

IN THE HIGH COURT OF AUSTRALIA
SYDNEY REGISTRY

No. S134 of 2016

BETWEEN:

BYWATER INVESTMENTS LTD
CHEMICAL TRUSTEE LTD
DERRIN BROTHERS PROPERTIES LTD
Appellants

and

COMMISSIONER OF TAXATION
Respondent



10

APPELLANTS' SUBMISSIONS

20

Part I:

1. This submission is in a form suitable for publication on the internet.

Part II:

2. Whether *central management and control* in the definition of *resident or resident of Australia* in relation to a company in section 6(1) of the *Income Tax Assessment Act 1936* (Cth) (**1936 Assessment Act**) is where the lawful organs of the company control its activities or where an outsider gives those organs directions and instructions.

Part III:

- 10 3. The appellants certify that, by their lawyers, they have considered whether notice should be given in compliance with s 78B of the *Judiciary Act 1903* (Cth) and have concluded that no such notice should be given.

Part IV:

4. The Full Court of the Federal Court (Robertson, Pagone and Davies JJ) decision is reported as (2016) 329 ALR 385; (2015) 2015 ATC 20-549. The medium neutral report is [2015] FCAFC 176 (**AJ**).
5. The Primary Court (Perram J) decision is reported as (2014) 2014 ATC 20-480. The medium neutral report is [2014] FCA 1392 (**PJ**).

Part V:

- 20 6. Each of Bywater Investments Ltd, Chemical Trustee Ltd and Derrin Brothers Properties Ltd (**Bywater, Chemical and Derrin**) was incorporated abroad: PJ [404], [405], [410] and [411]. Derrin and Chemical were incorporated in the United Kingdom and found to be resident there: PJ [421]. Bywater was incorporated in the Bahamas: PJ [411]. The appellants' ultimate parent companies were two Cayman Islands entities, JA Investments Ltd and MH Investments Ltd (**JA Investments** and **MH Investments** respectively and together **JA and MH Investments**). JA and MH Investments held their interests in the shares in the appellants through interposed entities.
- 30 7. Peter Borgas was a director of each appellant from 1998. He was resident in Switzerland where he conducted his business. He was the sole shareholder of JA and MH Investments. Mr Borgas executed all documents by which the appellants engaged in business. He did this by signing letters of instruction in his capacity as director: PJ [65] & [66]. The memorandum and articles of association of each appellant vested the directors with corporate authority. This was done directly in

the case of *Bywater*¹ and, in the case of *Derrin and Chemical*, through the incorporation of the standard articles in the First Schedule of the *Companies Act 1948* (UK).²

8. A third party, Mr Gould, had no formal place in the corporate structure or activities of the appellants. However, as set out at PJ [70] to [80], JA Investments' articles of association gave the appointor the power to appoint additional members (Article 3) and allowed members to remove (Article 43) and appoint (Article 24) directors. The Primary Judge found that Mr Gould was the appointor of JA Investments: PJ [79]. As a consequence of this finding, and the finding that payments from JA Investments supported organisations to which Mr Gould wished to provide financial assistance, Mr Gould was found to be the *true owner* of JA Investments: PJ [110]. The Primary Judge reached the same conclusion in relation to MH investments: PJ [117].
- 10
9. The findings of the relationship between Mr Gould and Mr Borgas call for careful examination in the context of Mr Gould's role as appointor. While the primary judgment includes various findings that Mr Borgas implemented Mr Gould's instructions, e.g. PJ [339], the primary judgment did not make any finding that Mr Gould had any power lawfully to require Mr Borgas make a decision, or exercise any powers as a director in a particular way, or that Mr Borgas was Mr Gould's agent, or that any of the transactions in question was a sham: PJ [406]. A sham has never been alleged by the respondent.
- 20
10. Mr Borgas's evidence that he was the owner of the appellants was rejected: PJ [97]. That finding, and the finding that Mr Borgas had no economic interest in the appellants, led the Primary Judge's to infer that Mr Borgas made no decisions on behalf of the appellants: e.g. PJ [151].

Part VI:

SUMMARY OF ARGUMENT

11. This matter concerns statutory construction of the definition *resident or resident of Australia* in s 6(1) of the 1936 Assessment Act and, therefore, calls for examination of the text, context and purpose of the statute.³ The relevant text is:
- 30

¹ AB (Appeal book reference to be inserted) Memorandum and Articles of Association, *Bywater*, Article 66.

² AB (Appeal book reference to be inserted) Articles of Association, M&N Securities Ltd (now *Derrin*), Article 20 and Table A of the *Companies Act 1985* (UK) s 70; Articles of Association, Raybell Properties Ltd (now *Chemical*), Article 1 and First Schedule of the *Companies Act 1948* (UK), s 80.

³ See *Military Rehabilitation and Compensation Commission v May* [2016] HCA 19 (11 May 2016) at [10] (French CJ, Kiefel, Nettle and Gordon JJ) and the cases there cited.

"resident or resident of Australia" means:

...

(b) a company which ... not being incorporated in Australia, carries on business in Australia, and has either its central management and control in Australia, or its voting power controlled by shareholders who are residents of Australia.

12. Within this definition, only the concept of *central management and control* is in issue. The dispute concerns the appropriate test to determine where a company's central management and control is located.
- 10 13. The appellants contend that the test for a company's central management and control looks to where the company's organs lawfully and regularly exercise their authority. Ownership and owners' directions or instructions to directors are a distraction. They are a distraction for three reasons: first, the authorities are to that effect; second, the words used in the definition create alternative tests, one test looks to central management and control and the other looks to the residence of shareholders with controlling voting power; and third, because the statute as a whole does not make ownership relevant to the central management and control test, rather the statute deals with income and profits of foreign companies that are controlled by Australians in other ways under the controlled foreign corporations provisions.
- 20 14. This Court's decisions, and those of United Kingdom courts, require a finding for the appellants. A company is controlled by its lawfully appointed board of directors. The test for where *central management and control* is located requires a focus on the lawful organs of a company. There is a distinction between the decisions of an economic owner of a company and those of directors.
15. This case is outside those United Kingdom decisions that have accepted that it is permissible to look to an organ exercising control in place of the board where a board stands aside or is by-passed. It might also be possible, that a third party could constitute a company's central management and control if vested with the power to control the directors to act in a particular way or to dictate particular decisions, but that is not a matter arising on the facts of the present case.
- 30 16. The Primary Judge's findings about the conduct of Messrs Borgas and Gould require the conclusion that the appellants' central management and control was exercised by Mr Borgas, outside Australia, in Switzerland.

THE TEXT OF THE STATUTE

17. The s 6(1) definition is set out above.
18. The critical phrase in the statutory test for residence of a company adopts and concepts deriving from decisions in the United Kingdom, in particular the passage from *De Beers*⁴ that:

*[A] company resides for purposes of income tax where its real business is carried on... and the real business is carried on where the central management and control actually abides.*⁵

19. Matters which are especially pertinent to the determination of the place of central management and control are the places of incorporation and registered office,⁶ the places of residence of directors and directors' meetings,⁷ and the provisions of the Constitution of the company regulating the lawful exercise of the functions and activities of the company. Weight must be given to each of such features, depending on the circumstances of the case.⁸ The analysis required is one of fact and degree.⁹ In the present case, the location of the appellants' central management and control falls to be considered in circumstances where every relevant feature was located outside Australia. See [6] and [7] above.

This Court's authorities

20. *Esquire Nominees*,¹⁰ *Koitaki*¹¹ and *North Australian Pastoral*¹² direct the analysis of a company's central management and control to the location of the body which is lawfully vested with the authority to exercise that control. In the case of the present companies, as with most companies, that authority was vested in the board of directors.
21. In *Esquire Nominees* the Court considered the circumstances of companies acting consistently with directions or instructions of persons who were not vested with power under the companies' constitutions. In dealing with these circumstances, Gibbs J distinguished between an external body having the power to control directors in the exercise of their voting rights and the power to remove those

⁴ *De Beers Consolidated Mines Limited v Howe* [1906] AC 455.

