HIGH COURT OF AUSTRALIA

FRENCH CJ,
KIEFEL, GAGELER, KEANE AND GORDON JJ

VAUGHAN RUDD BLANK APPELLANT

AND

COMMISSIONER OF TAXATION RESPONDENT

Blank v Commissioner of Taxation
[2016] HCA 42
9 November 2016
S144/2016

ORDER

1. *Appeal dismissed with costs.*

2. *Application for special leave to cross-appeal dismissed with costs.*

On appeal from the Federal Court of Australia

Representation

M Richmond SC with T O Prince for the appellant (instructed by Clayton Utz Lawyers)

J T Gleeson SC, Solicitor-General of the Commonwealth and J O Hmelnitsky SC with M J O'Meara for the respondent (instructed by Minter Ellison Lawyers)

CATCHWORDS

Blank v Commissioner of Taxation

Income tax – Assessable income – Where taxpayer participated in employee incentive profit participation agreement – Taxpayer granted claim to deferred compensation calculated on basis of company profit – Amount payable under agreement to taxpayer on termination of employment and execution of declaration of assignment and release – Whether amount income according to ordinary concepts or capital gain.

Words and phrases – "deferred compensation", "*Genussscheine*", "incentive profit participation agreement", "ordinary income", "pecuniary account".

Income Tax Assessment Act 1936 (Cth), s 26(e).
Income Tax Assessment Act 1997 (Cth), s 6-5(1), (4).
Swiss Code of Obligations, Art 657.

FRENCH CJ, KIEFEL, GAGELER, KEANE AND GORDON JJ.

Introduction

1 The appellant, Mr Blank, was employed by Glencore Australia Pty Ltd, a wholly owned subsidiary of Glencore International AG ("GI"). Glencore Australia provided services including the services of Mr Blank to Glencore AG, also a wholly owned subsidiary of GI. An incentive profit participation agreement between Mr Blank, GI and Glencore AG provided "deferred compensation" for services to be rendered by Mr Blank, payable after notice of termination of his employment ("the IPPA 2005"). Mr Blank resigned and, pursuant to the IPPA 2005, on 15 March 2007 he became entitled to receive USD 160,033,328.25 payable in instalments ("the Amount"). Was the Amount income according to ordinary concepts and therefore part of Mr Blank's assessable income pursuant to s 6-5 of the *Income Tax Assessment Act* 1997 (Cth) ("the 1997 Act")? The answer is "yes".

2 Mr Blank did not return the Amount as income according to ordinary concepts but treated the 15 March 2007 event as giving rise to a capital gain in the 2007 income year. On appeal to this Court, Mr Blank contended that the Amount was the proceeds of the exploitation of interconnected rights that conferred on him a right to receive, in the future, a proportion of the profit of GI and therefore assessable as a capital gain. That contention should be rejected.

3 Accordingly, the alternative contentions of the respondent, the Commissioner of Taxation, that the Amount was assessable income in Mr Blank's hands on other bases – under the second limb of *Federal Commissioner of Taxation v Myer Emporium Ltd*[1] or as an eligible termination payment under s 27A(1) of the *Income Tax Assessment Act* 1936 (Cth) ("the 1936 Act") or an employment termination payment under s 82-130(1)(a)(i) of the 1997 Act (both "ETP") – do not arise. Similarly, any issue about how the cost base of any "rights" was to be determined if the Amount was in the nature of a capital gain does not arise.

4 The appeal should be dismissed with costs.

5 By an application for special leave to cross-appeal, the Commissioner sought to contend that if the Amount was assessable income under s 6-5 of the 1997 Act, then Mr Blank derived two instalments of the Amount in the

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1 (1987) 163 CLR 199; [1987] HCA 18.

2007 income year because those instalments were "applied or dealt with" on his behalf or as he directed within the meaning of s 6-5(4) of the 1997 Act ("the timing question"). Special leave to cross-appeal on the timing question should be refused. The special leave application should otherwise be dismissed because the other issues do not arise.

6 These reasons will address the facts and then turn to consider whether the Amount was income according to ordinary concepts and therefore part of Mr Blank's assessable income pursuant to s 6-5 of the 1997 Act. Finally, the Commissioner's application for special leave to cross-appeal on the timing question will be addressed.

Facts

The Glencore Group and Mr Blank's employment

7 Glencore Holding AG ("GH") was the ultimate holding company of the Glencore group of companies ("the Glencore Group"). The Glencore Group operated one of the world's largest international commodity trading businesses.

8 GI was incorporated in Switzerland. 85% of the shares in GI were held by GH. Until 2002, the remaining 15% of the shares in GI were held by an unrelated industrial company. From 2002, the remaining 15% of the shares in GI were owned by Glencore LTE AG, another company in the Glencore Group.

9 The shares in GH and Glencore LTE AG were owned by employees of the Glencore Group who were invited and agreed to participate in "employee profit participation plans" operated by GI. Key employees of GI were therefore the indirect owners of shares in GI.

10 Between November 1991 and 31 December 2006, Mr Blank was employed by either GI or one of its wholly owned subsidiaries and, until early 2002, he worked variously in South Africa, Switzerland and Hong Kong.

11 Mr Blank arrived in Australia in early 2002 to take up a position as a senior trader in the coal division with Glencore Australia. Mr Blank became a resident of Australia on 2 January 2002 and retained that fiscal status.

Profit participation agreements and shareholders' agreements

12 From about 1993 until 2010, GI operated employee profit participation plans. Certain employees of GI and its subsidiaries were selected to participate in a plan and become entitled to receive financial benefits. Employees'

participation in the plans was in addition to their salary and any bonuses they were entitled to receive.

