Tax agents: beware of "administrative overpayments" added to your RBA

by John Glover, FTI, Barrister, Victorian Bar

The Commissioner has recently debited tax agents' running balance accounts (RBAs) with tax refund payments received by agents on behalf of their clients. It is alleged that the refunds can be recovered as amounts that the Commissioner "paid to a person by mistake" pursuant to s 8AAZN of the *Taxation Administration Act 1953* (Cth). The practice is insupportable. First, the wrong RBA is debited. The client, not the tax agent, is the "person" to whom tax refunds are paid. Second, the Commissioner rarely makes mistakes when paying tax refunds. Refunds are paid automatically and entitlement derives from self-assessment. Australia's only two s 8AAZN authorities have upheld these propositions.

Introduction

The *DCT v MWB Accountants Pty Ltd*[1] litigation in the Victorian courts and the Federal Court of Australia decision in *Auctus Resources Pty Ltd v FCT*[2] have put in doubt the correctness of the Commissioner debiting tax agents' running balance accounts (RBAs) with "tax debts" pursuant to s 8AAZN of the *Taxation Administration Act 1953* (TAA53), which provides:

> "**8AAZN Overpayments made by the Commonwealth under taxation laws**
>
> (1) An administrative overpayment (the ***overpaid amount***):
>
> (a) is a debt due to the Commonwealth by the person to whom the overpayment was made (the ***recipient***); and …
>
> (3) In this section:
>
> ***"administrative overpayment"*** means an amount that the Commissioner has paid to a person by mistake, being an amount to which the person is not entitled."

A recent practice of the Commissioner is to debit tax agents' RBAs with "administrative overpayments" of tax refunds pursuant to s 8AAZN. It is alleged that the payments were made "by mistake" to tax agents when acting for their clients. The identity of the person paid, or the "recipient", is the first issue of concern. Section 8AAZN supplies no basis for debiting tax agents' RBAs with "administrative overpayments" received by tax agents acting on behalf of their clients.

Proposition 1: the client is the "recipient" of tax refund payments

The structure of Pt IIB TAA53 assumes that RBA surplus refunds are paid to the entities that have generated the surpluses. Where, in the words of s 8AAZLF(1), a "refund" is paid to "an entity" of "the RBA surplus of the entity" or a "credit … in the entity's favour", the *intended object* of the payment must be the entity. This is obvious. Running balance account surplus provisions are otherwise inexplicable.[3]

Interpreting Pt IIB as it applied to overpaid GST refunds made to a tax agent, Steward J, for the Full Court of the Federal Court in *FCT v Travelex Ltd*, observed that there was a necessary correspondence between RBA surpluses which generate refunds and the Commissioner's "historical" allocation of debits and credits to RBAs.[4] There is no equivalent correspondence between overpaid refunds and the RBAs of tax agents.

Section 8AAZLH is titled "How refunds are made" and ends with a deeming provision. Section 8AAZLH(2) provides that the "Commissioner must pay … refunds to the credit of a financial institution account nominated in the approved form by that entity". Subsection (2A) states that the account must be held by one of three persons, including "the entity's registered tax agent or BAS agent". Finally, subs (5) states that:

> "If the Commissioner pays a refund to the credit of an account nominated by an entity, the Commissioner is taken to have paid the refund to the entity."

The wording of subs (5) makes it virtually impossible to contend that the tax agent, not the client, receives the Commissioner's tax refunds.

MWB Accountants litigation

In *MWB Accountants,* Judge Marks in the County Court of Victoria disallowed the Commissioner's s 8AAZN "administrative overpayments" claim. This was Australia's first reported decision on the section. Goods and services tax refunds were paid to MWB Accountants Pty Ltd (MWB) as tax agent pursuant to business activity statements (BASs) lodged on the client's behalf.[5] Approximately two years later, the Commissioner alleged for the first time that the refunds were administrative overpayments.

