[HIGH COURT OF AUSTRALIA.]

TRAUTWEIN . . . . . APPELLANT;

AND

THE FEDERAL COMMISSIONER OF TAXATION RESPONDENT.

THE KING

AGAINST

THE FEDERAL COMMISSIONER OF TAXATION;

EX PARTE TRAUTWEIN.

[No. 2.]

H. C. OF A. 1935-1936.

SYDNEY, 1935, *Nov.* 18, 25, 29; *Dec.* 2-5, 9-13.

1936, *Feb.* 17, 18; *May* 11; *Sept.* 9.

Evatt J.

Income Tax (Cth.)—Assessable income—"Proceeds of any business carried on by the taxpayer"—"Business"—Horse-racing and betting—Interests in hotels—Sale—Proceeds—Penalty—Additional tax—Validity of section—Income Tax Assessment Act 1922-1934 (*No.* 37 *of* 1922—*No.* 18 *of* 1934), *sec.* 67.

A taxpayer, who owned or controlled several hotel businesses, had for many years been interested in racing and interested from the point of view of money-making. He devoted a substantial amount of time, trouble and organizing effort to acquiring what he could from the sport. He established a stud farm for the purpose of breeding racehorses. He raced his own horses and horses under lease. He paid large sums of money in the purchase of horses in order to race them. He used the names of other persons in order to obtain better financial results. He attended races regularly. He betted frequently and systematically, carefully selecting the races on which he would bet, and acquired valuable racing information from his trainers and others. He betted in large sums of money, and used agents to bet and to settle for him. From 1915 to 1923 he claimed deductions in his income returns in respect of betting losses.

Held, that the taxpayer's racing and betting transactions throughout the period under review constituted a business, the proceeds from which were assessable income.

Jones v. *Federal Commissioner of Taxation*, (1932) 2 A.T.D. 16, distinguished. *Graham* v. *Green*, (1925) 2 K.B. 37, and *Cooper* v. *Stubbs*, (1925) 2 K.B. 753, discussed.

The taxpayer also regularly bought interests in hotel properties, including hotel licences, for the purpose of selling them at a profit.

Held that, having regard to the number, continuity and extent of these transactions and to the nature of the scheme or enterprise they embodied, this form of the taxpayer's activities amounted to the carrying on of a business, the profits from which were properly treated as income.

Sec. 67 of the *Income Tax Assessment Act* 1922-1934 is not invalid as conferring judicial power on a non-judicial officer.

Trautwein v. *Federal Commissioner of Taxation*; *R.* v. *Federal Commissioner of Taxation*; *Ex parte Trautwein*, *ante*, p. 63, referred to.

APPEAL from the Federal Commissioner of Taxation and ORDER NISI for mandamus.

Theodore Charles Trautwein lodged objections against assessments made by the Federal Commissioner of Taxation in respect of Trautwein's income for the years ended 30th June 1921, 1922, 1923, 1924, 1926 and 1927. The commissioner disallowed the objections and, in accordance with a request by Trautwein, forwarded them, as appeals, to the High Court for determination. The appeals were heard before *Evatt* J., who, upon certain questions of law arising, stated a case for the opinion of the Full Court (1).

An application by Trautwein for a writ of mandamus to compel the commissioner to forward to the High Court as an appeal an objection lodged by Trautwein against an assessment made in respect of his income for the year ended 30th June 1925, and disallowed by the commissioner, was referred to *Evatt* J. by the Full Court.

The material facts are set forth in the case stated (1) and the judgment hereunder.

Mason K.C., *McKell* and *Gain*, for the appellant and applicant.

Lamb K.C. and *Alroy Cohen*, for the respondent.

Cur. adv. vult.

(1) *Ante*, p. 63.

H. C. OF A. 1935-1936.

TRAUTWEIN v. FEDERAL COMMISSIONER OF TAXATION.

THE KING v. FEDERAL COMMISSIONER OF TAXATION; EX PARTE TRAUTWEIN. [No 2.]

Sept. 9.

EVATT J. delivered the following written judgment:—

These are six appeals by the taxpayer against assessments made by the Federal Commissioner of Taxation in respect of the appellant's income for the years ending June 30th, 1921, 1922, 1923, 1924, 1926 and 1927 respectively.

