FEDERAL COURT OF AUSTRALIA

Hart v Commissioner of Taxation [2018] FCAFC 61

Appeal from:	*Hart v Commissioner of Taxation (No 4)* [2017] FCA 572
File number:	QUD 299 of 2017
Judges:	**ROBERTSON, WIGNEY AND STEWARD JJ**
Date of judgment:	20 April 2018
Catchwords:	**INCOME TAX** – appeal by taxpayer from objection decision disallowing objections to notice of assessment and notice of amended assessment – where Commissioner determined two amounts should have been included in applicant's taxable income for the 1997 income year – applicant taxpayer was a principal of a law firm and specialised in taxation law – whether first amount should have been included in taxpayer's assessable income per ss 95A(1), 97 and 101 and/or Pt IVA of the *Income Tax Assessment Act 1936* (Cth) – whether the second amount should have been included in taxpayer's assessable income per Pt IVA
Legislation:	*Income Tax Assessment Act 1936* (Cth) ss 25, 26, 95A, 97, 100A, 101, 177A, 177C, 177D, 226 *Income Tax Assessment Act 1997* (Cth) s 6-5 *Taxation Administration Act 1953* (Cth) s 14ZZO
Cases cited:	*Accent Management Limited v Commissioner of Inland Revenue* [2007] NZCA 230 *East Finchley Pty Ltd v Federal Commissioner of Taxation* (1989) 90 ALR 457 *Federal Commissioner of Taxation v Anstis* (2010) 241 CLR 443 *Federal Commissioner of Taxation v Ashwick (Qld) No 127 Pty Ltd* (2011) 192 FCR 325 *Federal Commissioner of Taxation v Dalco* (1990) 168 CLR 614 *Federal Commissioner of Taxation v Dixon* (1952) 86 CLR 540 *Federal Commissioner of Taxation v Mochkin* (2003) 127 FCR 185 *Federal Commissioner of Taxation v Peabody* (1994) 181

	CLR 359 *Federal Commissioner of Taxation v Spotless Services Ltd* (1996) 186 CLR 404 *Federal Commissioner of Taxation v Stone* (2005) 222 CLR 289 *Federal Commissioner of Taxation v Vegners* (1989) 90 ALR 547 *Futuris Corporation Ltd v Federal Commissioner of Taxation* [2010] FCA 935 *Hart v Federal Commissioner of Taxation (No.2)* [2016] FCA 897 *Normandy Finance and Investments Asia Pty Ltd v Federal Commissioner of Taxation* [2015] FCA 1420 *Pascoe v Federal Commissioner of Taxation* (1956) 30 ALJR 402 *Raftland Pty Ltd v Federal Commissioner of Taxation* (2008) 238 CLR 516 *RCI Pty Ltd v Federal Commissioner of Taxation* [2011] FCAFC 104 *Richard Walter Pty Ltd v Federal Commissioner of Taxation* (1996) 67 FCR 243 *Union-Fidelity Trustee Co of Australia Limited v Federal Commissioner of Taxation* (1969) 119 CLR 177
Date of hearing:	5 March 2018
Registry:	Victoria
Division:	General Division
National Practice Area:	Taxation
Category:	Catchwords
Number of paragraphs:	110
Counsel for the Appellant:	Mr Wilson Q.C. with Mr Anderson
Solicitor for the Appellant:	Cleary Hoare Solicitors
Counsel for the Respondent:	Mr Williams S.C. with Ms Brennan Q.C. and Mr Jedrzejczyk
Solicitor for the Respondent:	Australian Government Solicitor

ORDERS

QUD 299 of 2017

BETWEEN:	**MICHAEL JAMES PATRICK HART** Appellant
AND:	**COMMISSIONER OF TAXATION** Respondent

JUDGES:	**ROBERTSON, WIGNEY AND STEWARD JJ**
DATE OF ORDER:	**20 APRIL 2018**

THE COURT ORDERS THAT:

1. The appeal be dismissed with costs.

Note: Entry of orders is dealt with in Rule 39.32 of the *Federal Court Rules 2011*.

REASONS FOR JUDGMENT

THE COURT:

INTRODUCTION

1 The appellant is a solicitor in the Brisbane law firm of Cleary Hoare. He specialises in taxation law. Towards the end of the 1997 financial year, he, together with others, entered into two arrangements, each known as the "New Venture Income Scheme" ("NVI Scheme"). The broad effect of each scheme was to divert two classes of earnings away from the appellant, or entities he controlled, and direct it ultimately into the hands of a company with carry forward tax losses, called Retail Technology Holdings Pty Ltd ("RTH"). From then, following a series of gifts and subscriptions for capital, the earnings were paid to the appellant. The appellant contends, and the respondent (the "Commissioner") denies, that he was lent these monies. The Commissioner has assessed the earnings as income taxable in the appellant's hands.

2 One class of income, called the Practice Amount (in the sum of $220,398) was said to be part of the earnings of the firm Cleary Hoare, owned at the time by a unit trust known as the Cleary Hoare Practice Trust (the "Practice Trust"). The other class of income, called the IET Amount (in the sum of $275,481), was part of the earnings of three so called "income earning trusts", called the IETs, which promoted and sold certain fiscal arrangements invented or devised by the appellant, with others.

3 In the year of income ended 30 June 1997, the earnings of Cleary Hoare were paid to the Practice Trust. Four solicitors of that firm, including the appellant, owned the units in that trust through intermediate family discretionary trusts. In the case of the appellant, his units were owned by Outlook Crescent Pty Ltd ("OCPL") as trustee for the Outlook Practice Trust (the "Outlook Trust").

4 The appellant disputes that he was ever paid the Practice Amount. He contends, instead, that the Outlook Trust lent him $185,698. He does not dispute that this sum was sourced from a distribution which he contends was made by the Practice Trust to the Outlook Trust. The appellant also disputes that he was ever paid the IET Amount.

5 The Commissioner included in the assessable income of the appellant the Practice Amount pursuant to Div 6 of Pt 3 of the *Income Tax Assessment Act 1936* (Cth) (the "1936 Act"), or

alternatively, pursuant to Pt IVA of that Act. He also included in the assessable income of the appellant the IET Amount, but only pursuant to Pt IVA of the 1936 Act.

FACTS

6 As the primary judge found, many of the facts were not in dispute, save for the contended for loan and perhaps, the source of some payments. One commences with the appellant himself who is a solicitor. He joined the firm Cleary Hoare in January 1990 as a salaried partner. At that time it had three partners. As already mentioned, his speciality was tax law. Between 1990 and 1992, the appellant was a bankrupt by reason of certain guarantees he had given.

7 Following his discharge from bankruptcy, the appellant commenced discussions with Cleary Hoare concerning a possible partnership. At that time, the firm was encountering financial difficulties. It owed its bank a large sum of money and the appellant was not prepared to assume personal liability for any part of that debt. On 1 July 1992, OCPL, in its capacity as trustee of the Outlook Trust, became a partner of Cleary Hoare, through the appellant as nominee. In 1993, the firm decided to reorganise its ownership structure because of continuing concerns about its financial soundness. The Practice Trust was established to own the business of Cleary Hoare pursuant to the then rules of the Queensland Law Society. The original trustees of the Practice Trust were the three other original partners of the firm. Units in the Practice Trust were issued in equal shares to discretionary family trusts established for the families of each partner, including, as already mentioned, the Outlook Trust. The appellant was not an original trustee of the Practice Trust but he had assumed that role, together with the three other original partners, by the 1997 income year. Whether the NVI structure which was adopted for the Practice Amount complied with the Queensland Law Society rules is an issue which we will return to below.

8 As a previously employed solicitor of Cleary Hoare in 1991 and in 1992, the appellant had been paid a salary for the provision by him of legal services. In the 1994, 1995 and 1996 income years the whole of the income of the Outlook Trust, derived from distributions made to it by the Practice Trust, was distributed to Cleary & Hoare Chol Corporation (No 1) Pty Ltd as trustee of the Cleary Hoare Office Unit Trust ("CHOUT"). CHOUT was the service trust for the firm Cleary Hoare. It would appear that CHOUT had sufficient tax losses to absorb this income, although these had been largely used up by the 1997 income year.

9 At some point prior to the end of the 1997 fiscal year, two of the three IETs mentioned earlier, being the LM Income Discretionary Trust and the CHC Discretionary Trust were

established. The third IET, the Annesley Trust, had been established earlier in 1994. These trusts earned income from the sale of tax planning and tax scheme services. It is accepted that the appellant had never himself received distributions directly from these trusts and indeed, at least in the case of the LM Income Discretionary Trust, was not eligible to receive such distributions. He was, however, a director of each corporate trustee of each trust and, we infer, closely involved in carrying out the business of each trust. In 1997, the LM Income Discretionary Trust and the CHC Discretionary Trust had never made any previous distribution of income, save for those the subject of this appeal. There was evidence before the primary judge that the Annesley Trust had made a prior distribution in 1996 to beneficiaries, including the Outlook Trust.

10 The NVI Scheme, described below, was developed following consideration by the appellant of the decision of the High Court in *Federal Commissioner of Taxation v Peabody* (1994) 181 CLR 359. It will be recalled that in that case, the High Court had decided that Pt IVA did not apply to the taxpayer, Mrs Peabody, because it was not reasonable to conclude for the purposes of s 177C of the 1936 Act that, but for the scheme entered into in that case, she might reasonably be expected to have derived assessable income. Another taxpayer would have instead derived that income. For that purpose, the High Court (at 385) endorsed the proposition that a reasonable expectation for the purposes of s 177C involves:

> …a prediction as to events which would have taken place if the relevant scheme had not been entered into or carried out and the prediction must be sufficiently reliable for it to be regarded as reasonable.
>
> (Citations omitted)

11 This was apparently the inspiration for the NVI Scheme. Its fiscal efficacy, so it was said, depended upon the derivation of income by a series of new trusts which had no previous history of making distributions, and the receipt, at some point in the structure, of that income by an entity with substantial tax losses followed by a series of gifts and capital contributions of the same income. The final step was intended to be a loan to the taxpayer of that income. However, other than the use of new trusts with no previous pattern of making distributions, much of the NVI Scheme did not appear to be inspired by the decision in *Peabody*. The clear inference is that much of the structure was inspired by a desire to avoid the "trust stripping" provisions in s 100A of the 1936 Act. These had been originally introduced into the 1936 Act in 1979.

12 In the 1997 income year, s 100A relevantly provided:

> (1) Where:
>
> (a) apart from this section, a beneficiary of a trust estate who is not under any legal disability is presently entitled to a share of the income of the trust estate; and
>
> (b) the present entitlement of the beneficiary to that share or to a part of that share of the income of the trust estate (which share or part, as the case may be, is in this subsection referred to as the "relevant trust income") arose out of a reimbursement agreement or arose by reason of any act, transaction or circumstance that occurred in connection with, or as a result of, a reimbursement agreement;
>
> the beneficiary shall, for the purposes of this Act, be deemed not to be, and never to have been, presently entitled to the relevant trust income.
>
> (2) Where:
>
> (a) apart from this section, a beneficiary of a trust estate who is not under any legal disability would, by reason that income of the trust estate was paid to, or applied for the benefit of, the beneficiary, be deemed to be presently entitled to income of the trust estate; and
>
> (b) that income or a part of that income (which income or part, as the case may be, is in this subsection referred to as the "relevant trust income") was paid to, or applied for the benefit of, the beneficiary as a result of a reimbursement agreement or as a result of any act, transaction or circumstance that occurred in connection with, or as a result of, a reimbursement agreement;
>
> the relevant trust income shall, for the purposes of this Act, be deemed not to have been paid to, or applied for the benefit of, the beneficiary.
>
> (3) In the preceding provisions of this section:
>
> (a) a reference to income of a trust estate to which a beneficiary is, apart from this section, presently entitled shall be read as not including a reference to:
>
> (i) income of the trust estate to which the beneficiary is presently entitled in the capacity of a trustee of another trust estate, being income that was paid to, or applied for the benefit of, the beneficiary before 6 March 1980; or
>
> (ii) income that was paid to, or applied for the benefit of, the beneficiary before 12 June 1978; and
>
> (b) a reference to income of a trust estate that was paid to, or applied for the benefit of, a beneficiary of the trust estate shall be read as not including a reference to:
>
> (i) income of the trust estate that, before 6 March 1980, was paid to, or applied for the benefit of, the beneficiary in the capacity of a trustee of another trust estate; or
>
> (ii) income of the trust estate that was paid to, or applied for the

benefit of, the beneficiary before 12 June 1978.

(3A) Where:

(a) apart from this section, a beneficiary (in this subsection referred to as the "trustee beneficiary") of a trust estate is presently entitled to a share of the income of the trust estate in the capacity of a trustee of another trust estate (in this subsection referred to as the "interposed trust estate");

(b) apart from this subsection, the trustee beneficiary would, by virtue of subsection (1), be deemed not to be, and never to have been, presently entitled to that share or a part of that share of the income of the first-mentioned trust estate (which share or part is in this subsection referred to as the "relevant trust income"); and

(c) apart from this section, a beneficiary of the interposed trust estate is or was, or beneficiaries of the interposed trust estate are or were, presently entitled, or deemed to be presently entitled, to any income of the interposed trust estate (in this subsection referred to as the "distributable trust income") that is attributable to the relevant trust income;

subsection (1) does not apply, and shall be deemed never to have applied, in relation to the trustee beneficiary, in relation to any part of the relevant trust income to which the distributable trust income is attributable.

(3B) Where:

(a) apart from this section, a beneficiary (in this subsection referred to as the "trustee beneficiary") of a trust estate would, by reason that income of the trust estate was paid to, or applied for the benefit of, the trustee beneficiary, be deemed to be presently entitled to income of the trust estate in the capacity of a trustee of another trust estate (in this subsection referred to as the "interposed trust estate");

(b) apart from this subsection, that income or a part of that income (which income or part is in this subsection referred to as the "relevant trust income") would, by virtue of subsection (2), be deemed not to have been paid to, or applied for the benefit of, the trustee beneficiary; and

(c) apart from this section, a beneficiary of the interposed trust estate is or was, or beneficiaries of the interposed trust estate are or were, presently entitled, or deemed to be presently entitled, to any income of the interposed trust estate (in this subsection referred to as the "distributable trust income") that is attributable to the relevant trust income;

subsection (2) does not apply, and shall be deemed never to have applied, in relation to the trustee beneficiary, in relation to any part of the relevant trust income to which the distributable trust income is attributable.

(3C) A reference in paragraph (3A) (c) or (3B) (c) to a beneficiary of a trust estate shall be read as not including a reference to a beneficiary who is under a legal disability.

(4) Where subsection (1) or (2) applies in relation to any income of a trust estate

of a year of income:

(a) in the application of this Division in relation to the trust estate in relation to the year of income, section 99A shall be read as if subsections (2), (3) and (3A) of that section were omitted; and

(b) for the purposes of any application of section 99A in relation to the trust estate in relation to the year of income, the trust estate shall be deemed to be a resident trust estate.

