HIGH COURT OF AUSTRALIA

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IN THE HIGH COURT OF AUSTRALIA
SYDNEY REGISTRY

BETWEEN: **Appeal S158/2025**

Gordon Stanley Merchant
First Appellant

GSM Pty Ltd ACN 074 508 124
Second Appellant

and

Commissioner of Taxation
Respondent

BETWEEN: **Appeal S157/2025**

Commissioner of Taxation
Appellant

and

Gordon Stanley Merchant
First Respondent

GSM Pty Ltd ACN 074 508 124
Second Appellant

APPELLANTS' SUBMISSIONS IN APPEAL S158/2025

CROSS APPELLANTS' SUBMISSIONS ON THE CROSS-APPEAL AND RESPONDENTS' AMENDED NOTICE OF CONTENTION IN APPEAL S157/2025

PART I: CERTIFICATION

1. These submissions are in a form suitable for publication on the internet.

PART II: CONCISE STATEMENT OF THE ISSUE

2. The Commissioner has conceded that s 177D of the *Income Tax Assessment Act 1936* (Cth) (**ITAA36**) does not prevent a taxpayer from exercising an ordinary incident of ownership – that of timing a sale of property so as to realise a capital loss which can be used to offset a future capital gain that is then in prospect, where that sale is to a wholly independent third party. The issue in this appeal is whether s 177D applies to such a transaction where the sale is at market value to a related party – one that is controlled by the same person but is not the "alter ego" of the first, and is subject to different legal, commercial and taxation considerations. On the Commissioner's case, s 177D applies in those circumstances to put the taxpayer to an election: sell the property to a wholly independent third party or defer the sale until such time as no future capital gain is in prospect. Such an election cannot have been contemplated by the ITAA36.

PART III: NOTICE UNDER S 78B OF THE *JUDICIARY ACT 1903* (CTH)

3. No notice is required under s 78B of the *Judiciary Act 1903* (Cth).

PART IV: CITATIONS

4. The judgment of the primary judge is reported at (2024) 119 ATR 480. The medium neutral citation is [2024] FCA 498. The judgment of the Full Court of the Federal Court is reported at (2025) 309 FCR 144. The medium neutral citation is [2025] FCAFC 56.

PART V: RELEVANT FACTS

5. **Mr Merchant's connection to BBG.** Mr Merchant, the first appellant, co-founded the business that became Billabong International Ltd (**BBG**) in 1973, which was listed on the ASX in August 2000: PJ [42]-[43], FCJ [5], [97]. There are several other companies in the Merchant Group, of which Mr Merchant was at all relevant times the director: FCJ [97]. At listing, the Merchant Group held approximately 23% of the issued capital in BBG: PJ [43], FCJ [8], [101]. The size of this holding fluctuated over time: PJ [44], [47], [128]-[129]. The BBG share price was generally on a downward trend from around 2007: PJ [50]. Nevertheless, Mr Merchant believed that BBG would become successful again and on this belief, caused entities in the Merchant Group to continue to buy BBG shares, even after BBG stopped paying dividends in 2012: PJ [50], [74]-[79], [86]-[90],

[101], [128]-[130], [237], FCJ [26]-[27], [101]-[105]. The primary judge accepted that Mr Merchant had a unique connection with the BBG business, which caused him to wish to retain his substantial shareholding in BBG: PJ [267], FCJ [28], [101].

6. **The acquisition and funding of Plantic.** In March 2005, MFT acquired 14% of the issued capital in a start-up company, Plantic Technologies Ltd (**Plantic**): PJ [45], FCJ [11], [12], [98]. In November 2010, MFT acquired the balance of the shares in Plantic, for a total cost base of around $24m: PJ [56], FCJ [98]. Plantic's operations were not profitable, and the Merchant Group provided it with regular cash injections and loans (of approximately $1m per month): PJ [58]-[61], [133], [269], [293]-[309], FCJ [82], [125]-[126]. By March 2015, GSM Pty Ltd (**GSM**) had loaned Plantic $50.192m (the **GSM Loan**), and Tironui Pty Ltd (**Tironui**) had loaned Plantic $4.125m (the **Tironui Loan**). Mr Merchant had also sold assets "to free up cash to fund Plantic": PJ [137].

7. **Negotiations for the sale of Plantic.** Mr Merchant grew tired of Plantic being a continual drain on his funds: PJ [133]. From around 2012, Plantic negotiated with several competitors about a range of deals of various forms which would have ended the need for funding: PJ [95], [103]-[105], [108]-[113], FCJ [20]. Some involved the possibility of selling Plantic, but no sale occurred. In November 2013, Sealed Air expressed interest in buying Plantic, but Mr Merchant was concerned about being "sidetracked again by another we might want to buy the company scenario": PJ [112] and see also PJ [113]. In March 2014, Plantic and Multivac entered into an exclusive distribution agreement with an "introductory period" ending on 30 September 2014: PJ [131]. In April 2014, Plantic was expecting an offer from Braskem for a license agreement, but after delay, and with Mr Merchant increasingly frustrated by the ongoing funding requirements, in June 2014 Plantic engaged with Sealed Air about its interest in a sale of Plantic: PJ [132], [135], [139], [141]. Plantic adopted an explicit policy of dealing with Sealed Air in parallel with the negotiations with Braskem and Multivac: PJ [142]-[143], [156], [198]. On 24 July 2014, Sealed Air provided a non-binding letter of intent to purchase Plantic as "an asset sale or stock sale, as mutually agreed by the parties" on the basis of the business being acquired "free and clear of all liens and encumbrances", the company being "cash free and debt free", and conditional on the completion of due diligence. The offer had a closing date of 15 September 2014 (i.e. two weeks before the "critical deadline" of 30 September 2014 when Plantic had to decide about the deal with Multivac): PJ [143], [153], [160], FCJ [109]. Between July

and September 2014, Mr Merchant sought taxation advice about the potential sale of Plantic: PJ [150], [157], FCJ [110]. Consideration was given to the form of sale (share sale or asset sale) and how best to deal with the loans which Plantic owed to GSM and Tironui: PJ [144], [150]-[153], [157]-[184].

8. **The BBG share sale.** On 2 September 2014, Gordon Merchant No 2 Pty Ltd (**GM2**) as trustee for the Merchant Family Trust (**MFT**), sold around 10.3m shares in BBG to GSM Superannuation Pty Ltd as trustee of the Gordon Merchant Superannuation Fund (**GMSF**), for approximately $5.8m (the **BBG share sale**): PJ [185]-[186], FCJ [82], [113]. The sale price reflected the market value of the shares: PJ [295], FCJ [30]. One consequence of the BBG share sale was that MFT made a capital loss of approximately $56.5m, being a tax benefit that would crystallise *only if* MFT were able to sell the Plantic shares at a future date for a capital gain. Five other consequences were: (1) Mr Merchant maintained his level of control of BBG; (2) MFT received cash of $5.8m which was liberated from the superannuation environment; (3) GMSF received BBG shares at market value, such that the total value of the assets held in the concessionally taxed superannuation environment was not depleted; (4) MFT retained its other assets; and (5) Mr Merchant and his entities did not need to take on additional debt.[1]

9. **The sale of Plantic.** Negotiations with Sealed Air continued until November 2014 but did not eventuate in a sale: PJ [197]-[212], FCJ [116]. In the meantime, Kuraray Co Ltd expressed interest in Plantic. On 26 February 2015, the board of Kuraray resolved to approve the acquisition of Plantic if the GSM Loan and the Tironui Loan were forgiven: PJ [214]-[215], FCJ [117]. As explained by Logan J: "Kuraray, as with Sealed Air before it, was interested only in acquiring shares in Plantic if that company were … free of debts to entities controlled by Mr Merchant": FCJ [21]. The shares in Plantic were sold to Kuraray on 2 April 2015, which resulted in MFT deriving a capital gain of approximately $85m: PJ [228], FCJ [83], [119]. As part of the sale, the GSM Loan and the Tironui Loan were forgiven: PJ [227], FCJ [118].

