STATE TAXATION: UNREQUITED REVENUE AND THE SHADOW OF SECTION 90

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INTRODUCTION

This paper asks whether much State taxation is currently avoiding proper constitutional scrutiny, including the issue of its compliance with s 90 of the Commonwealth Constitution. That provision gives sole power to the Commonwealth to levy duties of customs and excise. The second part of the paper argues that the current interpretation of s 90 is in any event not capable of a sensible application to State laws.

It is well known that the States and Territories face formidable restrictions on their powers to raise revenue through taxes. Some of these restrictions are pragmatic and political in nature: the Commonwealth successfully ejected the States from the field of income tax in 1942.[1] Other restrictions flow from provisions of the Commonwealth Constitution such as s 90. Nevertheless, the States manage to raise substantial sums of money, relying on the Commonwealth for only about half their revenues.[2]

Around a quarter of State revenues come from standard State taxes in the form of stamp duty, pay-roll tax, business franchise licence fees, land taxes, financial institutions duties and debits taxes, gambling taxes, vehicle registration fees, driver's licences and other similar imposts.[3] Nearly as much again is raised from other substantial sources of State revenue. Many millions of dollars are collected annually in the form of royalties for mining and timber, contributions by government instrumentalities (water, gas, electricity), departmental fees and charges, fines and penalties, and interest payments.[4]

These latter type of receipts are not normally described as taxes. This means they regularly escape legal analysis as taxes. But it does not necessarily mean that they are not in fact taxes. This paper argues that a significant proportion of State revenue,

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1 See the *First* and *Second Uniform Tax Cases* (1942) 65 CLR 373 and (1957) 99 CLR 575.

2 For example, in Western Australia, recurrent revenue for 1992-93 was $4,982,907,000 of which only $2,220,703,000 came from the Commonwealth: Western Australia, *1993-94 Budget Paper No 2, Consolidated Fund Estimates* (1993) at 7.

3 $1,542,716,000 was raised in Western Australia from such taxes and licences in 1992-93. Western Australia, above n 2.

4 $1,219,488,000 was raised from such sources in Western Australia in 1992-93. Western Australia, above n 2.

currently classified as administrative charges and fees, may in fact be taxation revenue according to proper legal analysis. The failure to recognise this may mean that much of this revenue escapes the scrutiny appropriate to taxation from a constitutional and public finance perspective. The legal definition of tax is very broad. As we shall see, it is enough that the payment in question is compulsory, imposed by the state, and is neither requited nor a penalty for breach of law.

State fees and charges which escape recognition as taxes may as a consequence fail to meet some of the formal requirements for the exercise of taxation powers under State constitutions. For example, laws imposing taxation should deal only with taxation,[5] taxes should be paid into consolidated revenue,[6] they cannot be imposed without parliamentary sanction[7] and where they are set under delegated authority they must be appropriate to the legislative purpose for which the delegation has been made.[8]

But more fundamentally, if State fees and charges go unrecognised as taxes, there is a danger that they may actually breach s 90 of the Commonwealth Constitution, with the consequence that constitutionally the States may have no power to impose them. Section 90 prevents States (and Territories[9]) from levying duties of customs and excise. This provision has grown in significance over the years as the result of the increasingly broad interpretations of the word excise adopted by the High Court. The meaning of excise has recently received another coat of paint from the High Court in *Capital Duplicators Pty Ltd v ACT [No 2]*.[10]

In that case, three of the seven judges argued for a return to an interpretation of excise which would see it limited to taxes on the production of goods. The majority, in what may prove to have been a last ditch effort, clung to the current definition of excise which extends it to include taxes on the distribution of goods. But the most worrying aspect of the majority's decision, apart from its practical effect on State financial powers, is the dubious and ambiguous link which they appear to draw between the purpose of taxation legislation, its economic effect, and its constitutionality under s 90. The second part of this paper argues that this approach to the interpretation of excise is without promise, whereas the approach of the minority judges might be more appropriate from a legal perspective and from the point of view of the States in their quest for more adequate revenue raising powers.

UNRECOGNISED STATE TAXES

No matter what State (or local) governments may choose to call them, compulsory payments which they levy from us are taxes, unless they are requited by services or are

5 See, for example, s 46(7) of the Constitution Acts Amendment Act 1899 (WA). While s 46(9) protects the validity of laws which do not conform with that requirement, it would nevertheless be inappropriate for Parliament to flout it.

6 See, for example, s 63 of the Constitution Act 1889 (WA) and compare that provision with the High Court's interpretation of s 81 of the Commonwealth Constitution in *Australian Tape Manufacturers Association v Commonwealth* (1993) 112 ALR 53.

7 *Australian Tape Manufacturers Association v Commonwealth* (1993) 112 ALR 53 at 62.

8 *Marsh v Shire of Serpentine-Jarrahdale* (1966) 120 CLR 572.

9 *Capital Duplicators Pty Ltd v ACT [No 1]* (1992) 177 CLR 248.

10 (1993) 178 CLR 561.

imposed as penalties for breach of law. Such is the definition of taxation that emerges from the case law.

Compulsory

Firstly, a tax is a compulsory payment. This is a view shared by lawyers and economists. A leading public finance text states that "[t]axes are compulsory imposts, whereas charges ... involve voluntary transactions."[11] Latham C J, in a much quoted passage of his judgment in *Matthews v Chicory Marketing Board (Vic)*,[12] noted that a tax was "a compulsory exaction of money ... enforceable by law."[13]

A payment does not become voluntary (and therefore a charge rather than a tax) merely because it can be avoided by refraining from a particular activity or transaction. A fee for a dog licence is no less a tax merely because it can be avoided by "choosing" not to own a dog.[14] Federal sales tax[15] is no less a tax because it can be avoided by "choosing" not to purchase goods on which it is imposed.

