Administrative Appeals Tribunal

DECISION AND REASONS FOR DECISION

[2016] AATA 420

Division	Taxation & Commercial Division
File Number(s)	**2014/6145; 2014/6146; 2014/6147; 2014/6148**
Re	**Bruce Rowntree**
	APPLICANT
And	**Commissioner of Taxation**
	RESPONDENT

DECISION

Tribunal	**Professor R Deutsch, Deputy President**
Date	**24 June 2016**
Place	**Sydney**

The decision under review is varied by:

- excluding the amount of $1,000,000 and $80,000 from the assessable income of the Applicant in respect of the year to 30 June 2013; and
- reducing the base penalty from 75 % to 50%.

In all other respects the decision under review is affirmed.

.....[sgd].....

Professor R Deutsch, Deputy President

CATCHWORDS

TAXATION – loan agreements – whether funds received under loan agreements income – existence of loan agreement – objective assessment of advances made under loan agreement – taxpayer entered into enforceable voluntary undertaking – operation of Income Tax Assessment Act 1936 Division 7A and loan agreements – administrative penalty applied – decision affirmed

LEGISLATION

Income Tax Assessment Act 1936 (Cth), s 109N
Taxation Administration Act 1953 (Cth), ss 14ZZK, 284–75, 284-80, 284-85, 284-90, 284–220, 298–20

CASES

Bellinz Pty Ltd v Federal Commissioner of Taxation (1998) 39 ATR 198
BHP Billiton Direct Reduced Iron Pty Ltd v DCT (2007) 67 ATR 578
BKR (Bris) Pty Ltd v Federal Commissioner of Taxation (2001) 46 ATR 347
Danmark Pty Ltd v Federal Commissioner of Taxation (1944) 7 ATD 333
Dixon as Trustee for Dixon Holdsworth Superannuation Fund v Commissioner of Taxation (2008) 167 FCR 287
Re Johnston and Federal Commissioner of Taxation (2011) 81 ATR 908
Nguyen and Commissioner of Taxation [2011] AATA 544
Pearson v DCT (2009) 74 ATR 437
Re Applicant and Commissioner of Taxation (2012) 88 ATR 222
Ryvitch v Federal Commissioner of Taxation (2001) 47 ATR 381
Toll (FGCT) Pty Limited v Alphapharm Pty Limited (2004) 219 CLR 165
Commissioner of Taxation v Rawson Finances Pty Ltd [2012] FCA 735

SECONDARY MATERIALS

Taxpayer Alert 2011/1
ATO Practice Statement Law Administration 2005/2
ATO Practice Statement Law Administration 2014/4

REASONS FOR DECISION

Professor R Deutsch, Deputy President

24 June 2016

DRAMATIS PERSONNAE

1. This case involved a complex array of participants with Mr Bruce Rowntree, the Applicant, being a key participant as well as being connected one way or another with each of the other participants.

2. The participants and the relevant facts associated with each participant are set out below.

   (a) The **Applicant** is and has at all relevant times been:

      (i) a qualified practising solicitor in New South Wales;

      (ii) the trustee, appointer and primary beneficiary of the Rowntree Family Trust (the RFT);

      (iii) a director and secretary of BR Redd Holdings Limited ("Redd Holdings");

      (iv) the sole director of Eugenius Pty Limited, Eugenius Holdings Pty Limited and Galerius Pty Limited;

      (v) the sole shareholder of Eugenius Holdings Pty Limited.

   (b) **Lisa Rowntree** is and was at all relevant times the wife of the Applicant.

   (c) **Reginald Rowntree** is the father of the Applicant.

   (d) **BR Redd Holdings Ltd (Redd Holdings)**:

      (i) was a company limited by guarantee;

      (ii) was incorporated in Australia on 22 April 2009;

      (iii) was deregistered on 22 February 2011;

      (iv) had the Applicant as its main shareholder at all relevant times;

      (v) had 3 directors namely the Applicant, Lisa Rowntree and Reginald Rowntree;

      (vi) from 11 May 2009 until 1 July 2010 owned all the shares in a company now called Voluntary Credits Pty Limited.

(e) **Voluntary Credits Limited (Voluntary Credits)**:

(i) was previously named BR Redd Limited but changed its name to Voluntary Credits Limited on or around 18 January 2010;

(ii) was a company incorporated in Malaysia on 11 May 2009;

(iii) carried on a business of developing REDD trading schemes and forward selling REDD credits which broadly were carbon emissions trading schemes;

(iv) had Redd Holdings as its sole shareholder from 11 May 2009 to 1 July 2010 and Eugenius Pty Limited (Eugenius) from 1 July 2011 to 4 July 2011;

(v) had the Applicant as its director at all relevant times;

(vi) paid dividends totalling around $640,000 to its shareholder Redd Holdings and $1.6m to Eugenius.

(f) **Eugenius Pty Limited (Eugenius)**:

(i) was incorporated on 8 June 2010 and deregistered on 28 April 2013;

(ii) had the Applicant as trustee of the Rowntree Trust as its shareholder from incorporation until 22 July 2011 and Eugenius Holdings Pty Limited thereafter;

(iii) received a dividend of $1.6m from Voluntary Credits and paid a dividend of the same magnitude to Eugenius Holdings.

