

Decision impact statement

Greig v Commissioner of Taxation

Court citation(s):	[2020] FCAFC 25
Venue:	Federal Court of Australia (Full Court)
Venue reference no:	NSD 1427 of 2018
Judge names:	Kenny, Derrington and Steward JJ
Judgment date:	2 March 2020
Appeals on foot:	No, the Commissioner did not seek leave to appeal to the High Court
Decision outcome:	Unfavourable to Commissioner

Impacted advice

Relevant Rulings/Determinations:

Taxation Ruling TR 92/3 *Income tax: whether profits on isolated transactions are income*

Taxation Ruling TR 92/4 *Income tax: whether losses on isolated transactions are deductible*

The ATO considers this decision has no impact on these rulings.

Summary

This Decision impact statement outlines the ATO's response to *Greig v Commissioner of Taxation* [2020] FCAFC 25.

The main issue in this case was whether the taxpayer acquired shares in an Australian Securities Exchange (ASX)-listed company as part of a 'business operation or commercial transaction'. A majority of the Full Court concluded that the taxpayer did. Therefore, given the taxpayer also had a profit-making intention in acquiring those shares (which was not in dispute), the principle in *Commissioner of Taxation v Myer Emporium Ltd* [1987] HCA 18 (*Myer Emporium*) was engaged. As a result, the losses and outgoings made by the taxpayer from the compulsory transfer of those shares were deductible under paragraph 8-1(1)(a) of the *Income Tax Assessment Act 1997* (ITAA 1997).

The Commissioner's view is that the Full Court's finely balanced conclusion was open on the particular facts of this case and does not disturb the Commissioner's understanding of the *Myer Emporium* principle.

The Commissioner has reviewed existing public advice and guidance on the application of the *Myer Emporium* principle to ensure it reflects the Full Court's application of the principle in this case.

Brief summary of facts

The taxpayer was a senior executive for a global group of companies providing construction, project management and engineering services to clients, including those in the mining and resources industry. The case related to the taxpayer's acquisitions of shares in the former ASX-listed company, Nexus Energy Limited (Nexus). The taxpayer was familiar with Nexus because of his knowledge of the mining and resources sector. He considered there was value in the shares beyond that reflected in their share price, and reasonable prospects of him making a profit by selling the shares in the short-term. In particular, the taxpayer was of the view that Nexus' interest in a gas field off the north-west coast of Western Australia was undervalued. The taxpayer acquired a large number of Nexus shares over 64 transactions spanning approximately 2 years between 2012 and 2014, with an intention of making a profit from their sale prior to his retirement within 4 to 5 years.

During the period in which the taxpayer acquired and held Nexus shares, he regularly monitored their price and ASX announcements either directly or through his professional adviser, conducted research into the company's prospects by reading relevant financial press articles and research reports by investment banks and stockbrokers, and attended company meetings and presentations. During this period, the taxpayer played a key role in influencing a majority of the company's shareholders to reject a takeover proposal from Seven Group Holdings Ltd. However, when the company was placed into voluntary administration, the taxpayer was unsuccessful in legal proceedings (with some other shareholders) to oppose a deed of company administration (DOCA) that proposed the compulsory acquisition of his shares for no consideration. The Supreme Court of New South Wales approved the proposed DOCA in December 2014, which resulted in the taxpayer making share losses of approximately \$11.85 million. The taxpayer also incurred associated legal fees of \$507,198.

Aside from shares in Nexus, the taxpayer invested millions of dollars in the share market using both professional advice and his own business knowledge and experience. The taxpayer had treated his other considerable share investments (acquired in over 200 separate parcels, totalling approximately \$26 million, of which approximately 180 parcels were sold, and the majority held for only short periods of time) as being held on capital account. However, only the tax treatment of the Nexus shares was in dispute in this case.

At first instance in the Federal Court before Thawley J, the taxpayer argued his Nexus shares were acquired by him as part of a 'business operation or commercial transaction', or alternatively that he engaged in a 'business' of dealing in those shares, so as to (in either case) fall within the principle in *Myer Emporium*. Thawley J rejected both of the taxpayer's arguments, upholding the Commissioner's assessment (which treated the taxpayer's losses and outgoings as being on capital account) for the 2014–15 income year. The taxpayer appealed to the Full Court of the Federal Court.

The Full Court (Kenny and Steward JJ, with Derrington J dissenting) allowed the taxpayer's appeal. The majority agreed with the taxpayer that the primary judge erred by not accepting that he acquired the shares in a business operation or commercial transaction, so as to engage the principle in *Myer Emporium*. The taxpayer's share losses and legal fees were therefore deductible under paragraph 8-1(1)(a) of the ITAA 1997.

The Commissioner did not seek leave to appeal the Full Court's decision to the High Court.