Such imposts are compulsory in the sense that persons coming within a prescribed class (for example, land holders for land tax), or engaging in prescribed activities (for example, earning income, purchasing dutiable goods), must pay the tax imposed. It is not to the point that they come within such a class as a result of an exercise of free will. Once the person concerned has chosen to engage in a particular transaction or activity, he or she is liable to the payment which constitutes the tax.

A payment is voluntary when the person paying it makes a conscious choice to engage in the activity of making the payment itself. A woman may make a voluntary choice to acquire a dog; but by doing so she may become liable to a compulsory licence fee. The acquisition of the dog is voluntary, the liability for the fee itself is not. Voluntary payments usually only occur because the person making the payment receives something in return for it; that is, because the payment is requited.

Requited

The Organisation for Economic Cooperation and Development (OECD) defines taxes as "compulsory, unrequited payments to general government".[16] A payment is requited where it directly secures some advantage; for example, when it secures goods or services or access to particular resources. It does not affect the character of a payment as a tax that the person making the payment has access to general government services funded by tax revenue. There must be a direct relationship between the procurement of the services or assets, and the making of the payment. There should, for example, be a direct correspondence between the size of the payment and the share of the services or assets so secured. Thus the OECD treats a poll tax or community charge which is levied

11 R Musgrave and P Musgrave, *Public Finance in Theory and Practice* (5th ed 1989) at 212.

12 (1938) 60 CLR 263 at 276.

13 Note that in *Air Caledonie International v Commonwealth* (1988) 165 CLR 462 at 467, the High Court held that "there is no reason in principle why a tax should not take a form other than the exaction of money."

14 See generally *Ryan v Clayton* (1920) 20 SR (NSW) 524.

15 Sales Tax Assessment Act 1992 (Cth).

16 OECD, *The Revenue Statistics of OECD Member Countries 1965-87* (1988) cited in M Wilkinson, *Taxation* (1992) at 2.

to fund local services as a tax. Such payments are not requited by the provision of the services in question unless the charge is "in proportion to [the] services rendered."[17]

The legal definition of taxation also recognises that a payment is not a tax to the extent that it is requited.[18] Thus royalties paid to State governments for the extraction of minerals and timber are not taxes.[19] This is because they provide the royalty payer with access to particular material resources. The unrequited nature of taxation is reflected in s 53 of the Commonwealth Constitution, which provides that a law shall not be considered to impose taxation by reason only that it contains provisions for the charging of licence fees or of fees for services.[20] As early as 1938 in *Matthews v Chicory Marketing Board (Vic)*,[21] Latham CJ excluded "a payment for services rendered" from his description of payments in the nature of tax.[22]

A licence fee will not be a tax where it merely covers the actual cost of administrative services rendered to the licence holder in issuing the licence. (Note that we are not here concerned with the general notion that government is entitled to recoup its costs. The emphasis is rather on the fact that those costs represent the value of the service actually provided to the fee-payer.) In *The General Practitioners Society in Australia v Commonwealth*,[23] a $10 fee charged for the processing by the Minister of an application was considered to be within the bounds of a reasonable fee for that service. However, the High Court acknowledged that if a fee which purported to be charged for that service was out of proportion with the costs involved, so as to be unreasonably large, it would in fact be a tax.[24]

A payment is not requited merely because it secures a licence which permits the holder to engage in some activity proscribed for non-licence holders. A fee for a dog licence, if it is set at a rate greater than that necessary to meet the costs of administering the licensing scheme, is no less a tax because it allows the holder to avoid prosecution for owning a dog. The dog licence does not secure for the holder a right to own a dog. The dog must still be purchased from someone willing to sell it. Ownership passes to the buyer on sale. The only direct benefit which the licensing scheme provides to licence holders is the provision to them of the administrative services engaged in issuing the licence, but that accounts for only a portion of the fee. The remainder of the fee provides them with nothing that they would not have enjoyed in the absence of the licensing scheme. It is true that such a licensing scheme may well provide added benefits to the community at large, (in terms of the control of dogs) and thus to licence holders as members of that community. But these benefits do not constitute direct consideration to the person paying the licence fee.

Harper v Minister for Sea Fisheries[25] involved licence fees for abalone divers working in Tasmanian waters. The licence fee was calculated in accordance with the quota of

17 Ibid at 2-3.
18 See generally *China Navigation Co Ltd v Attorney General* [1932] 2 KB 197.
19 *Harper v Minister for Sea Fisheries* (1989) 168 CLR 314 at 333.
20 There is a similar provision in s 46(1) of the Constitution Acts Amendment Act 1899 (WA).
21 (1938) 60 CLR 263.
22 Ibid at 276.
23 (1980) 145 CLR 532.
24 Ibid at 562 per Gibbs J, and at 568 and, especially, at 571 per Aickin J.
25 (1989) 168 CLR 314.

abalone permitted under the licence. It was held that the fee was not a tax. Brennan J pointed out that such a fee:

> may be distinguished from a fee exacted for a licence merely to do some act which is otherwise prohibited (for example, a fee for a licence to sell liquor) where there is no resource to which a right of access is obtained by payment of the fee.[26]

The High Court held that the licence fee in *Harper* was requited because it directly secured a right of access to a limited resource, and the degree of access acquired was directly proportional to the size of the licence fee.

Where the size of a licence fee bears no relationship to the value of material rights acquired under it, it is likely that it will be, or will contain, a tax. This will be true where the size of the fee appears to be independent of the value of the rights acquired; for example, where different rights are acquired by licence holders all paying the one level of fee. It will also be true where the size of the fee exceeds the value of the rights secured.[27] This might occur in a scheme of taxation designed to discourage the use of certain assets by pricing them out of the market. For example if a royalty were deliberately set so high that it precluded profitable extraction, this might well convert it into a tax.

