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THE CONCEPT OF SHAM AND ITS LIMITED EFFECTIVENESS IN THE TAX FIELD

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TABLE OF CONTENTS

ABSTRACT

This paper endeavours to explore the concept of sham as the starting point. In order to do that, this paper cites differing judicial views to show the ambiguity of the concept, and shows how the principle of precedent is distorted by the way that the appeals process operates in the tax field, and the resulting inconsistency in approaching sham. This paper then seeks to ascertain how far the legal notion of "sham" has advanced, since Lord Justice Diplock's legal test in *Snook v London West Riding Investments*. How the common shared viewpoints and some existing ambiguities limit the application of sham in the tax field are illustrated next. The paper also examines mislabelling as an alternative to sham, to illustrate the courts' reluctance to find sham.

After examining the concept of sham, this paper discusses sham in the context of the form and substance doctrine. The United States approach of substance over form is compared with the commonwealth narrow approach. Then the paper concludes by demonstrating the limited effectiveness of the concept of sham in the tax field.

The text of this paper (excluding abstract, table of contents, footnotes and bibliography) comprises approximately 14,668 words.

I INTRODUCTION

The concept of sham has been described as the "principal weapon which a court can use to thwart avoidance, is a function of, and not a restraint on, the power of parties to create legal rights and according to their intentions."[1] Interestingly though, from another angle, sham doctrine has been described as a doctrine developed by common law, which arrogate to judges an illegitimate power to refuse to give effect to genuine agreements.[2] The sham doctrine has come to be applied in a variety of contexts and it forms an exception to many areas of law. However, Lockhart J in *Richard Walter Pty Ltd v Commissioner of Taxation*[3] warned of the ambiguity and uncertainty that surrounds the meaning of sham and its application.

This paper endeavours to explore the concept of sham as the starting point. In order to do that, this paper cites differing judicial views to show the ambiguity of the concept, and shows how the principle of precedent is distorted by the way that the appeals process operates in the tax field, and the resulting inconsistency in approaching sham. This paper then seeks to ascertain how far the legal notion of "sham" has advanced, since Lord Justice Diplock's legal test in *Snook v London West Riding Investments*[4]. How the common shared viewpoints and some existing ambiguities limit the application of sham in the tax field are illustrated next. The paper also examines mislabelling as an alternative to sham, to illustrate the courts' reluctance to find sham.

After examining the concept of sham, this paper discusses sham in the context of the form and substance doctrine. The United States approach of substance over form is compared with the commonwealth narrow approach. Then

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[1] Ben McFarlane and Edwin Simpson "Tackling Avoidance" in *Rationalising Property, Equity and Trusts: Essays in Honour of Edward Burn* (J Getzler (ed), LexisNexis Butterworths, London 2003) 135, 135.

[2] Joseph Isenbergh, *Musings on Form and Substance in Taxation*, (1982, 49 University of Chicago Law Review, 859); George Cooper "The Taming of the Shrewd: Identifying and Controlling Income Tax Acoidance" (1985) 85 *Columbia Law Review* 657, as cited in Donahue, above n 140, 165

[3] (1996) 67 FCR 243; 96 ATC 4550, 4552. ("*Snook*")

[4] [1967] 1 All ER 518, 528-529.

the paper concludes by demonstrating the limited effectiveness of the concept of sham in the tax field.

II CONCEPT OF SHAM

A Differing Views in Understanding the Concept of Sham.

"Sham" is defined by the *Shorter Oxford Dictionary* as "a trick, a hoax.... something that is intended to be mistaken for something else, a spurious imitation". However, this is far wider than the legal definition adopted in common law jurisdictions. This word first appeared evidently as slang in the seventeenth century and it has obscure origins.[5] Therefore, sham is not a word of precise meaning or application.[6]

The disinclination among members of the judiciary to define the concept of sham is evident in what Somervell LJ said in *O'Connor v Hume*[7]:

> Having had the evidence and the correspondence between the parties read to us, I see no ground for regarding the agreement in the present case as a "sham", whatever that may mean.

Even Diplock LJ himself, whose formulation is well accepted as the sham test[8], expressed his apparent reluctance to define sham as an independent legal concept: "it is, I think, necessary to consider what, if any, legal concept is involved in the use of this popular and pejorative word".[9] Ironically, a concept so reluctantly defined has fostered the belief that there is such a concept.[10]

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[5] Malcolm Gammie "Sham and Reality: the Taxation of Composite Transactions" [2006] 3 BTR 294, 311.
[6] Gammie, as above n 4, 311.
[7] [1954] 2 All ER 301, 303.
[8] It will be demonstrated in later chapter D.
[9] [1967] 2 QB 786, 802.
[10] McFarlane and Simpson, above n 1, 140.

Sham is regarded as an exception to the form over substance doctrine in law and a judicial concept applied by courts to look beyond the form of a transaction; and evaluate the transaction's substance. Justice Thomas said in *Peters v Davison*[11]:

> Whatever one's view of a doctrine of form over substance, it does not apply to instances where the transaction is a sham, that is, where the form merely conceals the fraudulent reality.

However, Windeyer J in *Scott v F C of T (No 2)*[12] considered "sham" involves "the difficult and debatable philosophic questions of the meaning and relationship of reality, substance and form".

In contrast, some judges[13] have referred to "sham" as just one word among many others to describe a legal situation differs from its reality, where the meaning is of no greater, or lesser significance than the other words used to describe a variety of situations in which the nature of legal acts or transactions are called into question. It is bad company to be found in and it was described as "popular and pejorative"[14] and "inherently worthless"[15] Nevertheless, after Diplock LJ's well-accepted description of "sham" in *Snook*, this word has been given a specific and particular legal character, which is evident by Turner J's observations in *Paintin & Nottingham v Miller, Gale & Winter*[16]:

> The word 'sham' is well on the way to becoming a legal shibboleth; on its mere utterance it seems to be expected that contracts will wither like one who encounters the gaze of a basilisk. But by a 'sham' is meant, in my opinion, no more and no less than an appearance lent by documents or other evidentiary materials, concealing the true nature of a transaction and making it seem something other than that what it really is. The word 'sham' has no applicability to transactions which are intended to take effect, and do take effect, between the parties thereto according to their tenor, even though those transactions may have the effect of fraudulently preferring one creditor to others, and notwithstanding that they are

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[11] [1999] 2 NZLR 164, 193, which refers to *Mills v Dowall*.
[12] (1966) 40 ALJR 265.
[13] For example, Winderyer J in *Scott v Commission of Taxation (No 2) (Cth)*(1966) 40 AJR 265.
[14] *Snook*, above n 3, 528.
[15] *Jaques v F C of T* (1924) 34 CLR 328. ("*Jacques*")
[16] [1971] NZLR 164, 175.

> deliberately planned with this in view. If such is their effect there are statutes and rules of law designed to thwart the intentions of those who entered into them; but the fact that the law discountenances such transactions as these does not render them 'shams'.

The different views of the concept of sham before *Snook* attributes to the disinclination among judicial members to define or utilize this concept. This potentially limits the application of sham because of the ambiguity around its concept.

B Hard to Maintain Consistency in Approach

As a question of fact, the finding of sham involves evaluating and weighing different factors. Before *Snook* was decided, in which Lord Diplock's formulation of sham was spelt out, there was no well accepted guided approach as to how sham should be found. The finding of sham depended largely upon how the judges of fact considered the concept of sham in each ease. Decisions before *Snook* displayed little consistency in attitudes toward the findings of sham. This inconsistency is amply illustrated in cases.

In *IRC v Sansom*[17], Mr. Sansom had operated a small timber business which he had turned into a company. He owned all of the shares except one being given to his employee, who was an independent shareholder. This company made huge profits during the war and the company never declared a dividend. As the governing director, Mr. Sansom instructed the Secretary to make cheques payable to him. These were entered in the company's books as loans. There was neither interest nor security agreed for these loans. Mr. Sansom invested the proceeds of these loans in War stocks in his own name. Thereupon the Crown assessed Mr. Sansom to super tax, taking the sums he received by way of loan as being profits received by him from the company. He paid off the loans and advances he drew from the company before 1912. He considered winding up the company in 1916 and drew further loans from the company, these loans remained unpaid. In 1917 a resolution was

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[17] *IRC v Sansom* (1921) 8 TC 20,("*Sansom*"), see Natalia Lee, "The Concept of Sham: a Fiction or Reality?" (1996) 47 *Northern Ireland law Review* 377, 381.

passed to wind up the company voluntarily. The liquidator did not call in the loans and advances but treat them as part of assets of the company. The Revenue assessed the taxpayer on the basis that the monies received by him were not loans but in fact distributions of the profits from the company to Sansom and therefore formed part of his income. This assessment came before the Commissioners, who found that the company was properly constituted; the company did have the power to make loans and it did make such loans; and that such loans did not form part of Sansom's income for the purpose of super tax (a higher tax rate). The assessment was therefore discharged.

On the appeal, the Crown contended that the company was the taxpayer (Sansom) himself in reality; therefore, the profits of the company were Sansom's income. Alternatively, the Crown argued that the loans and advances were not genuine loans but distributions, accordingly the loans and advances constituted income for super tax purposes. Rowlatt J made an order that the case should be remitted to the Commissioners to determine (a) whether the company was a sham and in fact carried on the business; or whether Sansom carried it on; (b) if the company carried on the business, whether it did so as agent for Sansom or on its own behalf for the benefit of the corporators.

Two out of three Court of Appeal judges expressed their suspicion as to what happened, which was described as "singular" and "remarkable".[18] They thought the case for the Crown was very strong before the Commissioners found those to be the facts. However, as stated in their judgment, they did not see how they could possibly interfere with a finding of the Commissioners, as the findings of the Commissioners were conclusive and unimpeached on questions of fact. Since the Commissioners had found genuine loans were made to Sansom, it negated both the questions directed by Rowlatt J to them. It would be wrong to send the case back to them to answer the questions.

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[18] The other judge did not really comment on the fact but form his reason upon the ground that the fact findings of the Commissioners negated both questions directed by Rowlatt J.

However, in *Jacob v IRC*[19], which was held four years later with similar facts to *IRC v Sansom*, the sham argument was accepted. In this case, Jacob was the controlling shareholder of five limited liability companies, which will be referred to as Scottish, Glasgows, Jackson's, Edwards, and Alexanders respectively. He had traded under different names before he converted his business into the limited liability companies. All of the companies had power to make loans with or without security. He drew monies from the companies in the form of loans without any security or any arrangement of repayment or interest. He used the proceeds of the loans toward financing the purchase in his own name of premises to be occupied by himself trading as a firm. None of these companies had declared a dividend. Although some of the loans made to Jacob were subsequently approved formally in general meeting, no previous formal authorisation was given for any of the loans. Alexanders was wound up under a voluntary liquidation, and Jacob was appointed as the liquidator. He did not take any steps to obtain repayment of the loans withdrawn by him. The Special Commissioners decided the loans in question were not made in the course of the business carried on by the companies, and they were not genuine loans but constituted income of Jacob for the purposes of super tax

It is quite ironic that both the taxpayer and the Crown used *Sansom* to support their contentions. Citing *Sansom* as authority, the taxpayer argued that the companies were properly constituted entities and these companies had the power to make loans and in fact they did make the loans. The Crown argued that the dicta of the judges of the Court of Appeal in *Sansom*'s case supported the contention that the sums were in fact a distribution to the appellant of the profits of the Companies and were assessable for super tax. On appeal, the Commissioners found that the taxpayer had used the monies for his own purposes and Jacob had no intention to repay in case of Alexanders. Therefore, the loans were not genuine and they formed part of Jacob's income for the purpose of super tax. The question of law for the Court was whether the Special Commissioners' finding was reasonable or not. The

[19] *Jacob v IRC* (1925) 10 TC 1, ("*Jacob*"). See Lee, above n 17.

Court answered the question in the affirmative. The sham argument was accepted accordingly.

The material facts of both cases are very similar. Companies had been properly incorporated and had the power to make loans. Loans were made without security and no repayment or interest was made. The companies wound up voluntarily with assets distributed to taxpayers. The crucial question in both cases is whether the loans were genuine as the taxpayer would not be assessed super tax if the loans were genuinely made to him. The Court of Appeal in *Sansom* emphasised that that there was an independent shareholder in Sansom's company (Sansom owned 2,499 shares while one share was owned by his employee). This indicated that the company is not in fact Sansom himself as the profits do not belong to the man who holds most of the shares. "That a man cannot have a genuine loan to himself out of his own money"[20]. As the Commissioner had found genuine loans were made, it would be pointless to send the case back to the Commissioners as it was impossible to find Sansom's company was in fact himself when genuine loans were found. In *Jacob*, Jacob was also not the sole shareholder of all the five companies. However, this factor was not considered in the same manner as in *Sansom* and no issue of whether the company was in fact Jacob himself was raised. It could be argued in *Jacob*, the fact that no formal authorisation was made for the loans as well as that the accountant who prepared the companies' accounts recorded the loans as "dividends" in some instance might support the sham argument. However, the fact that nothing except debits were recorded in the books for the sums drawn by Sansom also indicated that the formal procedures required for the loans were not followed in *Sansom*. As far as the "dividends" recorded in the accounts in *Jacob*, the accountant had no authority or warrant from either of the directors or from anything in these Companies' books to treat them as dividends. Obviously this factor cannot be relied upon to differentiate *Jacob* from *Sansom*. The Commissioner in *Jacob* found the loans were not genuine on the basis that Jacob had no intention to repay and took no steps to repay, together with the fact that Jacob used the sums

[20] *Jacob* , above n 19, 18 Lord Scrutoon.

as his own money. Regrettably, the Commissioner in Sansom did not reach a similar decision, although Sansom showed by his conduct[21] that he had no intention to repay the loans, and he used the sums for his own purposes[22] as well.