Perhaps the Commissioner chose *MWB Accountants* as a suitable case in which to litigate s 8AAZN because of certain additional facts. MWB did not pass on most of the refunds received on behalf of its client. Instead, the refunds were used to satisfy the client's debt owing to MWB's related company, the benefit of which was assigned to MWB. The Commissioner subsequently accepted the client's assertion that BASs lodged on its behalf were unauthorised and paid the tax refunds to the client for a second time. These facts gave the Commissioner the benefit of an additional contention: tax refunds which derived from *unauthorised* BASs were arguably outside TAA53 procedures.

Judge Marks held that the refund payments must have been "paid" to the client and not to MWB because surplus

and credit refunds due under Pt IIB's RBA provisions were payable to the "entities" for whom the RBAs were established. MWB's contentions about the interlocking structures of the TAA53 and the *A New Tax System (Goods and Services Tax) Act 1999* (GSTA99) were accepted by her Honour.[6]

Judge Marks considered that her analysis was fortified by s 8AAZLH, titled "How refunds are made". Section 8AAZLH(2) directs that RBA surpluses or credits be paid to the credit of a financial institution account nominated by the entity. Section 8AAZLH(3) provides that the nominated account be held, inter alia, by the entity's registered tax agent. Section 8AAZLH(5) then provides that:

> "If the Commissioner pays a refund to the credit of an account nominated by an entity, the Commissioner is taken to have paid the refund to the entity."

Deeming the refund to be paid "to the entity" leaves no room for the Commissioner's contention that MWB was the person paid.

Judge Marks also considered and rejected the Commissioner's unauthorised BAS argument, concluding that that authorisation was irrelevant to establishing the identity of the person receiving the payments.[7]

The Victorian Supreme Court of Appeal (Niall, Hardgrave and Sifris JJA) heard the Commissioner's appeal from the County Court's *MWB Accountants* decision on 3 September 2020.

The largest part of the Commissioner's case on appeal was based on his "additional" contention that the BASs were unauthorised, with the argued consequence that the tax agent was the "recipient" of the refund payments. Members of the court noted the case's unusual facts and drew attention to Judge Marks' observations to this effect.[8] One wonders why the appeal was brought, as an appellate decision in *MWB Accountants* based on the Commissioner's "unauthorised" argument would only have low precedential value about the application of s 8AAZN to refund payments.

A "wild card" in the *MWB Accountants* appeal was the effect of MWB's additional defence that the Commissioner's mistake was insufficient for the purposes of s 8AAZN The defence was based on the *Auctus* decision which was handed down in the Federal Court about a month before the hearing of the appeal. Not long after the hearing and prior to the judgment, the Commissioner quietly discontinued proceedings, paid MWB's costs and ended the *MWB Accountants* litigation.

Proposition 2: the Commissioner's mistake causes the making of few tax refund payments

Minimum conditions for a s 8AAZN "mistake" are not satisfied where the entitlement to an RBA surplus is self-assessed and refunds are paid by the Commissioner in an automatic procedure which excludes consideration. We are examining whether "administrative overpayments" comprising RBA surplus refunds can ever have been paid "by mistake". Such payments are obligatory. Section 8AAZLF(1) provides that:[9]

> "The Commissioner *must* refund to an entity so much of:
>
> (a) an RBA surplus of the entity … [as is not otherwise allocated]." (emphasis added)

Refunds are self-assessed

The Commissioner is not empowered to consider the correctness of a client's GST surplus claims in BASs lodged by or for the client. Running balance accounts and surplus refunds have prima facie validity. Stated by the Full Court of the Federal Court in the *Travelex* case:[10]

> "… Pt IIB gives the balance recorded in an RBA legal efficacy, even though the balance may be mistaken. Any other conclusion would seriously undermine the effectiveness of the RBA system. If a mistaken entry is made to an RBA it will then be a matter for either the taxpayer or the Commissioner to correct that balance by the filing of a GST return, or by the issue of an assessment."