10. **Cancellation of identified tax benefits.** On 20 July 2020, the Commissioner made determinations under Part IVA to cancel identified tax benefits from the BBG share sale and the forgiven debts. The BBG share sale scheme was identified by the Commissioner

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[1] See Logan J in dissent at FCJ [42]-[44] and [74]. The majority of the Full Court seems to have accepted that some of these occurred *as a matter of fact* (FCJ [270], [272], [273], [277], [296]), while rejecting the objective benefit to the entities involved (FCJ [263]-[265], [272], [273], [285]). This is discussed further below in the context of ground 1(b).

as follows (PJ [241], FCJ [128]):

> The scheme includes all of the actions and decisions that resulted in the transfer of 10,344,8228 BBG shares from MFT to GMSF. This includes Mr Merchant and Ms Paull, as directors of GM2 executing a standard share transfer form to transfer the BBG shares off-market to GMSF for $5.8million, with a recorded transfer date of 2 September 2014.

11. The Commissioner determined that the BBG share sale scheme was entered into or carried out for the dominant purpose of obtaining a tax benefit – to crystallise a capital loss which could be applied against the capital gain from the anticipated sale of Plantic: FCJ [84]-[86]. The tax benefit was identified as the $56.5m capital loss incurred on the share sale: FCJ [84](1). The Commissioner issued an amended notice of assessment to GSM, as the beneficiary presently entitled to the income of MFT: FCJ [84].

12. The Commissioner also identified a Tironui debt forgiveness scheme (the **Tironui scheme**) and a GSM debt forgiveness scheme (the **GSM scheme**) and formed the view that these schemes were substantially by way of or in the nature of dividend stripping within s 177E(1)(a)(ii), and made a determination to include in Mr Merchant's assessable income the amount of the forgiven loans: FCJ [304]-[305]. The Commissioner defined the debt forgiveness schemes in a way where the sale of the BBG shares realising a capital loss (the subject of the s 177D holding) was also the first, and integral, step in the each of debt forgiveness schemes: PJ [473]-[477], FCJ [306].

13. **Joint objections.** On 22 September 2020, Mr Merchant, GM2, and GSM lodged a joint objection in respect of the above assessments and related penalty assessments. On 27 July 2021, those objections were disallowed.

14. **Federal Court proceedings.** On 3 September 2021, Mr Merchant and GSM commenced proceedings in the Federal Court of Australia. At first instance, Thawley J concluded that s 177D was satisfied by the BBG share sale scheme: PJ [405]-[408]. His Honour also held that s 177E was satisfied in respect of both debt forgiveness schemes. On appeal, McElwaine and Hespe JJ upheld the primary judge's decision in respect of the BBG share sale scheme and the Tironui debt forgiveness scheme but overturned his Honour's decision on the GSM debt forgiveness scheme. Logan J dissented and held that neither s 177D nor s 177E applied to any of the schemes.

PART VI: ARGUMENT

15. This appeal (S158/2025) concerns the construction of s 177D and its application to the

BBG share sale. The related appeal (S157/2025) concerns the construction of s 177E and its application to the Tironui scheme and GSM scheme. These submissions cover the S158/2025 appeal, and the part of the S157/2025 cross-appeal and the notice of contention concerned with the purpose of the Tironui scheme and GSM scheme.

A. Submissions on the S158/2025 appeal (concerned with s 177D)

A.1 *Legislative scheme*

16. Part IVA of the ITAA36 applies, by s 177D(1), to any scheme where it would be concluded that those who entered into or carried out the scheme did so for the dominant[2] purpose of enabling a taxpayer to obtain a tax benefit in connection with the scheme, having regard to the eight matters set out in s 177D(2). Those matters "are posited as objective facts".[3] "Dominant purpose" means the "ruling, prevailing, or most influential purpose".[4] The purpose to be considered is that attributable to the persons who entered into or carried out the scheme, not the purpose of the scheme itself.[5] The inquiry is however objective:[6] "As the EM makes apparent, and consistent with the statutory text, it is the features of the scheme and its surrounding circumstances which are objectively examined through the s 177D factors… not… the subjective purpose or subjective motive of any party to the scheme".[7]

17. Under s 177D(3), Part IVA applies to a scheme only if the relevant taxpayer has obtained, or would but for s 177F obtain, a tax benefit in connection with the scheme. A "scheme" is defined in s 177A as "any agreement, arrangement, understanding, promise or undertaking", and "any scheme, plan, proposal, action, course of action or course of conduct". Under s 177C(1)(ba), a taxpayer is deemed to have obtained a tax benefit in connection with a scheme where they incur a capital loss during a year of income, which would not have been, or might reasonably be expected not to have been,

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2 ITAA36 s 177A(5).

3 *Federal Commissioner of Taxation v Peabody* (1994) 181 CLR 359 (***Peabody***) at 382 (the Court).

4 *Federal Commissioner of Taxation v Spotless Services Ltd* (1996) 186 CLR 404 (***Spotless***) at 416 (Brennan CJ, Dawson, Toohey, Gaudron, Gummow, Kirby JJ).

5 *Federal Commissioner of Taxation v Hart* (2004) 217 CLR 216 (***Hart***) at [15] (Gleeson CJ and McHugh J), [63] (Gummow and Hayne JJ).

6 *Hart* (2004) 217 CLR 216 at [37], [65] (Gummow and Hayne JJ); *Peabody* (1994) 181 CLR 359 at 382 (the Court).

7 *Minerva Financial Group Pty Ltd v Federal Commissioner of Taxation* (2024) 302 FCR 52 (***Minerva***) at [63] (the Court).

incurred if the scheme had not been entered into or carried out.[8]

18. The amount of the tax benefit is taken to be the amount of the capital loss: s 177C(1)(e). Where Part IVA applies, s 177F permits the Commissioner to determine that the capital loss was not incurred by the taxpayer during that year of income (and to give effect to such determination by making assessments accordingly).

A.2 *Ground 1(a) – failure to account for differences in legal entities*

19. A central aspect of the primary judge and the majority's reasoning as to purpose under s 177D was that Mr Merchant maintained control of the BBG shares before and after the sale, such that the sale "had no other practical, commercial or economic consequence for Mr Merchant as the ultimate controller" beyond the identified tax benefit: FCJ [232]; see also PJ [352], [403]-[404], FCJ [233], [296]-[297]. The BBG share sale was likened to a "wash sale" (where an investor sells an asset and then immediately repurchases it in order to lock in capital losses for tax purposes)[9]: FCJ [234]. The BBG share sale was similarly distinguished on this basis from a sale to a third party, which the Commissioner had conceded would not attract Pt IVA in otherwise the same circumstances (i.e. if the sale was conducted to realise a capital loss to offset a likely corresponding capital gain): FCJ [232]. Their Honours concluded that because the scheme "involved transactions between related parties, all controlled and ultimately owned by the same person, it was simple to look through and observe the significant benefits that accrued to Mr Merchant's interests as a whole": FCJ [285]; PJ [392].

A.2.1 *The first problem – differences between the entities involved were not considered*

20. It is true that Mr Merchant maintained ultimate control of the BBG shares. Mr Merchant wanted to maintain a substantial shareholding in BBG and consistently caused entities in the Merchant Group to acquire BBG shares so as not to have Merchant Group's shareholding diluted, including after the BBG share sale: PJ [267], [237]. This was a proper and lawful purpose. However, it is a misapplication of s 177D to treat MFT (a discretionary trust) and GMSF (a self-managed superfund) as though they are the same, such that there are no real practical, commercial, or economic consequences of the BBG share sale apart from the identified tax benefit.

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8 The combined effect of s 177CB(2) and the broad definition of 'scheme' is that any sale of an asset at a loss is a scheme whereby a taxpayer obtains a tax benefit. Part IVA will not apply to such a transaction only if obtaining a tax benefit was not the dominant purpose of those entering into or carrying out the sale.

9 *Cumins v Federal Commissioner of Taxation* (2006) 61 ATR 625 at [38] (Nicholson J).

21. ***First,*** MFT, GMSF, and their respective trustees are each subject to different legal regimes which affect what they can lawfully do. In respect of a discretionary trust, the trustee's duties, functions and powers are governed by the trust deed, the relevant *Trustee Act,*[10] as well as by common law principles. In respect of MFT, the trust deed provided the trustee with a very broad discretion to deal with the trust assets, including the power to transfer or lend any sum to any beneficiary or to the trustee or any company (cll 7 and 9), or "apply and invest all moneys at any time forming part of the Trust Fund in any such investments" as provided by the deed, which included the purchase of any interest in any business and the purchase of any real or personal property (cl 8).[11] The primary enforcement body for a breach of such a trust is the court.