The particular assessments under objection and appeal were made on November 23rd, 1931. In this judgment I am proceeding upon the assumption that the taxpayer's right of appeal in respect of each of the six income years specified is not limited to the amount whereby the amount of income mentioned in the notice of amended assessment of November 23rd, 1931, exceeded the amount of income mentioned in previous notices of assessment or amended assessments. The income year 1925 is in a special position. In view of the method adopted by the commissioner in ascertaining the amount of the income of the seven years, the taxpayer's dealings and affairs in 1925 could not be dissociated from his dealings and affairs during the remaining six years of the seven year period between June 30th, 1920, and June 30th, 1927. Accordingly it was necessary to allow evidence to be given also as to the year 1925, for the transactions of the seven year period could not be fully understood if all reference to that year had been excluded. In view of the close connection between all seven years and the expressed desire of both parties to these appeals, I shall express my opinion upon the objections made in respect of the year 1925 as well as upon the six appeals which are formally submitted for determination.

One general matter will first be dealt with. In April 1930, the commissioner notified a series of assessments to the taxpayer. Subsequently the taxpayer requested the commissioner to reconsider the question of the quantum of his liability to tax in the light of a report proposed to be made by Messrs. Smith, Johnson & Co., accountants, who were then investigating his dealings and affairs. It was plain that to obtain an accurate statement of his financial affairs between 1920 and 1927 was almost impossible because no proper book records or accounts had been kept. In due course the firm made a report dealing with the seven year period mentioned. The figures contained in the report were then taken by the commissioner as a basis for the amended assessments of November 23rd,

1931. Accordingly the taxpayer's appeal, though originally more widely framed in his notice of objection, became confined to both a general and detailed attack upon the commissioner's method of dealing with the accountant's report.

Here I should interpolate that, in taking the report of the accountants as a basis, the commissioner adopted substantially the same method of ascertaining income as the accountants themselves had done. The latter had found it quite impossible to present a complete or accurate account of the dealings of the taxpayer year by year. In the seven years' operations the taxpayer had had many and varied activities, involving the expenditure and receipt of money. He owned or controlled several hotel businesses where profit was derived in the main from the sale of liquor. He also became interested in acquiring and disposing of interests in hotel properties including hotel licences. He was also interested in the breeding and racing of racehorses and he had many transactions in betting both on his own horses and those of other persons. He controlled a number of bank accounts some of them in the names of relations. Those who had been preparing his returns of income for the information of the commissioner would have had a difficult task to perform even if proper books of account had been regularly kept. As it was, the task of reconstruction was practically impossible. Accordingly, in many important matters, both the accountant who had prepared his returns and Smith, Johnson & Co. in their special investigation were compelled to rely upon the taxpayer's vague recollections as to the nature and details of important transactions which could not be verified by independent scrutiny. Therefore, by the year 1930, when default assessments running into very large figures were issued, it had become practically impossible either for the accountants or the commissioner to ascertain the precise income and outgo of the taxpayer during each of the years 1920 to 1927.

In this difficulty, both Smith, Johnson & Co. and the commissioner thought it reasonable to adopt the following method of approach. So far as was possible, they ascertained the actual income receipts of the taxpayer and allocated them to one or other of the seven years. They then entered upon a comparison of the

H. C. OF A. 1935-1936.

TRAUTWEIN v. FEDERAL COMMISSIONER OF TAXATION.

THE KING v. FEDERAL COMMISSIONER OF TAXATION; EX PARTE TRAUTWEIN. [No. 2.]

Evatt J.