Refunds are automatic

Not only does the Commissioner not have the power to question the RBA net amount data supplied by a client (or supplied on their behalf), there is no *time* for the Commissioner to consider the correctness of the client's claims before refund payments must be made.[11]

FCT v Multiflex Pty Ltd[12] concerned a taxpayer which had worked out its "net amount" for a tax period under the GSTA99 and claimed to be entitled to an immediate refund. The Full Court of the Federal Court in *Multiflex* confirmed that neither the GSTA99 nor the TAA53 provided the Commissioner with the "reasonable time" necessary for him to determine if a taxpayer's claim were truly payable.

The "imperative language" of s 35-5 GSTA99 meant that the refund had to be paid without consideration, and sometimes, the court in *Multiflex* added, the Commissioner is "obliged to make a refund based on a claimed net amount which he knows to be wrong".[13] Any "disquiet" that the Commissioner might have in this event could be overcome though the issue of new assessments.[14] It is perhaps not too much to say that it is practically impossible for the Commissioner to make a mistake about whether or not a GST refund should be paid.

Nature of a necessary "mistake" for s 8AAZN purposes

An "administrative overpayment" made pursuant to s 8AAZN(3) is an amount that "the Commissioner has paid to a person by mistake". The word "mistake" is preceded in the subsection by the preposition "by". Together, the words "by mistake" connote an "act or judgment" which is both the *cause* and *contemporaneous with* the Commissioner's payment. Placing the expression in the context of s 8AAZN, the words "paid to a person by mistake" describe a cause which was present when an overpayment was made. It follows that mistakes of a retrospective or ex post facto nature cannot activate the section.[15]

Statutory construction of the words "paid to a person by mistake" in the wider contexts of Pt IIB TAA53, the GSTA99 and associated tax legislation introduces further qualifications. The mistake must be an act or judgment which is wrong or incorrect in a way which can be made in an automatic transaction and does not undermine the validity of taxpayers' self-assessment (discussed above). An entity's entitlement to a tax refund cannot be denied by the Commissioner until the RBA of the entity is corrected by the filing of (another) GST return or the issue of an assessment.[16]

Consistently, Steward J in *Auctus* said that the type of mistakes made by the Commissioner to which s 8AAZN was directed were "mistakes made in the administration of an RBA". Examples of an administration mistake which his Honour gave were payment to the wrong person, payment arising from a misallocation of tax debts, and payment arising from computer error.[17]

Auctus

At first instance, the Federal Court in *Auctus* disallowed the Commissioner's attempt to use s 8AAZN(1) to recover a tax refund automatically paid to Auctus Resources.[18] The refund was paid in 2014 as the consequence of a research and development tax offset claimed in the company's 2013 income tax return.[19] Not until 2019 did the relevant authority establish that the refund was not due. In some ways, the facts of *Auctus* closely paralleled those of *MWB Accountants*.[20] Refund payments were automatic, and the recipient's entitlement was self-assessed in each case. However, the Commissioner in *Auctus* paid the refund directly to the company which claimed it and not to the financial institution account of a tax agent intermediary.

Refund recovery proceedings in *Auctus* began in September 2019 when Auctus Resources received a s 8AAZN notice stating that the Commissioner required repayment of "an amount paid to you by mistake being an amount to which you are not entitled".[21] The facts of *Auctus* were anomalous. Recovery of the overpaid amount by amended assessment was not possible when it was finally determined that the company was not entitled to the payment.[22] Legislation enabling the Commissioner to amend the company's 2013 assessment was post-dated[23] and transitional legislation conferring a comparable power was repealed before the taxpayer's non-entitlement to the refund was determined.[24]

In reply to the s 8AAZN notice, Auctus Resources asserted that the refund it received in 2014 had not been paid "by mistake", nor was there any "administrative overpayment" in the sense required by s 8AAZN(3). The Commissioner instead had given effect to what the taxpayer had claimed in its self-assessed tax return.[25]