13 Mr Blank's participation was initially governed by two "stapled" agreements – an agreement with GI entitled "Profit Participation Agreement" ("the PPA 1993") and an agreement with GH entitled "Shareholders' Agreement" ("the SA 1994"). They were "stapled" in that the validity of each of the PPA 1993 and the SA 1994 depended on the execution of the other agreement. The PPA 1993 was amended in 1996 and replaced prospectively in October 1999 by a new profit participation agreement with GI ("the PPA 1999"). It was common ground that the PPA 1993, the PPA 1993 (as amended in 1996) and the PPA 1999 were substantially similar. It is therefore necessary to turn to consider the terms of the PPA 1999.

The PPA 1999 and the SA 1994

14 Under the PPA 1999, Mr Blank was granted a "Profit Participation", defined as "a participation in the results[2] of GI", in the form of (a) "Genussscheine" ("GS") and (b) a contractual claim[3].

15 GS are provided for by Art 657 of the Swiss Code of Obligations. The English translation of Art 657 relied on by the parties translated GS as "profit sharing certificates" and relevantly provided:

> "1 The articles of incorporation may foresee the creation of profit sharing certificates in favor of persons who are linked with the Company … as … *employee* or in a similar way. They must state the number of issued profit sharing certificates and the content of the rights attached thereto.
>
> 2 With the profit sharing certificates, the persons entitled may be granted ***claims*** *only to a share of the balance sheet profit* ...
>
> 3 The profit sharing certificate shall not have a par value; it shall neither be called participation certificate nor be issued against a contribution which is shown under the assets in the balance sheet." (emphasis added)

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2 The PPA 1993 used the expression "future profits" rather than "results".

3 cl A.1 of the PPA 1999.

16 An English translation of Art 8 of GI's Articles of Incorporation, entitled "Profit Sharing Certificates", recorded that GI had issued 150,000 profit sharing certificates "intended for distribution to employees" of GI or any other company controlled by GI[4]. Article 8.2 relevantly recorded that:

> "A profit sharing certificate *grants* ***upon restitution to [GI]*** *a* ***claim*** *to a cumulative portion of the balance sheet profit* … during the period of ownership in the profit sharing certificate in proportion to the total number of profit sharing certificates effectively issued at any given time. However, if a holder of profit sharing certificates ceases to be an employee of [GI], or of other companies directly or indirectly controlled by [GI], then he shall on cessation transfer any profit sharing certificates to [GI] and *he shall have no claim to any payment from [GI] in respect of the* ***restitution*** *to [GI] of any* profit sharing certificates allocated within 24 months of the date of cessation, except if termination of employment is due to death or disability." (emphasis added)

17 This provision is important. Consistently with Art 657 of the Swiss Code of Obligations, it provides that a profit sharing certificate – a GS – grants a *claim* to a cumulative portion of the balance sheet profit. However, Art 8.2 states that the *claim* is granted not upon the issue or allocation of the GS to the employee, but *upon restitution* to GI of the GS, and then only in respect of those GS issued more than 24 months before employment ceases. The limited nature of the GS is reinforced by other provisions of GI's Articles. The holders of GS have no voting rights (or rights in connection with voting), no right to call a general meeting of shareholders, no right to attend a shareholders' meeting, no right to information, no right of inspection and no right to move motions[5].

18 The PPA 1999 recorded that GI's Articles authorised it to issue GS registered in the name of a holder (an employee) which "grant a *claim* to profit participation"[6] (emphasis added).

19 Under the PPA 1999, the Profit Participation was calculated as follows. First, with effect from 31 December each year, the net income of GI on a consolidated basis was adjusted in accordance with an Annexure to the

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4 Art 8.1 of GI's Articles.

5 Art 8.3 of GI's Articles.

6 cl A.3.1 of the PPA 1999.

PPA 1999 to establish the "Net Income for Profit Participation"[7]. Mr Blank, as a holder of GS, was allocated a portion of that Net Income for Profit Participation for a particular year in the proportion of the number of GS held by him to the total number of GS on issue[8] ("Periodical Profit Participation"). The Periodical Profit Participation was allocated as profit participation under the GS and the contractual claim in a 55/45 split[9].

20 The Periodical Profit Participation for each issue of GS to Mr Blank was "aggregated" over the period he held GS from the date the GS were allocated up to and including, relevantly, the last day of the month in which notice of termination of employment was received ("the Notice Date")[10].

21 The PPA 1999 reinforced the terms of Art 8 of GI's Articles and provided that the only GS to "participate" in the Net Income for Profit Participation were those GS which, on the Notice Date, had been allocated for more than 24 months[11].

22 If a holder of GS ceased employment, returned all GS to GI and executed a declaration of assignment and general release substantially in the form annexed to the PPA 1999, then, 30 days after the Notice Date, that ex-employee's Profit Participation became due as a debt bearing interest and was to be paid in USD in 20 equal quarterly instalments[12]. A proportion of each instalment was to be withheld and paid to the Swiss Federal Tax Administration ("the Swiss FTA") on account of Swiss withholding tax[13], that proportion being 35% of the 55% of the instalment distributed under the GS. That proportion applied so long as approval by the Swiss FTA was maintained for 55% of the Profit Participation to be paid

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7 cll A.2.1 and A.2.2 of the PPA 1999.

8 cll A.2.2 and A.2.3 of the PPA 1999.

9 cl A.2.3 of the PPA 1999.

10 cl A.2.4 of the PPA 1999.

11 cll A.2.2 and A.2.3 of the PPA 1999.

12 cll A.5, A.6.1, A.6.2, A.7 of the PPA 1999.

13 cl A.9 of the PPA 1999.

as "profit distribution under his GS" and the balance (45%) under the contractual claim[14].

23 GI could offer to repurchase Mr Blank's GS prior to termination of employment on terms not more favourable than his Profit Participation[15]. GI did not enter into such an arrangement with Mr Blank. Mr Blank did not have a contractual right to require GI to repurchase GS from him.