⁵ *De Beers* at [1906] AC 458 (Lord Loreburn L.C.).

⁶ *Koitaki Para Rubber Estates Limited v F. C. of T.* (1941) 64 CLR 241 at 248.9 (Williams J).

⁷ *Esquire Nominees v F. C. of T.* (1973) 129 CLR 177 at 190.2 to 190.4 (Gibbs J).

⁸ *Re Little Olympian Each Ways Ltd* [1994] 4 All ER 561 at 569 g-j (Lindsay J).

⁹ *Esquire Nominees v F. C. of T.* (1973) 129 CLR 177 at 190.2 (Gibbs J).

¹⁰ *Esquire Nominees v F. C. of T.* (1973) 129 CLR 177.

¹¹ *Koitaki Para Rubber Estates Limited v F. C. of T.* (1940) 64 CLR 15 and (1941) 64 CLR 241.

¹² *North Australian Pastoral v F. C. of T.* (1946) 71 CLR 623.

directors for failing to comply with directions.¹³ His Honour rejected the Commissioner's submission that power to influence or remove directors from office constituted central management and control.¹⁴

22. Gibbs J's reasoning depends on, and gives effect to, the principle that a company acts through its lawfully appointed board of directors. His Honour's observations that the directors would have refrained from acting improperly,¹⁵ and were not compelled to act under the instructions of a third party¹⁶ do not create an exception to the principle that a company acts through its officers. Rather, these observations were a reflection of that principle, and an acknowledgment that a company's officers were empowered by and constrained by the company's constitution.
23. If the reasoning in *Esquire Nominees* extends the idea of central management and control to include third parties vested with the power to control the directors to act in a particular way or to dictate particular decisions,¹⁷ the present case requires a distinction between the power Mr Gould was found to have (to replace Mr Borgas) and what he was not found to have (namely any further power to control Mr Borgas in the exercise of his duties, whether through contract or other means). If there is an exception to the rule that a company acts through its lawful officers, then it must be limited to circumstances where a board is controlled by a third party with power of that kind.
24. The Primary Judge and Full Court applied the wrong test to determine the appellants' places of residence and wrongly rejected the Part IVC appeals.
25. The Full Court purported to distinguish *Esquire Nominees* on the basis that it was [*c*]ritical to the outcome in that case, ... those exerting influence, albeit strong influence, were not those making the decisions of the company: AJ [8]. This distinction finds no basis in the judgments delivered by the Court, at first instance and on appeal, in *Esquire Nominees*.
26. *Esquire Nominees* concerned a chain of Norfolk Island companies transacting a round robin of funds with no commercial purpose other than to avoid an expected tax burden.¹⁸ It was a contrived structure designed, overseen and managed by the companies' Australian accountants for the benefit the ultimate owners of the group of entities (the Manolas Trust). The steps served no commercial purpose for any company or trust in the chain. Although the directors of *Esquire Nominees Ltd*

¹³ *Esquire Nominees* at 129 CLR 191.1 – 191.2 (Gibbs J).

¹⁴ *Esquire Nominees* at 129 CLR 190.4 – 191.5 (Gibbs J).

¹⁵ *Esquire Nominees* at 129 CLR 191.4 (Gibbs J).

¹⁶ *Esquire Nominees* at 129 CLR 191.2 – 191.3 (Gibbs J).

¹⁷ *Esquire Nominees* at 129 CLR 191.2 – 191.3 (Gibbs J).

¹⁸ *Esquire Nominees* at 129 CLR 181.8 – 186.8 (Gibbs J).

may properly have been guided by the interests of the beneficiaries of the Manolas Trust (of which it was trustee), the same could not be said for the directors of Mitchell Credits Ltd or Pharmaceutical Investments Ltd. They cannot (as the Full Court suggested at AJ [8]) have properly made decisions guided by *the interests of the beneficiaries to give effect to the scheme* as those interests were irrelevant to their duties as directors. The only sensible explanation for the directors' decisions was that they were following instructions from the accountants who developed the scheme.¹⁹ The external accountants prepared detailed agendas of the directors' meetings and advised those directors in detail of the manner in which the scheme ought to be carried out.²⁰ What happened was clear. The directors of each company did what they were told.

10

27. The first error in the Full Court's reasoning at AJ [8] was its implicit premise that a third party can make decisions of a company. It reflects a view advanced by the Commissioner to the Primary Judge that *Mr Borgas was the director of the [appellants] and he needed to make the actual decisions as a matter of formality*: PJ [129]. To say that a director's involvement in the affairs of is *a matter of formality* is to ignore reality. Without Mr Borgas' decision to enter a transaction, no transaction can take place. Mr Borgas' decision is therefore critical, not as formality but as a matter of fact or reality.

20

28. The second error in the Full Court's reasoning at AJ [8] is that, contrary to the passage extracted at [25] above, Gibbs J's reasoning makes no mention of decision-making. His Honour instead focuses on the critical importance of the ability to control the directors in either the exercise of their powers or their voting rights.²¹ In the absence of any finding that Mr Gould could control Mr Borgas in the exercise of his voting rights, the Full Court ought to have found that Mr Borgas controlled the appellants as their lawful director.

30

29. The Full Court below upheld the reasons of the Primary Judge on the basis that his Honour *referred to the authorities bearing upon the issue in question, including the decision in Esquire Nominees* (AJ [11]). Although strictly true, PJ [399] to [402] show that the Primary Judge rejected the appellants' reliance on *Esquire Nominees* as *fanciful*, on the basis that the entities in *Esquire Nominees* were corporate trustees. The Primary Judge incorrectly rejected the appellants' reliance on *Esquire Nominees* for three reasons.

30. First, the Primary Judge's conclusion that Gibbs J's decision separated out the company's role as trustee from its personal role ignores the fact that the company's

¹⁹ *Esquire Nominees* at 129 CLR 181.6 – 186.8 and 183 (Gibbs J).

²⁰ *Esquire Nominees* at 129 CLR 190.5 – 190.7 (Gibbs J).

²¹ *Esquire Nominees* at 129 CLR 190.10 – 191.3 (Gibbs J).

10 role as a trustee was its business²² and, as such, it took direction in what it did in relation to its business. Second, and related to the first, Gibbs J did not differentiate between the central management and control of Esquire Nominees Ltd, which was a trustee, and Mitchell Credits Ltd or Pharmaceutical Investments Ltd which were not. Each company participated in one arrangement, took the same direction from the same source and all were found to reside in Norfolk Island. On appeal, Barwick CJ²³ noted that both Mitchell Credits Ltd and Pharmaceutical Investments Ltd were incorporated and centrally managed and controlled in Norfolk Island. Menzies J²⁴ accepted the Norfolk Island residence of Esquire Nominees Ltd and Mitchell Credits Ltd, and Stephen J²⁵ held that Mitchell Credits Ltd and Pharmaceutical Investments Ltd were residents of Norfolk Island. Third, it is a material misstatement of the reasons of the Full Court of the High Court to say, as the Primary Judge did at PJ [393], that *[a]lthough the ... decision of Esquire Nominees went on appeal to a Full Court the issue of residency was not in issue in that appeal (although Barwick CJ referred to it in passing)*. The Chief Justice expressed unreserved endorsement of Gibbs J's²⁶ conclusion and Menzies J²⁷ was to like effect. Stephen J's findings of residence²⁸ reflected those made by Gibbs J.

20 31. At AJ [7], the Full Court also considered the first instance and appeal decisions in *Koitaki*.²⁹ The Full Court relied on the observations of Dixon J³⁰ that a factor involved in the determination of residence is the *superior or directing authority by means of which the affairs of the company are controlled*. It also relied on what Williams J (with whom the other members of the Court relevantly agreed) said in the appeal: *But the crucial test is to ascertain where the real business of the company is carried on, not in the sense of where it trades but in the sense of from where its operations are controlled and directed. It is the place of the personal control over and not of the physical operations of the business which counts*.³¹ These authorities were said by the Full Court below at AJ [7] to support the conclusion that the focus of the test for residence is *where [a company's] activities are controlled from*. The authorities do not support the application of that test to look beyond the lawful organs of corporate control.

