~~P C~~
~~G D + G C~~

8, 1966

No. 29 of 1965.

IN THE PRIVY COUNCIL

ON APPEAL
FROM THE HIGH COURT OF AUSTRALIA

BETWEEN:

DESMOND LEES PEATE — Appellant

AND

THE COMMISSIONER OF TAXATION OF THE COMMONWEALTH OF AUSTRALIA — Respondent

CASE FOR THE RESPONDENT

RECORD

INTRODUCTION.

1. The question in this Appeal is whether Menzies, J. exercising the original jurisdiction of the High Court of Australia and the Full Court of the High Court rightly decided that the Appellant had been correctly assessed to income tax under the Income Tax and Social Services Contribution Assessment Acts 1936-1958, 1936-1959 and 1936-1960, in respect of the years of income ended 30th June, 1958, 30th June, 1959, and 30th June, 1960 respectively, on the basis that his income for those years included amounts of £6,690, £6,091 and £6,097 respectively derived by him as a medical practitioner carrying on practice in association with a number of other medical practitioners. In his returns of income for the years in question the Appellant had claimed that substantially the whole of his income from the practice of medicine had been derived as a salaried employee and not otherwise of a company carrying on the industry of medical services. His returns disclosed that the Appellant's salary as such an employee was £1,560 in the year ended 30th June, 1958 and £2,080 in each of the years ended 30th June, 1959 and 30th June, 1960.

2. The circumstances giving rise to this question may be broadly outlined as follows. For some years prior to the years of income in question the Appellant, a legally qualified medical practitioner, had carried on a medical practice in and around the town of Cessnock in New South Wales in partnership with a number of other medical practitioners. Following upon discussions between themselves and their accountants and legal advisers the partners, for reasons including the intention of avoiding income tax, decided to put into operation a plan which, broadly speaking, would result in the fees

Vol.1. p.72, ll.30-36.

Vol.1. p.73, l.27- p.76, l.49.

attributable to their services being received by a company, and in the former partners becoming salaried employees of associated companies. In accordance with the Plan A.E. Westbank Pty. Limited (hereinafter called Westbank) was incorporated on 29th June, 1956 and shortly thereafter the partners were appointed as its directors. There was then incorporated in respect of each partner a company (hereinafter called a family company) of which the partner soon after became Governing Director and the shares in which, apart from signatory shares, were subsequently allotted to trustees for his infant children. The family companies then acquired the issued shares in Westbank in the same proportions as the partners had been entitled to share in the assets, profits and losses of the partnership. The partnership was dissolved on 31st August, 1956 and each partner sold the assets and goodwill of his practice to his family company. On 1st September, 1956 each former partner entered into an agreement with his family company whereby he agreed to serve it (or such company or firm as it might direct) as a medical practitioner at a salary. On the same day it was agreed between Westbank, each family company and each practitioner that each practitioner for an annual salary should serve Westbank and that Westbank would remunerate his family company for those services by a fee which should be a percentage of Westbank's gross income less certain expenses. Each practitioner agreed that he would ensure that every patient treated by him would contract with Westbank that payment for medical services rendered by the practitioner should be due to Westbank and not to the practitioner.

Vol.2. p.470 p.488
Vol.1. p.94, ll.18-21.
Vol.1. p.94, ll.38-40.
Vol.1. p.81, l.47- p.82, l. 7.
Vol.1. p.77, ll.5-13. p.94, ll.22-31.

3. At all material times after 1st September, 1956 the receipts arising from the professional activities of the former partners were paid into the bank accounts of Westbank, which after paying expenses including staff salaries, and making contributions to a staff superannuation fund, paid service fees to the family companies in the proportions agreed upon from time to time by its directors. In the years of income ended 30th June, 1958, 30th June, 1959 and 30th June, 1960 the service fee paid to W. Raleigh Pty. Limited (the Appellant's family company, hereinafter referred to as Raleigh) were £5,820. 8. 8., £5,155.12. 3. and £5,271. 4. 4. respectively. From its share of service fees Raleigh paid certain expenses incurred in connection with the services rendered by the Appellant, paid director's fees and salaries to the Appellant and his wife, and paid dividends on the shares (other than signatory shares) held by trustees for the Appellant's infant children. In the years of income referred to above the Appellant received from Raleigh by way of salary amounts of £1,560, £2,080 and £2,080 respectively. He also received £200 director's fees in the year ended 30th June, 1960. The Respondent disregarded these amounts

and assessed the Appellant to tax on the basis that he had derived as income from the practice a share of the gross fees returned as income by Westbank less certain expenses incurred by Westbank. In the years of income referred to above the Appellant's share was calculated to be £6,690, £6,091 and £6,097 respectively.

4. In the High Court of Australia Menzies, J. held that, subject to certain adjustments, the basis of assessment adopted by the Respondent was correct, and appeals from the decisions of Menzies, J. were unanimously dismissed by the Full Court of the High Court. Both Menzies, J. and the Full Court of the High Court held that the basis of assessment adopted by the Respondent was justified by reason of the application of section 260 of the Income Tax and Social Services Contribution Assessment Act which provides:-

> "260. 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 purpose".

5. The Respondent submits that the facts of this case disclose an arrangement having the purpose or effect of avoiding the liability of the Appellant to tax on what, but for the arrangement, would have been income derived by him or having the purpose or effect of preventing the operation of the Act or having the purpose or effect of altering the incidence of tax. Section 260, in the Respondent's submission, applies to render void as against the Respondent the separate corporate existence of Westbank, the agreement between the Appellant and Raleigh, the agreement between Westbank, Raleigh and the Appellant, the agreements between Westbank, the other family companies and the other doctors and the agreements (if any) made between Westbank and the patients and the Appellant and the patients so far as they provided that fees should be the property of Westbank.

6. Alternatively, the Respondent submits that section 260 renders void as against the Respondent the agreement between the Appellant and Raleigh, the agreements between Westbank and the family companies and the doctors (including the Appellant) and the agreements (if any) made between Westbank and the patients and the Appellant and the patients, so far as they provided that fees should be the property of Westbank.

STATUTORY PROVISIONS.

7. In addition to section 260 the following provisions of the Income Tax and Social Services Contribution Assessment Act are material -

(a) the definition of 'assessable income' in section 6(1) which is as follows:-

"'assessable income' means all the amounts which under the provisions of this Act are included in the assessable income."

(b) the definition of 'partnership' in section 6(1) which is as follows:-

"'partnership' means an association of persons carrying on business as partners or in receipt of income jointly, but does not include a company."

(c) the definition of 'taxable income' in section 6(1) which is as follows:-

"'taxable income' means the amount remaining after deducting from the assessable income all allowable deductions."

(d) Section 17 which is as follows:-

"17. Subject to this Act, income tax and social services contribution at the rates declared by the Parliament shall be levied and paid for the financial year which commenced on the first day of July, One thousand nine hundred and fifty, and for each financial year thereafter, upon the taxable income derived during the year of income by any person, whether a resident or a non-resident."

(e) Section 19 which is as follows:-

"19. Income shall be deemed to have been derived by a person although it is not actually paid over to him but is reinvested, accumulated, capitalized, carried to any reserve, sinking fund or insurance fund however designated, or otherwise dealt with on his behalf or as he directs."

(f) Section 23(j) (i) which is as follows:-

"23. The following income shall be exempt from income tax:-

(j) The incomes of the following funds, provided that the particular fund is being applied for the purpose for which it was established -

(i) a provident, benefit or superannuation fund established for the benefit of employees."

(g) Section 46(1) which is as follows:-

"46.-(1) Subject to this section, a shareholder, being a company which is a resident, shall be entitled to a rebate in its assessment of the amount obtained by applying to that part of the dividends included in its taxable income the average rate of tax payable by the company."

(h) Section 66(1) which is as follows:-

"66.-(1) Where a taxpayer, for the purpose of making provision for individual personal benefits, pensions or retiring allowances for, or for dependants of, employees of the taxpayer, being or including employees engaged in producing his assessable income, sets apart or pays in the year of income a sum as or to a fund from which such benefits, pensions or allowances are to be provided, and the rights of the employees or dependants to receive the benefits, pensions or allowances are fully secured, an amount ascertained in accordance with the provisions of this section shall be an allowable deduction."

(i) Section 79(1) which is as follows:-

"79.-(1) Where a taxpayer, for the purpose of making provision for individual personal benefits, pensions or retiring allowance for, or for dependants of, employees of a person or persons other than the taxpayer, being or including employees who are residents and are engaged in the business of the employer or employers, sets apart or pays in the year of income a sum as or to a fund from which such benefits, pensions or allowances are to be provided, and the rights of the employees or dependants to receive the benefits, pensions or allowances are fully secured, an amount ascertained in accordance with the provisions of this section shall, subject to subsection (3) of the last preceding section, be an allowable deduction."

(j) Section 82F which, so far as is material, is as follows:-

"82F.-(1) Amounts paid by the taxpayer in the year of income as medical expenses in respect of himself, or in respect of a dependant who is a resident, shall, to the extent to which he has not been, and is not entitled to be, recouped those expenses by a government, public authority, society or association, be allowable deductions.

(2) The deductions allowable under this section shall not include, in respect of any one year of income, so much of the amount of medical expenses in respect of any one person as exceeds One hundred and fifty pounds.

(3) In this section -

"dependant" means -

(a) the spouse of the taxpayer;
(b) a child of the taxpayer less than twenty-one years of age; or
(c) a person in respect of whom the taxpayer is entitled to a deduction under section eighty-two B or eighty-two C of this Act;

"medical expenses" means payments -

(a) to a legally qualified medical practitioner, nurse or chemist, or a public or private hospital, in respect of an illness or operation".

8. The Income Tax and Social Services Contribution Acts of 1958, 1959 and 1960 imposed income tax and social services contribution at the rates declared therein on taxable income derived during the years ended 30th June, 1958, 30th June, 1959 and 30th June, 1960 respectively.

In each of the years referred to tax was imposed at a progressively increasing rate on taxable income derived by persons. By way of example the tax on a taxable income of £1,000 was £106. 5. 0., and the tax on a taxable income of £5,000 was £1,701. 5. 0. For the years ended 30th June, 1958, and 30th June, 1959 the taxable income of private companies was taxed at the rate of 4s. 6d. in the £ on so much of the taxable income as did not exceed £5,000 and 6s. 6d. in the £ on the remainder. For the year ended 30th June, 1960 the taxable income of private companies was taxed at the rate of 5s. in the £ on so much of the taxable income as did not exceed £5,000 and 7s. in the £ on the remainder. There was also, in each of the years referred to, tax imposed at the rate of 10s. in the £ on the undistributed income of private

companies. (Westbank is a private company within the meaning of the Income Tax and Social Services Contribution Assessment Act).

9. The Medical Practitioners Act 1938-1958 of the State of New South Wales makes provision for the registration as medical practitioners of persons possessing specified qualifications. Sections 35 of the Act provides, inter alia, that every registered person shall be entitled to sue in any court of competent jurisdiction for the recovery of the charge or remuneration for any medical or surgical advice, service, attendance, or operation rendered or performed by him. By section 40 unregistered persons are disqualified from holding certain appointments and by section 41A unregistered persons are prohibited from treating certain diseases. Section 41B of the Act provides that an unregistered person shall not be entitled to sue or counter-claim for or to set-off or otherwise recover any charge or remuneration for any medical or surgical advice, service, attendance or operation given or performed by him.

THE PARTNERSHIP.

