

*Privy Council Appeal No. 3 of 1970*

**Owen Thomas Mangin** - - - - - *Appellant*

v.

**The Commissioner of Inland Revenue** - - - - - *Respondent*

FROM

**THE COURT OF APPEAL OF NEW ZEALAND**

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JUDGMENT OF THE LORDS OF THE JUDICIAL COMMITTEE OF  
THE PRIVY COUNCIL, DELIVERED THE 21ST OCTOBER 1970

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*Present at the Hearing:*

LORD DONOVAN  
VISCOUNT DILHORNE  
LORD WILBERFORCE  
LORD PEARSON  
SIR FRANK KITTO

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*(Majority Judgment delivered by LORD DONOVAN)*

The appellant, a farmer in New Zealand, desired to reduce his burden of income tax. After seeking the advice of his accountant and solicitor he created what is called a "paddock trust".

This involved his leasing in 1965 25 acres of his farm of 385 acres to trustees. These 25 acres were sown with wheat. The trustees were to hold the land for one year at a rent of £3 per acre and were to cultivate it. Under a separate trust deed any resulting income was to be held on trust for the appellant's wife and children.

The appellant himself, as the employee of the trustees, harvested and sold the ensuing wheat crop and accounted to the trustees for the proceeds. The trustees paid him for his labour and certain expenses he had incurred. They then distributed the bulk of the net income so remaining in their hands to the appellant's wife, partly for herself and partly for the benefit of his children.

In 1966 a similar transaction took place in relation to another 24 acres which were ready to be sown with wheat. These were leased to the trustees at £4 an acre. The appellant again sowed and reaped the crop as employee of the trustees, and again sold it and accounted to the trustees for the proceeds. They reimbursed him as before for his labour and expenses. Once more the bulk of the net income so accruing to the trustees was distributed by them under the still existing trust deed for the benefit of the appellant's wife and children.

By these transactions part of what would have been the appellant's total income from his farm was hived off and became (via the trustees) the income of his wife and children. This meant that each of the beneficiaries could claim allowances and reduced rates of tax. Thus the appellant mitigated what would otherwise have been his burden of tax. The "spreading of the liability" led to less tax being paid on the profits of the whole 385 acres.

The respondent made amended assessments on the appellant for the years ending 31st March 1966 and 1967 with the object of restoring the appellant's income tax liability to what it would have been for these years but for these "paddock trusts". Against these amended assessments the appellant appealed to the Supreme Court in New Zealand and won. In the Court of Appeal, however, he lost; and now appeals to this Board.

The respondent justified the amended assessments in terms of section 108 of the Land and Income Tax Act 1954 ("the 1954 Act"). This reads:

"Every contract, agreement, or arrangement made or entered into, whether before or after the commencement of this Act, shall be absolutely void in so far as, directly or indirectly, it has or purports to have the purpose or effect of in any way altering the incidence of income tax, or relieving any person from his liability to pay income tax."

If this section has the effect contended for by the respondent then the "paddock trusts" must be considered as non-existent. The appellant concedes that in that event the amended assessments would stand because he received the disputed income into his own hands and would be unable to contend that it belonged to trustees. The "annihilating effect" of section 108 does not, in other words, here produce the kind of difficult problem which arose in *Peate v. Commissioner of Taxation* [1967] A.C. 308 and which led to a dissenting judgment on the Board in that case.

The appellant contends, however, that section 108 has no effect in this case for the following reasons:

First, because it has no fiscal effect but operates only as between the parties to the contract, agreement or arrangement.

Second, because if the section does have fiscal effect, that effect is confined to cases where liability to income tax has already accrued.

Third, because in any event the section can operate only upon income derived by the taxpayer.

Fourth, because if all else fails, the facts of the present case take it outside the ambit of the section.

These contentions pose the question of the true construction of section 108. Its history will be outlined presently; but it may be useful to recall at the outset some of the rules of interpretation which fall to be applied.

First, the words are to be given their ordinary meaning. They are not to be given some other meaning simply because their object is to frustrate legitimate tax avoidance devices. As Turner J. says in his (albeit dissenting) judgment in *Marx v. C.I.R.* (1970) N.Z.L.R. at p. 208, moral precepts are not applicable to the interpretation of Revenue Statutes.