22. The superannuation system is regulated and enforced by the Commissioner of Taxation, ASIC and APRA.[12] Unlike ordinary trusts, superannuation funds are governed by the SIS Act,[13] which provides for specific statutory covenants,[14] and other special rules,[15] which supplement (except to the extent of inconsistency) the other obligations imposed on the trustees under the trust deed,[16] or other general legal principles.[17] For example, a regulated superannuation fund (such as GMSF)[18] must be maintained solely for one or more of the "core purposes" set out in s 62(1)(a) of the SIS Act, which include the provision of benefits for members on or after their retirement or attainment of a certain age,[19] and the provision of death benefits to the member's dependents. Further, the trustee of a regulated superannuation fund is prohibited from certain dealings with the trust assets, including lending money of the fund to a member (SIS Act s 65(1)(a)(i)) and acquiring assets from a "related party",[20] other than listed securities acquired at market value, "business real property" acquired at market value, or an "in-house asset"

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10 *Trustee Act 1925* (NSW), *Trustee Act 1958* (Vic), *Trusts Act 1973* (Qld), *Trustee Act 1936* (SA), *Trustee Act 1898* (Tas), *Trustees Act 1962* (WA), *Trustee Act 1893* (NT), *Trustee Act 1925* (ACT).

11 MFT Trust Deed dated 31 October 1979 (as amended on 13 June 1980 and 16 October 1991) (Appellants' book of further materials (**ABFM**) 1 p 13-24, ABFM 2 p 34, ABFM 3 p 36).

12 *Superannuation Industry (Supervision) Act 1993* (Cth) (**SIS Act**) s 6.

13 And the *Superannuation Industry (Supervision) Regulations 1994* (Cth) (**SIS Regulations**).

14 SIS Act Part 6.

15 SIS Act Part 7.

16 GMSF Trust Deed dated 30 June 2006 (ABFM 4 p 40).

17 *Invensys Australia Superannuation Fund Pty Ltd v Austrac Investments Ltd* (2006) 15 VR 87 at [106] (Byrne J).

18 See SIS Act s 19 (definition of regulated superannuation fund).

19 See SIS Regulations Sch 1, Part 1, Item 106.

20 A "related party" includes a member of the fund, a relative of a member, a trustee of a trust controlled by the member, and a company that is sufficiently influenced by, or in which a majority voting interest is held by a member: SIS Act ss 10 (definition of "related party"), 70B (meaning of "Part 8 associates").

(which includes loans to or investments in a "related party")[21] acquired at market value that does not result in more than 5%[22] of the fund's assets being in-house assets (SIS Act s 66). These limits constrain the use that can be made of any assets held by a self-managed superannuation fund like GMSF (in contrast to the unfettered discretion of the trustee of MFT to deal with the trust's assets).

23. ***Second***, and relatedly, the interest of the "beneficiaries" of each entity in the trust assets is different. In a discretionary trust like MFT, "the entitlement of beneficiaries to income, or to corpus, or both, is not immediately ascertainable",[23] such that they may be better described as objects of a power than beneficiaries in the strict sense.[24] By contrast, Mr Merchant was the sole beneficiary of GMSF (PJ [352]), and had reached the preservation age (FCJ [272]), giving him a vested beneficial interest in the fund.[25] These differences would have objective significance for the people and entities involved, for example in the event of the following:

(a) **Bankruptcy**. Subject to certain limited exceptions, the interest of a bankrupt in a regulated superannuation fund (like GMSF) is not property divisible amongst the creditors of a bankrupt.[26] In contrast, the interest of a bankrupt in a discretionary trust may amount to property divisible amongst the creditors of a bankrupt where the trust is controlled by a trustee who is the alter ego of a beneficiary.[27]

(b) **Insolvency**. A corporate trustee of a regulated superannuation fund becomes a "disqualified person" under s 120(2) of the SIS Act on being wound up or on the appointment of an administrator or liquidator, such that it will be an offence under s 126K of the SIS Act if it is or acts as a trustee of a superannuation entity.[28] The corporate trustee of a discretionary trust is not subject to an equivalent regime.

(c) **Death**. In the case of a superannuation fund, benefits must be paid to the member's

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21 SIS Act s 71(1).
22 SIS Act ss 82, 83.
23 *Federal Commissioner of Taxation v Vegners* (1989) 20 ATR 1645 at 1649 (Gummow J).
24 *Kennon v Spry* (2008) 238 CLR 366 at [60], [62] (French CJ), [125] (Gummow and Hayne JJ).
25 *Finch v Telstra Super Pty Ltd* (2010) 242 CLR 254 at [30], [66] (French CJ, Gummow, Heydon, Crennan and Bell JJ); *Shimshon v MLC Nominees Pty Ltd* (2021) 66 VR 277 at [13] (Sifris and Walker JJA), [253] (Whelan JA).
26 *Bankruptcy Act 1966* (Cth) s 116(2)(d)(iii)(A).
27 *Bankruptcy Act 1966* (Cth) ss 116(1)(a), 116(1)(b); *Australian Securities and Investments Commission v Carey (No 6)* (2006) 153 FCR 509 at [29], [36]-[37] (French J).
28 See *Re Stansfield DIY Wealth Pty Ltd (in liq)* (2014) 291 FLR 17 at [35], [51] (Brereton J); *Federal Commissioner of Taxation v The Mai Family Pty Ltd (in liq)* [2019] FCA 865 (Besanko J).

legal personal representative or nominated dependents on the death of the member.[29] The same is not true of a discretionary trust.

(d) **A matrimonial dispute**. Superannuation payments can be split pursuant to Part VIIIB of the *Family Law Act 1975* (Cth) (the **FLA**),[30] and an interest in a superannuation fund is treated as "property" under the FLA.[31] Part VIIIB does not apply to an interest under an ordinary discretionary trust. A party would need to seek orders under s 79 of the FLA in respect of the trust assets, raising room for contestation, informed by the terms of the particular trust deed at hand, as to whether those trust assets constitute "property of the parties to the marriage".[32]

24. ***Third***, the two entities are also subject to different tax laws: the assessment of income derived through an ordinary trust is governed by Divs 6 and 6E of Part III of ITAA36 and Sub-Divs 115-C and 207-B of Chapter 3 of the *Income Tax Assessment Act 1997* (Cth) (**ITAA97**), while a special tax regime applies to superannuation funds under Div 295 of ITAA97. This can result in a preferable tax environment for holding assets. For example, while the superfund is in accumulation phase, investment earnings are generally taxed at 15% (but the effective tax rate for capital gains is 10% where the asset has been owned for 12 months or more), which is a concessional rate compared with higher individual marginal rates.[33] In the pension phase, investment earnings (including capital gains) are tax exempt if the relevant assets are set aside to meet current pension liabilities.[34] In contrast, beneficiaries of a discretionary trust pay tax on income distributed to them at their individual marginal rates, and a capital gain discount is only available if distributions are made to individuals, not corporate entities.[35]

25. The effect of these differences means that assets held in each distinct "environment" are subject to different restraints and protections. In the case of the BBG share sale from MFT to GMSF, these differences resulted in cash being "liberated" from the restrictions placed on GMSF, and the BBG shares being protected in the environment of GMSF.

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29 See GMSF Trust Deed cl 9.5 (ABFM 4 p 52).

30 See also *Family Law (Superannuation) Regulations 2001* (Cth), recently replaced by the *Family Law (Superannuation) Regulations 2025* (Cth).

31 FLA ss 4, 39, 90MC (now s 90XC).

32 See *Kennon v Spry* (2008) 238 CLR 366 at [66], [69]-[70] (French CJ); *In the Marriage of Goodwin* (1990) 101 FLR 386 at 391-392 (Nicholson CJ).

33 ITAA97 ss 115-5, 115-10(b), 115-15, 115-25, 115-100(b), 295-10; *Income Tax Rates Act 1986* (Cth) s 26(1)(a).

34 ITAA97 s 295-385.

35 ITAA97 s 115-10.

That Mr Merchant retained ultimate control of the BBG shares does not detract from the fact that these advantages were substantial consequences achieved by the share sale.