The High Court in *Air Caledonie International v Commonwealth* stated that if an impost "has no discernible relationship with the value of what is acquired, the circumstances may be such that the exaction is, at least to the extent that it exceeds that value, properly to be seen as a tax."[28] This passage was quoted by three of the judges in *Harper v Minister for Sea Fisheries*, who went on to say that:

> This may be so notwithstanding that the exaction is one means of ensuring the conservation of a natural resource ... [W]hat is otherwise a tax is not converted into something else merely because it serves the purpose of conserving a natural public resource.[29]

The passage from *Air Caledonie International* raises the interesting issue of whether profits made by State instrumentalities which enjoy a monopoly are likely to be taxes. In such monopoly situations, the consumer of an instrumentality's services has no choice in regard to any component of the price which may represent a margin earmarked for consolidated revenue as opposed to the cost or value of the service provided. Such a situation might occur, for example, where instrumentalities are given responsibility not just for providing the service in question, but for contributing to the repayment of State debts or for bolstering revenue available for other government purposes.

Penalties

In *Air Caledonie International v Commonwealth* the High Court said that a payment will not be a tax where it represented a "fine or penalty imposed for criminal conduct or breach of statutory obligation."[30] Section 53 of the Commonwealth Constitution also

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26 Ibid at 335.

27 "[A]n exaction may be so large that it could not reasonably be regarded as a fee": *General Practitioners Society v Commonwealth* (1980) 145 CLR 532 at 562 per Gibbs J.

28 *Air Caledonie International v Commonwealth* (1988) 165 CLR 462 at 467.

29 (1989) 168 CLR 314 at 337 per Dawson, Toohey and McHugh JJ.

30 (1988) 165 CLR 462 at 467.

states that a payment will not (in the absence of something more) be a tax where it is in the nature of a fine or penalty.[31]

While this exception to the legal definition of taxation is not in doubt, it does provide a curious paradox. A licence fee is not rescued from characterisation as a tax merely because it enables the holder to avoid prosecution for not having a licence. However, the penalty imposed on someone for not having such a licence does escape such characterisation.

Fines share the characteristics of taxes. It would be difficult, for example, to sustain an argument that they are requited payments. Some fines (say, for certain traffic offences) even have a distinct revenue-raising flavour about them. The distinction appears merely to be that fines are levied on proscribed activities, whereas taxes are levied on prescribed ones. For example, would State legislation, under which the penalty for the sale of cannabis was limited to a fine per ounce sold, escape characterisation as an excise (that is, a tax on any point in the production or distribution of goods before consumption)? The answer would probably be that its characterisation as a criminal law would depend on a court accepting that Parliament was not intending that the sales in question were to be condoned.

Imposed by the State

We have seen[32] that the OECD considers that taxes are "payments to general government." Latham CJ included in his description of a tax referred to above the phrase "a compulsory exaction of money by a public authority for public purposes."[33] However, it does not detract from a levy's character as a tax for "public purposes" that it is earmarked for application to specific purposes or persons.[34]

One way of expressing this is to say that an exaction can be a tax "notwithstanding that it was ... for purposes which could not properly be described as public". This was the approach adopted by the High Court in *Air Caledonie International v Commonwealth*.[35] This approach seems to equate public purpose with general public purpose rather than allowing it to comprehend specific purposes, which in turn leads to the conclusion that such a public purpose is not the only acceptable revenue target of a tax.

Perhaps a better approach is that adopted by the High Court in *Australian Tape Manufacturers Association v Commonwealth*.[36] Any purpose designated by the state as a fit target for government revenue is deemed to be a public purpose.[37] As a result, it is not necessary to demonstrate that a Parliament's purpose is characterisable as a public one.

In order for an exaction to be imposed *by* the state, it is not essential that it to be paid *to* the state. In *Australian Tape Manufacturers*[38] a charge was levied on the sale of blank tapes for direct payment to a corporation representing the copyright holders of

31 See also s 46(1) of the Constitution Acts Amendment Act 1899 (WA).
32 Above at 478.
33 *Matthews v Chicory Marketing Board (Vic)* (1938) 60 CLR 263 at 276.
34 However such earmarking may itself be improper: see below n 43.
35 (1988) 165 CLR 462 at 467.
36 (1993) 112 ALR 53.
37 Ibid at 62.
38 (1993) 112 ALJR 53.

works vulnerable to domestic copying. The moneys were paid directly to a corporation. This did not stop the High Court ruling that the charge was a tax.

In *Air Caledonie International v Commonwealth*,[39] the High Court stated that an exaction could be a tax notwithstanding that it was collected by a non-public authority.[40] Again, an alternative way of expressing this is to say that all bodies authorised to collect moneys by the state do so as quasi-public authorities.[41]

It seems that authorisation by the state, that is, state compulsion under law, is sufficient nexus with the state to characterise a levy as a tax.[42] It is true that for constitutional reasons moneys so collected *should* be paid first into consolidated revenue. But failure to do so does not rob the exaction of the character of a tax.[43]

Delegated taxes

The characteristics that mark a fee or charge as a tax apply equally to those collected under delegated authority. It is precisely in the area of such delegation that the taxation character of a fee or charge is most likely to escape notice. There is no doubt that a State Parliament has the power to delegate the setting of tax rates to Ministers, departments and local government authorities.[44] Similarly, it can delegate a non-tax power, such as a power to set charges for licence fees or registration. If the legislation delegating the latter powers refers only to the need to set fees for a particular service or to the need to regulate a particular activity, then any charge which is designed to generate additional revenue will in fact be a tax and be beyond the power of the delegation.

In *Marsh v Shire of Serpentine-Jarrahdale*,[45] the High Court considered a power delegated to Shire Boards under the Road Districts Act 1919 (WA). This Act gave the Boards power to issue and charge for licences with a view to regulating quarrying. But the by-law in question imposed a charge fixed by the area of land to be quarried by the licence-holder. Such a formula would, if applied, have reaped fees well in excess of the costs of the licensing scheme. The High Court held the by-law was *ultra vires*. It held that power delegated to the Boards was limited to the raising of such funds as were necessary to institute the authorised regulatory scheme. Barwick CJ considered that:

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39 (1988) 165 CLR 462.