24 The PPA 1999 was "stapled" to the SA 1994 in the sense that the validity of the PPA 1999 was conditional on the execution of the SA 1994[16]. Under the SA 1994, Mr Blank was entitled to purchase and be issued shares in GH from time to time at their par value of CHF 50 per share, provided that he had executed a profit participation agreement with GI, executed the SA 1994 and paid cash for the shares[17]. Upon occurrence of a "Triggering Event", including termination of employment of the employee, GH had a call option by which it could require Mr Blank to sell to it the shares in GH at their par value[18]. The employee could not sell, assign, transfer or otherwise deal with the shares in GH without the prior written consent of GH[19] or the occurrence of a Triggering Event.

25 The SA 1994 also provided that GH, in its capacity as majority shareholder in GI, would to the extent permitted by law provide that "profits [of GI] are otherwise distributed according to [GI's] contractual obligations", and "in particular" under profit participation plans concluded with shareholders of GH[20].

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14 cll A.3.5 and A.4 of the PPA 1999.

15 cl A.10 of the PPA 1999.

16 cl B.1 of the PPA 1999.

17 cll A.2 and B.5 of the SA 1994.

18 cl D.4.1 of the SA 1994.

19 cl D.3 of the SA 1994.

20 cl C.2.3.1 of the SA 1994.

26 Between 1994 and May 2002, Mr Blank was successively issued with a total of 1,500 GS by GI and subscribed for an equal number of shares in GH.

The IPPA 2003

27 In about June 2003, Mr Blank executed an agreement entitled "Incentive Profit Participation Agreement" ("the IPPA 2003") with GI and Glencore AG. The Preamble recorded that Mr Blank was employed by a subsidiary of GI – at that time, Glencore Australia. That subsidiary provided services including the services of Mr Blank to Glencore AG. The IPPA 2003, between Mr Blank, GI and Glencore AG, provided "deferred compensation" in "consideration of the services to be rendered" by him to the subsidiary[21], payable after notice of termination of his employment.

28 In an English translation of Art III of Glencore AG's Articles of Association, which dealt with GS, "Genussscheine" was translated to mean "bonus papers" and the article relevantly recorded that:

> "The company may issue up to 150,000 [GS] to its … staff …
>
> *When it is handed back to the company*, a [GS] *gives an entitlement to a cumulative share of the balance sheet profit* to be determined by the General Meeting on the basis of the change in the equity capital during the period of possession of the [GS], in proportion to the total number of [GS] effectively issued on each occasion.
>
> The holders of [GS] have no voting rights and none of the accompanying rights, in particular no right to convene a General Meeting, no right to attend meetings, no right to information, no right to inspect documents and no right to make proposals.
>
> The [GS] are registered and may not be transferred to third parties without the approval of the Board of Directors; such approval may be withheld without stating reasons …
>
> The company may at any time withdraw and re-issue [GS] which have already been issued.
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> …

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21 pars 4 and 5 of the Preamble to the IPPA 2003.

> The person whose name is entered in the [GS] register is regarded as the owner of that [GS] in relation to the company.
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> …
>
> Ownership of a [GS] and the exercise of any rights carried by that [GS] presupposes acknowledgement of the articles of association in their currently valid version." (emphasis added)

29 Under the IPPA 2003, rather than Mr Blank being issued with GS by GI, Glencore AG agreed to issue GS to GI[22]. The IPPA 2003 recorded that the GS issued by Glencore AG to GI under Art 657 of the Swiss Code of Obligations were "[s]olely for [the] purposes of calculating the amount of Profit Participation" and were to "serve as phantom units (PHANTOM UNITS) for the purpose of calculating" Mr Blank's Profit Participation under the IPPA 2003, which was the "deferred compensation"[23]. Mr Blank had no interest whatsoever in the GS issued by Glencore AG[24]. A Phantom Unit issued under the IPPA 2003 had the same purpose as a GS – as the calculation mechanism for determining an employee's Profit Participation.

30 Unlike the PPA 1993, which defined Profit Participation as participation in the "future profits" of GI, or the PPA 1999, which defined Profit Participation as participation in the "results" of GI, the IPPA 2003 defined Profit Participation as "deferred compensation which will be calculated on the basis of the results of GI"[25].

31 In July 2003, Mr Blank was allocated 100 Phantom Units and purchased 100 shares in GH.

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22 cll A.1.1 and A.1.2 of the IPPA 2003.

23 cll A.1.1 and A.1.2 of the IPPA 2003.

24 cl A.1.2 of the IPPA 2003.

25 cl A.1.1 of the IPPA 2003.

The IPPA 2005 and the SA 2005

32 In 2005, Mr Blank entered into the IPPA 2005, an "Incentive Profit Participation Agreement" with GI and Glencore AG, and a "Shareholders' Agreement" with GH ("the SA 2005").

33 The Preamble to the IPPA 2005 recorded that Glencore Australia performed services including the services of one of its employees, Mr Blank, for Glencore AG under a Service Agreement. The IPPA 2005 was an incentive profit participation agreement between Mr Blank, GI and Glencore AG to provide "deferred compensation" for services to be rendered by Mr Blank to Glencore Australia in connection with the Service Agreement, but payable after notice of termination of his employment. The Preamble also recorded that GI had adopted a "plan of deferred compensation known as the 'Incentive Profit Participation Plan'" for selected employees of GI and its subsidiaries "in consideration of the services to be rendered by" Mr Blank.

34 The IPPA 2005 terminated forthwith "[a]ny prior oral or written agreement related to the *PPU* which are the subject matter of this Agreement"[26] (emphasis added). "PPU" was defined in the IPPA 2005 to mean[27]:

> "[T]he number of GS actually allocated and participating as of a respective date, whether issued by [Glencore] AG under the Plan and any Incentive Profit Participation Agreement (including this Agreement) and held by GI in accordance with the terms of the Plan and this Agreement *or GS issued by GI and held directly by Employees of GI or any of its Subsidiaries pursuant to profit participation agreements*." (emphasis added)

35 That is, all GS or equivalents issued under previous profit participation plans became PPU under the IPPA 2005, with Allocation Dates the same as the dates on which the GS or equivalents had previously been issued[28]. Thus, the IPPA 2005 regulated both the 1,500 GS and the 100 Phantom Units previously allocated to Mr Blank, and was the agreement on foot that governed Mr Blank's entitlements when his employment was terminated. The IPPA 2005

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26 cl C.7 of the IPPA 2005.

