to be applied to conditions and circumstances that could not have been foreseen by its authors ... the meaning of the language of the *Constitution* at the time of its adoption and of the intentions of the authors have a limited value in resolving current issues': *The Mason Papers* (Federation Press, 2007) 134-135
- . 'the world has changed considerably since federation in 1901. Issues that were once clearly the responsibility of the states have taken on a more national character ... as the world globalises, barriers to the free movement of people, goods and services become increasingly anachronistic': Business Council of Australia *Reshaping Australia's Federation* (2006)

The World Has Changed

- . *Constitution* drafted in the 1890s - colonies were isolated, business generally local, little concept of a national economy, believed role of national government would be relatively limited, environment not important
- . Today Australia is a tightly integrated nation - ease of travel and communication around Australia, businesses generally national/international, concept of a national economy, greater demands for co-ordination, concept of Australian citizenship, realisation that most issues have a national/international character, globalisation and internet
- Eg aged care sector, NDIS - little sense in having different rules in different states
- . Education, health - questionable sense in having different curricula
- . National business understandably seek national company law, national industrial relations, national OHS, national recognition of qualifications, national discrimination laws, national payroll tax, workers' compensation - has occurred in first two examples
- . eight changes to the express terms of our *Constitution* since federation, most minor in scope, very difficult to formally amend
- . James Buchanan spoke of the challenges of the 'progressive national integration of the economic system within a decentralised political structure' (speaking of the United States): 'Federalism and Fiscal Equity' (1950) *American Economic Review* 583, 585

How Does Australia's Governance 'Work' Given the World Has Changed So Much But Text of our *Constitution* Largely Has Not

- . *Constitution* sets out areas of legislative responsibility of Cth, rest to States
- . Much more demand for uniform regulation than at federation eg health, education, business, transport, communication
- . Commonwealth raises the three biggest taxes by revenue (income tax, corporate tax, GST) - states voluntarily gave up levying income tax
- . States reliant on range of taxes, including payroll tax, land tax, stamp duty, mining royalties, gambling taxes, liquor and tobacco - mostly inefficient
- . Australia's federation characterised by high level of vertical fiscal imbalance (VFI) - serious mismatch between level of government raising revenue and level of government spending the money - Cth raises about 80% revenue, spends about 60%
- . Not ideal in terms of accountability and transparency
- . Federal Government provides significant financial grants to states each year (\$170 billion in 2022-2023: *Federal Fiscal Relations* (Federal Budget Paper No 3, 2022), about half of total state revenue
- . As a result, federal government indirectly controls policy areas in which they have no direct constitutional power (school education, higher education, health, aged care, disability, environment)
- . Commonwealth's spending power has provided the necessary 'fluidity' to allow the federation to 'work' for today, to respond to legitimate calls for a national approach to an issue, though the *Constitution* does not expressly support it (Cf *Pape* decision)

Wallace Oates *Fiscal Federalism* (1972)

- Classically three main functions of government
- . *Stabilisation function* - economic growth, low unemployment, price stability - consensus is federal government must control this in a federation
- . *Distribution function* - concern for relatively equal distribution of wealth, structure of taxation, social safety net, spending on public goods such as health, education, housing - consensus is federal government better placed to do so, attempts by sub-national governments to do so met by attempts to evade
- . *Allocation function* - government decisions regarding allocation of resources to their most efficient use, including provision of public goods, including where there is market failure - no general consensus as to which level of government, or what proportions between different levels is ideal
- This model supports federal government having broad power over taxation.
- . 'strongly arguable that the Commonwealth cannot discharge its responsibility for (inflation, wages policy, credit policy, money supply and the redistribution of income) unless it is conceded control over commodity taxation' (Peter Hanks 'Section 90 of the Commonwealth *Constitution*: Fiscal Federalism or Economic Unity' (1986) 10 *Adelaide LR* 365, 383

