IN THE HIGH COURT OF AUSTRALIA
BRISBANE REGISTRY

NO B 60 OF 2017

THE COMMISSIONER OF TAXATION OF THE COMMONWEALTH OF AUSTRALIA

Appellant

MARTIN ANDREW THOMAS

Respondent

APPELLANT'S SUBMISSIONS IN REPLY

Filed on behalf of the Appellant: The Commissioner of Taxation of the Commonwealth of Australia

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Part I: Certification

1. The submissions are in a form suitable for publication on the Internet.[1]

Part II: Argument

2. **Ultimate issue**. The ultimate issue remains, as the Commissioner indicated at the outset of his submissions in Thomas Primary Tax,[2] whether the Full Court erred in finding that it was bound by *Executor Trustee* to conclude that paragraph 1(b)(iii) of the Declaration made by the Queensland Supreme Court determined conclusively as against the Commissioner the existence of the alleged rights referred to in the Declaration.

3. **Respondent's issues**. Accordingly, only Issues 2 and 4, identified at RS B60 [3(b)] and [3(d)], engage with the dispositive questions in these appeals. Nothing in Mr Thomas's submissions on Issues 2 and 4 identifies a satisfactory basis upon which a decision by one court which depends for its correctness or purported efficacy upon a construction of the tax acts can create a taxable fact binding the Commissioner or a later Court. The Commissioner refers to:

   (a) AS B60 [53]-[60], addressing the Assessment, Objection and Appeal Process of the Tax Legislation;

   (b) AS B60 [63]-[84], addressing the State Court Proceedings, Declarations, and *Executor Trustee* itself.[3]

   The balance of the matters raised by Issues 2 and 4 relate to s 118 of the Constitution and s 185 of the *Evidence Act 1995* (Cth). The Commissioner apprehends that these matters will be dealt with by the Commonwealth Attorney-General, who has given notice of the Commonwealth's intention to intervene in these proceedings.

4. Assuming the Commissioner to be correct in his identification of the ultimate issue, the remaining taxation issues raised by Mr Thomas should be dealt with as follows.

5. **Relevance of Bifurcation Assumption**. The Respondents' income tax returns,[4] their

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[1] Capitalised terms used in these reply submissions are as defined in the Commissioner's principal submissions of 24 November 2017 filed in this appeal.

[2] For convenience, the submissions of the Commissioner and Mr Thomas in B60 are treated as the principal submissions and referred to as **AS B60** and **RS B60** respectively. References to MAPL Primary Tax are denoted by B61, to the 2009 Year by B62 and to Thomas Penalty by B63, where AS refers to the Commissioner's submissions and RS refers to the Respondent's submissions.

[3] See also: Originating application in the Queensland Supreme Court proceeding 9167/2010 (24 August 2010); written submissions; transcript of hearing (29 September 2010); and orders and reasons for judgment of Applegarth J.

[4] Summarised in the Commissioner's submissions at AS B60 [15].

argument before and the decision of Applegarth J,[5] and their argument before Greenwood J[6] all reflected the Bifurcation Assumption. The Respondents contended that Div 207 enabled them to place the franking credits in the hands of one Beneficiary for tax purposes, and the corresponding franked distributions in the hand of the other Beneficiary. This contention was reflected in the finding by Greenwood J at FCA [519] (emphasis added):

> *What cannot occur if the tax offset is to be preserved and available in conformity with the tax legislation is an allocation of the s95 net income amongst beneficiaries on a particular basis and a distribution of the franking credits otherwise attached or stapled to the franked dividends on an entirely unrelated basis, amongst the same beneficiaries. That is what occurred in each income year in this case ...*

6. The form of "streaming" to which Mr Thomas refers in RS B60 [5] is a different concept and involves allocating some of the franked dividend income of the Trust to one Beneficiary and the balance to the other.