10. Pursuant to a deed made on the 30th November, 1954 nine persons, including the Appellant, each of whom was registered as a medical practitioner under the Medical Practitioners Act of the State of New South Wales, carried on a medical practice in partnership in and around Cessnock in that State. The parties to the deed and their respective share in the capital, assets, profits and losses of the partnership were -

Vol.3. pp.603-641.
Vol.1. p.72, ll.32-39.
Vol.3. p.603,ll.8-22. p.604, l.18- p.605, l.13.

Charles Angus Wiles	14 per centum
Desmond Lees Peate	14 per centum
Deryk Willard Lawson	12½ per centum
Leonard Dolan Bertinshaw	12½ per centum
Peter Mathers	11 per centum
Kenneth John James Atkinson	11 per centum
Benjamin Short	11 per centum
William Allan Spence	7 per centum
Joseph Arthur Lancelot Allen	7 per centum
	100 per centum

11. The partnership deed recited that the parties had agreed to carry on in partnership the practice or profession of physicians surgeons and general medical practitioners in and around Cessnock. Pursuant to clause 1 of the deed the partnership

Vol.3. p.603,ll.24-30.
Vol.3. p.604, ll.1-15.

RECORD

was to commence from and including 1st October, 1954 and was to continue until determined in accordance with the deed. The partnership business was carried on in sections or groups. One group consisted of Wiles, Mathers and Short. A second group consisted of the Appellant, Atkinson and Spence and the third of Lawson, Bertinshaw and Allen (see clause 15).

Vol.1. p.100, ll.1-20.

Vol.3. p.612, l.25- p.613, l.29.

12. Each partner undertook to employ himself diligently in the practice and devote his whole time and attention thereto (clause 18(a)). He also undertook not to carry on any other profession directly or indirectly without the consent of the other partners or practice in any department of the medical or surgical profession except for the partnership benefit (clause 19 (g)).

Vol3. p.615, ll.10-16.

Vol.3. p.616, ll.42-48.

13. Clause 5 of the deed provided that the partners were to carry on their practice at their respective individual surgeries and professional rooms and were to duly pay all rent, rates and taxes or other charges in respect thereof. It was provided that the practices at Paxton and Bellbird were to be carried on at surgeries on certain land specified in the deed, such land and surgeries being held by William Arnold Conolly and the said Charles Angus Wiles as trustees for the partnership. The capital and assets of the partnership were to consist of the medical practice carried on by the partners and its goodwill, the stock of medicines, drugs and dressings held by the firm, the books of the partnership, the benefit of all covenants by other medical practitioners against competition and the said freehold properties at Paxton and Bellbird (clause 6). Apart from the said freehold premises at Paxton and Bellbird, the assets of the partnership did not include the residence or surgeries of the individual partners or any furniture, fittings, fixtures, plant and instruments usually kept by the individual partners in their surgery premises or any motor vehicle or vehicles in the possession of individual partners (clause 7). Under clause 9 all fees paid to any partner for professional services and the emoluments of every professional office or appointment were to be partnership property. The partnership was to bear all expenses, and outgoings incurred in carrying on the practice except the cost of replacement of motor vehicles used by the doctors (clause 10).

Vol.3. p.605, l.32- p.606, l.1.

Vol.3. p.606, ll.1-14.

Vol.3. p.606, ll.15-31.

Vol.3. p.607, ll.8-17.

Vol.3. p.608, ll.8-14.

14. Peter Mathers ceased to be a member of the partnership as from 1st July, 1956. At some time prior to 29th June, 1956 Mathers had given a notice under the partnership deed. Thereupon the proportions in which the partners were to share in the capital, assets, profits and losses of the partnership were as follows:-

Vol.3. p.648.

Vol.1. p.72, ll.37-39.

Charles Angus Wiles	14 per centum
Desmond Lees Peate	14 per centum
Deryk Willard Lawson	12½ per centum
Leonard Dolan Bertinshaw	12½ per centum
Kenneth John James Atkinson	12½ per centum
Benjamin Short	12½ per centum
Joseph Arthur Lancelot Allen	11 per centum
William Allan Spence	11 per centum
	100 per centum

15. On 20th August, 1956 there was a meeting of partners and it was agreed that the partnership would be dissolved on 31st August, 1956.

Vol.1. p.90, ll.4-10.

PRELIMINARY DECISIONS.

16. There were from time to time discussions between the partners (including the Appellant) with a view to the formation of a company to provide medical services. The partners (including the Appellant) obtained advice from their accountants and legal advisers and consideration was given to the formation of Westbank and the family companies and the manner in which they would operate. The partners (including the Appellant) then decided upon a scheme to be adopted and decided to take all the steps and make all the agreements which were subsequently taken and made to put the scheme into effect.

Vol.1. p.73, ll.12-22.
Vol.1. p.74, ll.15-20.
p.76, ll.9-49.
p.94, ll.14-17.
p.96, l.1-
p.102, l.26.
p.146,ll.23-29.

A.E. WESTBANK PTY. LTD.

17. On 29th June, 1956 Westbank was incorporated under the Companies Act 1936 of the State of New South Wales as a proprietary company limited by shares. The subscribers to the memorandum and the articles of association were Ernest Berge Phillips and Geoffrey Charles Davies (the solicitor and accountant of the Appellant) each of whom agreed to subscribe for one ordinary share in the capital of the company. The objects of the company included the following -

Vol.3. p.503
Vol.2. p.470, ll.13-18.
Vol.3. p.517, ll.1-12.
p.548, ll.1-10.
Vol.3. p.517, l.4, l.10.

(1) To purchase or otherwise acquire and carry on manage finance and undertake the whole or any part of the business (including the goodwill) property rights and liabilities of any person or company carrying on any business which the Company is authorised to carry on or possessed of property suitable for the purposes of the Company.

Vol.3. p.504, ll.10-17.

RECORD

p.505, 11.43-50. (9) To carry on the business of and dealers in anatomical, orthopaedic, radiological, scientific, chemical, photographical and surgical appliances of all kinds and the business of chemists, druggists and providers of medicinal surgical and hospital facilities and services of all kinds whether alone or in conjunction with any other person firm or corporation.

p.508, 11.14-25. (24) To purchase or otherwise acquire carry on and undertake all or any part of the business (including the goodwill property goods chattels effects choses in action and liabilities) of any person co-partnership or company carrying on any business of a like nature to any business which this Company is authorised to carry on or possessed of property suitable for any of the purposes of this Company and to conduct carry on liquidate and wind up or otherwise deal with any such business.

p.513, 11.7-22. (50) To provide for the welfare of persons in the employment of the Company or formerly engaged in any business acquired by the Company and the wives widows and families of any such persons by grants of money pensions or other payments and by providing or subscribing towards places of instruction and recreation and hospitals dispensaries medical and other attendances and other assistance as the Directors shall think fit and to form subscribe to or otherwise aid benevolent religious scientific national or other institutions or objects which have any moral or other claims to support or aid by the Company by reason of the locality of its operations or otherwise.

Vol.3. p.516, 11.9-10. 18. At all material times the nominal capital of Westbank was £25,000 divided into 25,000 shares of £1 each. The capital of the company

p.520, 11.17-33. was divided into a number of classes of shares. These classes were set out in article 5(1) of

Vol.2. p.471, 11.33-39. the articles of association. Prior to 10th September, 1956 the issued capital of Westbank consisted of 2 ordinary shares. Prior to 31st August, 1956 these shares had been held by the subscribers (being the solicitor and accountant of the Appellant) to the memorandum of

Vol.2. p.475. association. At a meeting of the directors of Westbank on 31st August, 1956 approval was given to transfers by Ernest Berge Phillips and Geoffrey Charles Davies (the solicitor and accountant of the Appellant) of the one ordinary share which each held to W. Raleigh Pty. Limited and W. Gladstone Pty. Limited

Vol.2. p.478. respectively. On 10th September, 1956 a further 198 ordinary shares were issued bringing the issued capital to 200 ordinary shares of £1 each. At all material times

thereafter the issued capital of the company consisted of these 200 shares. These shares were held as follows:- Vol.2. p.342, l.26- p.343, l.13.

W. Raleigh Pty. Limited	28 ordinary shares
W. Gladstone Pty. Limited	28 ordinary shares
Carban Pty. Limited	25 ordinary shares
G. Dalton Pty. Limited	25 ordinary shares
C. Hinton Pty. Limited	25 ordinary shares
Repton Pty. Limited	25 ordinary shares
C. Marlow Pty. Limited	22 ordinary shares
T. Neville Pty. Limited	22 ordinary shares
	200 ordinary shares

19. Until otherwise determined by ordinary resolution the company was to have not less than two nor more than seven directors. It was provided that a director need not be a member of the company (article 76). Article 77 provided that the first directors should be appointed by the subscribers to the articles of association by instrument in writing under their hands and that such directors when appointed should hold office until vacated under article 85. That article provided, inter alia, that the office of a director should, ipso facto, be vacated if the director resigned his office by notice in writing to the company. By ordinary resolution of the company passed on 13th August, 1956 the maximum number of directors was increased from seven to twelve. This was done in anticipation of other steps which were to follow.

Vol.3. p.536, ll.25-28. p.536, l.28. p.536, ll.29-32. Vol.3. p.540, ll.1-12. Vol.2. p.487. Vol.1. p.101, l.29- p.102, l.5.

20. The first directors of Westbank were William Berge Phillips and Ernest Berge Phillips, who were appointed pursuant to article 77 on 29th June, 1956. On 18th August, 1956 the eight medical practitioners who were then carrying on business in partnership were appointed directors of the company and on 20th August, 1956 William Berge Phillips and Ernest Berge Phillips ceased to be directors. On 4th November, 1959 Benjamin Short resigned as a director.

Vol.2. p.470, ll.9-28. p.472. Vol.2. p.501, ll.40-42.

W. RALEIGH PTY. LIMITED.

21. On 31st August, 1956 Raleigh was incorporated under the Companies Act 1936 of the State of New South Wales as a proprietary company limited by shares. The subscribers to the

Vol.3. p.550.

RECORD

Vol.3. p.564, 11.21-36. p.597.

memorandum and the articles of association were Ernest Berge Phillips and William Berge Phillips (the Appellant's Solicitors) each of whom agreed to take one ordinary share. The objects of the company included the following:-

Vol.3. p.551, 11.10-19.

(1) To purchase or otherwise acquire and to sell, exchange, surrender, lease, mortgage, charge, convert, turn to account, dispose of and deal with property and rights of all kinds and in particular mortgages, debentures, produce concessions, options, contracts, patents, annuities, licenses, stocks, shares, bonds, policies, book debts, business concerns and undertakings and claims, privileges and choses in action.

p.555, 11.7-18.

(20) To purchase or otherwise acquire carry on and undertake all or any part of the business (including the goodwill property goods chattels effects choses in action and liabilities) of any person co-partnership or company carrying on any business which this Company is authorised to carry on or possessed of property suitable for any of the purposes of this Company and to conduct carry on liquidate and wind up or otherwise deal with any such business.

p.560, 11.1-6.

(45) To carry on the business of importers and dealers in pharmaceutical, medicinal, chemical, industrial and other preparations and articles and providers of medical surgical hospital services and facilities of all kinds.

Vol.3. p.563, 11.17-20. Vol.3. p.567, 1.39- p.568, 1.18. Vol.2. p.449, 11.32-41. Vol.2. p.455.

22. The nominal capital of Raleigh was £25,000 divided into 25,000 shares of £1 each. The classes of shares were set out in article 5(1). Prior to 28th February, 1958 the issued capital of the Company consisted of two ordinary shares held by the subscribers to the memorandum of association. On 28th February, 1958 approval was given to the allotment to William Berge Phillips of 15 'C' class shares of £1 each fully paid and 15 'D' class shares of £1 each fully paid. On 24th April, 1958 approval was given to the allotment to William Berge

Vol.2. p.457.

