[HIGH COURT OF AUSTRALIA.]

BELL . . . . . APPELLANT;

AND

FEDERAL COMMISSIONER OF TAXATION RESPONDENT.

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1951. SYDNEY, *Sept.* 26-28; *Oct.* 2, 3.

1952. *July* 18.

McTiernan J.

1953. SYDNEY, *April* 13, 14; *May* 8.

Dixon C.J., Williams, Webb, Fullagar and Kitto JJ.

Income Tax (Cth.)—Assessable income—Acquisition and sale of surplus war materials—Torokina Island—Residents of Australia—Arrangement for purpose of effect of defeating, evading or avoiding liability to tax—Formation of ad hoc organizations—Partnerships and companies—Proceeds of sale—Income or capital—Income from property—Income Tax Assessment Act 1936-1947 (*No.* 27 *of* 1936—*No.* 63 *of* 1947), *ss.* 6, 44 (1) (*a*), 260.

Section 260 of the *Income Tax Assessment Act* 1936-1947, so far as relevant, provides:—"Every contract, agreement, or arrangement made or entered into, orally or in writing, . . . shall so far as it has or purports to have the purpose or effect of in any way, directly or indirectly . . . (*c*) defeating, evading, or avoiding any duty or liability imposed on any person by this Act . . . be absolutely void, as against the Commissioner, or in regard to any proceeding under this Act, but without prejudice to such validity as it may have in any other respect or for any other purpose."

Held that the section has no further or other operation than to eliminate from consideration for tax purposes such contracts agreements or arrangements as fall within the descriptions it contains; it assists the commissioner only if, when all contracts agreements and arrangements having such a purpose or effect as the section mentions are obliterated, the facts which remain justify his assessment.

Held, further, that the word "arrangement" is the third in a series which as regards comprehensiveness is an ascending series, and extends beyond contracts and agreements so as to embrace all kinds of concerted action by which persons may arrange their affairs for the purpose, or so as to produce the effect, mentioned in the section. A conveyance or transfer of property may be void as against the commissioner as being part of a wider course of action which constitutes an arrangement in the relevant sense of the word.

Jaques v. *Federal Commissioner of Taxation* (1924) 34 C.L.R. 328 and *Clarke* v. *Federal Commissioner of Taxation* (1932) 48 C.L.R. 56 referred to.

Decision of *McTiernan* J. affirmed.

APPEAL from *McTiernan* J.

In an assessment for income tax purposes made by the Federal Commissioner of Taxation in respect of income said to have been received by the taxpayer, George James Bell, during the year ended 30th June 1948, the commissioner set out therein taxable income of £1,495 personal exertion and £11,000 property and a total amount of £9,425 8s. 0d. tax payable.

The taxpayer objected to the assessment on the grounds, *inter alia* :

1. That the assessment was excessive and contrary to law.

2. That there was not any provision in the *Income Tax Assessment Act* 1936-1947 for taxing him on £11,000 property income, shown in the adjustment sheet issued with the assessment notice as " amount received in respect of your share in Simmonds, Harper and Larkin Ltd. included as assessable income ".

3. That the £11,000 property income as taxed, was received by him from the sale of a share in Simmonds, Harper and Larkin Ltd., which share was held by him as an investment and, therefore, there was no provision in the *Income Tax Assessment Act* for taxing him on the profit on sale of such share, namely £11,000 less £1 cost of the share.

4. That the £11,000 property income as assessed could not be deemed to be a dividend if such was taxed as a dividend by the commissioner, as no dividend was ever received by him from Simmonds, Harper and Larkin Ltd.

5. Without prejudice to ground 4, that if the £11,000 could be deemed to be a dividend, then such was received by him from a source in Papua and therefore the dividend must be exempt from Federal income taxation under the provisions of s. 7 of the *Income Tax Assessment Act.*

6. Without prejudice to the abovementioned grounds of objection, there was not any provision in the *Income Tax Assessment Act* whereby the £11,000 taxed at property rate of tax, could be so taxed. If the £11,000 could be deemed to be subject to taxation, then it could only be subject to taxation spread over the income years ended 30th June 1947 and 1948 and taxed at personal exertion rate of tax. Full facts relating to the circumstances under which the £11,000 was received by the taxpayer were, he stated, held by the commissioner.

The commissioner disallowed the objection whereupon pursuant to a request by the taxpayer the objection was treated as an appeal to the High Court.

The appeal came on for hearing before *McTiernan* J.

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The relevant facts and statutory provisions are sufficiently set out in the judgments hereunder.

M. F. Hardie K.C. and *J. D. Evans*, for the appellant.

J. D. Holmes K.C. and *E. J. Hooke*, for the respondent.

Cur. adv. vult.

July 18, 1952.

The following written judgment was delivered by :—

McTIERNAN J. This is an appeal from an assessment of Federal income tax which was levied for the financial year, 1st July 1947 to 30th June 1948.

The taxpayer complains of the inclusion of the sum of £11,000, which is assessed as income from property, in the taxable income. This sum is described in the adjustment sheet, which the Commissioner of Taxation sent with the notice of the assessment, in these words : " Amount received in respect of your share in Simmonds, Harper and Larkin Ltd."

This company was on 15th January 1947 incorporated at Port Moresby. The taxpayer at all material times was a resident of Australia.

The issued capital of the company was only seven £1 shares. On 24th March 1947 the taxpayer was registered as the holder of one of these shares, and on 3rd February 1948, according to the books of the company, he ceased to be a member. Its books represent that on 4th February 1948 it paid a dividend of £11,000 on each of its seven shares.

The sum of £11,000, which the taxpayer contends was wrongly included in the taxable income, represents the dividend which the company professed to pay.

If the dividend was paid as represented by the company's books, it would satisfy the definition which is given, by s. 6 (1) of the *Income Tax Assessment Act* 1936-1947, to the term " dividend " ; and such payment would also satisfy all the conditions necessary, under s. 44 of the Act, to make a dividend paid to a shareholder, who is a resident of Australia, part of his assessable income.

The description, which appears in the adjustment sheet, of the sum of £11,000 is wider than the term " dividend ", although it includes such a payment. The sum of £11,000 would come within the description if it was a receipt of the nature of income and the share itself was the source from which the taxpayer directly or indirectly derived the moneys. In the latter case, by reason of s. 25 of the

Act, the sum would have been part of the taxpayer's assessable income; and by reason of the definitions of "income from personal exertion" and "income from property" it would have been income of the latter class.

The taxpayer admits that in the "year of income", which ended on 30th June 1948, he received the sum of £11,000 for which, in the income tax return lodged in respect of that period, he did not account as income.

The case which the taxpayer set up in the appeal was that the sum of £11,000 was the proceeds of the sale of the share which he held in the company and he acquired and held it as an investment. If the evidence establishes that case the sum was not assessable income.