The only reason that different conclusions were reached was that the fact-finding Commissioners took very different approaches. In *Sansom*, although the required procedures for the form of loans were not followed, the Commissioners looked at no more than the legal form Sansom employed to avoid personal tax liability. While in *Jacob*, the Commissioners were prepared to look beyond the legal form of the loans and examined the transactions' substance. The fact that no formal resolution was made in both cases for the loans as well as no security and no interest for the loans, casts doubt on whether the taxpayer intended to create the legal rights and obligations as loans. Although the loans were made in the name of the companies, in reality they were distributions from the companies to the taxpayers. This is illustrated in the dicta of the Court of Appeal judges in *Sansom*, which was relied on by the Crown in *Jacob*. Sham is a question of fact, which involves weighing competing legal principles and considering different factors in different cases. Different findings could be reached even in two similar cases such as *Jacob* and *Sansom*. It is apparent from the comparison of these two cases that consistency is hard to maintain as to how to detect whether a document or transaction is a sham since the fact findings of the Commissioners were conclusive and binding. It is important then, to consider how appeals in tax cases operate in the United Kingdom.

C How Appeals in Tax Cases Operate

Whether or not a transaction is a sham must be a question of fact. In *IRC v Garvin*[23], Buckley LJ spelt out this by saying: [24]

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[21] In 1916, Sansom had the idea of selling the business and the company wound up voluntarily eventually in September, 1917. During this period, in view of the intention of the taxpayer to discontinue the business, very little fresh stock was purchased and the existing stock was sold off as occasion arose without it being replenished. During that period, some property belonging to the company was also sold. The loans in issue were withdrawn during this period.

[22] Sansom bought war stocks under his own name using the sums he drew from the company.

> "In this jurisdiction the function of determining the facts of the cases belongs exclusively to the Commissioners. We cannot treat as a sham any transaction which the Commissioners have found to have taken place and which they have not found to be a sham."

This view was affirmed later in *Ramsay v IRC*[25], where Lord Wilberforce said:

> "It is for the fact-finding commissioners to find whether a document, or a transaction is genuine or a sham. In this context to say that a document or transaction is a "sham" means that while professing to be one thing, it is in fact something different. To say that a document or transaction is genuine means that, in law, it is what it professes to be, and it does not mean anything more than that."

The Commissioners, General or Special are the ones who are responsible for finding the facts. There can be no appeals on the facts. The only ground to challenge is reasonableness of the view of the facts that the Commissioners entertained.[26] All further courts are bound by the Commissioners' findings as long as the view taken of the facts is not unreasonable. There are a number of cases where a member of further court had viewed the facts and thus the whole case entirely differently, but that member was bound by the finding of the Commissioners, which was the case in *Sansom*. Another example is Lord Fraser's observation in regard of the Rawling scheme in the *Ramsay* decision[27]:

> "There was apparently no evidence before the Special Commissioners that Thun actually possessed the sum of $543,600 which they lent to the taxpayer to set the scheme in motion…and it might well have been open to the Special Commissioners to find that the loan, and all that followed upon it, was a sham. But they have not done so."

Similar regrets were demonstrated in other cases both before and after the *Snook* case. In *William v IRC*[28], a highly artificial scheme was used to attempt to minimize the tax liability on the sale of some development land. Although there were indications during the hearing before the Commissioners that some of the transactions were paper shams, there was no investigation carried out in regard to them. No argument of sham was advanced. The finding of this case was that all the

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[23] *IRC v Garvin* [1980] STC 295, ("*Gravin*"), as cited in Lee, above n 17, 382.
[24] As above n 10, 300. The decision of the Court of Appeal was affirmed by the House of Lords; see [1981] 1 WLR 793.
[25] [1981] 1 All ER 865 (HL). ("*Ramsay*").
[26] *Edwards v Nairstow & Harrison* [1956] AC 14.
[27] *Ramsay*, as above n 25, 338D (HL).
[28] *William v IRC*(1980) 54 TC 257, as cited in Lee, above n 17, 382.

transactions did take place. Browne-Wilkinson J viewed the facts and the whole case differently, he said: "Although I understand how this has come about, I express regret that the court is required to treat as genuine certain transactions which may well not have been genuine".

In *IRC v Gravin*, which concerned another highly artificial scheme entered into for the purpose of avoiding tax, Templeman LJ explained "the scheme only created rights and liabilities in order that those rights and liabilities might be destroyed. The 999-year leases were created and destroyed in six days" and he went on to say "it is now too late for the Revenue to cry 'sham'". Buckley LJ agreed with him on this point by saying that:[29]

> "anyone who creates a series of 999-year leases in the knowledge that they are to be determined within a week....or who accepts a purchase price upon terms that much the greater part of it will not be payable for 200 years in the knowledge that within a fortnight he will receive a substantial capital sum as the price of all future installments of the delayed payments, seems to....run a very real hazard of being held to enter into a sham transaction, however, no such finding was made in this case".

The Commissioners found the facts as being, that all the transactions had taken place. The Court of Appeal was bound to follow.

The above cases demonstrate the reluctance amongst the fact-finding Commissioners to conclude anything near to a finding of sham. Another point to note is that, the General Commissioners are not lawyers but ordinary members of the public[30]. If members of the judiciary find it difficult to understand the concept of sham[31], it sounds unrealistic to expect a lay person to examine whether the various agreements in question have followed the correct form, and consider what happened thereafter to the term agreements as shams as matters of fact.

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[29] *Garvin*, above n 23, as cited in Lee, above n 17, 382.

[30] See *Hudson Contract Services Ltd v Revenue and Customs Commissioners* [2007] EWHC 73 (Ch); [2007] STC 1363; *Usetech Ltd v Young (Inspector of Taxes)* [2004] EWHC 2248 (Ch), 76 TC 811, [2004] STC 1671.

[31] For example, as I demonstrated earlier that Somervell LJ was not willing to define sham in *O'Connor v Hume.*

As illustrated above, the effect of such a procedure is that the common law fundamental doctrine of precedent has been distorted.[32] A particular proposition arising from a case may only have been decided reluctantly, because the court was obliged to follow the Commissioners' findings.[33] Further courts cannot interfere with the approach taken by the Commissioners as to how and whether a sham should be found.

Interestingly, it is reasonable to expect the appeals system in tax cases to be identical in civil cases in the same jurisdiction, for example, in the United Kingdom. However, that is not the case. In *Snook*, Court of Appeal judges evaluated different factors, and they were *not bound* by the findings of facts found by the Country court judge. Although the finding of sham is a question of fact, the legal approach of how sham should be found is a question of law. It is evidenced by Dipolock LJ's statement that "as regards to the contention of the plaintiff that the transaction between himself, Auto Finance and the defendants was a 'sham', it is, I think, necessary to consider, what, if any legal concept is involved in the use of this popular and pejorative word", that is how his famous formulation came out. Notwithstanding that, the Court of Appeal judges in *Snook* did not base their decisions upon the ground of reasonableness in respect of the finding of sham, but simply interfered with how the Country court judge entertained the facts. Comparing this to how the appeals system operates in tax cases, seems illogical.

D Snook's Formulation of Sham

It is not until the Diplock LJ's well-known dictum in *Snook* that a clear guided sham test has been well accepted and regarded as a universal set of criteria. This most frequently cited description of sham is:

> "...means acts done or documents executed by the parties to the 'sham' which are intended by them to give to third parties or to the Court the appearance of creating between the parties legal rights and obligations different from the actual legal rights and obligations (if any) which the parties intend to create. One thing I think, however, is clear in legal principle, morality and the authorities....that for acts or documents to be a 'sham', with

[32] Lee, above n 17, 385.
[33] Lee, above n 17, 385.

whatever legal consequences follow from this, **all the parties thereto must have a common intention that the acts or documents are not to create the legal rights and obligations which they give the appearance of creating**. No unexpressed intentions of a 'shammer' affect the rights of a party whom he deceived." [Emphasis added]

The legal meaning of the term is isolated by Lord Justice Diplock. He did so by not referring to the word's ordinary meaning, but solely to the apparent and actual legal rights and obligations. He did not have regard to any synonyms either. Instead, he enunciated a clear legal test with the following elements:

- Acts done or documents executed;
- That appear to others to create legal rights and obligations; and
- The parties intend that the apparent legal rights and obligations are either different from the actual legal rights and obligations; or, there aren't any actual legal rights and obligations.

Recently, the legal test of sham was outlined by her Honour Lady Justice Arden in *Hitch v Stone (Inspector of Taxes)*[34]. This approach is a conclusive guide as to how the legal test of sham should be applied, which strictly follows the Diplock LJ's formulation. It is to be taken as a matter of English law. Arden LJ stated:[35]

"An inquiry as to whether an act or document is a sham requires careful analysis of the facts and the following points emerge from the authorities.

First, in the case of a document, the court is not restricted to examining the four corners of the document. **It may examine external evidence. This will include the parties' explanations and circumstantial evidence, such as evidence of subsequent conduct of the parties.**

Second, as the passage from *Snook* makes clear, **the test of intention is subjective**. The parties must have intended to create different rights and obligations from those appearing from (say) the relevant document, and in addition they must have intended to give a false impression of those rights and obligations to third parties.

Third, the fact that the act or document is uncommercial, or even artificial, does not mean it is a sham. A distinction is to be drawn between the situation where parties make an arrangement which is unfavourable to one of them, or artificial and a situation where they intend some other arrangement to bind them. In the former situation, they intend the agreement to take effect according to its tenor. In the latter situation, the agreement is not to bind their relationship.

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[34] [2001] STC 214.
[35] *Hitch v Stone*, above n 34, 223.

> **Fourth, the fact that parties subsequently depart from an agreement does not necessarily mean that they never intended the agreement to be effective and binding.** The proper conclusion to draw may be that they agreed to vary their agreement and that they have become bound by the agreement as varied (see for example *Garnac Grain Co Inc v HMF Faure & Fairclough Ltd* [1966] 1 QB 650 at 683-684 per Diplock LJ, which was cited by Mr Price).
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> Fifth, the intention must be a common intention (see *Snook*)...." [Emphasis added]

The High Court of Australia took a similar approach in *Equuscorp Pty Ltd v Glengallan Investments Pty Ltd*[36], where the legal meaning of sham was specifically considered. Being the most recent sham case held in High Court of Australia, it has been applied in a number of later cases as the standard Australian legal expression of sham.[37] In this case, the High Court of Australia states:

> "'Sham is an expression which has a well-understood legal meaning. It refers to steps which take **the form of a legally effective transaction** but which the parties intend should not have the apparent, or any **legal consequences**."[38] [Emphasis added]

This formulation is a slimmed-down version of the *Snook* test. Sparser language is used such as the phrase "legal consequences" in instead of "legal rights and obligations" as well as "the form of a legally effective transaction"[39].

The definition of sham referred to by Diplock LJ in *Snook* has been cited with approval by the New Zealand Court of Appeal on a number of occasions[40]. It has been reaffirmed as the legal test in NZ in the recent Court of Appeal case of *Accent Management Ltd v C of IR*.[41]

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[36] [2004] HCA 55. ("*Equuscorp*").

[37] *Halloran v Minister Administering Parks and Wildlife Act 1974* [2006] HCA 3; *NPV W.A. Securities v Interactive Network Services and Anor* [2006] VSC 284; *Palgo Holdings Pty v Gowans* [2005] HCA 28; see Paul Stacey "When are Transactions a Sham" (2006) Vol 44 No10 *Law Society Journal* 59, 60.

[38] *Equuscorp*, as above n 36, [46].

[39] See Stacey above n 37, 61.This arguably precludes the situation that parties executed a sham transaction without the knowledge it is legally ineffective, which is different from the situation where parties genuinely enter into a transaction without knowing the transaction being legally ineffective.

[40] *NZI Bank Ltd v Euro-National Corp Ltd* [1992] 3 NZLR 528; *Mills v Dowdall* [1983] NZLR 154.

[41] [2007] NZCA 230. ("*Accent Management Ltd*")Although Fogarty J considered the argument was now open in light of Lord Hoffmann's approval in *Macniven* of Judge Learned Hand's decision in *Gregory v Helvering* and the adoption in NZ of the *Macniven* decision by Privy Council in Miller v C of IR, the issue of whether the transaction were a sham was not the focus of the hearing before either the Court of Appeal or the Privy Council in *Miller v C of IR*. For present purposes, unless

Although the *Snook* formulation of sham is well accepted in common law jurisdictions, there are still ambiguity around the application of sham as the *Snook* concerned a bill of sale single contract situation, it has limitations when applied to other contexts, such as in the context of sham marriage, trusts and in the tax field, which irrevocable limits the application of sham. This will be discussed later in this paper. Furthermore, some shared viewpoints on sham as a result of the *Snook* formulation of sham being applied as a universal set of criteria also has the effect of narrowing down the application of sham.