27 Item 17 of the definitions in the IPPA 2005.

28 cl A.3.2 and Annex B of the IPPA 2005.

replaced any rights and obligations under previous profit participation plans with the rights and obligations under the IPPA 2005. Such replacement can be described as novation, in the "sense [that] 'novation' means simply a new contract standing in the place of the old"[29].

36 Under the IPPA 2005, GI granted Mr Blank "deferred compensation" to be calculated on the basis of the results of GI, referred to as the Incentive Profit Participation or "IPP"[30]. The GS issued by Glencore AG and "owned and held by GI" were issued solely for the purpose of implementing the plan "and calculating the amount of deferred compensation in the form of PPU" which would be allocated to Mr Blank[31]. Mr Blank had no interest whatsoever in the GS[32]. The IPPA 2005 recognised that Glencore AG had issued GS to GI and stated that the GS would "serve as the PPU hereunder"[33].

37 The IPP "commence[d] as of the Allocation Date"[34]. "Allocation Date" was defined to mean the date when the PPU were allocated[35]. However, only the PPU *allocated* at the *Notice Date* for more than 24 months from the *Allocation Date* were "vested"[36]. "Notice Date" was relevantly defined to mean "the last day ... of the month notice of termination of [Mr Blank] by GI or a Subsidiary is received either by [Mr Blank] or by the employing company"[37].

38 "Net Income for IPP" was defined to mean "income for the year (before attribution) less attribution to minorities, adjusted by other changes in reserves

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29 *Olsson v Dyson* (1969) 120 CLR 365 at 389; [1969] HCA 3.

30 Item 10 of the definitions and cl A.1.1 of the IPPA 2005.

31 cl A.1.2 of the IPPA 2005.

32 cl A.1.2 of the IPPA 2005.

33 cll A.3.1 and A.3.2 of the IPPA 2005.

34 cl A.2.1 of the IPPA 2005.

35 Item 1 of the definitions in the IPPA 2005.

36 cl A.2.1 of the IPPA 2005.

37 Item 13 of the definitions in the IPPA 2005.

(before attribution), but excluding movements in asset revaluation or equivalent reserves and cash flow hedge reserves"[38]. The Net Income for IPP for a particular period was then divided by "the number of PPU *allocated and participating* during that period to produce the Period Amount"[39] (emphasis added). "Periodical IPP" for each allocation of PPU to an employee were aggregated over the period the employee held such PPU from the Allocation Date up to and including the Notice Date[40]. If, at the Notice Date, the aggregated Periodical IPP was negative, it would be deemed to be zero[41].

39 What was then to occur when employment was terminated was addressed in cl A.3.3 of the IPPA 2005, read in conjunction with cl A.2.1. At the Notice Date, only the PPU that had been allocated for more than 24 months vested[42]. Then, with effect from the Notice Date[43]:

> "(a) [Glencore AG] will (i) purchase from GI the GS owned or held by GI with respect to [Mr Blank] or (ii) request that GI change its records as to the GS and reallocate the PPU to a different employee selected under the terms of the Plan, and (b) [Mr Blank] shall execute and remit to GI a declaration of assignment and general release substantially in the form [of an Annexure]."

40 As with the PPA 1999, Mr Blank was to receive 55% of his IPP as profit distribution, which was subject to Swiss withholding tax at a rate of 35%[44]. Amounts for Swiss withholding tax were to be withheld from each instalment paid to Mr Blank[45].

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38 Item 12 of the definitions in the IPPA 2005.

39 cl A.2.3 of the IPPA 2005.

40 cl A.2.4 of the IPPA 2005.

41 cl A.2.5 of the IPPA 2005.

42 cl A.2.1 of the IPPA 2005.

43 cl A.3.3 of the IPPA 2005.

44 cl A.4 and Annex C of the IPPA 2005.

45 cll A.4 and A.9.1 of the IPPA 2005.

41 The IPP became due on the "Due Date", provided that a declaration of assignment and general release had been executed by Mr Blank and submitted to GI[46]. "Due Date" was defined to mean the 30th day *after* the Notice Date[47]. The IPP was a debt bearing interest, which was to be paid in USD in 20 equal quarterly instalments[48]. It was acknowledged for "US federal income tax purposes" that payments made pursuant to the IPPA 2005 represented "compensation being paid in consideration of the services to be rendered" by Mr Blank[49].

42 The SA 2005 replaced the SA 1994[50]. The SA 2005 and the IPPA 2005 were "stapled" in that the IPPA 2005 was only effective if Mr Blank had executed the SA 2005 and purchased shares in GH equal to the number of PPU allocated to him under the IPPA 2005[51]. The shares in GH were to be purchased at their par value of CHF 50[52]. The SA 2005 stated that the "purpose of GH is neither the generation of profits nor the distribution of dividends to Shareholders"[53]. Generally, no dividends were payable on the shares in GH[54]. The shares in GH were not transferable and could not be encumbered without the prior written consent of GH[55]. The SA 2005 granted cross put and call options for the sale and purchase at par value of the shares in GH on, amongst other events, termination of the shareholder's employment with the relevant Glencore

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46 cl A.5 and Annex C of the IPPA 2005.

47 Item 4 of the definitions in the IPPA 2005.

48 cll A.6 and A.7 of the IPPA 2005.

49 cl A.9.2 of the IPPA 2005.

50 cl E.5 of the SA 2005.

51 cl B.1 of the IPPA 2005.

52 cl A.2 of the SA 2005.

53 cl C.1.3.2 of the SA 2005.

54 cl C.2.3.1 of the SA 2005.

55 cl D.3 of the SA 2005.

entity, redemption of the shareholder's interest in the IPPA 2005 or termination of the SA 2005 or the IPPA 2005[56].