7. **Issue 1 (No allocation of franked dividends).** There was *no* "streaming" or allocation of the *franked dividend income* of the Trust by Thomas Nominees. As Greenwood J found:[7]

> *There can be no doubt that the trustee failed to directly allocate the franked dividends themselves. They simply were not streamed as contemplated by the trust deed. The clear intention was to allocate the benefits by reference to the franking credits. At no point did the trustee seek or intend, by the franking credit distribution resolutions, to distribute, notionally or otherwise, the franked dividends, that is, the franked distributions to the trust.*

8. Certain consequences flow from that finding:

(a) the Franking Credit Resolutions were inoperative because, as Pagone J correctly observed,[8] they could not distribute to either Beneficiary any amount or share of the Trust's income covered by s 97(1)(a) of the 1936 Act if that income had been distributed by the Net Income Resolutions;

(b) the Net Income Resolutions and the Franking Credit Resolutions are therefore not capable of treatment as one instrument, whether they are now sought to be characterised by Mr Thomas as "twin" resolutions or otherwise (Mr Thomas has not, by notice of contention or otherwise, sought to have them treated in that way);

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[5] *Thomas Nominees Pty Ltd v Thomas* [2010] QSC 417 at [44].
[6] The relevant arguments, as articulated in the Respondents' appeal statements, are summarised in the Commissioner's reply submissions in B63 (Penalties) at [3].
[7] FCA [496]. The finding was not challenged on appeal by any of the Respondents.
[8] FCAFC [22].

(c) each Beneficiary had an interest in the dividend income of the Trust,[9] such that s 207-50(3) gave effect, by force of statute, to an indirect flow to each of them of franked distributions;

(d) specifically, Div 207 operated to treat the Beneficiaries as having a share of the franked distributions in proportion to each Beneficiary's respective share of the s 95 income of the Trust as was specified in the Net Income Resolutions, which purported to distribute all of that income; and

(e) it is irrelevant for the purposes of this appeal that had the franked distributions been streamed, Div 207 might have operated such as to result in franking credits being allocated in proportions different from the Trustee's sharing of the distributable income of the Trust. It is irrelevant because it was found that there had been no streaming by the Trustee of franked distributions.[10]

9. **No allocation of trust expenses.** It is also irrelevant for the purposes of this appeal that, had Trust expenses been allocated differentially between the Beneficiaries, a particular Beneficiary might have become entitled to receive an amount which was less than the amount of the franked distributions received by the Trustee, but remain entitled to the entirety of the franking credits associated with those franked distributions:[11] Greenwood J found that there had been no allocation by the Trustee of expenses differentially among separate categories of income.[12]

10. **Issue 3,** identified at RS B60 [3(c)], and a corollary of Issue 1, essentially asks whether the Resolutions may be construed so as to achieve streaming of franked dividend income by a process of reverse engineering from the amount of franking credits purportedly distributed. In response, the Commissioner refers to his principal submissions at AS B60 [43]-[52]; AS

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[9] To adopt the language of the Explanatory Memorandum to the *New Business Tax System (Imputation) Bill 2002*, paragraphs 5.36 and 5.37.

[10] FCA [496]. As Greenwood J observed at FCA [516], the Trustee allocated franking credits as if they were a floating pool of offsets, related to franked dividends but entirely independent of the shares of s 95 net income of the Trust, on the footing that they could be claimed by a corporate beneficiary *simpliciter* and by a natural beneficiary so as to enjoy a refund of excess offsets. However, as Greenwood J also observed, the Franking Credit Resolutions did not operate as a proxy distribution of the franked dividends, rather as a proxy distribution of those *offset entitlements*, as if they could be allocated free of the distribution of franked dividends.

[11] The statements of principle at RS B60 [12(a)-(c)], [20] and [25] are not controversial. Although the Commissioner apprehends that Mr Thomas has at RS B60 [22] of his submissions misinterpreted the Commissioner's principal submissions at AS B60 [40]-[41], in that the Commissioner does not suggest that the inclusion of a franking credit in assessable income does not necessarily result in an equal amount of the franking credit being identifiable in a beneficiary's net income required to be returned, nothing turns on this.

[12] FCA [496]. The finding was not challenged on appeal by any of the Respondents.

B61 [12], and AS B62 [9]-[17].

11. **Residual issues 5 to 8 are not apt for consideration in this appeal.** These appeals are not the occasion for a rehearing of the appeal to Greenwood J or to the Full Federal Court. None of these issues is apt for determination by this Court: each entails consideration of evidence and questions of fact and ought be dealt with on any remitter of these appeals to the Full Federal Court.

