Administrative Appeals Tribunal

DECISION AND REASONS FOR DECISION

Arnold and Commissioner of Taxation (Taxation) [2017] AATA 1318

Division: TAXATION & COMMERCIAL DIVISION

File Number(s): **2012/4203; 2013/0273; 2014/4923; 2015/4019**

Re: **Stephanie Arnold**

APPLICANT

And **Commissioner of Taxation**

RESPONDENT

DECISION

Tribunal: **The Hon. Justice Perram, Deputy President**

Date: **18 August 2017**

Place: **Sydney**

The decisions under review are affirmed in part.

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

The Hon. Justice Perram, Deputy President

CATCHWORDS

TAXATION AND REVENUE – appeal from objection decisions of Commissioner – deductions – charitable donations to deductible gift recipients – HIV/AIDS medicines supplied to charities located in Africa – consideration of market value of goods – consideration of amount paid for goods – construction of 'paid' in s 30-15 of Income Tax Assessment Act 1997 (Cth) – whether title to goods transferred to charities within relevant income years – whether supply agreements void for illegality – whether objection decisions upheld – whether administrative shortfall penalties upheld

LEGISLATION

Evidence Act 1995 (Cth)

Income Tax Assessment Act 1936 (Cth) s 78A, Part IVA

Income Tax Assessment Act 1997 (Cth) ss 8-1, 30-15, 30-15(1), 30-212

Taxation Administration Act 1953 (Cth) sch 1, ss 284-75, 284-75(1), 284-75(5), 284-75(6), 284-75(6)(b), 284-90, 284-220

Sale of Goods Act 1923 (NSW) ss 5, 21, 23, 25A, 25A(1), 78A

Surveillance Devices Act 2007 (NSW) s 7(1)

CASES

Air New Zealand Ltd v Australian Competition and Consumer Commission [2017] HCA 21; (2017) 91 ALJR 648

Commissioner of Taxation v Arnold (No.2) [2015] FCA 34; (2015) 324 ALR 59

DW v The Queen [2014] NSWCCA 28; (2014) 239 A Crim R 192

Federal Commissioner of Taxation v James Flood Pty Ltd [1953] HCA 65; (1953) 88 CLR 492

Goben Pty Ltd v Chief Executive Officer of Customs (1997) 74 FCR 36

In the matter of Renovation Boys Pty Ltd (admins apptd) [2014] NSWSC 340

Neilson v Overseas Projects Corporation of Victoria Ltd [2005] FCA 65; (2005) 223 CLR 331

Re Tooth & Co Ltd (1979) 39 FLR 1

SECONDARY MATERIALS

Norman Palmer, *Palmer on Bailment (Sweet & Maxwell, 3rd Ed, 2009)*

REASONS FOR DECISION

The Hon. Justice Perram, Deputy President

18 August 2017

1. INTRODUCTION

1. Mrs Stephanie Arnold claimed as a deduction in the financial year ending 30 June 2010 the sum of $40,000, and in the financial year ending 30 June 2011, the sum of $560,000. Where currency is referred to in these reasons, unless stated otherwise, the default currency is AUD. Both deductions were rejected, a conclusion upheld on objection. The Commissioner also imposed administrative penalties in relation to the shortfall resulting from the disallowances which were also subject to unsuccessful objections. Mrs Arnold now applies to the Tribunal to review these decisions. With the exception of one of the penalty decisions, each should be affirmed. It is convenient to deal with the $40,000 deduction first.

2. THE $40,000 DEDUCTION CLAIMED IN FINANCIAL YEAR ENDING 30 JUNE 2010

2. On its face, Mrs Arnold's case is straightforward. She says that on 30 June 2010 she purchased HIV medicines for $40,000 and donated them in kind to a charity operating in Kenya called African Enterprise ('the Charity') which, there is no dispute, was a developing country relief fund to which item 1 of the table in s 30-15 of the *Income Tax Assessment Act 1997* (Cth) ('the ITAA 1997') applied. Subsection 30-15(1) provides that a gift or contribution to such a recipient is deductible in the manner indicated in the table.

3. Under item 1 of that table, Mrs Arnold was entitled to claim as a deduction:

> *(a) if the gift is money – the amount you are giving; or*
>
> *(b) if the gift is property… – the lesser of the market value of the property on the day you made the gift and the amount you paid for the property;*

4. Mrs Arnold submits that she paid $40,000 for the medicines (i.e. the second part of sub-clause (b)) and that this was also their market value (i.e. the first part of sub-clause (b)). Hence, she argues that she was entitled to deduct $40,000.

5. Because Mrs Arnold submits that she donated the medicines to the Charity on 30 June 2010 she needs to demonstrate that:

   (a) she owned the medicines on 30 June 2010;

   (b) on the same day she donated them to the Charity;

   (c) the amount she paid for the medicines was $40,000; and

   (d) the medicine's market value was $40,000.

6. For the reasons which I will shortly give, I do not accept that she had acquired the medicines by 30 June 2010 and hence I am unable to accept that she was able to donate them to the Charity on that day: *nemo dat quod non habet*. In any event, even if she did donate the medicines on that day, what she paid for them was $3,000 not $40,000, and their market value was USD$665.20 not $40,000. Even if she had made a gift of property on 30 June 2010 (which she did not) subclause (b) of item 1 of the table would entitle her to claim only the lesser of those two amounts, i.e., USD$665.20. There are three aspects to this reasoning and it is best to deal with them separately: ownership, purchase price and market value.

(a) Ownership

7. Mrs Arnold claims to have purchased the medicines from an entity called MedAid Pty Ltd ('MedAid') on 30 June 2010. During the financial year ending 30 June 2010, the evidence shows that MedAid acquired in the United Kingdom several tonnes of medicines used in the treatment of HIV and AIDS. These medicines appear to have been manufactured in Hyderabad in India and then exported to the United Kingdom by sea and air via a series of intermediaries operating from Belize. One of these entities was called Solstar Ltd ('Solstar'). There were contractual relations between Solstar and MedAid which provided for title to the medicines to be transferred from Solstar to MedAid upon their delivery at MedAid's nominated warehouse or earlier if agreed in writing. The evidence before the Tribunal throws little light on the title issues as between the various Belizean entities, the

Indian manufacturer and Solstar. However, the Commissioner made no point about this and I propose to assume that Solstar acquired title to the medicines prior to their delivery to the United Kingdom.