Secondly, "one has to look merely at what is clearly said. There is no room for any intendment. There is no equity about a tax. There is no presumption as to tax. Nothing is to be read in, nothing is to be implied. One can only look fairly at the language used" [Per Rowlatt J. in *Cape Brandy Syndicate v. Inland Revenue Commissioners* [1921] 1 K.B. 64 at p. 71, approved by Viscount Simons L.C. in *Canadian Eagle Oil Co. Ltd. v. R.* [1946] A.C. 119.]

Thirdly, the object of the construction of a statute being to ascertain the will of the legislature it may be presumed that neither injustice nor absurdity was intended. If therefore a literal interpretation would produce such a result, and the language admits of an interpretation which would avoid it, then such an interpretation may be adopted.

Fourthly, the history of an enactment and the reasons which led to its being passed may be used as an aid to its construction.

The argument for the appellant in this case leans heavily on this last rule. He prays it in aid first in support of his opening contention that s. 108 has no fiscal effect. To do justice to this argument it is necessary to trace the ancestry of the section and for this purpose to cite a number of New Zealand enactments going back to 1878. This involves lengthening the present judgment but is better than attempting a summary.

*"The Land Tax Act 1878 s. 62*

Every covenant or agreement heretofore made or hereafter to be made between landlord and tenant, mortgagor and mortgagee, or between any other persons, altering or attempting to alter the nature of the estate in any land so liable to duty for the purpose of defeating or in any other manner evading the payment of land-tax imposed by this Act, or which shall be in any manner contrary to the true intent of this Act, or calculated to prevent its operation in any respect, shall, so far as regards any such covenant or agreement, be void and of no effect as between the parties thereto.

*The Property Assessment Act 1879 s. 29*

No contract, covenant, or agreement touching the payment of taxes to be charged on their respective premises heretofore made, or hereafter to be made, between any persons which is contrary to the intent and meaning of this Act shall be binding on the parties.

*The Property Assessment Act 1885 s. 35*

No contract, covenant, or agreement touching the payment of taxes to be charged on their respective premises heretofore made or hereafter to be made between any persons which is contrary to the intent and meaning of this Act shall be binding on the parties.

*The Land and Income Tax Assessment Act 1891 s. 40*

Every covenant or agreement heretofore made or hereafter to be made between landlord and tenant, mortgagor and mortgagee, or between any other persons, altering or attempting to alter the nature of the estate or interest in any land or mortgage for the purpose of defeating or in any other manner evading the payment of tax imposed under this Act, or which shall be in any manner contrary to the true intent of this Act, or calculated to prevent its operation in any respect, shall, so far as regards any such covenant or agreement, be void and of no effect as between the parties thereto.

*The Land and Income Tax Assessment Act 1900 s. 82*

Every contract, agreement, or arrangement made or entered into, in writing or verbally, either before or after the commencement of this Act, shall be absolutely void in so far as, directly or indirectly, it has or purports to have the purpose or effect of in any way directly or indirectly altering the incidence of any tax, or relieving any person from liability to pay any tax or make any return, or defeating, evading, or avoiding any duty or liability imposed on any person by this Act, or preventing the operation of this Act in any respect.

*The Land and Income Tax Assessment Act 1908 s. 103*

Every contract, agreement, or arrangement made or entered into, in writing or verbally, either before or after the coming into operation of this Act, shall be absolutely void in so far as, directly or indirectly, it has or purports to have the purpose or effect of in any way directly or indirectly altering the incidence of any tax, or relieving any person from liability to pay any tax or make any return, or defeating, evading, or avoiding any duty or liability imposed on any person by this Act, or preventing the operation of this Act in any respect.

*The Land and Income Tax Act 1916 s. 162*

Every contract, agreement, or arrangement made or entered into, either before or after the coming into operation of this Act, shall be absolutely void in so far as, directly or indirectly, it has or purports to have the purpose or effect of in any way altering the incidence of land-tax or income-tax, or relieving any person from his liability to pay such tax.

*The Land and Income Tax Act 1923 s. 170*

Every contract, agreement, or arrangement made or entered into, whether before or after the coming into operation of this Act, shall be absolutely void in so far as, directly or indirectly, it has or purports to have the purpose or effect of in any way altering the incidence of land-tax or income-tax, or relieving any person from his liability to pay such tax."

The present section 108 is in the same form as in section 170 of the 1923 Act save that the reference to "land tax" is omitted.