As the taxpayer's complaint against the assessment is that it is excessive by reason of the inclusion of the sum of £11,000, it is necessary to observe that s. 190 (*b*) of the Act provides that, upon an appeal by a taxpayer from an assessment, the burden of proving that the assessment is excessive rests upon him. In order to succeed in the appeal the appellant has the burden of proving that the sum of £11,000 was the proceeds of the sale of the share which he acquired in the company, as he does not account for the receipt of the sum otherwise than by setting up that he sold the share for £11,000. The appeal must fail if upon the whole of the evidence the taxpayer has failed to discharge that burden.

The taxpayer adduced evidence that on 24th March 1947 a share in the company was transferred to him by Basil T. Swanton, a resident of Port Moresby, in consideration of £1, and that on 2nd February 1948, the taxpayer transferred the share to Ralph Corlett, a resident of the same place, in consideration of £11,000 paid to the taxpayer by Corlett. The two transfers are in evidence. The company's books show that, in pursuance of these transfers respectively, the taxpayer became and, after a period of less than a year, ceased to be a member of the company. The date of the former event was 24th March 1947 and of the latter event 3rd February 1948. The taxpayer said in evidence that he received the consideration of £11,000 for which he transferred the share to Corlett. This is an excessive simplification of an extremely artificial series of banking operations of which the commissioner adduced evidence, and in the course of which the taxpayer alleged that he received from Corlett the sum of £11,000 as consideration for the sale of the share.

The taxpayer relied on the transfers and his own evidence of the receipt of £11,000 to prove that on 2nd February 1948, Corlett

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purchased the share and paid him £11,000 for it. Specific evidence that the share was not acquired for the purpose of sale was not adduced for the taxpayer. If he was assessable to tax on the basis that he realized £11,000 by the sale of the share, the net profit was assessable as income from personal exertion.

The commissioner was not concerned with the rebuttal of the taxpayer's case that he did not acquire the share for the purpose of sale. He was concerned with the rebuttal of the taxpayer's assertion that he sold the share to Corlett for £11,000 and divested himself of it before the company on 4th February 1948 professed to pay a dividend of £11,000 on each of its shares. If the taxpayer's case that he sold the share to Corlett for £11,000 failed, the taxpayer's allegation that he bought it as an investment would not be of much materiality. If he failed to prove that he sold the share to Corlett, the share stands out as the only source from which the taxpayer could have derived the sum of £11,000. He did not put forward any other case than that he sold the share.

The commissioner made three alternative and inconsistent contentions. First, it was contended for the commissioner that the transaction between the taxpayer and Corlett was a sham. Facts were elicited on behalf of the commissioner with the object of establishing that contention. In *Jaques* v. *Federal Commissioner of Taxation* (1), *Isaacs* J. said " A sham transaction is inherently worthless, and needs no enactment to nullify it ". The commissioner's contention, as I understand it, relates both to the supposed sale and the transfer. There is much difficulty in deciding that the transfer was a nullity. The taxpayer in fact executed it and it operated to convey to Corlett at least the taxpayer's legal title to the share. Consistently with the sale being a sham, the transfer could operate to divest the taxpayer of the legal title to the share.

Secondly, the commissioner contends that the transaction between the taxpayer and Corlett was hit by s. 260 of the Act. This section assumes a transaction is valid until it strikes. But the section applies only to a contract, agreement, or arrangement. *Deputy Federal Commissioner of Taxation* v. *Purcell* (2); *Jaques' Case* (3) and *Clarke* v. *Federal Commissioner of Taxation* (4). In the second of these cases, *Isaacs* J. said of s. 53 of the *Income Tax Assessment Act* 1915-1918, which is parallel with s. 260 of the present Act, that the " collocation " of words " contract, agreement, or arrangement " does not include a " conveyance or transfer of property, legal or equitable, as such " (5). Section 260 could not be applied to

(1) (1924) 34 C.L.R. 328, at p. 358.
(2) (1921) 29 C.L.R. 464.
(3) (1924) 34 C.L.R. 328.
(4) (1932) 48 C.L.R. 56.
(5) (1924) 34 C.L.R., at pp. 358, 359.

the transfer of the share from the taxpayer to Corlett without careful consideration of the abovementioned cases and, perhaps, without overruling the dictum made by *Isaacs* J. in *Jaques' Case* (1) as to the scope of the words " contract, agreement, or arrangement ".

The commissioner's third contention would, if accepted, involve not only the transaction between the taxpayer and Corlett but also the formation of the company, and the other company, Torokina Disposals Pty. Ltd. to which reference will be made. The contention was that the formation of these companies was part of an " arrangement " which fell within s. 260. If this contention was upheld, the sum of £11,000 would be assessable as the taxpayer's share of a total " profit " rendered assessable income by s. 26 (*a*). Such " profit " is income from personal exertion. For the taxpayer, it was argued that the statutory powers of the court upon an appeal from an assessment would not enable the court to give effect to the contention, even although it was held to be right, because the sum of £11,000 was assessed as income from property.

The defence of the inclusion of the sum in the taxpayer's assessable income by three inconsistent alternatives has increased the intricacy of the case. Each contention raises difficult questions, especially the second and third contentions.

Evidence of things done as far back as September 1946 and subsequently to 4th February 1948 was elicited for the commissioner mainly, if not solely, to establish the second and third contentions. The evidence consists of oral testimony and documents. It covers much detail, but there is hardly any conflict between the witnesses, at any rate, on matters which are material in this appeal. The evidence deals with a number of matters to which it does not seem to me to be necessary to refer.

The salient facts proved are as follows. In September 1946, the taxpayer and six other men bought for £10,000 a large quantity of military trucks and accessories which the army had dumped at Torokina. The seven men had previous experience as dealers in the Territory. They bought the goods for resale in Australia and elsewhere. In October 1946 they entered into a formal agreement of partnership. They adopted the firm name of Simmonds, Harper and Larkin. Each partner contributed £2,000 to the capital of the partnership and their interests were equal. The principal object of the partnership was to sell the goods deposited at Torokina and it was their intention to sell the bulk in Australia. When the ship was being loaded with the goods consigned to Sydney, one of the partners was accidentally killed. His widow appears to have been

(1) (1924) 34 C.L.R. 328.

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taken into the partnership or, at any rate, to have become the beneficial owner of his share.

The taxpayer and his six associates were residents of Australia. To their dismay they learned that the profits which they expected to make from the sale of the goods in Australia would be subject to income tax. They were advised to adopt a plan whereby it was expected that the tax could be minimised.

The substance of the plan appears in a paragraph of Exhibit 5. It was as follows :

" A Company should be registered in New Guinea to purchase 'Disposal' goods, and then sell such goods in *New Guinea* at a profit to a Company registered in Australia. Care must be taken to see that the sale of goods to the Australian Company is effected in New Guinea. A direct order by the Australian Company to the New Guinea Company would constitute a sale in New Guinea by the New Guinea Company. As the profit would have been derived by the New Guinea Company from a source in New Guinea, then the profit would not be subject to Australian Income Taxation, under Section 7 quoted in (5) above. The New Guinea Company may also be considered to be a resident of Australia (see definition of resident of Australia in (4) above), but notwithstanding this the decision in the *Waterloo Pastoral Co. Ltd.* v. *Federal Commissioner of Taxation* (1) should apply.

