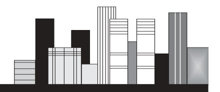

Mass marketed tax scheme cases[1]

Robert Gordon*

Introduction

In the late 1970s, the need for retrospective 'bottom of the barbour' legislation arose due to the failure of the ATO to identify and shut down the sale of current year profit companies to scheme promoters. The then Treasurer John Howard was the first Treasurer to take such truly retrospective steps, ie, not just to change the law with effect from the date of announcement.

Except perhaps in a small way in 1988 and 1989, the 1980s were somewhat quiet on the mass marketed schemes front, as the Commissioner was in the habit of threatening to apply Part IVA (the general anti-avoidance provision introduced in 1981 to replace the then apparently toothless s260), but was shy of having the provision tested before the courts, anecdotally, on the basis that the provision was more useful to him while its coverage was uncertain.

The introduction of s82KZM with effect from May 25, 1988 did not have a major impact on scheme activity, as it was generally possible to ensure that the thing agreed to be done for which the expenditure[2] was incurred, would be done within 13 months of incurring the expenditure. If not, the deduction was to be spread rateably over the period for which the thing was to be provided, or if from more than 10 years, spread rateably over 10 years. For instance, interest would only be prepaid for say, 12 months. Management fees would be charged at the end of a year, for the whole of the year to come.

What started to change by 1990 was the Commissioner giving non-binding Advance Opinions to persons who might seek to exploit a perceived advantage from reliance on the Opinion to a much boarder class of taxpayers than the ATO presumably intended. As much can be seen from the pleadings in *Remuneration Planning Corporation Pty Limited v FCT (2001) 46 ATR 400 at 404*, concerning whether the Commissioner is estopped from applying binding public ruling TR99/5 at least before the date it was issued, in relation to a form of 'mass marketed tax effective scheme' known as the 'employee benefits trust'.[3]

By the late 1990s, the system of private binding rulings introduced with the system of self assessment in 1992, had been used by some scheme promoters to give the impression to the public that the view expressed in a particular private ruling for one individual was likely to be available to all persons with the same arrangements, or even only similar arrangements. The charges against former Second Assistant Commissioner for 'strategic intelligence', Nick Petrolious, stem out of his alleged exploitation of his position in relation to the giving or influencing the giving of such rulings to promoters, when his job was to shut aggressive tax planners down.[4]

Mass Marketed 'Tax Effective' Schemes

It would seem that a 'mass marketed tax effective scheme' is one more likely to be tax effective if not 'mass marketed', but becomes subject to attack if 'mass marketed'. Whilst there may be some disagreement as to the definition of what a 'mass marketed tax effective scheme' is, the Commissioner applies the concept to widely promoted arrangements including:

1. Agricultural schemes with either: round robin and limited recourse funding, or the initial subscription being used to fund a guaranteed return (1994-1997);
2. Film schemes using Div 10B or s51(1) with either: round robin and limited recourse funding, or the initial subscription being used to fund a guaranteed return (1995-2001);
3. Retirement villages using s51(1) with round robin and limited recourse funding (1995-2000).
4. Employee Benefit Trusts (1989-1999);
5. Non-complying New Zealand superannuation

schemes (1997-1999);
6. Controlling shareholder superannuation schemes (1997-1999);

Pro forma settlement offers originally made by the Commissioner did not extend to all these arrangements, but only to agricultural and film schemes. However, the Commissioner is now seeking to settle cases in all mass marketed schemes.

Whilst each of these arrangements may have been carried out for years before the 'start' date referred to above, the problem in each case was that it took years from the time the particular arrangement started to be heavily promoted, before the ATO's views were made sufficiently public to stop their widespread promotion, pending judicial clarification or legislative action. The longer there was silence from the ATO, the greater the ability of the promoter to allege that the arrangement didn't offend the ATO. Ultimately the deductions at stake across all these schemes was of the order of $4.495 billion.[5]

Prepayments

On the legislative front, the further 'clamp down' on prepayments was effected by the introduction of ss82KZMA — 82KZMD with effect from September 21, 1999 and ss82KZME — 82KZMF from November 11, 1999. These provisions phased in over a four year period, a regime whereby most business taxpayers would only be able to deduct prepaid expenditure, over the period to which it relates, with the notable exception of prepaid interest on rental properties, publicly traded shares and units in widely held unit trusts,[6] in which case the prepayment could be for up to 12 months[7] and still be immediately deductible.

Individuals not carrying on business, and STS taxpayers[8] continue to be entitled to deduct all other wise deductible amounts for up to 12 months,[9] except those under managed investment schemes.[10]

Non Commercial Business Losses

A further legislative measure was introduced with effect from July 1, 2001, termed the 'non commercial business loss' provisions, contained in Div 35 of the 1997 Act. They apply where an individual (alone or in partnership) would otherwise be entitled to offset a deduction from carrying on a business against other income, unless one of four tests is met. Rather than define when a business is being carried on, the approach is to quarantine losses from that 'business' if one of the four tests is not met. This measure is clearly directed at 'hobby' farms and direct marketing franchisees, eg, Amway. The four tests are the 'assessable income test', the 'real property test', the 'other assets test', and the 'profits test'.

The 'assessable income test' requires the assessable income from the business to be at least $20,000 for the year. The 'real property test' requires real property with a reduced cost base of at least $500,000 to be used on a continuous basis in the business. The 'other assets test' requires the total value of other assets (excluding motor vehicles) to be at least $100,000. The 'profits test' requires the business to have resulted in a taxable income in at least three out of the last five income years (including the current year).

The Commissioner has a discretion that Div 35 not be applied in s35-55(1)(b) if he is of the view that, there is an objective expectation, based on evidence from independent sources (where available) that within a period that is commercially viable for the industry concerned, the business activity will meet one of tests.

Unless the individual taxpayer concerned is relying on the second limb of what is now s8-1 ('expenditure necessarily incurred in carrying on a business'), the 'non commercial business loss' provision will not be relevant. However, as the Commissioner will assert that the taxpayer in a managed investment scheme that does not have a Product Ruling, needs to be in business though the medium of the manager of the scheme, in order for the purported deductions to be available, Div 35 will be a problem for those investors. The Commissioner invariably agrees to exercise his discretion to treat Div 35 as not applicable if he gives an investment scheme a product ruling.

Forestry

Having caused the managed forestry industry near collapse[11] due to the tightening of the prepayment rules impacting on investment in such schemes in June, 2001, the prepayment rules relating to that industry were essentially reversed by the introduction of s82KZMG with effect from October 2, 2001, whereby the prepayments for such investments for up to 12 months were again made allowable.

Margin Lending

The exception for 12 months prepaid interest on rental property, publicly traded shares and widely held unit trusts created a boom in 'margin lending' and products which specifically made use of the exception.

Equity Linked Bonds

For example, the Macquarie Equity Linked Bonds were financed by Macquarie with interest payable 12 months in advance, and paid an interest rate in arrears at a base

lower rate, together with extra interest if the All Ordinaries Index or particular nominated shares (at the investors choice) moved up by more than 30 per cent. In the case that extra interest became payable the investor was ahead, but not otherwise. If no extra interest was paid, it was hoped that at least a deduction was allowable for the prepaid interest. No test case has to my knowledge been mounted to challenge the Commissioner's disallowance of the interest deductions.