Costs of Federalism in Australia

- . \$9 billion per year: Access Economics 'The Costs of Federalism', Appendix 2 to *Reshaping Australia's Federation: A New Contract for Federal-State Relations* (Business Council of Australia, 2006)(only personal cost to households, not including business)
- . Quotes CEO of large corporation that they are crippled in growth by excessive business regulation associated with myriad of state laws (growth of business 15% per year, with simple, consistent regulation 30% per year), regulation compliance costs them nearly 1% of their yearly revenue, without excess regulation would have between \$24-30 million pa more for further investment, would pay \$8-\$10 million pa more in tax to govt): *Reshaping Australia's Federation* (2006)
- . Access Economics estimated cost of inefficiencies associated with state taxes in Australia at \$4 billion per year
- . Cost of federation \$20 billion per year according to another: M L Drummond 'Costing Constitutional Change: Estimating the Costs of Five Variations on Australia's Federal System' (2002) *Australian Journal of Public Administration* 43
- . Impedes movement of labour around Australia through licensing systems that don't always work well together (Gray 'State-Based Business Licensing in Australia: The Constitution, Economics and International Perspectives' (2009) 14(2) *DLR* 165)
- . States impose taxes like payroll tax and stamp duty considered to be among the most inefficient: Robert Albon 'The Efficiency of State Taxes' (1997) 30 *Australian Economic Review* 405
- . Department of PM and Cabinet *Reform of the Federation Green Paper 2015*: 'the Commonwealth can collect most taxes at a lower administrative cost and compliance costs and red tape are lowered for businesses operating in multiple jurisdictions as they only have to deal with one set of uniform rules'

Wish List

- . A new Australian *Constitution* suitable for the current age - setting out which level of government is responsible for particular areas of policy, where Commonwealth and States will work together
- . Expected areas of Cth responsibility broader than 1900, reflecting growth of national identity, realisation most issues are common across the federation, efficiencies associated with national not sub-national regulation - ie aged care, health, education, commerce, climate change policy, economic management - better alignment between level of government raising \$ and spending it, state differences exaggerated
- . Commonwealth to retain control over income, corporate and GST type taxation; make corp tax competitive worldwide
- . Less reliance on income taxes, more reliance on GST-type taxes (with appropriate compensation)(argument regarding the extent to which these are regressive) - will increase the supply of labour, increase investment, Australia's GST tax take low by OECD standards, these taxes relatively efficient: Freebairn 'A Better and Larger GST?' (2011) *ELRR* 85, 86; *Australia's Future Tax System* (2010)(Henry Review)
- . Removal of inefficient state taxes such as payroll tax - penalising businesses taking on workers, removal of stamp duty - inhibitor to goods moving from less efficient to more efficient uses - inefficient tax, more reliance on land tax (less easy to avoid), death duties (?), super profits tax (?) - potentially administered federally, \$ to states
- . Serious conversation about the size of government and that people have a realistic idea of the role of government

Conclusion

- . Second Reading Speech introducing the Bill to create the High Court (Alfred Deakin, 1902):
- 'Our written *Constitution*, large and elastic as it is, is necessarily limited by the ideas and circumstances which obtained in the year 1900 ... (formal amendment) is a comparatively costly and difficult task and one which will be attempted only in grave emergencies. In the meantime, the statute stands and will stand on the statute book just as in the hour in which it was assented to. But the nation lives, grows, and expands. Its circumstances change, its needs alter, and its problems present themselves with new faces.
- The organ of the national life which (while) preserving the union is yet able from time to time to transfuse into it the fresh blood of the living present is the Judiciary, the High Court of Australia ... it is one of the organs of government which enables the *Constitution* to grow and be adapted to the changeful necessities and circumstances of generation after generation that the High Court operates'
- . The founding fathers themselves never intended to lock the *Constitution* into a fixed meaning, including a fixed view of federalism, as at 1900. They entrusted the High Court with the delicate task of adapting its provisions to a new era. This was the genius of the founding fathers - creating a document to endure but also to 'breathe'.

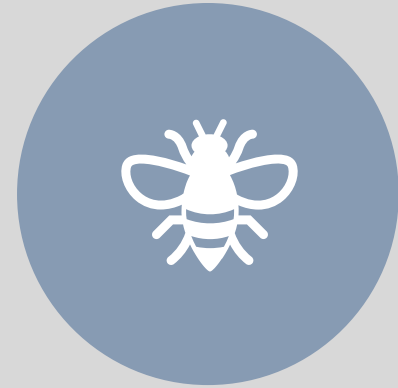
Title Lorem Ipsum



LOREM IPSUM
DOLOR SIT AMET.



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