# CASE [1999] AATA 401
# Re SREE and INDUSTRY RESEARCH and DEVELOPMENT BOARD

**42 ATR 1071**

Headnote | Catchwords | Holdings | Potion | Counsel | Decision

ADMINISTRATIVE APPEALS TRIBUNAL - GENERAL ADMINISTRATIVE DIVISION

B J McMahon, Deputy President

Ref no: N95/1168

Dec no: [1999] AATA 401

27, 28, 29 April, 10 June 1999 - Sydney

## Headnote

### Catchwords

Research and development expenditure - Computer software - Purpose of activity - Whether purpose in engaging in activity must be sole or dominant or originating purpose for expenditure to qualify as deductible - 'During' a year of income - *Industry Research and Development Act 1986* (Cth), s 39T - *Income Tax Assessment Act 1936* (Cth), s 73B.

### Facts

The taxpayer was a large Australian bank that had spent considerable sums of money on the development of a computer system. It claimed that the money spent should be deductible as research and development within the meaning of s 73B of the *Income Tax Assessment Act 1936* (Cth). The Commissioner, after reviewing a determination received from the Industry Research and Development Board (IRDB), found that the amount was not deductible as the software was for internal use of the bank, and therefore was excluded from the definition of research and development by s 73B(2). The taxpayer appealed to the AAT for a review of the IRDB's decision made this application to the tribunal claiming that the purpose of sale etc did not need to be the sole or dominant or originating purpose.

### Holdings

**Held**, setting aside the decision under review and remitting the matter to the IRDB with a direction that the activities constitute research and development:

(1) In order to qualify as research and development it was not necessary that the dominant or actuating purpose of the activity was sale or profit, as there may be a number or multiplicity of purposes, and it is necessary only that the taxpayer show that one of the purposes found in s 73B(2) was a collateral or relevant purpose that was not an insubstantial purpose in conducting the activity.

*Clyne and Anor v DCT and Anor* (1981) 150 CLR 1; *FCT v Mt Isa Mines Ltd* (1991) 28 FCR 289, cited.

(2) In seeking to discern a corporate purpose in a large organisation evidence may be adduced as to the purposes of the Board of Directors and any managers to whom the board may have delegated decision making power.

*Hamilton v Whitehead* (1988) 166 ALR 121; *Daniels & Ors (formerly practising as Deloitte Haskins & Sells) v Anderson and Ors* (1995) 37 NSWLR 438, cited.

(3) In determining whether a collateral or relevant purpose existed for purposes of tax deductibility it is necessary that the taxpayer establish that such a purpose existed in the course of a year of income, rather than being required to demonstrate that the purpose existed throughout the whole of the year. 42 ATR 1072

**Application**

This was an application to set aside a decision of the IRDB that certain activities conducted by the taxpayer were not research and development.

## Counsel

A H Slater QC and M Richmond instructed by Allen Allen & Hemsley for the applicant.

D Yates SC and I Harvey instructed by Blake Dawson Waldron for the respondent.

JOEL BUTLER

# Judgment - B J McMahon, Deputy President.

**B J McMahon, Deputy President.**

This is an application brought pursuant to s 39T of the *Industry Research and Development Act 1986* (Cth) to review a decision of the respondent which had been confirmed under s 39S.

**[2]** The applicant is a major Australian bank. Because s 39T(4) requires that the hearing of this proceeding take place in private, I am not permitted to indicate which bank. The size of the applicant corporation, however, is an important factor and will be referred to later in these reasons. It is sufficient to note at this stage that by Australian standards, it is a very large company. According to annual reports that were tendered in evidence, its group net profit during one of the years in question was approximately $380 million. It had many thousands of employees and a large number of branches.

**[3]** After lodging its income tax returns for the 1986, 1987 and 1988 years, the applicant requested the Commissioner of Taxation, pursuant to the former s 169A of the *Income Tax Assessment Act 1936* (Cth) (ITAA 1936) to consider whether certain expenditure claimed in specified schedules to those tax returns for the period 1 July 1985 to 27 November 1987, was research and development expenditure within the meaning of s 73B of the ITAA 1936.

**[4]** That section introduced availability of a deduction of 150% of expenditure which was found to be eligible research and development expenditure. The government announced its intention of introducing this concession in July 1985 in general terms. The Bill to give effect to that announcement was not, however, introduced until May 1986, Income Tax Assessment Amendment (Research and Development) Bill 1986 (Cth). It was enacted in June 1986, *Income Tax Assessment Amendment (Research and Development) Act Act 1986* (Cth), with retrospective effect to 1 July 1985. The broken period referred to in the preceding paragraph commences with the operative date of s 73B and concludes with the date of its repeal on 27 November 1987 and its replacement, in part, by another Act, *Taxation Laws Amendment Act 1988* (Cth) setting out slightly different criteria to be met in order to achieve eligibility for the deduction. From the date of the announcement in July 1985 until the introduction of the Income Tax Assessment Amendment (Research and Development) Bill 1986 to Parliament in May 1986, the exact terms upon which the concession was to be made available were not known publicly.