(5) For the purposes of subsection (1), but without limiting the generality of that subsection, where:

(a) a reimbursement agreement was entered into at or after the time when a person became a beneficiary of a trust estate (whether the person became a beneficiary of the trust estate before or after the commencement of this section); and

(b) the amount (in this subsection referred to as the "increased amount") of the share of the income of the trust estate to which the beneficiary is presently entitled exceeds the amount (in this subsection referred to as the "original amount") of the income of the trust estate to which the beneficiary would have been, or could reasonably be expected to have been, presently entitled if the reimbursement agreement had not been entered into or if an act, transaction or circumstance that occurred in connection with, or as a result of, the reimbursement agreement had not occurred;

the present entitlement of the beneficiary to so much of the increased amount as exceeds the original amount shall be taken to have arisen out of the reimbursement agreement.

(6) For the purposes of subsection (2), but without limiting the generality of that subsection, where:

(a) a reimbursement agreement was entered into at or after the time when a person became a beneficiary of a trust estate (whether the person became a beneficiary of the trust estate before or after the commencement of this section); and

(b) income of the trust estate was paid to, or applied for the benefit of, the beneficiary and the amount (in this subsection referred to as the "increased amount") of that income exceeds the amount (in this subsection referred to as the "original amount") that would have been, or could reasonably be expected to have been, paid to, or applied for the benefit of, the beneficiary if the reimbursement agreement had not been entered into or if an act, transaction or circumstance that occurred in connection with, or as a result of, the reimbursement agreement had not occurred;

so much of the increased amount as exceeds the original amount shall be taken to be income of the trust estate that was paid to, or applied for the benefit of, the beneficiary as a result of the reimbursement agreement.

(6A) Where:

(a) subsection (1) or (2) applies, or would but for subsection (3A) or (3B) apply, in relation to a beneficiary of a trust estate in relation to a

reimbursement agreement in relation to any income of the trust estate; and

(b) as part of, under or in connection with the reimbursement agreement, the beneficiary incurred or incurs a loss or outgoing after 5 March 1980 in respect of which a deduction has been allowed or would, but for this subsection, be allowable;

then, notwithstanding any other provision of this Act, a deduction shall be deemed not to have been, or not to be, allowable, as the case may be, in respect of that loss or outgoing.

(6B) Where subsection (6A) deems a deduction not to have been, or not to be, allowable in respect of a loss or outgoing incurred by a taxpayer in the acquisition of property that, for the purposes of the application of this Act and the Income Tax Assessment Act 1997 in relation to the taxpayer is or was trading stock, then, notwithstanding any other provision of this Act or that Act, the cost or cost price of that property, for the purposes of the application of Subdivision B of Division 2 of Part III of this Act or Division 70 (Trading stock) or 385 (Primary production) of the Income Tax Assessment Act 1997 in relation to that property in relation to the taxpayer, shall be taken to be, and at all times to have been, nil.

(7) Subject to subsection (8), a reference in this section, in relation to a beneficiary of a trust estate, to a reimbursement agreement shall be read as a reference to an agreement, whether entered into before or after the commencement of this section, that provides for the payment of money or the transfer of property to, or the provision of services or other benefits for, a person or persons other than the beneficiary or the beneficiary and another person or other persons.

(8) A reference in subsection (7) to an agreement shall be read as not including a reference to an agreement that was not entered into for the purpose, or for purposes that included the purpose, of securing that a person who, if the agreement had not been entered into, would have been liable to pay income tax in respect of a year of income would not be liable to pay income tax in respect of that year of income or would be liable to pay less income tax in respect of that year of income than that person would have been liable to pay if the agreement had not been entered into.

(9) For the purposes of subsection (8), an agreement shall be taken to have been entered into for a particular purpose, or for purposes that included a particular purpose, if any of the parties to the agreement entered into the agreement for that purpose, or for purposes that included that purpose, as the case may be.

(10) A reference in subsection (7) to the payment of money to a person or persons shall be read as including a reference to the payment of money to a person or persons by way of loan.

(11) A reference in this section to a person shall be read as including a reference to a person in the capacity of a trustee.

(12) For the purposes of this section, an agreement that provides for a person to release, abandon, fail to demand payment of or postpone payment of, a debt owed by another person shall be deemed to be an agreement that provides for the payment of money to that other person.

(13) In this section:

> **agreement** means any agreement, arrangement or understanding, whether formal or informal, whether express or implied and whether or not enforceable, or intended to be enforceable, by legal proceedings, but does not include an agreement, arrangement or understanding entered into in the course of ordinary family or commercial dealing;
>
> **property** includes a chose in action and also includes an estate, interest, right or power, whether at law or in equity, in or over property.

13 Section 100A was intended to address schemes which involved the introduction of a new beneficiary presently entitled to all, or a part of, the income of a trust which could absorb trust distributions without the payment of tax, or at least full tax, usually because that beneficiary had some fiscal attribute enabling it to avoid the payment of tax, such as the presence of carry forward tax losses. A payment would then be made to the taxpayer, who might otherwise have received the distribution, under what in s 100A is called a "reimbursement agreement". The payment could include a loan. Under s 100A, where its provisions were satisfied, the new beneficiary was deemed not to be presently entitled to a share of the income of the trust, and tax was instead assessed at the top rate in the hands of the trustee. The provisions addressed the possibility that the new beneficiary might be acting in the capacity of trustee of another trust and might itself redistribute the income it had received to its own beneficiaries.

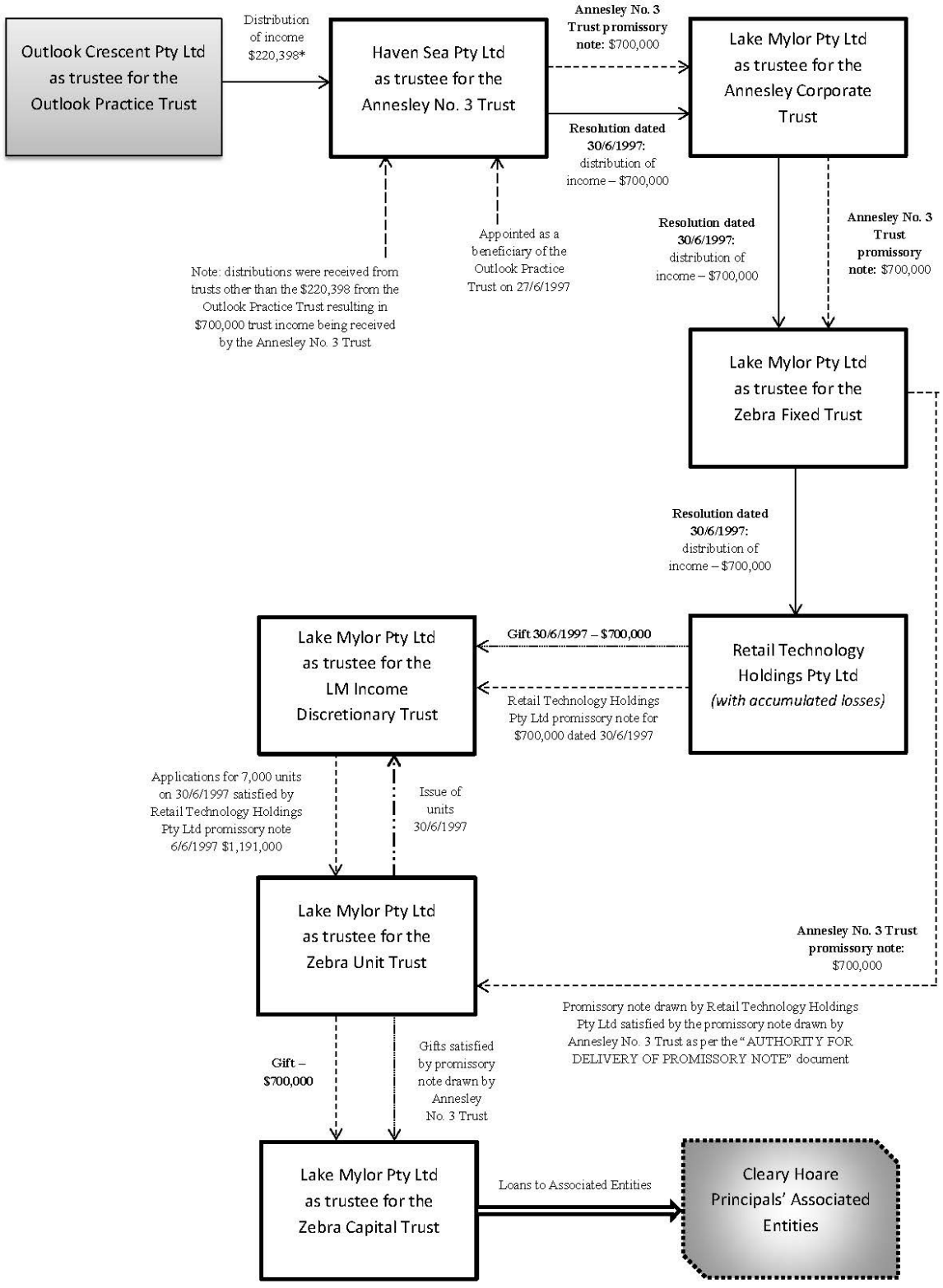
14 The NVI Scheme involved some of the attributes of trust stripping under s 100A. These included the introduction of a new beneficiary, the use of an entity with tax losses, and the payment of a purported loan. Whether the NVI Scheme successfully avoided the reach of s 100A is not a question which arises for determination in this appeal.

15 As it happens, it is probably unnecessary for the detail of each step of the NVI Scheme to be completely analysed. That is because, at least in relation to the Practice Amount, its efficacy ultimately turned on accepting that what the appellant in fact received was by way of loan. Generally speaking, and focusing for the moment on the NVI Scheme used for the Practice Amount by way of illustration, the scheme involved the payment of a share of the earnings of Cleary Hoare, derived by the Practice Trust to the Outlook Trust. In prior years, the Outlook Trust had paid these earnings to CHOUT, which had tax losses. Under the NVI Scheme this did not happen. Instead, the earnings were paid to a new beneficiary, acting in the capacity as trustee of another trust (the Annesley No 3 Trust). The earnings were then distributed twice to two successive trustees, and from there to RTH. It was critical that RTH, and not the

previous trustees, who did not have carry forward tax losses, be presently entitled to those earnings. RTH had the necessary tax losses. The earnings then had to reach the taxpayer in a tax-free way. This was achieved by RTH using the earnings to subscribe for units in a unit trust, then that trust gifting the earnings to another trust and then a loan to the taxpayer. Whether the last step was effectively achieved is a key issue in this case.

16 The two NVI Schemes were ultimately entered into at the end of the 1997 income year and were described by the primary judge at [62] to [68], which it is convenient to reproduce in full:

> 62. The Commissioner's flowchart in relation to the Practice Trust NVI Scheme, remembering the dispute noted above as to the last stage marked "*Loans to Associated Entities*", depicted the following:



63. The narrative which the above flowchart depicts from [52] of the Commissioner's third further amended appeal statement is as follows (per original):

(ii) The Practice Trust NVI Scheme

52. Based on the documents and information supplied by the Applicant and his advisers the respondent understands that the Practice Trust NVI scheme for the 1997 income year comprised the following steps, matters, transactions and events:

(a) On 9 May 1997, the LM Income Trust, the Zebra Fixed Trust and the Zebra Unit Trust were settled.

(b) On 30 May 1997, the Annesley No. 3 Trust and the Annesley Corporate Trust were settled.

(c) On 27 June 1997, the following events occurred:

i. The directors of OCPL as trustee of the Outlook Trust resolved to appoint Haven Sea Pty Ltd as trustee of the Annesley No. 3 Trust as a tertiary beneficiary of the Outlook Practice Trust.

ii. The directors of OCPL as trustee of the Outlook Trust resolved to distribute all the income for the year ended 30 June 1997 to the Annesley No. 3 Trust.

(d) On 30 June 1997, the following events occurred:

i. The directors of Haven Sea Pty Ltd as trustee of the Annesley No. 3 Trust resolved to distribute $700,000 to Lake Mylor Pty Ltd as trustee of the Annesley Corporate Trust. The resolution stated that the distribution was to be by bearer promissory note drawn by 'the Company' for $700,000 with the balance by cheque payable as directed by Lake Mylor Pty Ltd.

ii. The directors of Lake Mylor Pty Ltd as trustee of the Annesley Corporate Trust resolved to distribute $700,000 to the Zebra Fixed Trust. The resolution stated that the amount was to be paid forthwith by delivery of a bearer promissory note received by Annesley Corporate Trust from Annesley No. 3 Trust for $700,000 to the Trustee of the Zebra Fixed Trust or as otherwise directed by it.

iii. The directors of Lake Mylor Pty Ltd as trustee of the Zebra Fixed Trust resolved to distribute $700,000 to the fixed beneficiary (being Retail Technology Holdings Pty Ltd). The resolution stated that the distribution was to be paid forthwith by delivery of a bearer promissory note received by Annesley Corporate Trust to the fixed beneficiary or as otherwise directed by it.

iv. A bearer promissory note was issued by Haven Sea Pty Ltd as trustee of the Annesley No. 3 Trust for $700,000. Receipt of the bearer promissory note is acknowledged by Lake Mylor Pty Ltd as trustee of

the Annesley Corporate Trust and Lake Mylor Pty Ltd as trustee of the Zebra Unit Trust.

v. By letter from Retail Technology Holdings Pty Ltd to Lake Mylor Pty Ltd it advised that it has decided to make a gift of $700,000 to Lake Mylor Pty Ltd in its capacity as trustee of the LM Income Trust.

vi. A bearer promissory note was issued by Retail Technology Pty Ltd for $700,000. Receipt of the bearer promissory note is acknowledged by Lake Mylor Pty Ltd as trustee of the LM Income Trust and Lake Mylor Pty Ltd as trustee of the Zebra Unit Trust.

vii. The directors of Lake Mylor Pty Ltd as trustee of the LM Income Trust resolved to accept the gift of $700,000 from Retail Technology Holdings Pty Ltd by way of delivery of a bearer promissory note drawn by Retail Technology Holdings Pty Ltd. It was further resolved to subscribe for 7000 'B' units at $100 each in the Zebra Unit Trust with the promissory note to be delivered in satisfaction of the application monies.

viii. Lake Mylor Pty Ltd as trustee of the LM Income Trust made application for 7,000 units in the Zebra Unit Trust with payment of the application monies by means of delivery of the bearer promissory note drawn by Retail Technology Holdings Pty Ltd.

ix. The directors of Lake Mylor Pty Ltd as trustee of the Zebra Unit Trust noted that an application for units had been received from Lake Mylor Pty Ltd as trustee of the LM Income Trust for 7,000 units at $100 each together with the bearer promissory note referred to in the application in satisfaction of the application monies. It was resolved to accept the promissory note of $700,000 issued by Retail Technology Holdings Pty Ltd as payment in satisfaction of the application monies and to issue units.

x. Lake Mylor Pty Ltd as trustee of the Zebra Unit Trust issued a unit certificate for 7,000 'B' units to Lake Mylor Pty Ltd as trustee of the LM Income Trust.