Capital Protected Loans

In *FC of T v Firth 2002 ATC 4346* (Full Court), special leave to appeal to the High Court was refused November 5, 2002. In that case, the taxpayer, a Sydney solicitor had margin loans on publicly listed shares, the interest rate being higher than it would otherwise have been, as the lender had no personal right of recourse against the borrower, but only had recourse to the listed shares. Ultimately the taxpayer did not need to rely on the limited recourse as his shares appreciated by millions. However, the Commissioner disallowed the extra interest on the basis that it was a capital cost of buying protection against a loss on his shares. The taxpayer won. The Treasurer announced on April 16, 2003 that the law will be changed to disallow such extra interest incurred after the date of the announcement.

Agricultural schemes

FCT v. Lau (1984) 16 ATR 55, 84 ATC 4929 involved an afforestation project where Dr Lau borrowed on a limited recourse basis from a finance company associated with the promoter, and obtained a tax deduction for the payment of management fees using the borrowing from the finance company, even though the transaction was effected by a round robin. The Commissioner also lost on the s82KL argument as it was said that whether there was any additional benefit from not having to repay the borrowed funds, was a question which could only be answered at a later time. The Commissioner accepted the result in the administratively binding ruling IT2195 issued on September 24, 1985.

The main 'thrust' of the ATO's position papers issued to promoters before disallowing deductions, is to refuse to follow Lau's case, and not to apply the ATO's own ruling, as was acknowledged in the ATO media release (June 9, 1999) concerning the Ombudsman's report into the behaviour of the ATO in the arrangements which ultimately litigated as the *Budplan* case.[12]

IT2195 had the effect, by way of example, that by 1994 the Main Camp tea tree oil project was creating a huge tea tree oil plantation on the NSW north coast using this technique, so that the tax deduction obtained by the participant far exceeded the amount of arm's length funds being put into the project by the participant. In fact, the tax refunds were often funding the participants' contributions. As the Commissioner did not act quickly, those investors who claimed deductions before 1996 cannot now have their deductions disallowed, as the Commissioner is out of time, as the relevant assessments are now more than six years old, being the limitation period where Part IVA applies. Note that if the Commissioner only relies on s51(1) not being applicable, the relevant limitation period is four years.

By 1996 the promoter of Main Camp (Mr Stotter) decided to use the same technique to fund research into the use of the Main Camp tea tree oil, under the so called 'Budplan Syndicates', in which it is now said there are about 9,000 participants with tax deductions claimed of about $500 million. Many other agricultural schemes were also established, growing apples, plums, grapes and other agricultural products utilising the general deduction provisions for management, maintenance and licence fees; and the specific deduction provisions contained in sections 75B and 75D for irrigation systems and drainage works and soil erosion control.

Originally the ATO test case funding program denied funding for cases such as *Budplan* as they involved 'tax avoidance'. However, in view of the public importance of attacking mass marketed schemes, the policy was altered to allow funding of selected 'test cases' where Part IVA was in issue. Two-thirds of the way though the litigation, the ATO agreed to providing funding for the *Budplan* case.

The Commissioner didn't agree that the outcome of the *Budplan* case should legally bind him with respect to those participants in Budplan Scheme, other than the test case individuals. He sought to arrange for taxpayers to become test case individuals, who he thought were representative of the different types of factual backgrounds that might have been relevant to the application of Part IVA. Ultimately, that was a difficult task, as invariably very few people are brave enough to become the test case individuals. Interestingly, one participant in BPS had a positive private ruling concerning his investment, but not surprisingly, the Commissioner said he was not 'representative', and he fought hard and successfully to keep that person out of the test case.

The use of round robins and limited recourse funding from associates of the promoter was first attacked by the withdrawal of IT2195 and the issue of draft ruling TR97/D17. The draft ruling did not turn into a final ruling[13] until it issued as TR2000/8.

From July 1, 1998 the Commissioner has instituted a system of 'Product Rulings' whereby he provides assurance of the tax outcome of managed investment structures, often confirming that the participants who 'don't get there hands dirty' as they have appointed managers, are none the less entitled to deductions as carrying on business when he denies that outcome to those who have not applied for a Product Ruling. He has now issued over 585 Product Rulings.[14] Without a Product Ruling, a mass marketed scheme is unlikely to be able to achieve market credibility, especially after *Budplan*.

Further, absent a Product Ruling an investor in a managed investment scheme is now likely to have a Div 35 problem. The irony of this is that before Div 35 was introduced, the Commissioner would invariably assert that investors in managed investment schemes without Product Rulings were not carrying on business, which he said meant they weren't entitled to deductions under the second limb of s8-1 (previously s51(1). Now he is likely to assert that the same person is carrying on a business though the scheme manager, but apply Div 35 to quarantine the losses.

In his Product Rulings he now invariably accepts that the taxpayer is carrying on business through the manager, but he exercises his discretion under s35-55(1)(b) to allow the deduction that otherwise would have been quarantined.

He also accepts that services to be provided by a manager under a managed investment scheme, will be provided in the same year as the investor put in his first year's contribution, even though the investments are accepted up until mid June in the relevant year, thereby overcoming the operation of s82KZME. For those without a Product Ruling, invariably he would argue that the services won't be provided until the end of the following year, with the effect that apportionment will be required and most of the deduction will be in the following year.

A problem for invested in managed schemes, even those with a Product Ruling, is that the manager may unbeknown to the investor, not implement the scheme as promoted and as described in the Product Ruling. *Carey v Field (2002) ATC 4837* is a recent decision as to when the Commissioner can withdraw a Product Ruling.[15]

Budplan

In *Howland-Rose & Ors v FCT ((2002) 49 ATR 206: 'Budplan'),* the Federal Court (Conti J) affirmed the Commissioner's decision to disallow amounts plus interest loaned to investors for participation in the Budplan Personal Syndicate ('BPS') for research into the use of tea tree oil. The BPS was one of many 'Budplan Syndicates'. The case was a test case in relation so called 'mass marketed tax effective schemes'. The test case applicants were four out of 2371 taxpayers who invested in the BPS pursuant to a prospectus.

The ratio of the decision in the Budplan case was that the expenditure was not deductible under s51(1) as it related to research and development when there was no pre-existing business to which the research related, and was not related to the derivation of assessable income. What was said otherwise, was *obiter*.

The *obiter* was occasioned by the fact that it was a test case likely to go on appeal. However, it is the *obiter* which is the most interesting aspect of the case, as most of the deductions claimed in other limited recourse lending schemes, was not on research and development. Hence the *Budplan* case was an unusual case to choose as a test case, other than that it involved a lot of participants and potential tax deductions in monetary terms. However, his choice of test case was not as bad as in his attempt to justify his so called 'Statement of Principles' (June 9, 1999) concerning trust resettlement. There he litigated *FCT v Commercial Nominees to the High Court (2001) 47 ATR 220* and lost, then claimed that it wasn't a relevant precedent.[16]

Conti J held that if the expenditure in *Budplan* was contrary to his view, deductible, that Part IVA would apply to disallow the deduction, as it was apparent from the prospectus that the dominant purpose for investing (objectively determined) was to obtain the promoted tax deductions. Indeed, for a taxpayer on the top marginal rate, if a tax deduction was allowed, the taxpayers net cash position would be positive even if no assessable income was ever derived. This was because the tax refund exceeded the cash outgoing required to participate. Of course it was the 'round robin' feature combined with the loan being limited recourse, as in Lau, which created this result.