Income Tax was introduced into New Zealand in 1891: and whatever may be said about the earlier enactments cited above the language of section 82 of the Land and Income Tax Assessment Act of 1900 seems to their Lordships directly to contradict the appellant's first contention; and they take the same view of the succeeding sections. In particular the direction that the impugned contracts, agreements or arrangements should be "absolutely" void, appears to the Board to involve the consequence that they are void as against the respondent as well as against all others. On this part of the case their Lordships are in agreement with the opinions to the like effect expressed in the Court of Appeal in New Zealand in *Elmiger v. C.I.R.* (1967) N.Z.L.R. 161.

It is true that section 16 of the Land and Income Tax Amendment Act of 1968 (which does not apply retrospectively so as to affect the amended assessments under appeal in this case) specifically provides that the words "as against the Commissioner for Income Tax purposes" should be added to section 108 after the word "void". In their Lordships' view this did no more than to declare the existing law.

The second contention of the appellant is that section 108 refers only to accrued liabilities to tax and not to liabilities which may be expected *in futuro*. It is said that no contract, agreement or arrangement can alter the incidence of income tax, for that is prescribed by law. This expression in section 108 must therefore be taken to refer to some contract, agreement or arrangement which shifts the burden of some accrued liability to tax. There is, however, another possible meaning. The taxpayer, considering the provisions of fiscal legislation, may discern that by entering into some arrangement he can so distribute the legal incidence of tax upon his income that he himself will pay less. In other words the economic incidence is altered. In their Lordships' view this is what is contemplated by section 108.

The appellant's argument under this head is based alternatively on the omission from the Land and Income Tax Act 1916, section 162 and from its successors, of the expression

"or defeating evading or avoiding any duty or liability imposed on any person by this Act or preventing the operation of this Act in any respect"

which appeared in section 40 of the Land and Income Tax Assessment Act of 1891 (though not in identical terms) and again in section 82 of the similar Act of 1900. These words, it is said, are apt to refer to future expected liabilities, whereas the expression "relieving any person from his liability etc." are not. Accordingly the omission of the words is significant.

Their Lordships cannot accede to this argument. Nor is it really supported by anything which was said in *Peate v. Commissioner of Taxation of the Commonwealth of Australia* [1967] 1 A.C. 308. In that case the Board was simply concerned with the annihilating effect of section 260 of the relevant Australian Statute, and did not have to consider the respective effects of the component parts of the section. In the ordinary use of language one "secures relief from tax" if one "defeats" it or "evades" it, or "avoids" it; and their Lordships think that the true reason for the omission of these words from the present section 108 and its predecessors of 1916 and 1923 is probably that they were regarded as tautologous. Moreover to construe section 108 as referring only to liabilities which had already accrued would be to deprive it of almost all effect, and a construction having this result is not to be adopted unless the words of section 108 compel it, which they do not.

So far as this second contention is concerned their Lordships find themselves in agreement with the majority of the Court of Appeal in *Marx v. C.I.R.* and *Carlson v. C.I.R.* (1970) N.Z.L.R. 182.

The third contention of the appellant is that section 108 can have no application to any income which the taxpayer did not derive. The 1954 Act provides—see section 77 (2)—that income tax is to be payable on all income derived by the taxpayer; and in this case the appellant did not derive that portion of the income of the farm which went, under the "paddock trusts" to the trustees.

This contention throws into relief the difficulties caused by leaving a section such as section 108 completely silent as to what is to happen once the contract, agreement or arrangement has been declared absolutely void so far as its tax relieving purpose or effect is concerned. Is a vacuum left or is the taxpayer to be deemed to go on deriving the income? What is to happen if, simply in order to avoid tax, he has parted with the source of the income? Or receives money which is capital and not income? Section 108 gives no guidance at all on these points whether regarded alone or in conjunction with section 77 of the 1954 Act or section 78. In consequence, and in consequence also of some of the absurdities to which a strictly literal interpretation of section 108 would lead, judges have been compelled to search for an interpretation which would make the section both workable and just. In doing so they inevitably approach the line where interpretation ceases and legislation begins—a line which they may not cross. It is not that the problem confronting the legislator is insoluble. What is needed is simply a provision to the effect that where section 108 applies the taxpayer shall be deemed to have derived the income which he would have derived but for the contract, agreement or arrangement avoided by the section: and that the Commissioner might make assessments upon him accordingly.

But if future cases may reveal lacunae in section 108 which (if that section be left in its present half-finished state) judges must refuse to fill, the present case does not. The appellant here did derive the income. He sold the crop and received the proceeds. True, he then had to account for them to the trustees. But if this obligation has to be regarded as void under section 108, and the trusts non-existent, then one is left with the appellant receiving the income and accountable to nobody for it. In these circumstances it seems to their Lordships that the third contention of the appellant must fail.