xi. The directors of Lake Mylor Pty Ltd as trustee of the Annesley Corporate Trust noted that it had as the trustee of the LM Income Trust received a gift of $700,000 from Retail Technology Holdings Pty Ltd. It was further noted that Retail Technology Holdings Pty Ltd was the fixed beneficiary of the Zebra Fixed Trust with the result that the Zebra Fixed Trust qualified as a beneficiary of the Annesley Corporate Trust. It was also noted that the Annesley Corporate

Trust had received a final income distribution from the Annesley No. 3 of $700,000 by way of delivery of a bearer promissory note. It was further resolved to make a final income distribution of $700,000 to the Zebra Fixed Trust by delivery of the promissory note to the trustee of the Zebra Fixed Trust or as otherwise directed by it.

xii. The directors of Lake Mylor Pty Ltd as trustee of the Zebra Fixed Trust noted that the trust had received a final income distribution from the Annesley Corporate Trust of $700,000 by way of delivery of a bearer promissory note. It resolved to:-

> make a final distribution of income in the amount of the above total to the fixed beneficiary to be paid forthwith as to the amount of the promissory note by delivery of the promissory note to the fixed beneficiary or as otherwise directed by it.

xiii. An undated document, titled 'AUTHORITY FOR DELIVERY OF PROMISSORY NOTE' addressed to Lake Mylor Pty Ltd as trustee of the Annesley Corporate Trust and Lake Mylor Pty Ltd as trustee of the Zebra Fixed Trust from Retail Technology Holdings Pty Ltd and Lake Mylor Pty Ltd as trustee of the LM Income Trust in regard to the distributions of income from the Annesley Corporate Trust:-

- authorised the promissory notes issued by Haven Sea Pty Ltd as trustee of the Annesley No. 3 to be delivered to Lake Mylor Pty Ltd as trustee of the Zebra Unit Trust;
- in satisfaction of the obligations arising under the bearer promissory note for the same amount drawn by Retail Technology Holdings Pty Ltd and delivered by Lake Mylor Pty Ltd as trustee of the LM Income Trust to Lake Mylor Pty Ltd as trustee of the Zebra Unit Trust in respect of the application for 'B' units in the Zebra Unit Trust;
- to be delivered by the [sic] Lake Mylor Pty Ltd as trustee for the Zebra Unit Trust in respect of any gift it resolves to make to Lake Mylor Pty Ltd as trustee of the Zebra Capital Trust.

64. The sequence of events reproduced above from [52(d)] of the Commissioner's third further amended appeal statement is not accepted by Mr Hart. However, the asserted correct sequence was not pleaded and no argument was advanced as to how or why the unstated correct sequence made any difference given that all the events described at [52(d)] took place on 30 June 1997. Moreover, the Commissioner did not ultimately rely upon any particular sequence of events on that day, and Mr Hart did not ultimately dispute any particular sequence of events on that day.

65. There was no specific pleading to [53] of the Commissioner's third further amended appeal statement as follows, but it is apparent that [53(3)(ii)] in particular reflects the dispute between the parties as to the characterisation of the money received by Mr Hart or to his benefit, his case being that the money was received as a loan (per original):

> 53. Further steps in the NVI scheme included:
>
> (1) On 1 July 1997, the Zebra Capital Trust was settled.
>
> (2) On 2 July 1997, the following events occurred:
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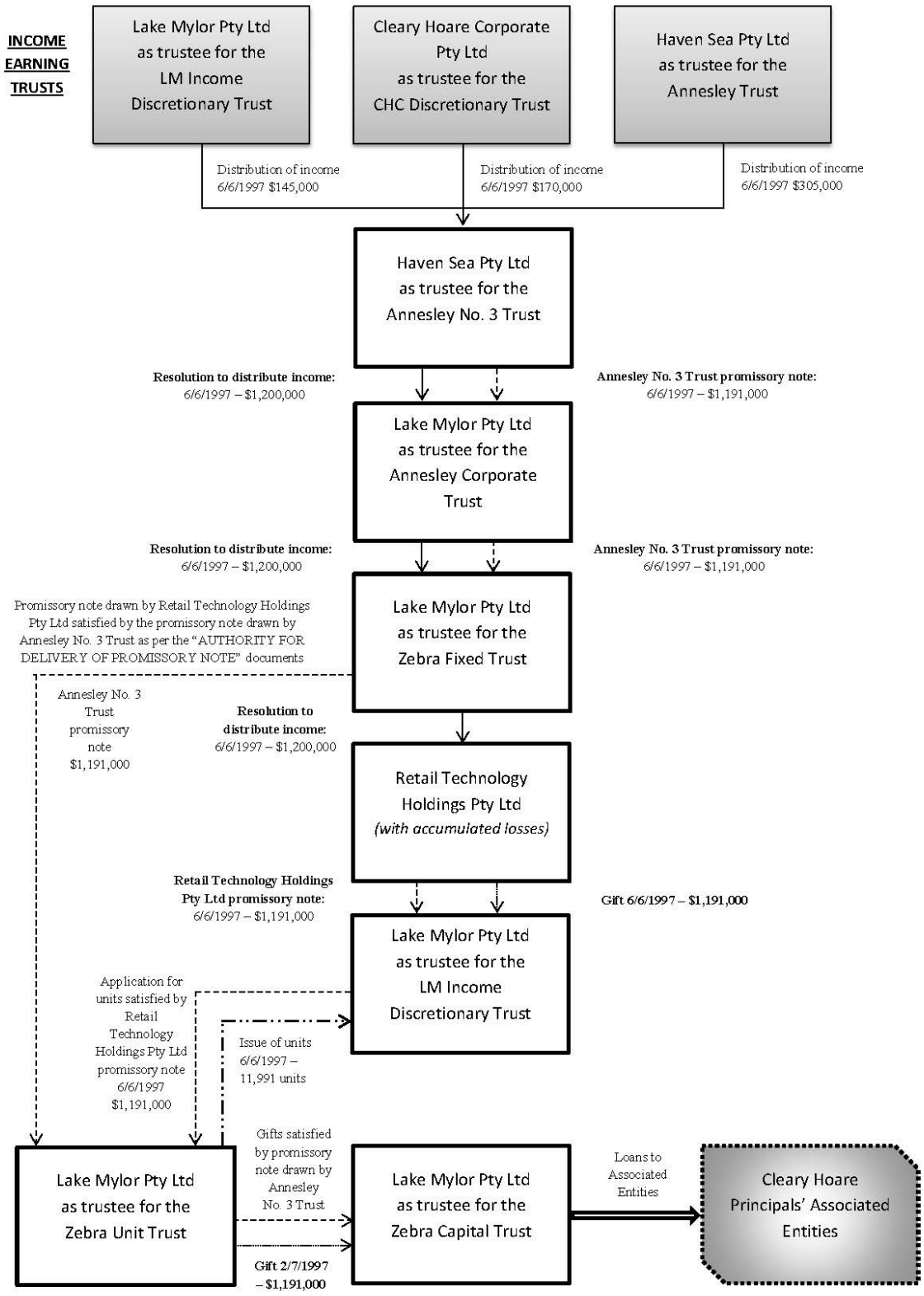
> i. The directors of Lake Mylor Pty Ltd as trustee of the Zebra Unit Trust resolved to make a gift of $700,000 out of capital of the trust to Lake Mylor Pty Ltd as trustee of the Zebra Capital Trust. It was further resolved that the gift be satisfied by way of delivery of a bearer promissory note for $700,000 issued by Haven Sea Pty Ltd as trustee of the Annesley No. 3.
>
> ii. The directors of Lake Mylor Pty Ltd as trustee of the Zebra Capital Trust resolved to accept the gift of capital for $700,000 from Lake Mylor Pty Ltd as trustee of the Zebra Unit Trust. It was further resolved to accept delivery of the bearer promissory note in satisfaction of the gift.
>
> (3) On a date or dates unknown
>
> i. Lake Mylor Pty Ltd as trustee of the Zebra Capital Trust lends $700,000 to Cleary Hoare Principals and associated entities including entities associated with the applicant
>
> ii. who in turn lends a corresponding amount to the applicant.

The Income Earning Trusts NVI Scheme flowchart and transactions narrative

66. The Commissioner's flowchart in relation to the Income Earning Trusts NVI Scheme, remembering the dispute noted above as to the last stage marked "*Loans to Associated Entities*" whereby Mr Hart denied that the evidence demonstrated that he received this money at all, depicted the following:



67. The narrative which the above flowchart depicts from [102] of the Commissioner's third further amended appeal statement is as follows:

(ii) The Income Earning Trusts NVI Scheme

102. Based on the documents and information supplied by the Applicant and his advisers the respondent understands that the Income Earning Trusts NVI scheme comprises the following steps, matters, transactions and events:

(a) On 9 May 1997, the LM Income Trust, the Zebra Fixed Trust and the Zebra Unit Trust were settled.

(b) On 30 May 1997, Annesley No. 3 and the Annesley Corporate Trust were settled.

(c) On 6 June 1997, the following events occurred:

i. The directors of Haven Sea Pty Ltd as trustee of the Annesley Trust resolved to distribute $305,000 to Haven Sea Pty Ltd as trustee of Annesley No. 3.

ii. The directors of Cleary Hoare Corporate Pty Ltd as trustee of the CHC Discretionary Trust resolved to distribute $170,000 to Haven Sea Pty Ltd as trustee of Annesley No. 3.

iii. The directors of Lake Mylor Pty Ltd as trustee of the LM Income Trust resolved to distribute $145,000 to Haven Sea Pty Ltd as trustee of Annesley No. 3.

iv. The directors of Haven Sea Pty Ltd as trustee of Annesley No. 3 resolved to distribute $1,200,000 to Lake Mylor Pty Ltd as trustee of the Annesley Corporate Trust. The resolution stated that the distribution was to be by bearer promissory note drawn by 'the Company' for $1,191,000 with the balance by cheque payable as directed by Lake Mylor Pty Ltd.

v. The directors of Lake Mylor Pty Ltd as trustee of the Annesley Corporate Trust resolved to distribute $1,200,000 to the Zebra Fixed Trust. The resolution stated that the distribution was to be paid forthwith and as to the amount of $1,191,000 by delivery of a bearer promissory note received by Annesley Corporate Trust from Annesley No. 3 to the Trustee of the Zebra Fixed Trust or as otherwise directed by it.

vi. The directors of Lake Mylor Pty Ltd as trustee of the Zebra Fixed Trust resolved to distribute $1,200,000 to the fixed beneficiary (being Retail Technology Holdings Pty Ltd). The resolution stated that the distribution was to be paid forthwith and as to the amount of $1,191,000 by delivery of a bearer promissory note received by Annesley Corporate Trust to the fixed beneficiary or as otherwise directed by it.

vii. A bearer promissory note was issued by Haven Sea Pty Ltd as trustee of the Annesley No. 3 Trust for $1,191,000. Receipt of the bearer promissory note is acknowledged by Lake Mylor Pty Ltd as trustee of the Annesley Corporate Trust and Lake Mylor Pty Ltd as trustee of the Zebra Unit Trust.

viii. An 'AUTHORITY TO PAY' was issued by Lake Mylor Pty Ltd as trustee of the Annesley Corporate Trust authorising

and directing Haven Sea Pty Ltd as trustee of the Annesley No. 3 Trust to pay $9,000 to the Cleary Hoare Trust Account.

ix. By letter from Retail Technology Holdings Pty Ltd to Lake Mylor Pty Ltd it advised that it has decided to make a gift of $1,191,000 to Lake Mylor Pty Ltd in its capacity as trustee of the LM Income Trust.

x. A bearer promissory note was issued by Retail Technology Holdings Pty Ltd for $1,191,000. Receipt of the bearer promissory note is acknowledged by Lake Mylor Pty Ltd as trustee of the LM Income Trust and Lake Mylor Pty Ltd as trustee of the Zebra Unit Trust.

xi. The directors of Lake Mylor Pty Ltd as trustee of the LM Income Trust resolved to accept the gift of $1,191,000 from Retail Technology Holdings Pty Ltd by way of delivery of a bearer promissory note drawn by Retail Technology Holdings Pty Ltd. It was further resolved to subscribe for 11,991 'B' units at $100 each in the Zebra Unit Trust with the promissory note to be delivered in satisfaction of the application monies.

xii. Lake Mylor Pty Ltd as trustee of the LM Income Trust made application for 11,991 units in the Zebra Unit Trust with payment of the application monies by means of delivery of the bearer promissory note drawn by Retail Technology Holdings Pty Ltd.

xiii. The directors of Lake Mylor Pty Ltd as trustee of the Zebra Unit Trust noted that an application for units had been received from Lake Mylor Pty Ltd as trustee of the LM Income Trust for 11,991 units at $100 each together with the bearer promissory note referred to in the application in satisfaction of the application monies. It was resolved to accept the promissory note of $1,991,000, issued by Retail Technology Holdings Pty Ltd as payment in satisfaction of the application monies and to issue units.

xiv. Lake Mylor Pty Ltd as trustee of the Zebra Unit Trust issued a unit certificate for 11,991 'B' units to Lake Mylor Pty Ltd as trustee of the LM Income Trust.

xv. The directors of Lake Mylor Pty Ltd as trustee of the Annesley Corporate Trust noted that it had as the trustee of the LM Income Trust received a gift of $1,991,000 from Retail Technology Holdings Pty Ltd. It was further noted that Retail Technology Holdings Pty Ltd was the fixed beneficiary of the Zebra Fixed Trust with the result that the Zebra Fixed Trust qualified as a beneficiary of the Annesley Corporate Trust. It was also noted that the Annesley Corporate Trust had received a[n] interim income distribution from Annesley No. 3 of $1,200,000 of which $9,000 was by way of cheque payable as directed and the balance by delivery of a bearer promissory note. It was further resolved to make an interim income distribution of

$1,200,000 to the Zebra Fixed Trust by delivery of the promissory note to the trustee of the Zebra Fixed Trust or as otherwise directed by it.

xvi. The directors of Lake Mylor Pty Ltd as trustee of the Zebra Fixed Trust noted that the trust had received an interim income distribution from the Annesley Corporate Trust of $1,200,000 of which $1,191,000 had been paid by delivery of a bearer promissory note. It resolved to:-

> make a[n] interim distribution of income in the amount of the above total to the fixed beneficiary to be paid forthwith as to the amount of the promissory note by delivery of the promissory note to the fixed beneficiary or as otherwise directed by it.

xvii. An undated document, titled 'AUTHORITY FOR DELIVERY OF PROMISSORY NOTE' addressed to Lake Mylor Pty Ltd as trustee of the Annesley Corporate Trust and Lake Mylor Pty Ltd as trustee of the Zebra Fixed Trust from Retail Technology Holdings Pty Ltd and Lake Mylor Pty Ltd as trustee of the LM Income Trust in regard to the distributions of income from the Annesley Corporate Trust:-

- authorised the promissory notes issued by Haven Sea Pty Ltd as trustee of the Annesley No. 3 to be delivered to Lake Mylor Pty Ltd as trustee of the Zebra Unit Trust;
- in satisfaction of the obligations arising under the bearer promissory note for the same amount drawn by Retail Technology Holdings Pty Ltd and delivered by Lake Mylor Pty Ltd as trustee of the LM Income Trust to Lake Mylor Pty Ltd as trustee of the Zebra Unit Trust in respect of the application for 'B' units in the Zebra Unit Trust;
- to be delivered by the [sic] Lake Mylor Pty Ltd as trustee for the Zebra Unit Trust in respect of any gift it resolves to make to Lake Mylor Pty Ltd as trustee of the Zebra Capital Trust.

xviii. The sum of $9,000 was paid to the BDO Nelson Parkhill Trust Account.