Phillips of 335 'C' class shares of £1 each and 335 'D' class shares of £1 each in part satisfaction of dividends declared on that day.

Vol.2. p.460.

On 1st April, 1960 approval was given to the allotment to William Berge Phillips of 530 'C' class shares of £1 each and 530 'D' class shares of £1 each in satisfaction of dividends declared on that day. William Berge Phillips

Vol.1. p.103, 11.23-28.

held the 'C' class shares in trust for the Appellant's infant son John Peate and the 'D' class shares in trust for the Appellant's infant daughter Carolyn Peate under deeds of

settlement bearing date 21st November, 1957.

23. Article 76 provided that, until otherwise determined by ordinary resolution of the company, the number of directors should not be less than two nor more than seven. It was also provided that a director need not be a member of the company. Article 77 provided that the first directors should be William Berge Phillips and Ernest Berge Phillips and that each of them should hold office until vacated under article 85 thereof. Article 85 provided, inter alia, that the office of a director should, ipso facto, be vacated if the director resigned his office by notice in writing to the company.

Vol.3. p.584, ll.29-32. p.584, ll.33-36. p.588, ll.20-31.

24. Under clause 7 of the memorandum of association William Berge Phillips was appointed governing director with all the powers of the Board of Directors. The governing director was empowered to appoint his successor. On 1st September, 1956 the Appellant and his wife were appointed directors of the company and on 3rd September, 1956 the Appellant became governing director in place of William Berge Phillips. William Berge Phillips and Ernest Berge Phillips ceased to be directors of the company on 3rd September, 1956.

Vol.3. p.563, l.40- p.564, l.20. p.564, ll.15-20. Vol.2. p.451, ll.38-43. p.452, ll.11-26. p.452, ll.11-17.

STEPS TAKEN PRIOR TO 31ST AUGUST, 1956.

25. The following steps were taken prior to 31st August, 1956 -

(a) Westbank was incorporated on 29th June, 1956.

Vol.2. p.470, ll.13-18.

(b) On 13th August, 1956, article 76 of the articles of association of Westbank was amended to increase the maximum permissible number of directors from seven to twelve.

Vol.2. p.487.

(c) On 18th August, 1956 the eight partners were appointed directors of Westbank.

Vol.2. p.472.

(d) On 20th August, 1956 the partners agreed to dissolve the partnership as from 31st August, 1956.

Vol.1. p.90, ll.4-10.

(e) On 20th August, 1956 William Berge Phillips and Ernest Berge Phillips resigned as directors of Westbank and the Appellant was appointed Chairman of the Board of Directors.

Vol.2. p.473, ll.15-20. p.473, ll.21-23.

STEPS TAKEN ON 31ST AUGUST, 1956.

26. The following steps were taken on 31st August, 1956 -

(a) Raleigh was incorporated.

Vol.2. p.447, ll.13-18.

RECORD

p.447, ll.19-22. (b) William Berge Phillips and Ernest Berge Phillips were elected directors of the company and William Berge Phillips became the governing director.

Vol.1. p.94, ll.18-21. (c) Seven other companies were incorporated and each of the doctors who had previously been carrying on business in partnership became the governing director of a company. The names of the companies and of the doctor associated with each were as follows:-

Vol.1. p.80, ll.9-30.

W. Gladstone Pty. Limited	Charles Angus Wiles
Repton Pty. Limited	Deryk Willard Lawson
C. Hinton Pty. Limited	Leonard Dolan Bertinshaw
Carban Pty. Limited	Kenneth John James Atkinson
G. Dalton Pty. Limited	Benjamin Short
T. Neville Pty. Limited	William Allan Spence
C. Marlow Pty. Limited	Joseph Arthur Lancelot Allen

Vol.2. p.475. (d) Ernest Berge Phillips and Geoffrey Charles Davies transferred the ordinary shares in Westbank which they held to W. Raleigh Pty. Limited and W. Gladstone Pty. Limited respectively.

STEPS TAKEN ON 1ST SEPTEMBER, 1956.

Vol.2. p.450. 27. A meeting of the directors of Raleigh was held in Sydney on 1st September, 1956 at 10.40 a.m. William Berge Phillips reported that he had conducted negotiations with the Appellant on behalf of the company in connection with the purchase of the goodwill of the Appellant's medical practice together with instruments, furniture and plant at valuation. It was resolved that the company purchase the practice for £7,500 and the instruments, furniture and plant at a valuation to be mutually agreed upon between the Appellant and the company.

Vol.2. p.451. 28. A further meeting of the directors of Raleigh was held in Sydney on 1st September, 1956 at 10.50 a.m. William Berge Phillips reported to the meeting that, in accordance with the instructions of the Board, he had conveyed verbally on behalf of the company the acceptance of the verbal offer made by the Appellent for the purchase by the company of

certain assets. It appears from the documents annexed to Raleigh's return of income for the year ended 30th June, 1957 that the contract price for the purchase of goodwill, instruments, furniture, etc., was £9,542 including £7,500 for goodwill.

Vol.2. p.320, ll.28-33.

Vol.2. pp.313-314, 320.

29. It was also resolved at the meeting of Raleigh held at 10.50 a.m. that the company enter into a service agreement with the Appellant and that the company's seal be affixed thereto. It was further resolved that the company's seal be affixed to a form of agreement between the company and Westbank. Also at this meeting the Appellant and his wife Margaret Peate were appointed directors of Raleigh.

Vol.2. p.451, ll.21-30.

p.451, ll.38-43.

30. The service agreement between Raleigh and the Appellant was executed on 1st September, 1956. It provided that the company would employ the Appellant who would faithfully and to the best of his skill serve the company as medical practitioner in the business carried on by the company from the date of the agreement until the agreement should be terminated (clause 1). The Appellant was to receive a salary at the rate of £1,000 per annum or such other rate as might be mutually agreed upon from time to time (clause 2). Clauses 3, 7 and 9 of the agreement provided as follows -

p.451, ll.21-31.

Vol.2. p.223, ll.15-22.

p.223, ll.23-28.

"3. During the period of his employment hereunder the Doctor shall

Vol.2. p.223, l.29- p.224, l.21.

(a) Observe and conform to all the laws and customs of the medical profession.

(b) Fulfil and obey all the lawful directions and orders of the Directors of the Company from time to time and not at any time except in case of illness or other unavoidable cause absent himself from the service of the Company without the previous consent of the Directors of the Company.

(c) Not disclose (except to the Directors of the Company) any professional secrets or any information with respect to the Directors of the Company or his family, patients practice or affairs in relation to the affairs of the Company or any directions given him by the Directors of the Company.

7. (a) The Doctor hereby covenants that he will as the agent of the Company or its nominee ensure that any person to whom the Doctor renders medical or surgical treatments contracts whether

Vol.2. p.225, l.13- p.226, l.22.

orally or otherwise with the Company or its nominee that payment for such medical and surgical treatment is due to the Company or its nominee directly and even although the accounts for such services may be rendered by the Company or its nominee in the name of the Doctor AND IT IS EXPRESSLY AGREED that if the Doctor fails to carry out the terms of this covenant there shall become due and payable by the Doctor to the Company or its nominees as liquidated damages an amount equivalent to the amount of the usual fees for such treatment and in satisfaction of such liability for liquidated damages the Doctor covenants with the company that any moneys tendered or forwarded to him by any person in respect of such fees shall be the property of the Company or its nominee.

(b) The Doctor hereby authorises the Company or its nominee during the term of his employment hereunder to render in his name accounts for all medical and surgical treatment carried out or given by him during his employment and covenants that he will at the request and expense of the Company or its nominee do and agree to permit to be done all such actions and things as may be necessary or required by the Company for the purpose of ensuring payment of any account to the Company or its nominee.

Vol.2. p.227, ll.5-10.

9. The said Doctor agrees that he will during the term of this Agreement whenever required by the Board of Directors serve any Company or partnership carrying on a similar business to the Company as a medical practitioner during such time as the Board of Directors shall direct."

Vol.2. p.229, ll.26-30.

31. The agreement between Westbank, Raleigh and the Appellant, also executed on 1st September, 1956, provided that Raleigh would arrange for the Appellant its employee to serve Westbank as a medical practitioner to the best of his skill and ability from the date of the agreement until the agreement was terminated (clause 1).

p.229, l.31- p.230, l.14.

By clause 2 of the agreement Westbank was required to pay Raleigh during such time as the Appellant served Westbank a fee representing 14 per centum of the amount remaining after deducting from the gross income of Westbank all the expenses incurred in conducting Westbank's

business including any contributions to a provident fund to be established by Westbank. Clause 3 provided for an accounting in the event of the Appellant for any reason ceasing to serve Westbank. Clause 6 of the agreement was in identical terms to clause 7 of the agreement between the Appellant and Raleigh which is set out in paragraph 30 hereof.

Vol.2. p.230, ll.15-29.

p.231, l.26-p.233, l.11.

32. Similar agreements, except as to the amount payable by Westbank, were entered into between Westbank, the seven other family companies and the other doctors on the same day. The execution of these agreements by Westbank was authorised by a meeting of directors of that Company held at Cessnock on 1st September, 1956 at 8.30 p.m. At this meeting it was also resolved that Westbank make application to register the following as business names under the provisions of the Business Names Act 1934 of the State of New South Wales -

Vol.1. p.94, ll.21-30.

Vol.2. p.476, ll.16-34.

p.476, ll.45-54.

(a) D.L. Peate, K.J.J. Atkinson, W.A. Spence.

(b) C.A. Wiles, B. Short, J.A.L. Allen.

(c) L.D. Bertinshaw, D.W. Lawson.

The business name 'D.L. Peate K.J.J. Atkinson W.A. Spence' was registered under the said Act on or before 2nd July, 1957.

Vol.3. p.598.

33. It was also resolved at the meeting of directors of Westbank held on 1st September, 1956 that a draft agreement between Westbank and the family companies be executed under the common seal of the company, this agreement was not executed. There was an oral agreement between Westbank and the family companies under which each of the family companies undertook to supply a doctor, a car and a surgery; it was also agreed that if the family company did not have a surgery it would have to arrange to have a surgery available.

Vol.2. p.476, ll.35-44.

Vol.1. p.88, ll.16-28.

Vol.1. p.89, ll.1-8.

34. On 1st September, 1956 William Berge Phillips signed a document appointing the Appellant his successor as governing director of Raleigh and providing that the appointment should take effect as from the date of his resignation as a director or his death whichever should sooner happen. The Appellant became Governing Director of Raleigh on 3rd September, 1956.

Vol.2. p.467.

Vol.2. p.468.

STEPS TAKEN ON 3RD SEPTEMBER, 1956.

35. On 3rd September, 1956 a meeting of directors of Raleigh was held at Cessnock. The Appellant produced at the meeting a notice of resignation received from William Berge

Vol.2. p.452.

p.452, ll.11-17.

Phillips as governing director and Ernest Berge Phillips as director and these resignations were accepted. William Berge Phillips also resigned as director. The formal appointment of the Appellant as governing director was tabled and it was resolved that the appointment be noted. The Appellant's wife was appointed Secretary and the Appellant Public Officer of the company. It was also resolved that the company accept the offer of the Appellant to make available to the company the surgery at 230 Main Street, Cessnock, such surgery to be exclusively occupied by the company with a right to sub-let the same provided that the company either arranged for the rent to be paid directly to the Appellant or paid to him the amount it received for sub-letting.

Vol.2. p.469.
Vol.2. p.452, ll.11-26.
p.452, ll.27-32.
p.452, ll.33-39.
p.452, ll.40-53.