The Commissioner made a logical error, the taxpayer said, by relying on subsequent events in order to justify the making of an earlier "mistake". The "administrative overpayment" definition in s 8AAZN(3) was inapplicable where the Commissioner made no "error in action, opinion or judgement … misconception or misapprehension" at the time that the payment was made.[26] Additionally, the Commissioner's action undermined a safeguard contained in Australia's tax legislation.[27]

Steward J held that the mistake required by the "administrative overpayment" definition in s 8AAZN(3) had to be "the activating cause of the overpayment". A mistake of this nature had to be made by (or imputed to) the Commissioner in order to satisfy the words "an amount the Commissioner has paid to a person by mistake".[28] His Honour's views correlate with the Full Court of the High Court of Australia's view in *Australia and New Zealand Banking Group Ltd v Westpac Banking Corporation* that "fundamental mistakes" are needed to base general law restitutionary recovery of mistaken payments.[29]

Entitlement mistakes were not the sort of "mistake" with which s 8AAZN is concerned, Steward J added. The Commissioner does not make this type of mistake. The scheme of the *Income Tax (Transitional Provisions) Act 1997* (Cth), the *Industry Research and Development Act 1986* (Cth) and relevant provisions of the ITAA36 and the *Income Tax Assessment Act 1997* (Cth) were to the contrary. Entitlement mistakes are made by self-assessing taxpayers.[30]

His Honour then examined the right way to recover research and development tax offset refunds paid to persons who were not entitled the refunds:[31]

> "The Commissioner should have used the mechanism created by that former Subdivision [Subdiv 67-L] of the *Transitional Act* to recover the tax refund."

Parliament plainly so intended.[32] Section 8AAZN was more limited. The Commissioner had given that section a competence which made the Act's other provisions otiose.[33]

"It follows that, in my view," Steward J said, s 8AAZN is directed to "errors, essentially administrative or procedural in nature", such as "a payment to the wrong person, a payment arising from a misallocation of tax debts, or a payment arising from a computer error".[34] This is a significant passage. Section 8AAZN is denuded of the operation for which the Commissioner contended in *MWB Accountants* and *Auctus.*

Perhaps the Commissioner overreached statutory legalities in attempting to make s 8AAZN do the work of traditional assessment and amended assessment procedures.[35] The Commissioner's claim in *MWB Accountants* had the same characteristic — combined with an additional unfairness. For more than a year, the Commissioner invoked taxpayer confidentiality obligations owed to MWB's client in order to prevent MWB from learning details of the s 8AAZN liability added to its RBA.

Conclusion

Accountants, lawyers and tax agents should be concerned when client-related administrative overpayments are added to their RBAs. The practice is contrary to the terms of relevant legislation and to the relationship which exists between tax information professionals and their clients.

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Note: Dr Glover was counsel for MWB Accountants before the County Court of Victoria and the Victorian Court of Appeal.

References

1 [2019] VCC 1516; an appeal to the Victorian Supreme Court of Appeal was discontinued after the hearing.

2 [2020] FCA 1096.

3 The history and policy of Pt IIB TAA53 do not support the imposition of an inexplicit liability on tax agents under s 8AAZN. Parts IIA and IIB were inserted into the TAA53 by the *Taxation Laws Amendment Act (No. 3) 1999*. In the explanatory memorandum which accompanied the relevant Bill, the purpose of s 8AAZN was described (once) as: "[to] introduce tax debts for administrative errors by the Commissioner."

4 [2020] FCAFC 10 at [166]-[167] per Steward J, Kenny J agreeing.

5 Pursuant to s 8AAZLH TAA53. See the reasons of Judge Marks in *MWB Accountants* [2019] VCC 1516 at [100]-[103] and [124]. How the refunds were constituted is discussed below at ref 9.

6 See the reasons of Judge Marks in *MWB Accountants* [2019] VCC 1516 at [91]-[103], examining s 31-15 GSTA99, s 8AAZLH TAA53, and ss 388-70 and 388-75 of Sch 1 TAA53.

7 See the reasons of Judge Marks in *MWB Accountants* [2019] VCC 1516 at [110]-[119]. Her Honour also accepted MWB's evidence that the BASs were properly authorised.