Vincent

Vincent v FC of T 2002 ATC 4490 was the second case to deal with 1990s 'mass marketed tax effective schemes'. The taxpayer was one of several hundred people who, in the mid 1990s invested in a cattle breeding project. Ms Vincent claimed tax deductions in 1995 in respect of rent and management fees and prepaid interest on money borrowed from the promoter's finance company to pay part of the rent and management fees in connection with the project. In 1996 the deduction claim was only for rent and management fees.

French J found that Ms Vincent entered into the project in good faith after taking advice from her accoun-

tant. The gaining of a tax benefit was not her principal purpose. It was her hope that the scheme would eventually yield a modest income stream for her and her family. In the end the scheme has failed, the companies involved have been placed under administration and the deductions disallowed.

French J held that while the taxpayer was entitled to a deduction under s51(1), the outgoings being incurred for the purpose of deriving assessable income (ie, the 'first limb', it having been conceded she was not carrying on a business), and not being capital, as the finance company had not paid the contracted for rent and management fees to the manager, the taxpayer was only entitled to a deduction for that part of the rent and management fees which did not come from the finance company. In fact, she had borrowed those amounts from her father. She was not entitled a deduction for interest on the funds not advanced by the finance company.

However, French J held that Part IVA applied to disallow the deductions otherwise allowable, on the basis that a reasonable person would conclude based on the eight listed factors in s177D(b), that taxpayers entering the project did so for the dominant purpose of obtaining the tax deductions. From an objective point of view, there was little other benefit to be derived.

On the taxpayer's appeal, the Full Court (2002 ATC 4742) took quite a different approach. They held that as the underlying agreements was that the manager guaranteed to supply six calves to the owner with the time stipulated, and as the taxpayer was not carrying on a business, the cost of the acquisition of the calves would not be trading stock, and therefore the outgoings to produce the six calves were an outgoing of capital, and therefore not deductible.

However, as the claimed amounts were not deductible, the Commissioner's amended assessment for the 1995 year was out of time, and the appeal was allowed for the 1995 year. The appeal was unsuccessful for 1996.

Interestingly, the Full Court said in relation to Part IVA, that French J did not make an appealable error in holding that the promoter had carried on the project for the dominant purpose of obtaining a tax benefit for the taxpayer, it would be inclined to the view the dominant purpose of the promoter was the obtaining of profits by companies in the promoter's group.

Puzey

The third agricultural 'mass marketed schemes case' was *Puzey v FC of T 2002 ATC 4853*. In that case the taxpayer invested in a sandalwood project which in the 1997 year involved him in agreeing to purchase seedlings for $40,000, but only $100 'upfront', with the balance not payable until June 30, 1998. He also entered into a plot lease and a management agreement. He borrowed the required $39,900 from a finance company associated with the promoter, with recourse only to the project. In May 1998, under a restructured arrangement forced by the ASIC, he became a beneficiary of a forestry trust, but again agreed to purchase more seedlings for another $40,000, again financed by a company associated with the promoter, again with limited recourse.

Lee J held that the taxpayer had incurred the obligation in relation to the $40,000 in each of the 1997 and 1998 tax years, notwithstanding the nature of the loan agreements, and that he was carrying on a business though the manager until the restructure in May 1988.

For the 1997 year Lee J held that the deduction claimed was allowable under the second limb of s51(1) and for the 1998 year, that the deduction claimed was allowable under the first limb of s51(1), and were not capital.

However, on the basis of the evidence that the seedlings for which the taxpayer had paid $40,000 should have only cost about $3,000, this feature was such that objectively determined the dominant purpose of a taxpayer in entering into the scheme was to achieve a tax benefit.

Cook & Jamieson (appeal pending)

The fourth agricultural 'mass marketed schemes case' was *Cook & Anor v FC of T 2002 ATC 4937*.

The taxpayers at the time they invested in the Australian Horticultural Project No 1 in 1988, where partners in Allen Allen & Hemsley, and then contemplating retirement.

The project was offered pursuant to a prospectus to allow investors to conduct their own business of growing Australian native flowers.

Investors engaged a manager to carry on the business on their behalf, and the management fees for which deductions were claimed, were funded by a finance company associated with the manager.[17] The loans were full recourse, but the manager guaranteed a return which would repay the loans at the end of the project. The finance company in turned borrowed the moneys from a bank.

The guaranteed returns were funded by the manager placing sufficient of the management fees it received, on deposit with the finance company, rather than expending them on the project.

Without reference to any of Howland-Rose, Vincent or Puzey,[18] Stone J held that the taxpayers were entitled to deductions under s51(1). Her Honour held that the

taxpayers were carrying on the business of growing flowers; they were not merely passive investors.

Part IVA did not apply as the analysis of the eight factors in s177D(b) were all consistent with the taxpayers having a dominant purpose of generating income for retirement rather than obtaining a tax benefit.

Zoffanies (appeal pending)

Whilst this Tribunal case (2002 ATC 2129) dealing with R& D deductions for research into genetically modified pigs was not a mass marketed scheme as such, it did have elements of one. The taxpayer, which was a subsidiary of Macquarie Bank, had losses transferred to it in 1992 by another subsidiary, disallowed. The tranferor (MS3) joined a syndicate 99:1 with Bresatec, which was the owner of the relevant IP. MS3 was funded by Macquarie Bank with $10m of equity and $17m of debt.

Bresatec licenced Luminis (which was a tax exempt subsidiary of the University of Adelaide) with the IP for $269,000 plus a royalty. Luminis then granted the syndicate a licence for 15 years to use the IP, in return for a lump sum of $15m. There was valuation evidence that the rights granted may be worth that amount. There was nothing said by the Tribunal as to the commerciality of Bresatec's licence to the tax exempt body.

Bresatec granted Macquarie Bank a put option over its shares in MS3 for $45m, exercisable in 2000.

The syndicate then paid Luminis $12.125m (including a $3.125m profit element) to undertake research on its behalf.

All of the moneys received by Luminis from the syndicate were placed on deposit with Macquarie Finance. $8.9m was drawn down over time by Luminis to undertake the research.

In 2000 Macquarie Bank put its shares in MS3 (together with the debt owned by MS3 to Macquarie which was $10m together with $18m of capitalised interest) to Bresatec for $45m, which the Tribunal said was funded by the 'deposit in Luminis' name,[19] accruing since 1992, with Macquarie Finance'.

What isn't clear is why Bresatec was entitled or allowed to use Luminis' money to pay out Macquarie Bank.