8. In the United Kingdom, MedAid retained a firm called Southern Cross Freight Logistics Ltd ("Southern Cross') to receive the medicines and to manage them on its behalf. Southern Cross was named as the consignee in the bill of lading and a number of air waybills under which the medicines were exported from India to the United Kingdom. It is inevitable therefore that the carriers dealt with the medicines in the United Kingdom in accordance with Southern Cross' direction since it was the consignee. The relevant person at Southern Cross was a Mr Knibbs.

9. Upon the arrival of the medicines in the United Kingdom they were not entered for home consumption. They were therefore required to be held 'underbond' at a bonded warehouse. By a mechanism not disclosed in the evidence – but most likely by an instruction from Mr Knibbs to each carrier – they were transported to a bonded warehouse operated by Medway Bond and Storage Co. Ltd ('Medway') in Rochester, Kent.

10. As the bill of lading and air waybills show, each consignment was made up of pallets which contained boxes. The packing lists completed by the Indian manufacturer (as consignor) and provided with each of the bills, in turn, show that each box contained packets which, in turn, contained tablets. I accept that upon delivery to Medway's bonded warehouse, all of these pallets, boxes and tablets became MedAid's property. This is because title was to pass from Solstar to MedAid on delivery and because Southern Cross, as consignee under the bills, was MedAid's agent for that purpose. It should also be observed that all three of the consignments had been delivered to the warehouse prior to 30 June 2010 and within that financial year. The significance of this is that they were physically present in the bonded warehouse in the United Kingdom when Mrs Arnold says she purchased them on 30 June 2010.

11. Mrs Arnold's difficulty is to show that she acquired on 30 June 2010 what she says she purchased from MedAid. To this end, she relied upon a purchase agreement also dated 30 June 2010 which I am satisfied she entered into on that day. Under it she purported to purchase 200 'Treatment Kits'. According to the purchase agreement, each Treatment Kit ('Kit') was made up of 7 doses or sets of tablets as follows:

(a) a 3-in-1 AIDS anti-retro-viral cocktail made up of 2 pills, each containing a mixture of Lamivudine, Zidovudine and Nevirapine;

(b) a single tablet of Ciprofloxacin (a powerful anti-bacterial); and

(c) seven tablets of Fluconazole (an antifungal).

12. Each Kit consisted of seven sets of these doses (i.e. 70 tablets). It was 200 of these Kits that Mrs Arnold purported to purchase from MedAid. Under the agreement between them, title was to pass to Mrs Arnold within 150 days of payment on a date to be determined by the Vendor (cl 4.1). There is some controversy in this case about what Mrs Arnold paid, but there is no dispute that she paid at least some of the purchase price on 30 June 2010. In Mrs Arnold's case, MedAid determined on 30 June 2010 that title would pass to her on that day. The mechanism by which the transfer appears to have occurred was by a direction from MedAid to Southern Cross now to hold the medicines for Mrs Arnold. On the assumption that Southern Cross was holding the medicines as MedAid's bailee, Southern Cross was expressly directed now to hold them for Mrs Arnold. Southern Cross had authority to hold the medicines for Mrs Arnold because it was MedAid's agent and, in turn, MedAid held a limited power of attorney from Mrs Arnold specifically in order to give effect to the transfer. The letter which purported to achieve this was a delivery direction from MedAid to Southern Cross dated 30 June 2010 which was in the following terms:

> *Please be advised that the sale of the following pharmaceuticals warehoused by Southern Cross Freight Logistics has transpired:*
>
> *Sale from MedAid to purchasers as attached*

Number of Pills	*Rx*	*Quantity of Bottles/Packs*	*Quantity in Boxes/Cartons*	*Batch*
2,160	*ARV*	*35.83*	*0.6*	*3033*
296, 260	*ARV*	*4,937.7*	*82.3*	*50001*
19,850	*Cipro*	*198.5*	*0.92*	*41023*
22,780	*Cipro*	*227.8*	*1.06*	*50003*
7,750	*Flu*	*77.5*	*0.775*	*30052*

290,660	*Flu*	*2,906.6*	*29.066*	*50002*

Please deliver these units as described to the possession of the purchasers, as attached. We require immediate verification of such delivery. Please sign below acknowledging such delivery. Thank you.

(The 'purchasers as attached' referred to in the heading to the table included Mrs Arnold).

13. There is at least one potential difficulty with this. What Mrs Arnold was acquiring was *Kits* of 70 tablets of three different kinds of medicines. Kits of that kind were not what had been delivered to the bonded warehouse from Hyderabad. In fact, as might be expected each of the three different kinds of medicine had been delivered in bulk. The evidentiary record is not entirely complete but, for example, what was shipped by Maersk Line from Hyderabad under the bill of lading dated 21 September 2009 was 2,612 kgs of the antiviral cocktail contained in 45 separate boxes. What was shipped by air on or around 22 December 2009 was 1,867 kgs of Fluconazole in 271 separate boxes.

14. Although it is clear that all three kinds of medicine had arrived in considerable quantities at the bonded warehouse in Kent before 30 June 2010 when Mrs Arnold purported to buy her 200 Kits, it is also known that none of these boxes had been opened and that no Kits of the kind purportedly bought by Mrs Arnold had then been assembled from their contents. This degree of certainty about the state of some boxes on 30 June 2010 in a warehouse in Kent may appear surprising. However, Mr Arnold (who happens not only to be Mrs Arnold's husband but who also appeared on her behalf during the hearing) was the driving creative force behind this donation program and, at some time prior to 13 September 2010, he retained an English firm of accountants to go to the warehouse and there perform something of an audit. They reported back to him by letter of that date. So that the contents of this letter may make some sense, it is useful to know that Mr Arnold's endeavours were quite a bit more ambitious than Mrs Arnold's own individual donation might suggest, and that distribution of the medicines to two charities was contemplated on behalf of a large number of donors, all of whom were purchasing medicines on a similar basis to Mrs Arnold. The two charities were Australian Relief and Mercy Services and the Charity. With that background, the relevant portions of the letter are as follows:

Dear Sir,

Stock Verification 10 September 2010

We write to you further to your recent request for Reeves + Neylan LLP to attend the premises of Medway Bond & Storage Co. Ltd to physically count the quantities of stock donated by members of Donors without Borders to two particular Charities and stored at the warehouse.