40 Ibid at 467.

41 *Australian Tape Manufacturers Association v Commonwealth* (1993) 112 ALR 53 at 59.

42 In this respect, *Air Caledonie International* and *Australian Tape Manufacturers* appear to have greatly widened the definition of taxation from that used in *Vacuum Oil Co Pty Ltd v Queensland* (1934) 51 CLR 108. The latter case concerned a statute which compelled the purchase of power alcohol by the suppliers of petrol in proportion to the quantity of petrol they sold. The Court had no doubt that the net effect, and purpose, of the legislation was to levy suppliers of petrol as a way of funding the encouragement of power alcohol production. But the Court held that the liability imposed on petrol suppliers escaped characterisation as a tax because "[i]t is not a liability to the State, or to any public authority, or to any definite body or person authorised by law to demand or receive it" (at 125 per Dixon J; see also at 142 per McTiernan J and at 118-119 per Rich J).

43 See s 81 of the Commonwealth Constitution and the discussion of the effect of a breach of that provision in *Australian Tape Manufacturers Association v Commonwealth* (1993) 112 ALR 53 at 63. At the State level compare with the Constitution Act 1889 (WA) ss 63, 64 and 72 and see R D Lumb, *The Constitution of the Australian States* (5th ed 1991) at 69.

44 *Cobb & Co Ltd v Kropp* [1967] 1 AC 141.

45 (1966) 120 CLR 572.

> to require the payment of a sum of money rated to the volume of material capable of extraction is not, in my opinion, in furtherance of any purpose or policy discoverable in the Act nor is it a contemplated method of regulating or controlling the activity of quarrying in the public interest.[46]

Western Australian meat marketing scheme

The potential for dispute over the taxation nature of a whole range of State government schemes imposing levies and fees is demonstrated by litigation that arose in Western Australia in 1993 over the then Lamb Marketing Scheme.[47]

According to the plaintiffs, the scheme operated as follows. Domestic wholesalers were compelled to sell lambs to the Meat Marketing Corporation immediately before slaughter at a "producer price" and then to repurchase them immediately after slaughter at a higher "distributor price". The difference between those two prices (around 90 cents per kilo) was then used by the Corporation, not only to finance the administration of the scheme, but to fund a price equalisation subsidy. This allowed the "producer price" to be paid to growers who sold lamb directly to the Corporation, regardless of the fact that much of that lamb was destined for sale in the less lucrative export market. The Corporation had sole control over export sales. This meant that growers whose lamb was unable to find a place in the domestic market nevertheless received the same return as those whose lamb did. It might also have operated to reduce the incentive growers would otherwise have had to compete for entry into the domestic market, thereby keeping domestic retail prices artificially high.

The scheme as described by the plaintiffs was not detailed in the Meat Marketing Act 1971 (WA) or its Regulations. The plaintiffs, who were being prosecuted for their refusal to comply with the scheme, argued that it involved the imposition of a tax beyond any delegated power. They asserted that the levy was compulsory because it could not be avoided by those slaughtering lamb for sale domestically since sale to and re-purchase from the Corporation were mandatory. The levy was not requited: no benefit under the scheme accrued to such first-wholesale-purchasers-after-slaughter as a *quid pro quo* for their payment of the levy (whatever benefits might flow to growers). The funds were used for a public purpose (albeit an unconstitutional one), namely the paying of a bounty to domestic producers whose stock in fact ended up being exported. It followed that the levy was therefore a tax, the imposition of which would have required a specific delegation of authority under the Meat Marketing Act 1971 (WA).

In addition, the plaintiffs argued that this was a tax that the Western Australian Government could not in any event impose. It was their contention that the tax in question was an excise (and the resultant subsidy to exporters a bounty) contrary to s 90 of the Commonwealth Constitution. In the event, the case was settled out of court in late 1993 when the Western Australian Government announced that the Meat Marketing Act 1971 (WA) was to be substantially amended. Now is the appropriate time to consider recent developments in the interpretation of s 90 and to speculate about the effect on State fees and charges.

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46 Ibid at 580.

47 *Wynne's Pty Ltd and Others v Western Australian Meat Marketing Corporation*, Supreme Court Matter No 1032 of 1993. The matter originated in the High Court and was referred to the Supreme Court of Western Australia for resolution of a dispute as to fact.

SECTION 90

In *Capital Duplicators Pty Ltd v Australian Capital Territory [No 2]*,[48] the High Court decided by a majority of four to three to retain the current broad definition of excise. This treats an excise as "a tax in respect of goods at any step in the production or distribution to the point of consumption."[49] The minority judges (Dawson, Gaudron and Toohey JJ) favoured a return to the narrower interpretation originally adopted by the High Court.[50] That interpretation applied the term excise to taxes on production, but not to taxes on the distribution of goods.

The contest between the narrow and the broad view of s 90 is fascinating and far from finished. At its core is a debate about centralism. The narrow view of s 90 holds (on the basis of considerable, though not compelling, historical evidence[51]) that it was intended merely to secure for the Commonwealth effective control over customs duties. The broad view of s 90 holds (in the absence of supporting historical evidence) that "it may be assumed" that it was intended rather to secure for the Commonwealth "a real control of the taxation of commodities."[52]

In confirming their support for the broad definition of excise in *Capital Duplicators [No 2]*, the majority (Mason CJ, Brennan, Deane and McHugh JJ) made much of the isolated nature of recent judicial support for the narrow view.[53] This sits oddly with the fact that all three of the minority judges in the case adopted it. It also sits oddly with the acknowledgment by the majority[54] of the diversity of reasons lying behind the recent judicial support for the broad view itself, and with the recent willingness of the High Court to abandon well established, but flawed, approaches to s 92 of the Commonwealth Constitution and Aboriginal title.[55]

The virtues of the narrow view are spelt out in the minority judgments. The merits of the case for that view will not be re-visited here. It need only be noted that the broad view prevents States from levying a "consumption tax" (which is to say, a sales tax on goods as opposed to a tax on the act of consumption itself.[56]) The arguments canvassed prior to the 1993 federal election against the imposition of such a tax by the Commonwealth, with its wider range of effective taxing tools, do not apply with equal force in regard to the States. Such a tax may be preferable to many of the taxes the States are currently forced to impose.[57]

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48 (1993) 178 CLR 561.

