



HIGH COURT OF AUSTRALIA

1 June 2011

THE COMMISSIONER OF TAXATION OF THE COMMONWEALTH OF AUSTRALIA v BHP BILLITON LIMITED & ORS

[2011] HCA 17

Today the High Court dismissed appeals by the Commissioner of Taxation against the decision of the Full Federal Court of Australia regarding the construction of s 243-20(2) of the *Income Tax Assessment Act 1997* (Cth) ("the Act"). The Court held that a debt owed by BHP Billiton Direct Reduced Iron Pty Ltd ("BHPDRI") to BHP Billiton Finance Limited ("Finance") was not a "limited recourse debt" and therefore the respondents were not liable to an increase in assessable income under Div 243 of the Act.

BHP Billiton Ltd ("BHPB") is a listed company and its directly or indirectly wholly owned subsidiaries include Finance and BHPDRI. Finance raised, for the purposes of the BHPB group, large sums of money which it loaned to other members of the BHPB group on terms adopted by board resolution and which did not purport to limit the rights of Finance as an unsecured creditor. Finance earned a profit from the interest rates charged on loans to other members of the BHPB group.

BHPB's board approved the construction of plant and facilities near Port Hedland in Western Australia for the manufacture of iron briquettes to be undertaken by BHPDRI. BHPDRI was partly funded by a loan provided by Finance on its standard terms. Further capital expenditures required to complete the project were partly funded by advances by Finance which were subsequently partly written off by Finance. The project was not successful and terminated in May 2005.

The expenditure which BHPDRI incurred on the project gave rise to "capital allowance" deductions claimed by BHPDRI for the years 1996-2002 and by BHPB for the years 2003-2006. In 2007, the Commissioner issued a notice of assessment applying Div 243 of the Act to reduce the capital allowance deductions claimed by BHPDRI for the years 2003-2006. BHPDRI transferred its tax losses in the years 2000-2002 to other companies in the BHPB group ("the transferees") and the Commissioner's adjustments resulted in reductions to those transferred amounts which was reflected in assessments issued to the transferees.

BHPB's objection to the Commissioner's assessment was disallowed. BHPB and the transferees appealed to the Federal Court. The primary judge held that limited recourse debt was not used wholly or partly to finance or refinance BHPDRI's expenditure so that Div 243 did not apply. The Full Court dismissed the Commissioner's appeal. The Commissioner appealed, by special leave, to the High Court.

The Act provides, *inter alia*, that Div 243 applies if limited recourse debt has been used to wholly or partly finance or refinance expenditure. The dispute between the parties was whether limited recourse debt had been used.

One definition of "limited recourse debt" is found in s 243-20(2). Section 243-20(2) provides that an obligation imposed by law on a debtor to pay an amount to the creditor is limited recourse debt if it is reasonable to conclude that the rights of the creditor as against the debtor in the event of default in payment of the debt or interest are "capable of being limited" in the way mentioned in s 243-20(1) having regard to certain specified matters. It was the operation of this definition which was argued in the High Court.

The Commissioner argued that BHPDRI's debt to Finance was a "limited recourse debt" under s 243-20(2) of the Act. The Commissioner contended that s 243-20(2) of the Act was not concerned with current contractual limitations or rights or with economic equivalence but was concerned with a practical capacity or ability to bring about legal limitations on legal rights. The Commissioner also argued that Finance's contractual rights at the inception of each loan were "capable" of restriction should BHPDRI default because the parties were not dealing at arm's length.

The High Court held that BHPDRI's debt to Finance was not a "limited recourse debt" within the meaning of Div 243. The Court held that s 243-20(2) is not directed to possibilities for limitation of a creditor's rights of recourse which may arise in the future.

- *This statement is not intended to be a substitute for the reasons of the High Court or to be used in any later consideration of the Court's reasons.*