A.2.2 *The second problem – the significance of some differences was erroneously dismissed*

26. Their Honours accepted that "it is perfectly correct that assets held in the GMSF were subject to restrictions that did not apply to the MFT", but dismissed the significance of those restrictions on the basis that "[i]t was open to Mr Merchant, to withdraw cash in any amount from the fund and apply it to the MFT" (FCJ [272]). This counterfactual analysis suffered from several defects. The availability of this alternative did not negate the advantage of moving funds out of the restrictive environment of GMSF. Further, it ignored the fact that a lump sum payment would have depleted the total assets held in the concessionally taxed superannuation environment (and that Mr Merchant's ability to replenish the funds held in GMSF was affected by the limits on contributions under the SIS Act and the ITAA97).[36]

27. As to the protection afforded to assets held in GMSF, the majority concluded that this was "not an advantage", by reason of the primary judge's findings that the BBG shares were "a risky asset", unlikely to earn dividends, and that the effect of the purchase impaired the capacity of MFT to continue paying Mr Merchant a pension: FCJ [273]. The loss of pension was at best a neutral consideration, given the primary judge's finding that it would be funded elsewhere, presumably by the wider Merchant Group: PJ [399], FCJ [270]. More fundamentally however, the description of "advantage" here seems to reflect a judgment on the investment merits of the acquisition, rather than on the relevant "change in the financial position of" or "other consequence for" GMSF and Mr Merchant within the meaning of s 177D(2)(f) and (g).

28. In this respect, the majority incorrectly records the primary judge's finding as being that the BBG shares were a "risky asset", when the primary judge found that the BBG shares "were a riskier asset than cash": PJ [398]. This is inevitably the case with share investments and does not detract from the objective benefit of converting cash to a shareholding of the same value, given the potential for the risk to pay off and reap rewards in the concessionally taxed environment of the GMSF.

29. Further, the majority does not address the potential for the BBG shares to appreciate in

36 ITAA97 ss 291-15, 291-20, 292-80, 292-85, 292-90; *Superannuation (Excess Non-concessional Contributions Tax) Act 2007* (Cth) s 5. See also the restrictions discussed at [22].

value in the concessionally taxed environment of the GMSF. The shares were acquired at market value – i.e. a price that the market judged to reflect the risk and potential rewards of ownership of the shares. This is not a case where the capital loss was manufactured by artificially decreasing the value of the asset.[37] Plainly an objective purpose of Mr Merchant seeking to maintain overall control over BBG was to ensure he could profit from its shares increasing in value in the future (see FCJ [101]) and do so in the concessionally taxed environment of GMSF.

30. The majority's failure to consider the differences between MFT and GMSF in determining the purpose of the scheme undermines the intended operation of Part IVA. Obtaining a tax benefit cannot *ipso facto* prevail over the other legal and economic consequences of the shares moving from one legal entity to another distinct legal entity.

A.3 *Ground 1(b) – counterfactual inquiry miscarried*

A.3.1 *Relevant legal principles – the counterfactual enquiry required under s 177D*

31. This Court has held that to draw a conclusion under s 177D about the purpose of the persons who entered into or carried out the relevant scheme requires a counterfactual inquiry: a "comparison between the scheme … and an alternative postulate", or "consideration of what other possibilities existed".[38] Without this counterfactual lens, the matters in s 177D(2) are devoid of significance.[39] This counterfactual enquiry, relevant to purpose, is not however, a question of <u>causation</u>.[40] As recently explained by the Full Court:[41]

> The requisite dominant purpose is not to be drawn merely because, as a matter of objective fact, it is to be concluded that "but for" the tax benefit, another course of action would have been adopted. <u>Part IVA does not require that a taxpayer choose a form of transaction which results in the most tax or more tax being payable.</u>

32. Rather, the counterfactual inquiry required in applying s 177D(2) is a comparison

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37 Cf *Cumins v Federal Commissioner of Taxation* (2007) 66 ATR 57.

38 *Hart* (2004) 217 CLR 216 at [66] (Gummow and Hayne JJ). See also at [15], [18] (Gleeson CJ and McHugh J), [94] (Callinan J); *Spotless* (1996) 186 CLR 404 at 417, 424 (Brennan CJ, Dawson, Toohey, Gaudron, Gummow and Kirby JJ); *Federal Commissioner of Taxation v Consolidated Press Holdings* (2001) 207 CLR 235 (***Consolidated Press***) at [87] (the Court).

39 See also *Minerva* (2024) 302 FCR 52 at [100] (the Court).

40 *Hart* (2004) 217 CLR 216 at [15] (Gleeson CJ and McHugh J), [53] (Gummow and Hayne JJ); *Macquarie Finance Ltd v Commissioner of Taxation* (2005) 146 FCR 77 at [240] (Hely J); *Eastern Nitrogen Ltd v Commissioner of Taxation* (2001) 108 FCR 27 (***Eastern Nitrogen***) at [20] (Lee J); *British American Tobacco Australia Services Ltd v Federal Commissioner of Taxation* (2010) 189 FCR 151 at [46] (Dowsett, Jessup and Gordon JJ).

41 *Minerva* (2024) 302 FCR 52 at [62] (the Court).

between the "ordinary" or "routine" manner of entering into or carrying out a transaction, with one tax consequence, and the actual manner in which the scheme was carried out or entered into, which achieves substantially all the same commercial consequences but with better tax consequences.[42] All things otherwise being equal, if there is no explanation for adopting the alternative (contrived) manner, other than the tax consequences, it can be concluded that the scheme was entered into or carried out for that dominant purpose,[43] even though the particular scheme also advances a wider commercial objective or bears the character of a rational commercial decision.[44]

33. The requirement for this counterfactual enquiry is evident from the purpose of Part IVA, which was intended as a general measure against "blatant, artificial or contrived" tax avoidance arrangements; it was not intended to affect "arrangements of a normal business… kind".[45] In order to assess whether a measure is "artificial or contrived", this necessarily requires a comparison with the "ordinary" or "routine" <u>form</u> of transaction which achieves the same outcome in <u>substance (cf s 177D(2)(b))</u>. This is not to demand that there be only one alternative postulate or to require exacting identity between the actual transaction and the alternative postulate, but rather reflects the fact that Part IVA does not apply merely because less tax is paid by selecting one form of transaction,[46] or if taxation planning played a part in the shaping of the transaction.[47]

34. An illustration of the required counterfactual enquiry is provided by *Spotless* (1996) 186 CLR 404. In that case, the taxpayers held approximately $40m of surplus funds from a successful public flotation of shares, which was available for short-term investment. Those funds were invested on-deposit in the Cook Islands. In determining what a reasonable person would conclude as to the dominant purpose of the taxpayers in entering into and carrying out the particular scheme, the joint judgment compared the

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42 *Hart* (2004) 217 CLR 216 at [18] (Gleeson CJ and McHugh J), [67] (Gummow and Hayne JJ), [94] (Callinan J); *Spotless* (1996) 186 CLR 404 at 422 (Brennan CJ, Dawson, Toohey, Gaudron, Gummow and Kirby JJ).

43 *Hart* (2004) 217 CLR 216 at [18] (Gleeson CJ and McHugh J), [68] (Gummow and Hayne JJ); *Spotless* (1996) 186 CLR 404 at 422 (Brennan CJ, Dawson, Toohey, Gaudron, Gummow and Kirby JJ).

44 *Hart* (2004) 217 CLR 216 at [16] (Gleeson CJ and McHugh J); *Spotless* (1996) 186 CLR 404 at 415, 416 (Brennan CJ, Dawson, Toohey, Gaudron, Gummow and Kirby JJ).

45 Explanatory Memorandum to the Income Tax Laws Amendment Bill (No 2) 1981 (Cth) at 2-3.

46 *Hart* (2004) 217 CLR 216 at [15] (Gleeson CJ and McHugh J), [52]-[53] (Gummow and Hayne JJ); *Minerva* (2024) 302 FCR 52 at [65] (the Court).