E Shared Viewpoints on Sham Narrow down the Application of Sham

Firstly, a clear legal definition of sham is considered to be different from the ordinary meaning, as defined by a dictionary. For example, the High Court of Australia in *Equuscorp*, considered the primary Judge's approach as being wrong because of his departure from the "well-understood legal meaning" of sham. Likewise, by referring to the House of Lords decision in *AG Securities Ltd v Vaughan*[42], the High Court in England in its recent application in *Kensington International Limited v Republic of Congo*[43] confirmed that "sham" does have a meaning in law, that meaning being any attempt to disguise the true character of the agreement with the aim of deceiving the court. This potentially limits the possibilities of a wider concept of sham (such as the concept that sham occurs when form does not follow the reality) than the orthodox *Snook* being accepted.

Second, it is established from authorities that sham means more than artifice, façade and charade. To illustrate this point, in *Equuscorp,* "The primary Judge was wrong to characterise them, as he did by his reference to 'artifice', 'façade' and 'charade' as shams." Furthermore, in the New Zealand Court of Appeal case *Accent Management Ltd*, the Court stated that "The aspect of the case presents two different problems. The first is the artificiality of the transactions and the second is

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there is a new approach adopted by a Court of Appeal or Supreme Court as ratio, the definition of sham in *Snook* remains to be the standard New Zealand legal test of sham. See discussion at CCH New Zealand Electronic Tax Library (Issue 10, November 2005).

[42] [1990] 1 AC 417.

[43] [2005] EWHC 2684. ("*Kensington*")

whether they were intended to create genuine legal obligations". Accordingly, the artificiality of a transaction does not automatically and sufficiently establish a sham on the constituent document as long as each document "had the effect that it purported to have and none of the documents purported "to do something different from what the parties had agreed to do". Likewise, the complexity of a transaction does not give rise in itself its characterisation as a sham. When considering a gift in the form of redeemable preference shares rather than cash to a hospital in *Coppleson v F C of T*[44], Justice Halt observed that "the transaction became complex and elaborate rather than simple and straightforward does not seem to me affect its true nature if in legal form it is a gift and if the parties thereto intended in to be operative according to its tenor". Furthermore, a round-bin of cheques does not give rise to sham, even when no party has funds to meet the amount of the cheques[45] or no real money involved.[46] These shared viewpoints have a negative impact on the application of sham in the tax field, because many tax planning schemes aimed at obtaining tax advantages are complex and artificial. What is clear from these shared viewpoints is that even when a transaction is singular, remarkable and even immoral, it does not indicate a sham. This further limits the application of sham in the tax field.

Thirdly, the reference to "acts" or "documents" (plural) quoted above should not be taken to limit the application of sham to a single-step transaction, or a single step within a transaction. Sham can exist in a situation where some part of a multiple steps transaction is a sham.[47] This illustrate the point that the *Snook*

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[44] (1981) 34 ALR 377, as cited in AH Slater "Sham and Substance" (1999) Vol 28 No4 *Australian Law Review* 197, 207.

[45] *Re Barnett; Perpetual Trustee Co Limited v Barnett*[1969] 2 NSWR 721, see Slater, above n 44, 207.

[46] As established in *R v Connolly* (2004) 21 NZTC 18,844.

[47] *Faucilles Pty Ltd (Trustee for John Karridas Family Trust No 2) v Federal Commissioner of Taxation* (1989) 20 ATR 1712, where the default distribution clause in a trust deed was held to be sham without the entire trust deed being a sham. Page 60, see Stacey, above n 37, 61; *Case* X10 (Dec No 11/2005; TRA No 98/055, 8 August 2005), where the New Zealand Taxation Review Authority found that a "policy contract" was not a performance bond or a policy of insurance. In *Hitch v Stone*, it was held by English Court of Appeal that not only the single 1984 agreement (and the assignment and the related recitals in the 1984 deed) constituted a sham but that the 1984 deed, by which the 1984 agreement was completed as respects the green land, was also a sham.

formulation of sham should not be applied strictly regardless of context as it only concerned a single-step transaction.

Fourth, in tax cases, the concept of sham requires more than that tax may be the motivation for particular transactions, which is illustrated by Megarry J's decision in *Miles v Bull*[48]:

> "A transaction is no sham merely because it is carried out with a particular purpose or object. If what is done is genuinely done, it does not remain undone merely because there was an ulterior purpose [i.e. motive] in doing it."[49]

This is adopted by Tamberlin J in the Australian case *Richard Walter Pty ltd v F C of T*[50]: "Mere circumstances of suspicion do not by themselves establish a transaction as a sham; it must be shown that the outward and visible form does not coincide with the inward and substantial truth". Furthermore, in *Regina v Redpath Industries Limited*[51], the Court observed that taxpayers are not required "to show a 'business purpose' as against a 'tax purpose'" to justify a scheme because the basic principle remains that taxpayers are entitled to organise their affairs so as to minimize their liability for taxes. This is to say, even if the sole purpose of a scheme is to avoid tax, it does not render it a sham. In this situation, it is probably easier to argue tax avoidance instead of sham. This implication also limits the application of sham in the tax field.

Lastly, although when a sham is challenged, the court is not so restricted in excluding extrinsic evidence, it does not extend the limitation of sham in the tax field[52] as it is general for courts to accept any relevant evidence both before and

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[48] [1968] 2 All ER 632, 636.
[49] [1969] 1 QB 258, 264.
[50] (1995) 31 ATR 95, 108, as cited in Slater, above n 44, 208.
[51] [1983] CTC 132; 83 DTC 5117, see Slater, above n 44, 207.
[52] It might be possible to argue in light of the decision of *BNZ Investments Ltd v Commissioner of Inland Revenue* (also cited as *ANZ National Bank Ltd v Commissioner of Inland Revenue*) [2007] NZCA 356, where questions of sham and tax avoidance were involved; the Commissioner may invite the court to look at a much wider context (including similar transactions entered into by other banks) than in normal circumstances. However, this argument is quite weak as what context the courts look at should depend on the situation of each case (for example, the artificiality of the transaction) but not whether sham is alleged.

after the transaction in tax cases. This is evident in Megary J's passage in *IRC v Church Commissioners for England*[53]: "As a matter of principle, I cannot see on what ground it would be right on tax questions to exclude all evidence of negotiations between the parties or other matters extrinsic to the documents that create the contractual obligation."

F The Concept of Mislabelling As an Alternative to Sham

Mislabelling is a line of argument where a document or transaction is given a particular label by the parties, but its real nature and effect is different. It is regarded as a kind of quasi-halfway house between sham transactions and genuine transactions along with self-cancelling transactions, and transactions which have different effect when being interpreted in context than being read from itself.[54]

There are many similarities between sham and mislabeling. They both require courts to examine the true legal substance of transactions but not by nomenclatures parties employed. Intentions of parties are crucial for both of them. As evidenced in *Radaich v Smith*[55], which concerned a dispute as to whether a transaction was a licence, or a lease, McTierman J said:

> "The words 'lease', 'lessor' and 'lessee' ...are entirely excluded from the document, and the term 'licence', and its appropriate mutations, are sedulously applied to the rights purported to be created. This fact is, of course, far from conclusive in favour of the respondents. **It is the substance of the deed that matters**." [Emphasis added]

Winderyer J was of the same view[56]:

> "Whether the transaction creates a lease or a licence **depends upon intention**, only in the sense that it depends upon the nature of the right which the parties intend the person entering upon the land shall have in relation to the land. When they have put their transaction in writing this intention is to be ascertained by seeing what, in accordance with ordinary principles of interpretation, are the rights that the instrument creates. If those rights

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[53] [1974] 3 All ER 529, as cited in Slater, above n 44, 199.
[54] See J Prebble "Criminal Law, Tax Evasion, Shams, and Tax Avoidance: Part II – Criminal Law Consequences of Categories of Evasion and Avoidance" (1996) 2 *New Zealand Journal of Taxation Law and Policy*, 59, 63-66
[55] (1959) 101 CLR, 214; see also the comment of Rich J in *F C of T v Willamson* (1943) 67 CLR 561, 565 that the existence of goodwill depends on the propensities of customers, a matter "not affected by writing words on pieces of paper", as cited in Slater, above n 44, 200.
[56] (1959) 101 CLR 209, 221-222, as cited in Slater, above n 44, 198.

be the rights of a tenant, it does not avail either party to say that a tenancy was not intended. And conversely if a man be given only the rights of a licensee, it does not matter that he be called tenant; he is a licensee."[Emphasis added]

In addition, the onus of proof for both concepts is normally placed on the party wishing to claim sham. In *Northumberland Insurance Ltd (in liquidation) v Alexander*[57] the judge emphasized that a heavy onus laid upon the Official Trustee to prove the transaction is a sham so to displace the natural effect of the documents. However, this is not the case in the tax field.

In tax cases, the onus of proof is governed by legislation[58] as well as common law[59]. The procedure can be summarized as[60]: the taxpayer self-assesses; the Commissioner issues reassessment[61]; the taxpayer must prove the transactions; The Commissioner may allege sham upon some prima facie basis, and cannot simply allege sham on the ground that sham was not disproved; if sham is raised in evidence, the taxpayer must lead evidence to rebut it, but uncontradicted evidence of any party that the transaction was genuine will suffice to rebut the mere suggestion; the matter then becomes one of the balance of probabilities; if that balance is wholly even, the Commissioner will by virtue of the Administration Act succeed[62].

Notwithstanding the similarities, mislabelling has certain characteristics that differentiate it from sham. Mislabelling does not necessarily involve pretence or façade. Rather it is a misdescription or miscatergorisation which can be identified by assessing contractual documents objectively. Courts will enquire into the parties' intention to see whether the label used was a genuine statement or reflection of the

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[57] (1984) 8 ACLR 882 at 888-889, as cited in Andrew Nicol "Outflanking Protective Legislation – Shams and Beyond" (1981) 44 *The Modern Law Review* 21, 28.

[58] Such as in New Zealand, section 190(b) of the Act imposed on the appellants the burden of proving that the assessments were excessive. In Australia, it is governed by ss14ZZK and 14ZZO of the Taxation Administration Act.

[59] *McCormack v F C of T* (1979) 143 CLR 284 and *Macmine Pty Ltd v F C of T*(1979)53 ALJR 362; 9 ATR 638), See Slater, as above n 40, 211. Also see *Commissioner of Inland Revenue v Brown* (1962) NZLR 1091 and *Williams Property Developments Ltd v TR (NZ)* (1977) 3 NZTC 61,202.

[60] Slater, as above n 44, 211.

[61] There is no onus placed by legislation on the Commissioner to show that the assessments were correctly made. Nor is there any statutory requirement that the assessments should be supported by evidence.

[62] Slater, as above n 44, 211. See also *Commissioner of Inland Revenue v Brown* (1962) NZLR 1091.

parties' intention. This is not done in the same manner as associated with sham cases. The courts normally look at the words of the document to find the true nature of the instrument. The courts can, but do not directly consider extrinsic evidence unless necessary, as demonstrated by Lord Cottenham: [63]

> "If the provisions are clearly expressed and there is nothing to enable the Court to put upon them a construction different from what the words import, no doubt the words must prevail: but if the provisions and expressions be contradictory and if there be grounds appearing from the face of the instrument, affording proof of the real intention of the parties, then that intention will prevail against the obvious and ordinary meaning of the words. If the parties have themselves furnished a key to the meaning of the words used, it is not material by what expression they convey their intention."

Moreover, although the onus is on the party attacking the legal substance, it is not so high as that upon him who would assert a sham, as pointed out by Sugarman J in *Ex Parte Robert John Pty Ltd, re Forstars Shoes Pty Ltd*[64], where his Honour quoted Denning LJ's dictum in *Facchini v Bryson*[65]:

> "In the present cases, however, there are no special circumstances. It is a simple case where the employer let a man into occupation of a house in consequence of his employment at a weekly sum payable by him. The occupation has all the features of a service tenancy, and the parties cannot by the mere words of their contract turn it into something else. Their relationship is determined by the law and not by the label which they choose to put upon it. **It is not necessary to go so far as to find the document a sham.** It is simply a matter of finding the true relationship of the parties."[Emphasis added]

Mislabelling is a plant of the same genus as sham in some extent. It gives effect to the parties' real intentions recorded by their legal transactions and does not substitute transactions with a different legal character. In this regard, mislabeling is consistent with sham. Both concepts involve the question of how to properly construct documents by which the transaction is carried out and the exercise of matching the parties' intentions thereafter. The watershed between them can be really difficult to identify, as appears in Dillion LJ's passage in *Welsh Development Agency v Export Finance Co Ltd:* [66]

> "What is said is that in determining the legal catergorisation of an agreement and its legal consequences the court looks at the substance of the transaction and not at the labels which

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[63] *Lloyds v Lloyds* (1837) 1 My & Cr 192.
[64] (1962) 80 WN (NSW) 408 at 414, as cited in Slater, above n 44, 198.
[65](1952) 1 TLR 1386, 1389, as cited in Slater, above n 44, 198.
[66] [1992] BCLC 148, 159.