If the above is correct, then the New Guinea Company could over a number of years pay dividends to its shareholders so that the shareholders would receive a certain dividend each year on which Federal Income Tax would be payable, but the dividends being spread over a number of years would minimise taxation payable by the shareholders ".

Pursuant to this advice, Simmonds, Harper and Larkin Ltd. was incorporated at Port Moresby and Torokina Disposals Pty. Limited at Sydney. Mr. White, a solicitor practising at Port Moresby, formed the first company. He and six residents of Port Moresby, whom he selected, signed the memorandum of association of Simmonds, Harper and Larkin Ltd. The firm furnished Mr. White with £7 with which he paid for the seven shares allotted to him and the other six residents of Port Moresby. Mr. White and these six persons were the dummies of the seven members of the firm. With the exception of Mr. White, they were, as regards the company, ciphers. It was in fact controlled by Mr. White as the agent of the partnership.

(1) (1946) 72 C.L.R. 262.

No further capital than the seven shares allotted to the subscribers of the memorandum of association was issued. The Sydney company went through the form of making an offer to the Port Moresby company to buy the goods, sent to Sydney, for £170,000, and on 27th January 1947 the latter company accepted this offer. The correspondence relating to the offer and acceptance was submitted to a meeting which was held on 4th March 1947 of the directors of the Port Moresby company.

Torokina Disposals Pty. Ltd. employed the taxpayer and other members of the firm as salesmen and paid them wages for their services. The Torokina goods were quickly sold and very substantial sums were obtained for them.

The members of the firm decided to take over the direct control of the Port Moresby company, as these sums were due for transmission to it. The shares held by the seven original nominees were transferred to the seven partners. The transfers represented that £1 was paid for each share. Basil T. Swanton, who transferred a share to the taxpayer, was one of the seven nominees. But it was a matter of indifference whether the share held by Swanton or any other nominee was transferred to the taxpayer. The transfers of the shares are dated 24th March 1947. All the members of the firm, other than the widow of the member who was accidentally killed at Torokina, became the directors of the Port Moresby company. They superseded directors who were original shareholders. The taxpayer took the place of Mr. White as chairman of directors.

The members of the firm were no longer content with a gradual distribution of the profits of the venture by way of dividends, as contemplated by the original plan devised to minimise income tax. All the members of the firm were residents of Australia and would for that reason be liable to pay income tax, at property rates, on the dividends paid to them. The purpose of the original plan was to limit their liability to that amount of tax. The author of the original plan formulated a new scheme designed to enable the members of the firm to enjoy at once the whole profits of their venture and to avoid the payment of any income tax in respect of the profits. The gist of the new scheme was that the share of each member of the firm would ostensibly be sold at a price equal to a dividend, the amount of which was predetermined at £11,000. Under the scheme each partner would receive £11,000 in the guise of the proceeds of the sale of the share which he or she held in the company. In order to perfect the scheme, each member of the firm would need to represent that he held the share as an investment. This the taxpayer did in his income tax return. In this appeal the

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effectiveness of the scheme is put to the test. The scheme was reduced to writing. A summary of the scheme is to be found in Exhibit 1. It is necessary to set out this document.

"Simmonds Harper & Larkin Limited

Routine for 2nd, 3rd & 4th February, 1948.

Monday 2nd February, 1948

1. Seven prospective purchasers to have or to open accounts with Bank of New South Wales at Port Moresby prior to 2/2/1948.

2. Directors' Meeting (present Directors)

(*a*) Authorise Norman White to operate on Company's Banking account and complete all necessary bank authorities.

(*b*) Authorise acceptance of Bank Draft for £78,520 from Torokina Disposals Pty. Limited in full settlement for purchase of articles sold to that Company.

(*c*) Authorise payment of travelling expenses of £80 to each of the five directors attending the meeting. These payments should be made by open cheque which could be cashed.

(*d*) Present Directors resign.

3. Deposit to credit of Company's banking account Bank Draft for £78,520 from Torokina Disposals Pty. Limited.

4. General Meeting (Present Shareholders)

(*a*) Formal Business

(*b*) Increase number of Directors to seven

(*c*) Elect new Directors.

5. Norman White to draw six cheques all dated 2.2.1948 each for £11,000 for payment as a loan to credit of banking account of each of his six nominees.

6. Norman White and each of six nominees will each draw an open cheque payable to the named shareholder 'or Bearer' for £11,000 all dated 2/2/1948 payable in favour of the present shareholder from whom each proposes to purchase.

7. Share transfers all dated 2.2.1948 from each of seven present shareholders to be delivered to each of new shareholders in exchange for cheque for £11,000 in each case. These cheques could be held by the Bank Manager for safe custody until next day when after the cheque for £77,000 has been drawn they should be converted to drafts payable in Sydney.

Tuesday, 3rd February, 1948.

Directors' Meeting (New Directors)

(*a*) Register Transfers of shares to purchasers.

(*b*) Authorise loan of £77,000 to Norman White. Draw cheque dated 3/2/1948 for payment to his personal account.

Note. By arrangement with Bank Manager the cheque for £77,000 and the cheques referred to in paras. 5 and 6 above can be cleared simultaneously on 3.2.1948 but should appear in the Bank ledgers in the order in which they appear on this routine. Each present shareholder will then have an open cheque for £11,000 which should be converted to a draft payable in Sydney.

Wednesday 4th February, 1948.

A. General Meeting (New Shareholders)

B. Declare Dividend of at least £11,000 per share

B. Pay Dividend cheque to each shareholder by seven cheques all dated 4/2/1948

C. Each cheque to be paid to personal account of each new shareholder.

D. Each of the six new shareholders repays to Norman White loan of £11,000 by cheque dated 4/2/1948.

E. Norman White pays all six cheques to his personal account.

F. Norman White repays to Company loan of £77,000 by cheque dated 4/2/1948.

Note. By arrangement with Bank Manager the cheques referred to in paras. B. C. D. E. and F. can be cleared simultaneously on 4.2.1948 but should appear in the Bank ledgers in the order mentioned above.

Final result of all Steps.

The Company will have :—

(*a*) Seven new Shareholders.

(*b*) Seven new Directors.

(*c*) Cash credit balance of approximately £1,000 representing the existing credit balance together with the draft from Sydney £78,520 less Directors' fees £120, Travelling Expenses £400 and Dividend £77,000.

. . . . . .

Note. Arrangements have been made with the Bank of New South Wales Sydney that sufficient exchange will be paid in Sydney on original Draft to Port Moresby to cover transfer of funds to Port Moresby and back to Sydney so that Drafts drawn in Port Moresby payable in Sydney will be free of any exchange payment.

Important. All cheques should be drawn in favour of the appropriate payee '*or Bearer*'.

All cheques except those in favour of the present shareholders should be crossed '*not negotiable*'. The cheques in favour of the present shareholders should be drawn in favour of each ' or bearer ' and not crossed so that they can be cashed or exchanged for Drafts payable in Sydney. The drafts should be crossed ' Not Negotiable ' ".

