[HIGH COURT OF AUSTRALIA.]

JOWETT . . . . . APPELLANT;

AND

THE FEDERAL COMMISSIONER OF TAXATION . . . . . RESPONDENT.

H. C. OF A. 1926.

BRISBANE, *June* 22-25, 27; *July* 5.

Rich J.

Land Tax—Assessment—Crown leases—Unimproved value—Ascertainment—Method of valuation—Land Tax Assessment Act 1910-1916 (*No.* 22 *of* 1910—*No.* 33 *of* 1916), *secs.* 3, 28 (3) (*a*).

Held, by *Rich* J., that, in ascertaining for the purpose of sec. 28 (3) (*a*) of the *Land Tax Assessment Act* 1910-1916 "the unimproved value of the land" where the land is held under Crown leases, (1) the realization value of the supposed fee simple must be found, and not the amount of money which, according to some economic theory, is represented by the land; (2) the process of estimating what the land, if improved under proper conditions, is worth, and deducting what it would cost so to improve it, affords a guide which is evidentiary only, and not conclusive, of the unimproved value in fee simple, and aids in finding only the limit of what a buyer would give; (3) to compute what the land so improved is worth by capitalizing the profits of the operations carried on upon it is fallacious, because in the operations are involved personal exertion, experience and skill, and no allowance is made for these matters; (4) but if there has been a sale upon a walk-in-walk-out basis of a Crown leasehold of the same or comparable lands, the unimproved value of the fee simple may be arrived at by apportionment of the price to the various items, and an appropriate calculation of the fee simple equivalent of the term sold—(method of such calculation discussed); (5) if a method of capitalizing returns from pastoral undertakings in an average year is adopted the percentage taken should in general be at least 15 per cent; (6) the prevention of the growth of prickly pear, not merely its removal, is to be considered an improvement.

APPEALS from the Federal Commissioner of Taxation.

Edmund Jowett appealed to the High Court from amended assessments of him by the Federal Commissioner of Taxation for

H. C. OF A. 1926.

JOWETT v. FEDERAL COMMISSIONER OF TAXATION.

successive years from 1914 to 1922 in respect of the unimproved value of land, including his leasehold estate in several Crown leases in Queensland, comprising very large areas of land used as sheep or cattle stations. The appeals were heard by *Rich* J. For the purposes of the appeals three leaseholds were selected as examples, namely, "Quambatook" and "Bunda Bunda," situated inland from Townsville, and "Foxborough," in the Darling Downs district. Under the terms of the leases and the Queensland Land Acts, the rent payable was that for the time being prescribed by the Land Court, which might fix the rent for successive periods of five years and might do so retrospectively. The leases comprised areas of land portions of which might from time to time be resumed by the Crown.

Owen Dixon K.C., *Macrossan* and *Russell Martin*, for the appellant.

McGill, for the respondent.

Cur. adv. vult.

July 5.

RICH J. delivered the following written judgment:—

This case involves appeals against a number of assessments for the years 1914-1922, in respect of three leaseholds belonging to the appellant, known as "Quambatook," "Bunda Bunda" and "Foxborough." The appellant has many holdings in Australia, some being held in fee simple and others under leases of various tenures. The subject lands are not self-contained stations, but merely depots used by the appellant in his business, described by himself as dealing in sheep rather than grazing. "Quambatook" and "Bunda Bunda" are not breeding, but dry sheep propositions. It is impossible, in these circumstances, to consider them as separate income-making machines and to calculate the actual annual income arising from them. During the hearing I remarked upon the great difficulty of the task set the Commissioner. That is evidenced by the fluctuations in the assessments made by him from time to time; and I reserved my judgment, as I said at the conclusion of the case, not because I had any doubt about it, but because it had been suggested in argument that this

case was typical of a number of other appeals, and I wished to see whether there were any matters as to which I could usefully make suggestions that might serve as a guide to the Commissioner. I pointed out, however, that what Mr. *Macrossan* described as the "three-foot rule" cannot be applied indiscriminately. Each property must be treated separately on its merits.