Issues decided by the Court

Business operation or commercial transaction

The Full Court considered whether the taxpayer, who was employed as a full-time senior executive and not otherwise carrying on a business during the relevant period, acquired the Nexus shares in a 'business operation or commercial transaction'. This is the second limb of the principle in *Myer Emporium* that a profit or loss from an isolated transaction will generally be on revenue account where the:

- intention or purpose of the taxpayer in entering into the transaction was to make a profit or gain, **and**
- transaction was entered into, and the profit or loss was made, in the course of carrying on a business or **in carrying out a business operation or commercial transaction.**

It was not in dispute in the Full Court that the taxpayer acquired his relevant Nexus shares with a profit-making purpose (which satisfied the first limb of the *Myer Emporium* principle).

In applying the *Myer Emporium* principle, the Full Court explained:

- Profit-making purpose is not sufficient by itself to engage the *Myer Emporium* principle and will not of itself give a transaction a business-like or commercial character – at [31], [141] and [225]. However, such a purpose is relevant to how the activities of the taxpayer are characterised in determining whether there is a business operation or commercial transaction – at [31], [141–142] and [224–225].
- In determining whether there is a business operation or commercial transaction, '...it is necessary to make both a wide survey and an exact scrutiny of the taxpayer's activities' and emphasis should not be put on one or more features of a transaction to the exclusion of others – at [27] and [212].
- Whether a transaction is on revenue account or capital account will depend on an objective assessment of the facts – at [96] and [242(3)]. While a taxpayer's subjective intention may form part of the wide survey and exact scrutiny of a taxpayer's activities, it should be treated with caution – at [212] and [214]. However, evidence about a taxpayer's personal characterisation of the transaction as being either on revenue account or capital account may go to the credit of the taxpayer's evidence or be relevant to penalties – at [242(3)].
- Activities entered into after an acquisition of shares will generally not be relevant in determining whether the shares were acquired in a business operation or commercial transaction. However, where shares are acquired progressively over time, the taxpayer's activities over that period may be relevant as part of the wide and exact scrutiny of the taxpayer's activities, particularly where the transaction is not an isolated one – at [30], [242(1)] and [245(4)].
- Where a taxpayer acquires shares to sell at a profit rather than to hold as a long-term investment and to receive dividends over time, the taxpayer waiting to sell the shares so as to realise the profit sought will not be fatal to a characterisation of the transaction as being on revenue account – at [246].

The Full Court stated that it is the commercial or business-like nature of a profit-making transaction that distinguishes it from wagering, lotteries and hobbies, from an investment by a 'private investor' made to hedge against inflation, and from a mere realisation of a capital asset, gain or losses from which would be on capital account – at [29], [229] and [242(4)]. An example of a transaction that is unlikely to be part of a 'business operation or commercial transaction' is an investment in shares to hold over time for their dividend yield – at [29], [235] and [242(6)].

The Full Court also noted at [31] that:

...Whether a gain or loss is properly characterised as the outcome of a "business operation or commercial transaction" cannot be determined by further exegesis of the words "business operations" and "commercial transaction".

While the meaning of those words is 'plain enough', another way of expressing those words is 'business deal' or something a business person or person in trade would do – at [31], [242(4)] and [248].

In concluding that the taxpayer's acquisition of Nexus shares had the character of a business operation or commercial transaction, Kenny and Steward JJ had regard to the following matters:

- the taxpayer's 'sophisticated' plan to generate cash profits prior to his retirement in 4 to 5 years' time by acquiring shares in large volumes and selling them quickly at a substantial profit – at [29], [30] and [245(2)]
- the taxpayer acquired the Nexus shares in a 'systematic' fashion on 64 occasions – at [245(3)]
- the acquisitions of Nexus shares were part of, and indistinguishable from, the taxpayer's other share-trading activities which included the frequent and short-term acquisition and sale of 44 other stocks on 218 occasions – at [30] and [251]
- the taxpayer's participation directly, or indirectly through the agency of his adviser, in the plan to increase the value of his shares (including research, meeting company representatives and becoming a substantial shareholder to have a greater say over any future sale process by Nexus) block the proposed takeover of Nexus by Seven Group Holdings Ltd and contest the subsequent DOCA proposed by creditors of Nexus – at [18], [30], [204], [207] and [245(4)]
- the taxpayer's use of his own business knowledge and experience (that he had acquired as a senior executive of a global services group of companies which operated in the mining and resources industry) each time he decided to buy Nexus shares in a context where that knowledge and experience of the mining and resources sector was more than most ordinary private investors would have – at [30], [245(5)] and [247], and
- the taxpayer acted as a business person would by engaging in the previously listed activities; the taxpayer engaged professional advisers; the taxpayer used 'system and organization' in relation to the acquisition of his Nexus shares; his share trading activities were not consistent with a hobby, pastime, private gambling or gaming; and the disposal of his shares was more than a 'mere' realisation of an asset – at [30], [242(6)] and [248].