STEPS TAKEN ON 10TH SEPTEMBER, 1956.

36. At a meeting of the directors of Raleigh at Cessnock on 10th September, 1956, it was resolved that Raleigh apply for 27 ordinary shares of £1 each in Westbank. On the same day at a meeting of the directors of Westbank it was resolved that ordinary shares be issued to each of the family companies. The total number of shares so issued was 198 following which the issued shares were held as set out in paragraph 18 hereof. It was also resolved by the directors of Westbank that the company use the provisions of the agreements with the family companies when rendering accounts or making claims upon medical funds or public departments or like institutions if this course were more expeditious than rendering the accounts or making the claims directly in the company's name.

Vol.2. p.453, ll.19-22.
Vol.2. p.478, ll.22-45.
Vol.2. p.478, ll.13-21.

SUPERANNUATION.

37. By deed made 15th May, 1957 Westbank instituted a superannuation fund for the benefit of the employees of Westbank and their dependants and also for the employees of the family companies and their dependants. At a meeting of the directors of Raleigh on 15th May, 1957 Raleigh, as an associated company, nominated the Appellant and his wife as members of the Fund.

Vol.2. p.479, ll.13-38.
Vol.2. p.454, ll.10-48.

CONDUCT OF THE PRACTICE.

38. After 1st September, 1956 the former partners rendered medical services in the same manner as before and used the surgeries which had been used by the partnership. At some time after 1st September, 1956 a plate with the name A.E. Westbank Pty. Limited was added to the plates bearing the doctors' names

Vol.1. p.93, ll.1-18.
p.109, ll.1-5.
Vol.1. p.61, ll.15-27.
p.77, ll.15-23.

at the surgeries, and later still notices were exhibited at the surgery used by the Appellant indicating that the doctors were employees of Westbank and that fees were due to Westbank. The Appellant and his receptionist then commenced telling patients that this was the case. After some time the name A.E. Westbank Pty. Limited was stamped on accounts and receipts which had previously borne only the names of the doctors by whom the surgeries were used. During the years ended 30th June, 1958, 30th June, 1959 and 30th June, 1960 most of the patients and all of the public and private institutions for whom medical services were rendered paid by cheques made payable to the medical practitioners personally.

p.78, l.28-
p.79, l.23.
Vol.3.
p.599-600.
Vol.1.
p.53, l.21-
p.54, l.22.
Vol.1.
p.77, ll.25-38.
Vol.1.
p.51, l.42-
p.52, l.5.
p.54, l.32-
p.55, l.4.
p.55, l.8-
p.56, l.45.
p.61, ll.28-37.
p.62, ll.1-42.
p.151, ll.3-14.

YEAR ENDED 30TH JUNE, 1958.

39. The profit and loss account of Westbank for the year ended 30th June, 1958 disclosed gross fees paid or payable to Westbank of £56,245.9.9. Total expenditure for the year was shown as £51,245.9.9., including service fees paid to the family companies totalling £41,574.10.8., staff salaries £4,743.3.6. and contributions to the staff provident fund (in respect of receptionist - secretaries) £1,200.0.0. The account showed a nett profit of £5,000.0.0. The income tax return showed a taxable income of £5,013.0.0.

Vol.2. p.386.

Vol.2. p.381.

40. The profit and loss appropriation account of Westbank for the year ended 30th June, 1958 showed that dividends of £3,750 were paid. Of this sum £525 was paid to Raleigh.

Vol.2. p.387.
Vol.2.
p.391, ll.22-25.

41. The manner in which the sum of £41,574.10.8. service fees was apportioned between the various companies and the percentage which the amount credited to each company bears to the total appears from the table hereunder:-

W. Raleigh Pty. Ltd.	£5,820. 8. 8.	14%
W. Gladstone Pty.Limited	£5,820. 8. 8.	14%
Repton Pty. Limited	£5,196.16. 4.	12.5%
C. Hinton Pty. Limited	£5,196.16. 4.	12.5%
Carban Pty. Limited	£5,196.16. 4.	12.5%
G. Dalton Pty. Limited	£5,196.16. 4.	12.5%
T. Neville Pty. Limited	£4,573. 4. 0.	11%
C. Marlow Pty. Limited	£4,573. 4. 0.	11%
	£41,574.10. 8.	100%

Vol.3.
p.688, ll.7-15.

RECORD

Vol.2. p.374. 42. The profit and loss account of Raleigh in respect of the year ended 30th June, 1958 showed receipts payable to it totalling £6,345.8.8, being £5,820.8.8. service fees and £525 dividend, and expenditure totalling £4,767.3.4. which included salaries of £1,560 and £1,200 paid to the Appellant and his wife respectively and contributions to the Superannuation Fund of £200 in respect of the Appellant and £200 in respect of his wife.

Vol.2. p.370.

Vol.2. p.377.

43. The profit and loss appropriation account of Raleigh for the year ended 30th June, 1958 showed that the company paid dividends totalling £770 during the year.

Vol.2. p.374.

44. The Appellant's return of income derived by him in the year ended 30th June, 1958 disclosed a taxable income of £1,232. His assessable income as returned included an amount of £1,560, being salary from Raleigh, £113 from the former partnership and £225 from rents, making a total of £1,898.

Vol.1. p.3.
Vol.1. p.2.

45. The Respondent assessed the Appellant to income tax and social services contribution upon a taxable income of £4,298, which the adjustment sheet attached to the notice of assessment showed to have been calculated as follows:-

Vol.1. p.6.

Taxable income as returned		£1,232. 0. 0.
Add additional income from partnership		6,690. 0. 0.
Subscription to British Medical Association reduced from £12,12.0. to £10.10.0. maximum		2. 0. 0.
		£7,924. 0. 0.
Deduct:		
Salary from Raleigh now excluded:	£1,560	
Allowable deductions in connection with additional partnership income:	£2,066	3,626. 0. 0.
		£4,298. 0. 0.

Vol.1. p.7, ll.12-25. The amount of £6,690 was ascertained as follows:-

Net income of Westbank as returned		£5,013
Add:		
Superannuation contributions	£ 1,200	
Service Fees	£41,574	42,774
Net income as adjusted		£47,787

Individual interest of the Appellant therein: £6,690.

The said sum of £6,690 represented 14 per centum of the sum of £47,787.

46. The deductions of £2,066 were ascertained as follows:- Vol.1. p.7, ll.26-48.

Expenditure shown in profit and loss account for Raleigh for year ended 30th June, 1958		£4,767
Less:		
Private proportion of car expenses:	£ 45	
Private proportion of depreciation on car:	33	
Superannuation contributions	400	
Remuneration of the Appellant	1,560	
Remuneration of Appellant's wife reduced from £1,200 to £540	660	
Cost of signboard	3	£2,701
Deductions allowed		£2,066

Menzies, J. held that the sum of £1,200 representing superannuation contributions paid by Westbank in respect of six receptionist-secretaries should have been allowed as a deduction. Vol.1. p.167, ll.4-19. p.171, ll.23.-30.

YEAR ENDED 30TH JUNE, 1959.

47. On 19th November, 1958 G. Dalton Pty. Limited withdrew the services of Benjamin Short from Westbank, but Short did not resign as a director until 4th November, 1959. The shares which G. Dalton Pty. Limited had held in Westbank were purchased by the Appellant and C.A. Wiles and held in reserve and later sold to junior doctors. Upon the withdrawal of a doctor the accounts were made up to the date of his withdrawal and his family company received service fees for work done prior to that date. Vol.1. p.81, ll.11-14. Vol.2. p.501, ll.40-42.

48. The profit and loss account of Westbank for the year ended 30th June, 1959 disclosed gross fees paid or payable to Westbank of £51,559.4.5. Total expenditure for the year was shown at £46,559.4.5. including service Vol.2. p.410

fees paid to family companies totalling £34,386.4.11, staff salaries £5,829.14.10. and staff provident fund contributions £1,200. The account showed a nett profit of £5,000 and the same amount was also the amount shown as taxable income in the company's income tax return.

Vol.2. p.411. 49. The profit and loss appropriation account of Westbank for the year ended 30th June, 1959 showed that dividends of £5,175 were paid. Of this sum £724.10.0. was paid to Raleigh.

50. The manner in which the sum of £34,386.4.11. service fees was apportioned between the various companies and the percentage which the amount credited to each company bears to the total appears from the table hereunder:-

Vol.3. p.688, ll.16-25.

W. Raleigh Pty. Limited	£5,155.12. 3	14.993%
W. Gladstone Pty. Limited	£5,155.12. 3	14.993%
Repton Pty. Limited	£4,704. 5. 8	13.681%
C. Hinton Pty. Limited	£4,704. 5. 8	13.681%
Carban Pty. Limited	£4,704. 5. 8	13.681%
G. Dalton Pty. Limited	£1,456. 7. 2	4.235%
T. Neville Pty.Limited	£4,252.18. 2	12.368%
C. Marlow Pty. Limited	£4,252.18. 2	12.368%
	£34,386. 4.11	100%

Vol.2. p.399. 51. The accounts of Raleigh for the year ended 30th June 1959 showed service fees £5,155.12.3. and dividends £724.10.0. and expenditure totalling £5,642.18.2., which Vol.2. p.394. included salaries of £2,080 and £1,300 paid to the Appellant and his wife respectively, and contributions to the Superannuation Fund Vol.2. p.403. of £200 in respect of the Appellant and £200 in respect of his wife.

52. The profit and loss appropriation account of Raleigh for the year ended 30th June, 1959 showed that the company paid dividends Vol.2. p.400. totalling £1,060 during the year.

53. The Appellant's return of income derived Vol.1. p.17. by him in the year ended 30th June, 1959 disclosed a taxable income of £1,399. His assessable income as returned included salary Vol.1. p.16. from Raleigh £2,080 and an amount of £1 from the former partnership.

54. The Respondent assessed the Appellant to income tax and social services contribution on a taxable income of £3,243 which the adjustment sheet attached to the notice of assessment showed to have been calculated as follows:- Vol.1. p.20.

Net income as returned			£1,399
Add share of income from partnership	£6,091		
section 59(2) adjustment on sale of car	60		
rents	77		
subscription to British Medical Association reduced to £10.10.0.	2		£6,230
Deduct salary from Raleigh now excluded	£2,080		
expenses connected with practice	£2,306		£4,386
Taxable income			£3,243

The amount of £6,091 was ascertained as follows:

Net income as returned by Westbank		£5,000	Vol.1. p.21, ll.12-30.
Add Superannuation Fund contributions	£1,200		
Interest on loan	48		
Valuation fees	17		
Service fees	34,386	35,651	
Net income as adjusted		£40,651	
Individual interest of Appellant therein		£6,091	

The deductions of £2,306 were ascertained as follows:

Expenditure shown in profit and loss account of Raleigh for year ended 30th June, 1958		£5,643	Vol.1. p.21, l.31- p.22, l.23.
Less Private portion of car expenses	£ 55		
Private portion of car depreciation	39		
Private portion of car insurance	3		

Superannuation fund contributions	400	
Remuneration of Appellant	2,080	
Remuneration of Appellant's wife reduced from £1,300 to £540	760	£3,337
Deductions allowed		£2,306

Vol.1. p.167, ll.4-19. p.174, ll.24-31.

55. Menzies, J. held that the sum of £1,200 representing superannuation contributions paid by Westbank in respect of six receptionist-secretaries should have been allowed as a deduction. Menzies, J. also held that the Appellant should have been assessed on the basis of 14.993 per centum of the difference between the amounts paid to or credited to Westbank as fees and the amounts paid by it as expenses of the medical practice.

