(or its) employment." *Limpus* v. *London General Omnibus Co.*,[53] quoted above, is cited as the English authority. The effect of these *dicta*, if accepted, is to replace the proposition that all wilful acts of a servant are acts committed outside the scope of his employment, by the proposition that all wilful acts if committed within the scope of employment are the responsibility of the master as well as of the servant. However, we are nowhere informed whether the appropriate form of action against the master is trespass or case.

If the High Court in *Williams* v. *Milotin*[54] had adopted a broader approach to these complications, it might have done something to remove the doubts surrounding this question. As it was, it confined itself to looking at the rules relating to the direct-damage-negligent-act situation, and consequently added little to the law. The decision tells plaintiffs that they are bound by the consequences of their choice of form of action but does not help them in those cases where they may be uncertain as to what form of action they should bring. This surely is the important question. Should there be further cases in the courts involving the period of limitation applicable to trespass or case, we might see a situation somewhat similar to the eighteenth and nineteenth-century state of affairs where plaintiffs could be non-suited for bringing the wrong form of action, and fail altogether. It is to be hoped that if the trespass-case distinction again comes directly before the courts, very close attention will be paid to its analysis. Such an analysis could perhaps not escape the further issue, uncanvassed here, how far the distinctions made by the courts in this context under the labels "direct" and "indirect" damage, or "wilful" and "negligent" acts, are analytically (as distinct from merely historically) meaningful.

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LEGAL AVOIDANCE OF TAXATION AND SECTION 260

NEWTON v. *FEDERAL COMMISSIONER OF TAXATION*

Arrangements under which a man seeks so to order his affairs that the tax attaching under the appropriate Acts is less than it otherwise would be are common enough modern phenomena. An arrangement of this nature was the subject of litigation in *Newton's Case*.[1]

It is submitted that the correct judicial approach to such arrangements is that the courts should not concern themselves with the desirability or morality of the course taken but only with its legal operation and legal consequences.[2] It is to the end of nullifying the tax-avoiding effects of such schemes in their application to income taxation liability that s. 260 of the Income Tax and Social Services Contribution Assessment Act 1936-1948 (Cwlth.)[3] is principally directed. But notwithstanding both the legal difficulties attaching to its interpretation and the obviously far-reaching practical consequences embraced by its application, it was not until the recent decision in *Newton's Case* that s. 260 or its predecessors[4] had ever been brought before the Privy Council for judicial consideration. Section 260 is in the following terms:

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[53] (1862) 1 H. & C. 526. [54] (1957) A.L.R. 1145.

[1] *Lauri Joseph Newton and Others* v. *Commissioner of Taxation of the Commonwealth of Australia* (1958) 2 All E.R. 759 (P.C.).

[2] This was the contention of Jordan, C.J. in *In the Estate of William Vicars (Dec'd.)* (1944) 45 S.R. (N.S.W.) 85, 93. This view was expressly endorsed by Taylor, J. in *Newton's Case* (1956) 96 C.L.R. 577, 679. However, there is a certain amount of conflict of high judicial authority on this question. See the various cases referred to by G. Nettheim, "Legal Avoidance of Taxation" (1954) 1 *Sydney L.R.* 236.

[3] No. 27, 1936—No. 44, 1948.

[4] The best known are s. 53 of the Income Tax Assessment Act 1915 (No. 34 of 1915); s. 93 in the Act of 1922 (No. 37 of 1922).

> Every contract, agreement, or arrangement made or entered into, orally or in writing, whether before or after the commencement of this Act, shall so far as it has or purports to have the purpose or effect of in any way, directly or indirectly—(a) altering the incidence of any income tax; (b) relieving any person from liability to pay any income tax or make any return; (c) defeating, evading, or avoiding any duty or liability imposed on any person by this Act; or (d) preventing the operation of this Act in any respect, be absolutely void, as against the Commissioner, or in regard to any proceeding under this Act, but without prejudice to such validity as it may have in any other respect or for any other purposes.