47 *Spotless* (1996) 186 CLR 404 at 416 (Brennan CJ, Dawson, Toohey, Gaudron, Gummow and Kirby JJ).

scheme to an investment of the funds in Australia.[48] This comparison revealed that the investment in the Cook Islands had three significant consequences: (1) the investment yielded a return at least equivalent to that which the taxpayer would have received if the funds had been invested in Australia; (2) the interest rate earned on the investment was approximately 4% below the applicable bank rates available in Australia (described as a "commercially unattractive" aspect of the investment); and (3) it was anticipated that the interest received from the deposit would be exempt from income tax in Australia because withholding tax had already been paid on it in the Cook Islands. This comparison made clear that the anticipated tax advantages were "the key to the whole transaction",[49] because without them, "the proposal would have made 'no sense'".[50]

35. A further illustration is provided by *Hart* (2004) 217 CLR 216. In that case, the taxpayers borrowed money under a "split loan facility", part of which was applied to purchase a principal place of residence and part of which was applied to refinance an investment property. The loan agreement provided for the periodical payments to be directed to the first part of the loan, while interest on the balance of the loan was allowed to accrue and be capitalized and compounded. To draw a conclusion about purpose, a comparison was made between the actual scheme and other forms of loan.[51] This comparison revealed that the consequences of the scheme included: (1) the loan provided money for the financing and refinancing of the two properties; (2) the monthly repayments would be the same as those under other forms of loan; (3) because interest would continue to accrue and be capitalized on that part of the loan used for the investment property, the amount owing would increase above the value of the property; (4) the interest rate was marginally higher than would have been charged under a standard principal and interest loan; and (5) the taxpayers anticipated that they could deduct all of the interest attributed to that part of the loan referable to the investment property against their assessable income (which would be a higher amount compared to an ordinary loan). This comparison revealed that "the terms on which the loan was made available were explicable *only* by the taxation consequences";[52] the scheme "depended

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48 *Spotless* (1996) 186 CLR 404 at 422 (Brennan CJ, Dawson, Toohey, Gaudron, Gummow and Kirby JJ), citing with approval the observations of Cooper J below in *Commissioner of Taxation v Spotless Services Ltd* (1995) 62 FCR 244 at 285 and noting the similar observations of Beaumont J at 270.

49 *Spotless* (1996) 186 CLR 404 at 412 (Brennan CJ, Dawson, Toohey, Gaudron, Gummow and Kirby JJ).

50 *Spotless* (1996) 186 CLR 404 at 422 (Brennan CJ, Dawson, Toohey, Gaudron, Gummow and Kirby JJ).

51 *Hart* (2004) 217 CLR 216 at [67] (Gummow and Hayne JJ). See also at [18] (Gleeson CJ and McHugh J), [94] (Callinan J).

52 *Hart* (2004) 217 CLR 216 at [68] (Gummow and Hayne JJ).

entirely for its efficacy upon tax benefits generated by arrangements … that had <u>no explanation</u> other than their fiscal consequences”.[53]

36. In each of these cases, the counterfactual enquiry revealed that the “ordinary” manner of conducting the transaction achieved *all the same* commercial consequences, except for the anticipated tax benefit, allowing a conclusion that the predominant purpose of those involved in the scheme was tax avoidance, even though the scheme also advanced a commercial objective (shared with the ordinary manner of conducting the transaction).

A.3.2 *The correct application of the counterfactual enquiry in this case*

37. **Identifying the counterfactual.** The “ordinary” or “routine” manner of conducting the BBG share sale was to sell the shares, at market value, to an independent third party. Ordinarily – barring the example of a wash sale – such a transaction will not attract the operation of Part IVA, even though the sale took place when a corresponding capital gain was likely (as conceded by the Commissioner before the Full Court: FCJ [31], [232]). Indeed, the Commissioner expressly conceded on the hearing of the appeal that, had the BBG share sale entailed a sale not to a related party but to an unrelated third party, the dominant purpose of the sale would not have been to obtain a tax benefit. This would remain so, even though a crystallised loss of the same amount would thereby have become available: FCJ [31].

38. An objective application of the considerations in s 177D(2) must lead to such a conclusion. Such a sale would have resulted in MFT receiving an amount of cash, and in MFT, and all other related persons mentioned in s 177D(2)(f), ceasing to be exposed to the risks and potential rewards that would attend the ownership of BBG shares (see Logan J at FCJ [40]). Those would be changes in the financial position of those persons, or “other consequences” for such persons, relevant to the dominant purpose inquiry under s 177D(2)(f), (g) and (h). They would be changes of substance and not merely form, as relevant to s 177D(2)(b). Timing (s 177D(2)(c)) and tax effect (s 177D(2)(d)) might suggest that obtaining the associated capital loss tax benefit was <u>a</u> purpose of the transaction (although for the reasons given below, timing is better described as a neutral factor). But the other consequences of the transaction mean that it would be impossible to conclude, objectively, that obtaining the tax benefit was a purpose that prevailed over any other purpose so as to be the <u>dominant</u> purpose.

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[53] *Hart* (2004) 217 CLR 216 at [18] (Gleeson CJ and McHugh J).

39. This conclusion reflects the fact that an "ordinary" incident of ownership – indeed, an essential characteristic – is the power to sell or dispose of the property.[54] Implicit in this is that a person is entitled to choose when, on what terms, and to whom they sell. A further concomitant of this power – one that is recognised by the purpose of Part IVA, the structure of the CGT regime, and this Court[55] – is that a taxpayer is not prohibited from choosing the time, terms, and purchaser, *so as to maximise their tax position*.

40. Under the CGT regime, a taxpayer is taxed on their "net capital gain" for a given income year, which is worked out after deducting both current and carried-forward past-year capital losses.[56] By taxing capital gains and losses as realised,[57] the CGT regime contains a structural feature that an owner is entitled to take advantage of when exercising the ordinary incidents of ownership.[58] The CGT regime does not require taxpayers to defer realising capital losses until a point in time when they will have no gain for the loss to offset. As Logan J held at FCJ [40], when a share investment does not prove good, "it can be prudent to cut one's losses and to do so at a time when it is prudent to realise a capital gain". Were s 177D interpreted to outflank this essential incident of ownership it would run counter to the structural features of the CGT regime.

41. **Conducting the counterfactual enquiry.** If it is accepted that the "ordinary" or "routine" manner of conducting a share sale is to sell the shares at market value to an independent third party, it next becomes necessary to ask: what features of the BBG share sale distinguish it from this routine transaction? Tellingly, here, it is not the taxation consequences, which <u>remained identical</u> (subject to the operation of Part IVA). As set out at [8], and discussed below, the BBG share sale had other objective consequences, apart from the taxation benefits, which would not have been achieved had the sale been to an independent third party. *First,* Mr Merchant would not have maintained his level of control of BBG. *Second,* GMSF would not have acquired the

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54 *Yanner v Eaton* (1999) 201 CLR 351 at [25] (Gleeson CJ, Gaudron, Kirby and Hayne JJ). See also A M Honoré, "Ownership", in AG Guest (ed) *Oxford Essays in Jurisprudence* (1961) 107 at 117-118.

55 *Spotless* (1996) 186 CLR 404 at 416 (Brennan CJ, Dawson, Toohey, Gaudron, Gummow, Kirby JJ); *Hart* (2004) 217 CLR 216 at [15] (Gleeson CJ and McHugh J). See also FCJ [39] (Logan J).

56 ITAA97 s 100-50.

57 ITAA97 ss 100-20(1), 100-35 and 104-10(1) and (4).

58 Cf *Hart* (2004) 217 CLR 216 at [3] (Gleeson CJ and McHugh J). Their Honours recognise that it is part of the scheme of the ITAA36 that interest on money borrowed to finance the purchase of private property is not an allowable deduction, while the interest on money borrowed to finance an investment property is an allowable deduction. This being the case, "in considering the terms of the borrowing for investment purposes, the taxpayer [may take] into account the deductibility of the interest in negotiating the terms of the loan. How could a borrower, acting rationally, fail to take it into account?".

BBG shares, which provided Mr Merchant with the benefit of having that asset (with its potential to appreciate in value) in the protected environment of a regulated superannuation fund (and which carried with it all the additional consequences set out above). Both were significant and legitimate (in the sense of proper and lawful) consequences. This comparison demonstrates, clearly, that obtaining a tax benefit was not the dominant purpose of those carrying out the sale.

42. Further, as discussed below, there is <u>no alternative transaction</u> that would have resulted in all of the same commercial consequences as the BBG share sale. A sale to a third party would have reduced Mr Merchant's control. A lump sum payment from GMSF would have reduced the total assets in the superannuation fund. Drawing on debt would have increased the indebtedness of Mr Merchant's entities. Selling other assets would have ended MFT's exposure to those assets. Doing nothing would not have resulted in MFT receiving $5.8m in cash and GMSF gaining exposure to the economic consequences of the shares. Each of those things is a matter within the scope of s 177D(2). The fact that the BBG share sale was the only transaction which would have achieved all of the commercial consequences set out at [8] should equally have led – inexorably, as Logan J held in dissent – to a conclusion that obtaining a tax benefit was not the dominant purpose of those carrying out the sale.