> the parties have chosen to put on it....Thus the task of looking for the substance of the parties' agreement and disregarding the labels they have used may arise in a case where their written agreement is a sham intended to mask their true agreement. The task of the courts there is to discover by extrinsic evidence what their true agreement was and to disregards, as inconsistent with the true agreement, the written words of the sham agreement...But the question can also arise where, without any question of sham, there is some objective criterion of law by which the court can test whether the agreement the parties have made does or does not fall into the legal category in which the parties have sought to place their agreement."

"It is only where the genuineness of the agreement evidenced by the documents is challenged that it is then necessary to consider whether the substance of the transaction as represented by the documents is not the true substance of the transaction and the documents themselves are a cloak to conceal its true nature."[67] By subjecting the nomenclature, which is the legal form parties employed, to substance, mislabelling in fact does challenge the genuineness of the agreement in respect of the genuineness of the nomenclature used.

As demonstrated above, mislabelling could be utilized as powerful as sham but it does not involve searching parties' intention in the same manner as sham. As a result, it is favoured by the courts over sham in the tax field particularly given the uncertainty between the capital and revenue distinction together with the difficulty of ascertaining parties' intentions especially when corporate bodies in the capacity of taxpayers are involved in disputes.

Thus it can be argued that to some extent, mislabelling, as an alternative, supplants the application of sham in the tax field. The only arena where this would not apply is where the parties intend to create no legal rights and obligations at all. Otherwise, mislabelling can be as powerful as sham. In addition, mislabelling fits into the trend nowadays, which is that the courts endeavour to give business efficacy to commercial transactions.[68] A court will do its best to give effect to parties' intentions by being satisfied that the real intention was to enter into a binding agreement.[69] The courts are not willingly to go behind the clear words,

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[67] *Re Securitibank Ltd (No 2)* [1978] 2 NZLR 136 (CA).
[68] http://www.rossholmes.co.nz/default.asp?sectionid=214#666
[69] *Attorney-General v Barker Bros Ltd* [1976] 2 NZLR 495; unreported decision of Thorp J in *A.G.C v Broadlands Ltd and General Motors Acceptance Corporation (NZ) Ltd v A.G.C* and *Broadlands*

which are the form of agreements; unless there are some facts that indicate inconsistency between the parties' activities and the agreements. Jessel MR said in *Wallis v Smith*:[70]

> "I have always thought and still think that is of the utmost importance as regards contracts between adults – persons not under disability or at arm's length – that the courts of law should maintain the performance of the contracts according to the intention of the parties; that they should not overrule any clearly expressed intention on the ground that the judges know the business of people better than the people know it themselves."

However, contrast this with the concept of sham which invites a court to infer the true nature of the arrangement in an "in substance" manner, mislabelling may still invite the courts to discover the real substance but does not go as far as sham. From this angle, mislabelling appears to be a compromise or evolution of sham by the courts to promote business efficacy to commercial transactions by honouring mislabelled arrangements the intended legal obligations as effective rather than go as far as sham to knock down the whole transaction. This is evident in Denning LJ's speech in *Commissioners of Customs & Excise v Pools Finance Ltd*[71]:

> "This is no new doctrine. In life actions speak louder than words. So they do in law…So, here, these conditions cannot, under the cloak of contract, be allowed to speak that which is false. They cannot assert that black is white and expect the courts to believe it. **The Courts do not willingly go behind the conditions of a contract in this way. They would far rather reconcile the conditions with the transaction as a whole than reject them altogether**. But there does sometimes come a point when they must be overridden."[Emphasis added]

This compromise or evolution of sham by the courts of course, further narrows down the application of sham.

Finance Ltd (Unreported, High Court Auckland A256/80), see http://www.rossholmes.co.nz/default.asp?sectionid=214#666.

[70] (1882) 21 Ch D 243.

[71] [1952] 1 All ER 775, as cited in Slater, above n 44, 198.

G Controversial Elements of Sham and Their Effects to the Application of Sham

1 Common intention and the Snook test

According to Diplock LJ, the notion of a sham is that all parties to the arrangement must be parties to the sham, so a sham involving arrangements between two or more parties necessarily requires that all the parties to the arrangement have knowledge of the sham. It is quite clear from Diplock LJ's words that it is the subjective intentions of the parties that are determinative. Lockhart J spells this out in *Sharrment*. Arden LJ in *Bankway Properties v Pensfold-Dunsford*[72] expressed the same point of view that "a test of common subjective intention applies" to determine whether an agreement can be seen as a sham.

Although Diplock LJ's words appear to be of general application and his dicta has been adopted widely, it must be read with caution. For example, in the context of trust, the fundamental requirement is the settlor's intention to create a trust. Since both rectification and setting aside a deed for mistake require only the settlor's subjective intentions, it seems to be nonsense to require all parties particularly beneficiaries to be parties to the sham given that in some trusts beneficiaries can be indefinite and yet to be identified.[73] The limitation of Snook's test in respect of common intention is illustrated in *Midland Bank Plc v Wyatt*[74]. In that case, Mr Wyatt purported to execute a trust to share his equitable interest in his family home with his wife and their two children to resist the creditors' claims. He and his wife signed a trust deed to declare a trust over their family home. Whether this trust was valid or not depended on a finding as to Mr Wyatt's intention. Although the trust deed was prepared by a solicitor, the solicitor was not informed that the deed was signed by Mr Wyatt and his wife at a party. The lender who refinanced the family home was not informed about the creation of trust either. The judge held that Mr Wyatt had no intention to endow his children with the interest in the family home

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[72] [2001] 1 WLR 1369, 1380, as cited in McFarlane and Simpson, above n 1, 146.
[73] For example, some charity trusts may be set up with a group of beneficiaries yet to be identified.
[74] [1994] EGCS 113.

and therefore the trust was held to be a sham trust. However, there is nothing from the evidence that Mrs Wyatt intended to deceive creditors when signing the trust deed. She gave the evidence that she would have signed whatever was put in front of her without reading it. She was fully unaware of the trust's effect. Hence the requirement of all parties' common intention to sham in *Snook* was clearly not satisfied. In *Case S45*[75], the beneficiary was neither acknowledged of nor advised the alleged distributions. The distributions were not included in the beneficiary's assets upon her death too. It was held that the conduct of the trustee indicated that there was no genuine intention to make a distribution and therefore, the trust was a sham. The requirement of all parties' common intention was not satisfied either.

The need for all the parties' common intention is not so obvious either in the context of a gift. In *Chase Manhattan Equities Ltd v Goodman and others*[76], it is held that for a gift to be a sham, the donee must be a party to the sham. However, the donee does not have to have the same motivation as the donor. It is argued that it was not necessary in this case to apply the *Snook* formulation of sham and impose the requirement of mutuality.[77] It is argued that the court could have looked to the more fundamental requirement that the donor must intend to make a gift.[78] This suggested approach reflected the limitation of sham in *Snook* sense that in the context of gift, what matters is the donor's lack of intent, not mutuality.[79]

In *Skelton v Waisoongneon*[80], a New Zealander married a Thai national. The New Zealander believed the Thai was in love with him. However, he discovered after the marriage that the Thai married him for immigration purposes. The New Zealand applied to the Family Court that the marriage was void. He argued that the Thai had no intention to live with him. Judge Mather held that the marriage was a

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[75] *96* ATC 443, also reported as *AAT case 11,11533* ATR 1128 (AATA).
[76] *Chase Manhattan Equities Ltd v Goodman and others* [1991] BCLC 897, as cited in David Brownbill "When is a Sham is not a Sham" (1993) 2 *Journal of International Trust and Corporate Planning* 13, 16.
[77] Brownbill, above n 76, 16.
[78] See, for example, *Glaister-Carlisle v Glaister-Carlisle* (1968) 112 SJ 215, noted in Crossley Vaines, *Personal property*, 301. See Brownbill, above n 76, 106.
[79] Brownbill, above n 76, 107.
[80] [2002] NZFLR 894.

sham. Judge Mather saw no difference between a sham marriage intended by both parties for immigration purposes and one where one party is genuine but the other regards it as a sham.

This case sheds useful light on tax cases. It should not matter whether a party has actual knowledge or intention to carry the transaction in the manner as the other shammful party does. So long as one party of the transaction treats the transaction as a sham or tax avoidance arrangement, the transaction should be void for tax purposes. This is what happened in *Calkin v C of IR*[81]. In *Calkin*, a woman introduced the taxpayer some lucrative business deals for investments. The taxpayer paid various sums to this woman which he thought to be invested to properties of various kinds. The taxpayer received from time to time, funds said to be the proceeds of the investments. It was not until a cheque "representing" profit was dishonoured that the taxpayer discovered that all the transactions were fictitious. The taxpayer sought to deduct his net loss and the question before the Court of Appeal was whether the taxpayer was "carrying on [a] business". The Court of Appeal held that since a business involved real transactions and the transactions in this case were not genuine, the taxpayer was not entitled to the deduction he sought. In this case, the taxpayer intended to undertake the investments and he did everything he needed from his perspective. He did not have actual knowledge of what actually happened and therefore could not intend the transactions to be a sham. However, the lack of intention or mutuality in this instance did not prevent the Court of Appeal find the transactions were not genuine. This decision, along with the decision of the sham marriage case *Skelton v Waisoongneon,* seems irreconcilable with the requirements set out in the Snook's formulation that all the parties must have common intention to the sham.

Arden LJ also emphsised the importance of not applying the Snook's test regardless of context in *Hitch v Stone.* That case concerned a capital gains tax scheme adopted in connection with the disposal of a farm was concerned. The Commissioners found that only part of the instrument, namely elements in the

[81] (1984) 6 NZTC 61,781 (CA). ("*Calkin*")

documentation recording the transactions between the Hitch family and a tax adviser, fulfilled the requirements of a sham. Arden LJ concluded there are certain exceptions to the Snook's requirement of all the parties' common intention to sham. Her Honour said, "The law does not require that in every situation every party to the act or document should be a party to the sham". The judge believed that the *Snook* test must be read in the context of that case. Since *Hitch v Stone* is concerned with the situation where the document implemented multiple divisible transactions, as opposed to a single transaction in *Snook*, Arden LJ viewed the situation as an exception to *Snook*'s common intention requirement. Where the document reflects a transaction divisible into separate parts and only one certain part is alleged to be a sham, it is not necessary to search all the parties' intention as only the intentions of the parties involved in alleged sham part are relevant. This view is affirmed by the recent decided New Zealand case *Accent Management Ltd.*

In *Accent Management Ltd,* two promoters introduced a remarkable artificial insurance schemes to various taxpayers. Under the structure of the insurance scheme, various insurance policies were offered to different taxpayers. The Court of Appeal affirmed the development in the English case *Midland Bank Plc v Wyatt*[82] by stating:

> "Mr White also referred to us a line of authority that indicates that **a finding of sham may be made against a party to a purported contract who goes along with a shammer either not knowing or not caring whether a transaction is genuine or otherwise not caring what he or she is signing**, see *Midland Bank Plc v Wyatt* [1997] 1 BCLC 242 (HC), *Re Esteem Settlement (Abacus (CI) Ltd as Trustee)*[2003]JLR 188 (Royal Court of Jersey) and *Hitch & Others v Stone*[2001] STC 214 (CA)...we agree with Mr White that the structure of the insurance policy means that **it would be possible on orthodox *Snook* principles to treat the insurance arrangements as a sham** in relation to the taxpayers directly associated with Dr Muir and Mr Bradbury even though, as we have just held, it is not open to the Commissioner now to allege that the other taxpayer were implicated...." [Emphasis added]

This approach also illustrated that the requirement of *Snook*'s test that all parties must have common intention to the sham is under scrutiny. As stated in *Accent Management Ltd*, it is possible to treat part of the insurance scheme, which is the

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[82] [1997] 1 BCLC 242 (HC).

insurance contracts between the two promoters and their associated taxpayers, to be a sham. This does not require a search of other unassociated taxpayers' intention.

Thus, it is apparent that Diplock LJ's formula in *Snook* should not be operated as a universal set of criteria for a sham. Sham is merely part of a court's general inquiry into the correct legal characterisation of an act.[83] The starting point of such inquiry is to consider the factual indicators of the particular legal characterization to be applied.[84] The sham concept comes into play when looking for the intention of a party or parties if the factual indictors include such intention.[85] The concept of sham merely reflects that only genuine manifestation of intention should be taken into account when considering if the necessary factual indicators are present.[86] The finding of sham cannot be justified by any independent set of criteria. To find a sham, courts need to ascertain the genuine intentions of the party or parties in circumstances where the factual indicators show that those intentions are of relevance.[87] If a consequence of ascertaining the intentions does not reflect such genuine intention then a sham exists.[88] Therefore, there is no such a monolithic sham test capable of applying in every situation where a court is concerned with the intentions of a party or parties whose acts are being legally construed.[89] The application of *Snook*'s formulation of sham regardless of context clearly limits the application of sham.