The facts in *Newton's Case*, although complicated, were not in dispute. At the beginning of December 1949 the appellant taxpayers were the holders of 237,321 ordinary shares of £1 each which had been issued by a company L.[5]. At that time the company had available for distribution profits in excess of £400,000 mainly consisting as to part of profits derived during the year ended 30th June, 1949, and as to part of profits made during the then current income year. Early in December the existing 237,321 shares were converted into two classes. One-third of each shareholder's holdings, 79,107 shares, became A ordinary shares and two-thirds became B ordinary shares. The 445,000 unissued shares became B preference shares. Thereafter, special dividend rights, *viz.* the entitlement to receive the whole of the dividends declared by the company after that date not being less than £5/15/10 per share, and to a fixed preferential dividend of 5% per annum as from 1st January, 1950, were attached to the A ordinary shares. On 19th December the appellants sold to Pactolus Pty. Ltd., a company controlled by their taxation consultant, the A ordinary shares at £5/16/0 per share; share transfers and cheques were exchanged. Meanwhile, on 16th December, 1949, L resolved to make available for issue at par 402,679 B preference shares of £1 each, and specified that such shares should be offered to the persons entitled to the dividend upon the A ordinary shares on or after 19th December, 1949. On this date, Pactolus Pty. Ltd. applied to L for the issue to it of the 402,679 B preference shares and lodged with L its cheque for £402,679. On 20th December, 1949, L resolved to pay dividends of £5/12/10 per share on the A ordinary shares, amounting to £446,295, and thereafter to issue to Pactolus Pty. Ltd. the 402,679 B preference shares. On the same day L's cheque for £446,295 was handed to Pactolus Pty. Ltd. and the B preference shares were issued to it. On the same day Pactolus Pty. Ltd. sold the B preference shares to the appellants for £1 per share and received their cheques for a total sum of £402,679. All of the cheques which had passed between the parties were deposited on 21st December, 1949, in the same branch of the same bank where each of the parties concerned had a current account. Subsequently, the further dividends necessary to satisfy the special dividend rights attached to the A ordinary shares were declared.[6]

These transactions were part of a scheme designed to deal with a situation common enough under Australian taxation law, *viz.* the fiscal dilemma posed by Part III, Division 7 of the Assessment Act[7] whereunder a "private company"

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[5] This is an abbreviation, for the sake of clarity, of Lane's Motors Proprietary Ltd. In actual fact, there were five transactions under review, known as Lane's Transaction, First Neal's Transaction, First Melford Transaction, Second Melford Transaction, and Second Neal's Transaction. But as the material facts in each were substantially identical, it is not proposed to deal with each one separately.

[6] The Commissioner conceded that all the transactions were genuine and not shams, and that they had full force and effect according to their tenor.

[7] The Assessment Act draws an important distinction, for taxation purposes, between companies which are "private" companies and those which are not. The definition of the former is set out in s. 105(1) of the Act. After satisfaction of the two negative conditions that the company must not be "a company in which the public are substantially interested" or "a subsidiary of a public company", the most important class of "private" company is "a company which is capable of being controlled by any means whatever by

within the meaning of the Act must either make a "sufficient distribution" of its profits (thus usually burdening its shareholders with a high individual taxation liability) or alternatively pay additional tax on its undistributed profits. The purpose and practical effect of the transactions was clear: it was to enable the company (a) while parting with comparatively little cash, to replace the greater part of its 1949 and 1950 profits by paid-up share capital;[8] (b) to make the distribution required in order to exonerate itself from Division 7 tax; and (c) at the same time to avoid involving the original shareholders, though they became the holders of the new share capital, in an income tax liability on the footing that they had participated in a distribution of profits.[9]

The question for decision was the determination of the assessable income of the appellant taxpayers with respect to these transactions. Both the High Court and the Privy Council held that s. 260 applied so as to leave the appellants taxable in respect of the distributions made by L including the cash and shares which, when all the transactions were completed, were left in the hands of Pactolus Pty. Ltd.

The Privy Council judgment is stated in bold terms. Although in parts their Lordships' reasoning, resorted to a pragmatic approach to the legal difficulties involved, thus departing from a strictly literal and logical construction of the relevant statutory provision, the judgment on the whole represents an essentially satisfactory solution of a legal problem difficult in nature not only because of the complex fact-situation involved, but also because of the obscure nature of the principles (if any) to be derived from the authorities together with the imprecise wording of the Section itself.[10] The judgment has at last clarified, to an extent sufficient to satisfy the needs of the business community,[11] the effect and meaning of this all-important but obscurely drafted section.

It is proposed to trace the legal development in the interpretation of s. 260 under the following headings: (1) The stage reached in the interpretation by the High Court before the Privy Council judgment in *Newton's Case;* (2) The Privy Council judgment in *Newton's Case*. It should be borne in mind that the interpretation of s. 260 raises two questions which should be kept distinct and dealt with in their logical order. First, what is the nature of the circumstances which will call the Section into operation? Second, what is the effect which its application will produce?[12]

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one person or by persons not more than seven in number." (Para. (f).)