A3.3 *Error in the Full Court's approach to the counterfactual enquiry*

43. While the majority of the Full Court, in the context of the s 177E question, acknowledged that "an objective consideration of purpose without regard to the alternatives open to [achieve the relevant transaction] is artificial and sterile" (FCJ [356]), when it came to the s 177D enquiry, the majority wrongly compressed the counterfactual enquiry. This can be seen at a number of levels.

44. ***First***, the majority eschewed the relevant counterfactual enquiry by stating that "resolution of the dominant purpose question… does not turn on a high level analogy as though it stands apart from the specific and limited matters at s 177D(2)" and that such an inquiry "distracts attention from what objectively occurred" (FCJ [233]).

45. ***Second***, while there was no error in the majority acknowledging that a "routine" manner of conducting a share sale was by sale at market value to a third party (FCJ [231], [297]), there *was* error in the majority failing to carry out the full counter-factual enquiry into this postulated alternative. If a conclusion about dominant purpose by reference to the

matters in s 177D(2) is to be informed meaningfully by a consideration of what "other possibilities" existed, the other possibilities must be ones that achieve the *same non-tax consequences* (of the kind mentioned in s 177D(2)) as the actual scheme. The majority needed to ask: would this alternative form of transaction achieve *all* of the same commercial consequences as the share sale that was actually entered into? The answer to this question, as demonstrated above, is no. The form actually adopted for the transaction was the <u>*only*</u> one which achieved all the desired (and objectively desirable) commercial consequences. Once that point is reached, the conclusion of a dominant tax purpose cannot stand.

46. ***Third***, the majority erred by stating that "what stands this case apart from the 'routine' realisation of a capital loss to be offset against an actual or anticipated capital gain", was that "the control of the shares and the effective economic ownership did not alter and there was no divestment of investment risk" (FCJ [297]). Those high-level generalisations mask important differences: see [19]-[25] above. But even if taken on their own terms, the majority erred in treating them as *conclusive* of the s 177D enquiry.

47. The majority effectively reasoned that, if the taxpayers were not prepared fully to divest themselves of all ability to own, control and benefit from the BBG shares, s 177D did not permit them to exercise the ordinary incident of ownership of selling the shares, with their ordinary tax consequences. On this reasoning, once the sale of Plantic was in prospect, MFT was put to an election:

(a) *Sell* the BBG shares to a third party, which the Commissioner conceded would allow it to realise a capital loss which could be offset against a future capital gain without intervention of s 177D (but thereby reduce the Merchant Group's stake in BBG); or

(b) *Defer the sale* of the BBG shares until after the end of the financial year in which the Plantic shares were sold at a profit, such that the capital loss could not be offset against <u>that</u> capital gain, and could come into value only if some other asset of MFT was sold at a profit at a future date (provided that such sale was not also in prospect at the time of the BBG share sale – in which case, the BBG share sale would have had to be yet further deferred).

48. This cannot be the intended operation of s 177D. If a proper analysis of the eight factors in the context of a sale to a third party produces the consequence that the dominant purpose is <u>not</u> obtaining a tax benefit (as both sides agree), this conclusion is not altered

simply because Mr Merchant lawfully and legitimately sought to maintain control over the BBG shares by selling the shares from one of his entities to another.

49. ***Fourth***, the error in the majority's reasoning extends beyond its treatment of a counterfactual sale to a third party. The majority erected a series of *further counterfactuals*, variously said to achieve *singular consequences* of the BBG sale, without considering whether any of these other alternatives could meet *all* of the consequences of the BBG sale. We deal with the five consequences at [8] above in turn.

50. **(1) Mr Merchant maintaining his level of control of BBG** (FCJ [226]). Mr Merchant had a history of acquiring BBG shares and wished to maintain a substantial shareholding in BBG because of his connection to the company: PJ [267], FCJ [278]-[279]. The majority dismissed the objective benefit of Mr Merchant maintaining his stake in BBG through the BBG sale because he could have done so by **doing nothing at all**: FCJ [285]. That is true, but on that alternative postulate *none* of the other consequences would have been achieved for Mr Merchant and the Merchant Group more broadly.

51. The majority stated that there was "no objective explanation why the maintenance of control purpose required the sale to be timed as it was" (FCJ [288]). Equally, however, the timing of the BBG share sale was <u>not</u> explicable by reference to any anticipated tax benefit in connection with the sale of Plantic. At the time of the BBG share sale, negotiations with Sealed Air for the sale of Plantic were still ongoing. While the Plantic sale was a "real possibility", previous negotiations with other parties had not eventuated in a sale (PJ [104], [112]) and Sealed Air had already sought to reduce the price (PJ [156]), such that it was objectively reasonable to expect that the sale may not complete: cf PJ [187]. The form of any sale to Sealed Air (whether asset sale or share share) was not agreed (PJ [153]), and the form would have a significant impact on the utility to MFT of the capital loss on the BBG sale, because an asset sale would likely involve a much smaller capital gain being made by MFT and at a later time (eg on Plantic being wound up). Plantic was also pursuing the sale negotiations with Sealed Air in parallel with the negotiations with Braskem and Multivac about alternative deals which would not involve a sale of MFT's Plantic shares: PJ [142]-[143], [156], [198]. If obtaining a tax benefit had been the dominant purpose, the BBG sale could have been deferred to later in the financial year (when there would be greater certainty about any sale of Plantic) and had the same tax consequence, yet that did not happen, despite another trading window being available before the end of the 2015 financial year (PJ [377]).

52. **(2)(a) MFT receiving a cash injection** (FCJ [223]). Between 2012 and 2014, the operating expenses of MFT substantially exceeded its income (PJ [273]), which was addressed by selling down investments (both before and after the BBG share sale) (see PJ [274], [293], [302]) and drawing down on a margin facility (PJ [300]): FCJ [260]. A consequence of the BBG share sale was that MFT received a cash injection of $5.8m in circumstances where it was accepted that its "available cash … decline[d] significantly from April 2012" (FCJ [263]) and ran out on several occasions (see FCJ [256]).

53. The primary judge postulated, at the time of the BBG share sale, that the forecast cash requirements of Plantic could have been met **from MFT's existing cash reserves**, or in the *"same way as the MFT had funded its expenditure over the period 2012 to 2014"*, such that "Plantic's funding did not need to be sourced from the sale of BBG shares": PJ [309]. The majority agreed (FCJ [261]), noting that an alternative means to remedy the cash shortfall was to **draw down on the NAB margin facility** (FCJ [263]). Yet the alternatives postulated by the primary judge and the majority would not have achieved all the same consequences as the BBG share sale, and in particular would not have satisfied Mr Merchant's objective of avoiding additional debt.

54. The majority erred in suggesting that the primary judge had rejected Mr Merchant's evidence that he had an aversion to debt: FCJ [264]. The primary judge found that Mr Merchant did not like debt and was uncomfortable with the margin facility: PJ [301], [307]. This is consistent with the evidence of the use of the margin loan facility – where substantial drawdowns were substantially repaid within one to six months of the relevant draw down (see FCJ [257]). That there was a history of drawdowns is beside the point (cf FCJ [264]) – as the evidence demonstrated, borrowing money "to help keep our heads above water" was considered a measure of last resort in meeting Plantic's funding needs: PJ [277].

55. **(2)(b) The cash being liberated from the superannuation fund** (FCJ [225]). The majority dismissed this as an objective advantage because "it was open to Mr Merchant, to **withdraw cash in any amount from the fund and apply it to the MFT**": FCJ [272]. A mere withdrawal of cash would not have maintained the total value of the assets in the fund and would have created difficulties in the event Mr Merchant sought to re-instate the fund balance. The majority also considered that the liberation of $5.8m in cash was disproportionate in value to the "ultimate economic advantage" of the capital loss occasioned by the BBG share sale, which was approximately $12.8m: FCJ [274]-

[275]. This failed to account for the value (both fiscal and non-fiscal) of the other consequences simultaneously achieved by the BBG share sale, and for the fact that the $56.5m capital loss was not contrived, such that the "ultimate economic advantage" would have been identical had the sale been to a third party.