**[5]** On 6 September 1990, the Deputy Commissioner of Taxation requested the respondent to make a determination "whether those activities constitute research and development activities for the purpose of s 73B of the Act". Although it was not spelt out, the request was authorised by s 73B(34) which was in the following terms:

73B(34) For the purposes of making an assessment of the taxable income of an eligible company of a year of income, the Commissioner may, by notice in writing given to the Board, request the Board to determine in writing whether particular activities carried on by or on behalf of the company during the year of income were research and development 42 ATR 1073 activities and, where such a request is given to the Board, the Board shall comply with the request.

**[6]** It will be noted from the terms of this subsection that the Board's task was to determine whether the activities carried on "during the year of income" were research and development activities. The use of the phrase "during the year of income' raises questions whether activities must qualify during the whole of the year or from time to time and, in the latter event, whether the period during the year of income in which activities qualified as research and development activities has to be a significant part of that particular year.

**[7]** Pursuant to s 39L of the *Industry Research and Development Act 1986* (Cth), the respondent, by its delegate the Tax Concession Committee, determined and certified to the Deputy Commissioner of Taxation that in respect of the relevant period "the development of [the project] does not comply with the definition of research and development in the Act".

**[8]** Both "research and development expenditure" and "research and development activities" are defined in s 73B(1). Broadly speaking, qualifying activities are those that are systematic, investigative or experimental activities that involve innovation or technical risk and meet other qualifications of the subsection. During the relevant period, the applicant was developing computer software (the project) which was intended to be an information processing system for use in any environment demanding high volume, high throughput transaction processing and ongoing product development. There was no dispute that the project would have complied with the requirements of the definition of "research and development activities" were it not for one of the exceptions to be found in s 73B(2).

**[9]** This is in the following terms:

73B(2) For the purposes of the definition of "research and development activities" in subsection (1), activities that are carried on by way of -

(a) market research, market testing or market development, or sales promotion (including consumer surveys);

(b) quality control;

(c) prospecting, exploring or drilling for minerals, petroleum or natural gas for the purpose of determining the size of quality of any deposits;

(d) the making of cosmetic modifications or stylistic changes to products, processes or production methods;

(e) management studies or efficiency surveys;

(f) research in social sciences, arts or humanities;

(g) the development of computer software otherwise than for the purpose of sale, rent, licence, hire or lease, or

(h) the making of donations,

shall be taken not to be systematic, investigative or experimental activities.

Although some attempt was made by the applicant to draw matters covered by the above paragraphs into specified categories, I have been unable to discern any connecting link between them. The 8 exceptions appear to have been arrived at haphazardly or at best with reference to the experience of the respondent in particular circumstances. Each of them involves the making of a separate value judgment in policy terms. I have not been able to derive any assistance in the interpretation of para (g) from a consideration of the terms of all the other paragraphs.

[10] The development of computer software, described in the first part of para (g), is excluded from compliance with part of the definition of research and development activities in that it is not to be taken to be a systematic, investigative or experimental activity. The remainder of para (g) constitutes an exception to an exception. What has to be decided, therefore, is whether the admitted development of computer software, which 42 ATR 1074 otherwise would have complied, is excluded from qualification by the terms of this paragraph or whether by establishing the existence of a relevant purpose, the applicant can bring itself within the exception to the exception.

[11] There are 3 principal questions to be determined. The first is the meaning of "purpose", appearing in para (g).

. The respondent contends that what must be shown is a dominant or actuating purpose. The respondent argued that the purpose of the applicant was to develop the project for the applicant's own internal needs. If there was another purpose of sale etcetera, it was merely incidental and was not the "ruling, prevailing or most influential purpose" driving the development.

. The applicant agreed (and the evidence supported its submission) that at all relevant times, the dominant purpose of the applicant in developing the project was to satisfy the applicant's own in-house requirements. However, it was the applicant's contention that the purpose requirement in the paragraph extended to any relevant purpose of sale etcetera that was not insubstantial and that such a purpose could exist side by side with a non-qualifying dominant purpose.

. The use of the definite article before the word "purpose" in para (g) may or may not support the respondent's argument that there can be but one purpose in considering the application of this paragraph, even though manifestly and from a commercial point of view, there may be more than one purpose and there may indeed be a multiplicity of purposes.

**[12]** The second matter to be considered is the way in which the applicant's purpose is to be discerned. It is, as I have said, a large company with a largely non-executive Board of Directors, a Board executive committee and a structured system of management. To what extent is the purpose of any of the managers the purpose of the bank? Formal records of Board involvement in the development of the project are not conclusive. It will be necessary to consider what evidence there is to support any imputed corporate purpose.