A "private company" so defined, has to bear a higher incidence of taxation liability than a "non-private" company, being subject to a tax which will be referred to as Division 7 tax, being the tax provided for by Division 7 of Part III of the Assessment Act. Section 104 in this Division, as it applied to the three companies in *Newton's Case*, provides in effect that where a "private" company has not made a sufficient distribution of its income of the year of income by the ensuing 31st December, the Commissioner may assess the aggregate additional amount of tax which would have been payable by its shareholders if the company had, on the last day of the year of income paid the undistributed amount as a dividend to the shareholders who would have been entitled to receive it, and that the company shall be liable to pay the tax so assessed. A "sufficient distribution" is defined in s. 103 (2) (c) as a payment in dividends, out of the taxable income of that year, of an amount not less than the aggregate of certain stated percentages of defined portions of the distributable income.

[8] It must be remembered that the assessable income of a resident shareholder includes dividends paid to him by the company out of profits derived by it (s. 44) and that the expression "dividend" includes the paid-up value of shares distributed by a company or its shareholders to the extent to which the paid-up value represents a capitalisation of profits.

[9] *Per* Kitto, J., (1956) 96 C.L.R. 577, 604.

[10] *Id.* at 596.

[11] Although such considerations are beyond the scope of this Note, it is clear that the commercial world did not at all welcome the wide operation apparently given to the section. See articles in *The Daily Telegraph* (10 July, 1958) headed: "The Tax Man Gets an Open Slather from Privy Council", and in *The Sun-Herald* (13 July, 1958) headed: "The Bogy of Section 260". It is, of course, common knowledge that, in deciding upon the prudence or otherwise of embarking upon a particular commercial venture, the factor of potential taxation liability occupies in the minds of businessmen in modern times a position of great prominence.

[12] *Per* Fullagar, J., (1956) 96 C.L.R. 577, 654; *per* Taylor, J., id. at 662.

I. *The Stage Reached in the Interpretation of Section 260 by the High Court*

1. *Before Newton's Case.* The courts had never previously delimited the scope and meaning of s. 260 with any real degree of precision.[13] Various tests as to the "purpose or effect" criterion had been formulated in different fact-situations. In *Purcell's Case,*[14] s. 260 was held to extend to cover transactions whereby the taxpayer is enabled to avoid payment of income tax on what is really and in truth his *income.* In *Jaques' Case,*[15] the court emphasized the lack of business reality in the relevant dealings. In *Clarke's Case,*[16] the court adopted the "sole purpose" criterion. And in *Bell's Case,*[17] the court appears to have stated as prerequisites first, a complex transaction, and, second, a predominant purpose of avoiding tax. The question of the effect of the application of the Section had never been thoroughly canvassed at all. In *Purcell's Case* (as indeed in *Keighery's Case*)[18] the question never arose; in *Clarke's Case* and *Bell's Case* it was merely a question of the removal of a facade, which was clearly with the power of the Section.

2. *Newton's Case in the High Court.*[19] This decision was notable for a set of closely reasoned judgments supporting opposite views.

The taxpayers first appealed against amended assessments to Kitto, J. who, sitting as a single Justice, upheld the appeal. After an exhaustive examination of the facts, his Honour first ruled[20] that the Section is an annihilating provision only, thus availing the Commissioner only where its effect in avoiding an arrangement to the extent mentioned is to leave standing a state of affairs in which a challenged assessment is justified. This does not mean that the operation of the Section upon an arrangement is to eliminate from consideration, as if it never occurred, either anything that was done or some severable part of the things that were done in the course of the arrangement. The Section leaves all the facts of the case exactly as it finds them, requiring neither that anything which was not done shall be deemed to have been done, nor that anything which was done shall be deemed not to have been done.

His Honour then stated[21] that two views favouring the Commissioner were possible. One was that the payment of the dividend to Pactolus Pty. Ltd. was made with the appellants' consent and notwithstanding that they, after the avoidance of the transfer, were entitled to it. But Kitto, J. ruled that the taxpayers never contemplated that the dividend should be regarded as payable to them notwithstanding their alienation of the shares. In this event s. 260 would not only have to annihilate the legal effect of a transfer of shares, but would have to add to the facts of the case a fictional agreement of this nature by the taxpayers. Yet the office of s. 260 is never to create notional acts or events, but to leave the facts of every case exactly as it finds them. The other possible view was that the money paid by Pactolus Pty. Ltd. to the original shareholders must be considered not to have been a price paid for the shares, and therefore not to have been capital, and that the receipt of it should accordingly be held a receipt of income. But his Honour held that it does not necessarily follow from the fact that the amount referred to is not to be considered as the price received on the sale of a capital asset, that it therefore is to be considered as income. A receipt cannot be held either capital or income unless circumstances are