total assets of the taxpayer both as at June 30th, 1920, and as at June 30th, 1927. After adding to the resulting amount of accretion of assets an amount representing private and other non-deductible items of expenditure which could not be shown as represented by assets, and after having already (as explained above) allocated each item of income to the year in which it could be definitely stated to have been derived, an unaccounted for accretion of £112,354 was left, accepting for the moment the figures adopted by the commissioner. Not being able to make the allocation of this accretion to any particular year, the commissioner divided it equally between the seven years under review by him. No doubt it was possible, though it would have caused considerable inconvenience trouble and expense, for the commissioner, in respect of each one of the seven years, to have attempted the task of comparing the assets of the taxpayer as at the beginning and as at the end of the income year. As such an attempt was not made, the position was this: it was quite impossible for the appellant to have earned the aggregate sum of £112,354 equally over the seven income years. But in the case before me the appellant failed to prove how, during the seven year period, the accretion of his assets from income sources took place. As a consequence, the appellant failed to establish affirmatively at what figure the income assessed against him in respect of each of the seven years should be fixed. Having regard to the absence of uniformity or even similarity in the derivation of his income receipts and to the *a priori* improbablity, infinitely great, that the income should be earned equally throughout the seven year period, I find that the amount of income included in each of the seven assessments under the method adopted by the commissioner must necessarily be inaccurate. It is also evident that one or more of the assessments must necessarily be excessive and that perhaps six of the seven may be excessive. On the other hand it is equally possible that six out of the seven are inadequate in amount. But the fact remains that the appellant failed to establish affirmatively what was the taxable or assessable income for any one of the seven years.

It was admitted that the commissioner's action in issuing the amended assessments could not be challenged under the time limitations contained in sec. 37 of the Act but whether all or any of the

six assessments under appeal are rendered invalid or unlawful by reason of the adoption of the above method of allocation raised an important question of law involving the construction of secs. 36, 37, 39, 50 and 51A of the Act.

The answer of the Full Court (1) is to the effect that the assessments under appeal are not invalidated by the commissioner's adoption of the method of distributing the seven years' accretion of assets as described above and that the onus of proof resting upon the taxpayer operates against him independently in respect of each separate year's assessment and is unaffected by the fact that, regarded in their totality, the assessments necessarily contain inaccuracy. Accordingly the first and main objection of the taxpayer, which is common to all six appeals, must fail.

Apart from this general objection, three grounds of attack were made upon the assessments under appeal. These were :—

I. That on June 30th, 1920, the taxpayer was possessed of the sum of £34,000 cash in his safe deposit, so that the amount of accretion should be reduced accordingly.

II. That a substantial part of the accretion in question consisted of sums derived from betting transactions which were not derived as the proceeds of any business and which were therefore not income assessable under the Act.

III. That a substantial part of the amount of the accretion of assets was due to profits which he had made, not from conducting any hotel business, but from capital transactions in acquiring or disposing of interests in hotels and hotel licences, such transactions not constituting the carrying on of a separate business.

It is convenient to deal with the three objections in order.

I. The taxpayer's case is that, on June 30th, 1920, he had in his possession in cash at a safety deposit the amount of £34,000. It is necessary to his case that possession at that date should be established as subsequent acquisition of cash can in no way affect the accuracy of the comparison of assets between June 30th, 1920, and June 30th, 1927. The taxpayer called Mr. Barker, a solicitor, to vouch for his possession of cash exceeding £12,000 in amount and I am quite willing to accept Mr. Barker's evidence on the point.

(1) *Ante*, p. 63.

H. C. OF A. 1935-1936.

TRAUTWEIN v. FEDERAL COMMISSIONER OF TAXATION.

THE KING v. FEDERAL COMMISSIONER OF TAXATION; EX PARTE TRAUTWEIN. [No. 2.]

Evatt J.

But his evidence relates to a period several months later than June 30th, 1920. On all the evidence, I am unable to find affirmatively that on June 30th, 1920, the taxpayer had in his possession in cash any definite sum of money. The first occasion upon which the possession on June 30th, 1920, of the £34,000 in cash was asserted by the taxpayer, was in October 1930, ten years after the relevant date. Yet occasions had previously arisen when the taxpayer and the department were in dispute and when an assertion by the taxpayer of the possession of this very large sum of money would naturally have been expected. The taxpayer was extremely vague as to the precise amount. He stated it, at different times, to be "£34,000," "£30,000" and "about £34,000." My impression is that the taxpayer always aimed at retaining in his possession in cash a fairly large sum of money and that it is quite possible that, on June 30th, 1920, as on any other day, he had a large sum of money in cash. But it is just as possible, for instance, that he had an equally large sum of money in cash in his possession on June 30th, 1927, when the septennial period ended and such a fact would be fatal to his present contention. A taxpayer is not compelled, by the income tax legislation, to keep books of account properly audited or authenticated. But in a case like the present when the material date is so distant, the absence of such authentication is apt to shake one's confidence in allegations which are dependent upon the admittedly faulty recollection of a most vitally interested witness.