[13] The third matter for consideration having established the legal framework is to examine the voluminous evidence before the tribunal to determine whether it supports a case for entitlement to the deduction in accordance with the construction of the paragraph which I must determine.

**[14]** For reasons which are not here relevant, the events upon which the applicant relies occurred between 12 and 14 years ago. Many of these events were conversations or rather, reconstructions of conversations. Naturally none of the witnesses (most of whom have retired from the bank's employment) were able to recall conversations in detail. Most relied upon impressions and recollections. Obviously, details of this nature would have faded from most memories were it not for the fact that the attentions of the witnesses have in recent times been focussed on these events for the purpose of these proceedings. That focus has included an examination of relevant documents to assist in their recollections.

[15] None of their oral evidence was seriously challenged and certainly no suggestion was raised as to the credit of any of the witnesses. Nevertheless, I consider it unsafe to rely upon reconstructed conversations of such an age and propose to take account of them only when corroborated by contemporaneous documents. Counsel for the applicant sought to distinguish between remembrance of a purpose and remembrance of conversations relating to that purpose. To my mind, this is a distinction without a difference.

**[16]** Before examining the factual evidence, however, it is necessary to settle the legal framework within which that evidence is to be assessed. I therefore turn to a consideration of the meaning of "the purpose" in para (g). 42 ATR 1075

**[17]** The respondent submitted that in considering the notion of "purpose" one should ask why was the development activity undertaken. I was referred to the discussion of the nature of an operative purpose in *Tillmanns Butcheries Pty Ltd v Australasian Meat Industry Employees' Union* (1979) 42 FLR 331 at 349. It

was submitted that this concept was equivalent to the notion of a dominant or actuating purpose as discussed in *Evans v FCT* (1936) 55 CLR 80 at 99 and *FCT v Spotless Services Pty Ltd* (1996) 186 CLR 404 at 416; 34 ATR 183 at 188; 96 ATC 5201 at 5206. An operative purpose, the respondent submitted, is to be distinguished from an appreciation that conduct might have a specified effect. The latter does not translate into the purpose for which the relevant conduct was engaged in. One does not look at the effect, it was submitted, but rather at the actuating reasons for the activity. The respondent submitted that one should look to the real reason why something was done or not done and to what was in truth the object in the minds of the relevant persons when they engaged in the conduct. In support of this proposition the respondent referred to *Crofter Hand Woven Harris Tweed Co Ltd v Veitch* (1942) AC 435 at 444-445. From these general submissions the respondent proceeded to the conclusion that the words "the purpose" in the relevant paragraph must be sufficiently fixed or definite as to constitute the operative or dominant or actuating reason why something is done. It submitted that an appreciation or realisation or expectation may not, and generally will not, suffice.

**[18]** I found these general submissions of limited assistance for a number of reasons. They are based upon considerations and judicial discussion of different statutes and of legal situations in different legal contexts from those with which the present application is concerned. It is not to the point to consider what meaning was attributed to the word "purpose" in a different statutory context. The statutory provision in *Tillmanns* was a penal provision and not a relieving one as in the present case. The discussion in *Crofter* dealt with standards of proof to be applied in establishing torts in the nature of conspiracies. *Spotless Services* concerned the application of Pt IVA in circumstances where the ITAA 1936 itself prescribed a dominant purpose. From these particular situations, it seems to me, that general propositions, having application to the particular circumstances presently under consideration, are not available. It is clear as a currently accepted principle of interpretation that the meaning of any phrase is to be determined having regard to the context in which it appears (*CIC Insurance Ltd v Bankstown Football Club Ltd* (1997) 187 CLR 384).

**[19]** Not only must the context be taken into account but the purpose of the statute must, so far as possible, be effected by an available approach to interpretation. In this respect, it is important to note that the provision to be construed is an incentive and relieving provision, not one imposing tax or preventing avoidance, as was considered in *Spotless Services*.

**[20]** The authorities dealing with the correct approach to interpretation of provisions of this kind were collected in the applicant's written submissions as follows:

In *FCT v Murry* (1998) 39 ATR 129; 98 ATC 4585 Kirby J said at ATR 149, ATC 4599:

Provisions of this kind, affording relief to the taxpayer, have conventionally been treated as, to some extent, beneficial. It has been said that they "should not be narrowly construed and should be interpreted to promote the purpose or object underlying the relevant Act" *Piessey Australia Pty Ltd v FCT* (1989) 20 ATR 1538 at 1543; 89 ATC 5163 at 5168. See also *FCT v Top of the Cross Pty Ltd* and *Travel Holdings (Australia) Pty Ltd* (1981) 12 ATR 413 at 422; 81 ATC 4563 at 4571 [Bowen CJ and Ellicott J]; *Penrith Rugby League Club Ltd v Comr of Land Tax (NSW)* (1983) 2 NSWLR 616 at 622; (1983) 15 ATR 1 at 6-7; 83 ATC 4109 at 4714. Each case must depend upon its own statutory language and apparent statutory purposes. However, I do consider that the foregoing approach is the correct one. **42 ATR 1076**