I surmise that what has really happened here is that the $15m paid by the syndicate to Luminis has accumulated tax free for eight years because of Luminis' tax exempt status, and has thereby grown to largely fund Bresatec's buy back from Macquarie. That is, Macquarie has got a deduction for $15m in 1992, and got it back at no real cost to Bresatec by virtue of it being placed on deposit tax free for eight years.

However, the Tribunal found MS3 was entitled to a deduction for the $15m cost of the 'core technology' under s73B. There was apparently no dispute about the claim for the actual R&D work. The capitalised interest[20] accrued by MS3 was deductible under s51(1). The parties were dealing with each other at arm's length.

Further, the objective of Bresatec and Luminis was to raise funding to finance ongoing research. The dominant purpose of Macquarie and MS3 was investment, and undoubtedly an important purpose of the scheme was to achieve a tax benefit, a reasonable purpose would conclude that it was not the dominant purpose.

Film schemes

These schemes broadly fall into one of two categories, whether the deductions are claimed over two years under Div 10B, or in the first year, under s51(1):

1. Guaranteed return films, where 100 per cent is borrowed and claimed as a deduction, and a guaranteed return of say, 105 per cent received several years later, all of which was represented as assessable, ie, essentially a deferral 'product';
2. Films partly financed with a round robin limited recourse loan, in which the participants' own and borrowed funds would be 'expended' on making the film, but with no guaranteed return.

The cost of acquiring the copyright in a film is a capital expense. However, Div 10B allows a deduction over two years for such capital expenditure.

In schemes relying on s51(1), the expenditure was said to have been incurred on providing services[21] to those making the film, termed, eg, 'production services' and the expected income was framed as fees for providing such services, termed, eg, 'production service fees'.

The guaranteed return films have been attacked by the Commissioner indirectly by his general approach to capital guaranteed products, wherein he says that if the participant bears no risk, no deduction is available (TR2001/D7). Where shares are bought with borrowed funds at a higher interest rate due to the limited recourse nature of the loan, he has ruled in PR2000/70 and previously stated in press release Nat 99/26, that the interest must be apportioned to exclude from deductibility that part that he says in effect funds the capital guarantee. He lost that argument before the Full Federal Court in Firth. The Treasurer announced on April 16, 2003, that the law would be amended from that date to disallow a deduction for that part of the interest expense representing the cost of the capital guarantee, thereby overcoming the decision in Firth. However, that announcement does not deal with the subscription moneys for a film being used to fund a guaranteed return. If *Cook &*

Jamieson is upheld on appeal, then there may still some scope for this technique.

The s51(1) limited recourse round robin films were in fact, but not by name, attacked by the issue of TR97/D17, referred to above in relation to agricultural ventures. The Div 10B film schemes were directly attacked by the issue of draft tax ruling TR2001/D7 on September 26, 2001, which cross references TR2000/8 (at para 95) and specifically refers to limited recourse loans (at para 66) and round robins (at paras 95-6).

Case 2/2002

Whilst this Tribunal case (2002 ATC 109) was not a mass marketed scheme as such, it had elements of one. RAL was a subsidiary of an Australian Bank. T and L were RAL's subsidiaries, and T and L formed a 99:1 partnership. They sought a private ruling that T and L would be entitled to deductions under Div 10B in relation to a complicated arrangement, in which they would have little commercial risk. The reduction in commercial risk was achieved by a combination of income guaranteed by an indemnifier (SFPL), and an ability to call for the indemnifier to subscribe capital in T and L.

Whilst the AAT's reasons for decision said SFPL was not 'associated' to the other parties to the arrangement, it appears that it must have had the support of some of them or else it would have no reason to provide the indemnity or agreement to subscribe for capital.

The partners (T & L) entered into an agreement with a US film Studio to buy the rights to a film for 15 years for A$105M, which was 122.5 per cent of the cost of the film to the Studio. The partners were capitalised by RAL as to 20 per cent of the required $105m, and borrowed the balance from RAL at a commercial rate of interest.

The Studio was owned by TCF. The partners then licensed TCF to distribute the film for 15 years, in return for licence fees which gave the partners a 50 per cent chance of receiving more than $220m over the 15 years.

My surmise is that 22.5 per cent of the $105m to be paid to the Studio (and the return on the investment of that amount for up to 15 years), would somehow fund the guaranteed return and subscription of capital by SFPL.

A firm of accountants were to be paid $500,000 to manage the partnership.

The Tribunal did not deal with how the guaranteed return and subscription of capital by SFPL was to be funded. In any event it held the $105m of deductions sought to be claimed under Div 10B were not allowable, and nor were the management fees to be paid to the accountants.

The Tribunal found that the practical effect of the distribution agreement was that the partners did not use their interest in the copyright in the film in the way required by Div 10B, and the Div 10B deductions sought were not allowable. Further, there was no business of the partnership which the accountants could manage, and so no s51(1) deduction would be available for the management fee.

Even if the deductions otherwise qualified under Div 10B, the $105m price for the film rights was not an arm's length bargain.

Even if the deductions were available, Part IVA would apply, as looked at objectively, the dominant purpose of the scheme was to achieve the tax benefits.

Krampel Newman

The taxpayers in this case (2003 ATC 4304) contracted with an Australia production company paying it $1.126m 'upfront' in June 1994 to produce a feature film provisionally entitled *Mephisto's Web*, using material from an existing TV animated series, for which the taxpayers agreed to pay a further $6m to the owners of the TV series, but only out of the proceeds of the exploitation of the copyright to *Mephisto's Web*. The taxpayer claimed deductions totalling $7.126m for the 1994 and 1995 years.

The documentation was such that the taxpayers did not get a copyright to a feature film *Mephisto's Web* and their claim for deductions under Div 10B failed for that reason.

Ryan J went on to hold that in any event, the taxpayers had not incurred the deferred $6m in the 1994 year or at all.

If he was wrong on those points, s82KL would disallow the deduction as the additional benefit[22] of not having to pay the $6m, together with the tax benefit of the deduction on $7.126m, exceeded the gross amount of the deduction ($7.126m).

Further, the difference between the cash outlay of $1.126m and the purported deduction for $7.126m was such that the dominant purpose of a taxpayer investing the film must have been to obtain that tax benefit, and therefore Part IVA would apply to disallow any deduction, if it was otherwise available.[23]

Retirement Villages

The whole tax driven retirement village industry was born out of a clearly incorrect taxation ruling: TR 94/24. That ruling was withdrawn on April 19, 2000, and was subsequently replaced with TR 2002/14.

The cost of developing retirement villages incorrectly said to be deductible under TR94/24 became of immense interest to the promoters of tax schemes as the deduction could be 'ramped up' by the usual limited

recourse loan method.[24] They had the added attraction of being an investment in 'bricks and mortar'.

Before the withdrawal of TR94/24, taxpayers may have relied on opinions that s82KZM did not require apportionment of the deductions over the period of the project. These opinions said that s82KZMA did not apply to the acquisition in the future of real property, on the basis that the section only applied to the provision of services or the 'doing of a thing' over time. However, the Explanatory Memorandum that introduced the provision refers to its application to supply of goods or services Whilst clearly real property is not goods, the assumed limitation of the application of s82KZMA only to services, may not stand up.[25]

'Drivers' of Wholesale Tax Avoidance: Limited Recourse Loans & Subscriptions Funding Guaranteed Returns

Product Rulings invariably expressly state that deductions will not be available to the extent that finance is provided involving limited recourse loans.