(g) **Eugenius Holdings Pty Limited (Eugenius Holdings)**:

(i) was incorporated on 21 July 2011;

(ii) had the Applicant as its sole director and the Applicant as trustee of the Rowntree Trust as its sole shareholder;

(iii) is argued by the Applicant to be the assignee of a loan of $640,000 originally made by Redd Holdings to the Applicant which was then assigned

to a further related company, Emporium Limited and which was then assigned to Eugenius Holdings;

(iv) is argued by the Applicant to have made a loan of $1.6m to the Applicant.

(h) **Galerius Pty Limited (Galerius)**:

(i) was incorporated as a company limited by shares on 23 August 2010;

(ii) had as its sole shareholder the Applicant acting as trustee of the Rowntree Trust;

(iii) had the Applicant as its sole director at all relevant times;

(iv) appears to have conducted no business of its own; and

(v) was in receipt of certain funds from entities within the group and paid out amounts to either the Applicant or entities owned or controlled by him.

(i) **Galerius Holdings Limited (Galerius Holdings)**:

(i) was incorporated as a company limited by shares on or around 18 July 2012;

(ii) had as its sole shareholder the Applicant acting as trustee of the Rowntree Trust;

(iii) appears to have conducted no business of its own;

(iv) had the Applicant as its sole director at all relevant times; and

(v) on or around 19 July 2012 took a transfer of the shares in Galerius in exchange for the issue to the Applicant of 1.7 million shares in itself.

3. The parties, their relationships and the transactions described further below are depicted with as much accuracy as possible in the diagram found in the Appendix.

THE TRANSACTIONS

4. There were three distinct purported loan arrangements entered into by the Applicant which I will refer to sequentially as the First Arrangement, the Second Arrangement and the Third Arrangement.

The First Arrangement

5. On or around 12 August 2009, Voluntary Credits paid a dividend of $500,000 to Redd Holdings.

6. On or around the same day the Applicant caused Redd Holdings to transfer the same amount being $500,000 to the Applicant purportedly under a Loan Facility Agreement between the Applicant and Redd Holdings.

7. On or around 5 January 2010, Voluntary Credits paid a further dividend of $140,000 to Redd Holdings.

8. On or around the same day, the Applicant caused Redd Holdings to transfer the same amount being $140,000 to the Applicant purportedly under a Loan Facility Agreement between the Applicant and Redd Holdings.

9. The Applicant asserts that the result was that at 5 January 2010, the Applicant owed Redd Holdings $640,000.

10. On or around 14 February 2011 the debt due by the Applicant to Redd Holdings was assigned to a company named Europium Limited (Europium). This was done by way of an Agreement to Assign dated 14 February 2011 (Exhibit A1). The debt due was further assigned by Europium to Eugenius Holdings on 16 June 2014.

11. Thus, after 16 June 2014, the Applicant asserts that he owed Eugenius Holdings the amount of $640,000.

The Second Arrangement

12. Voluntary Credits paid dividends to Eugenius in the following amounts on the following approximate dates:

Date	*Amount*
10 August 2010	*$500,000*
16 November 2010	*$150,000*
25 April 2011	*$150,000*
4 July 2011	*$800,000*

13. In each case on the same day as the dividend was paid the Applicant caused Eugenius to transfer the full amount of the dividend to the Applicant purportedly as a loan under a loan facility agreement between the Applicant and Eugenius.

14. On or around 22 July 2011 the share held by the Applicant in Eugenius in his capacity as trustee of the Rowntree Trust was transferred to Eugenius Holdings in consideration for the allotment by Eugenius Holdings of 1.6 million shares in itself to the Applicant as trustee for the Rowntree Trust.

15. On the same day Eugenius declared a dividend of $1.6 million to Eugenius Holdings the then new owner.

16. On the same day, Eugenius Holdings lent the Applicant $1.6 million which was used to reduce the amounts owing to Eugenius and offsetting the amounts owed to Eugenius Holdings.

17. As a result it is argued that the Applicant owes Eugenius Holdings $1.6 million as at 22 July 2011.

18. On 22 July 2011 a Loan Facility Agreement was entered into between Eugenius Pty Ltd as Lender and the Applicant as Borrower which applies to “any advance or loan made to the Borrower by the Lender after the date of this Agreement”: T23-181.

The Third Arrangement

19. Voluntary Credits paid dividends to Galerius in the following amounts on the following approximate dates:

Date	*Amount*
19 October 2011	*$200,000*
15 February 2012	*$100,000*
21 May 2012	*$500,000*
17 July 2012	*$1,000,000*
18 December 2012	*$80,000*

20. In each case on the same day as the dividend was paid the Applicant caused Galerius to transfer the full amount of the dividend to the Applicant purportedly as a loan under a loan facility agreement between the Applicant and Galerius.

21. On or around 19 July 2012, the share held by the Applicant in Galerius in his capacity as trustee of the Rowntree Trust was transferred to Galerius Holdings in consideration for the allotment by Galerius Holdings of 1.7 million shares in itself to the Applicant as trustee for the Rowntree Trust.

22. On the same day Galerius declared a dividend of $1.7 million to Galerius Holdings, the then new owner of Galerius.

23. On the same day, Galerius Holdings lent the Applicant $1.7 million which was used to reduce the amounts owing to Galerius and offsetting the amounts owed to Galerius Holdings.