2 *Abandonment*

Another ambiguity around the application of sham is concerned with abandonment. It is suggested the actions of the parties after the execution of the document is of

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[83] Macfarlane and Simpson, above n1, 139.
[84] Macfarlane and Simpson, above n1, 139.
[85] Macfarlane and Simpson, above n1, 139.
[86] Macfarlane and Simpson, above n1, 139.
[87] Macfarlane and Simpson, above n1, 139.
[88] Macfarlane and Simpson, above n1, 139.
[89] Macfarlane and Simpson, above n1, 139.

high relevance where abandonment can be shown. It was explained by the Privy Council in *Narich Pty Ltd v Commissioner of Pay-roll Tax (NSW)*:[90]

> "The first principle is that, subject to one exception, where there is a written contract between the parties whose relationship is in issue, a court is confined, in determining the nature of that relationship, to a consideration of the terms, expressed or implied, of that contract in the light of the circumstances surrounding the making of it; and it is not entitled to consider also the manner in which the parties subsequently acted in pursuance of such contract. The one exception to that rule is that, where the subsequent conduct of the parties can be shown to have amounted to an agreed addition to, or modification of, the original written contract, such conduct may be considered and taken into account by the court (see the *AMP case*[91])."

In *Chase Manhattan Equities Ltd v Goodman*[92] a helpful distinction was drawn by Knox J between, an inquiry into whether or not a document was a sham and any question with regard to the construction of the document. He indicated that the subsequent conducts of parties were only relevant to the former but not to the latter. It is clear that when sham is at stake, the court is not bound by parol evidence rule and it can take into account the subsequent conduct of the parties. This is highly relevant in situations where parties abandon the original agreement and leave it unaltered. Abandonment itself should not be regarded as a sham but abandoning the original agreement and adopting a different one subsequently without altering the original agreement might be challenged as a sham- again it depends on the mutual intention of the parties.

However, it is a very fine line to draw between abandonment of a transaction and (usually informal) adoption of a different one in practice.[93] The subsequent conduct of the parties may be relied on to identify the true nature of the contract made among them. On the other hand, it is conceptually another contention to

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[90] [1983] 50 ALR 417, as cited in Slater, above n 44, 212.
[91] *Australian Mutual Provident Soc v Chaplin* (1978) 18 ALR 385, 392-393.
[92] (1991) BCLC 897, as cited in Lee, above n 17, 391.
[93] As illustrated in *Revlon Manufacturing Ltd v F C of T* (1997) 34 ATR 555, the distinction is hard to draw. See Slater, above n 44, 212.

distinguish genuine abandonment from sham.[94] Nonetheless, since in practical terms the evidence relied upon would be much the same in each case, and it is almost practically impossible to separate a contention of abandonment of an accepted contract from identifying the contractual intention.[95] This situation is referred to in *Sonenco (No 87) Pty Ltd v F C of T*[96]:

> "Haphazard conduct or departures from the provisions of the documentation may, or may not, indicate that the documents do not truly reflect what was intended. What is crucial, for present purposes, is the ascertainment of the parties' real intentions."

In *Mills v Dowdall*, Richardson J explained his view in terms of abandonment:[97]

> "A document may be brushed aside if and to the extent that it is a sham: .... (b) where the document was bona fide in inception but the parties have departed from their original agreement while leaving the original documentation to stand unaltered".

It appears from Richardson J's dicta that there could be a sham in the situation where the parties depart from the original agreement but leave it unaltered. Likewise, as Arden LJ indicated in *Hitch v Stone*, subsequent abandonment cannot be a determinative factor but only an indicator to sham. A distinction should be drawn in the following situations:

1. The parties genuinely entered the arrangement but abandoned/departed from the agreement without amending it. In this situation, the parties' intention are genuine and they became bound by the varied agreement although there is no amendment made;
2. The parties were genuinely entered into an arrangement, but subsequently discovered there are certain ways to gain advantage from a third party by departing from the original agreement and leaving it unaltered. (For example, two students genuinely got married but later intended to get

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[94] *Spunwill Pty Ltd v BAB Pty Ltd* (1994) NSWLR 290 at 304-312 supports this contention. However, the argument was rejected in *FAI Traders Insurance Co Ltd v Savoy Plaza Pty Ltd* (1993) 2 VR 343. See Slater, above n 44, 212.
[95] Slater, as above n 44, 212.
[96] (1992) 38 FCR 555.
[97] [1983] NZLR 154, 159 (CA).

divorced, however, they found out they could get more student allowances by staying together as a married couple than being single. They decided to stay and pretend as married couple despite that they lived in separate bedrooms only as flat mates. The two students arguably became bound by the subsequent agreement, as they are in fact single and living apart).

In my opinion, there is clearly a sham in the second but not the first situation. However, the practical question remains on that how a court may differentiate the subsequent shamming minds from the genuine intentions in the second category?

In *Accent Management Ltd*, New Zealand Court of Appeal said:

> "**An obligation can be genuinely entered into** even though subject to legal or practical defeasance or **entered into on the basis that it might be replaced by another amended obligation… Whether these transactions are shams depends primarily on the states of mind** of Dr Muir and Mr Bradbury as to their genuineness. Given that it is not to their advantage that the transactions be shams, it might be thought a little perverse to them states of mind which are inconsistent with their best interests."

This affirms Arden LJ's view that although subsequent abandonment might be an indicator of sham, what matters in abandonment is the genuineness of the parties' intention.[98] Entering into an arrangement on the basis to replace or amend with genuine intentions, which is identical to the first situation I provided earlier, is not a sham. In contrast, if shammful minds could be found later from evidence, then it is clearly a sham. However, I believe it is extremely hard in practice to ascertain the intentions of parties later so that a sham could be found.

It is obvious that abandonment and sham are two very different legal concepts and Richardson J's dictum in *Mills v Dowdall* cannot be used as authority for holding abandonment as sham without search parties' intentions. This is demonstrated in *Burdis v Livsey*[99]. In that case, a party to a contract was well aware that a term of the contract would not be enforced in practice before entering into the

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[98] This is going to be discussed in the following section.
[99] [2003] QB 36, 65, para 44.

contract. The Court of Appeal held that the term was not invalid because it would not be enforced, as they put it: "Commercial parties may, and often do, choose not to enforce their strict legal rights without intending to create or demonstrate some different state of affairs". As subsequent departures from the original agreement cannot solely relied upon to reflect what was in fact intended, it is not easy to ascertain the parties' real intentions. This results in a situation where it is fairly difficult to find a sham in abandonment cases, and therefore the application of sham in this area is very much limited.

3 Nullity

In *Hadjiloucas v Crean*[100], Mustill LJ suggested there are broadly three situations in which the court may take an agreement otherwise than at its forms:

1. Where the surrounding circumstances show that the arrangement between the parties was never intended to create any legally enforceable obligation;
2. The case of sham in *Snook* case, i.e.: where there is an agreement or series of agreements which are deliberately framed with the object of deceiving third parties as to the true nature and effect of the legal relations between the parties;
3. Where the document does not precisely reflect the true agreement between the parties, but where the language of the document (and in particular its title or description) superficially indicates that it falls into one legal category whereas when properly analysed in the light of the surrounding circumstances it can be seen to fall into another.

The first category is concerned with legal nullity and fiscal nullity while the second category is concerned with the *Snook* criteria where parties intend the substance to be different from its form. The third category is more mislabeling than a sham. There is rather a misdescription or miscatergorisation which doesn't necessarily

[100] [1988] 3 All ER 1008, 1019. See Gammie, as above n 4, 311.

lead to an inquiry into the parties' intentions. It would likely be evident from an objective evaluation of contractual terms and documents.

Nonetheless, I would include the first category as constituting sham given that sham includes situations where parties intend no legal rights and obligations although they appear to create some legal rights and obligations by the documents they execute. Distinctions should be drawn here between the following situations:[101]

(a) Where all parties entered the arrangement being aware that there is no practical possibility that the rights and obligations contracted for can be enforced or performed. The transaction is entered into in order to gain an advantage as against a third party such as the revenue or an Official Receiver. The performance may not be completely legally or physically impossible but rather it would not occur within the powers or intentions of the parties to procure or promote.

(b) The parties entered the arrangement with genuine belief that the transaction will be effective.

The first category provided by Mustill LJ is identical to situation (a) above but different from (b). In the words of Diplock LJ, parties in (a) never intend to create the rights and obligations set out by the agreement but to gain advantage from a third party while situation (b) is only genuinely ineffective transaction. The distinction spelt out by Mustill LJ had the effect of limiting the *Snook* definition of sham to a particular set of criteria, namely the second category but exclude the application of sham from the first category. Thus the concept of nullity has caused the concept of sham in this regard to be restrictive.

III SHAM AND THE FORM AND SUBSTANCE PRINCIPLE

Sham is one of the exceptions allowing courts to depart from the so-called form over substance principle. When sham is challenged, courts will look beyond the

[101] Slater, as above n 44, 204.

legal form of the agreement concerned and examine its substance and reality. As substance can be divided into legal substance and economic substance[102], it is necessary to examine which substance sham doctrine can challenge. Referring back to Diplock LJ's dictum that sham is where parties intend to create different legal rights and obligations than in the agreement, the answer is quite clear that it is the legal substance of the transaction that the courts seek to examine. This is evident in the decision in *Jones v Lipman*[103] where it is suggested that it is the company's legal substance and not economic substance that the court was prepared to concentrate on, before holding that the companies were a sham used to conceal the true facts. This is affirmed by a recent decision *Kensington*.

It might be open to argument that by disregarding the corporate veil, legal substance could not be properly ascertained given in law, a corporate body is treated as an independent legal entity. As case law illustrated, once a company is properly registered and observes all the compliance obligations imposed by statute, it continues to exist as a legal entity and the company itself is a reality and not a sham.[104] The sham exception to pierce the corporate veil is only used when the court does not accept a legitimately incorporated entity at face value on the basis that it acts as a front to mask the real operations.[105] In this sense, the corporate body is merely used as a sham device or means to hide the real purpose of the controller, just like a sham trust. The concept of sham is not merely following what legal obligations were created by parties, but characterises the real legal rights and obligations in reality considering other parties' conduct and surrounding circumstance, Furthermore, as Cooke J in *Kensingto*n held, before any corporate veil is pierced, an element of impropriety or dishonesty is required and the corporate veil may only be pierced when the corporate structure is used to avoid

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[102] John Prebble, "Avoidance and Other Consequences of Publishing Commissioner's Interpretation Guideliness" (2004) 19 Australian Tax Forum 245, 247.
[103] [1962] 1 WLR 832, see Anil Hargovan "Piercing the Corporate Veil on Sham Transactions and Companies" (2006) 24 Company and Securities Law Journal 436.
[104] *Peate v Federal Commissioner of Taxaion* (1964) 111 CLR 443.
[105] *Gilford Motor Co Ltd v Horne* [1933] Ch 935; *Jones v Lipman* [1962] 1 WLR 832; *Creasey v Breachwood Motors Ltd* [1992] BBC 638; *Artedomus (Aust) Pty Ltd v Del Casale* [2006] NSWSC 146, see Hargovan, above n 103, 440.

existing (not future) obligations and liability. This affirms the view established by previous authorities[106] that it is legitimate to use corporate structure to avoid future obligations and liability. This draws a useful analogy to tax cases. If a tax planning scheme is purported to be used to gain future tax advantage it should be legitimate, whereas current existing corporate structures or schemes to obtain tax advantage would be a sham. However, as discussed later, instead of planning ahead and getting a specific designed scheme, very few taxpayers would have incentives to subject themselves to severe criminal evasion penalties by using a current corporate structure or scheme not designed for gaining tax advantages. Therefore, although the concept of sham can be very powerful to pierce the corporate veil, it does not extend its application in the tax area.

In the tax field, the form and substance (economic substance) issue is never ever an easy problem. It is envisaged that the source of the problem is that the tax laws can only have a limited number of terms, but these terms must be applied to an unlimited range of transactions.[107] The terms are analogized as the art created by statutes to impose their own form on the world as well as reflecting the world.[108] The problem with form and substance (economic substance) is that in tax law, "life" imitates "art".[109] The same ends could be reached with so many ways of engaging in transactions, but with different tax liabilities.

In common law jurisdictions, the court rejects economic substance and favours legal form. This can be seen from the classic statement of Lord Tomlin in *Duke of Westminster v IRC* [110]:

> "Every man is entitled if he can to order his affairs so that the tax attaching under the appropriate Acts is less than it otherwise would be. If he succeeds in ordering them so as to secure this result, then, however unappreciative the Commissioners of Inland Revenue or his fellow taxpayers may be of his ingenuity, he cannot be compelled to pay an increased tax. This so-called doctrine of 'the substance' seems to me to be nothing more than an attempt to

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[106] Such as *Trevor Ivory Ltd v Anderson* [1992] 2 NZLR 517, see Hargovan, above n 103, 441.
[107] Isenbergh, above n 2, 863-866
[108] Isenbergh, as above n 2, 863-866.
[109] Isenbergh, as above n 2, 863-866.
[110] (1935)19 TC 490, 520.

make a man pay notwithstanding that he has so ordered his affairs that the amount of tax sought from him is not legally claimable".