Similar statements can be found in *Jetmaster Fireplaces Pty Ltd v FCT* (1989) 20 ATR 689 at 693-4; 89 ATC 4464 at 4468, *FCT v Reynolds Australia Alumina Ltd* (1987) 18 FCR 29 at 35, 46; 19 ATR 598 at 604, 614; 87 ATC 5018 at 5022, 5031, *FCT v Faywin Investments Pty Ltd* (1990) 22 FCR 461 per Bowen CJ and French J, and *Cronulla Sutherland Leagues Club Ltd v FCT* (1990) 23 FCR 82 at 109; 21 ATR 300 at 325; 90 ATC 4215 at 4237.

**[21]** It is true that these primary approaches to interpretation may be modified if a contrary intention appears in the legislation. I see no such intention in the paragraph under consideration. The relieving nature of the provision is not abated by the fact that the research was ultimately non-productive. It is not a requirement of the section that the product of the research be income-producing or that the research be carried out by a taxpayer conducting an income-producing business. There is no reason to imply a presumption that the research and development should be undertaken principally to produce something for sale. The fundamental thrust of the legislation is that activities with a necessary degree of risk, innovation and novelty will qualify for the incentive. In looking at the terms of the paragraph one should not take a narrow approach to construction (*Industry Research and Development Board v Unisys Information Services Services Australia Pty Ltd* (1997) 77 FCR 552; 37 ATR 62; 97 ATC 4848). Furthermore, a provision designed to encourage a class of activity should not be given a narrow application (*Diethelm Manufacturing*

*Pty Ltd v FCT* (1993) 44 FCR 450 at 457; 26 ATR 465 at 470-1; 93 ATC 4703 at 4708-9).

**[22]** The use of the definite article "the" does not, in my view, limit the approach that one should take to construing the meaning of the word "purpose". If "purpose" includes "collateral purpose", its meaning is not changed by a reference to it in this way. There is no reason, in any event, why the purpose must ordinarily be regarded as a dominant purpose in the absence of any consideration pointing to a desired contrary meaning (*FCT v Mount Isa Mines Ltd* (1991) 28 FCR 269 at 279; 21 ATR 1294 at 1302-3; 91 ATC 4154 at 4162).

**[23]** The strongest argument for the applicant's submission that purpose is not to be restricted to "dominant purpose" is, in my view, to be found within the context of the legislation. Elsewhere there are references to an exclusive purpose. For example, there are references to "exclusively for the purpose of" in ss (4), (5), (7), (15), (21), (23), (24), (28) and (31) of s 73B. In para (7)(b) there is a reference to "for that purpose and not ... for any other purpose". A reference to different degrees of purpose elsewhere in the same statute indicates to me that the unadorned use of the word in para (g) means that the word is left unqualified and that the inference properly to be drawn is that no qualification relating to sole, dominant or main is to be imputed. There is a presumption that unless the context indicates to the contrary, words used in the same section have the same meaning (*Clyne v DCT* (1981) 150 CLR 1 at 10; 12 ATR 173 at 178; 81 ATC 4429 at 4433). From the various subsections of the actual section under consideration, it is clear that Parliament was aware of the various contents the word "purpose" could have. The fact that para (g) was not cast in similar terms can not have been an oversight. The absence of the restrictive words indicates to me an intended broader approach to the meaning of "purpose".

**[24]** A further argument which I find persuasive is based upon logic. An application of the word in the way contended for by the respondent would bring about surprising **42 ATR 1077** results. In this respect, I adopt what was put in the written submissions of counsel for the applicant as follows:

If in the context of s 73B the expression "for the purpose of" (without further qualification) is always a reference to the "dominant", "main" or "major", or "real motivating" purpose, then

(a) In order to qualify as R&D activities within subs (1) definition, the activities must have the dominant, or main or major, or real motivating purpose of acquiring new knowledge, etc;

(b) they therefore cannot have the dominant, or main or major, or real motivating purpose of

(i) discovering minerals, etc (para (2)(c)), or

(ii) sale, rent etc (para (2)(g)),

as that purpose would displace the "dominant", "main" or "major", or "real motivating" purpose of acquiring knowledge, etc.

This would mean that para (c) was otiose - a conclusion a court will reach only with reluctance - and that para (g) was inherently contradictory, since expenditure which passed its test would thereby fail the definition satisfaction of which the purpose exception in para (g) seeks to preserve. This cannot be the correct conclusion.

It follows that in these provisions "for the purpose of" cannot always be a reference to the "dominant", "main" or "major", or "real motivating" purpose.