His final contention is that section 108 does not apply to the facts of this case which make it an ordinary family trust for the maintenance and advancement of the appellant's wife and family. On this aspect of the matter Turner J. in the Court of Appeal said

“The lease of the 24-acre paddock was a lease for one year only. A disposition of an income-earning asset, if the primary reason for it were to provide income for members of the settlor’s family might confidently be expected to be a disposition for a longer period than this. It was an essential part of this scheme that while the lease of the wheat paddock was for one year, in the following year another paddock was to be leased—and again another the following year. It was the rotation of crops, of course, which made this kind of thing necessary—but which at the same time made this kind of transaction one particularly unfitted to be the basis of a family trust providing assured regular income for its beneficiaries. I cannot think that successive one-year leases of that particular paddock of the farm which by crop rotation happened to be the wheat paddock can be described as an ordinary family dealing, a typical family trust. I find it difficult, too, to accept Wilson J.’s conclusion that the rent charged for the paddock was realistic. The profit made undermines such a conclusion. It may well be that the rent, calculated on a basis of arithmetical average with reference to the area involved and the comparative area of the whole farm may appear justifiable; but it is to be remembered that the paddock leased was always the very paddock which in the particular year under consideration was ready for wheat—a highly profitable crop—and it seems to me that the rent charged for such a paddock in a particular year should have been greatly in excess of a mere arithmetical average. The whole scheme smacks of such business unreality that I cannot accept the conclusion of Wilson J.; and for myself I am convinced that the only proper inference to be drawn from the facts of the arrangement, and of the profits resulting therefrom, is that this scheme was devised for the sole purpose, or at least the principal purpose, of bringing it about that this taxpayer should escape liability on tax for a substantial part of the income which, without it, he would have derived.”

Their Lordships are in complete agreement with these observations. North P. expressed his conclusion as follows

“In my opinion, with all respect for the views expressed by Wilson J. this arrangement was obviously an attempt by the respondent to escape payment of income tax on what was really in truth his income.”

Their Lordships do not think that the learned President was basing his conclusion on a view of the matter which differed from that of Turner J; but it may nevertheless be useful to recall that strictly the question is not whether the diverted income “was really in truth his income” but whether section 108 had the effect of making that which was *not* in truth the appellant’s income but instead that of the trustees, nevertheless become the appellant’s income for the purposes of the 1954 Act.

Both sides relied upon the decision of the Board in *Newton v. The Commissioner of Taxation of the Commonwealth of Australia* [1958] A.C. 450. This was a decision upon section 260 of the Australian Income Tax etc., Act 1936–1951—a section apparently copied from section 82 of the New Zealand Act of 1900 above quoted. The judgment was delivered by Lord Denning and in the course of it he said:

“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 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."

In their Lordships' view this passage, properly interpreted, does not mean that every transaction having as one of its ingredients some tax saving feature thereby becomes caught by a section such as section 108. If a *bona fide* business transaction can be carried through in two ways, one involving less liability to tax than the other, their Lordships do not think section 108 can properly be invoked to declare the transaction wholly or partly void merely because the way involving less tax is chosen. Indeed, in the case of a company, it may be the duty of the directors *vis-à-vis* their shareholders so to act. Again, trustees may in the interests of their beneficiaries, deliberately choose to invest in Government securities issued with some tax-free advantage, and to do so for the express purpose of securing it. They do not thereby fall foul of section 108. The clue to Lord Denning's meaning lies in the words "without necessarily being labelled as a means to avoid tax". Neither of the examples above given could justly be so labelled. Their Lordships think that what this phrase refers to is, to adopt the language of Turner J. in the present case "a scheme . . . devised for the sole purpose, or at least the principal purpose, of bringing it about that this taxpayer should escape liability on tax for a substantial part of the income which, without it, he would have derived."

The present case clearly exhibits such a scheme; and for the reasons above set out their Lordships will humbly advise Her Majesty that the appeal should be dismissed. There will be no order as to costs, an agreement over which has been come to by the parties.

*(Dissenting Judgment by LORD WILBERFORCE)*

Section 108 of the Land and Income Tax Act 1954 is in the following terms. To facilitate later argument I set out in parallel the provisions of the corresponding Australian (Commonwealth) enactment—s. 260 of the Income Tax Assessment Act 1936–60.