49 Ibid at 583.

50 *Peterswald v Bartley* (1904) 1 CLR 497 at 509 and 512.

51 The evidence is discussed at length in the judgment of Dawson J in *Capital Duplicators Pty Ltd v ACT [No 2]* (1993) 178 CLR 561 at 606-609.

52 *Parton v Milk Board (Vic)* (1949) 80 CLR 229 at 260 per Dixon J.

53 (1993) 178 CLR 561 at 587 and 590.

54 Ibid at 592-593.

55 *Cole v Whitfield* (1988) 165 CLR 360 and *Mabo v Queensland* [No 2] (1991-92) 175 CLR 1. Note also the remarks by Mason CJ to the effect that it is "no longer feasible to decide cases by reference to obsolete or unsound rules": *Australian* 16 March 1994 at 1.

56 For a tax on consumption itself see *Dickenson's Arcade Pty Ltd v Tasmania* (1974) 130 CLR 177.

57 See D J Collins writing in the Australian Tax Research Foundation, *State Taxation: Assessing the NSW Tax Task Force Report* (Conference Series No 9, 1989) at 10; *Hematite Petroleum v*

The majority in *Capital Duplicators [No 2]* also declined to review the constitutionality of current State business franchise fees on tobacco, alcohol and petrol, that is, to determine if they were in reality taxes on commodities at the point of production or distribution. One reason for refusing to re-open that question was that these franchise fees are important to the States in financing the operations of government and had been imposed in reliance on previous High Court decisions. It was also suggested that the States might face hefty claims from taxpayers for refunds if the decisions relied on were over-turned.[58]

But there was another reason too. And it is that reason I wish to turn to here. The majority's judgment promotes the proposition "that there are some grounds for treating tobacco and alcohol products as constituting a special category of goods for the purpose of considering whether what purports to be a licensing fee under a regulatory regime should be characterised as a duty of excise."[59] The extraction from the judgments of the exact basis for the proposition that tobacco and alcohol charges under a regulatory regime might escape characterisation as excises takes considerable effort. The arguments which are found to underlie that proposition are far from satisfactory.

Not an excise if regulatory

In support of the proposition that charges under a regulatory scheme may not be excises, the majority in *Capital Duplicators [No 2]* cite the following passage from the judgment of Taylor J in *Dennis Hotels Pty Ltd v Victoria* in regard to franchise fees on alcohol, namely that "... the system of licensing erected by the *Licensing Act* ... is ... a traditionally accepted method of regulating a trade which the public interest demands shall be subject to strict supervision."[60] The suggestion seems to be that there is something intrinsically hazardous about alcohol (and tobacco) which requires it to be regulated.[61] It is harder to extend that rationale to petrol of course.

The majority in *Capital Duplicators [No 2]* themselves acknowledge[62] that the regulatory approach does not support the petrol franchise fees upheld in *H C Sleigh Ltd v South Australia*[63] with the same cogency as the alcohol fees upheld in *Dennis Hotels* and the tobacco fees upheld in *Dickenson's Arcade Pty Ltd v Tasmania*.[64] But they conclude that:

Victoria (1982) 151 CLR 599 at 617-618 per Gibbs CJ and at 639 per Murphy J; and note also *Capital Duplicators [No 2]* (1993) 178 CLR 561 at 605-606 per Dawson J.

58 (1993) 178 CLR 561 at 593.

59 Ibid at 591.

60 (1960) 104 CLR 529 at 576.

61 See the judgment of Toohey and Gaudron JJ in *Capital Duplicators [No 2]* (1993) 178 CLR 561 at 628: "There are of course judgments in this Court which have attributed particular qualities or characteristics to certain commodities, alcohol and tobacco in particular. The characteristics are said to invoke the need for their regulation, with the consequence that those commodities do not in any event fall within the operation of excise. There are, we suggest, considerable difficulties in that approach, particularly if a distinction is to be made on the basis of their harmfulness."

62 (1993) 178 CLR 561 at 593.

63 (1977) 136 CLR 475.

64 (1974) 130 CLR 177.

> All that means, however, is that, if a fee imposed in purported conformity with *H C Sleigh* were of sufficient magnitude to deny a regulatory character to the law which imposes it, the validity of the fee would require close consideration.[65]

This seems to suggest that the potentially harmful aspects of alcohol and tobacco might justify a more elaborate licensing scheme, with, say, intensive checks on applicants, inspection of premises and enforcement of the terms of the licence. A relatively higher fee would be needed to cover the costs of such a scheme. Such a fee would not arouse suspicion that the description of the scheme as regulatory was a matter of form rather than substance. But the same fee for a product not obviously in need of such close regulation in the interests of the public might raise just such a suspicion. Given the enormous contribution all of the franchise fees make to State coffers in excess of the costs of instituting them, this talk of possible "suspicions" seems rather quaint.

But this still begs the question: why is a fee designed to regulate trade in a commodity (such as tobacco or alcohol) not an excise? On the basis of our earlier discussion, there are two possible explanations. Either the levy is a tax but not an excise, or it is not a tax at all.

Not a tax because requited?

Are such regulatory fees taxes at all? We have already noted that a licence fee which is set to recoup the administrative costs of issuing it will not be a tax. This is because the payment made by the licence holder is requited — the licence holder receiving in return the administrative service involved in issuing the licence.