There is a further inherent difficulty in applying a dominant or main purpose requirement in s 73B(2)(g) as it envisages several eligible purposes, none of which may be dominant. It would be an odd result if a taxpayer's activities, directed to the development of software for the purposes of both sale and lease, in circumstances where neither was a dominant or major purpose, failed to satisfy s 73B(2)(g). An analogy may be drawn with the former definition of "trading stock" in s 6(1) of the ITAA 1936, as to which Mason CJ, Wilson, Dawson, Toohey and Gaudron JJ observed in *John v FCT* (1989) 166 CLR 417 at 430; 20 ATR 1 at 8; 89 ATC 4101 at 4107:

The definition of "trading stock", in speaking of the "purposes of manufacture, sale or exchange", clearly predicates that one such purpose shall attend the acquisition of the item in question. The definition does not require that the relevant purpose be the sole or even the dominant purpose.

The level of purpose required is that spoken of by Gibbs CJ in *Gulland v FCT* (1985) 160 CLR 55 at 67; 17 ATR 1 at 8; 85 ATC 4765 at 4772 in the context of s 260 (where there is no specification of dominant or incidental purpose):

... the avoidance of tax (by which I mean to include any of the purposes mentioned in s 260) need not be the sole purpose of the arrangement. In *Hollyock v FCT* (1971) 125 CLR 647 at 657; 2 ATR 601 at 606-7; 71 ATC 4202 at 4205-6, I respectfully dissented from the view ... that the avoidance of tax must be the sole or at least the principal purpose of the arrangement, although I considered that it would not be enough to justify the application of the section that tax avoidance was an inessential or incidental feature of the arrangement. ...

If tax avoidance is one of the main purposes of the arrangement in the sense that it is not inessential or merely incidental, that is enough.

His Honour took a similar approach to the construction of an unqualified requirement of "use" in the *Sales Tax (Exemptions and Classifications) Act 1935* (Cth) in *DCT (SA) v Stewart* (1984) 154 CLR 385 at 390; 15 ATR 387 at 391; 84 ATC 4146 at 4149:

No doubt an article would not fall within item 81 if the use to which it was to be put by the hospital or institution was transient or insubstantial; the suggestion in *FCT v Hamersley Iron Pty Ltd* (1981) 12 ATR 429 at 439; 81 ATC 4582 at 4590 that the goods must be for use to a "significant degree" would appear to be correct.

[25] Yet another reinforcing consideration favouring an unqualified interpretation of "purpose" is to be found in the extraneous material. Again, I am indebted to the written 42 ATR 1078 submissions of counsel for the applicant which put this argument as follows in terms which I adopt:

The Explanatory Memoranda to the Bills which introduced s 73B into the ITAA 1936 and subsequently amended it by the deletion of s 73B(2)(g) and the substitution of s 73B(2A) also support this view. The Explanatory Memorandum to the Income Tax Assessment Amendment (Research and Development) Bill 1986 (Cth), which introduced s 73B into the ITAA 1936, does not suggest that "purpose" in former s 73B(2)(g) was intended to mean dominant or main purpose. The only relevant part of the Explanatory Memorandum is the following passage at p 16:

computer software development - the eligibility of software research and development which forms part of another research and development project will generally be dependent on the eligibility of that project being established. Provided the general definition in research and development activities is met, computer software developed for the purpose of sale, rent, licence, hire or lease to multiple clients may qualify. Routine computer programming or in-house software development would generally not satisfy the requirement.

It may be noted that s 73B(2)(g) does not in fact require the purpose of sale, etc to multiple clients as suggested by the Explanatory Memorandum. This deficiency in s 73B(2)(g) was remedied by the Taxation Laws Amendment Bill (No 5) 1987 (Cth) which repealed s 73B(2)(g) and substituted s 73(b)(2A). The Explanatory Memorandum to that Bill made the following comments relevant to this amendment:

The second of the announced proposals will amend the special concession for research and development expenditure so that the development of computer software that is not for sale, rent, hire, or licence or lease to two or more persons who are not associates of the developer will be excluded from the definition of "research and development activities" in s 73B of the Principal Act. At present only the development of computer software that is not for sale, rent, hire or lease to another person is excluded. The intention of this exclusion is that expenditure incurred in the development of computer software required only for "in-house" purposes should not be deductible.

It is clear from this passage that the intention of the amendment was to give effect to the original intention of the legislature that, in the case of computer software, a purpose of sale etc to multiple persons was required and that the amendment had nothing to do with the introduction of a new "purpose" requirement.

The purpose requirement in s 73B(2A) is expressed in a different manner from s 73B(2)(g). The new wording makes clear that the purpose requirement is not a dominant purpose.

The fact that s 73B(2)(g) was replaced by s 73B(2A) would only be relevant to the interpretation of s 73B(2)(g) if the words of that section were ambiguous: see *Allina Pty Ltd v FCT* (1991) 28 FCR 203 at 212; 21 ATR 1320 at 1328; 91 ATC 4195 at 4202-3. In our submission, the wording of s 73B(2)(g) is not ambiguous. Even if the section was ambiguous, the fact that s 73B(2)(g) was replaced by s 73B(2A) supports our submission as to the purpose requirement of the former section because there is nothing in the Explanatory Memorandum to the Taxation Laws Amendment Bill (No 5) 1987 which suggests that the legislature intended to change the purpose requirement in relation to the development of computer software.