This so called choice principle assures the legitimacy of taxpayers' arrangements to achieve the same economic equivalent end by using the forms that may gain maximum tax advantage. As demonstrated earlier in this chapter, it is the legal substance that courts will look at to examine whether there is a sham. So long as taxpayers plan their schemes and take steps according to the documents, even if the sole purpose of the scheme is to gain tax advantage, it would not be a sham although it might be subject to a tax avoidance challenge. This illustrates that the concept of sham is enervated and is of very limited application in the tax field. However, the application of the sham doctrine is very different in the United States.

IV USA – AN ALTERNATIVE SUBSTANCE OVER FORM APPROACH

To be considered as a sham in the United States, a so-called substance (economic substance) over form approach is taken. The word "sham" is so used as a word in a wider sense to express "pretence" or "trick". The substance of a transaction is favoured over the form and the form is then said to be a sham. A transaction would be disregarded as a sham for tax purposes if it serves no business purpose other than to provide tax benefits to the taxpayer (subjective test), and offers no reasonable possibility of a profit and thus lacks economic substance (objective test).[111] This is a far wider approach than the approaches taken in Commonwealth jurisdictions.

The case *Gregory v Helvering*[112] is regarded as the leading case for this approach. In this case, the taxpayer owned all the stock of the first corporation, which in turn owned some shares of the second corporation and all the stock of the third corporation. The first corporation transferred all the shares of the second corporation it owned to the third corporation. The first corporation then

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[111] Karen M Cooley and Darlene Pulliam, "IRS, B&D tool up for trial" (2007) 203:5 *Journal of Accountancy* 91(1).
[112] 69 F 2d 809; (1934) affd 293 US 465 (1935).

immediately distributed the stock of the third corporation to the taxpayer. The taxpayer subsequently liquidated the third corporation and sold the shares of the second corporation in its possession. In this way, the transaction met the explicit requirements of the Revenue code for a tax-free reorgnisation. Judge Learned Hand concluded all the transactions were real and had their usual effect but they were not what the statute meant by "reorganisation" for the reason not being part of the conduct of the business of either or both companies. The Supreme Court held this transaction in substance is the same as a simple dividend distribution and the taxpayer should be taxed as such. They held it on the ground that the formulation and distribution of the third corporation had no legitimate business purposes other than tax avoidance. They introduced a new legitimate business purpose requirement into the sham doctrine to safeguard against transactions elevating form over substance.

It is because of the limitation of the application of sham in commonwealth jurisdictions that a wider meaning of sham, modeling the sham doctrine in United States, is frequently argued. Some academics suggested that the wider concept of sham should be used instead of judicial anti-avoidance rules such as *Ramsay*, where the rules have so often been criticised for usurping the powers from Parliament.[113] In addition, some judges like Lord Templeman even developed his own doctrine of pretence[114] because of the enervated sham doctrine.

In *R v Connolly*[115], Fogarty J was of the view that a broad meaning of sham would be possible in New Zealand given that in *Miller v CIR*[116], since the Privy Council adopted the legal method of Judge Learned Hand in *Gregory*, via an adoption to New Zealand of their decision in *MacNiven v Westmoreland*

[113] Lee, above n 17, 389.
[114] Lord Templeman said in *Antoniades v Villiers* [1990] 1 AC 417 "It would have been more accurate and less liable to give rise to misunderstandings if I had substituted the word 'pretence' for the references to 'sham devices' and 'artificial transactions'". From his speech in this case later, he saw pretence as a flexible doctrine, which is not so constrained by the *Snook* definition of sham. This approach enable to disregard terms in an occupancy agreement inserted to sidestep the Rent Acts. This is demonstrated in *Antoniades v Villers*. See Bright, "Beyond Sham and into Pretence" (1991) 11 *Oxford Journal of Legal Studies* 136.
[115] (2004) 21 NZTC 18844.
[116] [2001] 3 NZLR 316.

Investments Ltd[117]. In a tax case where a complicated tax planning schemes are concerned. Applying Judge Learned Hand's methodology, even if the transactions were intended to be real, and if carried out according to intent would have been real, a sham could be found if they were only for the purposes of striving to amount to what parliament intends by certain concepts such as "expenditure".[118] However, despite adopting Judge Learned Hand's methodology, Lord Hoffman in *MacNiven* did not use Judge Learned Hand's concept of sham.[119] Judge Learned Hand's methodology was endorsed only to emphasise the importance of reading concepts in statutes in the sense intended by Parliament. As he said in his speech[120]:

> "My Lord, it seems to me that what Lord Wilberforce was doing in the Ramsay case [1982] AC 300 was no more (but certainly no less) than to treat the statutory words "loss" and "disposal" as referring to commercial concepts to which a juristic analysis of the transaction, treating each step as autonomous and independent, might not be determinative. What was fresh and new about Ramsay was the realization that such an approach need not be confined to well recognized accounting concepts such as profit and loss but could be the appropriate construction of other taxation concepts as well."

Fogarty J's view was rejected in a later case *Accent Management Ltd*, in which the Court of Appeal upheld the orthodox *Snook* principle. The application of sham remains restricted to the *Snook* formulation.

V LIMITED APPLICATION OF SHAM IN THE TAX FIELD

A No Point for Taxpayers to Produce A Sham

Since sham involves dishonesty to conceal transactions from reality, sham in this sense can be seen to mirror the fundamental distinction between tax avoidance and tax evasion. Although sham can be used in a variety of contexts such as inappropriate nomenclature in residency occupancy agreements and employment law, the concept of sham is likely to only apply to the other extreme end of criminal

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[117] [2003] 1 AC 331.
[118] See discussion at CCH New Zealand Electronic Tax Library (Issue 10, November 2005).
[119] See discussion at CCH New Zealand Electronic Tax Library (Issue 10, November 2005).
[120] *Gregory v Helvering*, above n 112, para 35.

deceit. In *F & C Donebus v FCT*[121], which concerned an extraordinary transaction where a taxpayer purchased a domestic refrigerator for $100,000 and resold it for $100, it was said "The doctrine of sham strikes down that which was put up as a mere façade not intended to have legal consequences but to cloak the true transactions. In the present case, the documents of the parties were intended to achieve their stated purpose". Likewise, in *Gilsborne v Burton*[122], Dillon LJ explained when the parties genuinely intended to create complex rights and liabilities disclosed by the documents, the transaction is not a sham.[123]

Now it will be readily perceived that the participants in virtually every tax avoidance scheme will endeavour to ensure that the complex legal structures sought are indeed operated.[124] They would not have the slightest incentive to produce a sham.[125] Although the structures or transactions are highly artificial and contrived, proposed purely for avoiding tax, it is only when the structures and transactions are real and effective that they will get their desired tax treatment.[126] There is no point for the taxpayers to pretend to take the transactions rather than take them. As Lord Steyn said in *IRC v McGuckian*[127], "on the contrary, tax avoidance was the spur to executing genuine documents and entering into genuine arrangements". The defendants, normally advised by tax professionals, should hold the reasonable belief that they would obtain the desired tax advantage only if the transactions were genuine, and that was an excellent reason for inferring that they were genuine. This point is illustrated in *Accent Management Ltd* by the New Zealand Court of Appeal:

> "Whether these transactions are shams depends primarily on the states of mind of Dr Muir and Mr Bradbury as to their genuineness. **Given that it is not to their advantage that the transactions be shams, it might be thought a little perverse to them states of mind which are inconsistent with their best interests**."

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[121] (1988) 81 ALR 635, see Slater, above n 44, 210.
[122] [1988] All ER 759 (CA)
[123] [1988] All ER 759 (CA), 765.
[124] McFarlane and Simpson, as above n 1, 147.
[125] McFarlane and Simpson, as above n 1, 147.
[126] McFarlane and Simpson, as above n 1, 147.
[127] [1997]WLR 991, 1001G-H.

Accordingly, the application of sham in the tax field if fairly limited. There are very few New Zealand tax cases that have found a sham.

B Sham and Anti-Avoidance Provisions

In Commonwealth jurisdictions, it is regarded that although the line between sham and tax avoidance is a fine line to draw, they are conceptually distinct. Sham is given a particular legal meaning by Diplock LJ in *Snook*[128]. The "delicate legal art' of 'avoidance'" is defined as "the attempt by a party or parties to arrange their affairs in such a way as to avoid the application of a particular legal characterisation"[129].

In many commonwealth jurisdictions such as New Zealand and Australia, there is an anti-avoidance rule in tax legislation, which is a kind of substance-focused rule to reverse the form taxpayers used to avoid tax. Richardson J's dictum *Mills v Dowdall* needs to be referred to here:

> "The only exceptions to the principle that the legal consequences of a transaction turn on the terms of the legal arrangements actually entered into and carried out are: (i) where the essential genuineness of the transaction is challenged and sham is established; and (ii) where there is a statutory provision, such as s 99 of the Income Tax Act 1976, mandating a broader or different approach which applies in the circumstances of the particular case."[130]

It is clear from the above passage that first of all, both sham and tax avoidance provisions are exceptions to the form over substance principle; second, the New Zealand Court of Appeal separates out the tax avoidance from the application of sham. Consequently, the argument for a broad meaning of sham as "substance and reality" is untenable, as the anti-avoidance rule would not bring into play any broader meaning of sham than the orthodox *Snook* principle. However, as both sham and tax avoidance provisions are used by Revenue to counter taxpayer's desired results through planning their transactions, the ultimate result is to draw the

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[128] As discussed earlier in this paper.
[129] McFarlane and Simpson, above n1, 135.
[130] [1983] NZLR 154, 159.

line between legitimate and illegitimate tax schemes, as Bowman J described in *Continental Bank of Canada et al. v The Queen:*[131]

> "In cases of this type expressions such as sham, cloak, alias, artificiality, incomplete transaction, simulacrum, unreasonableness, object and spirit, substance over form, bona fide business purpose, step transaction, tax avoidance scheme and, no doubt, other emotive and, in some cases pejorative terms are bandied about with a certain abandon. Whatever they may add, if anything, to a rational analysis of the problem, apart from a touch of colour in an otherwise desiccated landscape, they do not exist in separate watertight compartments. They are all merely aspects of an attempt to articulate and to determine where "acceptable" tax planning stops and fiscal gimmickry starts".

Notwithstanding that, in commonwealth jurisdictions, the concepts of sham and tax avoidance are not correlatives.[132] Nonetheless, what frequently happens is that counsels use the sham argument to colour the eyes of judges so that a conclusion of tax avoidance could be reached.[133] Sham doctrine is developed in common law to recharacterise the legal nature of a transaction when the genuineness is challenged. A sham is inherently ineffective at law. It does not require any legislation to strike it down. This proposition is supported by Isaacs J's words in *Jacques v FC of T*[134], "a sham transaction is inherently worthless and needs no enactment to nullify it." This view was also taken in *Hancock v FC of T*[135] and *Newton v FC of T*[136]. In *Case U32*[137], which is the case decided in TRA before it appealed all the way to Privy Council[138], the TRA found the non-recourse loan was never made, and therefore "this aspect of the transaction was a fraud on the investors and therefore a sham for tax purposes"[139] The TRA also commented that there is no need to use the anti-avoidance rule for the Commissioner to counteract the deductions the investors claimed as the Commissioner was entitled to assess on the real transactions and disregard the fraudulent transaction. In addition, the anti-avoidance provisions apply to actual transactions not sham transactions.

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[131] 1994 DTC 1858, 1866-1867 (TCC). as cited in David Wentzell "Sham and Its Synonyms: a Tour of Landscape" (1995) Vol 42 No6 *Canadian Tax Journal* 1583, 1583-1584.
[132] *Accent Management Ltd*, [59].
[133] *Accent Management Ltd* is a classic example.
[134] (1924) 34 CLR 328, 358.
[135] (1961) 12 ATD 312, 328.
[136] (1958) 11 ATD 187, 225.
[137] (2000) 19 NZTC 9302. That case concerned the film Utu, which is the very successful and profitable one.
[138] *Peterson v C of IR* (2005) 22 NZTC 19,098.
[139] (2000) 19 NZTC 9302, 9310.