Commentary

A representative of Reeves + Neylan LLP attended Medway Bond & Storage Co. Ltd (Rochester, Kent) on 10 September to verify the stock held on behalf of the following charities; African Enterprise and Australian Relief & Mercy Services. You provided us with a listing of the stock that is held by each of the charities.

The warehouse management had segregated the stock relating to the charities and we confirm that we counted the number of boxes held of each product as scheduled. The results of the count are scheduled at appendix 1.

Due to the rules relating to bonded warehouses, we were not able to verify the contents of the boxes, we did however confirm the box labels agreed to the stock listing and can confirm that it did not appear that any of the boxes had been opened or tampered with.

The labels did not confirm that the stock was in the ownership of each of the charities. However we have seen documentation provided by Southern Cross Logistics who manage the stock on your behalf confirming that the stock had been transferred to these charities by 30 June 2010. We attach at appendix 2 the documentation upon which we have relied in confirming the quantity and date of stock transfers.

Conclusion

We conclude that there is sufficient stock held in the warehouse to cover the amount of stock transferred to each of the charities. However as there was no identification on the boxes shown to us, we have relied upon the transfer documents in appendix 2 to provide evidence of the ownership of the stock.

15. There was then attached to the letter an inventory audit list which was in these terms:

Donors Without Borders

Inventory audit 10 September 2010

Australian Relief and Mercy Services (ARMS)

Inventory item	***Description***	***Doses***	***Box eq-uivalents***	***Actual boxes per DWB***	***Boxes counted R+N***	***Discrep-ancy***	***Comments***
3033	*ARV*	*12,250*	*3.40*	*4*	*4*	*0*	
40023	*Ciprofloxacin*	*1,750*	*0.08*	*0*	*0*	*0*	

30052	*Fluconazole*	*12,250*	*1.23*	*2*	*2*	*0*
50001	*ARV*	*2,800*	*0.78*	*1*	*1*	*0*
50003	*Ciprofloxacin*	*400*	*0.02*	*1*	*1*	*0*
50002	*Fluconazole*	*2,800*	*0.28*	*1*	*1*	*0*

African Enterprise

Inventory item	***Description***	***Doses***	***Box eq-uivalents***	***Actual boxes per DWB***	***Boxes counted R+N***	***Discrep-ancy***	***Comments***
3033	*ARV*	*2,150*	*0.60*	*1*	*1*	*0*	
40023	*Ciprofloxacin*	*19,850*	*0.92*	*1*	*1*	*0*	
30052	*Fluconazole*	*7,750*	*0.78*	*1*	*1*	*0*	
50001	*ARV*	*293,460*	*81.52*	*81*	*81*	*0*	*3 full pallets*
50003	*Ciprofloxacin*	*22,380*	*1.04*	*1*	*1*	*0*	
50002	*Fluconazole*	*287,860*	*28.79*	*29*	*29*	*0*	*24 in pallet, 5 loose*

Notes:

Where part boxes are owned by the charity, full boxes are held until the stock is removed from bond. Due to bonding requirements boxes cannot be opened.

Normally therefore box quantities counted are "rounded up" from the boxes owned by each charity. But the 0.08 boxes of 40023 held by ARMS is to be taken from the balance of the 40023 box held by AE.

16. The point of this otherwise unremarkable correspondence is twofold. First, it shows that the Kits purportedly purchased by Mrs Arnold on 30 June 2010 cannot have existed at that date because, even by September 2010, the boxes containing the individual medicines had not been opened and, indeed, could not be opened whilst they remained under bond. Secondly, quite apart from that, the medicines were being held in bulk

without any attempt to segregate them by reference to the various individual donors who had purportedly purchased from MedAid. To do so would have required the boxes to be opened which was not permitted. Those handling the boxes had instead sorted them by charity inside Medway's (not Southern Cross') warehouse.

17. This state of affairs would appear to be fatal to Mrs Arnold's deduction. It is very likely that what Mrs Arnold purported to buy on 30 June 2010 – namely, 200 Kits – simply did not exist as an item of property on that day at all.

18. The Commissioner, however, did not take this point and so I will not decide the case on the basis of it either. He did, however, pursue a closely related argument to the effect that what Mrs Arnold had entered into was a sale of unascertained goods. Such a sale is governed in New South Wales by s 21 of the *Sale of Goods Act 1923* (NSW) ('SGA'). It provides:

> ***21 Goods must be ascertained***
>
> *Subject to section 25A, where there is a contract for the sale of unascertained goods, no property in the goods is transferred to the buyer unless and until the goods are ascertained.*

19. This section either applies of its own force because the contract between Mrs Arnold and MedAid was expressly governed by the law of New South Wales or because, in the absence of evidence to the contrary, I should proceed on the basis that the law of the United Kingdom on this point is the same as that of New South Wales: *Neilson v Overseas Projects Corporation of Victoria Ltd* [2005] FCA 65; (2005) 223 CLR 331 at 343 [16], 372 [125], 396 [202], 411 [249] and 420 [275]. As the dissents in that case show, the application of that principle can at times occasion conceptual difficulties. This, however, is not one of those cases.