In that event, the Commissioner says he will apply Part IVA. As some of the recent case have dealt with this issue in cases that preceded the advent of Product Rulings, it is important to see whether the Commissioner is right, or else the 'drivers' of wholesale tax avoidance may survive. I tackle that issue after briefly mentioning the other mass marketed schemes, which don't use these 'drivers'.

Employee Benefits Trusts

Essentially these arrangements involved an employer sponsoring a trust for the benefit of that employer's employees, by paying an arguably deductible contribution to the trust, for investment of those funds to produce a deferred benefit to the employees from the trust in due course. It was represented that the contribution was deductible to the employer, and the receipt by the trust did not create a fringe benefits tax liability for the employer. Whilst those arguments were tenable when the employer company was really seeking to benefit arm's length employees, and with the benefit of hindsight this would be proven to be the case, promoters 'sold' this arrangement to companies who only had two shareholders and who had no non-shareholder employees, such that the only people likely to benefit from the arrangement would be the shareholders. As they were always the ones to benefit from the performance or otherwise of the employer company, they hardly needed the trust structure to achieve it. This was especially so where the arguably deductible contribution was loaned back, interest free to the employer company.

These arrangements were extremely widespread, having started in about 1988, albeit not in a big way until about 1993. The schemes which were not bona fide were largely stopped by the issue of TR99/5. The Commissioner's offer to settle these schemes has to date been on less generous terms than with agricultural schemes. Whether any of them actually work may see the light of day, as the critical issue for each arrangement will be its bona fides, and that will be dependent upon its own particular set of facts. Astonishingly, some schemes have never paid any benefits to employees, with all contributions immediately lent back to the employer. Other schemes, which are performance based, pay employee benefits on a regular basis to employees who achieve pre-set performance, sales or profit criteria.

Essenbourne

The taxpayer company in this case (2002 ATC 5201) was the owner of a motor dealership controlled by the Marino family, in which three sons were employed and owned shares, and each of whom were paid salaries of only $25,000. In 1992 the Essenbourne Superannuation Fund was established to which age-based contributions were made. In 1994, at the suggestion of the company's accountant, an employee share plan was established to which the company contributed $225,000 for the benefit of the three sons, being the difference between their salaries and an amount that would retain their services in the business.[26]

Again at the suggestion of the company's accountant, in 1997 the employer company established an Incentive Trust. The company contributed $252,000 to the trust, and each of the three sons was allotted 84,000 employee units, paid for by an advance from the trust. During the life of the trust, the employee units were entitled to receive distributions of income. The employer company had no right to get any part of the income or capital back from the trust, but curiously, the Essenbourne Superannuation Fund held a residuary unit to receive distributions on a winding up of the trust.[27]

Suggestions were made in evidence that one of the brothers (Sam) was considering leaving the business and this was the motivation for setting up the Incentive Trust.

However, Sam did not give evidence, and the rule of evidence therefore worked against this motivation being accepted, and in any event Sam was not being provided for any differently from the other brothers.

The Commissioner disallowed the deduction to the employer company for the $252,000 contribution, and also, in the alternative, assessed the employer company

to FBT for the provision of a benefit to employees of $252,000.

Kiefel J held that the contribution to the Incentive Trust effected a distribution of profits of the employer company, and was not an expense of the company referable to the company's business. It was a distribution of profits of the company: a payment on capital account.

Her Honour held that as no particular employee could be identified as benefiting as a result of the contribution to the Incentive Trust, that the FBT did not apply to the contribution.

As the contribution was not deductible, it was not necessary to decide the Part IVA point, but Kiefel J said obiter, that it was unlikely that no like-sized deductible superannuation contribution would have been made in the 1997 year, if no contribution had been made to the Incentive Trust.[28]

The Commissioner did not appeal the FBT decision but has refused to withdraw TR99/5. He has said that he does not accept the logic of the decision and will look for more suitable cases in which to test the position. The implications of the Commissioner's approach for the Rule of Law have been pointed out to him in strong terms by the Law Council of Australia.[29]

Kajewski

The taxpayer and two family members in this case (2003 ATC 4375) were the directors of Askena Pty Limited, which conducted a rural machinery business as trustee of the taxpayer's family discretionary trust.

In 1990 Askena expected a much larger tax liability for the beneficiaries than in the previous year. The accountant to Askena, Mr Steve Hart, suggested that Askena set up an employee retention plan. The taxpayer said this was as he was contemplating leaving the business, and the plan would encourage him to stay.

In June, 1990, Askena executed documents to establish the Askena Staff Benefits Trust. The evidence was that Askena was to make a contribution of $200,000 to the plan. It paid $25,400 of its own money into the plan's bank account in June 1990. Mr Hart was to arrange from Askena to borrow the balance from AMP Chase before June 30, 1990, which the trustee of the plan (a Harts' company) was to invest in an AMP Life policy with an investment component.

Late in 1990, the taxpayer was first told Mr Hart had caused the borrowing to be under taken from Mevton Pty Limited (controlled by Mr Hart), and the life policy to have been taken out with Security Life, a Vanuatu company, from improbable reasons. Askena had made payments totalling $97,196 in purported repayment of the loan. Drummond J found that the documentation of the loan and the insurance policy were probably fabricated.

Based on the apparent fraud[30] by Mr Hart, Drummond J held that the Commissioner was empowered to amend the taxpayer's 1990 assessment (more than six years old), and that the taxpayer had not satisfied the burden of proof that any of the $200,000 was deductible in the 1990 year. As to the $174,600 purported borrowed from Mevton Pty Limited, that there was never any loan made, which Askena could have contributed to the plan. As to the $25,400, that there was insufficient evidence lead, to characterise the payment.

For present purposes, it is important to note that Drummond J was only prepared to assume[31] that if the $200,000 was actually contributed to the plan before June 30, 1990, for the purpose of retaining the taxpayer's services, that is would have been a business outgoing, within s51(1). However, His Honour found the plan was not set up for that purpose,[32] but rather was part of a 'mass marketed tax avoidance[33] arrangement'. Not surprisingly, His Honour did not consider Part IVA.

Non-complying New Zealand superannuation schemes

These arrangements were less widespread, presumably as they involved a New Zealand element, which even the most brazen types must have wondered about, for anyone with no New Zealand connections, and no international business purpose. The contribution was allegedly not subject to the superannuation surcharge as the recipient fund was not a resident of Australia, nor was fringe benefits tax said to be payable due to the provisions of the Australia/New Zealand double tax agreement dealing with fringe benefits tax.

They started in about 1997. They were largely stopped by the issue of TR99/5 and were later legislatively stopped from the date of the issue of the ruling, by the repeal of s82AAE to preclude deductions for contributions to non complying funds (Act 89 of 2001, with effect from 4.00pm AEST on June 30, 2000). Prior to the amendment, a literal construction of s82AAE would have allowed the deductions for contributions to non complying New Zealand superannuation funds.

