

REASONS FOR JUDGMENT

COURT : High Court of Australia.
Sydney Registry.

PARTIES : SCHARKIE AND ANOR.

versus

THE COMMISSIONER OF TAXATION
OF THE COMMONWEALTH OF AUSTRALIA

NATURE OF PROCEEDINGS : Thirteen appeals as to whether
property bought in 1954 and sold
off in parts over a number of
years, was acquired for resale at
a profit.

CORAM : MENZIES J.

JUDGMENT : Thirteen Appeals dismissed with
costs.

DATE OF JUDGMENT : 17th October 1968 at Melbourne.

SCHARKIE AND ANOR

v.

THE COMMISSIONER OF TAXATION
OF THE COMMONWEALTH OF AUSTRALIA

JUDGMENT

MENZIES J.

SCHARKIE AND ANOR.

v.

THE COMMISSIONER OF TAXATION
OF THE COMMONWEALTH OF AUSTRALIA

ORDER

Appeal No. 22 of 1967 dismissed with costs.
Appeal No. 23 of 1967 dismissed with costs.
Appeal No. 24 of 1967 dismissed with costs.
Appeal No. 25 of 1967 dismissed with costs.
Appeal No. 26 of 1967 dismissed with costs.
Appeal No. 27 of 1967 dismissed with costs.
Appeal No. 28 of 1967 dismissed with costs.
Appeal No. 29 of 1967 dismissed with costs.
Appeal No. 30 of 1967 dismissed with costs.
Appeal No. 31 of 1967 dismissed with costs.
Appeal No. 32 of 1967 dismissed with costs.
Appeal No. 33 of 1967 dismissed with costs.
Appeal No. 34 of 1967 dismissed with costs.

JUDGMENT

MENZIES J.

SCHARKIE AND ANOR.

v.

THE COMMISSIONER OF TAXATION
OF THE COMMONWEALTH OF AUSTRALIA

On 20th October 1954 the taxpayers, C.R. Scharkie and his wife Edith Scharkie, acquired a property known as Maryvale by purchase for £40,000. Beginning in 1957 parts of Maryvale have been sold and assessments to income tax have been made on the footing that the profits from these sales constitute assessable income of the taxpayers. Although other objections to the assessments were made, the only one persisted in at the hearing was that Maryvale was not acquired for sale at a profit. The only question, is therefore, whether I am satisfied that profit making by the sale was not the dominant purpose of the taxpayers in buying Maryvale.

My conclusion ultimately depends upon whether I accept the evidence of the taxpayer, C.R. Scharkie, who said, in effect, that at the time of the purchase he never gave a thought to the re-sale of the property. The taxpayer, Edith Scharkie, was by reason of mental infirmity, not able to give evidence, but it is common ground that her case stands or falls with that of her husband. For convenience I shall call Mr. C.R. Scharkie, "the taxpayer".

Maryvale, in 1954, was a property of 980 acres fronting Windsor Road at Rouse Hill about 25 miles from Sydney. It had been a property of some consequence with a history of 130 years. The large house, built of brick on stone and solidly constructed out of good materials, dated back to convict days. It had, and has, a fine outlook. In 1954 the whole property was run down. The house, although liveable, needed a lot spent upon it to make it into the comfortable and attractive home that it has since become. There were a number of out-buildings, including a wool shed, but all needed some attention. The yards and fencing were

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not in good repair. The property was not then being used for any agricultural or pastoral purpose but its last use had been for spelling race-horses and there were a number of small paddocks. Having regard to what was happening in the district, Maryvale was in 1954 a property which an estate agent might recognise as having sub-divisional prospects in the not very distant future.

No issue has arisen about the sales by the taxpayers of parts of Maryvale and what has happened may be stated shortly.

Early in 1957 instructions were given by the taxpayer for the sub-division of an area of about 130 acres facing Windsor Road, and a plan for the sub-division of this area into 24 five acre lots was approved in April 1958. The first transfer was in December 1958. This first sub-division was followed in July 1958 by a second sub-division of 47 five acre lots, although it was not until later that this sub-division was carried through. An area of 292 acres was sold to the Austral Brick Company Pty. Ltd. on 10th March 1960, pursuant to an option given on 9th November 1959. In May 1962 an area of 173 acres was sold to Australian Memorial Park Pty. Ltd. These two sales were fortuitous. Later, and outside the period with which I am actually concerned, a further area was sub-divided into three substantive lots leaving the homestead and 31 acres which, with unsold lots, remained in the ownership of the taxpayers. The house has, for some years, been occupied by one of their sons and has, by an expenditure of £7,000 or £8,000, been restored to something of its former distinction.