43 As with the SA 1994, GH undertook in the SA 2005 to provide that GI would meet its obligations under the profit participation plans concluded with shareholders of GH[57].

Termination of employment and the Declaration

44 On 31 December 2006, Mr Blank's employment with Glencore Australia terminated.

45 On 15 March 2007, Mr Blank executed a Declaration. Clause B provided that Mr Blank, in consideration of USD 160,033,328.25 and CHF 80,000 to be paid by GH:

> "(a) relinquishe[d] his claim to payments with respect to the PPU and GS *allocated* in his name together with all preferential and ancillary rights to GI;
>
> (b) assign[ed] all GS, registered and/or held in his name together with all preferential and ancillary rights to GI, and irrevocably authorize[d] GI to take over the respective certificates;
>
> (c) assign[ed] all his shares of GH, registered and/or held in his name together with all preferential and ancillary rights to GH, and irrevocably authorize[d] GH to take over the respective certificates." (emphasis added)

46 The Declaration mistakenly deleted elements of the pro-forma declaration contained in the IPPA 2005 and made it appear that the Amount was to be paid by GH when the Amount was in fact to be paid by GI[58]. Neither party suggested that this error was significant.

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56 cll D.4.1 and D.4.2 of the SA 2005.

57 cl C.2.3.1 of the SA 2005.

58 *Blank v Federal Commissioner of Taxation* (2014) 95 ATR 1 at 19 [39]; see also at 17-18 [36].

Decisions below

47 The primary judge (Edmonds J) held that the Amount was ordinary income because it was deferred compensation for services rendered by Mr Blank, as recorded in the IPPA 2005. His Honour rejected Mr Blank's contention that the allocation of the GS and the PPU were the reward for services and that the Amount was simply the realisation of the rights attached to the GS and the PPU[59].

48 The primary judge also rejected the Commissioner's contentions that, even if the GS could be characterised as assets of Mr Blank (in the form of contractual rights), they were revenue assets and the gain on realisation of them was ordinary income under the second limb of *Myer Emporium*, and that the Amount was an ETP[60]. In separate reasons, the primary judge relevantly held that, in relation to the timing question, the first two instalments of the Amount were not derived in the 2007 income year[61].

49 On appeal to the Full Court of the Federal Court, Kenny and Robertson JJ held that the Amount was assessable as ordinary income. Their Honours rejected the contention that the rights under the profit participation plans, or the PPU, were themselves a benefit provided in consideration of services to be provided by Mr Blank[62].

50 Pagone J, in dissent, held that the combined effect of the IPPA 2005 and the SA 2005 was to confer on Mr Blank "an entitlement like that of a shareholder"[63] in the form of an entitlement to GI's profits and that the Amount

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59 *Blank v Federal Commissioner of Taxation* (2014) 95 ATR 1 at 31-32 [94]-[97].

60 *Blank v Federal Commissioner of Taxation* (2014) 95 ATR 1 at 31 [93], 34 [105].

61 *Blank v Federal Commissioner of Taxation (No 2)* (2014) 98 ATR 379 at 388 [44]-[45].

62 *Blank v Commissioner of Taxation* (2015) 329 ALR 213 at 235-236 [84]-[85], 237 [92].

63 *Blank v Commissioner of Taxation* (2015) 329 ALR 213 at 252 [130].

was therefore the realisation of those "entitlements" and a gain of a capital nature rather than ordinary income[64].

51 The Full Court unanimously agreed with the primary judge on the timing question[65].

Applicable law

52 The arrangements in issue in this appeal, including Art 657 of the Swiss Code of Obligations and the Articles of GI and Glencore AG, have their foundation in Swiss law. Each profit participation plan was governed by, and to be construed and interpreted in accordance with, the substantive laws of Switzerland[66]. The parties conducted the matter below and in this Court on the agreed basis that the proper construction of those arrangements was to be determined according to Australian law[67].

Issues on appeal

53 The primary issue on appeal was the proper characterisation of the receipt of the Amount in Mr Blank's hands – was the Amount ordinary income as a reward for services or, as Mr Blank contended, the proceeds of the exploitation of interconnected rights that conferred on him a right to receive, in the future, a proportion of the profit of GI and therefore assessable as a capital gain?

54 If the Amount was ordinary income then, aside from the question of the Commissioner being granted special leave to cross-appeal on the timing question, the Commissioner's alternative contentions – the applicability of *Myer Emporium*, whether the Amount was an ETP and, if the Amount was in the nature of a capital gain, how the cost base of the "rights" was to be determined – do not arise for determination.

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64 *Blank v Commissioner of Taxation* (2015) 329 ALR 213 at 258 [138], 260 [142].

65 *Blank v Commissioner of Taxation* (2015) 329 ALR 213 at 238 [96], 263 [146].

66 See cl C.6 of the PPA 1993; cl C.8 of the PPA 1999; cl C.11 of the IPPA 2005.

67 See *Neilson v Overseas Projects Corporation of Victoria Ltd* (2005) 223 CLR 331 at 343 [16], 370 [116], 372 [125], 411 [249]; [2005] HCA 54.

55 The question of characterisation of the receipt of the Amount is the issue addressed in the next section.

Amount income according to ordinary concepts

Principles

56 Section 6-5(1) of the 1997 Act provides that a person's "***assessable income*** includes income according to ordinary concepts, which is called ***ordinary income***" (emphasis in original). "Some things are so obviously income that their nature is unchallengeable"[68]. One is the reward for services rendered in the form of remuneration or compensation. The characterisation of the reward for services rendered as income is not lost because the reward is paid in a lump sum, because the payment is deferred or because it is payable upon the occurrence of a particular event. An amount paid as a lump sum because a person has retired from an office or employment, or has had their office or employment terminated, is income of that office or employment if it is deferred remuneration[69]. That proposition was "well established" by 1975[70]; its correctness is not in dispute.

57 The question in this case is one of characterisation. The question is "whether the amount received in a lump sum was part of the consideration for the services rendered in the office or employment"[71]. If the answer is "yes", it is income according to ordinary concepts even though payment is deferred.