24. As a result it is argued by the Applicant that the Applicant owes Galerius Holdings $1.7 million as at 19 July 2012.

25. On 19 July 2012 a Loan Facility Agreement was entered into between Galerius Pty Ltd as Lender and the Applicant as Borrower which applies to “any advance or loan made to the Borrower by the Lender after the date of this Agreement”: T33-212.

The totality of the three arrangements

26. As a result of these three arrangements, it is asserted by the Applicant that:

    (a) as at 16 June 2014, the Applicant owed to Eugenius Holdings $2,240,000 being two separate loans of $640,000 (Loan Arrangement 1) and $1,600,000 (Loan Arrangement 2); and

    (b) as at 19 July 2012, the Applicant owed to Galerius Holdings $1,700,000 (Loan Arrangement 3).

Repayments of Outstanding Loan Amounts

27. The Applicant commenced what he describes as loan repayments in relation to loans due to Eugenius Holdings and Galerius Holdings on or around 30 June 2014. The repayments involved amounts of $5,000 per month and other amounts as and when available.

Enforceable Voluntary Undertaking

28. On 15 February 2011, the Respondent identified a problem with companies limited by guarantee and the application of Division 7A of the *Income Tax Assessment Act 1936* (Cth) ("the 1936 Act") and accordingly released Taxpayer Alert 2011/1 (TA 2011/1) entitled "Loans to members of companies limited by guarantee and the operation of Division 7A."

29. On 8 August 2011, the Applicant gave an Enforceable Voluntary Undertaking to the Respondent concerning companies limited by guarantee. The undertaking referred to TA 2011/1 and at paragraph 5 provided:

> *"The entities (**including the applicant)** have undertaken transactions comprising the setting up of companies limited by guarantee on behalf of clients and **on their own behalf,** and given advice to clients on the commercial and taxation consequences of setting up companies limited by guarantee." (Emphasis added)*

30. Under clause 13.1 of the Enforceable Voluntary Undertaking, the Applicant covenanted not to "promote, market, or otherwise encourage another entity to participate in, enter into or carry out" a company limited by guarantee arrangement.

31. Under clause 13.3 the Applicant covenanted not to make any attempt, directly or indirectly, to obtain "any payment, consideration or further agreement or transaction" in connection with companies limited by guarantee arrangements.

32. The Respondent makes reference to the Enforceable Voluntary Undertaking in his Written Outline of Submissions (paragraph 48) but did not include it in the T-documents, opposed its tender at the hearing and declined to allow his auditor to be cross-examined on the effect or the import of the Enforceable Voluntary Undertaking. The Enforceable Voluntary Undertaking was however admitted into evidence at the hearing and is presented as Exhibit A4.

ISSUES

33. There are three potential issues in this case:

    (a) first, are the amounts purportedly received as loan funds properly characterised as loan funds as the Applicant asserts or are they income of the Applicant as the Respondent asserts;

    (b) secondly, if the first issue is resolved adversely to the Applicant, was the Respondent correct to assess the Applicant for an administrative penalty of 75% of the shortfall amount under s 284-85 of Schedule 1 of the *Taxation Administration Act* 1953 (Cth) ("the Administration Act") for the 2010 income year. Further, if the first issue is resolved adversely to the Applicant, was a 20% uplift so as to increase the penalty to 90% for the 2011, 2012 and 2013 income years appropriate;

    (c) thirdly, if the first issue is resolved adversely to the Applicant, should the penalty be remitted in whole or in part.

THE ONUS PLACED ON THE TAXPAYER

34. Under s 14ZZK of the Administration Act, it is the taxpayer who bears the onus of proving that each of the amended assessments in this case are excessive.

35. Thus, in *Danmark Pty Ltd v Federal Commissioner of Taxation* (1944) 7 ATD 333 at 337 Latham CJ said:

> *"…upon an appeal the onus rests upon the taxpayer of establishing the facts upon which he relies and if it is necessary for him to establish a particular fact in order to displace the assessment he must satisfy the Court with respect to that fact."*

36. In this case, there are a number of factors upon which the taxpayer relies in asserting that the amended assessments are excessive.

37. Most particularly he asserts that at the time that each of the payments were made to him (or at least to an account which he controlled) by each of Redd Holdings, Eugenius and Galerius, there was in existence a loan agreement between the taxpayer and the relevant entity and that the advances were made pursuant to those particular loan agreements.

38. In seeking to satisfy the onus which is placed upon the Applicant it is important to note the following:

    (a) first, if there is an absence of contemporaneous, corroborating records which could confirm the existence of the loan in question, the Applicant's task of discharging his onus will be more difficult to achieve: *Nguyen and Commissioner of Taxation* [2011] AATA 544 at [6] and [8];

    (b) secondly, as it is the Applicant who is asserting the existence of such a loan and the advances made under it, he may and should give evidence as to the existence of the loan. However, as such assertions are clearly self-serving such evidence will be approached critically and will be subject to careful scrutiny: *Nguyen and Commissioner of Taxation* [2011] AATA 544 at [7]; and

    (c) thirdly, in assessing whether the taxpayer has discharged the onus placed upon him, the existence of a loan agreement and the character of the advances in particular as to whether they are made pursuant to that loan agreement must inevitably be assessed objectively – that is according to what a reasonable person would conclude having regard to the words and actions of the parties. In this context the subjective intentions of the parties, while broadly speaking relevant, would in no way be determinative: *Toll (FGCT) Pty Limited v Alphapharm Pty Limited* (2004) 219 CLR 165 at [40].