(d) On 30 June 1997 the following events occurred:

i. The directors of Cleary Hoare Corporate Pty Ltd as trustee of the CHC Discretionary Trust resolved to distribute $550,375 to Haven Sea Pty Ltd as trustee of Annesley No 3.

ii. The directors of Lake Mylor Pty Ltd as trustee of the LM Income Trust resolved to distribute $89,625 to Haven Sea Pty Ltd as trustee of Annesley No 3.

iii. The directors of Haven Sea Pty Ltd as trustee of Annesley No. 3 resolved to distribute $700,000 to Lake Mylor Pty Ltd as trustee of the Annesley Corporate Trust. The resolution

stated that the distribution was to be by bearer promissory note drawn by 'the Company' for $700,000 with the balance by cheque payable as directed by Lake Mylor Pty Ltd.

(e) The Zebra Capital Trust was settled on 1 July 1997.

(f) On 2 July 1997, the following events occurred:

i. The directors of Lake Mylor Pty Ltd as trustee of the Zebra Unit Trust resolved to make a gift of $1,191,000 out of capital of the trust to Lake Mylor Pty Ltd as trustee of the Zebra Capital Trust. It was further resolved that the gift be satisfied by way of delivery of a bearer promissory note for $1,191,000 issued by Haven Sea Pty Ltd as trustee of Annesley No. 3.

ii. The directors of Lake Mylor Pty Ltd as trustee of the Zebra Capital Trust resolved to accept the gift of capital for $1,191,000 from Lake Mylor Pty Ltd as trustee of the Zebra Unit Trust. It was further resolved to accept delivery of the bearer promissory note in satisfaction of the gift.

iii. Lake Mylor Pty Ltd, as trustee of the Zebra Unit Trust, resolved to make a gift of $700,000 to Lake Mylor Pty Ltd, as trustee of the Zebra Capital Trust. It was further resolved that this gift be satisfied by delivery of a promissory note issued by Haven Sea Pty Ltd, as trustee of Annesley No. 3.

iv. Lake Mylor Pty Ltd, as trustee of the Zebra Capital Trust, resolved to accept the gift of capital of $700,000. It was further resolved to accept delivery of promissory note in satisfaction of the gift.

(g) On a date or dates unknown:

i. Lake Mylor Pty Ltd as trustee of the Zebra Capital Trust lends $1,191,000 to Cleary Hoare Principals and associated entities including entities associated with the applicant

ii. who in turn makes corresponding payments to or on behalf of the applicant.

68. The sequences of events reproduced above from [102(c)], [102(d)] and [102(f)] of the Commissioner's third further amended appeal statement, and the terms of [102(g)] of that statement (the last stage of the flowchart) were not accepted by Mr Hart. However, the asserted correct sequences were not pleaded and no argument was advanced as to how or why the unstated correct sequences made any difference given that all the events described at [102(c)] took place on 6 June 1997, all the events described at [102(d)] took place on 30 June 1997 and all the events described at [102(f)] took place on 2 July 1997. Moreover, the Commissioner did not in terms ultimately rely upon any particular sequence of events on those days, and Mr Hart did not ultimately dispute any particular sequence of events on those days.

17 Before us, the accuracy of the steps described above, as well as the diagrams setting out the flow of funds, was not disputed by either party.

ASSESSABILITY OF THE PRACTICE AMOUNT

18 The appellant contended below that:

(a) the Outlook Trust became presently entitled to a share of the income of the Practice Trust in the sum of $220,398; and

(b) the trustee of the Outlook Trust lent the appellant $185,698.

19 On appeal, the appellant submitted that there was no evidence that the Practice Trust paid any amount directly to him, though he accepted that the sum of $185,698 was ultimately sourced from the earnings of the Practice Trust. In addition it would appear that the appellant received regular payments in the 1997 income year totalling $97,754. These were described by the primary judge at [141] as follows:

> The Commissioner relied upon the undisputed fact that Mr Hart received regular payments during the 1997 income year totalling $97,754. The Commissioner asserted, and Mr Hart disputed, that these payments ultimately came from the Practice Trust. The sum of $97,754 was arrived at by adding up the following amounts, and the ultimate source was asserted by reference to the following surrounding circumstances:
>
> (1) $49,415.52 by way of 22 fortnightly deposits of $2,246.16 by Cleary Hoare into a joint account held by Mr Hart and his wife with Suncorp Bank, with accompanying narrations "*Cleary Hoare Pay Pay*", "*Cleary Hoare Pay*" or "*Cleary Hoare Sol Pay*" between at least 5 July 1996 and 23 April 1997;
>
> (2) $6,738.48 by way of three fortnightly payments of $2,246.16 made by the Outlook Trust bank account to the same joint bank account, which given the identical amount for each deposit should be inferred as having been ultimately sourced from the net income of the Practice Trust and paid to the Outlook Trust bank account for on payment to the joint account at the direction of Mr Hart and for his benefit;
>
> (3) $35,200 by way of 22 deposits of $1,600 with accompanying narrations "*Cleary Hoare Pay*" or "*Cleary Hoare Sol Pay*" by Cleary Hoare into an account in the name of Oak Arrow Pty Ltd, the directors of whom were Mr Hart and his wife and which was the trustee of the Oak Arrow Trust, supporting the inference that this money was paid by, or at the direction of, the Trustees of the Practice Trust at Mr Hart's direction and for his benefit into the Oak Arrow account; and
>
> (4) $6,400 by way of four fortnightly payments of $1,600 made from the Outlook Trust bank account into the Oak Arrow bank account, supporting the inference that these payments, like the earlier and matching payments from Cleary Hoare, were ultimately sourced from the net income of the Practice Trust and were paid to the Outlook Trust bank account at the direction of Mr Hart and for his benefit.

20 The primary judge was satisfied that the majority of this amount ($84,615.52), formed part of the appellant's assessable income. This was largely because the appellant could give no adequate explanation about the nature of the amounts deposited into bank accounts he either owned or controlled. The exact relationship between the sum assessed ($220,398), the sum admitted to have been received (said to have been a loan ($185,698)), and the sum of $84,615.52 paid into the bank accounts owned or controlled by the appellant, is perhaps, a little unclear. That lack of clarity is probably reflected in the state of the evidence. On appeal, the Commissioner submitted that the sum of $84,615.52 formed part of the amount assessed which also included the sum of $185,698. The aggregate of these two figures exceeded, he submitted, the amount assessed which had been determined by reference to the Outlook Trust's share of the earnings of the Practice Trust as alleged by the appellant. The appellant did not specifically address this issue, other than to contend that he was lent monies by the Outlook Trust, and denied receiving monies from the Practice Trust, although he led no evidence to demonstrate this. Given that many of the payments made into his bank account were described as "Cleary Hoare Pay", it was open to the trial judge to infer that the appellant did receive funds directly from the Practice Trust because this trust owned Cleary Hoare. In any event, other than the loan issue, no serious challenge was mounted by the appellant against the primary judge's conclusion at [147] that he had failed to prove that he did not derive at least $220,398.

21 It is convenient to address the loan issue first. The evidence supporting the existence of a loan was scant. It was undocumented, no payments of principal or interest had ever been made, its terms were never identified, and the appellant's capacity to repay the loan if it existed, appeared from inception to be either non-existent or negligible given his intention never to derive beneficially any income. No evidence addressing a capacity to repay the loan was ever led by the appellant.

22 The existence of the loan was asserted by the appellant in his witness statement, but that assertion was not evidence of its existence. He did not depose to any conversations or meetings or to any other fact which had taken place in 1997 in support of his contention. No other witness was called to corroborate the existence of the loan. The appellant instead pointed to the books of account of the Outlook Trust and resolutions of the trustee of that trust which refer to or acknowledge the existence of a loan. This entity was, of course, under

the control of the appellant. The primary judge found that these documents assumed the existence of a loan rather than directly proving its existence.

23 The primary judge decided that the appellant had not discharged his onus of demonstrating that any loan existed in the 1997 year of income. For that purpose, he declined to make any adverse finding about the appellant's credibility although he was invited to do so by the Commissioner. His Honour simply preferred to decide that the appellant had failed to discharge his onus of proof.

24 In support of the primary judge's finding, the Commissioner relied upon the overall lack of evidence supporting the existence of a loan and the objective circumstances such as the failure to make any repayments of principal. He also relied upon contemporaneous bank statements which recorded many of the payments received by the appellant or paid into accounts he controlled as "pay" or "sol[icitor] pay" which were made on a fortnightly basis. These were described in the judgment below at [141].

25 More significantly, the Commissioner relied below upon certain documents arising out of a request made in 1999 to the appellant's bank for loans which were to be used to purchase two investment properties by Rio Villa Pty Ltd as trustee for the Rio Villa Trust, a trust controlled by the appellant. The documents were described by the primary judge at [111] as follows:

> (1) an undated "*Credit Approval Request*" form (**CAR form**) of eight pages, with handwriting having the appearance of two writers - the application is made in the name of "*Rio Villa P/L as Trustee for Rio Villa Trust*", with the solicitor being named as Cleary Hoare and the contact person being Mr Hart;
>
> (2) a form of six pages which is printed with the title "*Application for a Loan/Limit*", above which is handwritten "**PERSONAL DETAILS*", undated, in the name of Mr Hart and his wife and apparently signed by them (**personal details form**) – that form contains certain identical financial information to the CAR form, namely of a net monthly income of $8,333 and appears to have been completed by the same person as one of the authors of the CAR form; and
>
> (3) a typewritten "*CREDIT DEPARTMENT, BANKING SERVICES FATE ADVICE*", in respect of a CAR received on 29 July 1999, dated 13 August 1999, and approved by a handwritten note by a named bank officer dated 13 August 1999 (**approval form**).

26 The primary judge inferred in all the circumstances that the appellant was the source of the information contained in the three documents. This included statements that the appellant owned one third of Cleary Hoare, that Cleary Hoare was paying him around $220,000 per

annum, that his personal taxable income was $220,000 gross, and that, as identified as "applicant number 1", his net fortnightly income after tax was $3846 or $8333 per month. In particular, one of the forms records under the heading "Income details – Self Employed Applicants" net profit before tax for the 1997 year of income of $220,398, being the precise amount assessed by the Commissioner and said by the appellant to have been distributed to the Outlook Trust by the Practice Trust.

27 The primary judge concluded, based upon the contents of these documents, that the appellant was prepared to have the money that was in fact paid to him in the 1997 income year represented as his income to the bank for loan approval purposes. The primary judge was not prepared to conclude, on the balance of probabilities, that the appellant was seeking to mislead his bank. Rather the better view was that what was represented to the bank was the underlying truth, even if a different characterisation was now being advanced for a fiscal advantage.

28 On appeal, the Commissioner relied upon an additional consideration, namely that if the amounts paid to the appellant were really loan advances, the appellant would have made clear representations to his bank that he was significantly indebted to the Outlook Trust to enable the bank to assess his creditworthiness. There are, however, no such representations contained in the bank forms.

29 On appeal, the appellant submitted that the trial judge erred when he inferred that the information recorded in the bank forms was sourced from the appellant. That finding, it was said, should be set aside as it had no evidentiary basis. In that respect, the appellant emphasised that the forms in question were not the appellant's documents, that the authors of their contents had not been identified, and that the Commissioner's reliance on them was misplaced. His case, it was said, rose no higher than speculation. The appellant submitted that the only form which contained clear representations from him was two pages which were attached to a Suncorp–Metway Limited "FATE advice" from 1998 which recorded the following:

> Outlook Crescent Pty Ltd as trustee of the Outlook Practice Trust owns one third of the practice of Cleary Hoare, Solicitors. It normally derives income in the order of $200,000.00 per year from that source.

The only basis for contending that the attached two pages were sourced from the appellant was said to be the footer on each of the two pages which contained the phrase "MJH personal". Based on this, the Court was asked to infer that the appellant was the author of the

document. The appellant then submitted that the better inference to be drawn from the documents in the light of that "FATE advice" representation was that the bank employees had misunderstood what the appellant had represented to them, and that the references to the income being that of the appellant was a mistake made on the part of those employees.

30 We are prepared to infer that the 1998 attachment was prepared by or at the direction of the appellant. However, in and of itself, it does not justify the inference that all of the other representations made and recorded on the other bank forms were not accurately sourced from the appellant and were instead misunderstandings on the part of the bank's employees. In our view, the recording of the exact amount said to have been distributed by the Practice Trust to the Outlook Trust, namely the sum of $220,398, gives one considerable confidence from which to infer that the source of all the other financial information recorded in the forms was the appellant and that it was recorded accurately.

31 The primary judge addressed the two-page attachment relied upon by the appellant in these terms (at [124]):

> That earlier 1998 document also referred to the net profit for the Practice Trust for the following 1998 income year of $750,000 being "*distributed between three partners*" and also made references to "*Trust income generated by Cleary Hoare*" and "*net profits of Solicitor firm*". The language use suggests that the suggestion of loans to account for money received was taken to be a matter of form rather than substance by the bank, rather than constituting any proof of a loan in fact existing. The language used is consistent with the bank treating that money as being, in substance and reality, income available to be taken into account for credit assessment purposes, rather than as constituting competing financial obligations detracting from creditworthiness.

At par [126], the primary judge said:

> The contents of the CAR form significantly undermine Mr Hart's case that, contrary to what he must have represented to the bank as to the reality of his situation, the money he received from the Outlook Trust in the 1997 income year was really the product of a loan arrangement as opposed to ordinary income at his disposal. The nature and content of his representations to the bank must be given due weight, especially in circumstances when he had the opportunity in this Court to disown what was recorded by the unknown bank officer writing on the unsigned CAR form in a manner that is consistent with the bulk of the financial information (as opposed to calculations) being provided by him. While Mr Hart went some way towards this, he did not confront the real burden and substance of the bank record evidence.

32 In our view, it was entirely open to the primary judge to conclude that the appellant, in substance and in reality, told his bank that the money was his. The inferences his Honour drew from the bank documents were rational and were not defeated by the two page

attachment. It could not be said, as the appellant contended, that the findings of the primary judge here were not open because there was no evidence to support them. We reject that submission. In our view, the findings were supported by contents of the bank forms. They are also supported by the complete absence of any reference to any suggested liability to the Outlook Trust.