*New Zealand*

S.108. Every contract, agreement or arrangement made or entered into, whether before or after the commencement of this Act, shall be absolutely void in so far as, directly or indirectly, it has or purports to have the purpose or effect of in any way altering the incidence of income tax or relieving any person from his liability to pay tax.

*Australia*

S.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\*

[\* as against the Commissioner added in 1936]

The question is as to the application of either of the two limbs (altering the incidence, or relieving) in the New Zealand section to transactions of which the following represents the essentials.

The taxpayer owned a farm of 385 acres at Methven, used for sheep-farming and mixed cropping with emphasis on cropping. He had a wife and two children. After his father had set up a trust for the benefit of his wife and children, the taxpayer agreed to lease to the Trustees a paddock of 25 acres at a rent of £3 per acre. The Trustees employed the taxpayer to prepare the leased paddock and to sow it in wheat. In due course the crop was harvested and sold. After the taxpayer was paid for his work, goods supplied, and rent a sum of £401, a net income was left of £739. £652 was distributed, £52 to the wife, £600 to the wife for the benefit, in equal shares, of the two children.

A similar operation was performed in the following year, with a different paddock of 24 acres, leased at £4 per acre.

It is relevant to notice the following features of these transactions:

- (1) The Trustees, in each case, became genuinely lessees of the leased paddock, and so liable to income tax in respect of the profit of farming it.
- (2) The income of the paddocks was, in each relevant year, derived by the Trustees and not by the taxpayer. ("derived" is the word used in s.77 the basic charging section.) A contention to the contrary was put forward at the trial but was negatived by the judge. There was no appeal against this finding.
- (3) The fact that the Trustees employed the taxpayer to carry out farming operations was not relied on, either in the judgments appealed from, or in argument, as having any relevance.
- (4) The taxpayer was not a Trustee of the settlement and had no control over the income of the settlement. He neither received nor, under the trusts, could receive any part of it. The payment of income to members of his family may have brought him some benefit, but this, in itself, is not a material consideration, as regards his liability to tax in New Zealand.
- (5) Before carrying out the transactions, the taxpayer had consulted his accountants and sought advice how he could reduce the amount of income tax payable in the future. But this would only be material if (a) the test were to be the motive of the taxpayer rather than the purpose of the contract etc. (as to this see *Newton v. Commissioner of Taxation* 1958 A.C. 450 in a contrary sense) and (b) the case was shown to be within one or other of the limbs of the sections (altering the incidence, or relieving).

I turn then to consider the meaning of the section. I approach it with four points in mind.

*First*, it is a section with a history. I do not trace it in detail; the successive enactments are set out in the majority judgment and they have been analysed with clarity in more than one judgment in the New Zealand Courts. I select what seem to me certain significant points.

The starting point was the Land Tax Act 1878 s. 62, a section dealing only with Land Tax, as to which the policy in New Zealand (comparably to the policy in Great Britain concerning Landlords' Property Tax) was to ensure that this tax should be borne by the owner of the land and its burden not shifted on to others—such as tenants of the land. This section made covenants or agreements contrary to the intent of the Act "void and of no effect as between the parties thereto". These words are perhaps not free from ambiguity, but it seems to have been accepted



in New Zealand that they limited the voiding effect of the section to the parties and that it did not relate to or affect the landowner's liability to the Crown. The "inter partes" character of the legislation was clearly stated in the differently drafted Property Assessment Acts (1879 s. 29, 1885 s. 35).

The first statute dealing with income tax was the Land and Income Tax Assessment Act 1891. That related both to Land Tax and to Income Tax. It provided, in terms similar to the Act of 1878, that the relevant covenants or agreement should "be void and of no effect as between the parties thereto".

The parent of the present section, and of the Australian s. 260 is The Land and Income Tax Assessment Act 1900 s. 82. This contained the four limbs now found in the Australian section and used the words "absolutely void." The disappearance of any reference to "the parties" lends force to the argument that, thereafter, the section had fiscal effect. But the words "absolutely void" would also be fully sufficient to operate inter partes.

The words "absolutely void" continued to be used in New Zealand down to and including s. 108 of the Act of 1954 and in Australia down to 1936. In that year Australia, in the Commonwealth Act, added the words "as against the Commissioner", an example followed in New Zealand in 1968, subsequently to the assessments now under appeal. These amendments no doubt had the effect of making the sections into purely fiscal sections but only as from the date of their enactment. Before then, they were both fiscal and inter partes.

I have referred to this history because it exposes the difficulties which have faced the Courts in interpreting the section—particularly the words "altering the incidence".