LOANS OR INCOME – THE TRIBUNAL'S EVALUATION

Did the First Arrangement create a loan or loans?

39. In the year to 30 June 2010, the Applicant was in receipt of funds totalling almost $640,000 from Redd Holdings. The Applicant asserts that that amount was entirely the subject of a loan agreement which was in existence as at the date the funds were received namely on 12 August 2009 and 5 January 2010.

40. There are a number of aspects to the arrangement which suggest that there is insufficient evidence here to support the existence of the said loan. In particular, there is no documentary evidence whatsoever to suggest:

- the existence of such a loan agreement between Redd Holdings and the Applicant;
- what the terms of the purported loan were;
- whether the directors of Redd Holdings passed any resolutions to make such a loan;
- that there was an advance or drawdown of an initial amount pursuant to a loan arrangement;
- that there was any interest to be paid by the Applicant (or any other party for that matter) on the purported loan;
- that Redd Holdings received any such interest – there is certainly no indication in any evidence to suggest for example that interest income was received by Redd Holdings;
- that there was to be any repayment of the loan and if so on what timeframe.

41. The Applicant contends that:

- the existence of the loan is supported by the Agreement to Assign dated 14 February 2011 which was provided to the Tribunal and bears the identifier Exhibit A1. That agreement declares that all "right, title and interest in the Debt and the Agreement" is assigned. "Debt" was defined in Schedule 3 as "all indebtedness (present or future, actual or contingent) of the Debtor to the Assignor under the Agreement and "Agreement" was defined as "the Loan Agreement dated around 30 June 2010 between the Debtor and the Assignor".

- the fact that repayments were made from 30 June 2014 support the fact that the loans previously existed; and
- the fact that the accounts of Eugenius and Galerius make reference to the relevant loans also support the fact that the loans previously existed.

42. I agree that the matters raised by the Applicant are relevant but their cogency is significantly diminished by the following facts:

- no written loan agreement has ever surfaced;
- the Agreement to Assign refers to a loan agreement dated around 30 June 2010 but the advances in dispute here were made on 12 August 2009 and 5 January 2010. The Applicant asserts that the receipts by the taxpayer on those dates were received as advances made pursuant to a loan agreement. Even if one accepts the Agreement to Assign on its face, it would only support the existence of the relevant loan as having come into existence on or around 30 June 2010 which post-dates the relevant period in which the actual payments were made;
- there is no other independent, verifiable evidence of the existence of the loan or its terms – no relevant director's resolutions, no reference to the loans in bank documents or valuations, or in any other form;
- the repayments were commenced only after the Applicant became aware that the Respondent was conducting a careful review of these financial arrangements and was likely to challenge the existence of the loans in question;
- the loan repayments weren't made in accordance with a prescribed repayment schedule, nor was there evidence of any schedule in the corroborating material;
- the accounts of both Eugenius and Galerius were unsigned and unaudited accounts of two companies of which the Applicant was the sole director. This can hardly be used as objective evidence of the existence of a loan when the very person who is asserting the existence of the loan is solely responsible for the preparation of the relevant accounts.

43. In determining whether there was in existence a loan of the kind advocated for by the Applicant, the words of Edmonds J in *Commissioner of Taxation v Rawson Finances Pty Ltd* [2012] FCA 735 (*Rawson Finances*) at [20] are apposite:

> *"The essence of a loan of money from A to B is a corresponding contemporaneous obligation on the part of B to repay the money transferred from A to B: Commissioner of Taxation v Radilo Enterprises Pty Ltd* [1997] FCA 22; (1997) 72 FCR 300 at 313 per Sackville and Lehane JJ*: Commissioner of Taxation v Firth* (2002) 120 FCR 450 at para [73] per Sackville and Finn JJ*. Absent that obligation, the transfer of the money from A to B is something else – a gift, a payment by direction , a payment or repayment of an anterior obligation – but it is not a loan. The obligation of repayment is not proved by subsequent payment of the same amount, let alone a different amount, from B to A; that may be explicable by reference to another obligation or circumstance having nothing to do with the original payment from A to B. Rather the obligation of repayment is proved by the terms of the contract under which the money was transferred from A to B."*

44. Here there was no contract reflecting any obligation to repay let alone a contemporaneous obligation. Further, as Edmonds J indicates, the repayments that were made in and of themselves do not prove the existence of an obligation to repay.

45. In the end, it appears to me that the only two pieces of relevant evidence available are the Agreement to Assign which, for reasons I have already explained, would appear to have little probative value, and the taxpayer's assertions that the loan existed and payments were made pursuant to that loan.

46. In the face of all these matters I find as a fact that the loans in question did not exist at the relevant time the advances were made to the Applicant under the First Arrangement.

Did the Second Arrangement create a loan or loans?