8 See the reasons of Judge Marks in *MWB Accountants* [2019] VCC 1516 at [40]-[43].

9 "RBA surplus amounts" are allocated by the Commissioner to the client's RBA pursuant to s 35-5 GSTA99. Refund entitlements are generated by s 35-5(1) and are payable under s 35-10 GSTA99 when entities lodge GST returns with "net amounts" which are "less than zero".

10 *Travelex* [2020] FCAFC 10 at [166] per Steward J, Kenny J agreeing.

11 This is the effect of ss 35-5 and 35-10 GSTA99, combined with s 8AAZLF(1) TAA53 and s 155-15(1) of Sch 1 TAA53.

12 [2011] FCAFC 142.

13 *Multiflex* [2011] FCAFC 142 at [26] and [40].

14 *Multiflex* [2011] FCAFC 142 at [26], referring to the now-repealed s 105-5 of Sch 1 TAA53. See also *Travelex* [2020] FCAFC 10 at [166].

15 As the successful taxpayer contended in *Auctus* [2020] FCA 1096 at [38] and [65] per Steward J. See also the definition of "mistake" in the *Oxford English Dictionary*, online version, 2019, Oxford University Press, 11.2.546.

16 As stated in *Travelex* [2020] FCAFC 10 at [166] per Steward J, Kenny J agreeing.

17 See *Auctus* [2020] FCA 1096 at [73].

18 The Commissioner has appealed from the *Auctus* decision.

19 Pursuant to s 27J of the *Industry Research and Development Act 1986* (Cth), and former s 166 of the *Income Tax Assessment Act 1936* (Cth) (ITAA36).

20 See *Auctus* [2020] FCA 1096 at [24]-[35].

21 See *Auctus* [2020] FCA 1096 at [28]-[31] per Steward J.

22 On the expiry of an appeals period on 19 July 2019, a determination by the board of Innovation and Science Australia pursuant to s 27J of the *Industry Research and Development Act 1986* (Cth) became binding to the effect that Auctus Resources was not entitled to the refund.

23 Section 172A ITAA36 was inserted in 2013 to allow the Commissioner to recover overpaid tax offset refunds by amended assessment. The provision operated only from 2014. See the reasons of Steward J in *Auctus* [2020] FCA 1096 at [12].

24 Subdivision 67-L of the *Income Tax (Transitional Provisions) Act 1997* contained a set of provisions applicable to the recovery of tax offset refunds paid by the Commissioner in the 2013 year. The transitional legislation was repealed in 2019. By this time, the two-year period for the amendment of assessments had expired. See s 355-710(2) ITAA36 and the reasons of Steward J in *Auctus* [2020] FCA 1096 at [14] and [40].

25 See *Auctus* [2020] FCA 1096 at [36]-[40].

26 The taxpayer's successful contention as set out by Steward J in *Auctus* [2020] FCA 1096 at [36].

27 See the reasons of Steward J in *Auctus* [2020] FCA 1096 at [40] and [68]-[72], noting the two-year limit on the time during which the Commissioner can alter an assessment.

28 See *Auctus* [2020] FCA 1096 at [65].

29 See [1988] HCA 17 at [8] and [14]. *Auctus* and *MWB Accountants* only involved s 8AAZN recovery claims. General law restitutionary principles were of no direct relevance.

30 See *Auctus* [2020] FCA 1096 at [14]-[27] and [77].

31 See *Auctus* [2020] FCA 1096 at [68].

32 See *Auctus* [2020] FCA 1096 at [71].

33 See *Auctus* [2020] FCA 1096 at [72].

34 Steward J in *Auctus* [2020] FCA 1096 at [73], citing (at [72]) *Project Blue Sky Inc v Australian Broadcasting Authority* [1998] HCA 28.

35 This was the view of Steward J in *Auctus* [2020] FCA 1096 at [62]-[72].

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The Tax Summit: Project Reform