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Loans and UPEs – potential for disruption

Commentary by DW Marks QC

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1 COMMENTARY

These are notes from my commentary on the paper by Mr J Byrne prepared for the conference, and which I addressed on Thursday, 16 September.

1.1 Re-characterising items

Fundamental to our practice in this area is *Re Associated Electronic Services Pty Ltd* [1965] QdR 36, 41.4-41.8, a decision of the Full Court of Queensland. Delivering that judgment, Gibbs J said:[1]

> The question remains whether the agreement that the dividend be treated as paid and that the amount of it be lent to the company discharged the company's liability to pay the dividend. There can be an accord and satisfaction where a debtor's promise, rather than the performance of his promise, is accepted in satisfaction of the original cause of action. … In the present case however the agreement between the parties was unsupported by consideration and was not binding. The only promise by the company that can be spelled out of the agreement was a promise to repay the amount … on request. A loan of money repayable on request creates an immediate debt. … But the declaration of the dividend had already created a debt immediately payable by the company to the appellant. … The position of the parties after the agreement had been concluded and the entries had been made in the books was exactly the same as it had been before; all they had done was to give a new label to an existing debt. The company did no more than promise to do something that it was already bound to do, and such a promise was no consideration for the alleged contract.

That was in a case where there was an attempt to recharacterise an amount (showing in the books as a declared but unpaid dividend) as a loan, so that the shareholders were not deferred to other unsecured creditors in the winding up. The shareholders were unsuccessful in that attempt. I say that this is fundamental because it shows that some care must be taken, and some understanding of the law applicable to each of the kinds of transactions under discussion must be applied.

1.2 Whether loan or gift

The proof of whether a payment by one person to another is a loan differs between Australia, on the one hand, and England and New Zealand on the other hand. In Australia we follow what I submit is the principled position that there must be proof of a promise to repay. It is not sufficient (as it is in England and New Zealand) merely to prove payment of an amount. The English case is *Seldon v Davidson* [1968] 1 WLR 1083. In Australia, there are two intermediate appellate decisions, one of which is binding, *Alexiadis v Zirpiadis* (2013) 302 ALR 148. But see the New South Wales Court of Appeal, albeit *obiter dicta*, which is *Gray v Gray* (2004) 12 BPR 22, 755. The position in New Zealand, following the UK position, is spelt out in *Re Matthews* [1993] 2 NZLR 91.

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[1] The whole of the Queensland Reports, and predecessor authorised reports, are located at the Queensland Judgments website, with free access on one-time registration.

A good definition of "gift" is found in *Federal Commissioner of Taxation v McPhail* (1968) 117 CLR 111. The High Court emphasises the need for a transfer of property, and that it be done voluntarily and without valuable consideration. There must be no advantage of a material character conferred on the donor.

1.3 Presumption of advancement

Whether something is a gift, rather than a loan, can also be addressed through the prism of presumption such as the presumption of advancement by a parent in favour of a child, or by a husband in favour of a wife. The former is seen in the recent New Zealand High Court decision of *Comins v The Public Trust* [2021] NZHC 1172, per Mallon J. It points out that the essential feature was the contemporaneous evidence, rather than what was done later: at [22]-[23] and [26].

In fact, that case was determined without application of the presumption of advancement in favour of the child, simply on the basis of the contemporaneous evidence.

In his paper, Mr Byrne refers to recent litigation in the Federal Court of Australia about whether there was a resulting trust in favour of a husband, arising from dealings with land which benefited a wife. The case has since gone on appeal, and the result at trial was reversed recently in *Commissioner of Taxation v Bosanac* [2021] FCAFC 158.

It shows that the presumption of advancement operates "unless 'rebutted' by evidence": at [2]. The presumption was "developed as a result of Courts of equity drawing an inference, from the type of relationship, that the gift was intended as an 'advancement'": [4].

Then at [5], "the presumption of advancement has particular significance where there is little evidence relevant to establishing the intention of the donor or where the Court is unable to reach a positive satisfaction on the issue from the evidence adduced".

But the presumption of advancement "does not preclude an examination of the actual relationship between the parties, or of other facts relevant to the intention at the time of the transaction, when it comes to the question whether the evidence rebuts the presumption": [6].

The presumption is "liable to be displaced or rebutted by evidence, including the circumstances of the particular transaction": [11].