47. In relation to this Second Arrangement there was a loan agreement in existence albeit one which is dated 22 July 2011 and which makes provision for "any advance or loan made to the Borrower by the Lender after the date of this Agreement". In other words, this loan agreement may be evidence of any advances that may have taken place after 22 July 2011. All the advances in relation to the Second Arrangement appear to have taken place at varying times prior to 22 July 2011 and accordingly, on its face, the loan document which has been tendered to the Tribunal cannot cover the payments made under the Second Arrangement. Picking up on the words of Edmonds J in *Rawson Finances*, it is difficult to see how the loan agreement that came into existence well after the initial advances were made can be said to give rise to a "corresponding contemporaneous obligation" on the part of the Applicant to repay Eugenius Holdings.

48. It was asserted by the Applicant that the definition of "Advance", as described above, was a mistake, but this seems unlikely when the provision itself makes reference to any advance or loan made to the Borrower by the Lender **after the date of this agreement** (emphasis added).

49. In this context, the following matters are also important to note:

- other than the post-dated loan agreement, there are no documentary materials evidencing any loan agreement between the Applicant and Eugenius for any of the payments that were made to the Applicant by Eugenius under the Second Arrangement;
- there is no other documentary evidence supporting the existence of the loan such as a resolution by the director of Eugenius, any bank records or any other possible means of objectively corroborating the existence of a loan;
- there is no evidence of any interest having been charged or paid on the alleged loan by Eugenius to the Applicant. Even if one took into account the loan agreement dated 22 July 2011, clause 3.1 made reference to the payment of interest but no such interest was ever paid and the clause was largely disregarded by the parties;
- that in the tax returns filed for the 2011 income year by Eugenius no interest was returned as having been received by Eugenius in respect of any loan made to the Applicant.

50. In the context of the Second Arrangement, it would seem that the only evidence which is available is the loan agreement which post-dates all the advances in question and the Applicant's own evidence as to his intention for a loan to have existed at all relevant times. The same comments made previously regarding the repayments and company accounts would apply here.

51. In the face of all these matters I again find as a fact that the loans in question did not exist at the relevant time the advances were made to the Applicant under the Second Arrangement.

Did the Third Arrangement create a loan or loans?

52. The Applicant has again identified a loan agreement dated 19 July 2012 which makes reference to "any advance or loan made to the Borrower by the Lender after the date of this Agreement". Once again, this loan agreement only contemplates the prospect of advances and does not contemplate advances which predate the date of the agreement. Again the Applicant asserts that the definition of "Advance" is a mistake and that the loan agreement supports the conclusion that the payments were made pursuant to the loan agreement in question.

53. With this arrangement, the circumstances are somewhat different - three of the five payments in question under this arrangement were similarly made well before the date of the purported agreement. In respect of the other two payments, one was made on 17 July 2012 and the other on 18 December 2012 with the purported agreement having been entered into on 19 July 2012.

54. In respect of the three payments made well before the loan agreement, again picking up on the words of Edmonds J in *Rawson Finances*, it is difficult to see how the loan agreement that came into existence well after the three payments were made can be said to give rise to a "corresponding contemporaneous obligation" on the part of the Applicant to repay Galerius.

55. As with the Second Arrangement, there are important factors which suggest that there was no loan in place at the time the payments in question arose. In particular, I refer to the following matters:

- there was no documentary evidence of any loan agreement between the Applicant and Galerius in respect of the three payments that were made. The loan agreement which the Applicant has produced is dated 19 July 2012, a date which is after the last of the three payments in question;
- other than the post-dated loan agreement, there is no documentary material evidencing the existence of the loan such as a resolution of the directors of Galerius to make such a loan to the Applicant nor any other documentary material such as a reference to the loan in bank documents etc.;

- there is no evidence of any interest having been paid on the purported loan made by Galerius to the Applicant. Again, clause 3.1 of the loan agreement dated 19 July 2012 did make provision for the payment of interest but this clause was essentially disregarded by the parties;
- the Applicant's assertion that the loan to him from Galerius was repaid on or around 19 July 2012 by Galerius declaring a dividend of $1.7 million in favour of Galerius Holdings Pty Ltd and a loan made by Galerius Holdings to the Applicant of the same amount on the same date is in my view untenable having regard to the fact that:

    (a) Galerius Holdings at that date had no bank account;

    (b) no amounts were advanced pursuant to the purported loan; and

    (c) no amounts were paid pursuant to the purported loan.

  In fact, none of the steps which the Applicant asserts occurred in July 2012 would appear to be supported by any income flows which are recorded in bank records.

56. Again, there appears to be little other than the existence of a post-dated loan agreement and the taxpayer's uncorroborated evidence to support the existence of a loan at the relevant times. The same comments made previously regarding the repayments and company accounts would apply here.

57. As to the payment of $80,000 made on 18 December 2012, this payment did post-date the Loan Facility Agreement made on 19 July 2012. That is a factor that would lend support to the view that the payment is made pursuant to that loan agreement.

58. On the other hand, there is no evidence to demonstrate that any interest was ever paid to Galerius by the Applicant as required by the terms of clause 3.3 of the Loan Facility Agreement. Even taking into account clause 3.2 of the Loan Facility Agreement which eliminates the need to pay interest until the end of the year in which the advance is made, some interest should have been paid under the facility. Indeed there is no evidence to suggest that a tax return was filed by Galerius disclosing interest received in the relevant year of income.