The taxpayer was, at all times material, an estate agent at Manly who took an active part in municipal affairs. He had had some experience of the sub-division of land. His marriage in 1952 to Edith Scharkie was his second marriage. Mrs. Scharkie was, at all times material, a woman of considerable wealth owning in 1954 real estate and shares worth, in all, £150,000 or thereabouts. Mrs. Edith Scharkie had a sister,

Miss Olive Proud, who was equally wealthy. By reason of mental instability Miss Proud could not look after herself. Mrs. Scharkie was her attorney under power and looked after her with sisterly care, earlier when the taxpayers and Miss Proud occupied adjoining houses in Manly, and later at Mungerie Park - a property to which I will have to refer later - when a room was added to the house there for occupation by Miss Proud. I have no doubt that the taxpayers felt under a compelling family obligation to care for Miss Proud. In October 1954, when Maryvale was purchased, Miss Proud was in a mental home.

In April 1954 three of the sons of the taxpayer by his former marriage, bought the property Mungerie Park, an area of about 431 acres, for £35,000, walk in, walk out. Mungerie Park fronted Windsor Road opposite Maryvale. The purchase price was provided by Mrs. Edith Scharkie supplying the deposit of £4,000 in cash and guaranteeing a bank overdraft of £31,000. Later on there was an addition to the area of Mungerie Park. Two of the purchasers of Mungerie Park had been trained at an agricultural college and Mungerie Park has been developed and is being run successfully as a dairy farm selling whole milk. It was when the taxpayers were staying at Mungerie Park that Maryvale was first brought to their attention. This, it seems, was in the second half of 1954 when one Moriarty, the brother of Mrs. Pearce, the then owner of Maryvale, offered the property to the taxpayer at a price of £45,000. It had been on the market for some time. The taxpayers eventually bought it for £40,000 in October 1954.

Here it is, I think, convenient to set out the effect of the taxpayer's evidence about the purpose with which Maryvale was bought. It seems that, although he had been looking up and down the State for a property to buy, he was, as he said, against buying Maryvale. "I did not want it" was his evidence. His wife, however, thought otherwise and after an inspection she said "We

will buy this and fix Olive up. We will bring her up here".

The taxpayer added for himself "That was her one thought in life". The taxpayer's evidence continued as follows :

"Did you discuss this proposition with any of your sons? ... With the boys who were there.

Which ones were there? ... Bob was there all the time.

Do you recollect having any conversation with Bob about it? ... I do not remember, but there was general conversation.

What is the next thing you did about it? ... Mr. Moriarty came down to see if we had made up our minds and Mrs. Scharkie said she would buy it.

Did you have any other inspection of it before the contract was signed? ... Not the house.

The property? ... You could not help but see it.

Did you go over it? ... Yes, with W.A. Tebbutt and with Mr. Nancarrow the manager of the Commonwealth Bank, Manly.

Did any of your sons go over it with you on that occasion? ... I had one of them drive me over.

Do you recollect which one? ... No.

There were your solicitor, your bank manager and yourself? ... Yes, we went over.

.....

Following that inspection, did you have a discussion with your bank manager, Mr. Tebbutt and Mrs. Scharkie? ... The bank manager was there and going home he said, "If you buy this it will be worth £100,000 in ten years".

What other conversation was there? ... That is all I had with him about that. I was against the whole project but Mr. Tebbutt was with Mrs. Scharkie all the way.

Did Mrs. Scharkie tell you why she wanted the place? ... She liked the old home. She has always fancied these historical places and is a connoisseur of that sort of thing. She said, "We will put Olive up there and we will build a nice home for her".

Asked about his intention he said:

"On the 20th October 1954 a contract for sale was entered into? ... Yes.

At that point of time did you have any intention at all of re-selling the property or any part of it? ... Never gave it a thought. We had looked around the country for a place and we found one.

Had your wife any such intention? ... None whatever".

It is to be observed that the taxpayer did not put forward, as part of the purpose with which Maryvale was bought, any idea that it should be used for dairying purposes in conjunction with Mungerie Park. The professed purpose with which the purchase was made, namely to provide a home for the taxpayers where provision would be made for the accomodation of Miss Proud, was one which was not, in fact, realised. It was said that Miss Proud, who had not been consulted about living at Maryvale, did not wish to do so, and that Mrs. Sharkie, when staying at Mungerie Park in the summer time, found that she disliked the heat of the district. A house at Leura was, in fact, purchased by the taxpayers in January 1956. An element in the decision against using Maryvale for the purpose of a home was, so it is said, an incident at some unspecified time when household goods belonging to the taxpayers, which had been stored in Maryvale, were stolen. Mr. Scharkie said this influenced Mrs. Scharkie against having anything more to do with the property. Such goods as were not stolen were, it seems, taken to the house at Leura. I think that it is a fair inference that any intention which the taxpayers may have had of living at Maryvale did not outlast 1955, but it is of critical importance to determine whether such a purpose was ever entertained. To this I will return.