ATO view of decision

Business operation or commercial transaction

The Commissioner considers that this case does not change the principle in *Myer Emporium* and, in particular, does not disturb the Commissioner's understanding of the factors that will be relevant in determining whether an acquisition of shares is made in carrying out a 'business operation or commercial transaction'.

The Commissioner considers that it was reasonably open to the Full Court on the facts of this case to conclude that the taxpayer acquired his Nexus shares in a business operation or commercial transaction. In particular, the majority of the Full Court had regard to the taxpayer's extensive business knowledge and experience, the significant commercial steps that the taxpayer took to increase the value of his Nexus shares, and the scale and periodicity of his overall share-trading activities (not just those involving the relevant Nexus shares) over 7 years.

In addition to the relevant Nexus shares, Steward J noted at [223] that:

...from 2007 to 2014 the taxpayer purchased parcels of listed shares on 218 occasions (he purchased Nexus shares on a further 64 occasions). He sold approximately 180 of these. He expended in aggregate about, by my reckoning, \$26 million. A great many shares were held for only months; a very great deal were held for less than two years.

The taxpayer also became a substantial shareholder in 3 ASX-listed companies (including Nexus). The Full Court majority concluded by the way that all of the taxpayer's other share transactions were on revenue account, notwithstanding he had self-assessed them as being on capital account - at [28] and [252].

As summed up by Steward J at [223] in referring to the taxpayer's overall share trading activities:

... It would, in my view, and generally speaking, be surprising if such trading, with its scale and periodicity, and with its express purpose of profit-making, could be characterised as an affair of capital.

The Commissioner considers that the Full Court majority's conclusion is not inconsistent with the existing advice and guidance in Taxation Rulings TR 92/3 *Income tax: whether profits on isolated transactions are income* and TR 92/4 *Income tax: whether losses on isolated transactions are deductible* and on the ATO's website.¹ Paragraph 13 of TR 92/3 sets out the matters which may be relevant in considering whether an isolated transaction amounts to a business operation or commercial transaction, including the nature and scale of other activities undertaken by the taxpayer, the amount of money involved in the operation, the magnitude of the profit sought, the nature, scale and complexity of the operation, and the timing of the transaction. Having regard to those matters, the Commissioner considers that the taxpayer's activities in this case as explained by the majority of the Full Court can reasonably be characterised as business or commercial in character.

The Commissioner notes Steward J's acknowledgment that the question of whether there was a business dealing or commercial transaction in this case raised a 'difficult issue of characterisation' and that his Honour reached his conclusion in this case

¹ [Shareholding-as-investor-or-share-trading-as-business](#).

‘... (a)fter much hesitation’ – at [225] and [245]. Kenny J also noted at [24] that existing cases on the *Myer Emporium* principle:

...do not directly address a case like this where the issue is whether a taxpayer was engaged “in a business operation or commercial transaction” for the purpose of making a profit, while also being a very well remunerated corporate employee in full-time employment.

The borderline nature of this case is also demonstrated by the different conclusions reached by Thawley J at first instance and Derrington J in dissent.

The Commissioner accepts that the activities of agents acting on behalf of a taxpayer (such as a professional adviser or broker) are relevant to the factual matrix which needs to be considered in characterising the nature of a transaction.

Carrying on a business

The majority of the Full Court did not address whether the taxpayer was carrying on a business of dealing in the relevant Nexus shares (as it was not necessary for them to do so). Where a taxpayer is carrying on a business, TR 92/3 and TR 92/4 provide guidance on when a profit or loss from an isolated transaction will be assessable as income or deductible (as relevant).

Individual taxpayers investing in shares who are able to establish that they are within the *Myer Emporium* principle on the basis that they are carrying on a business (such that gains or losses from their shares are assessable or deductible on revenue account, respectively) should also be aware of the non-commercial loss rules in Division 35 of the ITAA 1997, which can limit the ability to utilise losses from carrying on a business activity. The operation of the non-commercial loss rules is explained in Taxation Ruling TR 2001/14 *Income tax: Division 35 – non-commercial business losses*.

Implications for impacted advice or guidance

The Commissioner considers the decision is consistent with the ATO’s explanation of the *Myer Emporium* principle in existing advice and guidance and provides another example of the application of that principle to the particular facts before the Full Court.

Legislative references

ITAA 1997

8-1

8-1(1)(a)

Div 35

Case references

Commissioner of Taxation v Myer Emporium Ltd [1987] HCA 18; 163 CLR 199; 87 ATC 4363; 18 ATR 693

Greig v Commissioner of Taxation [2018] FCA 1084; 2018 ATC 20-662; 108 ATR 491

Other references

TR 92/3

TR 92/4

TR 2001/14

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