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Mr. White, whose name is mentioned in this document, was the solicitor who formed the Port Moresby company. He selected the persons who were to take the parts of the " prospective purchasers ". Six residents of Port Moresby were selected and Mr. White assumed one of the parts. Most of the persons whom he selected had no bank accounts. Mr. White arranged that they would have bank accounts in order to enable them to be effective instruments in the operation of the scheme. In par. 6 of the scheme, these " prospective purchasers " are described as " nominees ". The taxpayer and most of the members of the syndicate travelled to Port Moresby and on the dates mentioned in the routine attended the meetings of directors and any meetings which it provided that they should attend. The taxpayer brought from Sydney a bank draft for £78,500. He paid these moneys into the company's account at the bank in Port Moresby. The moneys were transmitted by Torokina Disposals Pty. Ltd. The total amount which it nominally owed to the Port Moresby company according to the contract between them was £170,000. The account between them was settled at £78,500, but this fact is not so surprising when it is remembered that both companies were, apparently, under the same control. The agenda prescribed, by the routine, for the meetings which it required to be held was carried out.

Mr. White and his six fellow " nominees " carried out their parts in the scheme. The banking arrangements for which the scheme provided were made and the bank fulfilled its part.

Each " nominee ", including Mr. White, drew a cheque dated 2nd February 1948 for £11,000 payable to a member of the firm. The cheque bearing the taxpayer's name was signed by Ralph Corlett. The taxpayer received this cheque from Mr. White. He also received cheques drawn in favour of the members of the partnership who did not travel to Port Moresby. The taxpayer received these cheques from Mr. White on behalf of those members. It was unimportant which nominee signed the cheque which was made payable to the taxpayer or any other member of the firm.

The taxpayer signed a transfer dated 2nd February 1948 whereby he conveyed the share he held in the Port Moresby company to Corlett. This transfer is in evidence. On 3rd February 1948, in pursuance of the scheme, the transfer was registered. All the other members of the firm signed transfers purporting to convey the other six shares to nominees. They drew the cheques payable to the transferors.

The taxpayer and the other members of the firm who travelled to Port Moresby personally took the cheques which Mr. White

handed to them on 2nd February to the bank. They did so immediately after receiving the cheques. They lodged the cheques at the bank for safe custody under the arrangement mentioned in par. 7 of the " routine ".

The crux of the scheme was the manipulation of the sum of £77,000, part of the total amount of £78,500. which was transmitted to the Port Moresby company by Torokina Disposals Pty. Ltd. It is plain upon the terms of the scheme that the result of its execution was that the moneys derived by the taxpayer and each of his partners, when the bank at Port Moresby issued the bank drafts, was in fact one-seventh of the sum of £77,000. It seems to me that the question which it is necessary to decide is who paid the sum of £11,000 to each of the partners. Did the company pay it ? The taxpayer's case is that it was paid by Mr. White or one of his nominees as consideration upon the sale of a share. Mr. White was interposed between the company and the partners in the guise of a borrower of the sum of £77,000. In my opinion he was not that in fact, but merely an automaton of the taxpayer and his partners. The same is true of each of Mr. White's nominees. Although each was interposed in the guise of a borrower of £11,000 from Mr. White and a purchaser of a share, they were all merely automatons of the partners. The scheme gives to the seven portions of the company's funds which were supposed to be loaned to the " prospective purchasers " the false colour of consideration paid for each of the seven shares.

The conclusion which I draw is that Mr. White and his selected nominees were only conduits through whom the sum of £77,000 was paid in equal shares by the company to the taxpayer and his partners, and the supposed loans and purchases of the shares were fictitious. The minute book records a decision taken by the company to lend the sum of £77,000 to Mr. White. I am not satisfied that the company made a genuine loan to him or that he made a genuine loan of £11,000 to the persons whom he selected as his fellow " prospective purchasers ". Corlett was called by the commissioner as a witness. He was ignorant of the name of the company in which Mr. White made him a shareholder and had no inkling as to the value of a share in the company.

Upon the whole of the evidence the taxpayer has not proved that Corlett really purchased the share transferred to him for £11,000 or at all. I find that the taxpayer only feigned to sell the share to Corlett. However, there is no doubt that the taxpayer executed a transfer of the share to Corlett and the company's books show that the transfer was registered. The direction on this

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matter, in the routine, was to register the transfers to Corlett and the others on 3rd February 1948. The date appointed by the routine for the payment of the dividends was 4th February 1948. The company professed to comply with that direction. But to draw cheques for this purpose and to pay them into the accounts of the seven nominees was a piece of *legerdemain*. The compliance with the routine in these respects created the appearance that dividends amounting to £77,000 were paid to the seven nominees. This was a false appearance. There was only one sum of £77,000 to manipulate under the directions contained in the routine. That sum was exhausted when the seven bank drafts were issued by the bank at Port Moresby to the taxpayer and his associates. The total amount of these drafts was £77,000. The company did not have another sum of £77,000 to distribute among Mr. White and his six fellow shareholders. There is evidence that his name for them was " shareholders of convenience ". Neither Mr. White nor any of his " shareholders of convenience " received anything out of the sum of £77,000 with which Mr. White juggled in carrying out the scheme. The drawing of the seven cheques, dated 4th February 1948, for £11,000, and the payment of the cheques into accounts of Mr. White and his " nominees " amounted to nothing but a pretence that the company paid dividends to them. The test of the matter is that in point of fact none of them received anything out of the £77,000 which had been available for the payment of dividends. It seems to me that the scheme was so devised that such a misadventure as that £11,000 would fall into the lap of any of them could not happen.

Upon the receipt of the bank drafts at Port Moresby, if not on the previous day, the taxpayer and his associates completely severed themselves from the Port Moresby company. Mr. White became the sole beneficial owner of the company's remaining assets. Practically, they consisted of the residue of the sum of £78,500 left after the sum of £77,000 had been paid by the tortuous manner provided in the scheme to the taxpayer and his associates, and the expenses of executing the scheme had been met. Apparently the taxpayer and his associates let Mr. White become the sole beneficial shareholder as remuneration for his services. But his fellow " shareholders of convenience " received nothing but small sums either as consideration for the transfer of the shares in their names or as remuneration for allowing Mr. White to use them in order to operate the scheme. These sums were paid by Mr. White.

The question whether, if the company had in fact advanced the sum of £77,000 to Mr. White for the purpose of the scheme, it was

lawful for the company to do so, was not raised in the case. As I am of opinion that there is no evidence which would justify the finding that the moneys were transferred to an account in Mr. White's name, by way of a genuine loan of the money, it is not necessary for me to deal with that question.

Upon the whole of the evidence I am not satisfied that the taxpayer derived the sum of £11,000 from the sale of his share to Corlett or any other person. On the contrary, I find that the taxpayer received the sum from the company, and it was derived by him out of the company's profits available for the payment of a dividend. In my opinion the sum was income which the taxpayer obtained by reason of the distribution, by the company, of a sum of £77,000. These moneys were profits of the company. The sum, in my opinion, was correctly described as an amount which the taxpayer received in respect of his share. The sum did not fall within any category of "income from personal exertion" which is defined in s. 6 (1) of the Act, and it was therefore within the definition, which is in this sub-section, of "income from property". I find that there was no payment in fact to Corlett of a dividend of £11,000 on the share which the taxpayer transferred to him.