²² *Esquire Nominees* at 129 CLR 191.2 (Gibbs J) and 219.10 (Menzies J).

²³ *Esquire Nominees* at 129 CLR 208.3.

²⁴ *Esquire Nominees* at 129 CLR 220.3.

²⁵ *Esquire Nominees* at 129 CLR 225.10 -226.1.

²⁶ *Esquire Nominees* at 129 CLR 209.7

²⁷ *Esquire Nominees* at 129 CLR 220.3

²⁸ *Esquire Nominees* at 129 CLR 225.10 – 226.1.

²⁹ In particular, *Koitaki* at 64 CLR 19 and at 64 CLR 248-9.

³⁰ *Koitaki* at 64 CLR 19.

³¹ *Koitaki* at 64 CLR 248-9.

32. The *superior or directing authority* by means of which the affairs of the company are controlled (emphasis added) referred to by Dixon J³² directs attention to the lawful organs with authority to bind the company, namely its directors or board.³³ The language used by this Court has been consistent in this respect, *control* and *authority* each direct attention to a power to enforce one's will. They aptly describe a corporate board, which has complete dominion over the operation and affairs of a company. A decision made by that board is binding, enforceable and beyond appeal. In contrast, the decision of a third party *owner* may carry great weight in the minds of the directors, but until they decide to implement that decision, the decision is of no significance for the company.
- 10
33. The question of what constituted controlling authority was not considered by the Full Court of this Court in *Koitaki*. The passage that the Full Court below relied on from the reasons of Williams J (and extracted at [31] above) was clearly distinguishing between the place of manufacturing operations and the place of control;³⁴ in that case being the rubber estate in Port Moresby as compared with company's board and head office in Sydney.
34. The Full Court below did not refer to this Court's decision in *North Australian Pastoral*.³⁵ That decision even more clearly directs the inquiry towards the lawful organs of a company. Dixon J observed that the determination of central management and control does not require *a search to be conducted for the person or persons whose will is most likely to prevail in any matter affecting the company*.³⁶ These observations were made in the context of a claim that one director exercised greater control over the affairs of a company than the others. They have greater force where the contention is that a third party exercises that influence. Unlike a single director, who might have some limited (at least ostensible) authority to act and bind a company, a third party has no role to play in the affairs of a company. Dixon J quoted,³⁷ with apparent approval, the comments of Gibson J in *John Hood & Co v Magee*³⁸ that even *an unusually perfect specimen on a one-man company did not reside where that one man did, because he was not the company whether he controlled the business personally or through managers ... and agents* (emphasis added).
- 20
- 30

³² *Koitaki* at 64 CLR 19.4.

³³ See *Union Corporation Ltd v Inland Revenue Commissioner* (1952) 1 All ER 646 at 657G to 658A.

³⁴ *Koitaki* at 64 CLR 248-9.

³⁵ *North Australian Pastoral v F. C. of T.* (1946) 71 CLR 623.

³⁶ *North Australian Pastoral* at (1946) 71 CLR 628.2 – 628.3.

³⁷ *North Australian Pastoral* at (1946) 71 CLR 628.3 – 628.8.

³⁸ *John Hood & Co Ltd v Magee* (1918) 7 Tax Cas. 327 at 346 and 350.

35. The submission equally applies to the decision of Williams J in *Malayan Shipping*.³⁹ There, the Court was faced with a managing director who executed each of the company's contracts on behalf of the company in Australia, before sending them to Singapore to be executed by a nominee director.⁴⁰ The managing director was empowered by the articles to contract on behalf of the company, and to vote on the decision to enter the contract – indeed without his vote the contract could not be executed by the company.⁴¹ The managing director's lawful dominion over the affairs of the company was sufficiently overbearing that the point appears to have been conceded by counsel for the appellant taxpayer company.⁴²
- 10 36. On the authorities of this Court, there is no place for Mr Gould in the affairs of the appellants. Mr Borgas decided to execute every transaction on behalf of the appellants and did so.

United Kingdom Authorities

37. Since the test for residence was introduced in Australia, authorities in this country and the United Kingdom have developed in a relatively consistent and interdependent way.
38. More recent decisions of the United Kingdom Court of Appeal have applied the test of central management and control to disputes involving the *place of effective management* test found in double taxation treaties. While aspects of those
20 decisions recognize the possibility of considering the actions of a third party in the affairs of a company in limited circumstances, they nonetheless decided that place by reference to the place where board of directors conducted the business of the company.
39. The analysis begins with the *De Beers* decision, and the critical passage extracted at [18] above.
40. In *Union Corporation*,⁴³ the taxpayer had a board of directors divided between two countries. A minority resided in South Africa, but on matters of policy, supremacy rested with the board in London.⁴⁴ In determining that central management and control was in London, the Court⁴⁵ adopted the reasons of both Dixon and
30 Williams JJ in *Koitaki*, and held that the real business test was directed towards

³⁹ *Malayan Shipping Co Ltd v Federal Commissioner of Taxation* (1946) 71 CLR 156.

⁴⁰ *Malayan Shipping* at 71 CLR 157.10 – 158.6.

⁴¹ *Malayan Shipping* at 71 CLR 160.6.

⁴² *Malayan Shipping* at 71 CLR 158.9

⁴³ *Union Corporation Ltd v Inland Revenue Commissioner* (1952) 1 All ER 646.

⁴⁴ *Union Corporation* at (1952) 1 All ER 654C (Sir Raymond Evershed MR, Jenkins and Hodson LLJ).

⁴⁵ *Union Corporation* at (1952) 1 All ER 658A and 661H.

the controlling authority, *which according to the ordinary constitution ... is vested in the board of directors.*⁴⁶ The Court found that the board remained the controlling authority, notwithstanding its decision to delegate substantial functions to a local manager who, through a power of attorney, had *the widest powers and responsibility.*⁴⁷ Thus, even where a board delegates its authority, it retains central management and control.

- 10 41. After *Union Corporation*, the House of Lords and the Court of Appeal considered allegations that a company acted other than through its board of directors in three decisions: *Bullock*,⁴⁸ *Wood v Holden*,⁴⁹ and *Smallwood*.⁵⁰ At AJ [9], the Full Court below relied on these decisions to suggest that *Esquire Nominees* required a distinction between *influencing* decision making and *usurping* or *directing* decision making.
42. *Bullock* involved an exception to the true rule from *De Beers*. The lawfully appointed directors of the taxpayer *stood aside* and no longer functioned as a board.⁵¹ The board of the taxpayers was effectively replaced by the board of its parent company, who exercised de facto control.⁵² The management of the business was therefore exercised in a manner *irregular, unauthorised and, perhaps, unlawful.*⁵³
- 20 43. Their Lordships accepted as the starting premise that a company's control is exercised by its constitutional organs. Lord Cohen explained that Sir Raymond Evershed's judgment in *Union Corporation* (and the passage extracted at [40] above) did not qualify the *true rule* or real business test, it simply applied the rule: where the articles of a company vest control in the board and the board actually meets in a particular country, that is where the central management actually abides.⁵⁴ Lord Radcliffe⁵⁵ (Lord Goddard agreeing) also approved Sir Raymond Evershed's focus on *controlling power and authority* and Dixon J's reasons in *Koitaki*.
44. However, the decisions acknowledge that the articles and constitution of a company are not the end of the inquiry. As Lord Radcliffe, said, *the articles ...*

⁴⁶ *Union Corporation* at (1952) 1 All ER 657G.

⁴⁷ *Union Corporation* at (1952) 1 All ER 662G-H.

⁴⁸ *Unit Construction Co Ltd v Bullock* [1960] AC 351.

⁴⁹ *Wood v Holden* [2006] 1 WLR 1393; [2006] EWCA Civ 26.