I understand there is a case to be heard by the Federal Court (Wallstern). In that case I understand that the Commissioner has taken the view that Part IVA can have no application as the dominant purpose of contributing to a super plan must be to provide retirement benefits, and this is mutually exclusive of having a dominant purpose of obtaining a tax benefit.[34]

Controlling shareholder superannuation schemes

The arrangements involved an individual arguably obtaining deductions for superannuation contributions to a non complying fund when they were the controller of an employer company. The argument that the deduction was available relied on a literal construction of s82AAA which were not supported by the apparent intention of the superannuation provisions read as a whole (assuming it is still possible to glean overall policy objectives in a legislative scheme characterised by its obscurity and obfuscation). The contribution was arguably not subject to the superannuation surcharge as the contribution was for oneself not another, nor were fringe benefits said to be payable to any particular employee.

These arrangements were widespread, although they only started in about 1997. They were largely stopped by the issue of TR99/5, and were later legislatively stopped from the date of the issue of the ruling, by the repeal of s82AAE to preclude deductions for contributions to non complying funds.

Many taxpayers did not claim the deduction at first instance and may exercise their right to object based on any test case determinations in the interim.

Harris (Full Court)

The taxpayer in this case (2002 ATC 4659) was a director of G Harris Automobile Pty Ltd and held a controlling interest in it. The company, as trustee of the the Harris Wood Unit Trust carried on business as a motor vehicle dealer. In the 1998 tax year, Mr Harris established the POHA Superannuation Fund for the purpose of providing benefits for, amongst others, himself, and in that year he contributed $315,600 on his own behalf.

Affirming the decision of Merkel J disallowing the deduction, the Full Court held that since 1915 the statutory scheme in the Commonwealth income tax law contained a dichotomy between the deductibility of contributions to a super fund made by an employer for an employee, and another for contributions for the taxpayers own benefit.

Prebble

The taxpayer in this case (2002 ATC 5045) was a doctor and a director of his medical practice company, and held a controlling interest in it. In the 1998 tax year, Dr Prebble established a non complying super fund for the purpose of providing benefits for, amongst others, himself, and in that year he contributed $300,000 on his own behalf.

Cooper J decided the case after the Full Court decision in Harris, and held he was bound by it.

It of interest that Cooper J reduced the culpability component penalties on the basis that the taxpayer had a 'reasonably arguable position' as the Commissioner himself had issued private binding rulings[35] that such contributions were deductible, until he changed him mind.

The Commissioner has subsequent to the Full Court decision, settled controlling shareholder super cases on the basis of no culpability component penalties.

Recent Cases, Round Robins and Limited Recourse Funding

The 'driver' in Lau's case in 1984 was a round robin and limited recourse loan. The use of a round robin did not of itself cause the highly artificial annuity scheme the High Court dealt with in 1991 in Fletcher[36] to fail, although that was a s51(1) case not dealing with Part IVA.

In *Budplan*, Conti J did not find the $57m round robin where the finance company had no money to lend, to mean the funds weren't actually advanced. *Budplan* does not deal with *Merchant's case ((1999) 41 ATR 116)*, where the Federal Court held that the funds purported to be advanced there, in similar circumstances, were not in fact advanced, in reliance on the authority of the Queensland Court of Appeal in *Australian Horticultural Finance Pty Ltd v Jekos Holdings Pty Ltd* (December 9, 1997 unreported), where loans were purported to be effected by a round robin, but where it was held the funds were not advanced as the lender had no money to lend. In *Merchant*, the taxpayer was however, said to be entitled to the deduction for management fees, on the basis they were incurred by becoming obligated to pay them under the management agreement, whether or not the loan to make the payment was ever made.

Conti J did refer to Jekos, but distinguished it[37] on the basis that in Jekos the borrowers' case was that they had not been lent the money, whereas in *Budplan* the taxpayers were accepting that they had the money lent to them to pay for the research and management fees 'upon the footing of the financial arrangements outlined in the Prospectus'. However, Conti J did not deal with the fact that the round robin was in fact not disclosed in the prospectus.

At first instance in Vincent, French J found that the amounts to be loaned to the taxpayer under the loan agreement were not in fact advanced, by round robin or otherwise. However, unlike the taxpayer in *Merchant*, French J did not find the taxpayer had in any event incurred the management fee, except to the extent she paid it out of funds borrowed from her father.[38] The Full Court restricted its analysis to whether this $5,250 was capital or capital in nature, and held that they were.

In *Puzey* the seedlings were paid for by round robin,[39] and there was an obligation to make the payments, which Lee J held was sufficient for the taxpayer to incur the expenditure. His Honour cited *FCT v Woolcombers (WA) Pty Ltd (1993) 47 FCR 561* as authority,[40] but not *Merchant*.[41]

In *Krampel Newman* the taxpayers became obligated to make a $6m deferred payment for the copyright in the TV series, but no deduction was allowable on the basis inter alia, that the obligation had not been relevantly incurred, as no payment had been made by round robin or otherwise. No mention was made of *Woolcombers* nor *Merchant*.

The fact that the lending, where it actually takes place, is limited recourse, appears to go more to the Part IVA issue, than whether the outgoing is incurred. Certainly this is so in *Budplan* and *Puzey* where the issue was dealt with head on.

Interesting, in numerous Product Rulings, whilst it is said an in-house finance company lends investors funds on a full recourse basis, and this doesn't offend the ATO policy, I understand, but the rulings don't mention that the finance company doesn't in fact have any funds to lend, but rather, once signing up a 'loan book' of investors on a full recourse basis, it is able to realise funds in the market place by selling the 'loan book' for say, 85 per cent of its face value. So 15 per cent of the funds that on the surface of the prospectus are going into the project are in fact immediately not available to the project.

Recent Cases and Funding of Guaranteed Returns

In *Cook & Jamieson*, the 'driver' was the use of moneys subscribed to fund the guaranteed return. This was not disclosed in the prospectus and Stone J recognised that to the extent this was happening, it had the effect of limiting the amount available for the horticultural activity for which the prospectus raised the money.[42]

Indeed, Stone J seems to have accepted that the diversion of the subscription money to fund the guaranteed return did not challenge the genuine commercial nature of project, and cited[43] Beaumont J in *Lau* where his Honour said, at 218:

'Once it is concluded that the moneys were outlaid by the taxpayer for a real or genuine commercial purpose, any inquiry as to the manner in which those funds were subsequently applied by their recipients is immaterial for the purposes of s51. The reason is that, where, as here, the parties are at arm's length, the use made of the funds by the other parties to the transactions is not capable of throwing any light upon the purpose for which the taxpayer incurred the outgoings.'

In both Case 2/2002 and *Zoffanies* the taxpayers had guaranteed income and a put option, respectively, which had the effect of limiting the risk of both taxpayers. Nor do the reasons for decision make it clear whether the amounts for which tax deductions were claimed indirectly funded the guaranteed return or the put option. However, this does appear to be the case. If this is so, then the cases don't deal with the 'driver' to these highly structured transactions. In any event, for different reasons, one case was successful for the taxpayer (*Zoffanies*) and the other not.