In *Capital Duplicators [No 2]*, a franchise fee levied on traders in x-rated videos was held to be an excise on grounds which included the following:

> [T]he size of the fee (40 per cent) is larger than the fee exacted in the other franchise cases and clearly exceeds the cost of implementing the scheme. No endeavour was made to justify the size of the fee on that score ... Hence, the purpose of exacting the licensing fees is not simply regulatory but has a very substantial revenue purpose.[66]

Note the suggestion implicit here that "in the other franchise cases" — those dealing with tobacco, alcohol and petrol "franchise fees" — the fees might not have exceeded the costs of implementing the relevant schemes. But the "cost of implementing the scheme" is not the same as "the cost of issuing the licence". Where a scheme involves elaborate administration beyond that necessary to consider individual licence applications, any fee which recoups the costs of the additional administration will not be for services provided directly to the applicant. Consider again the following passage from *Air Caledonie International*:

> If the person required to pay the exaction is given no choice about whether or not he acquires the services and the amount of the exaction has no discernible relationship with the value of what is acquired, the circumstances may be such that the exaction is, at least to the extent that it exceeds that value, properly to be seen as a tax.[67]

In *General Practitioners Society v Commonwealth*, Aickin J noted that a licence fee charged to pathologists which exceeded the costs of their licensing "would not be a new form of

65 (1993) 178 CLR 561 at 593.
66 Ibid at 596-597.
67 (1988) 165 CLR 462 at 467.

tax for what may be called 'franchise' taxes have often been imposed, and this could well be regarded as such a tax."[68]

Nor does there appear to be anything in the judgments in previous cases dealing with liquor, tobacco and petrol franchise fees to suggest they are requited by services rendered to the holders.[69] Such franchise fees in fact incorporate a fixed licence charge apparently designed to cover the administrative costs of issuing the licence and a much more substantial charge based on volume of trade (usually in a prior period). While the latter component may be appropriate to raise the revenue necessary to fund other aspects of the regulatory scheme, it would be an inappropriate method of charging for the direct costs of issuing the licence: *Marsh v Shire of Serpentine-Jarrahdale*.[70]

In *Philip Morris Ltd v Commissioner of Business Franchises (Vic)*,[71] McHugh J considered that there was "a respectable, if not necessarily correct, argument" that the traditional franchise fees on alcohol, tobacco and petrol were exacted "for the privilege of carrying on the business."[72] Could this amount to requitement? The phraseology is reminiscent of the comment in *Air Caledonie International*[73] that payments such as "a charge for the acquisition or use of property [or] a fee for a privilege" are "unlikely to be properly characterised as a tax". However this is unlikely to have been what McHugh J had in mind. We have already seen that *Harper v Minister for Sea Fisheries*[74] explains that requitement occurs only where a real material advantage has been granted, not where the privilege granted is of the kind contemplated by McHugh J — access to a particular business rather than a particular material resource. Indeed, the Court in *Harper* specifically excluded liquor licences from this kind of requited payment. And in his judgment in *Philip Morris*, Brennan J describes the fee in *Dennis Hotels* as "a *tax* ... exacted for the privilege of engaging in the process at all (which is not an excise)."[75]

So, a levy does not cease to be a tax just because it is used to fund government regulation of trade in a particular commodity. If the method of regulation chosen by a government involves an unrequited impost, then the specific purpose for levying it is irrelevant to its nature as a tax.[76] Indeed, a purpose of regulation at either the micro-economic or macro-economic level is a normal characteristic of taxation.[77] Consider, for instance, the tax levied in *Australian Tape Manufacturers* which was designed to ensure

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68 (1980) 145 CLR 532 at 568-9.

69 See *Roberts v Business and Property Ltd* (1934) SR (NSW) 483 at 487. In *Dennis Hotels* (1960) 104 CLR 529 at 576-577, Taylor J did say that the value of licensed premises increased as a result of obtaining the licence. But he was not arguing that this amounted to requitement. After all, the increase in value results from the existence of the licence itself. If this were requitement, all licence fees could be said to be requited by the licences obtained in return for them.

70 (1966) 120 CLR 572.

71 (1989) 167 CLR 399.

72 Ibid at 500.

73 (1988) 165 CLR 462 at 467.

74 (1989) 168 CLR 314.

75 (1989) 167 CLR 399 at 460 (emphasis added).

76 *Northern Suburbs General Cemetery Reserve Trust v Commonwealth of Australia* (1993) 112 ALR 87.

77 See, for example, R Musgrave and P Musgrave, above n 11 at 6.

proper compensation to copyright holders for the likely exploitation of recordable works by the purchasers of blank audio cassettes.

Hence the proposition that a "regulatory" fee might not be an excise does not have as its basis the belief that such an impost is requited and therefore not even a tax. The answer must lie elsewhere. And indeed, the majority judges in *Capital Duplicators [No. 2]* seem to be suggesting that such an impost, while it is a tax, is not a tax *on goods*.

A personal tax, not an excise

The majority judges in *Capital Duplicators [No 2]* appear to be arguing that the regulatory nature of an impost can convert it from a tax *on goods* into a tax *on persons* involved in trading in such goods. A tax on the "privilege of carrying on the business" is seen as a personal tax as opposed to an excise.

Thus, one of the characteristics of a constitutional franchise fee cited by McHugh J in *Philip Morris*[78] (and quoted in *Capital Duplicators [No 2]*[79]) is that the licence period itself is for a relatively extended period of time. A regulatory scheme which is genuinely concerned about the character and conduct of those involved in a particular trade will be unlikely to review and renew licences on a monthly basis. Such regular renewals seem more appropriate to gauging turnover than seriously probing the suitability of those involved in the trade.

In *Philip Morris*, McHugh J also placed importance on "the length of time between the commencement of the licence period and the end of the period by which the licence fee was calculated."[80] This again is seen as lending some weight to an assertion that the focus of the tax is on a person's history in the trade rather than their current turnover. (Though why a scheme concerned to regulate the type of persons involved in a trade should charge more in the case of a person who has dealt successfully in it previously is more difficult to explain.)