The reasons for which I have arrived at the conclusion that the sum of £11,000 was not wrongly included in the assessment do not follow any of the contentions put on behalf of the commissioner but for the reasons which I have stated the appeal should be dismissed.

I dismiss the appeal with costs.

From that decision the taxpayer appealed to the Full Court of the High Court.

M. F. Hardie Q.C. (with him *J. D. Evans*), for the appellant. On the evidence, both documentary and oral, the proper inference to be drawn from the transaction was that there was a sale and transfer of the shares. As from the date when they were transferred, on 2nd February 1948, the transferors, the Australian shareholders, had not any further right to, or title or interest in, the shares. The shares vested at law and in equity in Mr. White, the solicitor at Port Moresby, and the other six persons at Port Moresby to whom the shares were transferred. There was not any arrangement or understanding at all as to what was to happen to the sum of approximately £1,000 left to the credit of the company's account. There were not any conditions imposed. The purchasers acquired

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the shares and, as from the date of the transfers, the Australian shareholders ceased to have any further interest in the shares, or in the company. From the point of view of its legal incidence and effect the transaction was just the same as if there had been a sale of shares under an agreement that provided that the purchaser need not pay the purchase price at the moment but could take control of the company, declare a dividend and then use the dividend to pay the purchase money. There is not any provision in the *Income Tax Assessment Act* 1936-1947 to preclude a person who owns shares in a company, but who cannot afford to have a dividend declared to him because of his liability to income tax, from obtaining a purchaser who can buy the shares and will be free from liability to pay income tax on any dividend that may be declared in respect of those shares. Mr. White, having bought out the other six New Guinea shareholders, has been the sole beneficial owner of the shares in that company from the time the transaction took place in February 1948. There is nothing in the document referred to as the "Routine" inconsistent with the shares being sold in the manner in which they were sold. The judge appealed from did not really address his mind to the crucial question as to the persons entitled to the funds as and from 4th February 1948. The dividends declared were not dividends of the Australian syndicate holders, therefore the previous Australian shareholders could not be taxed on those dividends. The whole of the evidence points to one conclusion only, namely that as from 4th February, when the Australian shareholders left and went back to Australia, Mr. White and his nominees were the beneficial owners of the shares. They must have become the beneficial owners of those shares by virtue of the transfers effected on 2nd February. That being established it shows that the New Guinea people were the beneficial owners of the shares when the dividend was declared. Any equity of the appellant in the shares when the dividend was declared was received by way of purchase price and not by way of dividend. The genuine nature of the transaction was not in any way affected by the fear that the arrangement might go wrong. The desire of the appellant and his fellow shareholders was to sell the shares at a good price. The documents establish that not only was the legal title to the share transferred from the appellant to Corlett before 4th February, but also that payment for the share had been fully made before that date. There is not any justification for the decision in the Court below that the commissioner was entitled to assess the appellant on the basis that he had received from the company an income or distribution of £11,000. The commissioner is

not entitled to get round the difficulty he is in under the Act, because residents of New Guinea are not liable for Federal income tax, by claiming and issuing an assessment on the basis that the vendor of the share must be treated as being the person who received the dividend. If the purchaser received the dividend and then used it, in effect, to make payment for the share he had bought two days previously, that does not in any way give its receipt by the appellant the characteristics of a receipt of income. It was not a dividend, it was purchase money. After the Australian shareholders had departed from Port Moresby they did not take any further interest in the matter at all. Mr. White was free to deal with the company in such way as he desired. The Australian shareholders parted with their legal and equitable interest in the shares at some point of time on 2nd, 3rd or 4th February 1948. Mr. White and his nominees acquired beneficial ownership at some point of time after 4th February 1948. The true and correct interpretation to put on the transaction is that the loans were only machinery to enable the purchasers to pay the purchase money they had agreed to pay out of dividends they would have received from the shares. The Court is concerned only with the question: has the commissioner correctly assessed the amount as income from property of the taxpayer? The amount received was not income from property and was not a dividend received by the Australian taxpayers. The Court should quash the assessment. There would not be any prejudice to the commissioner's right, if any, to issue an amended assessment, but the Court should not confer on the commissioner greater powers than he has under s. 170. There is not any decision on the question as to whether under s. 199 the Court has power to vary an assessment made on the wrong basis, that is, the basis that it was income from property whereas it should be income from personal exertion.

[*J. D. Holmes* Q.C. The submission that the issues were fixed by the objections and the commissioner could not go outside the objections, was dealt with in *Danmark Pty. Ltd.* v. *Federal Commissioner of Taxation* (1) and *Australian Machinery and Investment Co. Ltd.* v. *Deputy Federal Commissioner of Taxation* (2). The first-mentioned case was a special type of case.]

It was said in *Jaques* v. *Federal Commissioner of Taxation* (3), that s. 260 of the Act did not apply to a transfer of property as such. The disposal of property, that is the disposal of the right to

(1) (1943) 7 A.T.D. 191; (1944) 7 A.T.D. 333.

(2) (1946) 8 A.T.D. 81; 3 Aust. I.T. Rep. 359.

(3) (1924) 34 C.L.R. 328.

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receive income, the dividends, arising from a source which theretofore belonged to the appellant was a disposition in good faith (*Deputy Federal Commissioner of Taxation* v. *Purcell* (1)). Section 260 cannot be used in a case like this case, unless the court was satisfied that the transaction was in some way colourable or was not a real transaction. The sale by the Australian shareholders of their shares which were producing income, and about to produce income, was anything but an attempt to avoid liability to pay income tax (*Waterhouse* v. *Deputy Federal Commissioner of Land Tax (S.A.)* (2)). Section 260 cannot be used to vary a transaction that involves the disposition of an income producing asset, nor can it, in this case, be used to bring forward points of time at which the dividend is declared by the company (*Jaques* v. *Federal Commissioner of Taxation* (3)). The judge of first instance correctly held on the dicta in that case that s. 260 has no application, but he erred in not placing the correct interpretation on the facts, and in not giving the full effect to the documents which showed that the appellant and the other members of the syndicate effectually, finally and irrevocably disposed of their shares on 2nd February 1948.