20. Returning then to s 21, in *In the matter of Renovation Boys Pty Ltd (admins apptd)* [2014] NSWSC 340, Black J was asked to consider whether bathroom and kitchen products held in stock were 'unascertained' in the requisite sense, where the purchase price for those goods had been paid in full by the retailer's customers but, within the warehouse, had not yet been allocated to them. Although in obiter his Honour was of the view that such items could be viewed as 'specific goods' within the meaning of s 5 of the SGA where staff had made a relevant notation on the purchase order as to the availability of stock, ultimately his Honour concluded at [14]:

I accept, that, in the most likely case that numerous items were available to fill the order at the time of its placement, the goods are properly characterised as "unascertained" for the purpose of this rule ***until the stock was allocated to the order*** *and, where items were not available to fill the order when it was placed, the items were "future" goods for the purposes of this rule.*

(emphasis added)

21. I too am satisfied that the goods here were, in the requisite sense, unascertained. Out of the large piles of boxes and pallets consisting of literally several tonnes of medicines, none were specifically identifiable as the ones Mrs Arnold was purchasing. Consequently, title to them could only pass when they became ascertained within the meaning of s 21. When was that? To aid in the resolution of that issue, s 23 of the SGA sets out a series of rules, one of which, Rule 5(1), explains when unascertained goods become ascertained. It provides:

> ***23 Rules for ascertaining intention***
>
> *Unless a different intention appears, the following are rules for ascertaining the intention of the parties as to the time at which the property in the goods is to pass to the buyer.*
>
> *…*
>
> *Rule 5. (1) Where there is a contract for the sale of unascertained or future goods by description, and goods of that description and in a deliverable state are unconditionally appropriated to the contract either by the seller with the assent of the buyer or by the buyer with the assent of the seller, the property in the goods thereupon passes to the buyer. Such assent may be express or implied, and may be given either before or after the appropriation is made.*

22. So there needs to be an act of appropriation. This would have required, at the very least, the putting aside for Mrs Arnold of 2,800 AVR cocktail tablets, 1,400 Ciprofloxacin tablets and 9,800 Fluconazole tablets. Furthermore, this segregation needed to occur on 30 June 2010 if Mrs Arnold was to acquire title on that day. Necessarily, this would have required the boxes to be opened and, as is quite clear from the accountant's letter of 13 September 2010, this could not have happened whilst they remained underbond and in fact had not happened even by the date of that letter.

23. Mrs Arnold sought to deflect the force of this argument by resort to s 25A. It is entitled 'Contracts of sale for goods forming part of bulk quantity' and specifies rules for dealing with sales of parts of bulks. Although the several tonnes of medicines may well have been a 'bulk', the section cannot apply in this case. Subsection (1) provides:

> *(1) This section applies to a contract of sale for a specified quantity of unascertained goods of which some or all form part of a single bulk quantity of goods of the same kind (the bulk) if:*
>
> *(a) the bulk is identified, either in the contract or by subsequent agreement between the parties, and*
>
> *(b) the buyer has paid for some or all of the goods that form part of the bulk.*
>
> (emphasis added)

24. It is necessary therefore, for the provision to be enlivened that Mrs Arnold's contract should have referred to the 'bulk' of which she was apparently buying part. But the purchase agreement did not refer to Mrs Arnold buying a portion of MedAid's several tonnes of medicines but instead merely to her acquisition of the 200 Kits so that subsection (1) is not satisfied and s 25A does not apply.

25. It follows that no title can have passed from MedAid to Mrs Arnold on 30 June 2010. Since she did not own the medicines on that day, she cannot have donated them to the Charity on that day either. The claim for a deduction fails because she did not make 'a gift of property' on that day within the meaning of item 1 of the table to s 30-15 of the ITAA 1997.

26. There are three footnotes to this conclusion. First, Mrs Arnold's case assumed that MedAid could transfer title from itself to Mrs Arnold by giving an instruction to Southern Cross. This would be effective only as an attornment by a bailee. The difficulty is that the medicines were not in Southern Cross' warehouse but were instead in Medway's bonded warehouse from which they could not lawfully be removed without paying the customs duties which would be due on their import into the United Kingdom: see *Goben Pty Ltd v Chief Executive Officer of Customs* (1997) 74 FCR 36 (FC). It seems to me that whilst the owner of the warehouse, Medway, was a bailee, it may be that Southern Cross was not, because it had no right to possession of the medicines whilst they had not been entered for home consumption. If there was no bailment, there may be difficulties in seeing how a direction to Southern Cross could have been effective as an attornment. On one view, for this to have been successful it arguably needed to be done by an instruction to the party with possession of the goods, here Medway: *Palmer on Bailment* (Sweet & Maxwell, 3rd Ed, 2009) at p 1375. Most likely this would have required a direction to Medway that it held the goods for the consignee on behalf of Mrs Arnold. There are difficult issues about

this, however, and the matter was not argued. In that circumstance, it is not necessary to express a concluded view about it.

27. Secondly, as Edmonds J explained in *Commissioner of Taxation v Arnold (No 2)* [2015] FCA 34; (2015) 324 ALR 59 (‘*Arnold (No 2)*’) at 88-89 [112]-[115], on identical facts involving Mr Arnold, it is very difficult to see that even if Mrs Arnold had owned the medicines on 30 June 2010 that they could have been transferred by attornment to the Charity. This is not only because of all of the difficulties that exist in transferring title from MedAid to Mrs Arnold, but also because Southern Cross appears to have had no authority from the Charity to hold the medicines for it.

28. Thirdly, for the reasons given by Edmonds J in *Arnold (No 2)* at 91-92 [127]-[131], a purchase agreement made in Australia for the sale in the United Kingdom of pharmaceuticals of the present kind is illegal and void.

29. In any event, it is not necessary to rely upon these matters. Section 21 of the SGA is sufficient by itself to justify the conclusion that there was no transfer of title to Mrs Arnold and hence no possible gift of the property.

30. If that conclusion were incorrect so that Mrs Arnold had made a gift of the medicines on 30 June 2010, I would have reached the conclusion that she was entitled only to claim a deduction of USD$665.20. In that regard, item 1 of the table to s 30-15 of the ITAA 1997 requires a comparison between, on the one hand, ‘the amount you paid for the property’ and, on the other, ‘the market value of the property’ followed by the determination of the lesser which is then to stand as the figure that can be claimed. It is necessary then to deal with these two concepts separately.