33 It was also proper for the primary judge to have regard to the objective circumstances including the lack of repayment and the lack of documentation. In *Richard Walter Pty Ltd v Federal Commissioner of Taxation* (1996) 67 FCR 243, very similar objective factors were relied upon in finding that the loan alleged in that case was a sham. They included the following:

(a) the fact that the alleged loan was undocumented apart from book entries made by account staff;

(b) a lack of evidence concerning the terms and conditions upon which monies were said to have been lent or repaid;

(c) the fact that it did not appear that any interest had ever been charged;

(d) the taxpayer's control over the movement of monies within entities it controlled;

(e) an objective incapacity by the purported borrower to repay the amounts said to have been advanced.

It follows that the appellant has failed to demonstrate that he did not receive the funds paid to him beneficially.

34 It should be noted that the appellant also submitted that it was inherently improbable that an experienced tax lawyer, wanting to avoid fiscal liability, would subsequently have subjectively intended not to have created a loan obligation. He was, after all an architect of the NVI Scheme, the fiscal efficacy of which was dependent upon the taxpayer not deriving any income, but instead being lent funds. This submission evokes an observation of the New Zealand Court of Appeal in *Accent Management Limited v Commissioner of Inland Revenue* [2007] NZCA 230 at [63], in the context of an allegation of sham:

> Whether these transactions are shams depends primarily on the states of minds of Dr Muir and Mr Bradbury as to their genuineness. Given that it is not to their advantage that the transactions be shams, it might be thought a little perverse to attribute to them states of mind which are inconsistent with their best interests.

(Cited by Edmonds J in *Normandy Finance and Investments Asia Pty Ltd v Federal Commissioner of Taxation* [2015] FCA 1420 at [61]).

35 Whilst the appellant's determination not to derive income and pay tax may be accepted, it nonetheless is not sufficient to displace the finding of fact made below, based as it was on the contemporaneous banking documents and the objective circumstances including the history of repayments of principal and interest. The primary judge was well aware of the appellant's strongly held fiscal intention, but his Honour nonetheless found that the appellant ultimately treated the money paid to him as his own, and represented this as such to his bank. In other words, he simply failed to implement his fiscal objectives: cf *Raftland Pty Ltd v Federal Commissioner of Taxation* (2008) 238 CLR 516 at [58].

36 The primary judge was also criticised for not requiring the Commissioner to plead and prove sham: cf par [133]. That submission is misconceived. First, where sham is an issue in a tax case there is no onus on the Commissioner to prove it, although he is required to identify what he considers to be the real underlying transaction. As Hill J said in *Richard Walter Pty Ltd v FCT* at [259]:

> Even if it had been necessary to determine whether the so called loan transactions were shams, the onus could not have been on the Commissioner to show what the real transaction was, of which the payments formed part. Once sham is alleged by the Commissioner, he may then come under some factual obligation to identify the real transaction for which it is contended that the apparent transaction is but a disguise…

37 Secondly, it was entirely proper and open to the Commissioner to put his case based upon a failure on the part of the taxpayer to discharge the onus of proof imposed by s 14ZZO of the *Taxation Administration Act 1953* (Cth). As Brennan J, as his Honour then was, observed in *Federal Commissioner of Taxation v Dalco* (1990) 168 CLR 614 at 624:

> If the Commissioner and the taxpayer agreed to confine an appeal to a specific point of law or fact on which the amount of the assessment depends, it will suffice for the taxpayer to show that he is entitled to succeed on that point. Absent such a confining of the issues for determination, the Commissioner is entitled to rely upon any deficiency in proof of the excessiveness of the amount assessed to uphold the assessment, though the taxpayer is limited to the grounds of his objection.

Earlier, his Honour observed, at 621:

> The burden which rests on a taxpayer is to prove that the assessment is excessive and that burden is not necessarily discharged by showing an error by the Commissioner in forming a judgment as to the amount of the assessment.

That observation is particularly pertinent to the case put by the taxpayer here.

38 Thirdly, the Commissioner did identify what he considered to be the real transaction. He said it was a distribution of trust income to the appellant by the Practice Trust, or, alternatively by the Outlook Trust. Having done this, it was a matter for the taxpayer to discharge his onus of proving that there was a loan. Even if sham had been alleged, in our view, the task of the taxpayer would have remained almost exactly the same. He needed to prove positively that he either did not derive the amount assessed, or that he did not otherwise receive it beneficially.

39 The next issue for determination was whether the sums paid to the appellant were assessable income. The primary judge held that the amount assessed was income because it was either a distribution to the appellant from the Practice Trust or alternatively from the Outlook Trust, with present entitlement arising pursuant to ss 95A(1) or 101 of the 1936 Act, or pursuant to the terms of the deeds of the Practice Trust or Outlook Trust, or because of a specific resolution of the Practice Trust. In relation to the first basis for present entitlement, his Honour accepted (at [143]) the following submission made by the Commissioner:

> The Commissioner contended that, as discussed above, in addition to the terms of the trust deed, and to like effect, the operation of ss 95A and 101 of the *ITAA 1936* can be triggered by the fact of payment taking place, such that the payments above were sums that Mr Hart was presently entitled to once the loan characterisation was not accepted.

40 In relation to the second basis for present entitlement, the primary judge referred to cl 14 of the Practice Trust Deed and cl 3 of the Outlook Trust Deed and in relation to that deed concluded at [152]:

> The Commissioner's closing written submissions asserted, and I accept, that in accordance with the portions of clause 3 of the Outlook Trust deed reproduced above, Mr Hart acquired a vested and indefeasible interest in the amounts that were actually paid to him or to his benefit by Outlook Crescent Pty Ltd as trustee for the Outlook Trust during the 1997 income year, and was presently entitled to those amounts for the purposes of s 97 of the *ITAA 1936*.

41 In relation to the third basis for present entitlement, his Honour also accepted the submission put to him by the Commissioner that there existed an express resolution distributing a share of the income of the Practice Trust directly to the appellant in his capacity as a Special Unitholder in that trust. This submission was described at [144] as follows:

> The Commissioner's case in the alternative was that a resolution dated 30 June 1997 by the trustees of the Practice Trust provided that income for the year ended 30 June 1997 be applied to special unitholders, including any interim distributions, in the amounts paid or advanced during that income year. As noted earlier, Mr Hart was a special unitholder. It was submitted that therefore he was presently entitled to the amounts paid to him or on his direction for his benefit (being a portion of the income of the Practice Trust) by reason of the resolution.

42 The resolution of the Practice Trust relied upon by the Commissioner provided:

> IT WAS RESOLVED that income for the year ended 30 June 1997 be applied to Special Unitholders (including interim distributions to them, if any, during the year) in the amounts paid or advanced to them during the year.

As already mentioned, the appellant denies, notwithstanding that he was a Special Unitholder, that the Practice Trust paid him anything, but led no evidence as to whether an amount, and if so what amount, had been paid or advanced to the Special Unitholders pursuant to this resolution. He submitted that there was no evidence before the primary judge which demonstrated that money had in fact been advanced or paid to the appellant by the Practice Trust. However, the onus was on the appellant to demonstrate on the balance of probabilities that this was so. It was for the appellant to explain the presence and meaning of the resolution. He did not do so. Absent an explanation, inferentially, amounts were paid or advanced by the Practice Trust to the Special Unitholders, thus explaining the making of the resolution. In our view, it was open to the primary judge to find that the appellant received the full amount assessed, as a distribution in fact made by the Practice Trust. It was entirely open for his Honour to make such findings given the contents of the bank statements tendered into evidence described at [141] in the judgment below, and the appellant's positive contention that he was paid $185,698 by the Outlook Trust. The appellant's contention that there was no or insufficient evidence to support this finding is rejected.

43 On appeal, the appellant also submitted that the foregoing conclusion was inconsistent with the express resolutions to distribute income made by the Practice Trust and the Outlook Trust. Those resolutions, it was said, were to make distributions to beneficiaries other than the appellant. Absent a finding of sham, which was not contended for, the resolutions took effect in accordance with their tenor.

44 That submission faced an immediate difficulty, namely, that the appellant was unable to identify or produce to the Court any other resolution of the Practice Trust save for the one

concerning the Special Unitholders described at [42] above. He was unable to identify any resolution of the Practice Trust distributing income to the Outlook Trust.

45 The resolution of the Outlook Trust, which the appellant contended was inconsistent with the receipt by him of any distribution, is dated 27 June 1997 and is in these terms:

> IT WAS RESOLVED to appoint all the income of the Trust for the year ended 30th June 1997 to and for the benefit of the Trust known as Annesley No. 3 Trust, noting that that Trust is a beneficiary of the Outlook Practice Trust.

It will be recalled that the Anneley No 3 Trust was the first new trust in the NVI Scheme. The presence of the resolution does not address, in our view, the findings made by the primary judge that the appellant had not shown that he had not derived, beneficially, the amount assessed. It may evidence an attempt to implement the NVI Scheme. We say "attempt to implement" because, as already mentioned, a resolution from the Practice Trust to distribute income to the Outlook Trust, which might have been the first step in the NVI Scheme, was never produced, and the evidence set out above, which appears to show that monies were paid by the Practice Trust directly into bank accounts owned or controlled by the appellant, was expressly contrary to the design of the NVI Scheme.

46 It follows that the primary judge did not err in concluding that the amount beneficially derived by the appellant was probably a distribution by the Practice Trust to him as a Special Unitholder, and assessable as such.

47 As an alternative, the Commissioner relied upon s 95A or, alternatively, s 101 of the 1936 Act. In essence, this submission was that the appellant, having being paid the sum assessed, was thereby deemed to have become presently entitled to a share of the income of either trust pursuant to either of those provisions. Section 95A(1) at the time provided:

> **95A. Special provisions relating to present entitlement**
>
> (1) For the purposes of this Act, where a beneficiary of a trust estate is presently entitled to any income of the trust estate, the beneficiary shall be taken to continue to be presently entitled to that income notwithstanding that the income is paid to, or applied for the benefit of, the beneficiary.

Section 101 at the time provided:

> **101. Discretionary trusts**
>
> For the purposes of this Act, where a trustee has a discretion to pay or apply income of a trust estate to or for the benefit of specified beneficiaries, a beneficiary in whose favour the trustee exercises his discretion shall be deemed to be presently entitled to the amount paid to him or applied for his benefit by the trustee in the exercise of that

discretion.

48 The submission found favour below. If it matters, and with great respect to the primary judge, if what his Honour accepted was that the mere act of payment legally creates present entitlement, then we are unable to agree with it.

49 Below, and after considering a number of authorities, including the decision of Hill J in *East Finchley Pty Ltd v Federal Commissioner of Taxation* (1989) 90 ALR 457, the primary judge said at [86]:

> The burden of the above passages is that if the trustee of a discretionary trust exercises a discretion to pay or apply the income of the trust estate to or for the benefit of a beneficiary prior to the end of a given income year, the beneficiary will be presently entitled to that share of the income under s 97. If instead only a mere payment is made to the beneficiary prior to the end of the income year, s 95A(1) operates to deem the beneficiary to continue to be presently entitled to the income, so that s 97 continues to apply. In this way, in certain circumstances s 95A(1) overcomes the problem posed by the concepts of vested in interest and vested in possession operating to deny the necessary present entitlement. It helps to ensure, at least in some situations, that there is no advantage for tax purposes in merely making payments or advances rather than formal distributions.

50 In relation to s 101, the primary judge said at [89]:

> Thus the operation of s 101 is that, when a trustee of a discretionary trust has exercised a discretion to pay or apply the income of the trust estate to or for the benefit of a beneficiary, that beneficiary is deemed to be presently entitled to the amount so paid, including for the purposes of s 97(1).

51 The passage from *East Finchley*, relied upon by the primary judge for the conclusion he expressed at [86] concerning s 95A, is as follows (at 477):

> A discretionary trust deed may provide a discretion in the trustee to determine, in respect of the income of a particular year, who among a class of beneficiaries is to be entitled. If that determination were made prior to 30 June in a year of income and was irrevocable the consequence would be under s 98 that there would be as at the end of the year of income (that being the relevant time to determine the issue) present entitlement under s 97. There would be no need to have any deemed present entitlement in such a class of case assuming, for present purposes, that there had been no payment of any amount to the beneficiary. In the class of case where there had been a payment, then s 95A(1) would deem the beneficiary to continue to be presently entitled to the income and thus keep s 97 of the Act applicable: cf per Barwick CJ in *Union-Fidelity Trustee Co of Australia Ltd v FCT* [1969] HCA 36; (1969) 119 CLR 177 at 182.
>
> Where on the other hand a discretionary trust deed provides that the trustee has a

> discretion to pay or apply income of the trust estate to or for the benefit of beneficiaries at his discretion and where there has been a payment there would not (at least in the absence of s 95A(1) which was introduced in 1979) be present entitlement at the end of the year of income, nor in the event that income had been applied in favour of a beneficiary would there have been such present entitlement because, looking at the matter as at the end of the year of income, there would have been no right in the beneficiary to sue the trustee for his share of income, that right having been satisfied by the payment or application already made under s 101. Thus it is doubtful that s 101 was intended to cover the entire field. For almost all purposes (and perhaps indeed for all purposes) it will be irrelevant whether a beneficiary is presently entitled under s 97 or 98 or merely deemed to be presently entitled by force of s 101.

52 With respect, in our view, this passage does not support the proposition that where a trustee makes a payment to a beneficiary before the expiration of a year of income, the beneficiary is thereby taken thereafter, by reason of s 95A, to be presently entitled to that income for the purposes of s 97(1). Rather, in our view, s 95A exists to ensure that a beneficiary, who is already presently entitled to a share of the income of a trust estate, does not cease to be so presently entitled, because at some point thereafter, but before the expiration of the year of income, he or she is paid their entitlement.

53 Section 95A was introduced by the *Income Tax Assessment Amendment Act 1979 No.12, 1979*. The explanatory memorandum which accompanied the introduction of that Act relevantly states:

> Proposed section 95A is intended to remove any doubts that may exist that trust income *to which a beneficiary is otherwise presently entitled* in respect of a year of income does not, for the purposes of those provisions of the income tax law that turn on whether a beneficiary is presently entitled to income of a trust estate, cease to be income of that kind because the income concerned has been paid to or applied for the benefit of the beneficiary.
>
> (Our emphasis)

The "doubts" referred to in the sentence above, presumably arose from the following statement of Barwick CJ in *Union-Fidelity Trustee Co of Australia Limited v Federal Commissioner of Taxation* (1969) 119 CLR 177 where his Honour said at 182:

> In applying the provisions of Div. 6 a clear distinction must be maintained between the position of a person who is entitled to receive a share of the estate and one who has been paid the amount of it. When a beneficiary has been paid his share of the income of the estate in respect of a tax year he no longer satisfies the description of a beneficiary who is entitled to a share of the net income of the estate for that year. Thus, if at the close of the taxation year the appropriate share of the income of the trust estate has been already paid to the beneficiary who before the payment was merely entitled to it, the amount so paid to the beneficiary as his share of that income

> will form part of his assessable income by virtue of s. 26 (b) and not, in my opinion, by reason of s. 97.