Vol.1. p.167, l.20- p.168, l.21. p.174, l.25- p.175, l.7.

YEAR ENDED 30TH JUNE, 1960.

Vol.1. p.81, ll.16-22. p.86, ll.11-20.

56. On 1st October, 1959 W. Gladstone Pty. Limited withdrew the services of Charles Angus Wiles from Westbank, but he served the company as an employee and remained a director until approximately 18th December, 1959. The accounts of Westbank were made up as at 30th September, 1959 and again as at 30th June, 1960, and copies of both sets of accounts were attached to Westbank's return of income for the year ended 30th June, 1960.

Vol.2. p.433.

57. The profit and loss account of Westbank for the period ended 30th September, 1959 disclosed gross fees of £15,681.4.4. Total expenditure was shown at £14,598.9.4. including service fees paid to family companies totalling £10,462.18.9.

58. The manner in which the sum of £10,462.18.9. was apportioned between the various companies appears from the table hereunder:-

Vol.2. p.441.

W. Raleigh Pty. Limited	£1,674. 1. 6.
W. Gladstone Pty. Limited	1,674. 1. 6.
Carban Pty. Limited	1,494.14. 1.
C. Hinton Pty. Limited	1,494.14. 1.
Repton Pty. Limited	1,494.14. 1.
C. Marlow Pty. Limited	1,315. 6. 9.
T. Neville Pty. Limited	1,315. 6. 9.
	£10,462.18. 9.

59. The profit and loss account of Westbank for the year ended 30th June, 1960 disclosed gross fees of £50,763.10.4. and rents £285. Total expenditure for the year was shown as £46,048.10.4., including service fees paid to the family companies totalling £33,330.9.6., staff salaries £6,893.5.10. and contributions to staff provident fund £150. The account showed a nett profit of £5,000, and the income tax return of Westbank showed a taxable income of £5,040. Vol.2. p.437. Vol.2. p.428.

60. The profit and loss appropriation account of Westbank for the year ended 30th June, 1960 showed that dividends of £3,325. were paid. Of this sum £532 was paid to Raleigh. Vol.2. p.438. p.441.

61. The manner in which the sum of £33,330.9.6. service fees was apportioned and the percentage which the amount credited to each company bears to the total appears from the table hereunder:-

W. Raleigh Pty. Limited	£5,271. 4. 4.	15.815%	Vol.2. p.442.
W. Gladstone Pty. Limited	1,674. 1. 6.	5.022%	Vol.3. p.688.
Repton Pty. Limited	4,706. 8. 9.	14.121%	
C. Hinton Pty. Limited	4,706. 8. 9.	14.121%	
Carban Pty. Limited	4,706. 8. 9.	14.121%	
T. Neville Pty. Limited	4,527. 1. 5.	13.582%	
C. Marlow Pty. Limited	4,527. 1. 5.	13.582%	
Dr. W. Pitsch	1,670. 2. 0.	5.011%	
Dr. W. Cook	1,541.12. 7.	4.625%	
	£33,330. 9. 6.	100%	

62. The profit and loss account of Raleigh in respect of the year ended 30th June, 1960 showed receipt of service fees £5,271.4.4. and dividends £532. It also showed expenditure of £5,552.16.10. including salaries of £2,080 to the Appellant and £1,300 to his wife, director's fees of £200 to the Appellant and contributions to the Superannuation Fund of £200 in respect of the Appellant and £200 in respect of his wife. Vol.2. p.422. Vol.2. p.418. Vol.2. p.426.

63. The profit and loss appropriation account of Raleigh for the year ended 30th June, 1960 showed that the company paid dividends totalling £1,060 during the year. Vol.2. p.422.

64. The Appellant's return of income derived by him during the year ended 30th June, 1960 disclosed a taxable income of £1,735. His assessable income as returned included salary and director's fees from Raleigh £2,280, Vol.1. p.29. Vol.1. p.28.

lecture fees £2, fees earned prior to the formation of Raleigh £64, amount received from the former partnership £1 and rents £260.

65. The Respondent assessed the Appellant to income tax and social services contribution upon a taxable income of £3,574, which the adjustment sheet attached to the notice of assessment showed to have been calculated as follows:-

Vol.1. p.32.

Taxable income as returned		£1,735
Add net income from partnership		6,097
		7,832
Deduct salary and directors fees received from Raleigh	£2,280	
Expenses claimed by Raleigh	1,978	£4,258
Taxable Income		£3,574

The amount of £6,097 was ascertained as follows:-

Vol.1. p.33, ll.11-30.

Net income of Westbank as returned		£5,040
Add Superannuation fund contributions	£ 150	
Interest on super-annuation fund loan	164	
Registrar-General's fees	6	
Frames for Certificates of Incorporation	8	
Service fees	33,330	33,658
		£38,698
Less net income from rents		142
Net income as adjusted		£38,556
Individual interest of Appellant therein		£ 6,097

Vol.1. p.33, l.31- p.34, l.23.

The deductions of £1,978 were ascertained as follows:-

Expenditure shown in profit and loss account of Raleigh for year ended 30th June, 1960		£ 5,553
Less Registrar-General's fees	£ 6	

Superannuation contributions	400	
Interest and registration regarding mortgage	46	
Director's fees	200	
Wages of Appellant	2,080	
Wages of Appellant's wife reduced from £1,300 to £540	760	
Car expenses not incurred in production of assessable income	44	
Reduction of car depreciation in terms of section 61	39	£3,575
Deductions allowed		£1,978

66. Menzies, J. held that the sum of £150 representing superannuation contributions paid by Westbank should have been allowed as a deduction. He also held that the Appellant should have been assessed on the basis of 15.815 per cent. of the difference between the amounts paid to or credited to Westbank as fees and the amounts paid by it on account of the expenses of the medical practice.

Vol.1. p.167, ll.1-19. p.167, l.20-p.168, l.21. p.177, l.25-p.178, l.9.

DERIVATION OF INCOME.

67. Menzies, J., having held that the basis of assessment adopted by the Respondent was justified by the application of section 260, found it unnecessary to deal with an argument advanced by the Respondent that the whole of the fees returned as income by Westbank were in fact payments for services rendered by the doctors and constituted income derived by the doctors. Similarly the Full Court of the High Court found it unnecessary to consider arguments that if section 260 did not apply the whole or some part of the income assessed to the Appellant was nevertheless income derived by him within the meaning of section 17 of the Act. It was accepted by the parties that if the Court should hold that the assessments the subject of appeal were not justified by the operation of section 260 but that some part of the income returned as income by Westbank was in fact derived by the Appellant further investigation might be necessary in order to segregate such part; and it was agreed that in such an event it would be desirable that the Court should order that the assessments be remitted to the Respondent for re-assessment.

Vol.1. p.160, l.13-p.161, l.34.

SECTION 260.

68. The Respondent submits that the decisions of Menzies, J. and the Full Court of the High Court were right. It submits

(a) that there was an arrangement entered into having or purporting to have a purpose or effect stated in one or more of paragraphs (a), (b), (c) or (d) of section 260; and

(b) that upon the facts remaining, after stripping aside so much of the arrangement as gave effect to that purpose, the Appellant derived the income upon which he was assessed.

If both matters referred to in paragraphs (a) and (b) of the preceding sentence exist, the assessments appealed from are supported.

69. The section does not impose upon a person a liability to pay income tax; that liability is imposed by other sections. The function the section performs is to leave exposed to the liability-imposing sections what remains after it has treated as absolutely void in proceedings under the Act or as against the Commissioner so much of a 'contract, agreement or arrangement' as has or purports to have the purpose or the effect, inter alia, of avoiding a liability imposed by the Act on any person or of preventing the operation of the Act in any respect or of altering the incidence of tax.

70. It is every 'contract, agreement or arrangement' having or purporting to have one or more of the purposes or effects referred to in paragraphs (a) to (d) of the section that it renders absolutely void to the stated extent as against the Commissioner or in regard to proceedings under the Act. Such 'contracts, agreements or arrangements' may take a variety of forms. What appears in the two succeeding paragraphs of this case are but specific illustrations of 'contracts, agreements or arrangements' which may be of the type described in section 260.

71. A liability imposed by the Act may be avoided by the making of a 'contract, agreement or arrangement' having an effect that income was not derived by a person which income, if the 'contract, agreement or arrangement' had not been made, would have been derived by him.

72. The operation of the Act may be prevented if a 'contract, agreement or arrangement' is made having an effect of preventing the operation the Act would have in a given case

if the 'contract, agreement or arrangement' had not been made. We will hereafter refer to a 'contract, agreement or arrangement' simply as an arrangement.

73. Section 17 imposes upon persons deriving a taxable income during a year of income a liability to pay income tax and social services contribution at the rates declared by Parliament upon that taxable income.

74. The liability imposed by section 17 may be avoided or its operation in any given case may be prevented by arrangements which affect a taxpayer's income before that income has been derived by him. For no arrangement working on income after it has been derived can affect the liability it imposes on a taxpayer nor prevent its operation on that income. One arrangement may change into capital income which at the moment of change has not been derived by the taxpayer. The effect of such an arrangement is an ultimate beneficial receipt by the taxpayer but not of income : so that in such a case the escape from section 17 is made by selecting for avoidance so much of it as refers to 'taxable income'. Another arrangement may fasten on income which has not yet been derived by a particular taxpayer and substitute a person controlled by him to be the deriver of that income in his stead. The effect of this arrangement is the receipt by the substitute taxpayer of income for the benefit of the particular taxpayer; so that in this case the escape from section 17 is made by selecting for avoidance so much of it as refers to 'income derived'.

75. Thus an arrangement designed to substitute one person for another as the deriver of income may be an arrangement of the type described by section 260 as fully as an arrangement designed to substitute a capital receipt for an income receipt. In every case whatever form the arrangement may have taken, the ultimate question is : do the liability-imposing sections operate upon the facts exposed by section 260.

76. The arrangement which the Appellant set up is one the purpose of which was to substitute Westbank for him as the deriver of the income which his exertions produced. A purpose of that substitution was that the Appellant should derive part only of the income produced by his exertions and not the whole as theretofore. Because Parliament declared rates at which income tax and social services contribution should be paid which decreased progressively as the taxable income decreased, the arrangement was one having the effect of avoiding a liability to pay tax and contribution upon the

whole of the income produced by his exertions at the rate applicable to the whole of that income. The arrangement replaced that liability by a liability to pay tax and contribution upon a part only thereof and at a lower rate. The arrangement thus has as a purpose or effect within section 260.

77. The facts remaining after stripping aside so much of the arrangement as substituted Westbank for the Appellant as the deriver of the income produced by the Appellant's exertions are:

(a) the Appellant practising medicine as a physician and surgeon in the same manner as theretofore,

(b) income produced by that practice,

(c) that income being paid with other income into a bank account,

(d) the payment thereout of the cost of production of the entire income produced,

(e) the dealing with part of that income (after such payment) in accordance with the Appellant's directions.

These facts are sufficient to attract sections 17 and 19.

78. The Respondent submits that the construction of section 260 adverted to above is consistent with and supported by the authorities hereinafter referred to as well as the views of the section adopted by the High Court in this case.

79. The Respondent submits that the arrangement outlined above is not capable of explanation by reference to ordinary business or family dealing, particularly having regard to the following matters:-

(a) After the arrangement the work of the practices was carried out in the same manner as theretofore.

(b) Section 41B of the Medical Practitioners Act 1938-1958 of New South Wales which,

in the Respondent's submission, precludes a company from suing for fees for medical services.