(b) Purchase Price

31. The amount Mrs Arnold ‘paid’ under the purchase agreement was only $3,000. It is important to note that the word used in s 30-15 is ‘paid’ and this stands in contrast to the different concept elsewhere found in the Act of *incurring* a liability, e.g., the provisions governing deductibility under s 8-1 where an incurred liability, although unpaid, is deductible: *Federal Commissioner of Taxation v James Flood Pty Ltd* [1953] HCA 65; (1953) 88 CLR 492 at 506 [17]:

> *The word "out-going" might suggest that there must be an actual disbursement. But partly because such an interpretation would produce very strange and anomalous results, and partly because of the use of the word "incurred", the provision has been interpreted to cover outgoings to which the taxpayer is definitively committed in the year of income although there has been no actual disbursement.*

32. What is required by the distinct use of the word 'paid' rather than 'incurred' is the payment of actual cash or the discharge of a pre-existing monetary obligation. As Edmonds J explained in *Arnold (No 2)* at 86 [104]:

> *The concept of payment in the legal sense means a gift or loan of money or any act offered and accepted in performance of a money obligation. Money must therefore feature in some way, either because payment is in physical money or because the obligation to be discharged by the act of payment is a money obligation, in which case the mode of discharge is immaterial to the status of the act as an act of payment: see, Goode R, Commercial Law (3rd ed, Lexis Nexus UK, 2004) at p 461.*

33. This directs attention to the terms of Mrs Arnold's agreement with MedAid. Its critical parts were summarised in the 'purchase details' section as follows:

> ***PURCHASE DETAILS***
>
> | | | |
> |---|---|---|
> | *(A)* | *Number of Donation Units purchased: 20 as per Schedule 1. Total purchase price:* | *$40,000.00 (A)* |
> | *(B)* | *Required down payment equal to 7.5% of the total purchase price (A), due upon signing:* | *$3,000.00 (B)* |
> | *(C)* | *Amount of credit with Vendor (A - B):* | *$37,000.00 (C)* |
> | *(D)* | *Prepaid interest equal to 0.108% p.a. of the amount of credit (C) , due upon signing:* | *$2,000.00 (D)* |
> | *(E)* | *Total amount of first payment to vendor (B + D):* | *$5.000.00 (E)* |
>
> *The balance of the purchase price (being the amount of credit) is payable no later than fifty years from the date the Vendor accepts this Purchase Agreement.*

34. The transaction could have been brought to fruition either as:

(a) a loan to Mrs Arnold of $37,000 followed by a payment by her to MedAid of $40,000 (consisting of the borrowed funds of $37,000 and her own $3,000 downpayment); or

(b) the payment by Mrs Arnold of the $3,000 downpayment with the balance of the unpaid purchase price $37,000 due 50 years later.

35. In both cases, the charging of interest would be coherent, what differs is that upon which any such interest is being charged. Under (a), it is interest on a loan which has been extended; under (b), it is interest on the debt constituted by the unpaid portion of the purchase price. Under (a), the entire purchase price obligation has been discharged but not under (b). Under (b) the only monetary obligation discharged was the $3,000 part payment of the purchase price. As Edmonds J observed in *Arnold (No.2)* at 87 [107], the present situation is an example of the fact that it is possible to have a debt without a loan.

36. The question then is for what did Mrs Arnold's agreement provide? It seems to me that the words 'the balance of the purchase price (being the amount of credit) is payable no later than 50 years from the date the Vendor accepts this Purchase Agreement' provide the answer. The agreement left most of the purchase price unpaid. That the agreement refers to the balance of the unpaid purchase price necessarily connotes that the balance had not been paid.

37. The amount actually paid by Mrs Arnold was therefore only $3,000.

(c) Market Value

38. But item 1 of the table in s 30-15 of the ITAA 1997 calls for a comparison between the price paid and the market value of the goods. It is therefore necessary to assess the market value of the medicines as well. I reject Mrs Arnold's ambitious submission that the relevant market consisted of similar donors to herself buying the medicines from MedAid at the price she purportedly paid i.e. $200 per Kit. The persons purchasing at that price had access to extraordinary terms of credit and were not in any sense ordinary consumers.

39. Much ink has been spilled upon the question of where a market is geographically situated: see, eg, *Air New Zealand Ltd v Australian Competition and Consumer Commission* [2017] HCA 21; (2017) 91 ALJR 648. Traditionally it is thought that the limits of a market are bounded by the limits of substitutability which, in turn, can be supply or demand side: *Re Tooth & Co Ltd* (1979) 39 FLR 1 at 38. The first step is generally thought to be to identify the goods in question. Here the goods are HIV medicines for distribution to charities in Africa. Whilst it is true that people could have purchased such goods from MedAid from its bonded warehouse in Kent, it seems that they could also be purchased in Africa, where they were to be used, for very much less.

40. Dr Snaith was called to give evidence on this topic. He was an emergency registrar at Nepean Hospital who has worked in medical aid in Kenya for a number of years through his membership (including as president) of a charity called Kenya Aid Inc. His evidence was that in or around February 2012, a Kit could be purchased in Western Kenya for $2.124. Mr Johnathan Muli-Kiliko is the Head of the Customer Services Department of the Mission for Essential Drugs and Supplies in Nairobi, Kenya. He gave similar evidence that in July 2010 a Kit could be purchased for USD$3.326 (I leave out of this account uncontroversial evidence about exchange rates). I am not entirely sure about the arithmetic contained in these reports, however it was not disputed before me and I proceed on the basis that the figures are largely accurate. I accept both men's evidence but will act on Mr Muli-Kiliko's since it is most advantageous to Mrs Arnold.

41. Although a person wishing to buy such medicines to donate in Kenya could have purchased them from MedAid for $200, this seems an unlikely thing to do when they could be acquired for next to nothing in Kenya where they were to be used. In truth, the persons who were willing to pay $200 per Kit were a group who were interested in obtaining an Australian tax deduction using a credit facility of extraordinary and uncommercial generosity. I do not really think that such persons can sensibly be regarded as genuine market participants. The reality is that the market was located in Africa and the market value was, at most, USD$3.326 per Kit. This was also the evidence of Mr Wayne Lonergan, an expert in such valuation exercises, which I accept. Mrs Arnold's 200 Kits therefore had a market value of USD$665.20. If she had in fact made a donation, this is the amount I would have allowed being the lesser of the market value of the property on the day the gift was purportedly made and the amount she paid as prescribed by item 1 of the table in s 30-15 of the ITAA 1997.

42. Since I have concluded that Mrs Arnold is not entitled to a deduction, I do not need to consider whether, if she had been, she would have been caught by the specific anti-avoidance provision relating to gifts in s 78A of the *Income Tax Assessment Act 1936* (Cth) ('ITAA 1936') or the more general provisions of Part IVA of that Act.