54 Former s 26(b) of the 1936 Act included in the assessable income of a taxpayer a beneficial interest in income derived under, amongst other things, an instrument of trust.

55 The mischief which s 95A addresses, as explained by the Explanatory Memorandum, is the loss of present entitlement following payment to a beneficiary by the trustee of that entitlement. It is not directed at creating present entitlement. In our view the ordinary and natural meaning of the language used by s 95A aptly addresses that mischief. The operation of the provision is conditional upon the following state of affairs: – "where a beneficiary of a trust estate is presently entitled to any income of the trust estate". It then provides that the beneficiary "shall be taken to continue to be presently entitled" to the income notwithstanding that it has already been paid or applied for the benefit of that beneficiary. The act of payment or advancement does not make a beneficiary, who is not otherwise presently entitled to a share of the income of the trust estate, so presently entitled. Rather, the act of payment creates a fiction whereby a beneficiary, who was already presently entitled, does not cease to be so for the purposes of s 97 because they are paid out their entitlement prior to the expiration of the year of income.

56 Similarly, in our view s 101 does not deem present entitlement by reason of an act of payment absent some resolution or determination of the trustee of a trust to make that distribution or payment. It operates, not upon the act of payment, but upon the exercise of a discretion by a trustee. Practically, it probably is only operative where distributions are made to those who have a legal disability. That is why Gummow J made the following observation in *Federal Commissioner of Taxation v Vegners* (1989) 90 ALR 547 at 552:

> Section 101 of the Act has the result, with regard to discretionary trusts, that where the power in question is vested in the trustee and the trustee exercises the discretion in favour of an object of the power, then that person is deemed to be presently entitled to the amount paid to him or applied for his benefit. In the case of objects of the power who were *sui juris*, s 101 would, in such cases, add little to what would already be the work done by s 97 of the Act.

In other words, where a discretionary beneficiary is not under legal disability, and a trustee exercises a power to pay or advance funds to that beneficiary, s 101 adds little to s 97.

57 The language of s 101 supports the conclusion that a mere act of payment by a trustee to a beneficiary is not sufficient to make that beneficiary entitled to that income. First, the provision is conditioned upon the existence of a discretion to pay or apply income of the trust

for the benefit of specified beneficiaries. It then provides that where there is a beneficiary "in whose favour the trustee exercises the trustee's discretion", the beneficiary thereafter shall be deemed to be presently entitled to the amount paid to them or applied for their benefit. In our view, the provision is not engaged unless and until it can be shown that the trustee has in fact exercised its discretion to make a payment to a specified beneficiary. Normally that would occur by written resolution, although we accept that the exercise of discretion could be evidenced in other ways.

58 The third alternative basis for present entitlement arose out of clauses of the Practice Trust Deed which the Commissioner contended made the appellant presently entitled to a share of the income of that Trust in the sum assessed. Clause 14 of the deed addressed the power to make of the trustee distributions of income in each year and cl 14.7 provided:

> It is declared that each of the unit holders whose favour the trustee shall pay, apply or set aside the whole or a part of the net income all the whole or a part of the additional tax income of the trust fund for that year or failing and effective community accumulation who shall be entitled to share in the amount of such accumulation for that year as his hearing provided shall have an immediate infeasible vested interest in that part of the net income or additional tax income all the amount of such accumulation for that year twitch that unit holder is entitled hereunder, it being the express intention of the set law (as the trustee acknowledges) the such of the unit holders in whose favour the trustee shall pay, apply or set aside the said net income for the said additional tax income or failing and effective community accumulation who shall be entitled to share in the amount of such accumulation as hearing provided shall be presently entitled to his or her share of such net income additional tax income or the amount of such accumulation.

59 If it be necessary to do so, we would agree with the Commissioner's submission that cl 14.7 caused the appellant to become presently entitled to a share of the income of the Practice Trust upon payment being made to him by that trust.

60 Below, the Commissioner had also submitted that some, or all, of the amount assessed was a distribution from the Outlook Trust. He did so, we infer, because it was not clear to what extent payments were made to the appellant by either the Practice Trust or the Outlook Trust. For that purpose he relied upon cl 3.8 of the Outlook Trust Deed which is very similar to cl 14.7 of the Practice Trust Deed above. It renders a beneficiary presently entitled to the share of income paid by a trustee to her or him. The primary judge found (at [154]), that the appellant was probably assessable on this basis, at least in the sum of $185,698. On appeal, as at first instance, the focus of the appellant was not on the source of distribution – Practice or Outlook Trust – but on whether he had been lent monies.

61 In our view, there is yet another basis upon which it may properly be concluded that the amounts received by the appellant were impressed with the character of income for the purposes of s 25(1) of the 1936 Act (now s 6-5 of the *Income Tax Assessment Act 1997* (the "1997 Act")). That is because, the objective circumstances of their receipt show that the amount derived was likely to have been the product of the appellant's work as a solicitor and was also relied upon by him for his ordinary expenditure. In that respect, we emphasise that, other than contending that there was a loan, no other evidence was led by the appellant concerning the true character of the amounts he received, and no explanation was given concerning the other amounts found to have been paid to him and described at [141] below. The objective circumstances here are:

(a) the fact of receipt of monies by the appellant (the $185,698 and the $84,615.52), which included the making of regular payments described in the court below at [141]. Some of these were described in the bank statements of the appellant as "pay" or "sol pay";

(b) the money was sourced from the earnings of the Practice Trust or possibly the Outlook Trust. That is conceded in relation to the $185,698 and may, in our view, be inferred for the sum of $84,615 from the descriptions which appeared in the bank accounts;

(c) the appellant worked to secure the earnings of the Practice Trust by acquiring and then selling legal services to clients of Cleary Hoare. The sum assessed of $220,398 is equal to what was said by him to be the share of the income of the Practice Trust payable to his family discretionary trust, namely the Outlook Trust;

(d) the appellant did not identify the receipt by him of any other income which might have been used by him to fund his daily expenditure. When pressed on this issue on appeal, the appellant said that there was no evidence that he had or did not have other sources of income, although it was admitted that his tax return for the 1997 year of income disclosed only $100 of income. Counsel for the appellant said, quite properly, that one could assume that the appellant spent the money said to have been advanced to him on "everyday expenses" or for the purpose of investment.

62 Given these circumstances, we are satisfied that the appellant has not discharged his burden of showing that what was paid to him was not income according to ordinary concepts. We infer that what was received was his reward for the provision by him of legal services and was provided to him to fund his daily living expenses. For reasons which follow, the latter finding is sufficient to render what was received as assessable income.

63 In *Federal Commissioner of Taxation v Dixon* (1952) 86 CLR 540, the taxpayer had been an employee of a firm of shipping agents. In 1940 he voluntarily enlisted for service in the Australian Imperial Forces and served both in Australia and overseas. During that time his former employer voluntarily paid him the difference between his old salary and the lower salary which he received as a soldier. The payments were regularly relied upon to fund his ordinary living expenditure. The payments were not made in return for any service provided to the employer or in exchange for a promise that he would return to his employer after the war. Dixon CJ and Williams J held that the payments made by the former employer were assessable income of the taxpayer for the purposes of s 25 of the 1936 Act. At 557, their Honours said:

> Because the £104 was an expected periodical payment arising out of circumstances which attended the war service undertaken by the taxpayer because it formed part of the receipts upon which he depended for the regular expenditure upon himself and his dependents and was paid to him for that purpose, it appears to us to have the character of income, and therefore to form part of the gross income within the meaning of s. 25 of the *Income Tax Assessment Act* 1936-1943.

64 Fullagar J agreed with this conclusion. At 567-8, his Honour said:

> It seems to me that the appellant's receipts from Macdonald, Hamilton & Co. must be regarded as having the character of income. They were regular periodical payments – a matter which has been regarded in the cases as having some importance in determining whether particular receipts possess the character of income or capital in the hands of the recipient …. This consideration, while not unimportant, is not decisive. What is, to my mind, decisive is that the expressed object and the actual effect of the payments made was to make an addition to the earnings, the undoubted income, of the respondent. What the employing firm decided to do, and what it really did, in relation to the respondent and others in the same position was "to make up the difference between their present rate of wages and the amount they will receive". What is paid is not salary or remuneration, and it is not paid in respect of or in relation to any employment of the recipient. But it is intended to be, and is in fact, a substitute for – the equivalent *pro tonto* of – the salary or wages which would have been earned and paid if the enlistment had not taken place. As such, it must be income, even though it is paid voluntarily and there is not even a moral obligation to continue making the payments.

See also *Federal Commissioner of Taxation v Anstis* (2010) 241 CLR 443; cf *Federal Commissioner of Taxation v Stone* (2005) 222 CLR 289 at [65] and [66].

65 We would therefore have, in any event, and absent the trust resolutions and the terms of the Practice Trust deed upon which the Commissioner relies, been satisfied that the amounts received by the appellant were assessable as income in ordinary concepts. The reason for their assessability is that they were received, at least in part, regularly, but more importantly, were relied upon by the appellant to fund his daily expenditure. As counsel for the appellant said, "he had to live". In other words, he had the use of and enjoyment of what was paid to him. Consistently with the reasoning in *Dixon*, income regularly received and relied upon "to live", in the particular circumstances here, is income in ordinary concepts.

ADMISSIBILITY OF EVIDENCE

66 In his notice of appeal, at ground 20, the appellant contended that the primary judge had erred in admitting and relying upon an expert report of a forensic accountant which had been produced by the Commissioner for the purposes of determining what amounts of money had been paid into accounts owned or controlled by the appellant, and which had been sourced from the three IETs. The appellant also submitted, at ground 21, that the primary judge erred in ruling that certain paragraphs in his witness statement were not admissible and further submitted that a witness statement of a Mr McKnoulty should have been admitted into evidence.

67 Before us, the appellant said that he no longer pressed these grounds but did not abandon them. In our opinion, each of these evidentiary rulings made by the primary judge was correct.

68 The reasons for admitting into evidence the Commissioner's expert report, authored by Mr Van Homrigh, are set out at *Hart v Federal Commissioner of Taxation (No.2)* [2016] FCA 897. The essence of the attack upon this expert report was that the forensic accountant had not undertaken a full tracing exercise of the various bank accounts of the entities controlled by the appellant. That submission was rejected by the primary judge. At [33] of that judgment, the essential reason for the admission of this evidence was as follows:

> Mr Van Homrigh's evidence is not merely in the form of financial records which this Court can read for itself, and his opinion is not based solely on those records and nothing more in the way of specialised knowledge: see *ASIC v Rich* [2005] NSWSC 149; (2005) 190 FLR 242 at 309-310 [284]. Nor is it stating what is otherwise obvious from the bare collection of records: see *Quick v Stoland* (1998) 87 FCR 371

> at 382-3. To the contrary, Mr Van Homrigh's evidence entails drawing information from a range of records, presenting that information in a coherent and interrelated form, and drawing conclusions and expressing opinions as to the source and destination of moneys which are the very funds upon which the impugned assessments are based.

On this basis, it was admitted, correctly in our view, as expert evidence.

69 As for the paragraphs and sentences in the witness statement of the appellant which were not admitted into evidence, these comprised self-serving assertions without evidentiary foundation. Again the primary judge did not err in excluding them. Even if they had been admitted into evidence we would have given little or no weight to them.

70 Finally, in our opinion, the primary judge did not err in excluding, in its entirety, the witness statement of Mr McKnoulty. Mr McKnoulty was a partner of the firm McCullough Robertson Lawyers and he purported to give expert evidence on the following two issues:

(a) whether an advisor experienced in relation to Div 6 of the 1936 Act and experienced in areas of asset protection, would advise a professional practitioner in complex areas, who was the "controller" of trust deriving significant income and a beneficiary of that trust, to appoint income "away from" that advisor; and

(b) whether, to what extent, that advisor, in the years in question (1997 to 2002 tax years), would have advised a practitioner to cause the trustee of the trust to appoint income to a corporate beneficiary, the shares in which were owned by a passive trust controlled by the practitioner.

71 Whilst the primary judge's reasons for excluding the evidence of Mr McKnoulty do not appear in the reasons for judgment below, in our view it is obvious that the questions asked of Mr McKnoulty did not address any issue of relevance before the court below and the answers given by the witness were necessarily speculative in nature.

PART IVA

72 In relation to the Practice Amount, the Commissioner relied upon Pt IVA of the 1936 Act as an alternative to his primary case. In relation to the IET Amount, the Commissioner relied exclusively upon an application of Pt IVA.

73 At [52] and [53] of his third amended appeal statement the Commissioner identified the scheme for the purposes of s 177A of the 1936 Act in relation to the Practice Amount as

being the steps comprising the Practice Amount NVI arrangement particularised above (hereinafter the "Practice Amount Scheme"). At [102] of that same appeal statement the Commissioner identified the IET Amount scheme as being, broadly, the steps comprising the IET Amount NVI arrangement also set out above (hereinafter the "IET Amount Scheme").

74 The appellant did not dispute that each scheme so particularised is a scheme for the purposes of s 177A. In each case, the scheme comprises each step of each NVI Scheme, including the receipt of monies as the ultimate step by the appellant.

75 At the hearing of the appeal, the appellant:

(a) did not formally abandon his contention, for the purposes of s 177D of the 1936 Act, that each scheme was not entered into by the appellant for the dominant purpose of obtaining a tax benefit, although the appellant did not press this point and made no oral submissions about it; and

(b) contended that the real issue was whether the appellant had in fact obtained a tax benefit under either scheme pursuant to s 177C as it was in the 1997 year of income. In that respect, he submitted that his case was essentially the same for both the Practice Amount and the IET Amount.

76 It is convenient to deal with what the appellant describes as the "real issue" first. In the 1997 income year, s 177C(1) provided as follows:

> (1) Subject to this section, a reference in this Part to the obtaining by a taxpayer of a tax benefit in connection with a scheme shall be read as a reference to:
>
> (a) an amount not being included in the assessable income of the taxpayer of a year of income where that amount would have been included, or might reasonably be expected to have been included, in the assessable income of the taxpayer of that year of income if the scheme had not been entered into or carried out; or
>
> (b) a deduction being allowable to the taxpayer in relation to a year of income where the whole or a part of that deduction would not have been allowable, or might reasonably be expected not to have been allowable, to the taxpayer in relation to that year of income if the scheme had not been entered into or carried out;
>
> and, for the purposes of this Part, the amount of the tax benefit shall be taken to be:
>
> (c) in a case to which paragraph (a) applies - the amount referred to in that paragraph; and
>
> (d) in a case to which paragraph (b) applies - the amount of the whole of the deduction or of the part of the deduction, as the case may be,

referred to in that paragraph.