However, an opposite view was taken in *Withey v C of IR*[140]. In that case, Mr Withey and Mrs Withey owned a profitable concrete cutting company. They were introduced to a "JG Russel template", and they sold their shares of the company for 1 million dollars to JG's group as a tax loss. This made the profitable company entitled to transfer its profits to the loss group in various means to achieve tax benefits. Mr and Mrs Withey gave evidence that they had no knowledge about the tax avoidance resulting from the transaction. The only reason they entered into the template transaction was to make a capital gain on the sale so that Mr Withey could escape from a physically wearing occupation. Both of their advisors, one accountant and one solicitor, were struck off from the register. Baragwanath J expressed his sympathy to the complaints but nethertheless held the transactions as a sham. Clearly in this case the mutuality requirement of the *Snook* test was not satisfied as Mr and Mrs Withey's had neither knowledge nor intention of the proposed tax avoidance. Baragwanath J stated that the sham transactions fell within the black letter of the anti-avoidance provision (section 99). Since the wording of section 99(2) indicated it focused on the arrangement rather than the objector, the question of the relevance of the state of mind of the objector did not matter. The controlling test in this case according to his honour's view was the purpose of the arrangement, which ought to be determined by the effects of the transaction. In regard to whether section 99 applied to sham transaction or not, Baragwanath J relied on the wording on section 99 (2) that "'Arrangement' means any contract, agreement, plan or understanding **whether enforceable or unenforceable**, including all steps and transactions by which it is carried into effect" (emphasis added) and concluded that the operation of section 99 should not be withheld from sham transactions. Some doubts were cast on this aspect of Withey in *Case U6*[141], and there has been long established doubt about this kind of approach in Australia.[142]

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[140] (1998) 18 NZTC 13,606.
[141] (1999) 19 NZTC 9038, 9057- 9058.
[142] For example, the discussion in *Jacques*, above n 15 and *Hancock v FC of T*(1961) 12 ATD 312. See Income Tax Act 2004 Commentary ITAC-BG 1 [Tax Avoidance] 20051102 5.126 at Brooker Smart Tax.

This view is not easily reconcilable with the statement in the current anti-avoidance provision BG1, according to which a tax avoidance arrangement is void against the Commissioner as there is nothing to be declared to be void in the case of a sham.[143] Neither could this view be reconciled with his Honour's earlier approach expressed in another JG Russell template case, *Miller v C of IR; McDougall v C of IR*[144], in which he cited the dicta of Issacs J[145] and commented:[146]

> "... I am satisfied that s 99 is not at all on the same hierarchical level as sections such as 104, 188 and, as will appear, s 191. It is a section that deals with transactions altogether lawful in terms of the general law and the general provisions of the Income Tax Act but which nevertheless infringe its terms. Section 99 does concern reality and lawfulness, but in a sense is quite different from the general provisions. It begins to bite when their operation is complete."

It is argued that his earlier approach is consistent with the protective nature of section BG1 as this section plays a role to assure the operation of other provisions of the Income Tax Act in accordance with Parliament's intention that other provisions should apply before section BG1.[147] As a sham is inherently worthless, there is no provision that it would otherwise circumvent.[148]

Another interesting point to note is that other than spelling out that the transactions related to the 1987 return were clearly a sham, Baragwanath J made no effort to analyse why the transactions were a sham, nor did he referred to *Snook*'s test or any approach to sham. As the common intention requirement according to *Snook*'s test was obviously not satisfied, it is impossible to reconcile his decision with the *Snook*'s test.

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[143] Income Tax Act 2004 Commentary ITAC-BG 1 [Tax Avoidance] 20051102 5.126 at Brooker Smart Tax.
[144] (1997) 18 NZTC 13,001.
[145] Same as I cited earlier in 129.
[146] *Miller v C of IR; McDougall v C of IR* , as above n 139, 13,027, see Income Tax Act 2004 Commentary ITAC-BG 1 [Tax Avoidance] 20051102 5.126 at Brooker Smart Tax.
[147] Income Tax Act 2004 Commentary ITAC-BG 1 [Tax Avoidance] 20051102 5.126 at Brooker Smart Tax.
[148] Income Tax Act 2004 Commentary ITAC-BG 1 [Tax Avoidance] 20051102 5.126 at Brooker Smart Tax

In a later case *Erris Promotions Ltd v CIR*[149], it was held that three transactions were found to be a sham and also tax avoidance arrangements. This illustrates the point that sham and tax avoidance overlap in a situation where the taxpayer intended the legal rights and obligations to be different from its form, to avoid tax, however, it does not shed any useful light as to whether all sham transactions for tax purposes are ultimately tax avoidance arrangements. In *Peterson*, as stated earlier in this chapter, the TRA found the non-recourse loan in Utu was never made and was therefore a sham. This finding was not overturned by further courts. Ironically, the majority of Privy Council held that it did not constitute tax avoidance. In addition, one important thing to mention is that although as long as a sham is found, the purported transactions can be disregarded, it does not entitle the Commissioner to reconstruct the transaction, which is, to tax another form with the same equivalence. In contrast, if an arrangement is held to be a tax avoidance arrangement, the Commissioner is conferred the power of reconstructing the arrangement. For example, in a situation where a taxpayer claims some sum to be "expenditure" so that it could be deducted against income, the end result to reach is to disallow the deduction. If a sham was found, then the whole transactions will be disregarded and the Commissioner could disregard the deduction. While if the arrangement were held to avoid tax, the Commissioner would reach the same result by reconstructing the transaction, which is to disallow the deduction to be claimed. However, in a situation where the non-resident taxpayer entered into a scheme, which was structured to appear to be an overseas investment but was in fact a loan, to get the dividends overseas to be free of tax[150], the power conferred to the Commissioner will make a difference as the Commissioner would not be able to tax the sum as interests of a loan if a sham rather than tax avoidance were found.

Although there is ambiguity around whether the anti-avoidance provisions apply to a sham or not, it is clear from the above demonstration that a sham cannot

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[149] [2004] 1 NZLR 811; (2003) 21 NZTC 18,330 (HC).

[150] Such as what happened in *BNZI* case. According to conduit regime, the dividends of non-residents derived from overseas are free of tax.

confer the power to entitle the Commissioner to reconstruct the transactions and collect the highest revenue possible as section BG1. Although in some cases sham might be argued to colour the judges' eyes, tax avoidance is certainly a preferable decision rather than a sham from the Commissioner's perspective. This unavoidably limits the application of sham in the tax field.

VI CONCLUSION

Sham has been applied in a variety of contexts, but there is considerable ambiguity around the concept and its application. At one end of the scale, sham is seen in a context of criminal deception, at the other, it is described as an inappropriate form used differently from its legal substance. As an exception to the form over substance doctrine in law, sham is a judicial concept applied by courts to look beyond the form of a transaction; and evaluate the transaction's true legal substance. However, in common law jurisdictions, although arguably it could to be used as the "principal weapon" to "thwart avoidance", sham is found to be enervated especially in tax field. The well-accepted Snook formulation is frequently criticised for diminishing the effectiveness of the concept of sham. A wider meaning of sham has been argued in front of courts.

This paper reflects on the how the legal notion of "sham" has evolved by examining the ambiguity and uncertainty around the meaning of sham as well as its application. The United States economic substance over form approach is set out compared with the United Kingdom/New Zealand's formulistic and conservative approach. Diplock LJ's definition of sham has characterised the word "sham" in a way which is far narrower than the word's ordinary meaning and very limited particularly in the tax field. It should not be regarded as a universal set of criteria for sham. Sham, instead, is courts' inquiry to the act of a party or parties to see if it is consistent with the genuine intention. The wider meaning of sham in a sense is consistent with the sham doctrine but it ignores the essence of sham, which requires intention. Furthermore, in the tax field, as there is every incentive for taxpayers to take every step to get the desired tax treatment, the sham doctrine has little role to

play other than its application to tax evasion. The enactment of general anti-avoidance rules also narrows down the application of the concept of sham in the tax field. Although mislabelling can be seen as a compromise showing the courts' reluctance towards sham, it could be used to some extent as a judicial safeguard. The argument that supports the wider meaning of sham is not tenable and it has been frequently rejected by the courts. The application of sham remains restrictive in the tax field.

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The motivating intention of individual taxpayers irrelevant in a tax avoidance scheme.
Mills v IRC [1975] AC 338.
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Case Y11, Taxation Review Authority, Dec No 9/2007, TRA No 086/05, Hearing: 9, 10 May 2007; Decision: 16 July 2007

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Whether or not a person was an employee or independent contractor:
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Case K77 (1988) 10 NZTC 619.

An instrument can partly be a sham:
Hitch v Stone [2001] BTC 78 (CA).
Accent Management Ltd v C of IR [2007] NZCA 230.
Faucilles Pty Ltd (Trustee for John Karridas Family Trust No 2) v Federal Commissioner of Taxation (1989) 20 ATR 1712
Case W49 [1989] ATC 460.
Faucilles Pty Ltd (Trustee for John Karridas Family Trust No 2) v Federal Commissioner of Taxation (1989) 20 ATR 1712,
Case X10 (2005) 22 NZTC 12,155.

Backdating agreements could be a sham:
Withey v C of IR (1998) 18 NZTC 13,606.

No financial ability or finance never in fact obtained to make the loan may amount to a sham:
Peterson v C of IR (2005) 22 NZTC 19,098 (Case U32 (2000) 19 NZTC 9,302)

It's unfair to lift the corporate veil to expose taxpayer's involvement in the transaction:
Case R1 (1994) 16 NZTC 6,001, also reported as *Case 46* (1993) 18 TRNZ 399.

Sham trust:
Case Y34 91 ATC 332.
Case W48 89 ATC 460 (default provisions of distribution clauses constituted a sham)
Case S45 96 ATC 443, also reported as *AAT case 11,11533* ATR 1128 (AATA).
Faucilles Pty Ltd (Trustee for John Karridas Family Trust No 2) v Federal Commissioner of Taxation (1989) 20 ATR 1712

Manufactured expenditure could be a sham:
20070704 TRA 89/06, Decision 7/2007, Judge Barber

Finding of sham on the facts:
C of IR v Brown [1962] NZLR 1091
Erris Promotions Ltd v C of IR (2003) 21 NZTC 18,330.
AAT Case [2001] AATA 789, Re Owen & Ors and FCT (AAT, Ref: AT2000/27-29,32-47, 51-52, Pascoe SM, 17 September 2001)
Cranstourn v FCT [1984] ATC 4876

Common intention:
Calkin v C of IR (1984) 6 NZTC 61,781 (CA)
Hitch v Stone [2001] BTC 78 (CA).
Accent Management Ltd v C of IR [2007] NZCA 230.

Unhealthy (optimistic) attitude towards tax obligations is not sham:
Glenharrow Holdings Ltd v C of IR (2005) 22 NZTC 19,319.

Grossly inflated price is not a sham:
Glenharrow Holdings Ltd v C of IR (2005) 22 NZTC 19,319
Peterson v C of IR (2005) 22 NZTC 19,098
Indalex Limited v The Queen 86 DTC 6039.
F & C Donebus v FCT (1988) 81 ALR 635

Circular transaction does not necessarily constitute sham:
R v Connolly (2004) 21 NZTC 18,844
Peterson v C of IR (2005) 22 NZTC 19,098
Re Barnett; Perpetual Trustee Co Limited v Barnett[1969] 2 NSWR 721

Parties' inability to meet the cheques does not necessarily render the transaction a sham:
Re Barnett; Perpetual Trustee Co Limited v Barnett[1969] 2 NSWR 721

No real money involved does not necessarily mean the transaction is a sham:
R v Connolly (2004) 21 NZTC 18,844.

Non-recourse loan is not sham:
Peterson v C of IR (2005) 22 NZTC 19,098
20050324 *IRD v Reid*, CRI-2004-054-1469 and CRI-2004-054-1470, Palmerston North, Judge GM Ross

Inept implementation of the scheme did not render the transaction a sham.
R v Connolly (2004) 21 NZTC 18,844
CIR v Gulf Harbour Development Ltd [2005] 2 NZLR 162 (sold RPS instead of membership)

Meaning and application of sham:
Richard Walter Pty Ltd v Commissioner of Taxation(1996) 67 FCR 243; 96 ATC 4550.

Uncommerciality does not amount to a sham:
*Hitch v St*one [2001] BTC 78 (CA); [2001] STC 214.

Artificiality does not amount to a sham
AAT Case [2004] AATA 1041 (AAT, Ref No: WT2002/81, Barton M, 1 October 2004)
DZ v PB Pty Ltd, AAT Ref No: QT97/404, Muller SM, 27 October 1998
R v Redpath [1984] CTC 483.
Coppleson v F C of T(1981) 34 ALR 377.

Transactions bearing a purpose of gaining tax advantage is not a sham:
Australian Mutual Provident Society v Prisk (1987) 9 NZTC 6,015
Marac Life Assurance Ltd v CIR [1986] 1 NZLR 694.
R v Redpath [1984] CTC 483
Inland Revenue Commissioners v Brebner, [1967] All ER 779
Richard Walter Pty ltd v F C of T (1995) 31 ATR 95.

It is not necessary for anti-avoidance rule to be involved to strike down a sham:
Jacques v FC of T (1924) 34 CLR 328.
Hancock v FC of T (1961) 12 ATD 312
Newton v FC of T (1958) 11 ATD 187
Mills v Dowdall [1983] NZLR 154
Finnigan v C of IR (1995) 17 NZTC 12,170
R v Connolly (2004) 21 NZTC 18,844
Case U32 (2000) 19 NZTC 9,302.

Transaction merely reflecting the bargaining positions of the parties is not a sham:
Union Steamship Co of New Zealand Ltd v C of IR (1996) 17 NZTC 12,629.