56. **(3) GMSF received the BBG shares at market value, such that the total value of the assets held in the protected environment of a superannuation fund was not depleted** (FCJ [224]). No alternative way of achieving this objective was identified. Instead, the majority concluded that it was "not an advantage" for the BBG shares to be held in the protected environment of a superannuation fund (FCJ [273]), but for the reasons set out above at [27], this was erroneous. Further, as explained in relation to ground 1(a), no consideration was given to the real legal and economic consequences of holding the BBG shares in the protective environment of the superannuation fund and maintaining the overall level of assets in such protection.

57. **(4) MFT retained its other assets.** This consequence was not addressed by the primary judge or the Full Court, despite being raised in submissions below.[59]

58. **(5) The Merchant Group's level of debt was maintained.** The majority did not consider this consequence separately but dismissed it on the basis that Mr Merchant did not have an aversion to debt: FCJ [264]. As set out above, this was erroneous.

59. **Overall:** Judged objectively, the presence of these consequences, taken as a whole, means that it cannot be said that the BBG share sale had "no explanation" other than the taxation benefit, or that without that benefit the sale "would have made no sense".[60]

A.4 *Conclusion*

60. Only by failing to account for the relevant differences between MFT and GMSF, could it be concluded that the BBG share sale was different for s 177D purposes to the counterfactual "routine" sale to a third party to realise a capital loss to offset a likely capital gain. Each scheme would result, or did result, in meaningful legal, commercial and economic consequences for the entities involved beyond obtaining a tax benefit, and neither therefore attracts the operation of Part IVA.

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59 Appellants' Outline of Submissions dated 8 October 2024 at [49] (ABFM 8 p 88-89).

60 Cf *Eastern Nitrogen* (2001) 108 FCR 27 at [17]-[20] (Lee J), [116]-[119] (Carr J); *Federal Commissioner of Taxation v Macquarie Bank Ltd* (2013) 210 FCR 164 at [256]-[261], [294]-[297], [300]-[302] (Middleton and Robertson JJ).

B. Submissions on the S157/2025 cross-appeal and notice of contention <u>as to purpose</u>

B.1 *Structure of these submissions*

61. **Purpose of tax avoidance.** The majority found that, under s 177E(1)(a)(ii), the Tironui scheme and the GSM scheme had the necessary purpose of tax avoidance (FCJ [343]-[358]). These findings are the subject of ground 1(a) of the Merchant parties' cross-appeal (which concerns the Tironui scheme), and ground 1(a) of the Merchant parties' amended notice of contention (which concerns the GSM scheme). The Merchant parties' primary position, which is detailed below, is that the majority of the Full Court found purpose of tax avoidance where none existed, and that Logan J was correct to hold that both schemes were far removed from the necessary purpose: FCJ [53], [56].

62. **Substantially the effect of scheme by way of or in the nature of dividend stripping.** The majority found that the Tironui scheme <u>did</u> have the necessary effect, while the GSM scheme <u>did not</u>: compare FCJ [377]-[381] with FCJ [382]-[395]. These findings are the subject of ground 1(b) of the Merchant parties' cross-appeal (which concerns the Tironui scheme), and ground 1(b) of the Merchant parties' amended notice of contention (which concerns the GSM scheme). The Merchant parties' submissions on this issue will be made in the related appeal (S157/2025).

B.2 *Legislative scheme*

63. Section 177E of the ITAA36 relevantly provides that Part IVA applies to a scheme where the following conditions are met. *First,* the scheme is either a scheme by way of or in the nature of dividend stripping (s 177E(1)(a)(i)), or a scheme "having substantially the effect of a scheme by way of or in the nature of a dividend stripping" (s 177E(1)(a)(ii)). *Second,* as a result of a scheme, any property of the company is disposed of (s 177E(1)(a)). *Third,* in the opinion of the Commissioner, the disposal of that property represents, in whole or in part, a distribution of profits of the company (s 177E(1)(b)). *Finally,* if, immediately before the scheme was entered into, the company had paid a dividend out of profits of an amount equal to the amount of profits the distribution of which is represented by the disposal of the property, an amount would have been included, or might reasonably be expected to have been included, by reason of the payment of that dividend, in the assessable income a taxpayer (s 177E(1)(c)).

64. While s 177E(1)(a)(ii) in terms poses an enquiry into the "effect" of the scheme relative to the core concept instantiated in s 177E(1)(a)(i), this Court has held that the necessary

"effect" cannot be found unless the dominant purpose of the scheme is "tax avoidance",[61] understood as avoidance of tax of the same kind as that which is characteristic of a scheme by way of or in the nature of dividend stripping (being the avoidance of tax on a distribution of profits to the shareholders of the company, had that distribution been made immediately before the scheme was entered into). The requirement for a tax avoidance purpose under both sub-para (i) and (ii) explains why "a scheme which produced a substantial consequence which was in any respect the same as a consequence of dividend stripping would not ipso facto fall within para (a)(ii)".[62] This was correctly recognised by the majority of the Full Court at FCJ [337]-[342].

B.3 ***The purpose of the debt forgiveness schemes***

65. The majority held that both the GSM scheme and the Tironui scheme had the requisite tax avoidance purpose (FCJ [346]). This was on the basis that both schemes were objectively intended to derive a higher capital gain on the sale of the Plantic shares, "that was objectively intended to be sheltered by the capital losses that the Merchant Group believed had been incurred on the transfer of the BBG shares": FCJ [344], [345]. The majority accepted that purpose in the context of s 177E looks to the intended outcome of the scheme, such that the s 177D Determination made by the Commissioner to cancel the capital loss on BBG share sale was not relevant in considering the intended outcome of the debt forgiveness schemes: FCJ [342]-[344]. The majority concluded that there was "no economic reason for GSM and Tironui to each bear a loss on fully recoverable loans", and that there were "a myriad of ways in which the related party [loans] may have been dealt with prior to or upon the completion of the sale": FCJ [350].

B.3.1 *The first problem – the BBG share sale scheme was a component of the schemes*

66. The first problem with the reasoning of the majority arises at the outset in the event the Merchant parties are successful in their appeal on the s 177D issue – that is, if the Merchant parties successfully demonstrate that the BBG share sale was not entered into or carried out for the purpose of obtaining a tax benefit. The mere fact that MFT had capital losses as a result of the BBG Share Sale, at the time of the Plantic sale, cannot justify a conclusion that the dominant purpose of the debt forgiveness schemes was to avoid tax on a distribution of profits from GSM and Tironui if those capital losses were

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61 *Consolidated Press* (2001) 207 CLR 235 at [126], [129] (the Court).

62 *Lawrence v Federal Commissioner of Taxation* (2008) 70 ATR 376 at [81] (Jessup J).

themselves not obtained for the purpose of avoiding tax and MFT having non-BBG capital losses was not an identified component of either scheme.

B.3.2 *The second problem – the counterfactual enquiry miscarried*

67. In any event, the majority also erred in failing to conduct the required counterfactual enquiry to ascertain the purpose of the scheme, which necessitates a comparison between the scheme in question and the other possibilities that existed to achieve the same commercial end.[63]

68. ***First**,* the majority did not consider the alternative ways in which <u>the scheme</u> could have been accomplished and focused instead on the alternative ways in which the related party loans could have been "dealt with" (which were only one aspect of each identified debt forgiveness scheme): FCJ [350]-[352]. This analysis was particularly sterile in circumstances where it was accepted by the primary judge and the majority that if the schemes had been identified as comprising solely of the forgiveness of the debts, s 177E would <u>not</u> have been attracted: PJ [472], [477], FCJ [315]. This is because this step, by itself, did not result in the avoidance of any tax, it merely "shift[ed] value": PJ [477].