77 At trial, the Commissioner submitted that but for the entering into of the Practice Amount Scheme, assessable income might reasonably have been expected to have been derived by the appellant in the following way (as per the judgment below at [200]):

> The Commissioner contends that the relevant tax benefit for the purposes of s 177C(1) is the amount of $220,398 (or some lesser amount), which would or might reasonably be expected to have been included in Mr Hart's assessable income for the 1997 income year had the Practice Trust NVI Scheme not been carried out. The Commissioner contended that had the scheme not been carried out, the trustees of the Practice Trust would still have distributed Mr Hart's share of the net income of the Practice Trust for the 1997 income year to the Outlook Trust. The issue was whether Outlook Crescent Pty Ltd (**OCPL**), as trustee for the Outlook Trust, would have on-distributed the same or some lesser amount to Mr Hart or to his benefit. The Commissioner contended that on all the evidence, it was a reasonable prediction that this would have taken place because of the following facts established by the evidence:
>
> (1) Mr Hart, as a principal solicitor at Cleary Hoare, provided legal advice and services to clients and thereby generated income in the form of legal fees.
>
> (2) Mr Hart generated fees by doing solicitor's work, and managed others who did the same.
>
> (3) Employed solicitors of the firm were mainly remunerated by way of salary.
>
> (4) Mr Hart was remunerated in that way when he was a salaried partner, or alternatively a principal, then an employed solicitor in the 1991 and 1992 income years (as demonstrated by his tax returns).
>
> (5) Cleary Hoare was structured so that the legal practice was owned and conducted by the trustees of the Practice Trust, which was a unit trust.
>
> (6) The net income of the Practice Trust was distributed to the unitholders, which apart from the holders of special units comprised four discretionary trusts representing the interests of the four natural person principals of the firm, with Mr Hart's interest being represented by the Outlook Trust of which Mr Hart was a beneficiary, and at all material times a director of OCPL as trustee of the Outlook Trust.
>
> (7) Mr Hart was bound by the terms of the approval given by the Law Society limiting the sharing of receipts to Mr Hart's spouse, parents, children, grandchildren and any other person approved by the Law Society and any company or trust in which the only persons entitled to receive dividends or benefits were such family members or approved persons.
>
> (8) A properly available inference from all of the evidence was that Mr Hart had been the sole recipient of funds sourced from the Outlook Trust because:
>
> (a) the only recorded so-called "*loan account*" in the balance sheet for the Outlook Trust records Mr Hart's name, not any other beneficiary - thus even when the loan characterisation for the receipt of moneys was not accepted, that entry still reflects the sole actual beneficiary for the year in question;

(b) Mr Hart did not in his evidence (statement or oral evidence) refer to any distributions made by the Outlook Trust to any other beneficiary of that trust;

(c) in his letter to the Australian Taxation Office dated 1 July 2002, Mr Hart advised that his wife had never been involved in the conduct of the business of Cleary Hoare and that there was nothing in her records which was relevant to the income derived by him or any of the entities of which she was a director including entities associated with Comlaw Consultants, Cleary Hoare Corporate or Cleary Hoare; and

(d) in his letter to the Australian Taxation Office dated 11 October 2004, Mr Hart advised that flows of money took place in accordance with Law Society approval, including from Cleary Hoare to the Outlook Finance Trust and Outlook Finance No. 2 Trust and that the balance sheets of those two trusts show that the money went from there to Mr Hart, the holder of a full practising certificate.

(9) Mr Hart was solely responsible for directing payments from the Outlook Trust bank account to joint bank accounts with his wife and to the Oak Arrow bank account, with letters dated 24 December 1996, 2 January 1997, 21 January 1997, 3 February 1997, 13 February 1997, 5 March 1997 and 24 April 1997 from Mr Hart to Metway Bank Ltd and associated deposit slips being relied upon to demonstrate this;

(10) A credit approval request, dated 4 August 1998, records (supported by other bank records):

(a) significant expenditure on mortgage repayments, living and other expenses, including the lease of a motor vehicle; and

(b) in the 1998 and 1999 years, by reference to Mr Hart's sharing in the net profits of the Cleary Hoare legal practice, he undertook to pay for the purchase of an investment property and a holiday house albeit in his wife's name or that of an associated trust entity.

(11) Mr Hart signed a statutory declaration dated 22 June 1996 to the effect that all payments made and to be made by him to joint bank accounts with his wife and in the name of Oak Arrow Pty Ltd were intended to be gifts made by him.

(12) All of the above supported the only reasonable inference that Mr Hart was presently entitled to the income of the Outlook Trust and distributed the moneys from that trust accordingly.

(13) Accordingly, it was reasonable to expect that in the absence of the scheme, or some other scheme to which Part IVA would apply, Mr Hart's participation in the financial benefit of the profits generated by the Cleary Hoare legal practice would still have taken place, but in the form of the receipt of income and that was the only available reasonable prediction on the evidence.

78 In relation to the IET Amount Scheme, the Commissioner submitted below that, but for the entry into of that scheme, assessable income might reasonably be expected to have been derived by the appellant in the following way (below at [263]):

> The Commissioner contends that the relevant tax benefit for the purposes of s 177C(1) of the *ITAA 1936* is the amount of $275,481 (or some lesser amount), which would or might reasonably be expected to have been included in Mr Hart's assessable income for the 1997 income year had the Income Earning Trusts NVI Scheme not been carried out. The Commissioner asserted that, in the absence of the scheme, the following events would or might reasonably have been expected to take place:
>
> (1) The Annesley Trust would still have derived income of at least $305,000 and would still have distributed part of that income to the Outlook Trust, from where the income would have been distributed to Mr Hart as a beneficiary of the Outlook Trust.
>
> (2) The CHC Discretionary Trust would still have derived net income of at least $700,410 and would have distributed part of that income to the Outlook Trust, from where the income would have been distributed to Mr Hart as a beneficiary of the Outlook Trust.
>
> (3) In place of the LM Income Trust (which was established as part of the scheme and was precluded by its trust deed from distributing to Mr Hart), the income derived from the work done through that trust, being the provision of tax planning services and the promotion of tax minimisation schemes to accountants and small businesses by Mr Hart and his colleagues at Cleary Hoare (described by the Commissioner as **NVI promotional activities**) would have been attributed to, and accordingly derived by, a discretionary trust controlled by Mr Hart and/or the other principals of Cleary Hoare (such as the Annesley Trust, CHC Discretionary Trust or a similarly-constituted new trust). That trust would then have distributed part of that income to Mr Hart or alternatively the Outlook Trust or another trust controlled by Mr Hart. From there, the income would have been distributed to Mr Hart as a beneficiary of the Outlook Trust or such other trust that he controlled.

79 On appeal, the appellant submitted that the foregoing outcomes were the "least likely" to have occurred. For that purpose, he referred the Court to the decisions of *Peabody, Federal Commissioner of Taxation v Ashwick (Qld) No 127 Pty Ltd* (2011) 192 FCR 325 and *RCI Pty Ltd v Federal Commissioner of Taxation* [2011] FCAFC 104. The appellant's proposition was based upon the following factors:

> (a) the historical pattern of distributions in the 1994, 1995, in 1996 years of income in which the Outlook Trust had made distributions to CHOUT, because that trust had, at that time, sufficient tax losses to absorb the income distributed to it.
>
> (b) the use within the NVI scheme of brand-new trusts which had never made any previous distributions to any beneficiaries; and

(c) the desirability of not distributing to the appellant for predominantly fiscal reasons, but also for the purpose of obtaining the benefit of asset protection from current or future creditors.

80 In the appellant's submission these factors were the only objective evidence before the Court concerning the likely counterfactual. In particular, the appellant emphasised the past conduct of making distributions between 1994 and 1997. When regard was had to past conduct, so the appellant contended, it was reasonable to conclude that there was no possibility that the appellant would ever have received beneficially any distribution of income. The income would always have gone elsewhere.

81 The appellant did not identify with any precision who else would, or might reasonably be expected to, have derived the income generated by the Practice Trust, or alternatively the Outlook Trust, or, if there was to be more than one such recipient, how much each might reasonably be expected to have received and why. He contended that he did not need to be so particular and it was sufficient, based upon the factors he relied upon, for the Court to be confident that any of the tax preferred beneficiaries of the Outlook Trust, such as CHOUT or any of the appellant's children, might reasonably be expected to have received distributions. No evidence in support of these contentions was identified, other than the fact that CHOUT had losses in the 1997 year of income in the sum of $186,033, and had previously received distributions when it had sufficient tax losses. In any event, evidence of past conduct demonstrated, it was said, that the Commissioner's counterfactuals were not reasonable.

82 In *Ashwick*, Edmonds J said at [153](7) to (11), about the relevance of evidence from a taxpayer in relation to the application of s 177C:

(7) How the taxpayer establishes that there is no tax benefit is a matter for it: *Trail Bros* [(2009) 113 ALD 254] at [36].

(8) It is conceivable that a taxpayer may not lead positive evidence of an alternative postulate because, for example, the result of any objective enquiry of the alternative postulate is inevitable: *AXA Asia Pacific Holdings* [(2010) 189 FCR 204] at [139]. *Futuris Corporation Limited v Federal Commissioner of Taxation* [2010] FCA 935; 2010 ATC 20-206 provides an example of a case where the taxpayer did not lead any direct evidence, but established the alternative postulate through expert evidence.

(9) It is relevant to have regard to the evidence of the taxpayer as to the steps it says it would have undertaken or would have been likely to undertake in the absence of the scheme: *Federal Commissioner of Taxation v Spotless Services Limited* (1996) 186 CLR 404 at 423-424.

(10) The taxpayer may lead evidence that it would have undertaken a particular

> activity, or adopted a particular course in lieu of the scheme. If a taxpayer has given evidence of what he or she would have done but for entering the scheme, that evidence will be relevant and useful to the extent to which it reveals facts or matters that bear upon the objective determination of the alternative postulate: *Trail Bros* at [36]; *AXA Asia Pacific Holdings* at [139]; *Federal Commissioner of Taxation v Mochkin* [2003] FCAFC 15; (2003) 127 FCR 185 at 209 - 210.
>
> (11) The taxpayer can give evidence as to what it would have done in the absence of the scheme, provided foundation facts are given to support what would otherwise be a bald speculative statement: *McCutcheon v Federal Commissioner of Taxation* [2008] FCA 318; (2008) 168 FCR 149 at 163 - 164; *AXA Asia Pacific Holdings* at [140].

83 Subsequently, in *RCI*, the Full Court made it abundantly clear that a taxpayer does not discharge its onus for the purposes of s 177C by demonstrating that the Commissioner's counterfactual is not reasonable. More is required. At [129] and [130] their Honours said:

> It has been said in the past, and the learned primary judge at [88] of her Honour's reasons said below, that the taxpayer carries the onus of establishing that the Commissioner's counterfactual is unreasonable; and that if the taxpayer does not establish that the Commissioner's counterfactual is unreasonable, then the taxpayer fails to prove that the assessment is excessive on that ground. (Of course, the taxpayer may establish that the assessment is excessive on some other ground, such as that the conclusion required to be drawn as to the dominant purpose of a party to the scheme under s 177D(b) cannot be drawn, but that is another matter.)
>
> Such an articulation of the onus is erroneous, but if not, certainly unhelpful because it can lead one into error. Even if a taxpayer establishes that the Commissioner's counterfactual is unreasonable, it will not necessarily follow that he has established that the assessment is excessive. That is because the issue is not whether the Commissioner puts forward a reasonable counterfactual or not; it is a question of the Court determining objectively, and on all of the evidence, including inferences open on the evidence, as well as the apparent logic of events, what would have or might reasonably be expected to have occurred if the scheme had not been entered into. Thus, even if a taxpayer establishes that the Commissioner's counterfactual is unreasonable, that will not discharge the onus the taxpayer carries if the Court determines that the taxpayer would have or might reasonably be expected to have done something which gave rise to the same tax benefit.

84 In this case, the appellant has focused on trying to establish that the Commissioner's counterfactual was unreasonable, without himself sufficiently identifying and evidencing his own counterfactual. Showing that the Commissioner's counterfactual was unreasonable does not of itself operate as a discharge of the onus of proof imposed upon the taxpayer in relation to s 177C.

85 In his witness statement, the appellant asserted that he would not have taken any action which might have given rise to any entitlement on his part to a share of income produced by the Practice Trust. This was speculation and rightly ruled inadmissible by the primary judge. As the Full Court observed in *RCI* at [134]:

> [A taxpayer]…may, for example, lead evidence that the taxpayer would have undertaken a particular activity, or adopted a particular course, in lieu of the scheme; or it may lead evidence that the taxpayer would not have undertaken a particular activity, or adopted a particular course, in lieu of the scheme: see, for example, *Commissioner of Taxation v News Australia Holdings Pty Ltd* [2010] FCAFC 78. Generally, such evidence is unlikely to be sufficient to discharge the onus unless it is supported by objective indicia to be gleaned from the context and matrix of underlying or 'foundation' facts, as they have been called (see *McCutcheon v Federal Commissioner of Taxation* [2008] FCA 318; (2008) 168 FCR 149 at [37] - [39] per Greenwood J) as well as the logic of the taxpayer's counterfactual having regard to the commercial or financial aspirations and limitations of the parties to the scheme; without such support, such evidence is likely to be regarded as no more than purely speculative.

86 The task for the taxpayer under former s 177C is to adduce positive evidence of objective circumstances in existence in the year of income in dispute, or before that year, which ground a reasonable expectation of a counterfactual or alternative counterfactual, in which the taxpayer obtains no tax benefit. In the usual case, the production of contemporaneous documentation to evidence the objective circumstances will be far more probative than assertions made in a witness statement or affidavit, especially when regard is had to what was said by Fullagar J *Pascoe v Federal Commissioner of Taxation* (1956) 30 ALJR 402 at 404:

> Where a person's purpose or object or other state of mind in relation to a given transaction is in issue, the statements of that person in the witness box provide, in a sense, the "best" evidence, but, for obvious reasons, they must, as *Cussen*, J observed in *Cox v Smail* ((1912) VLR 274, at p 283), "be tested most closely, and received with the greatest caution".

87 In our view, the appellant's case fell far short of the required standard. No evidence was led of a counterfactual involving the distribution of income sourced from the Practice Trust to a particular person. The speculation, for it was no more than that, that it might reasonably have gone to anyone within a particular group of beneficiaries did not show that, but for each scheme entered into, it might reasonably have been expected that the appellant would not have received any income. After all, he was a beneficiary himself. The onus of proof imposed on a taxpayer is not discharged by expressing a desire to pay no tax as an eligible beneficiary of a trust estate, and then observing objectively from the terms of a trust deed that

there are other beneficiaries, some of whom might have a capacity to pay less tax. More is needed.

88 Nor did the introduction of new trusts with no prior patterns of distribution assist the appellant. It is true that the absence of a prior pattern of distributions makes it more difficult to identify which beneficiary might reasonably be expected to have received distributions, but for the scheme. But that is a difficulty for the taxpayer, not the Commissioner. If anything, it makes the discharge of the burden of proof all the more difficult: cf *Federal Commissioner of Taxation v Spotless Services Ltd* (1996) 186 CLR 404, 423-4.