I turn now to the use which was, in fact, made of Maryvale before the sales, which I have already mentioned, took place.

There is evidence, which I accept, that calves from Mungerie Park were run on Maryvale. I am also satisfied that one crop of oats was grown upon the 120 acres which was the first area sub-divided. This was probably in 1956. I am not satisfied that any other crops were grown. The oat crop which was grown was seemingly taken by the sons at Mungerie Park - who planted it - for there is no record of any receipt of the proceeds by the

taxpayers or either of them, although it does seem to have been said that those proceeds would be paid into the taxpayers' bank account. I accept the evidence of the witness Paterson that the oat crop which was grown was thin, and I am not satisfied that the crop of which a photograph appears in exhibit "EE" was a crop growing upon Maryvale. The most substantial use of Maryvale was to run sheep there. Early in 1955 the taxpayer entered into a share farming agreement with one Paterson whereby the latter agreed for a period of 2 years to carry on the business of sheep farming on Maryvale with sheep to the value of £1,500 to be paid for by the taxpayer and Paterson equally. Net profits were divisible on the basis of 60% to the owner and 40% to the shareman. The venture, which began on the 1st April 1955, was a complete failure. Only 700 sheep were bought and these did poorly. They did not have enough to eat and they were harrassed by dogs and crows. Paterson put the matter succinctly in reply to the question "Why did you leave the property?" when he said "Broke, I suppose. No sign of improvement, the sheep were not yielding enough income for me to live on, and even then I was working part time for wages for Scharkies over the last few months to survive". The last sheep were sold and Paterson left Maryvale early in 1957. The share farming episode does not suggest to my mind any intention on the part of the taxpayer to carry on any serious grazing or agricultural operations on Maryvale. Little was spent and little was received; not even the proceeds from the oats. After Paterson left the property part of it was used from time to time for the agistment of horses and cattle, but by this time it is common ground that the move to sub-divide was in progress. Once sub-division began it went ahead.

I now turn to such direct evidence as there is of any purpose on the part of the taxpayers, or either of them, to resell Maryvale at a profit. As I have said, the taxpayer denies that there was any such purpose and I have evidence that **neither**

Paterson nor R.F. Scharkie - one of the sons - heard any mention of such a purpose. Something did appear, however, in the evidence of the witness Nancarrow who was Manager of a Commonwealth Trading Bank at Manly in the period from 1954 to 1958. What appears requires examination, not to evaluate the oral evidence of the witness - which would afford no satisfactory basis for any conclusion - but to find out what contemporary records disclose. It seems that in 1954 what can conveniently be called the Scharkie Group - for so the family was referred to by all concerned; see for instance the letter C.R. Scharkie and Sons to the Manager, Commonwealth Bank, 2nd February 1966 - approached Mr. Nancarrow for overdraft accommodation in connection with the purchase of Mungerie Park. Arrangements were made for at least four overdraft accounts affording credit up to about £50,000. The accounts not in the name of Mrs. Edith Scharkie were guaranteed by her, for she was the only member of the Scharkie family with assets. There was on 22nd September 1954 an interview between the taxpayer and Mr. Nancarrow about what was called the C.R. Scharkie Group. The record of this interview includes the following:

"They have been offered Maryvale, a grazing property immediately opposite Mungerie, at a purchase price of £40,000 and they intend to proceed with this purchase. Mrs. Scharkie expects to realise £35,000 from the sale of her Edments Rights"

On 14th October 1954 there was another interview between the bank manager and Mrs. Scharkie, who called with her son Mr. R.F. Scharkie, "in connection", so it was recorded, "with a proposal to purchase an adjoining property of 960 acres, the price being £40,000. She desired to draw a deposit cheque for £4,000." The following information was given to the bank manager "Stock on hand at present consists of 148 cows of which 104 are in full milk with 44 dry and 18 young heifers. It is expected to add another 100 milking cows to the herd within 12 months and crop 400 acres annually on the total area." Other overdrawn

accounts were discussed and it was pointed out that the total current debt to the bank was £66,775. The bank manager was told of the prospective sale of two properties, the Edments Rights - now with an anticipated return of £10,000 - and the prospects of a further £10,000 from an undisclosed source. The record concluded as follows:

"We undertook to submit her proposal for an increase in overdraft accommodation up to £45,000 for the time being to enable development of Mungerie and to provide the deposit on 960 acres. We are to advise her after a reply has been received."