This brings me to a consideration of the general credibility of the taxpayer as a witness. I cannot venture upon a wholesale condemnation of the appellant as a witness despite the invitation of learned counsel. But in many respects he was an unsatisfactory witness. The two matters going to credit which were most stressed were his connection with the Quinologist litigation before *Gavan Duffy* J. in this court and the Whitehead-Belfield's Hotel litigation before *Harvey* J. in the Supreme Court. In those cases allegations of the utmost seriousness including imputations of systematic perjury and conspiracy were levelled against the taxpayer. In each case the taxpayer gave evidence. But in neither case did the judge presiding find the charges substantiated though in neither case did the judge exonerate the taxpayer from the suspicion of guilt. In each case,

accordingly, the judge's finding was largely governed by the legal onus of proof. In the Quinologist case, the onus of proof was on the side adverse to the taxpayer, so that *Gavan Duffy* J. found in the latter's favour, though, upon an appeal, in which this finding was impugned, the taxpayer found it prudent to compromise with the appellant on terms favourable to the latter. In the Whitehead-Belfield's Hotel case, it was the taxpayer upon whom lay the relevant onus of proof and there *Harvey* J. found against him without either finding him guilty of the serious charges preferred against him or exonerating him.

If I may say so, I think I can understand the difficulty both these learned judges had in either entirely accepting or entirely rejecting the taxpayer's evidence. Before me, his evidence necessarily occupied many days. At time his readiness both in assertion and denial seemed inconsistent with dishonesty and suggestive even of frankness. At others, his apparent frankness seemed to wear the aspect of a more subtle scheme of deception. Accordingly I have scrutinized his evidence with special care. Much of his evidence I have had to discard, not because I am positively satisfied that he was lying but because I was left in doubt as to its truth or accuracy. I find myself therefore in a position analogous to that of the two judges before whom the taxpayer previously gave evidence. Except where it is corroborated by other evidence or by the strength of cogency of the surrounding circumstances, I have not been able to place great reliance upon his testimony, particularly as it relates to such far off events and circumstances.

My finding as to the question of the £34,000 in cash on June 30th, 1920, is adverse to the taxpayer. Although I think that it is possible that he then held a substantial sum of money in cash, it is impossible to say what that sum was. In the circumstances I cannot accept the appellant's first ground of attack upon the assessments.

II. The next question is whether the taxpayer's betting receipts were derived from business. In the case of *Jones* v. *Federal Commissioner of Taxation* (1), which I decided in 1932, a question also arose whether a taxpayer's betting transactions constituted a business so

(1) (1932) 2 A.T.D. 16. [Noted, 6 A.L.J. 201.]

H. C. OF A. 1935-1936.

TRAUTWEIN v. FEDERAL COMMISSIONER OF TAXATION.

THE KING v. FEDERAL COMMISSIONER OF TAXATION; EX PARTE TRAUTWEIN. [No. 2.]

Evatt J.

that he might lawfully deduct his losses from his other income. I discuss *Jones' Case* (1) below.

In the English case of *Graham* v. *Green* (2) it appeared that the taxpayer's sole means of livelihood consisted in backing horses at starting price from his private residence. The question for decision was whether (*a*) the aggregate amounts of the taxpayer's winnings were derived from a trade or vocation, and (*b*) whether they were "profits or gains" within the meaning of Schedule D (1) of the English *Income Tax Act* of 1918. In giving judgment, *Rowlatt* J. said :—

> "What is a bet ? A bet is merely an irrational agreement that one person should pay another person something on the happening of an event. A agrees to pay B something if C's horse runs quicker than D's or if a coin comes one side up rather than the other side up. There is no relevance at all between the event and the acquisition of property. The event does not really produce it at all. It rests, as I say, on a mere irrational agreement" (3).

Rowlatt J. thus concluded that the taxpayer's bets were not "profits or gains" and he proceeded to consider whether the aggregate of the winnings had been derived from a "vocation." He emphasized that the contention that it was a vocation had very startling results, for it would enable a person to acquire a bad habit of betting with bookmakers so as to set off his losses on betting against his profits of industry. He then suggested an interesting contrast with the case of a bookmaker who did undoubtedly pursue a taxable vocation. He said that the bookmaker calculated the odds over a period of time and so arranged his book so that, if possible, the aggregate transactions would show a profit. *Rowlatt* J. considered that the case of a person who merely betted with the bookmaker was different.