[13] For a more thorough analysis of the relevant decisions, the reader is referred to G. Nettheim, *op. cit. supra* n. 2.
[14] *The Deputy Federal Commissioner of Taxation* v. *Purcell* (1921) 29 C.L.R. 464.
[15] *Jaques* v. *Federal Commissioner of Taxation* (1924) 34 C.L.R. 328.
[16] *Clarke* v. *Federal Commissioner of Taxation* (1932) 48 C.L.R. 56.
[17] *Bell* v. *Federal Commissioner of Taxation* (1955) 87 C.L.R. 548.
[18] *W. P. Keighery Pty. Ltd.* v. *Commissioner of Taxation* (1958) 32 A.L.J.R. 118.
[19] *Federal Commissioner of Taxation* v. *Newton* (1956) 96 C.L.R. 577.
[20] *Id.* at 597.
[21] *Id.* at 609.

found to exist which justify its being described as the one or the other. To remove from the case an existing reason for holding a receipt to be of a capital nature is one thing; to find in what is left of the circumstances a sufficient reason for holding the receipt to be of an income nature is quite another. The first is within the competence of a statutory provision having a voiding operation only, but the second is not. His Honour thus concluded that s. 260 could not operate so as to justify the assessment of the special dividends as income of the taxpayers.

The question of whether the transactions were in the nature of an arrangement struck at by the Section was hence immaterial, and his Honour accordingly held that s. 260 could not assist the Commissioner.

The Commissioner thereupon appealed to the Full High Court, the majority of whom (Dixon, C.J., McTiernan, J., Williams, J., Fullagar, J., with Taylor, J. dissenting) upheld the appeal. McTiernan, J. was of the opinion that the artificial routine used carried its tax-avoiding purposes and effects on its face, further holding that the series of steps constituted an "arrangement" within the Section. His Honour then concluded that if the transfers are absolutely void for the purposes of taxation, the result is that, in the contemplation of the Act, the taxpayers were always *sub modo* the shareholders and as such derived the whole of the dividends as income. Williams, J. also upheld the appeal. He was of opinion that "the purpose of a contract, agreement or arrangement must be what it is intended to effect and that intention must be ascertained from its terms."[22] His Honour was prepared to find an "arrangement" within the meaning of the Act and that such arrangement had the purpose of avoiding a liability imposed on the shareholders by the Act. The learned Judge then ruled that after s. 260 had done its work, the whole of the special dividends must be considered for the purposes of income tax to be the property of the original shareholders.

Fullagar, J. also decided in favour of the Commissioner. His Honour held that one of the proscribed purposes or effects was the only possible inference from the circumstances; that the present case was indistinguishable from *Bell's Case;* that the operation of s. 260 was to entitle the Commissioner to look at the end-result and to ignore all the steps which were taken in pursuance of the avoided arrangement. When he does that, what he finds is simply that profits of the company have come, in the shape of cash and new fully paid shares, into the hands of the shareholders in the company. And, when that is all that is looked at, it means that those shareholders have received income—dividends within the meaning of s. 6 of the Assessment Act.

On the other hand, Taylor, J. dissented from the majority view. His Honour was of the opinion that the cases showed that the Section only applied where the various dealings had no practical economical or commercial significance beyond the avoidance of a liability to pay income tax. His Honour then went on to hold that in the instant case there was no such artificiality in the transactions. His Honour next considered the effect of the application of s. 260 and his remarks hereon are dealt with at a later stage in this Note. His Honour concluded that the characterisation as income of the receipt by the appellants was *ultra vires* the Section.

3. *The High Court Decision in Keighery's Case.*[23] This decision represented a "retreat" in the local judicial approach to s. 260 in that, although the facts of the case disclosed an arrangement the avowed and ostensible purpose of which was the avoidance of tax, yet the Full High Court ruled that s. 260 had no application to it. This decision, which has received the express approval of the Privy Council, is of the utmost practical importance insofar as it reveals a simple method of reducing company taxation liability whilst circumventing the applicability of s. 260 to such a scheme.

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[22] *Id.* at 630.
[23] (1958) 32 A.L.J.R. 118.

The relevant facts were these: Mr. and Mrs. Keighery and their son between them held a controlling shareholders' interest in Aquila Steel Pty. Ltd., a private company within s. 105(1)(a) of the Assessment Act and which had a considerable amount of profits available for distribution. Subsequently W. P. Keighery Pty. Ltd. was formed to purchase from the Keigherys their shareholdings in Aquila Steel Pty. Ltd. The shareholders in the holding company as at 27th June, 1952, were Mr. and Mrs. Keighery as to three and one ordinary shares of £1 each respectively together with twenty other persons who each held one redeemable preference share which had been allotted to them by Mr. and Mrs. Keighery as the only Directors of the company. Under the articles of association each of the twenty-two shareholders was entitled as on a show of hands to one vote, and as on a poll to one vote for each share held. By the terms of issue of the redeemable preference shares, the company had reserved the power in the Directors (that is the Keigherys), subject to s. 149 of the Companies Act, 1936 (N.S.W.), at any time on or before 31st December, 1977, to redeem any of the redeemable preference shares, provided that not less than seven days' notice of redemption should be given and that *no such redemption should be made between 24th June and 7th July in any year.* It was clear, therefore, that if there had been a general meeting of the company on 30th June, 1952, no one shareholder, and no group of not more than seven shareholders, could have outvoted all other shareholders. There was nothing to suggest that any shareholder had the power by any means to govern the voting of another.