⁵⁰ *Commissioners for Her Majesty's Revenue and Customs v Smallwood* [2010] EWCA Civ 778.

⁵¹ *Unit Construction* at [1960] AC 360.4 – 360.6 (Viscount Simonds), and at [1960] AC 374.1 (Lord Cohen).

⁵² *Unit Construction* at [1960] AC 364.5 – 364.6 (Lord Radcliff).

⁵³ *Unit Construction* at [1960] AC 362.4 (Viscount Simonds).

⁵⁴ *Unit Construction* at [1960] AC 373.6 – 373.10, (Lord Cohen).

⁵⁵ *Unit Construction* at [1960] AC 367.3, (Lord Radcliffe).

cannot create an actual state of control ... which does not exist in fact.⁵⁶ This reasoning created an insurmountable hurdle for the taxpayer as *the board ... did not meet at all*.⁵⁷ The House of Lords was therefore faced with a situation where the constitutional organs did nothing, but they were being asked to find to the contrary. In those circumstances the parent company, found to exercise *de facto* control,⁵⁸ exercised central management and control in the absence of any such exercise by the board of the subsidiary. This does not diminish the force of the appellants' primary submission that a company acts through its lawfully appointed board. In *Bullock*, the House of Lords would have been required to *invent facts*⁵⁹ to find authority with the directors of the subsidiary. There is no need to do so here. Mr Borgas did not stand aside.

10

45. *Wood v Holden* concerned a scheme to minimise the capital gains tax exposure of two United Kingdom taxpayers. Nominee directors at ABN Amro in the Netherlands were appointed to various companies to facilitate a transaction to implement the scheme. In finding that the taxpayers were properly resident where these nominee directors were located, Chadwick LJ adopted the analysis of the law by the Judge at first instance, which distinguished *Esquire Nominees* and other cases from *Bullock* on the basis that *in the four cases [being Esquire Nominees and the decisions which have applied its reasoning] the parent companies or their equivalents, while telling the local boards what they wished them to do, left it to the local boards to do it*.⁶⁰ Against that background, Chadwick LJ noted that a board may be *usurped* on the basis of the facts found in *Bullock*, such that central management and control is exercised independently of the board.

20

46. His Lordship also remarked that where a company acts through its lawful organs, a distinction may be drawn *in concept at least* between a third party exercising *influence* and one engaged in *dictation*.⁶¹ Three observations concerning these remarks are necessary. First, in making these remarks Chadwick LJ approved of the legal analysis of the Judge at first instance noted above which confirmed that the fundamental distinction in the authorities is whether or not the board performs its constitutional function. Second, the distinction is qualified by the expression *in concept at least* which is a reflection of the fact that no decided cases in Australia or the United Kingdom have found that a third party exercised sufficient dominion over a functioning board of directors to wrest central management and control from the board. It supports the submission made at [22] above that these

30

⁵⁶ *Unit Construction* at [1960] AC 370.4, (Lord Radcliff).

⁵⁷ *Unit Construction* at [1960] AC 374.1, (Lord Cohen).

⁵⁸ *Unit Construction* at [1960] AC 364.5 – 364.6, (Lord Radcliff).

⁵⁹ *Unit Construction* at [1960] AC 363.3, (Viscount Simonds).

⁶⁰ *Wood v Holden* at [2006] 1 WLR 1410 [26] B-G citing, among others, *Esquire Nominees* and [27].

⁶¹ *Wood v Holden* at [2006] 1 WLR 1411 [27] A-B.

statements are properly understood as justifications for the principle that a company acts through its board, rather than exceptions or qualifications. Finally, Chadwick LJ's reasons were expressed as a summary, rather than an extension, of the authorities. They ought to be considered in light of those authorities and reflecting their orthodoxy. *Esquire Nominees* was analysed above. *Re Little Olympian Each Ways Ltd*⁶² held that the Court could only look past the formal decision making organs of a company where its board completely failed to act, even as a rubber stamp.⁶³ In *New Zealand Forest Products*⁶⁴ the New Zealand High Court applied *Esquire Nominees* to a factual situation where one board had the power to remove directors but not to direct them how to vote. Doogue J distinguished *Bullock* on the basis that there was no suggestion that the board had failed to act.

10

47. *Wood v Holden* also supports the submission that Mr Borgas made the relevant decisions and was not usurped. The Full Court below identified certain *critical* findings of effective decision making in the first instance *Wood v Holden* decision⁶⁵ to the effect that the directors were not merely *going through the motions* in signing documents.⁶⁶ These findings were not critical to the outcome in the appeal in *Wood v Holden* and the Full Court below wrongly gave them prominence. Instead, Chadwick LJ identified two *critical facts* that determined the issue of control.⁶⁷ First, the directors *were not by-passed nor did they stand aside since their representatives signed or executed the documents* and that, as a result, the reasoning in *Bullock* did not apply. Second, it was implicit in the directors' signing and executing documents that they must have decided to sign those documents.

20

48. These facts, and the Court of Appeal's findings, have their parallels in the present case. Mr Borgas executed each of the relevant documents that caused the Appellants to enter into all business transactions. He did not stand aside. By reason of his having signed the documents, he must have decided to do so. To the extent that Mr Borgas was required to have engaged in a decision making process, the appellants submit that this finding is all that is required to satisfy the requirement. As Sir Christopher Staughton observed in concurrence, language such as *real decisions* and whether something was *a piece of paper* are unhelpful and ignore the effect of what actually happened: Mr Borgas, as director, effected the transactions of the appellants.⁶⁸

30

⁶² [1994] 4 All ER 561

⁶³ *Re Little Olympian Each Ways Ltd* at [1994] 4 All ER 573h-j (Lindsay J).

⁶⁴ *New Zealand Forest Products Finance NV v Commissioner of Inland Revenue* [1995] 2 NZLR 357 at 367 l 44 - 53 (Doogue J).

⁶⁵ *Wood v Holden* [2005] EWHC 547 (Ch) [2005] STC 789.

⁶⁶ AJ [9] and *Wood v Holden* [2006] 1 WLR 1393 at [36], [40]-[43].

⁶⁷ *Wood v Holden* [2006] 1 WLR 1393 at [40] - [41].

⁶⁸ *Wood v Holden* at [2006] 1 WLR 1419 [50].

49. In *Smallwood*, Patten LJ's dissent adopted Chadwick LJ's analysis and characterised dictation as effectively ceding any discretion by agreeing to act in accordance with a third party's instructions.⁶⁹
50. The UK authorities therefore acknowledge the primacy of a company's board in the question of determining central management and control. The UK formulation of dictation is also entirely consistent with the appellants' submissions that for central management and control to lie in a person or entity beyond a company's board, either the board must be by-passed or stand aside, or that person or entity constituting the central management and control must have power to direct a board's actions through a mechanism superior to mere power to remove uncooperative directors. There is no principled basis for any further gloss to this Court's reasoning in *Esquire Nominees*.

Mr Gould's role

51. The respondent below relied heavily on the level of engagement Mr Gould had in the affairs of the appellants. The Court of Appeal's reasons in *Wood v Holden* rejected a similar contention by the revenue that certain decisions were not effective because they were made in the absence of information or consideration.⁷⁰ It was the directors' decision to sign documents to cause the company to enter into transactions that the Court of Appeal considered to be both the operative decision and also a demonstration that those who did so did not stand aside.⁷¹ And it was so in the present case.
52. The primary facts that the Primary Judge relied on from PJ [145] to [309] reveal that Mr Borgas engaged in conduct on behalf of Chemical, which the Primary Judge held was largely reflected in conduct on behalf of Derrin and Bywater, in a manner consistent with the interests of Mr Gould. In light of the factual findings concerning ultimate ownership, that is hardly surprising. Importantly, on each occasion it was Mr Borgas who engaged in the relevant actions that bound the company. For example, Mr Borgas, on behalf of Chemical, advanced loan funds to entities associated with Mr Gould: PJ [153] to [161]. The Primary Judge's conclusion at PJ [160] was that there was *no reason for Mr Borgas to have engaged in these transactions*. However, it was Chemical engaging in the transactions. Chemical did so because Mr Borgas controlled it to do so in the requisite sense. It does not matter that Mr Borgas likely engaged in the transaction because that is what Mr Gould asked him to do.⁷²

⁶⁹ *Smallwood* at [2010] EWCA Civ 778 [61].