Recent Cases and the purpose of the promoter or advisor

In *CPH Property*[44] the High Court held that Hill J was correct at first instance,[45] to have attributed the purpose of the tax advisers to their client in the relation to Part IVA.

Certainly in *Puzey*, and *Vincent* at first instance, Part IVA was applied *inter alia*, on the basis of the promoters' purpose.[46]

In *Vincent's* case, the Full Court (which included Hill J) said that although the primary judge did not err by concluding that the dominant purpose of the promoter was to secure for the taxpayer a tax benefit, they doubted that they would have reached the same conclusion. They were inclined to the view that the dominant purpose of the promoter in that case,[47] was more likely to have been to 'obtain the profits that clearly would have flowed to the various companies associated with him'.

Such an approach was also followed by another Full Court in *Eastern Nitrogen & Metal Manufactures*,[48] where the dominant purpose of Macquarie Bank who was the promoter, was said to be to sell its financial services.

It is implicit in what was said by the Full Court (again including Hill J) in *Hart v FCT 2002 ATC 4608* that the Bank lending the taxpayers the money must have had a like purpose to that in *Eastern Nitrogen & Metal Manufactures,* whereas Gyles J at first instance, was more focused on the Bank's purpose being to promote a tax effective product.[49] The fact that the High Court has granted special leave concerning Part IVA, shows that this issue is still very much alive, as is the issue of the breath of the Part IVA scheme and the commercial purpose being to 'borrow money'.[50]

In a paper delivered recently[51] by Hill J, entitled 'Part IVA and the Tax Adviser', His Honour concludes that the advisors' purpose in giving tax advice is usually to make fees, but if the fees are dependant on the tax benefit being obtained by the client, then the advisors' purpose will be the obtaining of the tax benefit for the client.

In response to this proposition,[52] The Second

Commissioner of Taxation Michael D'Ascenzo has said in a more recent paper[53] 'Part IVA — The Steward's Inquiry — A Fair Tax System' that the promoters purpose 'is the expected outcome of the scheme activities', ie, the obtaining of a tax benefit by the participants.[54]

There is also a debate as to the extent that the advisors' purpose is to be wholly objectively determined.[55]

D'Ascenzo's paper does not go as far as the Commissioner's address to the TIA National Conference on March 19, 1997, where he attempted to give specific examples of when Part IVA would not apply:

- decision to make a gift to a deductible charity rather than a non-deductible charity;
- decision to buy a building with an ongoing Division 10D deduction rather than an equivalent building with no deduction;
- decision to buy shares that pay franked dividends rather than unfranked dividends; and
- decision to invest in public infrastructure bonds.

But what is the principle as to why Part IVA wouldn't apply in those cases if the objective and subjective purpose of the taxpayer and his advisors, is to achieve a tax benefit?

For Australian purposes there has not been any judicial recognition of the difference between 'tax mitigation' and 'tax avoidance'.[56]

In *IRC v Challenge Corporation Ltd [1987] AC 155,* a decision of the Privy Council, the taxpayer purchased some tax loss companies. The purchase was structured so that it complied with provisions in the New Zealand legislation allowing deductions of losses within a company group. The Privy Council held by a majority of four to one that the transaction was struck down by the general anti-avoidance provision in the New Zealand Act (s99), although there had been compliance with the requirements of the group loss provisions. Section 191 of the New Zealand Act which permitted the transfer of losses within a company group contained anti-avoidance provisions, but the transaction was structured in such a way that these did not apply.

The Privy Council discussed the distinction between tax mitigation and tax avoidance. Lord Templeman, who delivered the majority judgment, pointed out that 'a taxpayer has always been free to mitigate his liability to tax'. However he stated at 167:

'In [*IRC v Duke of Westminster*] however the distinction between tax mitigation and tax avoidance was neither considered nor applied. Income tax is mitigated by a taxpayer who reduces his income or incurs expenditure in circumstances which reduce his assessable income or entitle him to reduction in his tax liability. Section 99 does not apply to tax mitigation because the taxpayer's tax advantage is not derived from an 'arrangement' but from the reduction of income which he accepts or the expenditure which he incurs.'

Lord Templeman then gave examples of 'mitigation' (which perhaps is the 'blueprint' of Michael Carmody's above four examples of when Part IVA will not apply):

- a taxpayer making a payment under a covenant exceeding six years which complies with certain statutory requirements reduces his assessable income (under UK law);
- a taxpayer making a settlement deprives himself of capital which is a source of income;
- a payment of a premium on an insurance policy which qualifies under tax legislation for a deduction;
- an expense of an export business or capital or other expenditure where Parliament grants specific relief for these expenses.

In a recent paper entitled 'Consolidation and Part IVA' by Peter Walmsley[57] of the ATO, he says:

'... it is to be observed that at the very end of the jurisprudence of s260, in the last cases decided upon it, the courts finally gave satisfactory expression to the doctrine of "choice". It was said that:[58]

'Resort to the "choice principle" is denied by s260 where a situation is devised to gain the advantage of a particular section of the Act which has no sensible or practical basis or justification in a business or family sense, and where resort to the section is for the purpose or purposes which include the purpose of conferring a tax benefit upon the taxpayer such that it is a misuse of the section or of the benefits which it is designed to confer on those who legitimately resort to it. If in all the circumstances the use of the specific or particular provision of the Act warrants the description of an "abuse" of it ... s260 will apply.

'It may be fairly said that, in this expression of it, the choice principle has a place in Part IV A, not as a doctrine qualifying its operation, but as a description of what it is intended to do.'

Walmsely's suggested approach[59] is a welcome attempt at suggesting an answer to the question of where the line is drawn with Part IVA and appears to mirror the principle of 'tax mitigation' accepted[60] in the UK and New Zealand, but without resort to those words.

The outcome of the High Court appeal in Hart's case is likely to be relevant to some of these unresolved issues.

* Robert Gordon BA LLB LLM is a Barrister at St

James Hall Chambers.

1 This is a revised version of a paper delivered to the Commercial Law Association on June 6, 2003, entitled 'Commissioner of Taxation v Year End 'Tax Effective' Investors'.

2 $1,000 or more: definition 'excluded expenditure' in s82KZL(1)

3 I understand that RPC has discontinued those proceedings.

4 Now see *Petrolious v Wills [2003] NSWSC 106* (3 March, 2003); also see *Clements, Dunne & Bell Pty Ltd v Comm Aust Fed Police 2002 ATC 4072*

5 Senate Economics Reference Committee 'Inquiry into Mass Marketed Tax Effective Schemes and Investor Protection' Final Report, February 2002 at para 1.17

6 and managed investments pursuant to Product Rulings issued or applied for before November 11, 1999.

7 From July 1, 2001, rather than 13 months.

8 'Simplified Tax System' taxpayers are those carrying on a 'small' business (individuals, companies or trusts) who have elected to be treated as such under Div 328 of the 1997 Act.

9 s82KZMA

10 as s82KZME isn't excluded by the application of s82KZMA.