J. D. Holmes Q.C. (with him *E. J. Hooke*), for the respondent. The person Corlett did not know anything about the transaction. He appeared as a mere nominee or automaton for the solicitor Mr. White. Substantially, the findings of the judge of first instance were proper findings to come to on the whole of the evidence. For reasons which his Honour gave it was a dividend which the appellant received, and he received it as a dividend. Once the arrangement started the dividend could only be paid as part of the whole arrangement. Section 199 was discussed in *Australian Machinery and Investment Co. Ltd.* v. *Deputy Federal Commissioner of Taxation* (4). Though the sum of £77,000 is described in the Routine as a loan, the payment to Mr. White on 3rd February 1948 was the dividend that was the distribution of the assets of the company. It was not a loan, it was a dividend. The Routine was devised as a cloak to disguise what was actually taking place. In its proper construction all the steps were simply a disguise for the facts, that the company had £77,000 to distribute and that those seven people were entitled to the distribution as and when it was made. The ordinary way to distribute it to them was either by dividend or

(1) (1921) 29 C.L.R. 464.
(2) (1914) 17 C.L.R. 665, at p. 671.
(3) (1924) 34 C.L.R. 328.
(4) (1946) 8 A.T.D., at pp. 98-99, 115-116; 3 Aust. I.T. Rep., at pp. 381-182, 402, 403.

by liquidation; dividend was the way selected. It was the kind of sham described in *Jaques* v. *Federal Commissioner of Taxation* (1). The appellant has failed to establish that those payments and transfers were genuine and bona fide transactions, intended to create real rights and obligations. Applying *Jaques* v. *Federal Commissioner of Taxation* (2) to the facts of this case they would read that as a shareholder the appellant would have been entitled to a dividend of £11,000. Had he so received it he would have been liable to pay income tax, his general tax would have included that sum. That was a purely personal arrangement indicated in law, but also indicated by the fact that it was arranged beforehand, an arrangement to which he was an active party. The appellant authorized Mr. White as the agent to obtain a purchaser for his shares in circumstances in which Mr. White was, by arrangement, to receive a loan from the company with which the purchaser could purport to pay for his share and the company would pay a dividend to the purchaser of an equal amount which would then be used to repay the loan. It was a case of seven shareholders, being the only shareholders in the company and being entitled to the assets by coming to this agreement before they proceeded to New Guinea, and agreeing to do the same thing, which brings them closer in. Though the legal obligation was not there, as between themselves they had agreed that the legal obligation would be created. It was the combined efforts of all the people entitled to the money. *Clarke* v. *Federal Commissioner of Taxation* (3) would make this an *a fortiori* case. Section 260 can be applied to part of the transaction (*Jaques* v. *Federal Commissioner of Taxation* (4)). So much should be taken as was necessary to maintain the assessment. As between the parties the arrangement was of full effect, but it was void as regards the commissioner. A " dividend " is simply a distribution made by a company to its shareholders, and a " distribution " only means a handing out of money. The syndicated people, the shareholders, by the Routine, made it very clear they were not going to rely on injunctions.

M. F. Hardie Q.C., in reply. The appellant and the other Australian shareholders were paid in full for their shares before the declaration of the dividend. The evidence shows that White and his nominees became the beneficial owners of the shares on 2nd or 3rd February 1948. They were equitable owners on 2nd February

(1) (1924) 34 C.L.R., at p. 355.
(2) (1924) 34 C.L.R., at pp. 338, 339.
(3) (1932) 48 C.L.R., at pp. 76, 77, 79.
(4) (1924) 34 C.L.R., at pp. 338-339.

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and became legal owners on 3rd February. The facts in this case cannot be ignored. When the crucial point was to determine whether there was an effective disposition by the appellant of his share either to Corlett or to Corlett on behalf of Mr. White, it is most important to note how the parties acted; what their conduct was and what inferences should be drawn from their conduct after 4th February, in order to determine who was the beneficial owner of the shares. If the arguments for the respondent are right, it would follow that the seven shares remained in equity the property of the Australian shareholders after 4th February. There was not any sale of the shares, nor any effective disposition of the equities in respect of the shares. Looking at the Routine the transfers, cheques, directors' minutes and other relevant documents, the inference is that it was a sale of shares under an arrangment with the purchasers that they were to pay the purchase money out of dividends that they would receive. That is the true construction to be placed upon those documents. Section 260 has not used language to permit the commissioner to twist the transaction around. Section 260 does not help the revenue authorities in this case. This is not a case to which s. 260 can be applied (*Clarke* v. *Federal Commissioner of Taxation* (1)).

Cur. adv. vult.

May 8, 1953.

THE COURT delivered the following written judgment:—

The appeal before us is from an order of *McTiernan* J. dismissing an appeal from an assessment under the *Income Tax Assessment Act* 1936-1947 of the income tax payable by one George James Bell in respect of the income derived by him during the year ended 30th June 1948. The assessment, as appears from the notice of assessment, was made on the footing that in the year mentioned the taxpayer derived, in addition to certain income from personal exertion, an amount of £11,000 as income from property. This amount was described in an adjustment sheet which accompanied the notice of assessment as "amount received in respect of your share in Simmonds, Harper and Larkin Ltd.". Bell objected to this amount being treated as assessable income, and contended in his notice of objection that it had been received by him from the sale of a share in the company named which had been held by him as an investment and was not liable to be brought to tax under any provision of the *Income Tax Assessment Act*. Other grounds of objection were stated, but they have not been pressed.

(1) (1932) 48 C.L.R., at p. 77.

The amount of £11,000 was credited to Bell's bank account with the Bank of New South Wales at Port Moresby, Papua, on 3rd February 1948, having been paid in by means of a cheque for that amount in Bell's favour drawn by one Corlett and dated 2nd February, 1948. The central contention in the commissioner's case is that the amount, notwithstanding the fact that it was received from Corlett, is to be regarded for the purposes of income tax as a dividend within the meaning of that word as defined in s. 6 of the *Income Tax Assessment Act*. As so defined, the word includes any distribution made by a company to its shareholders; and the word " paid " in relation to dividends is defined to include credited or distributed. The contention is that the amount in question either was in fact, or is to be deemed in consequence of the application of s. 260 of the Act to the facts of this case, the proportionate part paid to Bell as a shareholder in Simmonds, Harper and Larkin Ltd. of a distribution made by that company to its shareholders out of profits. If this be so, the argument proceeds, then the amount is rightly included in Bell's assessable income by virtue of s. 44 (1) (*a*) of the Act, for Bell was at all material times a resident of Australia, and the section provides that the assessable income of a shareholder in a company (whether the company is a resident or a non-resident) shall, subject to the section—if he is a resident—include dividends paid to him by the company out of profits derived from any source; and the case is not within any of the exceptions which the section makes to this general provision. In order to consider this argument, it will be necessary to examine the facts in some detail.

About October 1946, a partnership to carry on a business of motor vehicle and machinery dealers was formed by Bell and six other persons, whose names were H. Simmonds, H. G. Linden, N. A. Harper, J. Simmonds, J. F. Larkin and E. E. Chadwick, under the style of Simmonds, Harper and Larkin. The partnership acquired from the Commonwealth Disposals Commission a quantity of surplus war materials situated on Torokina Island, with the object of reselling them at a profit. Bell had negotiations on behalf of the partnership with a Mr. Allen, sub-manager of the Bank of New South Wales at its head office in Sydney, with a view to obtaining assistance to finance the purchase, and Mr. Allen pointed out to him that the partnership would have to pay income tax on any profit it might make by carrying out its venture in the manner proposed. He suggested that Bell should see an accountant, a Mr. Salenger, who could advise him on taxation matters. This he did, and Mr. Salenger's advice, which was given on 4th January 1947,

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was, in effect, that a company should be formed in New Guinea with New Guinea shareholders and a New Guinea board, so as to be a resident of New Guinea, that a company should also be formed in Australia, that the goods bought from the Disposals Commission should be sold by the partnership (presumably at cost) to the New Guinea company, and that they should be resold at a profit to the Australian company. The point of this scheme was that it would ensure that the profit in the goods would be reaped by the New Guinea company, and, being income derived by a resident of the Territory of New Guinea from sources within that Territory, it would be, by virtue of s. 7 (1) of the *Income Tax Assessment Act*, outside the application of that Act. It was realized that the shareholders would have to pay tax on distributions of the profit when made, but, as Mr. Salenger pointed out, the dividends could be spread over a number of years and tax liability would thus be minimized.