The question for consideration was whether W. P. Keighery Pty. Ltd. was a "private company" within s. 105(1) so as to be assessable for additional tax under Division 7.[24] The Commissioner relied on s. 260. He argued that its effect here was that the allotment of the redeemable preference shares formed part of an arrangement having the purpose of avoiding the liability to Division 7 tax under which the appellant company would otherwise have been; that the allotment was therefore to be disregarded as against the Commissioner; and that as a consequence the appellant company was to be treated as a "private company".

The majority in the High Court, consisting of Dixon, C.J., Kitto, J., and Taylor, J. considered that it was a fair inference from the evidence that all the applicants for the redeemable preference shares, who included acquaintances of the Keigherys, did so by way of obliging the Keigherys by assisting them to bring about a tax result that they desired; that the course adopted was planned mainly, though not exclusively, with the object of enabling Aquila Steel to distribute its profits so as not to incur Division 7 tax without causing any consequential increase in the assessable incomes of Mr. and Mrs. Keighery and their son; that the appellant company was brought into being so that it might be interposed between Aquila Steel and the Keigherys, and its affairs were so regulated that the dividend which it would receive from Aquila Steel might be retained by it and yet might be immune to Division 7 tax. But the majority held,[25] s. 260 is intended only to protect the general provisions of the Act from frustration, and not to deny to taxpayers any right of choice between alternatives which the Act itself lays open to them. It was therefore important to consider whether the result of treating the Section as applying in the present case would be to render ineffectual an attempt to defeat a liability imposed by the Act or to render ineffectual an attempt to give a company an advantage which the Act intended that it might be given. Their Honours said that if the persons interested in a company, which is a private company within s. 105(1), do not wish the company to be placed in the position of having either to make a sufficient distribution or to pay Division 7 tax, they may so act with respect to shares in the company that the public become substantially

[24] *Supra* n. 7.
[25] (1958) 32 A.L.J.R. 118, 122.

interested in it (within the definition in s. 105(2)) or they may turn it into a subsidiary of a public company (within the definition in s. 105(4)(b)) or they may bring about a sufficiently less concentrated holding of the shares or the beneficial interests therein, or of the voting power, or of rights by reason of which the company is capable of being controlled. It is only if they do not take any of the courses thus thrown open to them that Division 7 creates a liability. Their Honours therefore ruled that the very purpose or policy of Division 7 is to present the choice to a company between incurring the liability for which the Division provides and taking measures to enlarge the number capable of controlling its affairs. To choose the latter course cannot be to defeat, evade or avoid a liability imposed on any person by the Act or to prevent the operation of the Act.[26]

II. *The Privy Council Judgment in Newton's Case*

The taxpayers in *Newton's Case* had now appealed to Her Majesty in Council.[27] The judgment delivered by their Lordships on the whole adopted the views advanced by the majority in the High Court.

After consideration of the Section, their Lordships held that the word "arrangement" describes something less than a binding contract. It describes a plan arranged between two or more persons which may not be enforceable at law, and comprehends not only the initial plan but also the subsidiary transactions by with such plan is carried into effect.[28] Their Lordships then went on to consider[29] the nature of the arrangements avoided by s. 260. The Section, they held, is not concerned with the desire to avoid tax (that is, with motives) but with the means employed to do it. The court must see whether the arrangement *itself* discloses the purpose or effect of avoiding tax irrespective of the motives of the persons behind the plan. The court must be able to predicate—by looking at the overt acts by which the arrangement is implemented —that it was implemented in that particular way so as to avoid tax. If the court cannot so predicate but has to acknowledge that the transactions are capable of explanation by reference to ordinary business or family dealing without necessarily being labelled as a means to avoid tax, then they are not within the Section.