⁷⁰ *Wood v Holden* at [2006] 1 WLR 1418 [43].

⁷¹ *Wood v Holden* at [2006] 1 WLR 1417 [40] and 1418 [42] and [43].

⁷² *Esquire Nominees* at 129 CLR 190 and 191 (Gibbs J).

53. Mr Gould was found to possess the power to appoint directors to the shareholders of the appellants. However, there was no finding that Mr Gould had any contractual or other power to demand that Mr Borgas make a decision in a particular way. This can be contrasted with the nominee directors in *Wood v Holden*, who were contractually bound to act in accordance with the instructions of PwC and even those nominee directors were found to exercise central management and control, because they signed (and therefore considered) documents on behalf of the company. Instead, as with the accountants in *Esquire Nominees*, Mr Gould possessed nothing more than the power of appointment. If he wished, he could remove Mr Borgas as a director and appoint a replacement director. The authorities are clear, that is not central management and control.⁷³

Ownership does not constitute control and never has

54. Contrary to the Primary Judge's findings, it is entirely plausible, and consistent with widespread commercial practice, for directors to control entities in which they have no or minimal ownership interest.
55. The Full Court relied on the Primary Judge's findings that Mr Gould made decisions and Mr Borgas implemented them *without thought* to distinguish *Esquire Nominees* at AJ [8].⁷⁴ However, the findings that Mr Borgas acted *without thought or mechanically* should be properly analysed. They are inferences drawn by the Primary Judge from primary facts. These primary facts were that Mr Borgas did not own the company and that Mr Borgas did not give truthful evidence about that ownership: PJ [77].
56. The Primary Judge's reliance on the fact that Mr Borgas did not own the company rests on the unsound premise that directors do not make decisions in companies they do not own. The Primary Judge's understanding of what constituted a relevant *decision* and its use as a proxy for *control* by the Full Court was wrong. The Primary Judge's remarks at PJ [77] *why would [Mr Borgas] be making decisions in respect of a company that was not his* and at PJ [151] *it was implausible that Mr Borgas, who had no stake in Chemical Trustee, would be making decisions for it when it was Mr Gould's money*, and the Full Court's adoption of the Primary Judge's factual findings (e.g. AJ [14]), demonstrate that both Courts regarded the anterior directive by an interested third party to the lawful organs of the company, which the lawful organs caused the company to follow, as a *decision*. There is no rational reason for concluding that persons with no financial interest in a company cannot make relevant decisions in pursuance of their control of the company in the relevant sense. The directors in the chain of

⁷³ *Esquire Nominees* at 129 CLR 191 (Gibbs J).

⁷⁴ *Esquire Nominees* at 129 CLR 191 (Gibbs J); AJ [8].

companies considered in *Esquire Nominees* did not own those companies. Owners may wield substantial influence and power in the affairs of a company, but that is not relevant management and control.

57. This finding of ownership was considered *central* to the question of control in the Primary Judge's reasons: PJ [76] to [77]. At AJ [14], the Full Court attempted to remediate this finding by suggesting that the Primary Judge was referring to *central in an evidentiary sense*. That analysis ignores the fact that the Appellants consistently submitted in both the opening and closing of their case below that ownership was a *distraction*⁷⁵ or *collateral*: PJ [75].

10

The appellants acted through their lawful organs

58. On the factual findings of the Primary Judge, each of the appellants were centrally managed and controlled through their lawful organs.

59. Mr Borgas executed almost all relevant documents by which the appellants engaged in business: PJ [55] & [66]. He was responsible for communicating with the brokers who transacted the company's business. Although there are instances where Mr Gould was involved in particular transactions, the Primary Judge acknowledged that Mr Borgas was still required to sign off on those transactions: PJ [129] and [130]. These matters are entirely consistent with that fact that the articles of each appellant (either directly, or through the incorporation of model rules) vested the directors with authority for the company's actions (see [7] above). A company's existence, capacities and activities are only such as the law attributes to it⁷⁶ and it can only act through people. Estoppel and like considerations aside, it is only bound by an action where a person has the authority to bind, and that authority is granted either by the constitution of the company or a resolution of the company's governing body.⁷⁷

20

CONTEXT IN WHICH THE TEXT OF THE STATUTE APPEARS

60. As noted at [13] above, the words used in the definition create alternative tests; one that looks to central management and control, and the alternative which looks to the residence of shareholders with controlling voting power. That context compels the conclusion that controlling shareholders are not part of the test for central management and control.

30

⁷⁵ AB (Appeal Book reference to inserted).

⁷⁶ *Northside Developments Pty Ltd v Registrar-General* (1990) 170 CLR 146 at 171 (Brennan J).

⁷⁷ *Northside Developments* at (1990) 170 CLR 172 (Brennan J).

61. Further, the context of the definition in the scheme of the statute as a whole compels the same conclusion.
62. Together with the concept of source, the concepts of residence and resident are the gateway for determining whether the critical features of Australia's tax legislation apply to an entity.
63. The starkest example of the role of the residence concept in the statutory scheme is the way in which it determines the extent to which an entity is taxed in Australia on income and profits: see sections 6-5(2) and (3) and 6-10(4) and (5) of the *Income Tax Assessment Act 1997* (Cth). Subject to specific exemptions, Australian residents are taxed on all income, while foreign residents are taxed only on Australian source income. As well as Australia's domestic taxation regime, residence forms a cornerstone of the double taxation agreements that Australia has entered with other nations.⁷⁸ Many other ancillary provisions, such as the requirement to pay withholding tax, also depend on residence: see s128B of the 1936 Assessment Act.
64. In light of the significance of the concept of residence, it is hardly surprising that the definition, and the legislative response to the taxation of income and gains derived or made by non-residents, has been the subject of regular review and/or legislative change. Thus, two years after *Esquire Nominees* was decided, the Commonwealth Taxation Review Committee (the **Asprey Committee**) considered whether to extend the test for corporate residence to *include the exercise of control and direction of the company's affairs otherwise than in the formal proceedings of the board-room*⁷⁹ and whether Australia should replicate an initiative adopted by the United States of America: to tax domestic residents in respect of their respective shares of income earned by companies incorporated off-shore in tax haven countries that they control.⁸⁰ The Asprey Committee recommended the latter.
65. Ultimately, the Asprey Committee Report's observations concerning corporate residence were not enacted into law. Instead, as recommended, legislation to deal with the income and profits of companies and other entities incorporated and/or carrying on activities outside Australia under the control of Australians without any reliance on central management and control concepts was introduced: see Part X, *Attribution of income in respect of controlled foreign companies*, and Division

⁷⁸ The Explanatory Memorandum (EM) for the *International Tax Agreements Amendment Bill* (No. 1) 2007 noted (at 3.40) that a particular change was *consistent with the Government's decision in response to the Review of International Taxation Arrangements, to move towards a more residence-based tax treaty policy*.

⁷⁹ Asprey Committee Report at 17.15.

⁸⁰ Asprey Committee Report at 17.48.

6AAA--*Special provisions relating to non-resident trust estates etc.*, of the 1936 Assessment Act. Former Part XI of the 1936 Assessment Act, *Foreign Investment Funds and foreign life assurance policies*, followed.