58 In this matter, the answer to that question focuses attention on the IPPA 2005.

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68 Hannan, *Principles of Income Taxation*, (1946) at 8.

69 *Reseck v Federal Commissioner of Taxation* (1975) 133 CLR 45 at 56; [1975] HCA 38 citing *Henry v Foster* (1931) 16 TC 605 and *Dewhurst v Hunter* (1932) 16 TC 637; see also at 51.

70 *Reseck* (1975) 133 CLR 45 at 56.

71 *Reseck* (1975) 133 CLR 45 at 56.

The IPPA 2005

59 The terms of the IPPA 2005 expressly stated that the Amount was deferred compensation from Mr Blank's employment with Glencore Australia. The IPPA 2005 recorded that the "Plan" means a plan of "deferred compensation" to be known as the "Incentive Profit Participation Plan" for selected employees of the Glencore Group[72]. The IPPA 2005 described the IPP as "deferred compensation"[73]. Participation in the Plan of "deferred compensation" was "in consideration of the services to be rendered" by Mr Blank to Glencore Australia[74]. Mr Blank was described as the "Employee". The Amount was paid under the IPPA 2005 when Mr Blank's employment with Glencore Australia ceased[75]. The Amount was paid as a lump sum as an additional reward to Mr Blank for the services he had performed for the Glencore Group[76].

60 Not only was the Amount paid as deferred compensation under the IPPA 2005 when Mr Blank's employment with Glencore Australia ceased, but the right to *claim* the Amount as deferred compensation did not arise until Mr Blank's employment with Glencore Australia ceased. That last statement requires explanation. In the IPPA 2005, the parties acknowledged that the GS were issued by Glencore AG to GI pursuant to Art 657 of the Swiss Code of Obligations and were issued solely for the purposes of implementing the profit participation plans and to serve as PPU to calculate the amount of deferred compensation[77].

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72 pars 4 and 5 of the Preamble, Items 10 and 16 of the definitions, cll A.1.1 and A.1.2 of the IPPA 2005.

73 Item 10 of the definitions in the IPPA 2005.

74 pars 4 and 5 of the Preamble to the IPPA 2005.

75 cl A.5 of the IPPA 2005 read with Items 4 and 13 of the definitions in the IPPA 2005.

76 See *Mutual Acceptance Co Ltd v Federal Commissioner of Taxation* (1944) 69 CLR 389 at 403; [1944] HCA 34.

77 cll A.1.1 and A.1.2 of the IPPA 2005.

61 The IPPA 2005 also recorded that Mr Blank had no interest whatsoever in the GS and did not acquire any right in or title to any assets, funds or property of GI, Glencore AG or any other subsidiary[78]. That provision reflected, and was in accordance with, Art 657 of the Swiss Code of Obligations and the Articles of both GI and Glencore AG, which provided that a GS granted no more than a *claim* to a cumulative portion of the balance sheet profit, and that the *claim* was granted not upon the issue or allocation of the GS to the employee but *upon restitution* of the GS at the time the employment ceased. And then, any such claim was only in respect of those GS issued more than 24 months before employment ceased. Moreover, GI's and Glencore AG's Articles further provided that the holders of GS have no voting rights, no right to call a general meeting of shareholders, no right to attend a shareholders' meeting, no right to information, no right of inspection and no right to move motions[79].

62 Next, the terms and structure of the SA 2005 and the IPPA 2005 considered together disclose an intention that the profit of GI and the Glencore Group more generally should be distributed as deferred compensation to employees in that capacity and not as a return on the shares in GH. For example, under the SA 2005, the purpose of GH was expressly stated to be "neither the generation of profits nor the distribution of dividends to Shareholders" and shares in GH generally paid no dividends and were purchased and sold only at par value[80]. The fact that Mr Blank's entitlement was to be calculated by reference to the profits or "economic success" of GI does not indicate that such an entitlement was "like that of a shareholder"[81]. What the IPPA 2005 conferred on Mr Blank was an executory and conditional promise to pay an amount calculated *by reference to* those profits. The fact that GH had agreed in the SA 2005 to procure GI to meet that obligation[82] does not affect the character of the promise conferred on Mr Blank. Any analogy with the rights of a shareholder is neither necessary nor appropriate.

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78 cl A.1.2 of the IPPA 2005.

79 See Art 8.3 of GI's Articles; Art III of Glencore AG's Articles.

80 cll C.1.3.2, C.2.3.1, D.3, D.4 of the SA 2005.

81 cf *Blank v Commissioner of Taxation* (2015) 329 ALR 213 at 252 [130].

82 cl 2.3.1 of the SA 2005.

63 As the majority of the Full Court correctly concluded, what the IPPA 2005 conferred on Mr Blank was an executory and conditional promise to pay an amount at a future date determined by reference to the PPU allocated to Mr Blank. The fact that the Amount was paid after the termination of the contract of service, by a person other than the employer (here, GI) and separately to ordinary wages, salary or bonuses, does not detract from its characterisation as income if the payment is, as here, a recognised incident of the employment[83].

"Rights" not analogous to options

64 Mr Blank contended that his "associated rights" under the IPPA 2005 and the SA 2005 – including the GS and the PPU – were analogous to options and were assets of a proprietary nature[84]. That contention should be rejected. It is contrary to the terms of the IPPA 2005. The IPPA 2005 expressly stated that the PPU were issued *solely* for the purpose of calculating the IPP and conferred no interest of any kind on Mr Blank. The right to a payment calculated using the PPU crystallised *only* on termination of Mr Blank's employment. The Amount was not the proceeds of the exploitation of any anterior set of rights but was the performance of the promise to pay money made in the IPPA 2005 on satisfaction of the conditions on which that performance depended. Any "rights" Mr Blank had were "merely executory" and were neither vested nor accrued[85].