Brennan J considered it relevant to his dissenting view that the levy in *Philip Morris* was an excise, that Parliament intended it to be borne by only one person in the chain of distribution from producer to consumer and was indifferent as to which of those persons in fact bore it.[81] Again, the levy was not seen as genuinely concerned with the identity of the traders. Of course, a tax *intended* to regulate the persons engaging in a particular trade will still be an excise if it takes *the form* of a tax on goods. So the fundamental question that confronts us is: what is it about the existing franchise fees (on tobacco, alcohol and petrol) which means that they are not in substance taxes *on goods* at some point in their production or distribution?

A direct tax, not an excise

The answer seems to be that the various features associated with these "personal" taxes mean that they are not designed to be built into the price of the relevant commodities. An early warning that this might be the Court's approach was provided by the remark

78 (1989) 167 CLR 437 at 500.
79 (1993) 178 CLR 561 at 593.
80 (1989) 167 CLR 437 at 500, quoted in *Capital Duplicators [No 2]* (1993) 178 CLR 561 at 593.
81 (1989) 167 CLR 437 at 461-462.

in the joint judgment of Brennan, Deane and Toohey JJ in *Capital Duplicators [No 1]* that "[d]uties of excise are taxes which are likely to be borne by the consumer."[82]

We have noted that the majority judgment emphasised the size of the licence fee in *Capital Duplicators [No 2]*. Again, this seems to be tied to the view that a personal tax should be small enough to be paid without provoking a flow-on into prices during the period of the licence itself. This is an appeal to the "directness" of personal taxes.[83] In *Philip Morris*, Brennan J wrote :

> [A] modest licence fee calculated by reference to past transactions may be merely a business overhead in carrying on a current business ... [Whereas] a fee which must be paid as the price of continuing to carry on a business and which is calculated at a substantial rate on the value of the commodity in which transactions have taken place in the business is likely to enter immediately and precisely into the price charged for the commodity to the next buyer in the chain of distribution and wears the aspect of a tax on transactions in the commodity rather than a licence fee to carry on a business. It appears more clearly as a tax "upon goods".[84]

Likewise, the majority in *Capital Duplicators [No 2]*[85] quote the judgment of Barwick CJ in *Anderson's Pty Ltd v Victoria*[86] to the effect that "[t]he indirectness of the tax [and] its immediate entry into the cost of the goods" are two of the factors which indicate that a particular tax might be an excise.

But there are serious flaws in the notion that one particular form of a tax can be categorised as more direct than another. Consider the following quotation from the judgment of Mason J in *Hematite Petroleum Pty Ltd v Victoria*:

> [T]o justify the conclusion that the tax is upon or in respect of goods it is enough that the tax is such that it enters into the cost of the goods and is therefore reflected in the prices at which the goods are subsequently sold.[87]

All taxes associated with the activity of production will be taken into account in assessing the price structure necessary to pursue the business profitably. In that sense all taxes are reflected in the price of goods. If Mason J meant rather that an indirect tax is reflected in an *increased* price, then the problem is that such a consequence will depend largely on market conditions, not the form of the tax. Consider again the recent litigation on the WA Meat Marketing scheme, discussed above. The plaintiffs argued that the scheme involved a tax on a step in the chain of production of meat in Western Australia. That tax was levied on the first wholesale sale after slaughter.[88] Even the most narrow interpretation of the term excise acknowledges that it includes a tax on goods at the point of production.[89]

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82 *Capital Duplicators Pty Ltd v ACT [No 1]* (1992) 177 CLR 248 at 278.

83 A direct tax is one borne by the person on whom it is imposed. (That is, its legal incidence coincides with its economic incidence). An indirect tax is one intended to be passed on to others. An excise is described as an indirect tax because it is assumed that it will be passed on to those who purchase the goods at points in the chain of distribution subsequent to the imposition of the tax (ultimately, the consumers).

84 (1989) 167 CLR 437 at 462.

85 (1993) 178 CLR 561 at 583.

86 (1964) 111 CLR 353 at 365.

87 (1983) 151 CLR 599 at 632.

88 The size of the tax faced by domestic wholesalers was the difference between the "distributor price" and the "producer price".

89 *Peterswald v Bartley* (1904) 1 CLR 497.

But one argument that was raised against the WA Meat Marketing levy being an excise was that the moneys collected by the Corporation did not lead to higher domestic prices. This argument relied on the contention that WA domestic prices were constrained by the possibility of competition from Eastern State producers.[90] Assuming the validity of that contention, how does that prevent the levy having the character of an excise? Certainly, a levy imposed on wholesalers would have to be *built into* their price structure. All taxes faced by producers will lead to a rise in the prices they charge, or a fall in profits (returns to capital), or a fall in the return to factors in production (labour), or a combination of all three. The actual outcome will depend on the elasticity of consumer demand for the particular product and the elasticity of supply for capital and labour in the industry.[91]

The imposition of any cost to production which is actually incurred, be it, for example, labour costs, costs of raw materials, taxes, charges or association membership fees will inevitably be built into the pricing decisions of the producer. If the producer has no control over the imposition of the levy then it will have to be built into the price. It may either cause a rise in price or it may displace some other element previously built into the price (for example, part of the profit margin, other price inputs such as labour or employee amenities). It may be that the consumer is paying the same price but no longer contributing to the same level of profit margin. But it is indisputable that *the consumer will be bearing the full cost of the tax* since the decision as to the extent to which it is incurred is not a decision within the producer's control, and *the tax will have to be paid out of price receipts.*

Suppose we were to accept the argument that an added levy on domestic wholesalers of lamb would not impact on retail prices in Western Australia. Suppose further that the State Government were to impose a tax on domestic wholesalers chargeable on every kilo of lamb they sold. And suppose the funds were simply collected and paid into consolidated revenue. Could the State Government really argue that the levy did not constitute an excise because it would not lead to *higher* prices? If any tax is increased it will have to be paid out of receipts, and that fact remains true whether prevailing markets dictate that the taxpayer should adjust for the increased payment by passing it forward as increased commodity prices, backwards into input prices (rent, raw materials, labour, interest on borrowed capital) or absorb it in the form of reduced profits. Those competing against imported goods, or domestically produced substitute goods which are not subject to the tax, will find difficulty in raising the prices of the goods themselves.