59. Nonetheless, having regard to the totality of the evidence, I am satisfied that this payment was made pursuant to the Loan Facility Agreement. The fact that no interest was paid may amount to a breach of the terms of that agreement but does not lead to the inevitable conclusion that the payment was not made as part of that agreement.

60. As to the payment of $1,000,000 made on 17 July 2012, even though the payment precedes the date of the loan by 2 days, it is in such close temporal proximity that it is difficult to conclude that it was not made as part of the overall loan arrangement based simply on the timing. It is true that it is not "any advance or loan made to the Borrower by the Lender after the date of this agreement" as required by the definition of "Advance" in clause 1.1 of the Loan Facility Agreement but it is not reasonable in the circumstances to give the definition such precise application where the dates are so close in time. Again, even though it is the case that no interest was paid as required by the loan agreement, I am satisfied that this payment was made as an advance under the Loan Facility Agreement.

61. Thus, in light of all the matters raised above, the Tribunal concludes that in respect of the first three payments made to the Applicant on 19 October 2011, 15 February 2012 and 21 May 2012, those payments were all income of the Applicant. The two payments made on 17 July 2012 and 18 December 2012 were both loans made to the Applicant under the Third Arrangement.

Is Division 7A of the 1936 Act relevant in this context?

62. Reliance was placed by the Applicant upon Division 7A and in particular s 109N of the 1936 Act to give support to the existence of the loan which he asserted existed at the relevant time.

63. The Applicant noted in particular that s 109N(1)(a) requires that in order for a loan agreement to come within the section, it must be recorded in writing "before the lodgement date for the year of income". Thus, according to the Applicant, the section specifically contemplates that a loan agreement may be reduced to writing after the relevant year of income has concluded.

64. There is no doubt that the relevant subsection to which the Applicant refers is of assistance inasmuch as any loan which does exist can still satisfy the terms of the section

even if it is reduced to writing only after the conclusion of the relevant year of income. However, this does not mean that the essential requirements for the existence of a loan no longer need to be independently established before s 109N can come into play. To put it another way, s 109N says nothing about what is required to establish the objective existence of the loan.

65. In this case, the Tribunal is not satisfied the taxpayer has demonstrated, based on verifiable objective evidence that a loan existed at the relevant time. Division 7A of the 1936 Act is of no relevance to that fundamental question.

66. The Applicant argued that "Div 7A, as part of its operation as a 'shield' protects the Applicant from assessment because Div 7A loan agreements are in place": Applicant's Closing Submissions, paragraph [8].

67. Fundamentally that proposition in the abstract is correct because it assumes that a Division 7A **loan** is in place. In the present circumstances, the existence of a loan is the very thing which the Respondent is challenging. Division 7A neither proves nor disproves the existence of the loan.

Is the Voluntary Undertaking relevant in this context?

68. The Applicant made much of the Enforceable Voluntary Undertaking which the Applicant entered into. In particular, he asked the rhetorical question:

> *"if the arrangements generally concerning the applicant, and particularly with respect to BR Redd Holdings Ltd (a company limited by guarantee) were not properly loans, why was it necessary for the Commissioner to enter into the Enforceable Voluntary Undertaking, in respect of loans from companies limited by guarantee, for the applicant by him "setting up [a] company limited by guarantee… on [his] own behalf?"*

69. In raising this issue the Applicant appears to be asserting that the Respondent had at some point accepted that a loan did exist and was dealing with that loan arrangement through the so-called Enforceable Voluntary Undertaking.

70. An Enforceable Voluntary Undertaking is an arrangement which the Respondent has entered into in relation to a particular problem that he has identified and is designed to

prevent further cases arising based on the same facts until the initial cases are formally resolved either through a judicial or quasi-judicial process or by settlement.

71. It cannot be taken to in any way control or dictate the view which the Commissioner may take upon a full analysis of the relevant factual circumstances which may subsequently come to light.

72. In particular, the Respondent from time to time releases Tax Alerts and one such Alert was issued in relation to the arrangements in question here. This led to the Enforceable Voluntary Undertaking which was agreed to in circumstances where the Respondent had unearthed certain information about arrangements but often had little in the way of detail available to him. It cannot be seriously suggested that his hands are tied in any subsequent analysis of the arrangements which are based on a detailed understanding of the facts which have emerged later.

73. For that reason, I do not consider that anything the Respondent has accepted in the making of the Enforceable Voluntary Undertaking in any way constrains him in any subsequent analysis or review.

PENALTIES – TRIBUNAL'S EVALUATION

74. In this case, the Tribunal has concluded that the Applicant has not discharged his onus of demonstrating that the amounts in question were received by way of loans other than in respect of the amount of $1,000,000 paid on 17 July 2012 and the amount of $80,000 paid on 18 December 2012.

75. Accordingly, two consequences must follow:

    (a) first, the manner in which he has prepared and lodged his tax returns for each of the 2010, 2011, 2012 and 2013 income years means each of these returns contains a statement which is false or misleading in a material particular as referred to in s 284–75(1) of Schedule 1 of the Administration Act; and

    (b) secondly, the Applicant has a shortfall amount under s 284–80(1) of Schedule 1 because his taxation liability for each of the 2010, 2011, 2012 and 2013 income

years was in each case less than it would have been if the false or misleading statement had not been made (Item 1).