Bell conveyed these suggestions to his partners, and on 15th January 1947 a company named Simmonds, Harper and Larkin Ltd. was duly formed in the Territory of Papua, as to which Territory s. 7 (1) makes the same provision as it makes with respect to New Guinea. The signatories to the memorandum of association included one Norman White, a solicitor of Port Moresby, who was acting as solicitor for the partnership, and the six other signatories were local residents whose co-operation was obtained by Mr. White. One of these was a man named Swanton. These seven persons subscribed for one share each. On the following day, 16th January 1947, a company was formed in New South Wales with the name Torokina Disposals Pty. Ltd. On 17th January 1947 the Papuan company by letter accepted an offer which had been made to it by the partnership for the sale by the latter of a particular shipment of the war materials at Torokina Island for £6,000. On 27th January 1947 the Papuan company accepted an offer made to it by Torokina Disposals Pty. Ltd., for the purchase by the latter of the same shipment of war materials for the price of £170,000 payable out of the proceeds of the realization of the materials after arrival in Sydney, on the terms that the vendor should " accept as satisfaction for the purchase money the proceeds of the realization of the various articles less all costs incurred in bringing the same to Sydney and all expenses incurred in connection with the storage and realization thereof ".

The balance of the goods which the partnership had acquired at Torokina was sold to a firm called Curtis and Bannister for £6,000, and this sum was divided amongst the members of the partnership.

(The constitution of the partnership had by then been changed by the introduction of the widow of H. Simmonds in place of her husband who had died at Torokina.) The shipment which Torokina Disposals Pty. Ltd. had bought was brought to Sydney, and the individual members of the partnership other than J. Simmonds and the widow of H. Simmonds then became employees of Torokina Disposals Pty. Ltd., and as such disposed of all the goods in the shipment. This occupied the rest of the year 1947.

On 6th March 1947, at an extraordinary general meeting of the Papuan company, the local residents who had become the directors of that company were replaced by the six partners other than Mrs. H. Simmonds. About the same time, the signatory shareholders in the Papuan company transferred their shares to the partners, each partner acquiring for £1 one fully paid share. Bell purchased his share from Swanton.

Until some date about August 1947, it remained the intention of the partners to follow out the scheme Mr. Salenger had devised for them. But then either Mr. Salenger or the partnership's solicitor Mr. Christie suggested that as each partner had one share in the Papuan company they might sell their respective shares at a profit. A course of action was worked out in great detail and was embodied in a document headed : "Memorandum of Routine—Simmonds Harper and Larkin Limited. Routine for 2nd, 3rd and 4th February, 1948". Bell and four other partners went from Sydney to Port Moresby about 1st February 1948, taking with them this document and a bank draft for £78,520 which they had obtained from Torokina Disposals Pty. Ltd., that sum being the amount of the net proceeds of realization of the goods bought from the Papuan company after all expenses had been provided for. The sole purpose of the journey was to carry out the steps laid down in the Routine. A necessary preliminary step was to find seven persons to act as purchasers of the partners' shares, and this was attended to by the Port Moresby solicitor, Mr. White. He accepted the role of a purchaser of one share himself, and he persuaded six clients of his, including one Corlett, to do likewise. He explained to his clients what the routine involved, telling each that he or she would run no risk and would make a small profit. Six of the seven prospective purchasers had accounts already with the Bank of New South Wales at Port Moresby, and the seventh immediately opened an account with that bank.

The procedure that was carried out, in precise accordance with the Routine, was briefly as follows. On 2nd February, 1948, a directors' meeting of the Papuan company resolved to accept the

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bank draft for £78,520 from Torokina Disposals Pty. Ltd. in full settlement for the articles sold to that company. (The bank draft was accordingly paid in to the company's bank account on the same day.) After authorizing payment of travelling expenses to the five directors and authorizing Mr. White to operate on the company's bank account, the directors tendered their resignations. A general meeting which followed appointed Mr. White and three of his clients as new directors. Mr. White gave each of his six nominees (as the Routine called his clients) his own cheque for £11,000 "as a loan". Then he and his nominees each drew a cheque on his or her own bank account for £11,000, each cheque being made payable to one of the existing shareholders "or bearer", and each of these cheques was exchanged for a share transfer executed by one of the seven partners. All the cheques which thus passed on this day were taken by Mr. White to the bank manager, to whom Mr. White had previously explained what was being done, and the bank manager was requested in writing to hold the cheques until next day, when, it was stated, the necessary funds would be available to meet them.

On the next day, 3rd February 1948, there was a directors' meeting of the Papuan company. Authority was given for the registration of the share transfers, and a resolution was passed that a loan of £77,000 repayable on demand be made to Mr. White. A cheque for the amount of this loan was accordingly paid on this day to the credit of Mr. White's account at the bank. This cheque and the cheques drawn on the previous day were then cleared simultaneously; and thereafter each of the old shareholders, including Bell, obtained from the bank a bank draft on Sydney for his £11,000. The Routine provided that the various cheques should appear in the bank ledgers in the order in which they were to be given, and presumably this was observed.

On the third day, 4th February 1948, a general meeting of the Papuan company resolved that a dividend of £11,000 be paid forthwith on each share in the issued capital of the company. Cheques for these dividends were drawn by Mr. White on the company's bank account and paid into the respective bank accounts of the new shareholders. Each of these shareholders then gave Mr. White a cheque for £11,000 in repayment of the loan received from him on 2nd February 1948, and Mr. White paid into the company's account a cheque drawn on his account for £77,000 in repayment of the loan he had received from the company on 3rd February 1948. All the cheques drawn on this day were cleared simultaneously,

but presumably appeared in the bank ledgers in the order mentioned, as provided by the Routine.

The result of these transactions was as follows. The Papuan company had been paid £78,520 for the goods it had sold to Torokina Disposals Pty. Ltd., and this sum consisted almost entirely of distributable profits since the Papuan company had no external liabilities and its paid-up capital was only £7. It had disposed of £77,000 of these profits, and the old shareholders between them had received £77,000. The old shareholders had parted with their shares. The new shareholders held all the issued shares in a company whose assets consisted of a little over £1,100, being the surplus which remained after providing for directors' travelling expenses and other small outgoings. It may be added, in order to complete the history of the company, that Mr. White on 6th February 1948 was paid his costs and obtained £1,000 from the company's funds as a loan. He later bought in for £20 each the shares which his six clients had purchased. The company had then only about £30 left in its bank account and no one seems to have troubled about it since.