(c) Section 82F of the Income Tax and Social Services Contribution Assessment Act 1936-1958, as amended, which, in the Respondent's submission, does not permit a taxpayer to claim a deduction for fees paid to a company for medical services provided.

(d) The sale by the Appellant to Raleigh of the assets and goodwill of his practice and his agreement to serve Raleigh, a company which did not, and was not intended to, conduct a medical practice.

(e) The employment by Raleigh of the Appellant's wife.

(f) The provisions of clause 7 of the Appellant's agreement with Raleigh and of clause 6 of the agreement between Westbank, Raleigh and the Appellant.

(g) The registration by Westbank as business names of the names of the former partners.

80. The Respondent submits that the steps or elements of the arrangement which effectuated the purpose of avoiding the Appellant's liability to tax, or of preventing the operation of the Act, or of altering the incidence of tax, and which are therefore void as against the Respondent, are: the separate corporate existence of Westbank, the agreement between the Appellant and Raleigh, the agreement between Westbank, Raleigh and the Appellant, the agreements between Westbank, the other family companies and the other doctors and the agreements, (if any) made between Westbank and the patients and the Appellant and the patients so far as they provided that fees should be the property of Westbank. Alternatively the Respondent submits that the said purpose was effectuated by the agreements above-mentioned and that they are therefore void as against the Respondent.

81. It follows in the submission of the Respondent that the facts which remain to be considered after section 260 has done its work of annihilation for the purposes of assessing the Appellant to income tax are that

the Appellant was carrying on the practice of his profession in association with a group of other medical practitioners, and that the income the product of their activities was paid into Westbank's bank account and after payment of group expenses was, at the direction of the Appellant and his fellow-practitioners, distributed in agreed proportions. The Respondent submits that these facts permit of no other conclusion than that the fees the product of the activities of the group constituted income derived by the group and that the Appellant derived as income a part of the total income proportionate to the part agreed to be distributed to Raleigh. In the submission of the Respondent therefore, subject only to the adjustments directed to be made by Menzies, J., assessments made by the Respondent were correctly made.

DOUBLE TAXATION.

82. Section 260 operates upon arrangements. The effect of that operation is the absolute avoidance of the arrangement as against the Commissioner or in proceedings under the Act. The section works upon the arrangement by reason of its own force; the section is not invoked by any person nor is its application dependent upon the volition of the Commissioner; The avoidance which it brings about is an avoidance absolute as against the Commissioner. The extent of this absolute avoidance is determined by the expression "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."

Where the section has brought about the avoidance of an arrangement to the extent referred to above, the arrangement is to

that extent void and void absolutely as against the Commissioner. This avoidance is constant, that is to say, the arrangement remains void to the stated extent whomever the Commissioner is assessing.

83. In the instant case the effect of the avoidance of the arrangement was that Westbank and the family companies did not beneficially receive the income in question. This receipt was a receipt of income derived not by them but by the Appellant and the other doctors.

It thus follows:-

(a) The effect of the arrangement was to substitute Westbank for the Appellant as the beneficial recipient of the income produced by the Appellant's exertions.

(b) That arrangement is rendered void as against the Commissjoner so that there is exposed a naked receipt as distinct from a beneficial receipt by Westbank and the family companies of income dealt with by them as the Appellant directed or on his behalf.

(c) The result referred to in paragraph (b) above exists whether the Commissioner assesses the Appellant or Westbank or the family companies.

84. Therefore, neither Westbank nor the family companies could be assessed, nor have they been assessed upon the income assessed to the Appellant. Section 260 requires the Commissioner to treat Westbank and the family companies as not deriving the income they received. The result is that no question of double taxation can arise in the present case. This view of section 260 is supported by the decision of the Full Court of the High Court of Australia in Rowdell Pty. Ltd. v. The Commissioner of Taxation 111 C.L.R. 106. In that case Rowdell Pty. Limited, a company which dealt in shares, acquired shares in a number of companies and obtained their accumulated profits by means of distributions of dividends or on

RECORD

liquidation. The shares were acquired by Rodwell Pty. Limited pursuant to arrangements which were void against the Commissioner of Taxation under section 260 as far as the vendor-shareholders were concerned in that they had the purpose or effect of avoiding the liability to tax which the vendor-shareholders would have incurred on the profits which in the event were distributed to Rowdell Pty. Limited. The Commissioner sought to tax Rowdell Pty. Limited on the basis that in view of the arrangement the sums received constituted income of a character other than dividends. It was held by the Full Court of the High Court that the arrangement was void to the extent to which it had the purpose or effect referred to in paragraphs (a) to (d) of section 260 but because the arrangement did not have the purpose or effect of avoiding any liability imposed by the Act on Rowdell Pty. Limited the Commissioner could not treat the dividends received by Rowdell Pty. Limited as if they constituted income other than dividends. The Respondent relies in particular upon the passages in the judgment of Dixon, C.J. (as he then was) at pages 116-117; Kitto, J. at pages 122-125; Menzies, J. at pages 134-136.

10

20

30

85. In addition the structure of the Income Tax and Social Services Contribution Assessment Act differs significantly from that of the Income Tax Acts of the United Kingdom. The Commonwealth Act brings to charge not various classes of income only, but rather the income of the taxpayer (which is not exempt income) after permitting the statutory deductions.

40

86. Section 17 of the Act imposes income tax and social services contribution at the rates declared by the Parliament upon the taxable income derived during the year of income by any person whether a resident or a non-resident.

87. Section 6(1) defines 'taxable income' as meaning the amount remaining after deducting from the assessable income all allowable deductions.

50

88. Section 25(1) provides that the assessable income of a taxpayer shall include -

(a) where the taxpayer is a resident - the gross income derived directly or indirectly from all sources whether in or out of Australia; and

(b) where the taxpayer is a non-resident - the gross income derived directly or indirectly from all sources in Australia

which is not exempt income.

89. Section 26 provides that the assessable income of a taxpayer shall include the matters the section refers to. The Act contains no definition of income but does contain definitions of income from personal exertion, income derived from personal exertion and income from property.

90. Section 44(1) brings into the assessable income of a shareholder in a company as a fresh accrual of income, in the case where the shareholder is a resident, dividends paid to him by the company out of profits derived by it from any source and, in the case where he is a non-resident, dividends paid to him by the company to the extent to which they are paid out of profits derived by it from sources in Australia. The section in addition excludes certain types of dividend from the assessable income of the taxpayer.

91. It is, therefore, apparent in the Respondent's submission that the problems which were considered by the House of Lords in such cases as Cenlon Finance Co. Ltd. v. Ellwood (Inspector of Taxes) (1962) A.C. 782 and Inland Revenue Commissioners v. F.S. Securities Ltd. (1964) 1 W.L.R. 742 do not arise under the Commonwealth Act. Nor can the application of section 260 to the Appellant's income for the years in question here result in the Appellant paying income tax twice on the same income.

92. It would, in the Respondent's submission, follow that section 260 cannot be construed in a manner which would deny its application to the Appellant by reference to any rule relating to double taxation. This conclusion, the Respondent submits, is supported, so far as the Commonwealth Act is concerned, by the decision in Canadian Eagle Oil Co. Ltd. v. The King (1946) A.C. 119. Even if contrary to the Respondent's submission the construction of section 260 contended for by him "would really involve double taxation" (Inland Revenue Commissioners v. F.S. Securities Ltd. (supra)), the Respondent submits that the presence of section 260 in the Act and the language employed in the section involves that it was the intention of the legislature to penalise particular taxpayers who resorted to the contracts, agreements or arrangements the section refers to : Lord Howard de Walden

RECORD

v. Inland Revenue Commissioners (1942) 1 K.B. 389. In addition no argument was advanced by the Appellant before the High Court either that the application of the section in this case would result in his being taxed twice on the same income or that the section should be construed by reference to any rule relating to double taxation.

AUTHORITIES RELATING TO SECTION 260.

93. The Respondent submits that the application of section 260 to the facts of the present case and its operation in the manner submitted by the Respondent is supported by the authorities in which the section has been discussed by this Board and by the High Court of Australia.

94. The section was considered by the Board in Newton v. Federal Commissioner of Taxation (1958) A.C. 450 in which the principal previous decisions of the Full High Court on section 260 were considered and approved. In Newton's case the facts in brief summary were that three private companies trading in motor vehicles had accumulated large profits which, if distributed, would result in the shareholders being assessed to income tax at high rates of tax and upon which, if not distributed, the companies would be assessed to undistributed profits tax. Acting upon the advice of a consulting accountant a number of transactions were carried out by the companies, their shareholders and another private company, Pactolus Pty. Limited. Shares carrying special dividend rights were sold by the shareholders to Pactolus Pty. Limited at a price which took into consideration the anticipated dividends. The special dividends were then declared and paid to Pactolus Pty. Limited which was thereby enabled to pay the purchase price. At about the same time Pactolus Pty. Limited applied for and was allotted preference shares in the three companies, which it immediately resold to the shareholders at the same price. In all, the three companies distributed £1,764,136 as special dividends of which Pactolus Pty. Limited retained £102,414 and the shareholders received from Pactolus Pty. Limited as capital (the purchase price of shares) £1,661,722. It was held by the Full Court of the High Court of Australia and by this Board that there was an arrangement to which section 260 applied, that the section avoided the transfers of the special dividend rights, and that the Commissioner of Taxation was therefore entitled to treat the whole of the special dividends as income of the original shareholders of the three motor companies.

95. In Newton's case the Board said at p.465:-

"Their Lordships are of the opinion that the word 'arrangement' is apt to describe something less than a binding contract or agreement, something in the nature of an understanding between two or more persons - a plan arranged between them which may not be enforceable at law. But it must in this section comprehend, not only the initial plan but also all the transactions by which it is carried into effect - all the transactions, that is, which have the effect of avoiding taxation, be they conveyances, transfers or anything else."

and at p.466:-

"In order to bring the arrangement within the section you must be able to predicate - by looking at the overt acts by which it was implemented - that it was implemented in that particular way so as to avoid tax. If you cannot so predicate but have 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 the arrangement does not come within the section."

and at p.467-8:-

"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. Their Lordships agree with the way in which Fullagar J. put it in his judgment: 'Section 260 alters nothing that was done as between the parties. But, for the purposes of income tax, it entitles the commissioner to look at the end result and to ignore all the steps which were taken in pursuance of the avoided arrangement.' "

and at p.468:-

"Now the commissioner can trace the sum of £1,661,722 in cash actually into the hands of the original shareholders. He is entitled, therefore, to treat it as income derived by them. He cannot trace the balance of £102,414 actually into their hands. It remained in the pocket of Pactolus Limited. It was ostensibly the profit of Pactolus on buying the shares. But when the transfer is ignored, that profit is seen to be nothing more nor less than remuneration which the original shareholders allowed Pactolus to retain for services rendered. The position is the same as if the shareholders had received it as part of the special dividend and then returned it to Pactolus as remuneration. The commissioner can

therefore treat this £102,414 also as income derived by the shareholders".

96. Since the decision in Newton's case (supra) section 260 has been discussed by the Full Court of the High Court of Australia in Hancock v. Federal Commissioner of Taxation 108 C.L.R. 258, Rowdell Pty. Limited v. Federal Commissioner of Taxation 111 C.L.R. 106 and Cecil Bros. Pty. Limited v. Federal Commissioner of Taxation 111 C.L.R. 430.