> "I do not think he could be said to organize his effort in the same way as a bookmaker organizes his, for I do not think the subject matter from his point of view is susceptible of it. In effect all he is doing is just what a man does who is a skilful player at cards, who plays every day. He plays to-day, and he plays to-morrow, and he plays the next day, and he is skilful on each of the three days, more skilful on the whole than the people with whom he plays, and he wins. But it does not seem that one can find, in that case, any conception arising in which his individual operations can be said to be merged in the way that particular operations are merged in the conception of a trade. I think

(1) (1932) 2 A.T.D. 16. [Noted, 6 A.L.J. 201.]
(2) (1925) 2 K.B. 37.
(3) (1925) 2 K.B., at pp. 39, 40.

all you can say of that man, in the fair use of the English language, is that he is addicted to betting "(1).

The decision in *Graham* v. *Green* (2) was given on March 11th, 1925. Later in the same year, members of the Court of Appeal referred to the question of deriving money from betting transactions, (*Cooper* v. *Stubbs* (3)). *Warrington* L.J. (4) and *Atkin* L.J. (5) both said they desired to reserve for consideration the question whether betting transactions producing revenue to persons engaged in them might not result in profit assessable to taxation.

It is to be noted that *Warrington* L.J., dealing with this question of betting as a trade or vocation, said: "That question, when it arises, will have to be decided on the facts of the particular case" (6). Therefore, in *Jones' Case* (7), I endeavoured to make a close analysis of the particular facts of the case, and I ultimately found, as a fact, that the taxpayer who was also a grazier and who had made some heavy losses in betting was not engaged in betting as a business. It is convenient to repeat what I then said:—

"The appellant said in evidence that in July, 1927, he commenced betting 'as a business,' but, in my view, he is endeavouring to colour, and even to rationalize, his course of conduct, in the light of the point raised with the commissioner by his taxation advisers. He acquired no property in connection with betting at races, he had no business premises, he had no proprietary interest in any horse, he was not a trainer of horses, he kept no books and no records of his wins or losses, he had no bank account of his own at all, let alone any business account, he never hedged in any of his betting transactions, he did not set aside or determine upon any amount of capital outlay for the purpose of 'investment' in his supposed business, he never banked his winnings, he was not a member of any recognized club associated with racing and the trades incident thereto, and the only person he employed was one man for a short time to attend Tattersalls Club and pay his bookmakers upon settling day. With one or two exceptions, the appellant cannot remember the names of the horses upon whose success he wagered large sums of money. When he first claimed the betting losses by way of deduction he stated that his losses were £6,500 for the relevant year. In point of fact they were much greater in amount. In order to prepare a detailed statement, extensive researches had to be undertaken at the public library in order to find out in respect of what meetings the cheques were paid to the bookmakers. When he originally came to reside at Sydney, the appellant was greatly interested in school sport and I think that when he com menced to devote attention to racing upon a larger

(1) (1925) 2 K.B., at p. 42.
(2) (1925) 2 K.B. 37.
(3) (1925) 2 K.B. 753.
(4) (1925) 2 K.B., at p. 769.
(5) (1925) 2 K.B., at p. 776.
(6) (1925) 2 K.B., at p. 770.
(7) (1932) 2 A.T.D. 16. [Noted, 6 A.L.J. 201.]

H. C. OF A. 1935-1936.

TRAUTWEIN v. FEDERAL COMMISSIONER OF TAXATION.

THE KING v. FEDERAL COMMISSIONER OF TAXATION; EX PARTE TRAUTWEIN. [No. 2.]

Evatt J.

scale, the element of sport, excitement, and amusement was the main attraction. He was an obstinate man. When he lost, he betted more heavily and lost more and more. Instead of ceasing to wager, he kept it up until it became first a practice, and then something akin to a mania. Hope and obstinacy always triumphed over bitter experience. He would have been completely ruined financially, but for the intervention of his brother, and the stopping of his cheques. All that I have said can best be summed up by saying that, during the relevant period, the appellant acquired and developed a bad habit which he was in a special position to gratify. I do not think that the gratification of this habit was a carrying on of any business on his part, despite his many bets and his heavy losses " (1).