11 Indeed, I recall a listed company in the industry was placed into administration.

12 Howland-Rose & Ors v FCT ((2002) 49 ATR 206

13 Only final rulings are binding on the Commissioner. They bind him to the extent the ruling is more favourable to the taxpayer that the law. Unless a taxpayer's circumstances are 'on all fours' with the taxpayer described in a public ruling, the Commissioner will not be bound as against that taxpayer: *Bellinz case (1998) 84 FCR 154*.

14 Notwithstanding the lengthy lead time for agricultural projects to 'bear fruit', surely it is now time for Treasury to analyse the cost to the revenue of these Product Rulings compared to the economic benefit to Australia (other than the promotors), especially in the light of the fact that independent experts (eg, van Eyk) continually say that they will only recommend perhaps 10 per cent of these projects as worthy of consideration, often due to the high fee structures to promotors?

15 Also see *Barkworth Olives v FC of T [2003] FCA 443* (May 9, 2003)

16 See 'Statement of Principles' issued August, 2001.

17 Incidentally, one of the principals of the manager was sentenced to periodic detention for using moneys of the management company for his personal benefit, without the authority of the company: see *R v Towey (1996) 21 ACSR 46*.

18 Whilst argument was heard in *Cooke* before those cases were decided, *Cooke* was decided after those cases (nearly a year after the hearing), and Bar rule 27 that cases having a direct bearing on a case where the decision is reserved should be notified to the judge, should have had the effect of putting the judge on notice of these cases.

19 para 14

20 The issue of deductibility of capitalised interest in the subject of the High Court appeal in Hart's case.

21 The ATO had provided some funding for test cases concerning a schemes of this type for the film *Evita* (staring Madonna) and *Wing Commander*. Those movies were not made in Australia. The cases were set down for trial commencing June 11, 2002, but the trial date was vacated when the Commissioner extended his settlement offers, and ultimately all test case individuals did settle. *Evita* was a guaranteed return scheme in which it was alleged that the subscriptions were used to fund the guaranteed return. *Wing Commander* was a limited recourse loan scheme.

22 Lau's case on s82KL was not cited. In *Lau* the additional benefit of potentially not having to repay the borrowings was not taken into account, as it was too early to tell. Whilst the judgment doesn't say, perhaps the evidence was that at the time of the trial the $6m would never be paid. But does s82KL allow for hindsight?

23 But as *Krampel Newman* was not entitled to the deductions under Div 10B, on the authority of the Full Court in *Vincent*, the amended assessment for 1994 was out of time.

24 Some of the legal opinions in relation to the retirement village projects did not even explain how the promoted deduction was greater than investor' s cash outlaid. Of course, this was also the case with the *Budplan* prospectus

25 I am not aware of any cases on foot.

26 It was not decided whether this was a market salary.

27 The benefits to the employees were less than secure. This aspect drew no comment from Kiefel J, yet it would seem that such a feature must detract from the prospect that the Incentive Trust had any separate function from the super fund, other than the purported tax benefits.

28 As it was not necessary to decide the Part IVA point, Her Honour did not deal in detail with the eight issues to which s177D(b) requires attention. The observation that a like-sized superannuation contribution might have been made, does not necessarily conclude the issue of the reasonable hypothesis, as the fact that the contributions tax would have been payable by the super fund, but allegedly not by the Incentive Trust, as well as the inaccessibility of the super contributions until retirement, and whether the age based limits for superannuation were overcome for the sons by the use of the Incentive Trust, point to the dominant purpose of obtaining the tax benefit.

29 Submission under cover of letter to the Commissioner dated May 8, 2003.

30 eg, para 78

31 para 23
32 paras 23 & 29.
33 para 36
34 The High Court in *Gulland, Watson & Pincus 85 ATC 4765* certainly had the view that such contributions were outside s260 for similar reasons.
35 para 50
36 (1991) 173 CLR 1
37 para 130
38 para 107
39 paras 25 & 31
40 para 44
41 Indeed, Nicholson J in *Merchant* also seems to have relied on *Woolcombers*: 41 ATR at 126
42 para 7
43 para 58
44 (2001) 47 ATR 229
45 (1998) 88 FCR 21 at 42
46 para 105 in Puzey & para 124 in Vincent
47 para 100
48 (2001) 46 ATR 474 & 497 respectively; see particular Carr J at 491-2.
49 (2001) 48 ATR 317 at 340 para 59
50 see RF Edmonds 'Part IVA & Anti-avoidance — Where are we now?' delivered to a Law Council of Australia tax workshop in November, 2002 at p22
51 at the 17th National Convention of the Taxation Institute of Australia, Adelaide, March 27-29, 2003
52 noting the Full Court in Vincent, but not Hill J's paper specifically in this regard, although cross referencing it in other respects
53 at the TIA 37th WA State Convention, Perth, May 2, 2003
54 at page 3. At p4 he makes the point that 'drivers/features' of a transaction providing 'warning lights' about the possible application of Part IVA include 'arrangements heavily promoted on the basis of the tax benefits'. The irony is that the ATO assists in this by its issue of Product Rulings which confirm that Part IVA will not apply.
55 D'Ascenzo Op Cit p1; Cf Hill J Op Cit p13; and AH Slater QC 'Has Part IVA Reached Maturity?' also at the 17th National Convention of the TIA, p24
56 Beaumont J in the full court expressed refrained from so considering the distinction in *FCT v Ampol Exploration Ltd (1986) 18 ATR 102* at 134, whilst the full court in *Sonenco (No 87) Pty Ltd v FC of T 92 ATC 4704* at 4737 quoted part of the passage from *Ensign Tankers [1992] 1 AC 655* at 676, that referred to the distinction, but made no comment on it.
57 Law Council of Australia 'Consolidation/Part IVA Taxation Workshop' Werribee Park, Victoria, May 30-31, 2003
58 Lockhart J in *Pettigrew v FC of T 90 ATC 4124* at 4126
59 Dick Conti QC (as he then was), in a paper entitled 'Part IVA: Survival of the Choice Principle', delivered to the No 1 Tax Discussion Group in Sydney on September 25, 1996, before the decision of the High Court in Spotless, considered that the 'choice principle', beyond that expressly allowed by s177C must still exist, but through the language of the eight criteria in s177D(b), so as not to impede ordinary business decisions. He quoted from Beaumont J's comments in *Spotless (1995) 32 ATR 309* at 330, that the submission of the taxpayer was an echo of the choice principle, which Beaumont J rejected as having no application to Part IVA. The High Court went on to also reject 'muffled echos of old arguments' (ATR 186) without referring specifically to the 'choice principle' or what Beaumont J had said about it in particular.
60 But see Lord Hoffman in the House of Lords decision in *Macniven v Westmoreland Investments Limited [2001] 73 TC 1* at para 62 in relation to the utility of those words in defining the boundary of the 'fiscal nullity' principle. Also see 'Current Notes' in *No3 British Tax Review 2001* at 157. Although the Australian High Court rejected the 'fiscal nullity' principle in *John v FC of T 89 ATC 4101* at 4110 in relation to the Australian income tax law, as incompatible with a general anti-avoidance provision, Hill J has suggested that the issue might be reagitated: 'The Taxation Specialist' June, 2001 at 234.