43. I turn then to the financial year ending 30 June 2011.

3. THE $560,000 DEDUCTION CLAIMED IN THE FINANCIAL YEAR ENDING 30 JUNE 2011

44. Mrs Arnold's case in relation to this sum is that on 28 June 2011 she entered into an agreement with Solstar to purchase a gift certificate for $560,000. Under the terms of the agreement the gift certificate was 'redeemable for [its] face amount in Australian Dollars (AUD) for any goods provided by Solstar'. The agreement did not specify the nature of the goods provided by Solstar. They could have been bicycle pumps.

45. On the same day, Mrs Arnold says that she pledged the gift certificate to 'Australia Metamorphic International for Global Development Fund DGR (Ref #J678 Burundi)'. As I understood her case, it was that on 27 June 2011 her husband, Mr Arnold, had forwarded the gift certificate to Metamorphic International Ltd ('Metamorphic') (via an email to a Mr Clarke) and that Mr Clarke had forwarded the gift certificate to the Global Development Group ('GDG') on or before 30 June 2011.

46. There is no dispute that GDG is a deductible gift recipient under item 1 of the table in s 30-15 of the ITAA 1997. That being so, the argument is that Mrs Arnold donated property to GDG (i.e. the gift certificate) which she had purchased for $560,000 and which was worth $560,000. Accordingly, she was entitled to claim $560,000 as a deduction under item 1 of s 30-15.

47. I do not accept this argument.

48. Under the 'Purchase Details' section of the agreement between Mrs Arnold and Solstar the purchase price of the gift certificate was said to be $560,000. However, Mrs Arnold's obligations were in fact to pay $28,000 within 30 days with the balance of $532,000 being due 10 years later on 30 June 2021. Interest was payable on the unpaid portion of the purchase price – called in the agreement the 'balloon payment' – at 6 monthly rests at a rate of 0.5% per annum. The obligation to pay $28,000 within 30 days appeared to conflict with cl 3 of the agreement which required the downpayment to be paid on signing by 'bank wire' to Solstar in United States dollars. It is not necessary to resolve that contradiction.

49. There is no evidence which I accept that Mrs Arnold paid $28,000 to Solstar in US dollars either on or around 28 June 2011 or, for that matter, at any other time. There was in

evidence, it is true, a receipt dated 13 September 2011 from Bendix Foreign Exchange Corporation which indicated that Mrs Arnold had wired Solstar US$34,161.65 at a cost of $34,161.65 Canadian which makes little, possibly no, sense. Without wrestling with all of the mysteries of the receipt, it is certainly clear that US$34,161.65 was not AUD$28,000 and that 13 September 2011 is not within 30 days of 28 June 2011. It is the wrong amount at the wrong time. I do not accept therefore that this receipt proves that Mrs Arnold paid the downpayment under the agreement on or before 30 June 2011. There were other 'Bendix' wire statements which might be – one does not know – referable to the interest due. Whether that is so, or not, it cannot overcome the absence of satisfactory evidence that Mrs Arnold paid any part of the purchase price.

50. That is the end of the matter. The purchase agreement with Solstar, like the one she executed the previous financial year with MedAid, had two payment obligations: the downpayment and the payment of the balance of the purchase price plus interest. It has not been shown to my satisfaction that any payment due under the purchase agreement was made. In terms of item 1 of the table in s 30-15(1) of the ITAA 1997, the lesser amount is therefore nil and she is entitled to no deduction.

51. Strictly, it is not necessary to determine the market value of the gift certificate which cannot be less than nil. However, for completeness this much might be noted. It was issued by Solstar for $560,000 worth of unspecified goods which could only be purchased from Solstar. Beyond knowing that Solstar is incorporated in Belize, the only concrete fact known about it is that it was involved in 2010 in procuring HIV medicines from India and shipping them to the United Kingdom. It has no presence in Australia and there was no evidence that its gift certificates circulate in this country or anywhere else for that matter. Furthermore, it is relevant to know that Mrs Arnold has not demonstrated that she even paid the downpayment due to Solstar under the purchase agreement. Nothing is known of Solstar's financial position or how it arranged the supply of the goods apparently to be redeemed under its gift certificates.

52. There was evidence that Metamorphic had redeemed the gift certificate for the shipment of HIV medicines to an entity known as Burundi Parables Christian Ministries. This evidence suggests that title to approximately 9 boxes worth of medicines (comprising 49,500 treatment units) of the kind purportedly purchased by Mrs Arnold in the preceding financial year were purportedly transferred by Solstar to Metamorphic on 5 January 2012

by means of a delivery direction to Southern Cross. It is convenient, although probably legally adventurous, to assume that this was effective. It appears these medicines were then airfreighted from Heathrow, London to Burundi on or around 31 January 2012 by Metamorphic. The relationship between GDG and Burundi Parables Christian Ministries remains unknown.

53. Mr Lonergan gave evidence about the gift certificate too. He reasoned that the obscurity of Solstar's origins and nature made it necessary to value the gift certificate by reference to what it could, and in fact had been, exchanged for. This was HIV medicines for distribution to Africa. He thought that these were to be valued according to African prices and concluded, on that basis, that the certificate was worth no more than $11,788. I accept this evidence.

54. In any event, the gift certificate was not donated to GDG but rather to Mr Clarke's entity, Metamorphic. It is true that Mrs Arnold's pledge refers to the pledge of the gift certificate to Metamorphic 'for Global Development Fund DGR' but there is no evidence I would accept that Metamorphic was GDG's agent for the purpose of receiving such gifts and Mrs Arnold's pledge cannot, in the manner of Jean-Luc Picard, make so that which is not.

55. Mrs Arnold argued that Metamorphic was GDG's agent for the purpose of receiving the gift certificate because of a partnership agreement dated 8 June 2004 between Metamorphic and GDG. The agreement was as follows:

> *This is an agreement between Global Development Group of Australia and our partner.*
>
> *The intention is to document an understanding of cooperation to enable projects to be undertaken which will be 'for development and relief'. These projects will be undertaken in a professionally competent manner.*
>
> *This agreement signifies on one part that Global Development Group is an Australian company that has an interest in development and relief in developing countries.*
>
> *You signify on your part that you have an opportunity to carry out a project(s) in a developing country for development and relief.*
>
> *Both partners will seek to develop a plan to carry out these projects in a manner suitable to Global Development Group AusAID and other approved aid organisations. We also will adhere to the ACFID code of conduct.*
>
> *Together we will develop the project plan in a form suitable to attract public and/or government funding, sharing the cost on an agreed basis.*

Once a project is developed and approved there will be a requirement to complete specific 'project' documentation.