**[26]** I have concluded, therefore, that the applicant need show a relevant purpose which was not insubstantial, even though it was not the applicant's dominant or actuating purpose. It would be rare that any commercial venture was undertaken with one sole and undeviating purpose in mind. The conclusion I have reached has the added advantage that it is consistent with commercial reality, a subject with which the legislation itself is concerned. Research and development is not carried out in a commercial vacuum. It is undertaken (as the definition makes clear) to acquire new **42 ATR 1079** knowledge or to create new or improved products etc. The acquisition of new knowledge may lead to developments in a direction entirely unanticipated at the commencement of the research. The products created may be different from those originally envisaged. Research follows the path which it creates. The purpose of research would normally change and develop as the course of research itself dictated.

**[27]** How was this purpose manifested? How am I to discern a corporate purpose in such a large and diverse corporation as the applicant?

**[28]** Decisions such as *Allied Pastoral Holdings Pty Ltd v FCT* (1988) 1 NSWLR 1 at 5; (1983) 13 ATR 825 at 829-30; 83 ATC 4015 at 4017, which attribute to a company a state of mind found in the person or persons who are really the directing mind and will of the company (or as his Honour Hunt J observed "the very ego and centre of the personality of the corporation") are of little assistance in cases of this nature.

**[29]** There is little in the evidence before me directly indicating through resolutions of the Board of Directors that this governing body was a party to each and every stage of the development of the project so that it might be said that it was done in the Board's name, reflecting the company's purpose. Most of the research and development activity relied upon was carried out under a plan originally approved by the Board, but effectuated by managers. I see no problem in attributing the intention of those managers to the company.

**[30]** In *Tesco Supermarkets Ltd v Nattrass* (1972) AC 153 at 170-171, Lord Reid said:

I must start by considering the nature of the personality which by a fiction the law attributes to a corporation. A living person has a mind which can have knowledge or intention or be negligent and he has hands to carry out his intentions. A corporation has none of these: it must act through living persons, though not always one or the same person. Then the person who acts is not speaking or acting for the company. He is acting as the company and his mind which directs his acts is the mind of the company. There is no question of the company being vicariously liable. He is not acting as a servant, representative, agent or delegate. He is an embodiment of the company, or, one could say, he hears and speaks through the persona of the company, within his appropriate sphere, and his mind is the mind of the company...

...

Normally the board of directors, the managing director and perhaps other superior officers of a company carry out the functions of management and speak and act as the company. Their subordinates do not. They carry out orders from above and it can make no difference that they are given some measure of discretion. But the board of directors may delegate some part of their functions of management giving to their delegate full discretion to act independently on instructions from them. I see no difficulty in holding that they have thereby put such a delegate in their place so that within the scope of the delegation he can act as the company.

**[31]** These observations were adopted by the High Court of Australia in *Hamilton v Whitehead* (1988) 166 CLR 121 at 127.

**[32]** If there has been a delegation to particular officers of the company, their actions and their intentions are equated with those of the company (*Daniels v Anderson* (1995) 37 NSWLR 438 at 576; 16 ACSR 607 at 731-2). Even if there has been no formal delegation but the decision making function is nevertheless

assumed by or, in fact, entrusted to identified officers of the company, it is the intention or purpose of those officers that is the intention or purpose of the company.

**[33]** I turn now to the evidence presented to the tribunal. There were 7 lever arch files of documents produced by the applicant by way of discovery. These were carefully examined and analysed by those representing the respondent. However, references were made only to certain selected documents in volumes 1 and 6. Particular reference was 42 ATR 1080 made to minutes of conversations, file notes and memoranda passing between various officers of the bank. The respondent relied upon folios 1, 12-15, 16-17, 26, 120-131, 132-135, 184, 187, 388, 2018 and 2235. From all of these documents, the respondent sought to show that development of the project was primarily for the bank's own purposes. As this was readily admitted by the applicant, and as I have concluded that "purpose" may include a collateral purpose, there is little assistance to be derived from documentary evidence of an admitted fact.

**[34]** Evidence was also given by written statement from a number of persons who (with one exception) were retired officers of the bank. Only one of the witnesses was still employed in that capacity. All of them save those whose evidence was of a more formal nature were cross-examined. None of this cross examination, however, led to any substantial divergence from the evidence as originally presented. The documentary evidence was useful not only to support recollections, but also to chart the course of the project to the stage when the purpose of sale etcetera came into being. In fact, at the end of the day there was no real dispute on the evidence. The only argument which occupied most of the submissions turned upon the way in which the facts as presented should be interpreted in the light of the provisions of para (g). It is, therefore, possible to refer to this large volume of evidence in a somewhat abbreviated and summarised form.