The question has arisen, and it arises here, whether these words have an inter partes effect, or a fiscal effect or both, and different answers have emerged. In *Charles v. Lysons* (1922) N.Z.L.R. 902 (decided on s. 162 of the Act of 1916 which dealt with both Land and Income Tax) the Court of Appeal held that the section had inter partes effect. It "must be construed as directed to contracts or agreements altering the incidence as between the owner and third parties. This is the only escape if it is to receive any effect at all." But in *Elmiger v. C.I.R.* (1967) N.Z.L.R. 161, the present learned members of the Court of Appeal distinguished *Charles v. Lysons* as a decision limited to Land Tax and held that this limb had fiscal effect. In Australia the High Court decided in *De Romero v. Read and another* (1932) 48 C.L.R. 649 that the provision operates inter partes, a decision described as "unexpected" in Newton's case.

It would not be surprising if, after a development starting from 1878 in the field of Land Tax, with the separate strands of inter partes and fiscal applications interwoven in different ways and through the use of different language, a section should emerge which indubitably lacks clarity of purpose and may indeed largely fail of effect. At any rate its interpretation needs to be approached without any predisposition to believe that it adequately embodies or gives effect to modern fiscal policy.

Secondly, the New Zealand section is not one which, fiscally, has provoked much litigation—perhaps because tax "avoidance" has not been part of the New Zealand way of life.

Its consideration by the Courts begins in the 1960s. There were two cases in 1965 (*Lewis, Purdie*) decided in favour of the taxpayer. Then in 1966–7 *Elmiger* was decided by Woodhouse J. and the Court of Appeal. That was a case of an artificially created deduction, and it produced the holding that the section applied not only to accrued liabilities but to

future liabilities. It went no further. Each member of the Court confined his observations to the case where the effect of the attacked arrangement is that the income sought to be taxed was derived by the taxpayer, and expressed no opinion on any case, where the effect of the arrangement was that the income was not derived (see North P. p. 102/25, Turner J. p. 104/15–50 McCarthy J. p. 190/25).

So, to refuse the extension demanded by the present case does not run counter to a line of New Zealand decisions: it merely sets a limit to the application of a difficult section.

*Thirdly*, the present New Zealand section contains only two of the four limbs found in the corresponding Australian s. 260, in particular, it does not contain what would naturally appear to be the limb most directly relevant—the “avoiding” limb (c), that under which the great majority of Australian decisions has been given. The third and fourth limbs, previously appearing in the New Zealand Act of 1900, were dropped by the Act of 1916—one of consolidation and amendment.

Now I am prepared to believe that there is some degree of overlapping between the four limbs—although those with the widest spread would seem to be (c) and (d) rather than (a) and (b) which appear to deal with specific limited cases. But it requires a degree of credence, I would, with respect, almost say interpretative astigmatism, to conclude that the two New Zealand limbs cover effectively the whole of the territory occupied by the Australian section—specifically that they cover the whole field of “tax avoidance”. Why the New Zealand section was abbreviated in 1916 has not been satisfactorily explained, perhaps for reasons of elegance, perhaps, as the majority judgment suggests, because limbs (c) and (d) were thought to be tautologous. But, like the Venus of Milo, aesthetic improvement by loss of members may be paid for by a loss of potency; and an anonymous draftsman’s hypothetical belief as to tautology can hardly make a canon of construction. We have to consider it possible that he may have been wrong.

There are suggestions in the Court of Appeal that the truncated section may be construed according to a supposed legislative intention not to weaken a tax position in the middle of a major war. But I cannot accept this as a legitimate method and it was not urged upon us by the Solicitor-General. We must take the section as we find it: if it is weaker than its Australian counterpart, at least it may create less difficult cases.

*Fourthly*, if the Courts are agreed on anything about the section it is that it is a difficult one. Originating in a desire to deal with the simple matter of incidence of Land Tax, it has found itself confronted, with only minor changes of language, with all the sophistications of modern tax “avoidance”.

If one compares it with more recent examples of legislation, it can be seen, and the decisions show, that it is deficient in a number of respects:

- (a) It fails to define the nature of the liability to tax, avoidance of which is attacked. Is this an accrued liability, a future but probable liability, or a future hypothetical liability? Is it one which must have arisen but for the arrangement, or which might have arisen but for the arrangement, and if “might”, probably might or ordinarily might or conceivably might?
- (b) It fails to specify any circumstances in which arrangements etc. which in fact have fiscal consequence may be outside the section, and, if such exist, to specify on whom the onus lies, and to the satisfaction of whom, to establish the existence of such circumstances. The taxpayer is left to work his way through a

jungle of words, "purpose", "or", "effect", "purported purpose", "purported effect" which existing decisions have glossed but only dimly illuminated.