- 10 66. Part X of the 1936 Assessment Act was introduced to attribute certain income derived and profits made by a non-resident company that is controlled by Australian residents to the Australian resident controllers.⁸¹ Rather than amend the test for residence, and tax companies as though they were Australian residents, the chosen tool was to introduce a control rule, and tax the Australian residents found to exercise control. This was a considered policy direction which has, as amended from time to time, remained in place to this date. Further reforms to the legislation were announced in 2009,⁸² and exposure draft legislation introduced in 2011.⁸³
67. The 40 years since *Esquire Nominees* have provided ample time for legislative response to the decision. Implicit in this policy response is the acknowledgment that it is appropriate for foreign companies to organise their affairs in a manner consistent with those reasons.⁸⁴

POLICY AND PURPOSE OF THE STATUTE

68. These observations apply equally to considerations of the policy and purpose of the statute.

20 DISPOSITION OF THE APPEALS

69. A finding that Derrin and Chemical had no central management and control in Australia requires the conclusion that their appeals be allowed as each taxpayer is entitled to the protection afforded by the *Convention Between the Government of the United Kingdom of Great Britain and Northern Ireland and the Government of Australia for Avoidance of Double Taxation and the Prevention of Fiscal Evasion with respect to Taxes on Income and on Capital Gains*, signed 21 August 2003, [2003] ATS 22 (entered into force 17 December 2003) (for years following 2004) and the *Agreement between the Government of the Commonwealth of Australia and the Government of the United Kingdom of Great Britain and Northern Ireland for the Avoidance of Double Taxation and the Prevention of Fiscal Evasion with respect to Taxes on Income and Capital Gains*, signed 7
- 30

⁸¹ EM, *Taxation Laws Amendment (Foreign Income) Bill* (Cth) 1990 at 1, 3-4g.

⁸² Department of Treasury Consultation Paper, *Reform of the controlled foreign company rules*, January 2010 page iii, 7.

⁸³ Department of Treasury Exposure Draft, *Reform of the foreign source income deferral rules*, February 2011.

⁸⁴ *Review of International Taxation Arrangements: A consultation paper* at 53 – 54.

December 1967, [1968] ATS 9 (entered into force 8 May 1968) (for the earlier income years).

- 10 70. Bywater's position is different. Bywater was not found to be resident in Switzerland because it was not *managed and controlled* or did not have *effective management* in Switzerland: PJ [438] to [440]. The basis for the Primary Judge's conclusion was that all the *decisions* were made in Australia by Mr Gould. If this Court accepts the appellants' submissions about the relevance of Mr Gould, then it can also find that Bywater had its *effective management* in Switzerland with Mr Borgas. *Wood v Holden* and *Smallwood* each equated concepts of effective management with central management and control⁸⁵ and the findings of Swiss law made by the Primary Judge do not require a different approach. However, if this Court does not consider it appropriate to make that finding, the matter should be remitted for determination.

Part VII:

71. The applicable statutes as they existed at the relevant time, are annexed.

Part VIII:

- 20 72. The appellants seek the following orders:
- (a) The Appeal be allowed.
 - (b) The orders of the Full Court of the Federal Court of Australia be set aside and in lieu thereof the following orders be made:
 - (i) the appeal be allowed;
 - (ii) the orders of the primary Judge be set aside
 - (iii) the respondent's objection decisions be set aside; and
 - (iv) the appellants' objections to the assessments of taxable income and tax payable thereon be allowed in full and the matter be remitted to the respondent for him to reassess in accordance with law.
 - (c) The respondent pay the appellants' costs of and incidental to this appeal including the costs for the application for special leave to appeal, the Full Court of the Federal Court and at first instance.

⁸⁵ *Wood v Holden* at [2006] 1 WLR 1418 at [44] (Chadwick LJ; Moore-Bick LJ and Sir Christopher Staughton agreeing); *Smallwood* [2010] EWCA Civ 778 at [61] (Patten LJ) and [68] (Hughes LJ).

(d) Alternatively:

- (i) for Chemical and Derrin, the orders set out in (a) and (b) above; and
- (ii) for Bywater, the orders of the Full Court of the Federal Court of Australia be set aside and in lieu thereof the following orders be made:

(A) the appeal be allowed;

(B) the matter be remitted to the Full Court to determine:

(1) the nature and character of the profits that were taxed in the disputed assessments; and

10

(2) whether Bywater was a resident of Switzerland for the purposes of the Agreement between Australia and Switzerland for the Avoidance of Double Taxation with respect to Taxes on Income, signed 28 February 1980; and

(C) the respondent pay the appellant's costs of and incidental to this appeal including the costs for the application for special leave to appeal.

Part IX:

73. The Appellants estimate that 3 hours will be required for the presentation of the
20 appellant's oral argument in chief and 30 minutes in reply.

Dated: 3 June 2016



<p>A. J. Myers tel. 03 9653-3777 email: ajmyers@dunkeldpastoral.com.au</p>	<p>F.D. O'Loughlin tel. (03) 9225 7800 email: frank.oloughlin@vichar.com.au <u>u</u></p>	<p>T. L. Bagley tel. 02 8915 2142 email: bagley@selbornechambers.com.au</p>
--	---	---

ANNEXURE TO SUBMISSIONS - LEGISLATIVE PROVISIONS

Each provision is provided as at today's date. Section 6 of the *Income Tax Assessment Act 1936* (Cth) was not amended between the relevant tax years and today's date.

Income Tax Assessment Act 1936 (Cth)

6 Interpretation

10

...

resident or resident of Australia means:

...

(b) a company which is incorporated in Australia, or which, not being incorporated in Australia, carries on business in Australia, and has either its central management and control in Australia, or its voting power controlled by shareholders who are residents of Australia.

...

20 128 Liability to withholding tax

(1A) In this section, a reference to a person to whom this section applies is a reference to the Commonwealth, a State, an authority of the Commonwealth or of a State or a person who is, or persons at least 1 of whom is, a resident.

(1) Subject to subsections (3), (3A), (3D) and (3E), this section applies to income that:

(a) is derived, on or after 1 January 1968, by a non-resident; and

(b) consists of a dividend paid by a company that is a resident.

Note: An amount declared to be conduit foreign income is an amount to which this section does not apply: see sections 802-15 and 802-17 of the *Income Tax Assessment Act 1997*.

(2) Subject to subsection (3), this section also applies to income that:

30

(a) is derived, on or after 1 January 1968, by a non-resident; and

(b) consists of interest that:

(i) is paid to the non-resident by a person to whom this section applies and is not an outgoing wholly incurred by that person in carrying on business in a

country outside Australia at or through a permanent establishment of that person in that country; or

(ii) is paid to the non-resident by a person who, or by persons each of whom, is not a resident and is, or is in part, an outgoing incurred by that person or those persons in carrying on business in Australia at or through a permanent establishment of that person or those persons in Australia.

Note: An amount of interest paid to a person by a temporary resident is an amount to which this section does not apply: see section 768-980 of the Income Tax Assessment Act 1997 .

(2A) Subject to subsection (3), where income:

10 (a) is, or has, after 2 July 1973, been, derived, or derived in part, by a person to whom this section applies in carrying on business in a country outside Australia at or through a permanent establishment of the person in that country; and

(b) consists of interest that:

(i) is or has been paid to the person by another person to whom this section applies and is not an outgoing wholly incurred by that other person in carrying on business in a country outside Australia at or through a permanent establishment of that other person in that country; or

20 (ii) is or has been paid to the first-mentioned person by a person who is, or by persons each of whom is, not a resident and is, or is in part, an outgoing incurred by that last-mentioned person or those last-mentioned persons in carrying on business in Australia at or through a permanent establishment of that last- mentioned person or those last-mentioned persons in Australia;

this section also applies to that income or to the part of that income so derived, as the case may be.

Note: An amount of interest paid to a person by a temporary resident is an amount to which this section does not apply: see section 768-980 of the Income Tax Assessment Act 1997 .

(2B) Subject to subsection (3), this section also applies to income that:

(a) is derived by a non-resident:

(i) during the 1993-94 year of income of the non-resident; or

30 (ii) during a later year of income of the non-resident; and

(b) consists of a royalty that:

(i) is paid to the non-resident by a person to whom this section applies and is not an outgoing wholly incurred by that person in carrying on business in a foreign country at or through a permanent establishment of that person in that country; or

(ii) is paid to the non-resident by a person who, or by persons each of whom, is not a resident and is, or is in part, an outgoing incurred by that person or those

persons in carrying on business in Australia at or through a permanent establishment of that person or those persons in Australia.