**[35]** The contemporaneous documents show that the applicant embarked upon the project for the purpose of developing improvements to its way of carrying on business in the future. It had a need, which was referred to as a survival issue, to redevelop its computer system. It perceived that it needed to provide itself with a computer system of a kind which would replace its then systems (which it regarded as inflexible and antiquated, which could not be economically sustained and which could not be adapted to meet the challenges posed by deregulation) with one which it saw as being necessary not only to nurture, but to protect its core banking system from competition and which would sustain what the applicant saw as an inevitable evolution of its business which would move beyond its core banking business into other areas, including the supply of information services.

**[36]** The manager who was principally in charge of the project explained the envisaged area of utilisation outside of the applicant's core banking business. There was, for example, an area of information intermediation which could be covered by the system. Customers of the bank were customers of other organisations and governments. The servicing of programs such as loyalty programs seen today, could have been comprehended by the system if research showed that this was feasible.

**[37]** Other non-banking services could be made available. For example, one of the applicant's competitor banks now sells share broking services through the internet. The witness recalled that this was the type of service the applicant had in mind during the course of the project's development. Medibank was starting up at the time. His evidence was that the applicant tendered for the computer element of the program. In order to make this available, the design for the program had to be generic so that it could be broken down into modules and then reconstructed in accordance with the customer's requirements. Nevertheless he agreed that the prime motivation at the commencement of the project was to satisfy the bank's in-house requirements.

**[38]** This much is clear. However, as the project developed, its marketability to others became apparent. Third party marketing became more attractive as a prospect as the project developed. When it was commenced, the applicant had no idea of the final cost. These costs continue to escalate, however, to such an extent that serious consideration was given to cost recovery by way of third party marketing. The project was a high risk one. It involved the development of what was known as an integrated banking system. The evidence suggests that, at that time, no one had been able successfully to develop 42 ATR 1081 such a system. If the applicant were successful, then the software could be exploited commercially.

**[39]** After initial research project papers and subordinate developments, the overall project was reduced to a minute submitted to the Board for its approval. This was evidenced by a Board minute of 4 October 1985 setting budgetary limits. However within those limits, the evidence was the person whose budget was approved was authorised to determine the nature and extent of expenditure. The Board was kept informed of, rather than required to approve, undertakings within the authority of the chief general managers. This

was supplemented by a process of formal consultation and advice.

**[40]** In addition to the written material presented to the Board which was approved in the Board's formal resolution, there is a note of a presentation made at that meeting by the Chief Executive Officer. The contents of the presentation are not noted but, in his evidence, that officer recalled that the presentation occupied more than 3 hours.

**[41]** There was an executive committee which performed a communication and oversight role in relation to the activities of the chief general managers. By the time the matter was put to the Board, it had been thoroughly reviewed by the Board's own committee, whose recommendations were unlikely to be rejected.

**[42]** The evidence led before the tribunal demonstrates that the bank had at least a two-fold purpose in developing the project. The core system was, from the perspective of the bank's own operations, "a survival issue" but it also made sense to market the successfully developed software not only to other international banks (which the applicant at that time did not regard as competitors) but to other financial and non-financial organisations, among whom the decision-makers perceived that there was a market and need for such a system. The existence of the need and market shaped the structure of the system and was the background to the bank's choice of a development co-venturer.

**[43]** In my view, the limited formal involvement of the Board does not detract from the existence of a corporate purpose evidenced by the actions of those authorised by the Board to pursue the project. That purpose of marketing the system for sale or licence when it had reached the stage at which there was a marketable product was more than a merely incidental or insubstantial purpose of the decision makers and the bank. While the purpose of satisfying the bank's own needs was critical, and so it may be said to be the dominant purpose, there was a concurrent and substantial purpose involving an intention to market the product elsewhere.

**[44]** That purpose was amply demonstrated by contemporaneous documents distilled and highlighted in chronologies prepared for the purpose of this application and in the conversations of relevant officers, all of whom gave evidence and none of whose recollections were seriously challenged.

**[45]** From the outset, the system was designed at a level of generality beyond the needs of the bank's own business to make it generic and flexible enough to be adapted to other businesses. The bank's rights to a marketable system were protected. There were dealings with the bank's lawyers in the United States of America and with its suppliers and with its proposed co-venturer which could be explained only by reference to an intention to deal with the product outside the bank's own system.

**[46]** There was a joint marketing approach to American banks in late 1986 and the appointment of a marketing manager in 1987. Although the period in question commences on 1 July 1985 and concludes on 27 November 1987, the purpose evidenced by these events taking place during the relevant period is sufficiently shown in accordance with para (g) in my view. The purpose may not have existed at the commencement of the project. The fact that it arose and became a purpose of some **42 ATR 1082** substance during the relevant period and continuing for a substantial part of that relevant period is sufficient to qualify the expenditure.