Reference to the indirectness of excises dates back to *Peterswald v Bartley*.[92] In that case the word excise in s 90 was said "to mean a duty ... imposed upon goods ... and not ... a direct tax or personal tax". However, the concluding words have been interpreted by some to indicate only that a personal tax not calculated in accordance with the

90 One objection to this argument is that the existence of a ceiling is not, in fact, inconsistent with the scheme leading to higher domestic prices in Western Australia. Firstly, Western Australia has a peculiarly large domestic surplus of lamb and so one might ordinarily expect the domestic market price there to be *lower* than that in the east. Even were that not so, eastern State producers would face extra costs in terms of freight and market entry. These costs would present a buffer into which domestic lamb prices could be moved with relative impunity.

91 R Musgrave and P Musgrave, above n 11 at 237.

92 (1904) 1 CLR 497 at 509.

quantity or value of certain goods would not be an excise, rather than that excises cannot take the form of direct or personal taxes.[93] In any event, it has long been recognised by various judges that the indirectness of excises cannot be their distinguishing feature as it is a general characteristic they share with many other types of impost, and one which is largely influenced by the market forces facing particular types of taxpayer rather than by the particular form of the tax.[94]

Yet the majority judgment in *Capital Duplicators [No. 2]* represents a continuance of the acceptance of directness as a feature which saves a franchise fee from being a tax on goods. Their "regulatory" criterion in fact boils down to no more than this. Legitimate franchise fees are characterised by the majority as once-in-a-while payments levied from those conducting a particular type of business so as to regulate participation in that business. The crucial aspect which prevents these taxes from being taxes on the goods which are the trading stock of the business is that they are characterised as being borne by the taxpayer out of their own resources, rather than being factored into the running costs of that business whose continuing receipts represent the current source of those resources. This whole distinction seems to be based on a rather naive view of the way pricing structures are devised.

The suggestion that "personal" franchise fees are "business overheads" and therefore not likely to enter directly into the price of cigarettes must have had an ironic ring to the plaintiffs in *Philip Morris*. Just ten years earlier in *Philip Morris v Federal Commissioner of Taxation*[95] they were told that the correct way to value the cost price of their trading stock for income tax purposes was to use the full absorption cost method — a method that includes all the indirect business overheads attributable to producing the goods. *Any* tax faced by a producer will be a cost of production which will be factored into prices. Some judges and academic writers have already pointed out that a whole range of taxes, including pay-roll tax, might be excises on a test that is based on this inevitable occurrence.[96]

There is also an internal inconsistency in the majority's analysis. We have seen that the High Court would be suspicious of a large levy on traders in an innocuous commodity, since relatively little money would be necessary to adequately regulate that trade in the public interest. Suppose licence fees for dealing in alcohol and, say, cauliflowers, were set at the same rate. The suggestion seems to be that the former might be a personal tax on account of the higher costs likely to be incurred by the government in regulating the alcohol trade. But the cauliflower franchise fee would be suspected of being designed to generate revenue for other unrelated government activities. The problem is this: how can the limited costs likely to be incurred by government in regulating the sale of cauliflowers result in any greater likelihood that traders in cauliflowers will pass their franchise fees into the price of their goods? Why

93 See *Dennis Hotels*, (1960) 104 CLR 529 at 554 per Fullagar J, cited in the judgment of Dawson J in *Capital Duplicators [No 2]* (1993) 178 CLR 561 at 616.

94 See Dawson J's minority judgment in *Capital Duplicators [No 2]* (1993) 178 CLR 561 at 602 and 610, and the other judgments cited by him there, including *Dennis Hotels* (1960) 104 CLR 529 at 553-554 per Fullagar J and *Philip Morris* (1989) 167 CLR 437 at 445 per Mason CJ and Deane J and at 470-471 per Dawson J.

95 (1979) 79 ATC 4352.

96 *Logan Downs Pty Ltd v Queensland* (1977) 137 CLR 59 at 84 per Murphy J; *Gosford Meats Pty Ltd v NSW* (1985) 155 CLR 368 at 416 per Dawson J; G Pearson and G Lehmann, "Are State Payroll Taxes Unconstitutional?" (1990) 24 *Taxation in Australia* 864.

will traders in alcohol facing the same level of fees be less inclined to do so? Is there any nexus at all between the genuinely "personal" or "regulatory" intent of a licence fee and its movement into prices? The purpose of the levy in the minds of those collecting it cannot determine the economic effect on those paying it.

If the cases upholding existing business franchise fees cannot be salvaged on the basis of the "personal/direct" nature of those taxes, what of the argument that the States should nevertheless be undisturbed in their reliance upon those decisions? Apart from the interesting questions such a notion raises for the concept of rule by law, can it actually be said that the States have relied on those decisions? We have seen that the High Court understands that it was fundamental to those decisions that the taxes upheld were "personal/direct", and in particular were small enough to qualify for that description. In *Dickenson's Arcade* the *ad valorem* rate for the tobacco franchise fee was 2.5 per cent of the value of goods traded, in *Dennis Hotels* the franchise fee on alcohol was set at 6 per cent and in *H C Sleigh* the petrol fee was set at 10 per cent.

But by June 1992,[97] the fee for petrol in NSW was set at 15.5 per cent on motor spirit and 25.77 per cent on diesel; fees for alcohol were 10 or 11 per cent in all States, and tobacco fees had rocketed to 50 per cent in all States other than Queensland (30 per cent) and NSW (75 per cent) and have recently increased to 100 per cent in WA.

So it may be that the current franchise fee legislation is not supported by the High Court's earlier decisions after all. Perhaps the only road to salvation for these taxes is the path that leads to the narrow interpretation of excise in s 90, an interpretation which leaves the States free to impose taxes on the distribution of goods.

97 Commonwealth Grants Commission, *Commonwealth Grants Commission Report on General Grant Relativities 1993* Appendix G.