12. **Short response to Issues 5 to 8.** For the reasons set out in AS B60 [40]-[44] of the Commissioner's submissions, each Beneficiary's entitlement to *franking credits* arose only because a portion of the franked distributions "was taken into account in working out" each Beneficiary's share of the income of the Trust distributed *pro rata* that share.[13] To the extent that the entitlement for which Mr Thomas contends is inconsistent with Div 207, no such entitlement arose under the general law of trusts or pursuant to the Trust Deed. If they are to be dealt with, each of Issues 5 to 8 should be answered in the negative:

(a) **Issue 5.** An estoppel by convention may affect the rights of parties acting so as to create obligations between them. It does not permit parties to create a private arrangement to produce an outcome otherwise contrary to law, alter the effect of legislation or oust the statutory procedure for the determination of tax liabilities.[14] Mr Thomas's submission on this question was correctly rejected by Greenwood J for the reasons he gave;[15]

(b) **Issue 6.** As noted in the Commissioner's submissions at AS B60 [87], the Trustee's rectification case was dismissed. The Part IVC process was engaged on the basis of the Resolutions as they stood. The "true" intention of the Trustee is described by Mr Thomas not in terms of some mistake in what the Resolutions were actually intended to say but in terms of a result the Trustee sought to achieve.[16] Rectification required the Trustee to identify the language it claimed the Resolution ought to have been expressed in and how it ought to have been rewritten.[17] To rectify the Resolutions such that franked distributions were allocated to each Beneficiary by reference to the dollar amount mentioned in each Franking Credit Resolution would:

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[13] Mr Thomas has misinterpreted the Commissioner's principal submissions at AS B60 [40(a)]: the Commissioner contends that Part IVC was enlivened upon the making of the Deemed Assessments.
[14] Moreover, the estoppel by convention contended for in *Fischer v Nemeske* (2016) CLR 647 was said to have been created in connection with a bilateral agreement for a charge.
[15] FCA [525].
[16] RS B60 [62] and [64].
[17] See, e.g., *Maralinga Pty Ltd v Major Enterprises Pty Lt* (1973) 128 CLR 336 at 350.

(i) contradict Greenwood J's unchallenged findings concerning the Trustee's intention at FCA [488]-[490], and ignore the evidence of Beth Abbott, who drafted the Resolutions, summarised at FCA [482];

(ii) not be open as a matter of the construction of the resolutions since, as Pagone J observed, the "resolutions themselves do not reveal whether the two resolutions independently achieved that outcome [intended by their drafter]";[18] and

(iii) ignore the operation of Div 207 upon the Resolutions;[19]

(c) As to **Issue 7**, there was no operative denial of procedural fairness by Greenwood J. The only area where it is suggested that he did not hear submissions from the parties was at the very final step of his analysis.[20] By their appeals the parties placed the substantive question before the Full Federal Court, thus the matter turns on that question; and

(d) **Issue 8** is dealt with in the Commissioner's reply in the 2009 Year proceeding.

13. **Disposition of this appeal.** For the reasons set out in the Commissioner's submissions at AS B60 [43]-[48], s 207-55(3) and s 207-50(3)(b)(i) notionally allocated franked distributions between Mr Thomas and MAPL in the proportions 2.7 to 97.3. Greenwood J's analysis of Div 207 was correct.[21]

14. But for that final error, Mr Thomas' share of the franked distributions corresponds to his share of the s 95 income of the Trust.

15. If the Commissioner succeeds on grounds at [2] or [3] of each of his Notices of Appeal, the matter ought be remitted to the Full Federal Court.

Dated: 25 January 2018

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[18] FCAFC [21].

[19] According to which, as Pagone J found, "*the franking credits available in the 2006 year to each of Mr Thomas and MAPL, on that view, for example, would be that proportion of the total franking credits received as corresponds to their respective proportions of the amounts distributed to them by the net income distribution*": FCAFC [22].

[20] Reflected in his findings at FCA [515] and FCA [520].

[21] The only issue with Greenwood J's analysis was in respect of his interpretation and application of the expression of the phrase "taken into account in working out" in the table following s 207-55(3). Greenwood J's conclusion that none of the franked distributions was taken into account in working out each Beneficiary's share of the s 95 net income of the Trust entailed a misconstruction of that particular provision of Div 207 and led him erroneously to conclude that Mr Thomas failed to discharge his onus under s 14ZZO of the TAA.