As regards the present appellant, Bell, the net result of all that happened on 2nd, 3rd and 4th February 1948 was that, instead of receiving £11,000 from the company, as he might have done either as a dividend in the ordinary sense of the term or as a distribution in a winding-up, he received £11,000 from the purchaser of his share, Corlett, as the price thereof. Since his original acquisition of the share was not for the purpose of sale at a profit, this meant that the steps taken in accordance with the Routine, if treated as valid, made all the difference between his deriving £11,000 as assessable income and deriving £11,000 as a capital receipt not liable to inclusion in assessable income.

If there had been no more in the case than that Bell, in preference to retaining his share and deriving the dividends which it seemed certain to yield, chose to sell the share for a capital sum equal to the assured dividends, the commissioner would not have been entitled to treat the capital sum as assessable income on the ground of an actual or supposed economic or business equivalence between the two courses. But there was, of course, much more in the case than that. The sale of the share was a part of a complex transaction carefully planned and carried through by Bell and a number of other persons acting in concert, for one predominant purpose, which was to ensure that Bell and his six colleagues should each receive £11,000 tax-free instead of £11,000 subject to tax.

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There was nothing fraudulent or otherwise dishonest in this. Everyone concerned acted in good faith, animated by no other purpose than that of producing an immunity from tax in a manner which they believed was in strict conformity with the law. And indeed sedulous care was taken that it should be in conformity with the law. Certainly, it involved no breach of any penal provision of the *Income Tax Assessment Act*. Moreover there was no pretence or suppression about it. Of no step that was taken can it be said that it was not intended to be real or was intended as a cloak for anything else. That this was so is clear when one considers in what changed legal relationships the persons concerned (including the Papuan company) actually stood to one another when the events of 2nd and 3rd February 1948 were complete. Mr. White stood indebted to the company for £77,000 for money lent, although it is true that the Routine provided him with the means of repaying the amount the next day. He and his nominees had become registered by transfer as holders of the shares, and they held their respective shares beneficially, as was shown later by the fact that Mr. White paid his nominees £20 each for their shares. The former shareholders, including Bell, had effectively divested themselves both legally and equitably of all right, title and interest in their shares, each of them having received a consideration of £11,000 for which he held a bank draft in his own favour. And unquestionably Mr. White's six nominees each owed him £11,000, and none the less so because the Routine provided the means of repayment.

Since all parties acted openly, and there is no ground for denying that every step in their procedure was effectual as between themselves to do what it purported to do, the commissioner's assessment against Bell cannot be supported unless by reference to s. 260 of the *Income Tax Assessment Act*. That section, so far as its provisions need be considered in this case, provides that "Every contract, agreement, or arrangement made or entered into, orally or in writing, . . . shall so far as it has or purports to have the purpose or effect of in any way, directly or indirectly . . . (*c*) defeating, evading, or avoiding any duty or liability imposed on any person by this Act . . . be absolutely void, as against the Commissioner, or in regard to any proceeding under this Act, but without prejudice to such validity as it may have in any other respect or for any other purpose". The section is, of course, an annihilating provision only. It has no further or other operation than to eliminate from consideration for tax purposes such contracts, agreements and arrangements as fall within the descriptions it contains. It assists the commissioner, in a case like the present, only if, when all contracts,

agreements and arrangements having such a purpose or effect as the section mentions are obliterated, the facts which remain justify the commissioner's assessment. One other general observation should be made. In *Jaques* v. *Federal Commissioner of Taxation* (1), *Isaacs* J. said of the word "arrangement" that in this collocation it is the third in a descending series, and means an arrangement which is in the nature of a bargain but may not legally or formally amount to a contract or agreement. It must be remembered, however, that the section is concerned only with contracts, agreements and arrangements which have an effect in law and accordingly are capable of statutory avoidance. With this in mind, it may be said that the word "arrangement" is the third in a series which as regards comprehensiveness is an ascending series, and that the word extends beyond contracts and agreements so as to embrace all kinds of concerted action by which persons may arrange their affairs for a particular purpose or so as to produce a particular effect. The case of *Jaques* v. *Federal Commissioner of Taxation* (2) itself, and the later case of *Clarke* v. *Federal Commissioner of Taxation* (3), illustrate the application of the word. It is true that, as *Isaacs* J. observed in the former of these cases (1), the word does not include a conveyance or transfer of property as such; but, as the cases cited show, under the section a conveyance or transfer of property may be void as against the commissioner as being part of a wider course of action which constitutes an arrangement in the relevant sense of the word.

Such an arrangement was made, clearly enough, when Bell and his co-shareholders and White and his six clients co-operated, in accordance with the preconcerted plan embodied in the Routine document, in so ordering their affairs that although £77,000 of distributable profit was extracted from the Papuan company and Bell and his associates had their cash resources increased by amounts totalling that very sum, yet the company made no distribution to those persons and what they received they received as the sale price of their capital assets, the shares they held in the company. This arrangement, both in purpose and in effect, represented nothing but a method of impressing upon the moneys which came to the hands of Bell and his colleagues the character of a capital receipt and of depriving it of the character of a distribution by a company out of profits. It was therefore a means for avoiding the income tax which would have become payable had the £77,000 been distributed by the company in the normal way. Section 260 (*c*)

(1) (1924) 34 C.L.R., at p. 359.
(2) (1924) 34 C.L.R. 328.
(3) (1932) 48 C.L.R. 56.

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postulates a duty or a liability imposed on a person by the Act, but this refers, not to a liability to pay a particular amount of tax (which would be a liability imposed by a taxing Act), but to a liability such as s. 17 of the Act imposed on Bell, to pay tax in respect of his taxable income ascertained by including in his assessable income his proportion of the Papuan company's profits if and when he should participate in a distribution of them. It must therefore be held that the transactions of 2nd, 3rd and 4th February 1948 constituted an arrangement made by Bell and the others who took part, having the purpose, and (apart from the operation of s. 260) the effect, of defeating and avoiding a liability imposed on Bell by the Act.

Then if this arrangement be treated as void, what remains? Simply this, that on 3rd February 1948, £77,000, consisting entirely of profits, was withdrawn from the company's bank account, and £11,000 of it passed, indirectly but by steps which are clearly traceable on the face of the bank's ledgers, into Bell's bank account; and Bell is to be considered as remaining at that time a shareholder in the company, his transfer to Corlett being *ex hypothesi* void as against the commissioner as an integral part of the arrangement. This means that the application of s. 260 in this case is to eliminate those features of the case upon which the exclusion of the £11,000 from assessable income depends, and by that means to establish the correctness of the assessment appealed against.

For these reasons the appeal should be dismissed with costs.

Appeal dismissed with costs.

Solicitors for the appellant, *T. W. Garrett, Christie & Buckley.*

Solicitor for the respondent, *D. D. Bell*, Crown Solicitor for the Commonwealth.

J. B.