97. In Hancock's case (supra) members of the Lefroy and Hancock families held all the shares in Mulga Downs Pty. Limited. This pastoral company had accumulated large profits which, if distributed as dividends, would attract income tax in the hands of the shareholders, and which, if not distributed, would be subject to undistributed profits tax. All the shares were acquired by Rowdell Pty. Limited, a company which dealt in shares, which agreed to pay £40,000 for the Lefroys' shares and £23,500 for the Hancocks' shares. Rowdell Pty. Limited then received a dividend of £50,000 on the shares and, pursuant to an arrangement which has been made prior to the purchase of the shares, sold all the shares to the Hancocks for £21,000. Fullagar, J. held that there was an arrangement within section 260, that the transfers of shares by the Hancocks to Rowdell Pty. Limited were avoided, and that the Commissioner of Taxation was entitled to assess the Hancocks to income tax on the sum of £21,000. On appeal to the Full Court of the High Court it was held that there was an arrangement within section 260 and further (by Dixon, C.J., Kitto and Windeyer, JJ., Menzies, J. dissenting) that the Commissioner was entitled to assess the Hancocks on the dividends attributable to the shares originally held by them.

Fullagar, J. said at p.274:-

"But we have to treat as void the arrangement which involved the transfer of the Hancock shares to Rowdell and the payment to Rowdell of the dividend on those shares. When we eliminate that arrangement from consideration, there is left only a payment of a sum of money by Mulga Downs and a receipt of that sum by the Hancocks. And, since the payment by Mulga Downs was a payment out of the profits of that company to persons who must be treated as shareholders, that payment is income in the hands of the Hancocks."

Dixon, C.J. said at p.278:-

"In these circumstances I think that there was an agreement or arrangement to avoid either a liability imposed by the Act on Mulga Downs Pty. Ltd. or upon the Hancocks

and to prevent the operation of the Act in respect of the liberation of the company's profits. The liability imposed by the Act on Mulga Downs Pty. Ltd. was to pay tax under Div. 7 if there was not a sufficient distribution of income to satisfy s. 104. It may be said that the company did on any view distribute a sufficient amount of income and that is why liability under Div. 7 was avoided. In the end if you treat the distribution as valid, that is so. But if you look at the matter as at the time the arrangement was made, the parties were confronted with a dilemma, a liability under Div. 7 or a liability under or by reason of section 44 (Div. 2 sub-div. D) and a purpose of the plan evolved was to avoid the dilemma. The expression "preventing the operation of the Act in any respect" is generally regarded as difficult, but I treat it as simply meaning the operation which the Act would have in a given case if it were not for the contract agreement or arrangement made for the purpose (or having the effect) of preventing it. It is the operation of the Act in relation to the distribution and taxability of the profits of a private company that in part the plan was designed to 'prevent'".

and at p.281-2:-

"The view I have expressed depends in no respect upon tracing the identity of moneys employed in the steps taken to reach the result. When the purpose is to assess a taxpayer who has reached a situation which but for a scheme swept away by s.260 would or might spell liability to tax, it does not appear to me to be necessary to trace the identity of moneys as if one were seeking to identify in an investment trust funds that had been misapplied. Section 260 is directed against the validity of arrangements designed to avoid taxation where, but for the cover the arrangement would give, taxation would fall. The resource of ingenious minds to avoid revenue laws has always proved inexhaustible and for that reason it is neither possible nor safe to say in advance what must be found, after a scheme is struck down under s.260, before a consequential assessment can be justified. But it seems to me that what matters must be the resulting financial situation, one of change if not invariably of betterment, and the factors which would but for the void scheme have made it taxable. These factors will depend on general conceptions of what is taxable as income, but seldom, I should have thought, would the actual tracing of moneys be the test of that liability. For example, when Watson's company actually bought and paid for the Lefroy shares, to finance the payment it was necessary to use the proceeds of bonds which the company had 'bought on credit' from Mulga Downs Pty. Ltd. for the

purpose and resold for cash, and also to depend to some extent upon some moneys belonging to Watson's company. That does not seem to me to matter. It was all balanced out afterwards, of course, and was only part of the financial expedients for carrying that part of the plan through. It does not seem to me to matter at all what interim financial expedients were resorted to or which moneys or whose credit was used in the course of carrying out the transaction. It is the result that exposes the taxpayer to liability; a result necessarily involving the employment by the taxpayer of a distribution of the profit fund. The means, if otherwise they could be considered significant upon a question of ultimate liability, would be swept away like other parts of the 'arrangement' and the steps by which it was carried into effect. In the present case the only difficulty, as it seems to me, lies in the form in which the Appellant George Hancock derived in the end the greater part of benefit of the transaction, namely shares, the Lefroy shares. But for the reasons that I have given that should not be regarded as inconsistent with his having derived income, once the disguising elements of the 'arrangement' are stripped away under s.260'".

Kitto, J. said at p.282:-

"The notorious difficulties of the section have been the subject of a line of cases culminating in Newton v. Federal Commissioner of Taxation. From what is said and implied in the reasons of the Privy Council in that case it is possible, I think, to work out some general propositions by reference to which the present case may be decided. (1) The word 'arrangement' in s.260 comprehends a plan made between two or more persons (whether it be legally enforceable or not) and all the transactions by which it is carried into effect. (2) An arrangement 'has or purports to have the purpose or effect' referred to in the section if, and only if, the concerted action consisting of the making of the plan and the carrying out of the transactions by which it is given effect is properly to be characterized as a means to avoid income tax. (3) Whether it is to be so characterized is a question to be answered upon consideration of the overt acts by which the plan has been implemented. (4) If those acts are capable of explanation by reference to ordinary dealing, such as business or family dealing, without necessarily being labelled as a means to avoid tax, the arrangement does not come within the section. An example would be a simple sale or gift of shares, even though the motive of the seller or donor may have been to avoid receiving future dividends and incurring the liability to income tax which the receipt

of them would have entailed. (5) But the overt acts will enable the arrangement to be characterized as a means for the avoidance of tax, if they have included a transfer of property from the taxpayer in consequence of which income from the property, instead of being received as such by the taxpayer, has followed either of two courses: (i) a course which has carried it through the hands of other persons to the taxpayer, but so as to reach him with the character of capital; or (ii) a course which has amounted in effect to an application of the moneys by the taxpayer, and so has been a practical equivalent of a receipt by him followed by an expenditure by him. (6) If an arrangement has been a means for the avoidance of tax, the fact (if it be a fact) that it has been a means to other ends as well does not prevent the application of s.260. (7) Where an arrangement is found to be within the section because of a transfer having such a consequence as is mentioned in (5) above, the transfer is to be considered as void to the extent mentioned in the section. The result is that income which has followed either of the courses referred to in (5) is to be regarded as income to which the taxpayer was entitled. Consequently the receipt of the income by the transferee in pursuance of the arrangement is properly to be treated by the Commissioner as a derivation of it, as income, by the taxpayer".

and at p.292:-

"The consequence which s.260 produces is that the transfers of the 7,728 shares to Rowdell are to be treated as void, and Rowdell's receipt of the dividend moneys in respect of those shares is to be considered a receipt of the Hancocks' moneys by arrangement with them, and therefore as a derivation of those moneys by the Hancocks, with the character of company distributions still upon them."

98. The decision in Rowdell's case (supra) has been referred to in paragraph 84 hereof.

99. In Cecil Bros.' case (supra) a family company which carried on a retail shoe business purchased some of its stocks from another family company at a higher price than it could have purchased them from wholesalers. The company claimed the amount which it had paid for stock as an allowable deduction under Section 51 of the Act, but the Commissioner disallowed so much of the deduction as represented the excess price paid to the other family company. It was held by the Full Court of the High Court that assuming that section 260 can operate to extinguish a deduction otherwise allowable under section 51 and assuming that there was an arrangement between the two companies which fell within section 260, that

section did not authorise the Commissioner of Taxation to disregard part of the price actually paid for goods pursuant to contracts the validity of which was unaffected.

100. The Respondent submits that Hancock's case was rightly decided and that the Full Court of the High Court in the present case correctly applied the principles there laid down. The Respondent submits that in Rowdell's case and Cecil Bros.' case the Full Court of the High Court was concerned with different aspects of the application of section 260 from those with which this appeal is concerned but that, in any event, the decisions in those cases do not involve any departure from the principles of Newton's case and Hancock's case.

101. Assessments to income tax were upheld on the basis of the application of section 260 by Menzies, J. in Mayfield v. Commissioner of Taxation 108 C.L.R. 303 and Mayfield v. Commissioner of Taxation (No.2) 108 C.L.R. 323, and by Taylor, J. in Millard v. Commissioner of Taxation 108 C.L.R. 336.

102. In Mayfield v. Commissioner of Taxation 108 C.L.R. 303 the facts were that members of the Mayfield family were the only shareholders in Mayfield Investments Limited, an investment company, and were, with Mayfield Investments Limited the only shareholders in F.R. Mayfield Limited, a trading company. The latter company had substantial accumulated and accumulating profits which, if not sufficiently distributed, would shortly attract undistributed profits tax and which if distributed to the members of the family would attract income tax in their hands. The members of the family agreed to sell their shares in the investment company to purchasers found by their financial adviser at a price equivalent to the net asset value of the shares less an agreed profit to the purchasers. It was a condition of the agreement for sale that the investment company should have disposed of its shares in the trading company to a new family-owned company and it was also a condition that the trading company should have declared and paid such dividends as it could. On 17th November, 1950 the new family-owned company was incorporated. On 23rd November, 1950 the trading company declared dividends of all its profits available for distribution of which £12,280 was paid to the investment company. On the same day the investment company resolved to sell its shares in the trading company to the new company. The Mayfield family then sold all their shares in the investment company to the purchasers found by the financial adviser, who paid an initial deposit of £1,475. On 30th November, 1950 dividends of £11,600 were declared by the investment company and these (save £1,600 used to pay remaining unpaid calls on shares in the company) were paid to the purchasers. The

purchasers then paid a further £7,500 to the Mayfields in respect of the purchase of the shares. The purchasers borrowed moneys from the investment company in order to pay the balance of the purchase price and repaid these moneys when the company was subsequently wound up and the liquidator made a distribution of £32,196. The sum of £32,196 represented return of capital, £14,500, capital profits on sale of shares, £17,398, and ordinary profits £298.

103. Menzies, J. held that there was an arrangement to which the Mayfield family were parties having the purpose and effect of avoiding the liability to tax of the companies and the family. The transfer of the family's shares was the essential step in the avoidance of liability and was void as against the Commissioner. The family were liable to tax as though shareholders of the investment company until its dissolution. His Honour held that the whole of the distribution of £11,600, and £298 out of the distribution of £32,196, must be regarded as taxable income of the Mayfields. Menzies, J. said, at p.321:-

"There are therefore two amounts about which I have to make up my mind - the first, that part of the dividend of £11,600 which I find did not reach the Mayfields (i.e. £2,625); the second, the £298 distributed by the liquidator out of profits, which again, in my opinion, did not reach the Mayfields. (The sum of £2,625 to which I have just referred is made up of the £1,600 devoted to the paying up of unpaid shares and £1,025 retained by Argo, Dunfermline and the Provident Fund out of dividends paid to them). The question whether these sums are taxable is one that has occasioned me some difficulty but I have reached the conclusion that the decision of the Court in Hancock v. Federal Commissioner of Taxation ((1961) 108 C.L.R. 258) requires the conclusion that these are to be regarded as income of the Mayfields notwithstanding that they did not receive them. The reasoning of the Chief Justice, with whom Windeyer, J. concurred, is not identical with that of Kitto, J. and both differ from that of Fullagar, J., whose judgment was affirmed, but in this case, as in that, whichever line of reasoning is followed it leads to the conclusion that the taxpayers, being entitled to dividends, disposed of them by an arrangement to avoid taxation that the Commissioner is bound to disregard, and because the dividends here were paid as they were by reason of what the taxpayers, as the persons entitled to them, did they were income derived by them. As shareholders the Mayfields were entitled to all dividends, and the dividends were paid as they were by virtue of what the Mayfields themselves did to avoid taxation."