76. In view of that it was determined by the Respondent that the base penalty amount under s284–90(1) of Schedule 1 was to be 75% of the shortfall amount. This was on the basis that the shortfall amount resulted from intentional disregard of a taxation law pursuant to s 284–90(1), Item 1 of Schedule 1 of the Administration Act.

77. The critical issue for this Tribunal to determine is whether or not the shortfall amount has been appropriately determined on the basis of an intentional disregard for the law. The onus in this respect also rests on the taxpayer to demonstrate that the shortfall amount for each of the 2010, 2011, 2012 and 2013 income years did not result from an intentional disregard of the taxation law: *Re Applicant and Commissioner of Taxation* (2012) 88 ATR 222 at [202] and [214].

78. Intentional disregard by the very nature of the words themselves implies a requirement that there be actual knowledge that the statement in question is false or misleading. In other words, in order to support a conclusion that a taxpayer has intentionally disregarded the law, the taxpayer would have to have:

(a) understood the effect of the relevant legislation and how it operates in respect of their specific tax affairs; and

(b) made a deliberate choice to ignore that law.

79. In this case, the Applicant is an experienced lawyer with extensive academic qualifications in law, finance and taxation. He was also the directing mind and will of each of Redd Holdings, Eugenius and Galerius.

80. Nonetheless, it is the view of this Tribunal that the Applicant has not deliberately chosen to ignore the law. His evidence presented to the Tribunal suggests that he genuinely believed that there were arguments to support his view that a loan was in existence and while this may have been wildly optimistic in respect of all but two of the payments in question and not genuinely supportable on the basis of the evidence available, he appears to have been genuinely of that mistaken view.

81. The Applicant's testimony provided at the hearing provided a highly subjective view of whether a loan existed in respect of the monies which had been received by him. His language suggested that he genuinely believed in his own mind that the amounts in question were loans even though that view could not be sustained on an objective view of the facts other than in respect of the two amounts of $1,000,000 and $80,000 referred to previously.

82. In my opinion, this is more consistent with a person whose behaviour could be described as reckless in the sense of amounting to gross carelessness or gross indifference to the consequences rather than intentional disregard of the law: *BKR (Bris) Pty Ltd v Federal Commissioner of Taxation* (2001) 46 ATR 347; *Ryvitch v Federal Commissioner of Taxation* (2001) 47 ATR 381; *Pearson v DCT* (2009) 74 ATR 437.

83. Accordingly I am of the view that the preferable decision in these circumstances is to impose a penalty of 50% rather than 75% on the basis that the false or misleading statement here involved recklessness covered by Item 2 of s 284–90(1) rather than intentional disregard covered by Item 1 of that section.

84. In relation to the 2011, 2012 and 2013 income years, the administrative penalty of 75% was increased by a further 20% under s 284–220(1)(c) of Schedule 1 of the Administration Act. As a result of the finding by this Tribunal that the appropriate penalty is 50% based on recklessness rather than intentional disregard, the relevant item number becomes Item 2 of Schedule 1. As s 284–220(1)(c) of Schedule 1 refers to both Items 1 and 2 (and item 3 which is of no relevance here) the same base penalty increase by 20% applies in respect of the three income years identified.

REMISSION – TRIBUNAL'S EVALUATION

85. The Applicant has sought an exercise of the Respondent's discretion to remit penalties under s 298–20 of Schedule 1 of the Administration Act.

86. The legislation itself is silent on the matters the Respondent must consider in deciding whether to exercise the discretion to remit an administrative penalty. However, there are a number of important matters raised by the relevant case law and administrative rulings:

- the relevant factors are determined by reference to the subject matter, scope and purpose of s 298–20: *BHP Billiton Direct Reduced Iron Pty Ltd v DCT* (2007) 67 ATR 578;
- the question which the Tribunal must address itself to in connection with the application for the remission of penalties is whether the outcome arising by reason of the imposition of the penalty is harsh having regard to the particular circumstances of the Applicant: *Dixon as Trustee for Dixon Holdsworth Superannuation Fund v Commissioner of Taxation* (2008) 167 FCR 287 at [26];
- the Respondent is obliged to treat taxpayers in like circumstances consistently and must exercise the discretion in such a way as to not discriminate between taxpayers: *Bellinz Pty Ltd v Federal Commissioner of Taxation* (1998) 39 ATR 198;
- the penalty may be remitted if the prescribed penalty rate is blatantly unjust to the taxpayer: *Re Johnston and Federal Commissioner of Taxation* (2011) 81 ATR 908;
- taxpayers with a good compliance history are likely to be treated more leniently. However, the weight given to compliance history may vary depending on the circumstances of the breach in question: ATO Practice Statement Law Administration 2005/2;
- the penalty imposed for a false or misleading statement is unlikely to be remitted if a taxpayer has been reckless or intentionally disregards the law: ATO Practice Statement Law Administration 2005/2;
- a taxpayer's personal circumstances are important considerations – circumstances which are outside the taxpayer's control such as natural disasters or serious illness are taken into account where it would be fair and reasonable to do so: ATO Practice Statement Law Administration 2014/4.

87. Having regard to these matters, the Tribunal notes that the penalty imposed could not be described in this case as being harsh or unreasonable having regard to the reckless way in which the arrangements were by and large conceived and executed. There were no circumstances here that were outside the Applicant's control. Furthermore, as emphasised above, where a taxpayer's behaviour has been reckless such as to attract a 50% penalty it is unlikely that there would be a remission of the penalty.