(2C) Subject to subsection (3), where income:

(a) is derived, or derived in part, by a person (the recipient) to whom this section applies in carrying on business in a country outside Australia at or through a permanent establishment of the person in that country; and

(b) consists of a royalty that:

10 (i) is paid to the recipient by another person (the payer) to whom this section applies and is not an outgoing wholly incurred by the payer in carrying on business in a country outside Australia at or through a permanent establishment of the payer in that country; or

(ii) is paid to the recipient by one or more persons (the non-resident payers), each of whom is not a resident, and is, or is in part, an outgoing incurred by the non-resident payers in carrying on business in Australia at or through a permanent establishment of the non-resident payers in Australia;

this section also applies to that income or to the part of that income mentioned in paragraph (a).

(2D) Subsections (2B) and (2C) do not apply to income to the extent to which it is a return on an equity interest in a company.

20 (3) This section does not apply to:

(aaa) income that consists of a non-share dividend that is unfrankable under section 215-10 of the Income Tax Assessment Act 1997; or

(a) income derived by a non-resident that is:

(i) exempt from income tax because of section 50-5 (other than because of item 1.6 in the table in that section) or 50-10, item 6.1 or 6.2 of the table in section 50-30, section 50-40 or item 9.1 or 9.2 of the table in section 50-45 of the Income Tax Assessment Act 1997; and

(ii) exempt from income tax in the country in which the non-resident resides;
or

30 (aa) income derived by a non-resident that is an overseas charitable institution (within the meaning of section 121C) where the income is exempt under subsection 121ELA(1);
or

(ba) income that is exempt from income tax because of section 124ZM (which exempts dividends paid by PDFs); or

(bb) income that is not included in assessable income because of section 159GZZZZE;
or

(d) income in respect of which a trustee is liable to be assessed under section 99 or section 99A; or

(e) income that is derived by a trustee, being a trustee in relation to a trust created by a person who, at the time the income is derived, is a resident and in respect of which the Commissioner is empowered, under section 102, to assess the trustee to pay income tax; or

(ga) income that consists of:

(i) the franked part of a dividend; or

10 (ii) in relation to a dividend that is paid by a former exempting entity (within the meaning of the Income Tax Assessment Act 1997) on a share acquired under an employee share scheme (within the meaning of that Act)--the part of the dividend that is franked with an exempting credit; or

(iii) in relation to a dividend that is paid by a former exempting entity (within the meaning of the Income Tax Assessment Act 1997) to an eligible continuing substantial member (within the meaning of that Act)--the part of the dividend that is franked with an exempting credit;

20 other than a dividend in respect of which a determination is made under paragraph 204-30(3)(c) of the Income Tax Assessment Act 1997 or a dividend or a part of a dividend in respect of which a determination is made under paragraph 177EA(5)(b) of this Act; or

(gb) income that consists of a dividend derived from assets included in the insurance funds of a life assurance company that carries on business in Australia at or through a permanent establishment of the life assurance company in Australia; or

(gc) income that consists of interest derived on a nostro account by a non-resident that is a foreign bank; or

(h) income that consists of:

30 (ii) interest derived by a non-resident in carrying on business in Australia at or through a permanent establishment of the non-resident in Australia (except interest derived by a limited partner in a VCLP, ESVCLP or AFOF as such a partner);

(iv) interest to which section 128F, 128FA or 128GB applies; or

(j) income in respect of which a taxpayer is liable to be assessed under Division 9C; or

(jb) income that:

(i) is derived by a non-resident that is a superannuation fund for foreign residents; and

(ii) consists of interest, or consists of dividends or non-share dividends paid by a company that is a resident; and

(iii) is exempt from income tax in the country in which the non-resident resides; or

(k) income that is not included in assessable income because of subsection 271-105(1); or

(l) income derived by a trustee that, because of paragraph 102UK(2)(b) or 102UM(2)(b), is not included in the assessable income of a trustee beneficiary of the trust estate; or

(m) income that consists of a royalty that is paid to the non-resident by a person (the lessee) as consideration for the lease, by the lessee from the non-resident, of a vessel if:

10

(i) the lessee is an Australian resident company; and

(ii) the vessel is not an excluded vessel (within the meaning of the Shipping Reform (Tax Incentives) Act 2012); and

(iii) under the lease, the lessee has whole possession and control of the vessel (including the right to appoint the master and crew of the ship); and

(iv) during the period of the lease, the vessel is used, or is available for use, as mentioned in paragraph 8(1)(c) of the Shipping Reform (Tax Incentives) Act 2012 .

20

(3A) Paragraph (3)(ga) does not apply to income consisting of a dividend, or a part of a dividend, that is derived by the trustee of a trust, or a partnership, to the extent (if any) to which any amount paid to, or applied for the benefit of, a taxpayer (being a beneficiary in the trust or a partner in the partnership) that:

(a) was attributable to the dividend; and

(b) was paid or applied:

(i) in respect of an interest in the trust or partnership that was acquired, or was acquired for a period that was extended, at or after the commencing time; or

(ii) under a financing arrangement (including an arrangement extending an earlier arrangement) entered into at or after the commencing time;

may reasonably be regarded as equivalent to the payment of interest on a loan.

(3B) In subsection (3A):

30

"commencing time " means 7.30 pm by legal time in the Australian Capital Territory on 13 May 1997.

"financing arrangement " has the meaning given by subsection 995-1(1) of the Income Tax Assessment Act 1997 .

(3C) In determining for the purposes of subsection (3A) the extent (if any) to which an amount may reasonably be regarded as equivalent to the payment of interest on a loan, regard is to be had to:

- (a) the way in which the amount was calculated; and
- (b) the conditions applying to the payment or application of the amount; and
- (c) any other relevant matters.

(3D) This section does not apply to a demerger dividend to which section 45B does not apply.

(3E) This section does not apply to income that consists of a dividend that:

- (a) is paid to a person who is a non-resident carrying on business in Australia at or through a permanent establishment of the person in Australia; and
- (b) is attributable to the permanent establishment; and
- (c) is not paid to the person in the person's capacity as trustee.

10

Note: This subsection not only ensures that this section does not apply to that income to make withholding tax payable on it, but also (as a result) ensures that none of that income is non-assessable non-exempt income under section 128D. Subsection 44(1) makes that income assessable income.

(3F) In subsection (3E):

"permanent establishment " of a person:

- (a) has the same meaning as in a double tax agreement (as defined in Part X) that relates to a foreign country and affects the person; or
- (b) has the meaning given by subsection 6(1), if there is no such agreement.

20

(4) A person who derives income to which this section applies that consists of a dividend is liable to pay income tax upon that income at the rate declared by the Parliament in respect of income to which this subsection applies.

(5) A person who derives income to which this section applies that consists of interest is, subject to subsections (6) and (7), liable to pay income tax upon that income at the rate declared by the Parliament in respect of income to which this subsection applies.

(5A) A person who derives income to which this section applies that consists of a royalty is liable to pay income tax upon that income at the rate declared by the Parliament in respect of income to which this subsection applies.

(6) Where:

30

- (a) income to which this section applies consists of interest and is paid to the person by whom it is derived by a person to whom this section applies; and
- (b) the interest is, in part only, an outgoing incurred by that person to whom this section applies in carrying on business in a country outside Australia at or through a permanent establishment of that person to whom this section applies in that country;

income tax is payable under subsection (5) upon so much only of the income as is attributable to so much of the interest as is not an outgoing so incurred.

(7) Where:

(a) income to which this section applies consists of interest and is paid to the person by whom it is derived by a person who, or by persons each of whom, is not a resident; and

(b) the interest is, in part only, an outgoing incurred by the person or persons by whom it is paid in carrying on business in Australia at or through a permanent establishment of that person or those persons in Australia;

10 income tax is payable under subsection (5) upon so much only of the income as is attributable to so much of the interest as is an outgoing so incurred.