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[26] Webb, J., in an interesting dissent, was of the opinion that the transactions were struck at by s. 260. He held that on the face of it the arrangement was calculated to terminate the operation of the Act, in the sense that, apart from the arrangement in the normal course of events, either Division 7 tax would have become payable or a "sufficient distribution" would have had to have been made. It was therefore *prima facie* within the section. As s. 260 was not expressed to be subject to any other provisions of the Act, including provisions which vary the incidence of income tax for different categories of taxpayers; and as the Act is just as explicit that capital receipts are not liable to income tax as it is that the incidence of tax varies for different categories of taxpayers; and as in *Bell's Case* it was held that because of s. 260 capital receipts remained taxable as income in the particular year in which the arrangement was made that legally and effectively converted them into capital receipts; and as *Bell's Case* was indistinguishable from the present case, therefore s. 260 was applicable to the arrangement. It is difficult to find any strictly logical flaw in this argument. However, it is submitted, with respect, that the majority view is more acceptable if only on the broad ground that it is more in accord with the general policy of the Assessment Act in this context.

In actual fact, Webb, J.'s reasoning was set out in the decision in *The Commissioner of Taxation* v. *Sidney Williams (Holdings) Ltd.* (1958) 32 A.L.J.R. 123, judgment in which was delivered simultaneously with judgment in *Keighery's Case*. His Honour simply stated that his reasoning in both cases was the same.

As the facts in the *Sidney Williams Case* were on all fours with *Keighery's Case* and as the court carried the reasoning no further, it is proposed not to deal with the decision separately but simply to mention it *en passant*.

[27] *Lauri Joseph Newton and Others* v. *Commissioner of Taxation of the Commonwealth of Australia* (1958) 2 All E.R. 759.

[28] *Id.* at 763.

[29] *Id.* at 764.

Their Lordships agreed that the avoidance of tax was not the sole purpose disclosed by the overt acts involved in the transaction adopted by the appellant taxpayers. The raising of new capital was an associated purpose. But their Lordships held that the Section will still apply if *one* of the purposes is to avoid tax. The Section stipulates: "so far as it has . . . the purpose . . . ." Therefore it need not be the sole purpose. Their Lordships concluded that here the transactions showed concerted action to an end and that one of the ends was the avoidance of tax. This therefore was an "arrangement" struck at by the Section.

Their Lordships then addressed themselves to the question of the effect of s. 260 on the arrangement.[30] They were of the opinion that the Commissioner was entitled completely to disregard the arrangement and the ensuing transactions so far as they had the proscribed purpose. Their Lordships held that the Commissioner could avoid the transactions in so far as the original shareholders transferred the dividend rights (with the shares) to Pactolus for money, for it was that transaction which gave the character of capital to the money received by the appellants; that the court was thereby entitled to treat the special dividends as income of the taxpayers; and that the appeal should accordingly be dismissed.

III. *Conclusions*

1. *As to the Meaning of "Arrangement".* It is submitted that the Privy Council's interpretation of the word "arrangement" is far more satisfactory than any previously suggested by the courts. Their Lordships ruled that the word comprehended both (1) a broad plan of action merely in the nature of an understanding and lacking in legally operative effect; and (2) all the subsidiary transactions effectuating such plan. Isaacs, J. in *Jaques' Case*[30a] had ruled that the Section does not include a conveyance or transfer as such. In *Bell's Case*[30b] the Full High Court had held that the Section is concerned only with arrangements which have an effect in law and accordingly are capable of statutory avoidance. The writer, with respect, submits that the Privy Council opinion expresses the correct connotation of the word, for two reasons. First, by virtue of its physical position in the Section the word "arrangement" is by clear implication intended to be antithetic to "contract" and "agreement"; second, it would be purposeless to avoid the plan itself and yet leave standing the instruments carrying the plan into operation.

2. *As to the Nature of the Arrangement struck at.* It is submitted that the Privy Council has now evolved the following formula in this context. Section 260 will operate so as to avoid *pro tanto* and against the Commissioner any transaction explicable on the face of it by reference to its having as a purpose or effect one of the proscribed purposes or effects categorised in the Section. The motive of the individuals behind the plan is immaterial.

In this context the problem posed by the facts in *Newton's Case* was a difficult one: the avoidance of tax was not the sole or predominant purpose[31] nor did the dealings between the parties lack commercial reality.[32] It is submitted with respect that their Lordships' construction of the Section is not only eminently lucid but is valid by the test of literal interpretation.

It might appear that the formula propounded by the Privy Council could give rise to certain practical difficulties in its application. It is, however, submitted that the Section should be applied thus: (1) It must first be determined

[30] *Id.* at 765.
[30a] (1924) 34 C.L.R. 328, *supra.*
[30b] (1955) 87 C.L.R. 548, *supra.*
[31] As in *Clarke's Case* or *Bell's Case.*
[32] As in *Jaques' Case.*

whether, by looking at the transaction itself, it is possible to make the appropriate predication. (2) (And this is a negative stipulation.) It is no bar to the applicability of the Section that the proscribed purpose or effect is not the sole purpose or effect of the relevant arrangement.