DECISION

88. The decision under review is varied by:

- excluding the amount of $1,000,000 and $80,000 from the assessable income of the Applicant in respect of the year to 30 June 2013; and
- reducing the base penalty from 75 % to 50%.

In all other respects the decision under review is affirmed.

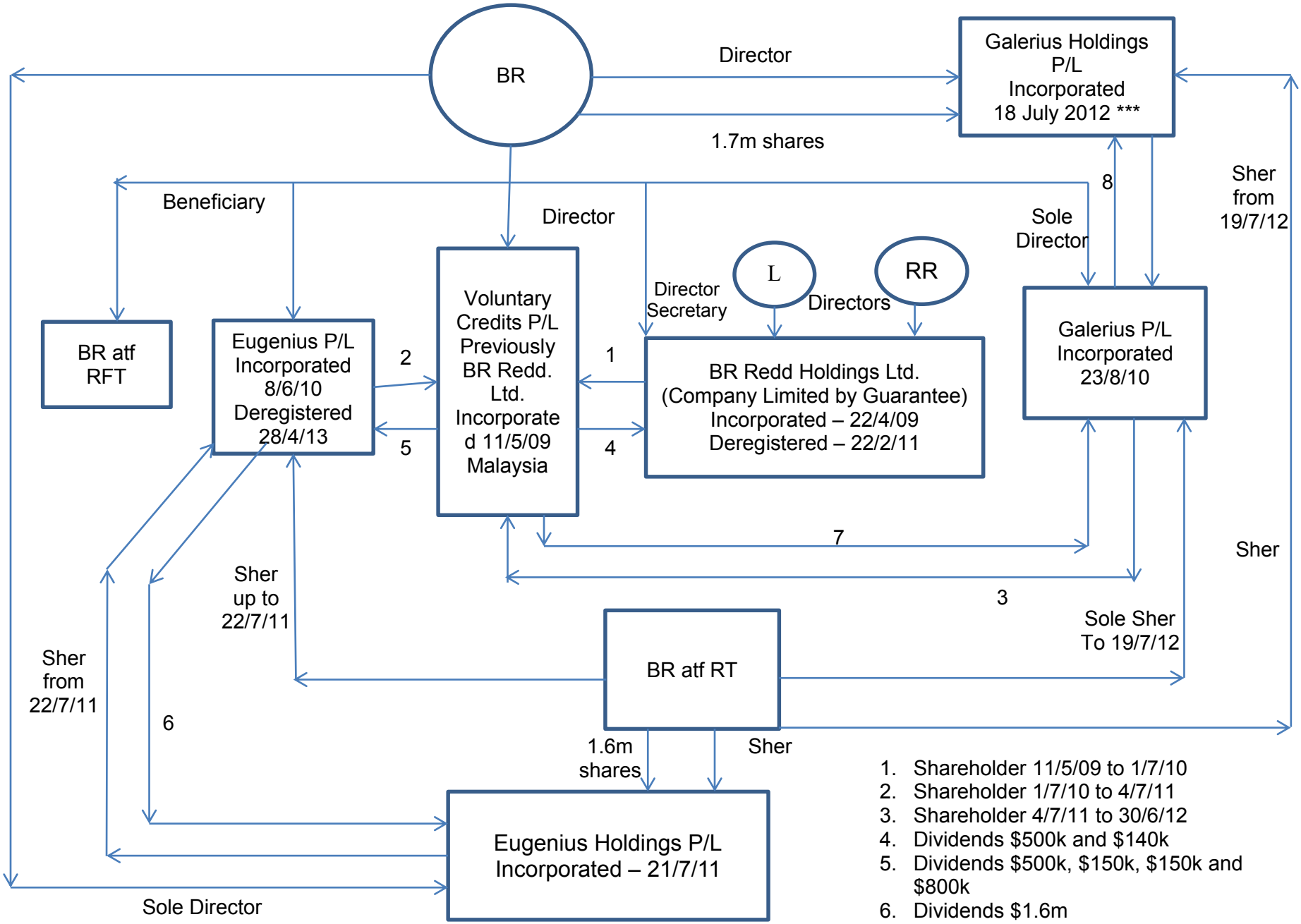
I certify that the preceding 88 (eighty -eight) paragraphs are a true copy of the reasons for the decision herein of Professor R Deutsch, Deputy President

.....[sgd].....

Associate

Dated 24 June 2016

Date(s) of hearing	**23 and 24 November 2015**
Date final submissions received	**8 December 2015**
Counsel for the Applicant	**Mr Ian Young**
Solicitors for the Applicant	**Rubicon Lawyers**
Counsel for the Respondent	**Mr Michael O'Meara**
Solicitors for the Respondent	**Australian Government Solicitor**



1. Shareholder 11/5/09 to 1/7/10
2. Shareholder 1/7/10 to 4/7/11
3. Shareholder 4/7/11 to 30/6/12
4. Dividends $500k and $140k
5. Dividends $500k, $150k, $150k and $800k
6. Dividends $1.6m
7. Dividends $200k, $100k, $500k, $1m and $80k
8. Dividend $1.7m