56. This does not operate as an authority to Metamorphic to collect property on behalf of GDG. It is possible, I suppose, that some kind of conventional arrangement between Metamorphic and GDG had come into existence in relation to the project known as J678 in Burundi. This might have been some kind of joint project between GDG (operating in Burundi) and entities engaged in fundraising in Australia on its behalf. Material which might suggest such an arrangement includes:

- the agreement referred to above;
- an email of 27 June 2011 from Mr Arnold to Mr Clarke referring to the use of medicines to be brought under the gift certificate at 'Metamorphic's J678 Burundi project'; and
- a document headed 'J678 Burundi HIV Meds Pilot Partner Reconciliation Report' which seems to suggest some kind of accounting relationship between GDG and Metamorphic (although it contains no trace of any gift certificate, or the value thereof, passing between the parties).

57. However, these matters really do not prove anything in the cold light of day. At best, they hint that such a relationship might be present; but allusion is not proof. Accordingly, I do not find it demonstrated that Metamorphic was GDG's agent for the purpose of receiving the gift certificate.

58. Another variant of Mrs Arnold's case was, I think, this: regardless of the legalities of whether Metamorphic was entitled to receive the gift certificate for GDG, the fact was that GDG had actually itself received it before 30 June 2011. But the highest this actually rose was an email of 27 June 2011 from Mr Clarke to Mr Arnold:

> *Hi Steve,*
>
> *Just confirming that I spoke to GDG today and they are fine with the gift certificates, so the receipts will be issued as per our discussion. Also the 10k donation has arrived into our account, if the other 5k arrives today I will sent it all together for receipting purposes.*
>
> *Enjoy the remainder of your stay in Canada.*
>
> *Talk to you soon,*
>
> *Linds*

59. This does not prove that the certificates were delivered at that time. Indeed, an email from Mr Arnold to Mr Clarke earlier the very same day suggests, to the contrary, that it was Metamorphic which was going to redeem the certificate:

> *Hi Lindsay!*
>
> *I trust you received the wire and credit card verification for Stephanie's cash donation to Metamorphic and attached are the 2 gift certificates for redemption whenever you wish for the same type of medicine outlined in Metamorphic's J678 Burundi project. I will pay for all shipping costs to Burundi when you want to redeem. I've confirmed to the company that I am donating them to you and that if anybody else tries to redeem the certificates, that they are to contact me first as these cost us a whack and the balance has to be paid off in only a few short years.*
>
> *Also attached are the 2 Donor Pledge forms stating that the 2 gift cards & Stephanie's cash donations for $15,000 are for* ***Australia Metamorphic International ABN 59 100 059 729 for Global Development Fund DGR (Ref#J678 Burundi)****.*
>
> *Can you confirm if the above wording is correct or whether I should re-word and re-send the Donor Pledges?*
>
> *Sincerely,*
>
> *Steve*

60. The second paragraph cuts probably in the opposite direction because of its reference to GDG. However, a delivery direction from Solstar to Southern Cross dated 5 January 2012 (which I have already referred to at [52] above) informed Southern Cross that it now held the medicines which had been purchased with the gift certificate for Metamorphic, that is to say, not GDG. This letter has the advantage of being relatively contemporaneous. It would be difficult to conclude that if the gift certificates had already been donated to GDG that the medicines purchased with it from Solstar could have been owned by Metamorphic.

61. I can find therefore no basis to conclude that GDG had received the certificate before the end of the financial year. I have not overlooked in reaching that conclusion a receipt from GDG dated 28 June 2011 for $580,000. But exhibit 14 was an email which showed that this was not issued until 17 August 2011. I therefore reject Mr Clarke's evidence that this showed that GDG had received the gift certificate before 30 June 2011. The receipt is also inaccurate because Mrs Arnold did not, on any view, donate $580,000. At best she had donated a gift certificate with that face value redeemable for unspecified goods from an entity in Belize. I do not see the receipt as a reliable guide to historical events and I do not therefore think it useful evidence of an act of donation on 28 June 2011.

62. For completeness, I should note that the Commissioner made something of the fact that the gift certificate seemed to have been sent by email on 27 June 2011 whereas the purchase agreement was dated 28 June 2011. I think this may be explicable because the agreement was executed by Mrs Arnold in Canada in one time zone and the emails were received by Mr Clarke in Sydney in another.

63. In any event, it follows that Mrs Arnold is not entitled to claim a deduction at all for the gift certificate in the financial year ending 30 June 2011. In that circumstance, it is not necessary to deal with the Commissioner's alternative scheme arguments based upon s 78A and Part IVA of the ITAA 1936.

4. SHORTFALL PENALTY – 2010

64. Mrs Arnold's statement in her return that she was entitled to claim a deduction for the $40,000 was incorrect and hence a false or misleading statement. Accordingly, she is liable to an administrative penalty under s 284-75(1) of Schedule 1 to the *Taxation Administration Act 1953* (Cth) ('TAA'). Liability under s 284-75 may be avoided if a taxpayer has used the services of a tax agent and provided that agent with all relevant information (and the tax agent did not make the false statement deliberately or recklessly): sch 1 s 284-75(6) TAA. In this case, in or around September 2010, Mrs Arnold used the services of an agent, Ms Vivien Tang. Ms Tang gave evidence that in preparing Mrs Arnold's return for the 2010 financial year, she had relied upon the opinion of a solicitor, Mr Peter Laverick, dated 23 December 2009 and a private ruling applying to Mr Arnold.