104. In Mayfield v. Commissioner of Taxation (No.2) 108 C.L.R. 323 a trading company had accumulated substantial profits which if not distributed would attract undistributed profits tax and which if distributed would attract tax in the hands of the shareholders, who were its manager, members of the Mayfield family and Eynesbury Ltd. (an investment company in which the only shareholders were members of the Mayfield family). On the advice of the family's financial adviser the business of the trading company was sold to a newly incorporated trading company controlled by the family. The shareholders in the old trading company then sold all their shares in that company to purchasers found by the financial adviser for £56,900, a price equal to the net asset value of the shares less an agreed profit of approximately £5,000 to the purchasers. At about the same time Eynesbury Ltd. and the manager of the old trading company took up shares in the new trading company, paying a sum substantially equivalent to the sum they had received for the sale of their shares. Also at about the same time the old trading company declared dividends of £48,000 and £1,200.

105. Menzies, J. held that there was an agreement to avoid tax liability on distributions to be made by the old trading company and that section 260 of the Income Tax and Social Services Contribution Assessment Act 1936-1953 applied to the arrangement so as to avoid the transfers of the shares; therefore the former shareholders must be regarded as having remained shareholders and as having received the dividends which in the event were received by the purchasers, not merely to the extent to which the payments received from the purchasers had their source in the dividends but also to the full extent to which but for the arrangement they would have received dividends that were, in accordance with the arrangement, diverted to the purchasers. Accordingly his Honour held that the dividends of £48,000 and £1,200 were, for the assessment of tax, the income of the former shareholders proportionately to their shareholdings immediately prior to the transfers. It was also held that the share of Eynesbury Limited in the dividends was to be taken into account as income in determining whether that company had made a sufficient distribution.

106. In Millard v. Commissioner of Taxation (108 C.L.R. 336) the taxpayer, who was a registered bookmaker under the Bookmakers' Act 1953 of Victoria, had entered into an agreement with a private company whereby it was provided, inter alia, that as from the date thereof the company should take over from the taxpayer and carry on the bookmaking business on its own behalf and that as from the same

date the taxpayer should carry on all bookmaking activities hitherto carried on by him on his own behalf for and on behalf of the company and as its agent. The company bound itself to pay the taxpayer a fixed sum at an annual rate during the continuance of the agreement. All the shares in the company were owned by the taxpayer, his wife and children. At all material times after the date of the agreement the taxpayer used only the company's money in the course of his bookmaking activities and paid all the profits thereof into the company's banking account. The Commissioner of Taxation assessed the taxpayer for the year of income ended 30th June, 1958 upon a taxable income which included the amount shown in the taxpayer's return and a net amount calculated by reference to the sums paid by the taxpayer into the company's account during the year of income.

107. Taylor, J. held that the assessment was justified by the operation of section 260 of the Income Tax and Social Services Contribution Assessment Act 1936-1958 and said, at p.342:-

> "To my mind it is about as plain as it could be that the whole purpose and effect of the agreement was to split the Appellant's income into a number of parts in order to minimize the amount of tax which would become payable. Any other effect of the agreement was entirely subsidiary to this. With the recent cases of Hancock v. Federal Commissioner of Taxation (108 C.L.R. 258) and Mayfield v. Commissioner of Taxation (108 C.L.R. 303,323) in mind I find it unnecessary to enter upon any discussion concerning the ambit of the section for in the present case the whole of the amount in question was received by the Appellant, it was the return from his own bookmaking activities and the provision made by the agreement for the subsequent disposition of the resultant profit was quite clearly merely for the purpose of avoiding taxation. That being so the appeal should in my opinion be dismissed."

108. The Respondent submits that the Mayfield cases and Millard's case were rightly decided and that the decisions support the application of section 260 in the present case.

JUDGMENT OF MENZIES, J.

109. Menzies, J. substantially upheld the correctness of the assessments in question as being justified by the application of section 260. His reasoning is summarized as follows :-

RECORD

Vol.1. p.162 (a) When all the transactions are looked at and in particular when the role of Raleigh is examined there is a strong prima facie case that what was done was done to obtain increased tax deductions from assessable income and to divide what would otherwise have been the Appellant's taxable income between himself, his wife and his children.

Vol.1. pp. 162-163. (b) An arrangement made whereby medical practitioners entitled to sue for their fees transferred their practices to a company which could not sue for fees and became that company's servants is not explicable by reference to ordinary business or family dealing.

Vol.1. pp. 165-166. (c) Neither in the language of section 260 nor in the authorities is there to be found any limitation of its application to income derived from sources of income already in existence. The steps taken in 1956 by the Appellant and the other doctors were taken to get out of the way of taxation which was in prospect if they were to continue their professional practice in partnership, and this amounted to avoiding a liability within the test propounded in Newton's case.

Vol.1. p.166 (d) Section 260 therefore applies.

Vol.1. p.166, ll.15-22 (e) The making of the agreements with Westbank and the making of the Appellant's agreement with Raleigh effectuated the tax avoiding purpose with regard to the Appellant and the agreements must therefore be disregarded.

Vol.1. p.166, ll.23-33. (f) What is left is a group of doctors practising together without any formal agreement of partnership, using Westbank to receive all fees paid, to provide services for the group, to pay group expenses and to make distributions of what remained in agreed proportions and using their family companies to receive those distributions and to pay the individual expenses of practice. On this basis, the assessable income of the doctors as a group was the total of the gross fees earned.

Vol.1. pp. 167-169. (g) Subject to the allowance of an additional deduction in respect of contributions to the Superannuation Fund for the benefit of receptionist-secretaries and to recalculation of the exact percentage of Westbank's receipts to which the Appellant was entitled, the assessments were correctly made.

110. McTiernan, J. said that he agreed with the judgment and reasons of Kitto, J. Vol.1. p.185

111. The reasoning of Kitto, J. was as follows: Vol.1. p.190

(a) The plan adopted by the doctors and all that was done under it constituted an 'arrangement' in the sense in which that word is used in section 260.

(b) When the arrangement is considered objectively, as is required by section 260, there is evident a purpose of diverting income away from the doctors to or for the benefit of their families to the end that a substantial part of the tax might be avoided which would have been incurred if the income had first been derived by the doctors and applied by them for the benefit of their families. Vol.1. p.191

(c) Section 260 therefore applies to the arrangement.

(d) Section 260 must be given full operation according to its terms and its operation is not limited to arrangements which avoid tax by converting what would have been a derivation of income into a derivation of capital. Vol.1. p.192

(e) Section 260 operates only to destroy, but if a statutory denial of any of the legal consequences of the steps taken in carrying a concerted plan into effect will suffice to defeat a tax avoidance for which the arrangement is a recognisable means the section supplies the denial and enables an assessment to be made in disregard of those legal consequences. Vol.1. p.192

(f) The Respondent took the view that by the operation of section 260 he could ignore the existence of Westbank, the contracts of doctors and patients with Westbank, and the position of the doctors as directors of Westbank, and that what was left was an association of doctors receiving income jointly and agreeing that the amount that they considered available should be divided, each doctor's share being paid to his family company. This was the view taken also by the primary judge and is, in the opinion of his Honour Mr. Justice Kitto, correct. Vol.1. pp. 193-194.

(g) What remains after the application of section 260 is income produced by an association of doctors, received by them jointly, and divided in agreed proportions and dealt with as directed. It follows that each doctor must be Vol.1. p.195

considered to have derived his proportion of the income, and it is not necessary nor would section 260 authorise it, to construct notional contracts between doctors and patients.

112. The reasoning of Taylor, J. was as follows :-

Vol.1. p.201 (a) It is clear on the facts that there was an arrangement which had the effect or was calculated to have the effect, of avoiding the liability of the Appellant to tax on a specified share of profits earned by him in co-operation with a number of other medical practitioners, but leaving him free to dispose of that share for the benefit of himself and his wife and children.

Vol.1. p.202 (b) There is nothing in section 260 by which its application is limited to an arrangement concerned with a fund already in existence.

Vol.1. p.203 (c) The arrangement was not capable of explanation by reference to ordinary business or family dealing because the avoidance of tax was not incidental to but was the heart of the arrangement.

Vol.1. pp. 203-205 (d) In dealing with an argument on behalf of the Appellant that no part of the profits could be found in his hands and that therefore it could not be said, after applying section 260, that the Appellant had derived the income, his Honour pointed to variations in the percentages of the service fees paid to Raleigh as evidencing agreement from time to time between the doctors as to how the profits should be shared among the family companies.

Vol.1. p.205 (e) His Honour agreed with Menzies, J. that when the agreements between the Appellant and Raleigh and between those parties and Westbank are treated as void what is left exposed is a receipt of moneys by Westbank on account of the medical practitioners and that the Appellant can be said within the meaning of section 19 to have derived a share of that income.

113. The reasoning of Windeyer, J. was as follows :-

Vol.1. p.206 (a) The fact that the arrangement had advantages other than the avoidance of tax did not take it outside the operation of section 260.

Vol.1. p.209 (b) The arrangement could not be regarded as an ordinary business arrangement particularly in the light of the constitution of Raleigh, its purchase of

the Appellant's practice, the fact that the Appellant became both servant and governing director of Raleigh, the hiring of the Appellant to Westbank and the employment by Raleigh of the Appellant's wife. Upon examination the role of Raleigh was to receive from Westbank the fruits of the Appellant's practice of his profession and to deal with them as he directed. Vol.1. p.211

(c) Consideration of the arrangement as a whole discloses that it was within section 260. Vol.1. p.212

(d) His Honour said that he was in agreement with the judgments of Kitto and Taylor JJ. on other matters raised in argument. Vol.1. p.212

114. Owen, J. said that he agreed with the reasons of Kitto, J. Vol.1. p.213

SUBMISSION:

115. The Respondent submits that the appeals should be dismissed.

R E A S O N S

(1) That an arrangement was come to between the Appellant and others having a purpose or effect of avoiding the liability imposed by section 17 of the Act upon the Appellant of paying income tax and social services contribution at the rates declared by Parliament upon the taxable income derived by the Appellant.

(2) That alternatively to (1) above, an arrangement was come to between the Appellant and others having a purpose or effect of preventing the operation of section 17 upon the taxable income of the Appellant.

(3) That alternatively to (1) and (2) above, an arrangement was come to between the Appellant and others having a purpose or effect of altering the incidence of tax.

(4) That the facts exposed after stripping away so much of the arrangement as avoided a liability imposed by or prevented the operation of the Act, or altered the incidence of tax attracted section 17 and section 19 of the Act.

(5) That the decisions of Menzies, J. and of the Full Court of the High Court of Australia were correct.

RE-ASSESSMENT:

116. The Respondent requests that in the event of the Board holding that the assessments the subject of the appeal are not

REASONS

justified by the operation of section 260 the Board will advise Her Majesty to remit the assessments back to the Commissioner for re-consideration.

M.H. BYERS.

J. GIBSON.

No. 29 of 1965

IN THE PRIVY COUNCIL

ON APPEAL

FROM THE HIGH COURT OF AUSTRALIA

BETWEEN:

DESMOND LEES PEATE Appellant

AND

THE COMMISSIONER OF TAXATION OF THE COMMONWEALTH OF AUSTRALIA Respondent

---

CASE FOR THE RESPONDENT

COWARD, CHANCE & CO.,
St. Swithin's House,
Walbrook,
London, E.C.4.

Solicitors for the Respondent.