89 The same observations and conclusions apply equally to the IET Amount Scheme.

90 In any event, we are not satisfied that the Commissioner's counterfactuals were unreasonable, given the paucity of evidence led by the appellant on this issue. Commencing with the Practice Amount, it is well to be remembered that, in the 1997 year of income, the appellant was a partner of Cleary Hoare as nominee of the Outlook Trust, where he worked as a solicitor earning fees for the Practice Trust. No evidence was led that he had other sources of wealth and, as we have already mentioned, his income tax return for that year disclosed only $100 of assessable income. It was not disputed that the Practice Amount was sourced from the earnings of the Practice Trust. Nor was it disputed in the case of the IET Amount that it was sourced from the earnings of the three IETs. The evidence was that the appellant was the originator of the NVI Scheme, perhaps developed with others, and, that this was a product sold by the three IETs with the active assistance of the appellant.

91 For reasons we have already given, it can readily be inferred that the appellant relied upon the Practice Trust amount for his day-to-day living expenses and for investment. In other words, he had the use and enjoyment of the Practice Amount. If the Practice Amount, contrary to our earlier finding, had been lent to the appellant, it is reasonable to expect that, but for that scheme, the appellant would, or might reasonably be expected to, have beneficially derived that amount, that being the only other obvious way for him to have secured the use and enjoyment of that sum. As already mentioned, no other specific way to so use and enjoy the money was identified by the appellant.

92 In relation to the IET Amount, it will be recalled that the Commissioner's counterfactual was, in part, similar to his Practice Amount counterfactual. He submitted that income earned by the Annesley Trust and by the CHC Discretionary Trust would, or might reasonably be

expected to, have been distributed to the Outlook Trust and thence to the appellant. In relation to the earnings of the LM Income Trust, the Commissioner's counterfactual was more conjectural. This was because that trust was prohibited by its deed from making distributions to the settlor of the trust, being the appellant. The Commissioner's counterfactual had the LM Income Trust making distributions to "a discretionary trust controlled by [the appellant] and/or the other principals of Cleary Hoare", and that trust either making distributions directly to the appellant or to the Outlook Trust, or a further trust controlled by the appellant, and from there to the appellant.

93 For these purposes, the Commissioner relied upon the expert report of Mr Van Homrigh which found that a total of $289,431 had been deposited into bank accounts operated by, or controlled by, the appellant out of the earnings of the three IETs: below at [261]. With less confidence, based on the evidence adduced, we find that this counterfactual was also reasonable. It may be inferred that the appellant had the use and enjoyment of the amounts deposited into bank accounts operated or controlled by him, or intended to have that use and enjoyment. But for personal derivation, no other way for him to secure that use and enjoyment was identified by the appellant. The Commissioner's counterfactual was accordingly reasonable.

94 Of course, it may be accepted that receiving monies in a taxable way diminishes the amount the appellant might otherwise have enjoyed. Does his professed intention not to pay tax change the outcome here? Can a taxpayer avoid the reach of s 177C by contending that but for the scheme, implementation of another arrangement of equal ingenuity would have been pursued to avoid the payment of any tax? In *Futuris Corporation Ltd v Federal Commissioner of Taxation* [2010] FCA 935, Besanko J observed, at [113]:

> The counterfactual must not itself be a scheme with a dominant tax purpose: *Commissioner of Taxation v Trail Bros Steel & Plastics Pty Ltd* [2009] FCA 1210 at [52].

95 The appellant accepted the correctness of the proposition set out above, but contended that the non-specific alternatives identified by him, such as a distribution to CHOUT, would not have been subject to Pt IVA, but would have constituted "legitimate ways in which income could and would have been distributed." In that respect, the appellant also conceded that some or all of that income would still need to be "lent" to him as a final step of his counterfactual.

96 Once again, we find that the appellant has not discharged the onus of demonstrating that the alternative transactions he has postulated would not have been subject to Pt IVA. It is true that, as a matter of logic flowing from the objective position of the Outlook Trust and the identity of its potential range of discretionary beneficiaries, one could speculate about the possibility of distributions being made, for example, to children, that might not, without more, be capable of being impugned by Pt IVA. But the appellant's case rose no higher than such speculation.

97 As already mentioned, the appellant was unable to identify with sufficient precision what distributions might reasonably have been expected to have been made and how much would have been distributed. Nor could he identify the particular manner in which such distributions might reasonably have been expected to have been made. One possibility suggested was an assertion that a distribution might have been made to CHOUT in 1997. Again, however, no evidence was adduced to support this assertion, and as a matter of inherent probability, we find it unlikely that a distribution might reasonably have been expected to have been made to CHOUT because it had only $186,033 of tax losses left in it by the 1997 year of income.

98 Of course, there may be cases where a taxpayer can discharge its onus of proof under former s 177C, by the drawing of inferences from a given transaction or transactions or from the structure of an organisation. In such cases, particular evidence of what might be reasonably be expected, but for the scheme, may not exist. As the Full Court said in *RCI* at [135]:

> On the other hand, in a given case, such evidence may not be necessary because, for example, the result of any objective enquiry as to the counterfactual is, at best, inevitable or, at worst, compelling. In such a case, the failure to lead evidence to say that the taxpayer would have undertaken a particular activity or adopted a particular course, in lieu of the scheme; or the failure to lead evidence that the taxpayer would not have undertaken a particular activity, or would not have adopted a particular course, in lieu of the scheme, will not lead to the taxpayer failing to discharge the onus.

In *RCI*, without the production of specific evidence of what might reasonably be expected to have occurred, but for the scheme in fact entered into, the Full Court held that there was no tax benefit. That was because it was inherently improbable that the RCI group would have entered into a voluntary re-organisation, designed over time to save money and to secure synergistic benefits, if it had also been required to have paid tax of $172 million. But for the scheme in that case, it would instead have done nothing.

99 This case is not like *RCI*. The objective circumstances do not throw up any obvious or inevitable counterfactual which leads to the conclusion that the appellant obtained no tax benefit. The existence of trusts, including the discretionary Outlook Trust with numerous potential beneficiaries, does not objectively support an inference that a particular distribution away from the appellant might reasonably have been expected to have occurred.

100 In that respect, whilst the appellant relied on past conduct to demonstrate the soundness of his criticism of the respondent's counterfactual, he nonetheless wanted to exclude some of that conduct. In particular, he argued that the fact that the appellant was paid a salary by Cleary Hoare 1991 and 1992, as evidenced from his tax returns, was irrelevant because he was then a bankrupt and an employee. If it matters, we accept that there is a difference between what might happen as an employee and what might reasonably be expected to happen when one is establishing a business structure as an owner. The circumstances of *Federal Commissioner of Taxation v Mochkin* (2003) 127 FCR 185 bear that out. In that case, the taxpayer was a stockbroker. He had been personally sued as a result of defaults made by his clients. He thereafter chose to run his business via a family discretionary trust. It was accepted that he did this for the dominant purpose of avoiding personal exposure to the liabilities and debts of the business.

101 At first instance here, the primary judge found as well that any counterfactual transaction would also need to be one that would have complied with the rules of the Queensland Law Society. In general terms, these precluded the making of distributions to non-family members of the earnings of a law firm which was owned by the trustee of a trust. It will be recalled that many of the entities within the NVI structure did not comply with this requirement, especially RTH. It is strictly unnecessary for us to comment upon the correctness of the primary judge's conclusion because on appeal it was not contended by the appellant that any particular counterfactual contended for by him would have involved a particular distribution to an unrelated non-family member. Having said that, there is no reason to doubt the primary judge's observation that, for the purposes of assessing the probability of any suggested counterfactual, one should assume that the taxpayer will behave lawfully: see [213].

102 The appellant also renewed his attack, in the context of s 177C, on the expert report prepared by Mr Van Homrigh. For that purpose, he was content rely to on what had been said by him in his written submissions. Those submissions criticised Mr Van Homrigh for not

undertaking a full tracing exercise. That failure was said – now correctly – to go to the level of weight to be attributed to the persuasiveness of the report. The problem for the appellant, however, is that he put nothing up to contradict Mr Van Homrigh. He did not produce a contrary expert report. And he did not lead evidence from himself about the correctness of the report. The latter factor is especially telling. If Mr Van Homrigh had erred in reaching his conclusions, it would have been an easy matter for the appellant to have adduced evidence to that effect. After all, the subject matter of the expert report was the very bank accounts the appellant controlled.

103 The primary judge was aware of the fact that Mr Van Homrigh had not undertaken an exhaustive tracing exercise, and well understood the limitations on the material that the expert had before him. But absent contradictory material, it was entirely proper for the primary judge to rely upon the conclusions of that report. The report was not inherently irrational, or devoid of reasoning, and did not lack a sufficiency of factual foundation: see below at [247]. In our view, the burden was on the appellant to contradict Mr Van Homrigh and that burden was not discharged by submitting that the report should have been given little weight. It follows that the appellant has failed to show that the primary judge erred by relying on the expert report produced by the Commissioner.

104 As already mentioned, the appellant did not abandon, but did not press, any argument concerning the application of s 177D and the primary judge's conclusion that the appellant had entered into and carried out each scheme for the dominant purpose of obtaining a tax benefit. In relation to the Practice Amount Scheme, the primary judge concluded, after carefully considering the eight matters in s 177D(b) as follows (at [237]):

> Senior counsel for the Commissioner characterised the utilisation of these arrangements as contrived and artificial, devoid of any commercial rationale. He submitted that the tax benefit that it achieved for Mr Hart, namely the avoidance of the payment of income tax on the Practice Amount, explained objectively the purpose of his participation in the scheme. I agree with that conclusion, especially as I have rejected the only alternative purpose advanced on behalf of Mr Hart, namely asset protection, as having any significant role to play. Senior counsel for Mr Hart submitted that even if Mr Hart obtained a tax benefit (which was denied), it could not be reasonably concluded that the objective of entering into the scheme was to obtain the tax benefit. I reject that submission. If a tax benefit was not in reality the sole purpose, it was so dominant that any other purpose, such as asset protection, pales into insignificance.

105 In relation to the IET Amount Scheme, the primary judge again carefully considered the eight matters required by s 177D(b) and concluded at [289]:

> Mr Hart did not appear to advance any additional arguments as to the dominant purpose for the Income Earning Trusts NVI Scheme than for the Practice Trust NVI Scheme. Dominant purpose was not really the centrepiece of his case. If, as he asserted, there was no tax benefit associated with a scheme, then dominant purpose did not arise. If there was such a tax benefit associated with the scheme, given the terms of the scheme and the way in which it was executed, a dominant purpose was, especially in light of all of the arguments set out above on behalf of the Commissioner, difficult, if not impossible, to resist. I therefore accept that the requisite dominant purpose has been established. The arguments advanced by the Commissioner are not overwhelming because of some of the gaps and uncertainties presented by the facts as proved. But they did not have to be either overwhelming or certain. On balance, I accept that the necessary dominant purpose has been established.

106 The appellant has not shown that the primary judge erred in relation to either conclusion. In his written submissions, the appellant asserted, without any apparent justification, the proposition that the dominant purpose of each scheme was asset protection as in *Mochkin*. However, that argument was no more than a bare assertion. It is accordingly rejected.

PENALTY

107 The respondent assessed the appellant to a penalty of 50% under former s 226 of the 1936 Act which was applicable in the 1997 income year. In the 1997 income year, s 226 provided:

> (1) Where:
>
> (a) for the purpose of making an assessment or arising out of the consideration of an objection, the Commissioner has calculated the tax that is assessable to a taxpayer in relation to a year of income;
>
> (b) in calculating the tax assessable to the taxpayer, a determination or determinations made by the Commissioner under subsection 177F(1) was or were taken into account; and
>
> (c) either of the following subparagraphs apply:
>
> (i) no tax would have been assessable to the taxpayer in relation to the year of income if no determination had been made under subsection 177F(1) in relation to the taxpayer in relation to the year of income;
>
> (ii) the amount of tax (in this section referred to as the "amount of claimed tax") that would, but for this section, have been assessable to the taxpayer in relation to the year of income if no determination had been made under subsection 177F(1) in relation to the taxpayer in relation to the year of income is less than the amount of tax referred to in paragraph (a);

the taxpayer is liable to pay, by way of penalty, additional tax equal to:

(d) in a case to which subparagraph (c)(i) applies – the penalty percentage of the amount of the tax referred to in paragraph (a); or

(e) in a case to which subparagraph (c)(ii) applies – the penalty percentage of the amount by which the amount of the tax referred to in paragraph (a) exceeds the amount of claimed tax.

(2) In this subsection (1):

penalty percentage means:

(a) subject to paragraph (b) – 50%; or

(b) if it is reasonably arguable that Part IVA does not apply – 25%

108 The Commissioner contended below that it was not reasonably arguable that Pt IVA did not apply in relation to each of the Practice Amount and IET Amount Schemes, and that accordingly the lower 25% rate of penalty was not applicable. The primary judge accepted that conclusion. The appellant challenged it in his notice of appeal. However, on appeal, he conceded, quite fairly, that it was difficult to maintain this challenge it if it was found that Pt IVA applied, given the findings made below about the blatancy of the scheme.

109 In that respect the primary judge found at [303] and [304]:

> I agree with the Commissioner that both manifestations of the NVI Scheme were blatant. In substance, Mr Hart obtained the Practice Amount and the IET Amount by the most artificial of devices of the very kind that Part IVA was evidently intended to capture. I also agree that the written opinions of Mr Russell QC obtained in February 1996 did not assist Mr Hart. They were not tailored to the present two situations and afforded a weak basis for resisting the application of Part IVA. As the Commissioner points out, in the internal opinion, the view is expressed at p 17 that *"[t]he operation of Part IVA is somewhat more problematical"* and that *"[i]t is difficult to see how any purpose other than the securing of [tax] relief can be attributed to any of the participants in the scheme"*, yet later states at p 18 *"[i]f, contrary to my views, Part IVA is capable of application ..."*. Relying on the largely generic advice in those opinions was a high risk strategy. The opinions, considered properly, provide at best very slight support for forming a view that it was reasonably arguable that Part IVA did not apply. I would prefer to characterise the opinions as containing at least implicit warnings that there was a very real chance that Part IVA did apply. In any event, generic advice or an opinion of that kind does not take account of adverse factual findings, which is another risk factor which a person implementing a Part IVA scheme necessarily takes.
>
> Applying the reasoning in *Walstern* [(2003) 138 FCR 1], I am unable to be satisfied that Mr Hart's argument as to the application of Part IVA is about as likely as not correct when regard is had to the well-established principles to be applied by long-standing authority. In the end result, the difference between the two cases was not really finely balanced as opposed to requiring attention to detail and conventional and predictable findings on the evidence. The competing arguments leave little room for

> it to be argued that, on balance, Mr Hart's argument can objectively be said to be one that, while wrong, could be argued on rational grounds to be right. That is especially so as it is very clear that Mr Hart did not take reasonable care in the implementation of the NVI Scheme.

These findings disclose no discernible error and are, in our opinion, plainly correct.

CONCLUSION

110 For the foregoing reasons, the appeal is dismissed with costs.

I certify that the preceding one hundred and ten (110) numbered paragraphs are a true copy of the Reasons for Judgment herein of the Honourable Justices Robertson, Wigney and Steward.

Associate: 

Dated: 20 April 2018