Before dealing with these appeals I propose to make some general observations which may be of some help to the Department. In the first place, the Department should obtain the services of experts of large practical experience, and give them a free hand, unfettered by departmental rules, to ascertain the values required for the purpose of taxation. The witnesses who gave evidence in this case on behalf of the Department had little or no practical experience in the pastoral industry, and were hampered by departmental rules, which they applied in a rigid and automatic fashion to the valuations in question, without exercising any individual judgment in the matter. I am unable to accept their estimates. I consider that the Department should not have any fixed percentage for capitalizing an undertaking of the hazardous nature of the pastoral industry. In the cases under consideration I think that at least 15 per cent should have been the rate to be applied. It may be that in more favourable districts a lower rate might be proper, but it must be remembered that you are not averaging income over a period of twenty-five to thirty years. This taxation process is concerned with a fictitious income of one year, computed on the basis that the season is reasonably good—a fair average season. It is common knowledge that the risks and hardships attached to the industry are very great. Droughts are periodical and inevitable, involving ruin to those engaged in the industry. Compared with the percentages looked for by buyers of other businesses, where the risks and hardships are inconsiderable, a 15 percentage is not by any means too high.

Now, the problem is to find the unimproved value of the fee simple. One must ascertain the realization value, and not the amount of money which, according to some economic theory, the land represents. I agree with what Mr. *Owen Dixon* said, that from a process of ascertaining what the improved land, as it would be improved under proper conditions, is worth, and deducting the

H. C. OF A. 1926.

JOWETT v. FEDERAL COMMISSIONER OF TAXATION.

Rich J.

cost of improving it, you cannot find what the unimproved land would fetch. This process is not conclusive, but is merely evidentiary, and a guide to the solution of the problem, "What would the unimproved land fetch?" It is, as I have said, a guide and helps your mind in setting a limit to what a buyer should give. It leads to ascertaining what is the purchase price of the business as a going concern. If one capitalizes the profits of the operations carried on upon the land, and then makes certain deductions, the residual value is the capital value of the operations and not the unimproved value. In the operations are involved personal exertion, experience and skill, and no allowance is made for the value of these matters. If these were separated out, the capitalization process might more nearly approximate to the unimproved value. In setting to work to capitalize what can be made out of the land, you overlook the fact that the problem set is to ascertain the realization value or how much capital is locked up in the land. I also think that a longer time should be allowed for the erection and completion of improvements on the land, so as to make it income-producing. The time allowed by the valuers for the Department was very short. Mr. Mitchell's estimate was not too liberal. Having regard to the finding I have made of the facts in this case, it is unnecessary to pass judgment upon the important question raised by Mr. *Owen Dixon* as to the applicability of the Act to leases of the character of the subject land. In the circumstances, any opinion I might express on this question would be *obiter*.

I proceed to consider the valuation of the three properties the subject of these appeals.

In the case of "Quambatook" I am not obliged to rely upon any expert opinion, because a conversion value has been found for it in a sale conducted on a business footing. The property was sold for £35,000, walk-in-walk-out. In Exhibit M the price is distributed among the items sold. That distribution was not questioned in any way, and both parties have accepted the allocation of values by the vendor and purchaser as correct. The value placed on the improvements was £10,696—that is what the buyer considered they were worth to him in a transaction where, at the expiration of the lease (at the end of twenty-five years), he

would lose his right to them. It is not the cost of improving the property under proper conditions. The value of the lease was set down at £2,908—that is, a lease with twenty-five years to run—with the added value which the existence of the improvements gave to the unimproved value. The bank rate of interest in 1921 was 7 per cent. The present annual value of £2,908 at 7 per cent, due twenty-five years hence, represents in round figures £249. This sum, added to the rent of £544 per annum, represents what, to the purchaser, was the annual value (£793) for twenty-five years he was giving for the property in its then condition. That sum, capitalized at 10 per cent—the rate adopted by the Department when it capitalizes another fixed annual charge, land tax—produces £7,930. Add £10,696 to this sum, and the improved capital value of the land in its actual condition with the existing improvements is arrived at, namely, £18,626. The next step is to subtract the cost of improving the property, and I take Mr. Mitchell's estimate, £18,250. The result is the unimproved value of the land, and it then appears that there is no lessee's estate in this land. This had already been shown when the figure of £7,930 was arrived at, because 4½ per cent of that does not exceed the annual rent (£544) reserved by the lease (sec. 28 (3) (*a*)). The difference between the value and the rent is in favour of the lessee, and consequently there is no taxable value of the land. The same result would follow if, instead of 10 per cent, one were to take 7 per cent, the bank rate of interest, to capitalize the annual value arrived at; but I think that 10 per cent is the rate that should be adopted. A sale of the subject land, or of comparable land, affords the best means of arriving at the fee simple value of any land, and in any other cases similar to this the Commissioner should adopt the method I have already indicated, and so solve the problem set by the Act.