**[47]** It is not possible to pinpoint the day upon which the ancillary purpose was formed. There is no egregious event to which one can turn and say here was the birth of the relevant purpose. It grew in the minds of senior officers as part of the bank's purpose over a period. All that is necessary for the applicant to show, however, is that the purpose existed "during" the relevant year of income. The 1 defines "during" in 2 ways which, in the present context, may be inconsistent. The first meaning given is "throughout the continuance of". The second meaning is "in the course of". It seems to me that the second meaning is to be preferred.

**[48]** It is the act of research or development for which expenditure is incurred which gives rise to the entitlement to the deduction. Common sense would seem to indicate that an applicant need not be involved in such activities on each of the 365 days of the year of income. If any research and development were carried out at all on any day or any number of days, and expenditure was incurred for that purpose, then the test would be met. Consequently, it seems to me that it is not necessary to show that the relevant purpose in para (g) was in existence throughout the whole of the period from 1 July 1985 to 27 November 1987. If it existed in the course of that period for however long or short a time, the Board would be bound by s 73B(34) to find that the activities were research and development activities for the relevant income year. To some extent, I was dependent upon undocumented recollections in determining when the relevant

purpose came into being.

**[49]** I am conscious of the fact that evidence of an applicant through its officers as to the applicant's own purpose must be received and tested cautiously. Nevertheless, the objective facts and corresponding documents (all of which were largely unchallenged) lead me to accept their affirmation of the applicant's purpose as a collateral or subsidiary but, nevertheless, substantial purpose, in accordance with para (g).

[50] Evidence was given by the man who was managing director at the relevant time. He was also a member of the Board. His unchallenged evidence supported those of his general managers as to the establishment of the existence of a potential market among overseas banks which would not be regarded as competitors to the applicant but which had similar problems and no corresponding solution. Contacts were made continually on an informal basis and prior to the relevant board meeting, on a formal basis. A particular general manager was the executive to whom the Board delegated decision making power in the information technology area subject only to control through budgetary limits as to the spending and the value of assets realised. As a result of discussions with other banks in similar non-competing positions, he formed the view that they would be interested in purchasing any system which the applicant successfully developed. He repeated on a number of occasions his intention, and the applicant company's consequent intention, of realising a benefit from the product of the project (a costly exercise) by marketing the system and its components. I have no reason to reject that evidence. He recognised that there had to be a marketable product before any marketing program could be commenced. In fact, no sales arose out of this research and development and the project was ultimately abandoned. That fact, however, has no bearing on whether the activities in respect of which the deduction is sought, qualified under the relevant paragraph. The deduction is available whether or not research and development was successful and whether or not it led to the development of commodities or systems which were ultimately sold etcetera.

[51] Other officers gave evidence which can be viewed only as supporting the evidence of the chief general manager as to corporate purpose. Evidence was given by other officers ranking below the general managers. Their evidence was useful, however, 42 ATR 1083 by way of corroboration of the corporate purpose of the decision makers. For example, one of the officers was not only told of the aim to market the system, he was also directed to take steps to protect the applicant's position from adverse claims, both by way of infringements of other rights and claims of infringement of the applicant's, and to watch the relationship with the proposed co-venturer for the same purpose. These instructions and the actions of this officer pursuant to those instructions are consistent only with an intention to capitalise on the software and not restrict its use only to the bank's purposes.

**[52]** Another officer at a subordinate level gave evidence that the instructions given to him as a programmer were to construct a set of programs at a level of generality which exceeded that necessary if the system were to be developed only for the specific needs of the applicant and was consistent only with an intention and purpose of making the system available for marketing for other institutions. This officer also received specific instructions as to the purpose for which the system was being developed, including a purpose of building a marketable product. These instructions were given as part of his introduction to the tasks he was to undertake. If these understandings on the part of subordinate officers were the only bases upon which the applicant argued that there was a sufficient corporate purpose then, of course, it would fail. The fact that a relatively junior employee harboured a firm belief that the project, if successfully carried out, would result in some computer software product that might be capable of being marketed to a third party, is not, of itself, to the point. It is, however, an added dimension to the evidence given by more senior officers and assists in giving credibility to events of long ago when those firm beliefs are attested by contemporaneous written records.

**[53]** In the light of this evidence, I am satisfied that the applicant had the requisite purpose, that the purpose could not be denigrated as consideration of a mere possibility, that the purpose was a substantial purpose and not marginally peripheral and that the purpose existed during, and for a substantial time during, the relevant period. Accordingly, in my view, the applicant is entitled to the deduction which it seeks.

**[54]** The decision under review is therefore set aside and the matter is remitted to the respondent with a direction that the activities in question constitute research and development activities for the purpose of s 73B of the *Income Tax Assessment Act 1936* (Cth).