Records to which I have just referred are the only relevant records prior to the purchase of Maryvale and I read the record to 14th October 1954 as indicating that the bank manager was told, in effect, that Mungerie Park and Maryvale would be worked together. Nothing more of significance appears. On 14th December 1954 the taxpayer called to discuss with Mr. Nancarrow the settlement for Maryvale on 1st January 1955. It appeared that the prospective dispositions of property referred to on 14th October had fallen through and the bank manager indicated "it was not apparent at present that we could finance the settlement for Maryvale". On 16th December 1954 Ian Scharkie, a son of the taxpayers, saw the bank manager and was told "It would seem, therefore, that the only chance of finalising the purchase of Maryvale through us is to ensure that funds totalling £30,000 were deposited prior to settlement. In any case it would be extremely difficult and most unlikely that we would be in a position to complete all detailed work by 1st January 1955 and that we could not proceed until such work was finalised. We indicated that in our opinion it was imperative to defer settlement, if this was at all possible". On 29th December 1954 there was a further interview when the taxpayer was told "We are not in any way committed to make further accommodation available to pay £20,000 mortgage to the Vendors of Maryvale. Any approach in this direction will be dealt with only on its merits". On 28th January 1955 there was an interview between Mr. Nancarrow and

the taxpayer, of which the following is part of the record :

"A conference with the Vendors of Maryvale has been held and they are prepared to leave £30,000 on mortgage for the time being on the basis of £30 p.w. reductions with a fixed mortgage of £20,000 at 5% for 2 years when the Scharkies are able to provide for the difference of £10,000. Mr. Scharkie states that the deposit of £4,000 is in hand and has requested permission for Edith Scharkie to draw a cheque for £6,000 on her overdraft account. Immediately after possession of Maryvale has been obtained he will proceed to sub-divide 400 acres from which he expects to obtain £40,000 by way of sale of ten acre blocks."

This is the first record of any proposal to sub-divide part of Maryvale. In fact it was not proceeded with. The record is, however, inconsistent with the taxpayer's evidence that it was not until 1957 that he gave any thought to sub-dividing and selling any part of Maryvale. When this record was put to the taxpayer he said that he did not remember whether he made the statement; that he couldn't think of saying it and that he had no knowledge of talking like that to Nancarrow at all.

The only other evidence of any moment was that of the witness Conlon - an investigating officer in the Department of the Commissioner of Taxation - who said that the taxpayer, in the course of interviews, when he was being questioned about the intentions with which Maryvale was purchased, said that he realised that in ten or twenty years time the area would develop into another city and that it would eventually be necessary to sub-divide the property. The taxpayer also said that he thought the purchase of Maryvale could be a good financial proposition at the price for the use to which it was to be put. Furthermore, Conlon gave evidence that when the taxpayer was asked about the entry in the bank record to the effect he said he would sub-divide 400 acres of Maryvale into five acre lots when he got possession, he replied that he could not recall mentioning that to the bank manager but "possibly it could have been an estate agent's exaggeration to impress the bank".

Upon the case as a whole I reject the appellants' contention that the dominant purpose for the purchase of Maryvale

was to provide a home for the appellants where they could care for Miss Proud. Not only do I regard this as inherently unlikely but I have no confidence in the evidence that it was so. I do not think that the taxpayer was a party to the purchase of Maryvale against his own inclination. Moreover, nothing was done to effectuate any intention of this sort. Mr. Hope naturally enough put in the forefront of his argument for the appellants the view that Maryvale was really purchased as an adjunct to Mungerie Park, but that was not the evidence of the taxpayer, nor did what occurred afford much support for such an explanation of the purchase, notwithstanding that a few calves from Mungerie Park were run on Maryvale, that a crop of oats was grown there and that a dairy licence was obtained for the combined area.

Having rejected the appellants' case the assessments must, of course, stand, but I should say that I have reached the positive conclusion that it is probable that, from the first, the taxpayer looked at Maryvale with the eye of a subdivider and that it was in keeping with the holding of a purpose to sub-divide and sell that he made the statement which he did to the bank manager in January 1955. I prefer this explanation of the statement which was made to the alternative explanation put forward by Mr. Hope that the taxpayer had, under the force of circumstances resulting from the non-realisation of other properties, formed in January a purpose which had been foreign to his mind in the previous October.

For the foregoing reasons each appeal will be dismissed with costs.

MENZIES J.