- (c) It fails to specify the relation between the section and other provisions in the Income Tax legislation under which tax reliefs, or exemptions, may be obtained. Is it legitimate to take advantage of these so as to avoid or reduce tax? What if the only purpose is to use them? Is there a distinction between "proper" tax avoidance and "improper" tax avoidance? By what sense is this distinction to be perceived?
- (d) It gives rise to a number of extremely difficult problems as to what hypothetical state of affairs is to be assumed to exist after the section has annihilated the tax avoidance element in the arrangement (c.f. (in Australia) *Peate v. Federal Commissioner of Taxation* [1967] A.C. 308). These difficulties are referred to in the majority opinion. I return to them later.

Many of these matters are dealt with in the English and Canadian legislation—see F.A. 1951 s. 32, F.A. 1960 s. 20. Canadian Income Tax Act s. 138—summarised in an Appendix hereto. No doubt these raise their own difficulties but the New Zealand section, precisely because it was one of the first in the field, leaves the emergent problems largely unassaulted.

In Australia and New Zealand the Courts have endeavoured to remedy some of the statutory deficiencies. In *Newton v. Commissioner of Taxation* [1958] A.C. 450, a dividend stripping case, this Board gave some fresh life to the Australian section by instancing transactions "capable of explanation by reference to ordinary business or family dealing, without necessarily being labelled as a means to avoid tax", a suggestion profitably generalised by Kitto J. in the words "capable of explanation by reference to ordinary dealing such as business or family dealing . . ." (*Huncock v. Commissioner of Taxation* [1961] 108 C.L.R. 258, 283) but it could hardly be claimed that these are indications of precision. They have in turn been "interpreted" in the majority decision in this case. But one difficulty leads to another, and the courts are now having to decide how "ordinary" a transaction must be to escape. In the present case, the judges have, not surprisingly, reached differing conclusions: Wilson J. thought the transactions were ordinary: the Court of Appeal found that they were extraordinary.

The last word was said on the Australian section; also by Kitto J. in *Newton's* case:

"Section 260 is a difficult provision, inherited from earlier legislation, and long overdue for reform by someone who will take the trouble to analyse his ideas and define his intentions with precision before putting pen to paper" (96 C.L.R. 578, 596).

It is because I believe that the limits of judicial interpretation, however liberal or commonsense the process may be claimed to be, are passed when one comes to attempt to apply the New Zealand section to this present case that I cannot agree with the Board's decision. I think that we have here a rusty instrument which breaks in our hands and is no longer capable of repair.

Briefly to restate the question. Is a transaction, by which the taxpayer has disposed of an income producing asset, so that in neither of the relevant years does he derive any income, directly or indirectly, fall within the terms of the New Zealand section as either altering the incidence of any tax or relieving him from his liability for income tax?

The case seems, if anything, one of "avoidance" as "avoidance" has been interpreted in Australia. But New Zealand lacks the word—it has "altering the incidence" and "relieving".

As to altering the incidence, I fail to see how this covers the present case. The tax falls on whom it falls according to the Act. Changing—for a period or indefinitely—the ownership of land does not alter the incidence of the income tax which is imposed on whoever makes a profit from farming the land. I do not think that this can be got over by calling it “economic incidence”. To suppose that it can, involves bringing within the section, subject only to the unexpressed and uncertain gloss of *Newton's* case, all transfers of property. Yet this has often been said not to be the purpose. Thus

“It (s. 53 of the Income Tax Assessment Act 1915–16—predecessor of s. 260) does not extend to the case of a *bona fide* disposition by virtue of which the right to receive income arising from a source which theretofore belonged to the taxpayer is transferred to and vested in some other person”

*Purcell's* case 29 C.L.R. 464, 466 per Knox C.J.

“Its office is to avoid contracts which place the incidence of the tax or the burden of the tax upon some person or body other than the person or body contemplated by the Act. If a person actually disposed of income producing property to another so as to reduce the burden of taxation, the Act contemplates that the new owner should pay the tax. The incidence of the tax and the burden of the tax fall precisely as the Act intends, namely, upon the new owner” (ibid. per Gavan Duffy J. and Starkey J. p. 473.)