65. The Commissioner submitted that there were aspects of the assumptions on which Mr Laverick's opinion was based which were not correct and Mr Arnold, at least, was aware of this. The one relied upon was that the 50 year credit arrangement in the purchase agreement had not been revealed to Mr Laverick (or in the process of obtaining the private ruling). This may be true, although the evidence that Mr Arnold knew that this was so was a little equivocal. The real problem with Mr Laverick's opinion was the erroneous assumption that 'paid' in item 1 of the table in s 30-15 of the ITAA97 was to be approached the same way as 'incurred' in s 8-1 of that Act. But it is not necessary to spend too much time on these matters of detail because one thing that Mrs Arnold certainly did not bring to Ms Tang's attention was the letter the ATO sent her on 13 September 2010. This letter said:

Your involvement in a potential tax exploitation scheme

Dear Ms Arnold

We have information that indicates you recently made a donation to a Deductible Gift Recipient (DGR). In addition to the donation, there was also an arrangement to purchase pharmaceuticals for an overseas charity funded through a long term loan.

We are currently reviewing the arrangement as we believe it may be a tax exploitation scheme. When the review is finalised, we will advise you of our view on the application of the law.

What you should do

We recommend that you do not claim any deductions arising under this arrangement other than the cash donation to the DGR. If you claim more than that amount and we conclude that the arrangement is a tax exploitation scheme, you will be liable for the tax shortfall and any associated penalties and interest.

If you have already claimed deductions relating to the purchase of pharmaceuticals when you lodged your tax return, we suggest you immediately request an amendment of your assessment. If you do, then any penalties that would otherwise have applied will be reduced to reflect the voluntary disclosure.

66. It is difficult to avoid the conclusion that Mrs Arnold should have provided this letter to Ms Tang. Accordingly, the safe-harbour of s 284-75(6)(b) of the TAA must be closed to her. The letter also provides the answer to the next question which is whether the misleading statement was made with intentional disregard of a taxation law, was reckless to the same, or was made without reasonable care. To claim the deduction after receiving such a letter must entail, at least, the conclusion that recklessness on Mrs Arnold's part about the operation of a tax law was involved. Accordingly, the penalty is 50% of the shortfall amount under item 2 of the table in s 284-90 of the TAA. Obviously, the defence of reasonable care under s 284-75(5) or item 3 of the table in s 284-90 cannot arise in that circumstance. The Commissioner in his submissions did not urge the imposition of a further penalty on the basis that Mrs Arnold had adopted a position that was not reasonably arguable in relation to the application of a tax law and I do not consider such an argument.

67. I should note briefly that Mrs Arnold sought to rely on a certificate of valuation issued on 7 July 2010 by the Australian Valuation Office to Mr Gordon Sparrow of Australian Relief & Mercy Services as conclusive evidence of the market value of a Kit during the 2010 financial year. This is despite the certificate being stated to be a determination of market value under a different section of the taxation legislation (ITAA97 s 30-212) and an express disclaimer that it was prepared on the basis that full disclosure of all relevant

information that could affect valuation had been made. This argument is bound to fail as the certificate was predicated on different factual assumptions to those which underpinned the transactions entered into by Mrs Arnold, such as the generous payment terms available to the donor and the fact that the Kits would never enter Australia. The certificate therefore does not assist her and is of no legal consequence to this proceeding.

5. SHORTFALL PENALTY – 2011

68. Ms Tang was, again, the person who prepared Mrs Arnold's return in this financial year. The only material with which she was provided was an email dated 8 May 2012 from Mrs Arnold which relevantly referred to '$560,000 cash gift card to Global Development Group' and the receipt from GDG dated 28 June 2011 which referred to a donation of $560,000. Ms Tang gave evidence before the Tribunal that she considered this to be indicative of an upfront payment of $560,000 and that she had no knowledge of any deferred payment or loan arrangement between Mrs Arnold and Solstar.

69. Ms Tang was also not told:

- the gift voucher was from the same Belize company (Solstar) involved in the previous year's deduction; or
- that the gift card was to be used to purchase pharmaceuticals.

70. Had these matters been disclosed, I am confident Ms Tang would have realised the import of the Commissioner's letter of 13 September 2010 (which she had by then received). It was most inappropriate for Mrs Arnold not to have revealed to Mrs Tang that the gift certificate was just a variant of the previous year's claimed deduction. Accordingly, the safe-harbour in s 284-75(6) of the TAA is not available to salvage her.

71. Was Mrs Arnold's approach to the taxation law one of intentional disregard, recklessness or just a failure to take reasonable care? Mrs Arnold knew that pharmaceutical donations schemes were under close scrutiny. She had been warned not to claim such a deduction in the previous year. This deduction was just a rebadged version of what she had already been warned about in 2010. She was, in that circumstance, recklessly indifferent to the operation of the taxation laws and hence liable to a 50% administrative penalty. As this was the second such breach the base amount is to be increased by 20% under s 284-220.

6. OTHER MATTERS

72. The Commissioner called a Mr Fratzia to give evidence. Mr Arnold sought to ask Mr Fratzia about a recording Mr Arnold had taken of Mr Fratzia without his permission. I declined to permit this to occur. The conduct in question was a breach of s 7(1) of the *Surveillance Devices Act 2007* (NSW) which prohibits the use of a listening device to record a private conversation. There is an exception where the recording is reasonably necessary to protect the lawful interest of one of the parties to the recording: s 7(3). The test is one of reasonable necessity not convenience. There were plenty of perfectly lawful ways for Mr Arnold to make his point about the valuation of the medicines without resorting to espionage: see, eg, *DW v The Queen* [2014] NSWCCA 28; (2014) 239 A Crim R 192 at 200 [38] ff. Accordingly, s 7(3) does not apply. The material was therefore unlawfully obtained. The *Evidence Act 1995* (Cth) does not apply to these proceedings. Nevertheless, I do not think that I should allow the material to be used unless its probative value outweighs the public ill involved in condoning unlawful behaviour. I did not think that the probative value of the material in question warranted permitting it to be used.

7. CONCLUSIONS

73. The Tribunal affirms the decisions under review except that relating to the shortfall penalty for 2011. In the case of that decision the Tribunal varies the decision to impose an administrative penalty of 50% with an increase in the base amount of 20%.

I certify that the preceding 73 (seventy-three) paragraphs are a true copy of the reasons for the decision herein of The Hon. Justice Perram, Deputy President

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

Associate

Dated: 18 August 2017

Date(s) of hearing:	**20-21, 28 September 2016**
Advocate for the Applicant:	**Mr S Arnold**
Counsel for the Respondent:	**Mr B Kasep**
Solicitors for the Respondent:	**Australian Government Solicitor**