Next, as to "Bunda Bunda":—It is, I think, for all practical purposes comparable with "Quambatook," and applying to "Bunda Bunda" the result of this sale of the equivalent property, "Quambatook," there results a sum which shows no taxable value, but a sum below that which at 4½ per cent would exceed the rent reserved. The result of the sale is not that there is no unimproved value on the properties, but that there is no statutory value in

H. C. OF A. 1926.

JOWETT v. FEDERAL COMMISSIONER OF TAXATION.

Rich J.

the land, because 4½ per cent of the unimproved value is less than the rent reserved by the lease. The result obtained from the realization sale of "Quambatook" is borne out by the capitalization process which I have said I regard as showing what is the largest amount a buyer should give for the land. In this process I rely on the evidence of the appellant's witnesses, and I have taken Mr. Mitchell's figures, which show that there is no lessee's estate in the land. No useful purpose will be served in criticizing the evidence or analyzing the figures, as they form no guide in other cases.

"Foxborough" stands on a different footing. There is no evidence of a sale of it, or of any land comparable with it. It is infested with prickly pear. The view presented by the respondent, that the clearing of prickly pear is to be ignored, is clearly wrong. Mr. *McGill* referred me to an unreported decision of *Ferguson* J. which, if I rightly understand it, is to the effect that, although the removal of the pear is an improvement, the prevention of its growing is not. I venture to disagree with that opinion. The freedom of the land from prickly pear must be treated as an improvement. If the growth of the prickly pear had not been checked by early removal, what would be the condition of the land? Would the price of the land be any different if the prickly pear which would have been there had not been stopped from growing? The expenditure of keeping the pear down on "Foxborough" gives the land its present value. If the expenditure had not been made, the land would not have its present value. The *Land Tax Assessment Act*, sec. 3, says that you must regard the land as if the improvements had not been made. If the prickly pear had not been constantly eradicated the land would have been unimproved, and covered with prickly pear.

"Now, what he" (the valuer) "has to consider is what the land would fetch as at the date of the valuation if the improvements made had not been made. Words could scarcely be clearer to show that the improvements were to be left entirely out of view. They are to be taken, not only as non-existent, but as if they never had existed. . . . Here is a plot of land; assume that there is nothing on it in the way of improvement; what would it fetch in the market?" (*Toohey's Ltd.* v. *Valuer-General* (1)). The decisions in the High

(1) (1925) A.C. 439, at p. 443.

Court—such as *Commissioner of Land Tax* v. *Nathan* (1), *Morrison* v. *Federal Commissioner of Land Tax* (2) and *McDonald* v. *Deputy Federal Commissioner of Land Tax* (3)—are in line with this opinion of the Privy Council. Assuming the removal of the pear is an improvement and, instead of supposing the improvement not to have been made, you deduct the value of the improvement from the improved value of the land, you are acting contrary to the section of the Act and the decisions of the Privy Council and of this Court. I consider, then, that there is no lessee's estate in land given up entirely to prickly pear. Moreover, assuming that prickly pear had not been allowed to grow to a greater extent than at present, Mr. Mitchell's figures, upon which I rely, also show that there is no taxable value in the land. The result, in these cases, is not surprising when the legislation of the Queensland Parliament is taken into account. Its intention was to extract the full rack or economic rent out of the land and, when the Court appointed by the Queensland Act has determined the rent payable, there is nothing left for the Federal Act to operate upon, because $4\frac{1}{2}$ per cent of the unimproved value of the land would not exceed the rent under the lease.

I allow the appeal, with costs, including the costs of the shorthand notes, and order the assessment of the appellant to be varied in each year by striking out the value of the lessee's estate in "Quambatook," "Bunda Bunda" and "Foxborough." The respondent having also consented to "Dirri Dirri," "Amelia Creek" and "Manabudgerie" being struck out, I order accordingly, and adjourn the question of costs as to "Mt. Marlow," "Eastmere" and "Berrimpa." The assessment should be adjusted in accordance with this order.

Order accordingly.

Solicitors for the appellant, *Whiting & Byrne*, Melbourne, by *Cannan & Peterson*.

Solicitor for the respondent, *Gordon H. Castle*, Crown Solicitor for the Commonwealth, by *Chambers, McNab & McNab*.

(1) (1913) 16 C.L.R. 654. (2) (1914) 17 C.L.R. 498.
(3) (1915) 20 C.L.R. 231.