This case was approved by this Board in *Newton's* case.

Then the second limb: “relieving any person from his liability to pay income tax”. The Commissioner’s argument placed much emphasis on the contention that “liability” here may include a future liability. So it may—*Elmiger's* case so decided—I agree with the decision. But it is one thing to say that an arrangement is caught if and when it applies to income to be received in the future, to which a future liability for tax would attach, and is by the arrangement avoided, and quite another to attack an arrangement under which, in the future, no income is ever derived at all. To describe the latter as one “relieving” a person “from his liability” seems to me, with respect, to involve not a flexible use of the word “relieving” but a simple misuse of language. I cannot forget that “relief” has a well accepted meaning in fiscal contexts which is a long way away from the more general concept of avoidance.

The objection against applying the section (either limb) to dispositions of income-producing property are underlined, I respectfully suggest, by the majority decision. The opinion, by reference to sections 77 and 78 of the Act, as to deriving of income, points out very clearly the difficulties which are likely to arise in the ordinary case, where a disposition within the section has been made, in assessing the disponent to tax. The opinion seeks to overcome this, in the instant case, by reliance on the special circumstance that the income passed through the taxpayer’s hands on its way to the Trustees. But with respect this ignores the finding of Wilson J. not challenged on appeal, that the taxpayer did not derive the income and I fail to see how the physical receipt by him as agent can form the basis of any derivation. As Wilson J. said “The income was not derived by him but by the trustees, and the fact that the merchant who purchased the crops . . . paid the proceed, for its own convenience, to the objector does not affect the position.”

For these reasons in agreement with the judgment of Turner L.J. in *Marx v. Commissioner for Taxation* I am of opinion that the taxpayer’s appeal ought to succeed.

**In the Privy Council**

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**OWEN THOMAS MANGIN**

**v.**

**THE COMMISSIONER OF  
INLAND REVENUE**

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## APPENDIX

## I. U.K. Enactments

## A. Finance Act 1951 s. 32

(1) Where the Commissioners are of opinion that *the main purpose or one of the main purposes* for which any transaction or transactions was or were effected . . . was the avoidance or reduction of liability to profits tax, they may, if they think fit, direct that *such adjustments* shall be made as respects liability to the profits tax *as they consider appropriate* so as to counteract the avoidance or reduction of liability to the profits tax which would otherwise be effected by the transaction or transactions.

(3) [avoidance or reduction of liability to the profits tax deemed to be the main purpose or one of the main purposes if the main benefit which might have been expected to accrue in the 3 years following completion of the transaction(s) was the avoidance or reduction of liability to the tax].

(5) [Exempted transactions specified].

(6) [duty of Commissioner to grant clearance if satisfied that the transaction(s) were or will be entered into for *bona fide* commercial reasons and are such that no direction under the section ought to be given].

## B. Finance Act 1960 s. 28

(1) Where—

a person is in a position to obtain, or has obtained, a tax advantage, then *unless he shows* that the transaction or transactions were carried out either for *bona fide commercial reasons, or in the ordinary course of making or managing investments*, and that none of them had as *their main object or one of their main objects*, to enable tax advantages to be obtained . . .

(3) Where this section applies to a person in respect of any transaction or transactions, the tax advantage obtained or obtainable by him in consequence thereof shall be counteracted by such of the following adjustments, that is to say, an assessment or additional assessment, the nullifying of a right to repayment or the requiring of the return of a repayment already made . . . other computation or recomputation of profits or gains, or liability to tax, on such basis as the Commissioners of Inland Revenue may specify by notice in writing served on him as being requisite for counteracting the tax advantage so obtained or obtainable.

43 (4) (g) "tax advantage" means a *relief or increased* repayment of, income tax, or the *avoidance of a possible* assessment thereto, whether the *avoidance or* reduction is effected by receipts accruing in such a way that the recipient does not pay or bear tax on them, or by a deduction in computing profits or gains.

## II. Canadian Enactment R.S.C. 1952 c. 148 Income Tax Act s. 138

(1) Where the Treasury Board has decided that *one of the main purposes* for a transaction or transactions was *improper avoidance* or reduction of taxes which might otherwise have become payable under the Act . . . the Treasury Board may give such directions as it considers appropriate to counteract the avoidance or reduction.

(3) When a direction has been given under this section, tax shall be collected, or assessed, or reassessed and collected, *notwithstanding* any *other provision of this or any other Act*, in accordance therewith.