Worryingly, the mere evidence that Mr Bosanac took on a very substantial liability in respect of the property in question appeared to sway the Full Court that he intended to acquire a corresponding beneficial interest in the property: [21]-[22].

This is a concerning development, because that evidence appears very slight indeed, and almost puts the presumption of advancement at nought here.

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2 Div 7A

2.1 Terms used had a heritage

Turning to the terms used in Division 7A of the 1936 Act, I mentioned the useful passages in Pannam, *The Law of Money Lenders in Australia and New Zealand*, 1965, Lawbook Company.

I commend chapters 1-2 of that book which can be obtained easily on application to your local Supreme Court library. The drafter of Division 7A was using well-known expressions, with a heritage in the moneylending legislation.

2.2 UPEs

Turning then to unpaid present entitlements or, "UPEs", the description of these as being equitable obligations of a certain type appears in the unreported decision of *Wood v Inglis* [2009] NSWSC 601 at [62], where it is said that upon distribution, the beneficiary became absolutely entitled to an interest in the trust fund where presenting that distribution. That decision was affirmed on appeal, but the appellant decision does not refer to this particular issue: 2010 ATC ¶20-194.

2.3 Forgiveness

Of course, *inter vivos*, forgiveness must be by deed, and thus in the past when people have given me things of varying quality, such as a mere resolution of a board, a post-it note to a bookkeeper, or entries in books of account, I have had to say that they did not assist. It is essential that legal advice be obtained in documenting a forgiveness.

The issue of forgiveness by Will is somewhat complicated because of a conflict of authorities between Australian and the UK. The precise way this is put in *Re Wedmore* [1907] 2 Ch 277 was that it was a specific gift of the loan concerned to the person intended to be forgiven.

This is significant in cases where the estate is insolvent, or at least unable fully to pay all the gifts prescribed in the Will. In such a case, the forgiveness of the debt will not operate, or will only operate *pro tanto*. The executor must be in a position to call in the unpaid debt, because there may be creditors that must be paid, or there may be priority gifts to be paid. The actual accounting for this will be complex in any case, but the principle is important.

On the other hand, *Re Bone* (1974) 134 CLR 38 seems to state that the forgiveness operated in equity, under the Will, and not as a gift of the debt to the beneficiary.[2]

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[2] The matter related to the extent of the assessable estate for succession duty purposes, and may be influenced by that. *Re Bone* seems to doubt the English authority cited above, but itself has been doubted in Australia since. This leaves the state of the authorities as confused.

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3 Sorting out affairs

3.1 Items held through companies

Turning to steps that might be taken to simplify affairs prior to death, or under the direction of executors after death, I mentioned *Thomas v Arthur Hughes Pty Ltd* (2015) 16 ASTLR 252, as warranting some caution.

This was a case where the so-called “testamentary intention” of a person was purportedly put into effect prior to that person’s death through the offices of the wife, who was a director, and with the assistance of one of the children, an accountant.

No one is reflecting on the actions of the family members here. But the question is to learn from what the court said, as the court has identified warning signs for us..

Looking at the headnote of that case, we see that there was a company of which the wife was a director and shareholder. The child who was an accountant was able to assist. The husband was unable to assist perhaps.

The headnote recounts a finding that the transfers of assets from the company to various trustees of trusts set up for the children were not for the company’s benefit and were disadvantageous to the company.

It is also said in the headnote that the director was in breach of her fiduciary and statutory duties owed by her as director to the company because she entered into transactions which were not for the benefit of the company, and further that she had a conflict between her duty to the company and her personal interest.

Most materially, at paragraph 58 of the decision, it seems that transactions entered into for the purpose of effecting testamentary wishes of shareholders were not entered into for a proper purpose.

It is important that professional advisers avoid being accused of being knowingly concerned in breaches of fiduciary obligations, and there is a question of how far an insurance policy responds to such an allegation. I am not referring to any such problem in the case discussed, and it was certainly not mentioned in the judgment.

3.2 Gifting a UPE by Will

Finally, when it comes to tidying up affairs, it is important to know whether it is possible to give a UPE by Will. Mr Byrne gives a convincing case that it is possible to do so, and I simply add a note to direct reading to the most useful report of the decision in *IRC v Ward* (1969) 1 ATR 287, and see page 300.

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I commend this useful paper by Mr Byrne.

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