The following are illustrations of the practical application of the Privy Council's interpretation of s. 260:

(a) A sale of shares *cum* dividend is not within the Section, since it is not possible to make the initial predication. Such a transaction is capable of explanation by reference to ordinary business dealing, without necessarily being labelled as a means to avoid tax.[33]

(b) Where an owner declares himself a trustee of certain land and stock for himself and his wife and his daughter in equal shares, reserving to himself wide powers of management, control and investment, his declaration is not within the Section. Here, also, one cannot make the initial predication. The transaction is capable of explanation by reference to ordinary family dealing. This was *Purcell's Case*.[33a] It is submitted that the well-known and widely-applied "family company" scheme may be upheld as not within the annihilating purview of s. 260. Basically such a scheme involves the transfer by their owner (the father) of the family's income-producing assets (generally, of course, the father's business) to a private company, the shareholders in which are all the members of the family, and under the articles of association of which wide powers of control are vested in the father, who is usually constituted a "Governing Director". Such an arrangement has the positive and intended effect of reducing the taxation liability on the overall income accruing to the family.[34] But it is not possible to make the initial predication, the condition precedent to the operation of s. 260, for such a transaction is fully capable of explanation by reference to its being an ordinary family dealing, *viz.* the granting by a father to his family of an interest in his income-producing assets. The scheme cannot be classified as necessarily having the purpose or effect of avoiding tax.

(c) A transaction of the nature of that in *Jaques' Case*, *Clarke's Case* or *Bell's* Case, possessing such features as the existence of an obvious alternative procedure for effecting the same end-result, cheques being exchanged for like amounts and so forth, is clearly within the Section. It is to avoid tax and accordingly such a transaction is struck at by the Section.[35]

(d) A transaction embodying all the elements of that in (c) above, together with a superadded element, namely, the existence of an additional purpose or effect, for example, the increasing of the share capital of a company. Such a transaction, of course, was in question in *Newton's Case* itself. The Privy Council, being able to make the initial predication, ruled that the existence of an additional purpose was immaterial and went on to hold that the transaction was struck at by s. 260. At the same time their Lordships offered an interpretation of *Keighery's Case* which requires some comment. The relevant *dictum* of their Lordships is as follows:[36] "Nor can anyone, by seeing a private company turn into a non-private company, predicate that it was done to avoid Division 7 tax." It is submitted with respect that this *dictum* is incorrect for the following reasons:

(1) It was clear on the face of the transactions that the basic purpose of the scheme was to reduce taxation. (2) It is incorrect in this context to speak of avoiding *tax*. The appropriate nouns used in the section are "duty" and

[33] (1958) 2 All E.R. 759, 764.

[33a] (1921) 29 C.L.R. 464, *supra*.

[34] It also, of course, has the well-known associated effect of avoiding certain death and succession duties.

[35] (1958) 2 All E.R. 759, 764.

[36] *Ibid.*

"liability". In *Keighery's Case*, considered in arithmetical terms, the relevant taxation payable was reduced by the arrangement (that is, *tax* was thereby *avoided*). Nevertheless the whole basis of the decision was that the company was merely taking advantage of a benefit which the Act itself intended that it might have; and that, to this extent, the company could not be said to be defeating or avoiding a duty or liability within the meaning of the Act. For these reasons s. 260 clearly could not apply.

3. *As to Operation of the Section.*

This aspect of the decision turns on the legal connotation of the term "void". It is clear that the expression means that the Section has an "annihilating" effect only;[37] that is, it may render an arrangement void to the stated extent but never provides any element that is absent and necessary for a valid assessment.[38] And as the Privy Council itself declared:[39] "The annihilation (of the transaction) does not in itself create a liability to tax. In order to make the taxpayers liable, the Commissioner must show that moneys have come into the hands of the taxpayers which the Commissioner is entitled to treat as income derived by them." But their Lordships went on to conclude:[40]

> When that transaction (that is, that of transferring the dividend rights with the shares to Pactolus for money) is ignored, it becomes apparent that special dividends were declared on shares which are to be deemed, for this purpose, to be still held by the original shareholders. . . . If and so far as the Commissioner can show that these special dividends reached the hands of the original shareholders, he is entitled to treat it as income derived by them from the shares.