(8) For the purposes of subparagraphs (2)(b)(i) and (2A)(b)(i) and paragraph (6)(b), where:

(a) interest is paid, or has, after 2 July 1973, been paid, to a person by another person, being a person to whom this section applies, carrying on business in a country outside Australia; and

(b) the interest or a part of the interest:

20 (i) is interest incurred by the other person in gaining or producing income that is derived by the other person otherwise than in carrying on business in a country outside Australia at or through a permanent establishment of the other person in that country or is interest incurred by the other person for the purpose of gaining or producing income to be so derived; or

(ii) is interest incurred by the other person in carrying on business for the purpose of gaining or producing income and is reasonably attributable to income that is derived, or may be derived, by the other person otherwise than in so carrying on business at or through a permanent establishment of the other person in a country outside Australia;

the interest or the part of the interest, as the case may be, is not an outgoing incurred by the other person in carrying on business in a country outside Australia at or through a permanent establishment of the other person in that country.

(9) For the purposes of subparagraphs (2)(b)(ii) and (2A)(b)(ii) and paragraph (7)(b), where:

30 (a) interest is paid, or has, after 2 July 1973, been paid, to a person by another person or other persons (in this subsection referred to as the borrower), being:

(i) another person who is or was carrying on business in Australia and is not or was not a resident; or

(ii) other persons who are or were carrying on business in Australia and each of whom is not or was not a resident; and

(b) the interest or a part of the interest:

(i) is interest incurred by the borrower in gaining or producing income that is derived by the borrower in carrying on business in Australia at or through a permanent establishment of the borrower in Australia or is interest incurred by the borrower for the purpose of gaining or producing income to be so derived; or

(ii) is interest incurred by the borrower in carrying on a business for the purpose of gaining or producing income and is reasonably attributable to income that is derived, or may be derived, by the borrower in so carrying on business at or through a permanent establishment of the borrower in Australia;

10 the interest or the part of the interest, as the case may be, is an outgoing incurred by the borrower in carrying on business in Australia at or through a permanent establishment of the borrower in Australia.

(9A) For the purposes of subparagraphs (2B)(b)(i) and (2C)(b)(i), where:

(a) a royalty is paid, to a person by another person, being a person to whom this section applies, carrying on business in a country outside Australia; and

(b) the royalty, or a part of the royalty:

20 (i) is a royalty incurred by the other person in gaining or producing income that is derived by the other person otherwise than in carrying on business in a country outside Australia at or through a permanent establishment of the other person in that country or is a royalty incurred by the other person for the purpose of gaining or producing income to be so derived; or

(ii) is a royalty incurred by the other person in carrying on business for the purpose of gaining or producing income and is reasonably attributable to income that is derived, or may be derived, by the other person otherwise than in so carrying on business at or through a permanent establishment of the other person in a country outside Australia;

the royalty or the part of the royalty, as the case may be, is not an outgoing incurred by the other person in carrying on business in a country outside Australia at or through a permanent establishment of the other person in that country.

30 (9B) For the purposes of subparagraphs (2B)(b)(ii) and (2C)(b)(ii), where:

(a) a royalty is paid to a person by another person or other persons (the licensee), being:

(i) another person who is or was carrying on business in Australia and is not or was not a resident; or

(ii) other persons who are or were carrying on business in Australia and each of whom is not or was not a resident; and

(b) the royalty or a part of the royalty:

(i) is a royalty incurred by the licensee in gaining or producing income that is derived by the licensee in carrying on business in Australia at or through a

permanent establishment of the licensee in Australia or is a royalty incurred by the licensee for the purpose of gaining or producing income to be so derived; or

(ii) is a royalty incurred by the licensee in carrying on a business for the purpose of gaining or producing income and is reasonably attributable to income that is derived, or may be derived, by the licensee in so carrying on business at or through a permanent establishment of the licensee in Australia;

the royalty or the part of the royalty, as the case may be, is an outgoing incurred by the licensee in carrying on business in Australia at or through a permanent establishment of the licensee in Australia.

10 (9C) If:

(a) apart from this subsection, tax would be payable under subsection 126(1) on an amount of interest paid to a person; and

(b) section 128F would apply to the interest, assuming that paragraph (1)(e) of that section had not been enacted;

then:

(c) despite anything else in this section, the interest is taken, for the purposes of this Division, to be income derived by the person and to be income to which this section applies; and

20 Note: As a result of this paragraph, the interest will not be subject to tax under subsection 126(1): see paragraph 126(1)(b).

(d) in addition to the effect of any credit arising under section 18-30 in Schedule 1 to the Taxation Administration Act 1953 in respect of the interest, the total tax payable by the person, other than under this section, is reduced by the amount of any tax payable under this section on the interest; and

(e) tax paid under this section on the interest is not an allowable deduction.

(10) Income tax payable by a person in accordance with this section is in addition to any other income tax payable by him or her upon income to which this section does not apply.

30 (11) Income tax payable by a person in accordance with this section upon income to which this section applies by virtue of subsection (2A) or (2C) is in addition to, and shall not be taken into account in arriving at the amount of, any other income tax payable by him or her in respect of that income.

316 Object of Part

(1) The object of this Part is to provide for certain amounts to be included in a taxpayer's assessable income (Division 9) in respect of:

- (a) the attributable income of a CFC (section 456); and
- (b) certain changes of residence by a CFC (section 457).

(2) To that end (and for other purposes of this Act) this Part contains rules relating to the following:

- (a) interpretation (Division 1);
- (b) types of entities (Division 2);
- 10 (c) control interests, attribution interests, attributable taxpayers and attribution percentages (Division 3);
- (d) attribution accounts (Division 4);
- (g) the calculation of attributable income of a CFC (Division 7);
- (h) the active income test (Division 8);
- (j) post-attribution asset disposals (Division 10);
- (k) the keeping of records (Division 11).

20

Income Tax Assessment Act 1997 (Cth)

6-5 Income according to ordinary concepts (*ordinary income*)

(1) Your assessable income includes income according to ordinary concepts, which is called ordinary income.

Note: Some of the provisions about assessable income listed in section 10-5 may affect the treatment of ordinary income.

(2) If you are an Australian resident, your assessable income includes the *ordinary income you *derived directly or indirectly from all sources, whether in or out of Australia, during the income year.

(3) If you are a foreign resident, your assessable income includes:

- 30 (a) the *ordinary income you *derived directly or indirectly from all *Australian sources during the income year; and
- (b) other *ordinary income that a provision includes in your assessable income for the income year on some basis other than having an *Australian source.

(4) In working out whether you have derived an amount of *ordinary income, and (if so) when you derived it, you are taken to have received the amount as soon as it is applied or dealt with in any way on your behalf or as you direct.

6-10 Other assessable income (*statutory income*)

(1) Your assessable income also includes some amounts that are not *ordinary income.

Note: These are included by provisions about assessable income. For a summary list of these provisions, see section 10-5.

10 (2) Amounts that are not *ordinary income, but are included in your assessable income by provisions about assessable income, are called statutory income.

Note 1: Although an amount is statutory income because it has been included in assessable income under a provision of this Act, it may be made exempt income or non-assessable non-exempt income under another provision: see sections 6-20 and 6-23.

Note 2: Many provisions in the summary list in section 10-5 contain rules about ordinary income. These rules do not change its character as ordinary income.

(3) If an amount would be *statutory income apart from the fact that you have not received it, it becomes statutory income as soon as it is applied or dealt with in any way on your behalf or as you direct.

20 (4) If you are an Australian resident, your assessable income includes your *statutory income from all sources, whether in or out of Australia.

(5) If you are a foreign resident, your assessable income includes:

(a) your *statutory income from all *Australian sources; and

(b) other *statutory income that a provision includes in your assessable income on some basis other than having an *Australian source.