69. ***Second**,* in any event, the "other possibilities" considered by the majority did not achieve the same commercial end as the debt forgiveness schemes. Those possibilities were identified at FCJ [350] as including MFT subscribing for further Plantic shares to finance the repayment of the loans and then selling the new shares as part of the sale of Plantic, the loans being assigned to the purchaser, or the purchaser paying less for the Plantic shares and refinancing the loans with new debt or an equity injection (FCJ [350]). The majority observed that "the evidence does not suggest that, to the extent that different commercial consequences would follow from the alternatives, those different commercial consequences objectively explained the dominant purpose of the debt forgiveness in this case": FCJ [352]. That is not the test. Just as with s 177D, the counterfactual enquiry under s 177E is <u>not</u> a question of causation. Merely because, in comparison to the other options available, the loan forgiveness schemes resulted in a better tax outcome for the Merchant parties, does not mean the dominant purpose was tax avoidance. Indeed, in accepting that different commercial consequences would follow from the suggested alternatives, the majority implicitly accepted that these

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63 See *Commissioner of Taxation v Consolidated Press Holdings Ltd* (1999) 91 FCR 524 at [174] (the Court). See also *Automative Invest Pty Ltd v Federal Commissioner of Taxation* (2024) 98 ALJR 1245 at [112]-[117] (Edelman, Steward and Gleeson JJ).

counterfactuals were inappropriate comparators, because they did not achieve substantially all the same consequences as the loan forgiveness schemes.

70. Properly analysed, the dominant purpose of the loan forgiveness schemes was to facilitate the sale of Plantic for the highest ultimate return to the Merchant Group. Indeed, this conclusion is compelled by the findings of the majority. The majority accepted that that "the dominant purpose of the sale of the Plantic shares was <u>not</u> tax avoidance" (FCJ [354]), that "it is objectively true that the MFT sought to maximise the sale price of Plantic" (FCJ [246]), and that "[e]ach of the GSM and Tironui debts was forgiven with <u>the principal intended outcome that the MFT would receive a higher price for the Plantic shares</u>" (FCJ [344]). See also PJ [548], [557]. As observed by the primary judge (and accepted by the majority), "[l]ooking at the position practically and commercially, a third-party purchaser… would… pay more for the Plantic shares if Plantic did not have the related-party loans of about $55 million (and was therefore essentially debt free)": PJ [524], FCJ [349].

71. In finding that there was "no economic reason" for GSM and Tironui to forgive the loans to Plantic, the majority failed to give adequate consideration to the relationship between these parties. As recognised by Logan J, "[t]he relationship between GSM, Tironui, MFT and Mr Merchant was such that the forgiving of the Plantic loans benefited the MFT and, in turn, each of GSM and Tironui as beneficiaries of the MFT. The debt forgiveness just increased the amount of the capital gain that MFT made on the sale of the shares in Plantic": FCJ [53].

72. The evidence also fails to support the conclusion that the predominant purpose of the GSM and Tironui schemes was tax avoidance. For example, the email of 28 August 2014 from Mr Burgess (a tax partner at EY who advised the Merchant Group in relation to the sale of Plantic) set out calculations for an asset sale instead of a share sale, so that "if you are deep in negotiation next week trying to get the transaction across the line and it appears that an asset sale might be the only way to get that done, that you have an understanding of what the fall back positions might be for [Mr Merchant] to help make the judgment on price etc": PJ [175]. Mr Burgess's email of 3 September 2014 explained that "if the 'cost' of getting Sealed Air to accept a share sale is much more than $2m-$3m, then it might be better to agree to an asset sale and aim for an increase in the sale price to compensate [Mr Merchant] for his increased costs" (being the extra

tax cost of an asset sale): PJ [178].

73. These communications demonstrate that the dominant consideration in the structure of the Plantic sale was selling at an acceptable after-tax return for Mr Merchant and the Merchant entities involved. A form of transaction where the appellants paid more tax was acceptable if the sale price was higher. This cannot be reconciled with a conclusion that the dominant purpose was tax avoidance. Contrary to the majority's reasoning at FCJ [354], this evidence was not consistent with the dominant purpose of the debt forgiveness being "the obtaining of an expected tax benefit", but rather is consistent with the dominant purpose of the debt forgiveness being to maximise the sale price of the Plantic shares (which had an <u>incidental</u> effect on the expected tax benefit because of the direct correlation between the sale price and the expected capital gain).

B.4 *Why special leave should be granted in respect of the cross-appeal*

74. Special leave should be granted in respect of the cross-appeal because it raises two issues of significant general importance. *First,* the cross-appeal raises the same issue as that raised in the S158/2025 appeal (concerned with s 177D) as to the proper counterfactual enquiry that is required when considering purpose under Part IVA. *Second,* the cross-appeal raises the same issue as that raised in the Commissioner's appeal as to the true point of intersection between s 177D and s 177E. This is because the BBG share sale (and its character as a s 177D scheme) is a defined element of each of the debt forgiveness schemes, which affects the outcome of the purpose enquiry.

PART VII: ORDERS SOUGHT

75. The orders sought by the appellants are set out in the notice of appeal in S158/2025 and the notice of cross-appeal in S157/2025.

PART VIII: TIME ESTIMATE

76. It is estimated that up to 4.5 hours will be required for oral argument (including reply) in both appeals.

Dated 27 November 2025

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ANNEXURE TO APPELLANTS' SUBMISSIONS

No	Description	Version	Provision(s)	Reason for providing this version	Applicable date or dates
1	*Bankruptcy Act 1966* (Cth)	Compilation C66 (18 July 2014 to 17 August 2015)	s 116	Act in force on the date of the relevant transaction	2 September 2014: date of BBG share sale
2	*Family Law Act 1975* (Cth)	Compilation dated 1 July 2014 to 17 August 2015	ss 4, 39, 79, 90MC, Part VIIIB	Act in force on the date of the relevant transaction	2 September 2014: date of BBG share sale
3	*Income Tax Assessment Act 1936* (Cth)	Compilation dated 18 July 2014 to 29 September 2014	Div 6 and Div 6E of Pt III, Part IVA	Act in force on the date of the relevant transaction	2 September 2014: date of BBG share sale
		Compilation dated 20 March 2015 to 13 April 2015	Part IVA		2 April 2015: date of Plantic share sale
4	*Income Tax Assessment Act 1997* (Cth)	Compilation dated 1 September 2014 to 19 September 2014	Sub-Div 115-C and Sub-Div 207-B of Ch 3, Div 295 of Ch 3, ss 100-20, 100-35, 100-50, 104-10, 115-5, 115-10, 115-15, 115-25, 115-100, 291-15, 291-20, 292-80, 292-85, 292-90, 295-10, 295-385.	Act in force on the date of the relevant transaction	2 September 2014: date of BBG share sale
5	*Income Tax Rates Act 1986* (Cth)	Compilation dated 25 June 2014 to 21 June 2015	s 26	Act in force on the date of the relevant transaction	2 September 2014: date of BBG share sale
6	*Superannuation (Excess Non-concessional Contributions Tax) Act 2007* (Cth)	Current (compilation dated 25 June 2014)	s 5	Act in force on the date of the relevant transaction	2 September 2014: date of BBG share sale
7	*Superannuation Industry (Supervision) Act 1993* (Cth)	Compilation dated 1 July 2014 to 24 February 2015	ss 6, 10, 19, Part 6, Part 7, 70B, 71, 82, 83, 120, 126K	Act in force on the date of the relevant transaction	2 September 2014: date of BBG share sale
8	*Trustee Act 1925* (NSW)	Current	Generally	For illustrative purposes only	N/A
9	*Trustee Act 1958* (Vic)	Current	Generally	For illustrative purposes only	N/A

10	*Trusts Act 1973* (Qld)	Current	Generally	For illustrative purposes only	N/A
11	*Trustee Act 1936* (SA)	Current	Generally	For illustrative purposes only	N/A
12	*Trustee Act 1898* (Tas)	Current	Generally	For illustrative purposes only	N/A
13	*Trustees Act 1962* (WA)	Current	Generally	For illustrative purposes only	N/A
14	*Trustee Act 1893* (NT)	Current	Generally	For illustrative purposes only	N/A
15	*Trustee Act 1925* (ACT)	Current	Generally	For illustrative purposes only	N/A
16	*Family Law (Superannuation) Regulations 2001* (Cth)	Compilation dated 1 July 2013 to 1 July 2015	Generally	Regulations in force on the date of the relevant transaction	2 September 2014: date of BBG share sale
17	*Family Law (Superannuation) Regulations 2025* (Cth)	Current	Generally	For illustrative purposes only	N/A
18	*Superannuation Industry (Supervision) Regulations 1994* (Cth)	Compilation dated 27 August 2014 to 16 December 2014	Sch 1, Part 1, Item 106	Regulations in force on the date of the relevant transaction	2 September 2014: date of BBG share sale