65 The fact that the IPPA 2005 and the SA 2005 were "stapled" does not detract from that characterisation. Contrary to the contention of Mr Blank, the rights created by the IPPA 2005 are not mere "associated rights" of the shares in GH, held by Mr Blank in his capacity as shareholder of GH. That contention is contrary to the express terms and purpose of the IPPA 2005.

66 Mr Blank's right to payment after the termination of his employment stands in stark contrast with the rights attached to the options considered in

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83 *Federal Commissioner of Taxation v Dixon* (1952) 86 CLR 540 at 556; [1952] HCA 65.

84 cf *Abbott v Philbin* [1961] AC 352; *Donaldson v Commissioner of Taxation (Cth)* [1974] 1 NSWLR 627; *Federal Commissioner of Taxation v McArdle* (1988) 19 ATR 1901; *Federal Commissioner of Taxation v McNeil* (2007) 229 CLR 656; [2007] HCA 5.

85 cf *McNeil* (2007) 229 CLR 656 at 665 [27].

Abbott v Philbin[86]. In that case, an employee (the company secretary) was granted an option to purchase shares in the company with the exercise price set when the option was granted. The options were non-transferable and were to expire on the earliest of 10 years from grant, the employee's retirement or his death. The grant of the option itself was held to be the relevant reward for service. The employee's gain – being the difference in value between the market price and the exercise price – was not assessable as ordinary income. In stark contrast with Mr Blank's "rights", immediately upon the grant of the option, the employee's rights in *Abbott* were unconditional, they could be exercised at any time in that year of income without any further act of the grantor, and their value could readily be ascertained by comparing the share price from time to time with the exercise price[87].

67 The non-proprietary nature of the "associated rights" is further evidenced by the fact that under the IPPA 2005, GS and the earlier iterations of GS that had been issued under earlier profit participation agreements would "serve as the PPU"[88] under the IPPA 2005. The Amount, to which Mr Blank became entitled on termination, was an amount calculated by reference to all of the PPU recognised by the IPPA 2005, including the 100 that were never issued as GS[89]. As a result, the Amount was the amount to which Mr Blank was contractually entitled under the IPPA 2005, being an amount calculated by reference to all 1,600 of the PPU identified in the IPPA 2005, regardless of whether they were previously issued as GS. The Amount was not and could not be characterised as the proceeds of disposal of GS, or any other "bundles of rights".

68 Accordingly, for Mr Blank, a receipts-based taxpayer, there was no derivation of any income as a result of the "rights" granted under the IPPA 2005 or any of the earlier agreements[90]. The receipt of the Amount by Mr Blank, as a receipts-based taxpayer, was income according to ordinary concepts on receipt and part of Mr Blank's assessable income. There was no earlier point when it

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86 [1961] AC 352.

87 See *Abbott* [1961] AC 352 at 371.

88 cl A.3.1 of the IPPA 2005.

89 See [29] and [31] above.

90 cf Parsons, *Income Taxation in Australia*, (1985) at 28-29 [2.15]-[2.16]; *Tagget v Federal Commissioner of Taxation* (2010) 188 FCR 128 at 138 [31].

could be said that Mr Blank had actual or constructive receipt of the Amount, or any part of it[91].

"Associated rights" could not be turned to pecuniary account

69 The conclusion that there was no derivation of any income by Mr Blank as a result of the "associated rights" is fortified by the fact that none of these so-called "associated rights" could be turned to pecuniary account. Unlike the options in *Abbott*[92], which could have been exercised at any time and the purchased shares immediately sold, the "associated rights" in issue in this appeal were (subject to one exception) unable to be dealt with by Mr Blank until the Notice Date. The rights and claims and GS issued under the various versions of the profit participation plans could not be transferred or alienated or subject to any grant of an interest[93]. The exception was that Mr Blank was able, under each profit participation plan (other than the PPA 1993), to seek an assignment to a personal holding company, trust or foundation that he controlled provided that GI consented. That ability to seek an assignment did not bring home the value of the "associated rights" to Mr Blank prior to the Notice Date. As the majority of the Full Court properly concluded, if and to the extent that occurred, it would involve no more than Mr Blank assigning his claims to payment under the IPPA 2005 to an entity that was already under his complete control[94].

GS and PPU not otherwise assessable

70 Next, it is necessary to address Mr Blank's contention that the GS and PPU were assessable either as ordinary income or under s 26(e) of the 1936 Act (or s 15-2 of the 1997 Act) and that Mr Blank was therefore at risk of double taxation. That contention should be rejected.

71 The contention ignores that the proper characterisation of Mr Blank's rights under the IPPA 2005 was an executory and conditional promise to pay money. Second, it is contrary to the terms and purpose of s 26(e) of the 1936 Act and would lead to absurd results. The purpose of s 26(e) was to ensure that

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91 *Tagget* (2010) 188 FCR 128 at 138-139 [31]-[33].

92 [1961] AC 352 at 366, 371-372, 377-379.

93 cl C.2 of the PPA 1993; cl C.2 of the IPPA 2003; cl C.2 of the IPPA 2005.

94 *Blank v Commissioner of Taxation* (2015) 329 ALR 213 at 237 [89].

receipts and advantages which are in truth rewards for a taxpayer's employment or services are treated as assessable income even if they are not paid fully in money, but by way of allowances or advantages that have a money value for the taxpayer[95]. That is not the position under the IPPA 2005.

72 Moreover, if Mr Blank's contention was correct and the value of executory and conditional promises to pay money in respect of, or for, or in relation directly or indirectly to, employment or services rendered were assessable under s 26(e) of the 1936 Act, every employee would be rendered an accruals-based taxpayer taxable on their wages and salary before they received it. Such a conclusion cannot be, and is not, correct.