Whether the interposition of an intermediary company between the employer and the employee was a sham
Enterprise Cars Ltd v CIR (1988) 10 NZTC 5,126; (1988) 11 TRNZ 768 (HC)
TNT Worldwide Express (NZ) Ltd v Cunningham [1993] 3 NZLR 681; (1993) 15 NZTC 10,234 (CA).
Case K10 (1988) 10 NZTC 163.
MNR v Leon [1976] CTC 532; 76 DTC 6299

Whether director can be assessed higher income tax on loans and advances drawn from company:
IRC v Sansom (1921) 8 TC 20
Jacob v IRC (1925) 10 TC 1

Sham is a question of fact, the finding of facts by the Commissioners are binding:
IRC v Garvin [1980] STC 295 (CA)
IRC v Garvin [1981] 1 WLR 793 (HL).
Ramsay v IRC [1981] 1 All ER 865 (HL).
Edwards v Nairstow & Harrison [1956] AC 14
IRC v Sansom (1921) 8 TC 20
Jacob v IRC (1925) 10 TC 1

The Court regretted that the Commissioners did not find the existence of sham when they ought to have:
William v IRC(1980) 54 TC 257
Ramsay v IRC [1981] 1 All ER 865 (HL)
IRC v Sansom (1921) 8 TC 20
IRC v Garvin [1980] STC 295 (CA)

Extrinsic evidence are admissible when issue of sham is raised:
Erris Promotions Ltd v CIR [2004] 1 NZLR 811; (2003) 21 NZTC 18,330 (HC)
IRC v Church Commissioners for England[1974] 3 All ER 529 (talking about generally in tax cases extrinsic evidence is admissible)

Assessing whether partnership was a sham:
Husky Oil Ltd v The Queen - 97-1060(IT)G - 22 December 1998 - Beaubier, JTCC(tax court of Canada)
Case U32 (2000) 19 NZTC 9,302.

Ultimately what matters is the parties' intention as assessed objectively by the courts:
Cranstourn v FCT [1984] ATC 4,876.

Subsidiary's lack of own business purpose other than carrying on transfer for its parent held as a sham:
Dominion Bridge Co Ltd v The Queen [1975] CTC 263; 75 DTC 5150
Richardson Terminals Ltd v MNR [1971] CTC 42; 71 DTC 5028
Lagace v MNR [1968] 2 Ex CR 98; [1968] CTC 98; 68 DTC 5143
MNR v Leon [1976] CTC 532; 76 DTC 6299

Form over substance discussion:
"A Taxpayer" v The Commissioner of Inland Revenue (1997) 18 NZTC 13,350
Tucker v Granada Motorway Services Limited
Henwood v Commissioner of Revenue (1995) 17 NZTC 12,271
Fraser v Commissioner of Revenue (1996) 17 NZTC 12,607
Commissioner of Revenue v New Zealand Refining Company (1997) 18 NZTC 13,187.

Onus of proof:
McCormack v F C of T (1979)143 CLR 284
Macmine Pty Ltd v F C of T(1979)53 ALJR 362; 9 ATR 638.
Commissioner of Inland Revenue v Brown (1962) NZLR 1091
Williams Property Developments Ltd v TR (NZ) (1977) 3 NZTC 61,202
Churchman v Churchman [1945] P 44;[1945] 2 All ER 190
Elsey v FC of T (1969) 1 ATR 389 at 395;121 CLR 99
Steinberg v FC of T (1975) 75 ATC 4221; 5 ATR 565 at 570;134 CLR 640
Buckley & Young v CIR (1978) 3 NZTC 61,271.

Mislabelling (but the effect is the same as sham)
Brent v FCT (1971) 2 ATR 563 (HCA)
F C of T v Willamson (1943) 67 CLR 561, 565 (the discussion about the existence of goodwill)
Ensign Tankers Ltd v Stokes [1992] 1 AC 655.

Abandonment:
Narich Pty Ltd v Commissioner of Pay-roll Tax (NSW) [1983] 50 ALR 417.
Sonenco (No 87) Pty Ltd v F C of T(1992) 38 FCR 555.

Taxation by economic equivalence is impermissible:
Withey v CIR (1998) 18 NZTC 13,606;
CIR v Europa Oil (NZ) Ltd [1976] 1 NZLR 546.
Duke of Westminster v IRC(1935)19 TC 490

Sham is just one means used by Revenue authorities to counteract avoidance:
Continental Bank of Canada et al. v The Queen (1994) DTC 1858

Tax avoidance is concerned genuine transactions:
IRC v McGuckian [1997]WLR 991.
Accent Management Ltd v C of IR [2007] NZCA 230

UK and Commonwealth Sham (non-tax)

Sham trusts:
Genc v Genc [2006] NZFLR 1,119 (FC).(no sham found)
Midland Bank Plc v Wyatt [1994] EGCS 113
Case S45 96 ATC 443, also reported as *AAT case 11,11533* ATR 1128 (AATA)
Re Butlin's Settlement Trust [1976]2 All ER 483 (not a sham case but talk about rectification)

Sham arises when parties use a form which does not fit the reality to deceive a third party:
Bateman Television v Coleridge Finance Co Ltd [1969] NZLR 794, 813 (CA).

Common intention:
Midland Bank Plc v Wyatt[1994] EGCS 113
Chase Manhattan Equities Ltd v Goodman and others [1991] BCLC 897
Equuscorp Pty Ltd v Glengallan Investments Pty Ltd [2004] HCA 55.
Re Esteem Settlement (Abacus (CI) Ltd as Trustee) [2003] JLR 188
Bankway Properties v Pensfold-Dunsford [2001] 1 WLR 1369
Ferris v Weaven [1952] 2 All ER 233
Antoniades v Villiers [1988] 3 All ER 1058(HL).

Sham marriages:
Skelton v Waisoongnoen [2002] NZFLR 894.
Maea v Sharma (2001) 21 FRNZ 400; [2002] NZFLR 382.

Abandonment of contract:
Spunwill Pty Ltd v BAB Pty Ltd (1994) NSWLR 290
FAI Traders Insurance Co Ltd v Savoy Plaza Pty Ltd (1993) 2 VR 343
Sport Australian Pty Ltd v Tallglen Pty Ltd (1998) 44 NSWLR 103
Ryan v Textile Clothing & Footwear Union Australian [1996] 2 VR 235
Garnac Grain Co Inc v HMF Faure & Fairclough Ltd [1966] 1 QB 650
Australian Mutual Provident Soc v Chaplin (1978) 18 ALR 385
Revlon Manufacturing Ltd v F C of T (1997) 34 ATR 555
Mills v Dowdall[1983] NZLR 154, 159 (CA).
Burdis v Livsey [2003] QB 36.
Bhopal v Wahlia (1999) 32 HLR 302.

A sham will not occur simply because a taxpayer adopts one legally available form over another:
Bateman Television v Coleridge Finance Co Ltd [1969] NZLR 794, 813

Corporate veil would be pierced only when sham is an issue:
Salomon v Salomon and Co [1897] AC 22
Lee v Lee's Farming Ltd [1961] AC 12,
Jones v Lipman[1962] 1 WLR 832
Kensington International Limited v Republic of Congo[2005] EWHC 2684.
Peate v Federal Commissioner of Taxaion (1964) 111 CLR 443 (the company itself is a reality and not a sham if properly registered)
Gilford Motor Co Ltd v Horne [1933] Ch 935
Creasey v Breachwood Motors Ltd [1992] BBC 638
Artedomus (Aust) Pty Ltd v Del Casale [2006] NSWSC 146

No halfway house between genuine and sham transactions:
Re Securitibank Ltd (No 2) [1978] 2 NZLR 136.

Occupancy agreements:
Somma v Hazlehurts [1978] 1 WLR 1014.
Street v Mountford [1985] AC 809.
Antoniades v Villiers [1990] 1 AC 417.
Samrose Properties v Gibbard [1958] 1 ALL ER 502 (CA).
Bhopal v Wahlia (1999) 32 HLR 302.
Radaich v Smith (1959) 101 CLR, 214.

Construction of contracts when there is question of mislabelling or sham:
Lloyds v Lloyds (1837) 1 My & Cr 192
Radaich v Smith (1959) 101 CLR, 214.

Lighter onus of proof in mislabelling cases than in sham cases:
Facchini v Bryson (1952) 1 TLR 1386
Bankruptcy v Baker (1995) 3 Insolv LJ 6n

Genuine intended complex rights are not a sham:
Gilsborne v Burton [1988] All ER 759 (CA)

Employment cases:
Ferguson v Dawson [1976] 3 ALL ER 817 (CA).
Thames Television v Wallies [1979] 1 IRLR 136 (EAT)
Massey v Crown Life Insurance [1978] 1 WLR 676 (CA).
Facchini v Bryson (1952) 1 TLR 1386

Bill of Sale cases:
Snook v London West Riding Investments [1967] 2 QB 786.
Re Watson (1890) 25 QBD 27 (CA)
Stoneleigh Finance Ltd v Phillips [1965] 1 All ER 513 (CA)
Lowe v Lombank [1960] 1 All ER 611 (CA)

Estoppel:
Lowe v Lombank [1960] 1 All ER 611 (CA)
Snook v London West Riding Investments [1967] 2 QB 786
Welch v Nagy [1950] a KB 455 (CA).

It is the content rather than printed heading that is the determining factor of litigation privilege:
Whitehill v Glasgow Corp 1915 SC 1015.
Waugh v British Railways Board [1979] 2 All ER 1169 (HL).

There is no sham if transactions took effect with a deliberately purpose to deceive creditors:
Paintin and Nottingham Ltd v Miller Gale and Winter [1971] NZLR 164.

Sham and rectification:
Buchmann v May [1978] 2 All ER 993 (CA)
Investors Compensation Scheme v West Bromwich Building Society [1998] 1 WLR 896. (extrinsic evidence permissible in rectification cases too)

Trends of the courts to give business efficacy to commercial transactions:
Attorney-General v Barker Bros Ltd [1976] 2 NZLR 495.
AGC v Broadlands Ltd and General Motors Acceptance Corporation (NZ) (High Court Auckland A256/80).

Sham may exist at inception or emerge later at abandonment:
Marac Finance Ltd v Virtue [1981] 1 NZLR 586.

Sham may exist only in a part of a transaction:
Re Mill's Declaration of Trust; Midland Bank Executor & Trustee Co Ltd v Mills and Others (1950) 1 All ER 789.

Onus of proof:
Northumberland Insurance Ltd (in liquidation) v Alexander(1984) 8 ACLR 882.

Meaning of sham:
O'Connor v Hume [1954] 2 All ER 301.
Snook v London West Riding Investments [1967] 2 QB 786.
Scott v Commission of Taxation (No 2) (Cth)(1966) 40 AJR 265
Paintin & Nottingham v Miller, Gale & Winter[1971] NZLR 164, 175
AG Securities Ltd v Vaughan[1990] 1 AC 417.
Hadjiloucas v Crean[1988] 3 All ER 1008
Kensington International Limited v Republic of Congo [2005] EWHC 2684.

Sham and the form and substance principle:
Peters v Davison [1999] 2 NZLR 164, 193 Thomas J.
Scott v Commission of Taxation (No 2) (Cth)(1966) 40 AJR 265
Jones v Lipman [1962] 1 WLR 832
Kensington International Limited v Republic of Congo [2005] EWHC 2684.

Unequal bargaining:
Consequeror Properties v Barnes Corporation [1944] 1 KB 96 (DC)

The rule against penalties:
Bridge v Campbell Discount Co Ltd [1962] 1 All ER 385

Gift:
Chase Manhattan Equities Ltd v Goodman and others [1991] BCLC 897.
Glaister-Carlisle v Glaister-Carlisle (1968) 112 SJ 215 (not a sham case, it looks at intentions in the context of gift)

Finding of sham on facts:
Halloran v Minister Administering Parks and Wildlife Act 1974 [2006] HCA 3
NPV W.A. Securities v Interactive Network Services and Anor [2006] VSC 284
Palgo Holdings Pty v Gowans [2005] HCA 28

Extrinsic evidence permissible when a question of sham is raised:
Dickenson v Gross (1927) 11 TC 20
Antoniades v Villiers [1990] AC 417
Sharrment v Official Trustee (1988) 82 ALR 530
Chase Manhattan Equities Ltd v Goodman(1991) BCLC 897.

Mislabelling cases:
Welsh Development Agency v Export Finance Co Ltd [1992] BCLC 148.
Commissioners of Customs & Excise v Pools Finance Ltd [1952] 1 All ER 775.

A court will do its best to give effect to parties' intentions:
Attorney-Generalk v Barker Bros Ltd [1976] 2 NZLR 495
Unreported decision of Thorp J in *A.G.C v Broadlands Ltd* and *General Motors Acceptance Corporation (NZ) Ltd v A.G.C and Broadlands Finance Ltd*
(Unreported, High Court Auckland A256/80)
Wallis v Smith (1882) 21 Ch D 243.

US Sham:

Arbitrage was a sham lacking economic substance:
Compaq Computer Corp v Commissioner of Internal Revenue, Docket No. 00-60648.

Transaction was a sham because it was inconsistent with Parliamentary intention
Knetsch v United States, 364 US 361.

Business purpose test introduced sham doctrine:
Gregory v Helvering 69 F 2d 809; (1934) affd 293 US 465 (1935).

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