It is submitted, with respect, that there is a *non sequitur* in the logical development of their Lordships' reasoning in the last sentence. It is submitted that, on the literal construction of the Section, the dividends are assessable only if the Commissioner can show that they reached the hands of the shareholders *as income*. It is axiomatic that the nature of a receipt is not determined by the nature of the fund out of which the money received is taken, and also that the power to characterize the receipt as income does not spring from the Section on its literal construction. On this latter point the writer would respectfully adopt the view advanced by Taylor, J. in *Newton's Case* in the High Court:[41]

> This final conclusion . . . does not depend merely upon the notional avoidance, as against the Commissioner, of the several transfers; it can be reached only by taking a further notional step for the purpose of giving a new colour or character to the payments, that is, by attributing to Pactolus Pty. Ltd. an intention to account to the respondents for the dividends received by it. But it is abundantly clear that nothing was further from the minds of the parties. The amounts paid by Pactolus Pty. Ltd. were paid in respect of a price legally payable, and, although the notional annihilation of the transfers may, again, notionally, leave those amounts without a character it cannot operate to invest them with a new character.

It is apparent that the Section, on its literal and logical construction, would be ineffectual to deal properly with a factual situation of any degree of complexity at all. It is true that in *Bell's Case* and in *Clarke's Case*, the Section had a successful operation. But in both these cases the dealings between the parties were merely set up as a façade, upon the removal of which a state of affairs which involved a taxpayer in a tax liability was simply left exposed.

To make the Section workable, their Lordships saw fit, illogically, it is submitted, to attribute to the Section an operation of sufficient efficacy to attach

[37] See *Newton's Case* in the High Court, *passim*.
[38] *Per* Kitto, J., (1956) 96 C.L.R. 577, 597.
[39] (1958) 2 All E.R. 759, 765.
[40] *Ibid.*
[41] (1956) 96 C.L.R. 577, 677.

to the amounts received by the taxpayers the character of income. To this extent the judgment must be regarded as going beyond literal and logical construction into the ground of judicial pragmatism.

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LIABILITY OF THE POST OFFICE IN CONTRACT

TRIEFUS & CO. LTD. v. *POST OFFICE*

What has been described as a "courageous endeavour"[1] to make the Post Office liable for loss of postal matter ended in failure with the decision of the Court of Appeal in the *Triefus Case*.[2] Both English and Australian case law is, in view of the volume of business handled by the post offices of both countries at the present day, surprisingly barren. In England there have been only two decisions, one of 1701 *(Lane* v. *Cotton*[3]*)* and the other of 1778 *(Whitfield* v. *Lord Le Despencer*[4]*)*, while in Australia there have been no reported cases at all. This dearth of cases seems to be not so much a result of the efficiency of the Post Office system in ensuring safe arrival of all matter despatched, as of practice and silence combining, apart from statute, to put the Post Office in a privileged position in the eyes of the public. This is strikingly illustrated in the judgment of Lord Mansfield in *Whitfield* v. *Lord Le Despencer* when he said,[5] (with reference to the earlier decision in *Lane* v. *Cotton*[6]):

> In that year (1701) a solemn judgment was given, that an action on the case would not lie against the Postmaster-General, for a loss in the office by the negligence or fault of his servant. The nation understood it to be a judgment; and therefore it makes no difference, if what has been thrown out were true, and the writ of error was stopped in the way that has been mentioned, for the bar have taken notice of it as a judgment; the Parliament and the people have taken notice of it, every man who has sent a letter since has taken notice of it; many Acts of Parliament for the regulation and improvement of the Post-office, and other purposes relative to it, have passed since, which by their silence have recognised it. The mail has been robbed a hundred times since, and no action whatever has been brought. What have merchants done since and continue to do at this day, as a caution and security against a loss? They cut their bills and notes into two or three parts, and send them at different times; one by this day's post, the other, by the next. This shews the sense of mankind as to their remedy. If there could have been any doubt therefore before the determination of *Lane* v. *Cotton*, the solemn judgment in that case having stood uncontroverted ever since, puts the matter beyond dispute. Therefore we are all clearly of the opinion that the action will not lie.

In order that the position of the Post Office in both countries may be better understood, it is proposed to give a short resumé of the earlier decisions, the *Triefus Case*,[8] and relevant statute law. The first case, *Lane* v. *Cotton*[9] followed the first Post Office Act[10] of 1660 which recited the existence of

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[1] (1957) 31 *A.L.J.* 367.
[2] *Triefus & Co. Ltd.* v. *Post Office* (1957) 2 Q.B. 352.
[3] (1701) 1 Ld. Raym. 646.
[4] (1778) 2 Cowp. 754.
[5] *Id.* at 766.
[6] (1701) 1 Ld. Raym. 646.
[7] This refers to the settlement of the action. The Court of King's Bench gave judgment for the defendants, who, apparently thinking that the plaintiff intended to bring a writ of error on the judgment, paid the money to the plaintiff. There are no traces in the Exchequer Chamber of any writ of error having been brought, nor in the Post Office of the money having been paid.
[8] (1957) 2 Q.B. 352.
[9] (1701) 1 Ld. Raym. 646.
[10] 12 Car. 2, c.35.