Declaration

73 Finally, it is necessary to address the Declaration. As the primary judge observed[96], the consideration of CHF 80,000 referred to in cl B of the Declaration was the price for Mr Blank's 1,600 shares paid by GH at a par value of CHF 50 per share, which were then assigned under par (c) of cl B of the Declaration. The consideration of the Amount referred to in cl B was paid by GI in satisfaction of the rights under the IPPA 2005 as determined by the PPU allocated to Mr Blank and was referable to pars (a) and (b) in cl B. The amounts in cl B cannot be regarded as constituting a global consideration for the sale of shares and the satisfaction of the rights under the IPPA 2005. That construction is contrary to the express terms of the Declaration and the express terms of the IPPA 2005, which is referred to in the Declaration. Paragraphs (a) and (b) in cl B of the Declaration record that the Amount was accepted on receipt in full satisfaction of the rights under the IPPA 2005 and not as attempting to confer on the GS and PPU a proprietary character they did not otherwise possess.

Conclusion

74 For those reasons, the appeal should be dismissed. The Amount was ordinary income of Mr Blank. It was deferred compensation for services Mr Blank rendered as an employee and therefore, on receipt, formed part of his assessable income pursuant to s 6-5 of the 1997 Act.

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95 *Scott v Federal Commissioner of Taxation* (1966) 117 CLR 514 at 525-526; [1966] HCA 48.

96 *Blank v Federal Commissioner of Taxation* (2014) 95 ATR 1 at 19 [39].

Other appeal grounds, cross-appeal and notice of contention

75 It is unnecessary to consider the other appeal grounds or the notice of contention filed by the Commissioner as the conclusion reached above means the issues raised by those grounds and contentions do not arise.

76 It is, however, necessary to consider ground 2(b) of the Commissioner's application for special leave to cross-appeal, which deals with the timing question. The balance of the application for special leave to cross-appeal does not arise and should be dismissed with costs.

Timing question

77 The Commissioner sought special leave to cross-appeal against the primary judge's and the Full Court's rejection of his contention that two instalments of the Amount due in the 2007 income year had been derived by Mr Blank in that year because they had been "applied or dealt with" on his behalf or as he directed, within the meaning of s 6-5(4) of the 1997 Act. That application should be dismissed with costs.

78 Section 6-5(4) of the 1997 Act provides that "[i]n working out whether you have ***derived*** an amount of *ordinary income, and (if so) when you ***derived*** it, you are taken to have received the amount as soon as it is applied or dealt with in any way on your behalf or as you direct" (emphasis in original).

79 The object of s 6-5(4) is to prevent a taxpayer escaping the imposition of tax where, although income has not actually been paid to him or her, his or her resources have actually been increased "by the accrual of the income and its transformation into some form of capital wealth or its utilization for some purpose"[97].

80 As we have seen, Mr Blank was a receipts-based taxpayer. Under the IPPA 2005, GI was obliged to pay Mr Blank the Amount in 20 equal instalments, payable at the end of each quarter, with the first payment due in January 2007.

81 The issue of derivation under s 6-5(4) arose because, although under the express provisions of the IPPA 2005 two instalments of the Amount were

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97 *Brent v Federal Commissioner of Taxation* (1971) 125 CLR 418 at 430; [1971] HCA 48 quoting *Permanent Trustee Company of New South Wales Ltd v Federal Commissioner of Taxation* (1940) 2 AITR 109 at 110-111.

payable to Mr Blank in the 2007 income year, Mr Blank did not receive those instalments in that income year. Therefore, the two instalments (or a part of them) could only have been *derived* by him in the 2007 income year by reason of s 6-5(4).

82 The primary judge made a finding, upheld on appeal, that the agreement to vary the payment terms, so that the first two instalments of the Amount were not paid in the 2007 income year, was not entered into until 24 January 2008[98]. That finding referred to a letter sent to Mr Blank dated 24 January 2008, which enclosed a copy of an agreement between GI and Mr Blank ("the January 2008 Agreement"). That agreement recorded that although under the IPPA 2005 GI had agreed to pay the Amount in 20 quarterly instalments with the first instalment payable on 31 January 2007, GI and Mr Blank had reached agreement to alter the payment terms. Under the altered payment terms, the first instalment of USD 32,006,565.65 would be due on 31 December 2007 and GI would withhold from that amount USD 30,806,415.70 and pay that amount to the Swiss FTA. In short, whereas under the IPPA 2005 GI was to withhold part of each instalment for withholding tax, the January 2008 Agreement recorded an agreement with the Swiss FTA to settle the whole withholding tax bill in advance[99]. That was an alteration to the terms of the IPPA 2005.

83 On appeal to this Court, the Commissioner submitted that that agreement was reached not in January 2008 but prior to 17 March 2007 and that therefore, during the 2007 income year, at least the instalments due in that year had been "applied or dealt with" on Mr Blank's behalf or as he directed within the meaning of s 6-5(4) of the 1997 Act. That contention was based on the fact that Mr Blank had provided affidavit evidence that on or about 17 March 2007 he was provided with a letter by GI, which summarised his entitlements under the IPPA 2005. That document recorded, in summary form, the payment arrangements included in the January 2008 Agreement. Neither the primary judge nor the Full Court found as a fact that the GI letter received by Mr Blank on or about 17 March 2007 reflected an oral agreement made in the 2007 year of income to the same effect as the January 2008 Agreement. Such a finding would have been inconsistent with Mr Blank's evidence that it was the January 2008 Agreement

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98 *Blank v Federal Commissioner of Taxation (No 2)* (2014) 98 ATR 379 at 388 [44]-[45]; *Blank v Commissioner of Taxation* (2015) 329 ALR 213 at 238 [95].

99 cl 2 of the January 2008 Agreement.

which established his instructions to GI as to how the first two instalments were to be applied, evidence in relation to which he was not cross-examined.

84 It was a question of fact when the agreement addressing the altered payment arrangements was entered into. The finding that the agreement was not made until January 2008 was a factual finding made by the primary judge and upheld on appeal. No question of principle of general application is raised by the Commissioner's application for special leave to cross-appeal. The application for special leave to cross-appeal on ground 2(b) should be dismissed with costs.

Conclusion and orders

85 The appeal should be dismissed with costs. The Commissioner's application for special leave to cross-appeal should be dismissed with costs.