In my opinion the present taxpayer occupies a very different position to that of the taxpayer in *Jones' Case* (2). From a long time antecedent to the seven years under review, he had become interested in racing and interested from the point of view of money-making. He had begun to devote a substantial amount of time trouble and organizing effort to acquire what he could from the sport. He established a stud farm for the purpose of breeding race horses. He raced his own horses and horses under lease sometimes operating to a very considerable extent. In these racing activities, he used the names of other persons so as to obtain better financial results. He betted frequently and systematically. He attended races regularly over all the years. He carefully selected the races on which he would bet and acquired valuable racing information from his trainers and others. He paid large sums of money in the purchase of horses in order to race them. He used agents both to bet for him and to settle for him. He used to bet in large sums of money, putting as much as £1,000 on a single race. From the years 1915 to 1923 he claimed deductions in his returns in respect of betting losses. It is contended that for him racing was merely a pastime and an amusement and he was, of course, active in the hotel trade. I have no doubt that he obtained enjoyment and amusement and sport from his racing activities especially when he was successful with his horses or in his bets. But it is not possible to find that the element of sport or pastime or amusement either dominated or was the main factor in these transactions. On the contrary, trying to look at the matter over a long period of time and having special

(1) (1932) 2 A.T.D., at pp. 18, 19. (2) (1932) 2 A.T.D. 16.

regard to his employment and organization of all the means of money-making that are associated with the sport of racing including prize money, betting on his own horses, and betting on other persons' horses, I reach the conclusion that, throughout the relevant period, his betting transactions were part and parcel of the carrying on of a horse-racing business by him, such business including systematic betting on his own horses and also those of other persons. It is true that, under the statute law of New South Wales, a contract by way of wagering is void. But of course this does not mean that the law treats such transactions as never having taken place but only means that the policy of the legislature is to prevent the courts of the land from being invoked for the purpose of directly enforcing wagering transactions.

The present case is quite distinguishable from that of *Jones*. Jones had no horses of his own nor did he ever lease any horses. He was not associated with racing at all except as a "punter." His period of betting was extremely limited in point of time and the element of sport, excitement and amusement rather than that of organized effort was supreme. But the case of the present taxpayer is much more analogous to that of the bookmaker himself than to that of the mere punter at starting price who was being considered by *Rowlatt* J. in *Green's Case* (1). Accordingly I find that the proceeds of betting throughout the years 1920-1927 were part of the proceeds of the taxpayer's business. It therefore becomes unnecessary to make any express finding as to the winning doubles relied upon by the taxpayer, though I am far from being affirmatively satisfied that these transactions resulted in the receipts mentioned in evidence or that, even if they did, these receipts were the net gains of betting between 1920 and 1927.

III. The third ground upon which the taxpayer attacked the assessments was that his profits from dealing in hotel properties and licences were of a capital nature and are wrongly included in the aggregate of the 1920-1927 accretion. Thus the question is whether such transactions also amounted to the carrying on of a business. In my opinion the question admits of only one answer. In his evidence the taxpayer kept on insisting that he was not "trafficking"

(1) (1925) 2 K.B. 37.

H. C. OF A. 1935-1936.

TRAUTWEIN v. FEDERAL COMMISSIONER OF TAXATION.

THE KING v. FEDERAL COMMISSIONER OF TAXATION; EX PARTE TRAUTWEIN. [No 2.]

Evatt J.

in hotel properties and licences. But I ascertained that his real objection was to the word "trafficking," to which he seemed to attribute something sinister or illegal. In terms, he admitted that he regularly bought these interests in hotel properties or licences for the sake of turning them over at a profit. Having regard to the number, continuity and extent of these transactions and to the nature of the scheme or enterprise which they embodied I have no hesitation in finding that in the years 1920 to 1927, this form of his activity amounted to the carrying on of a business and the profits derived therefrom were properly treated as income.

Throughout the investigation of the three grounds of objection now discussed and of the question answered by the Full Court, I have assumed in the taxpayer's favour that he is not bound to verify every item in the Smith-Johnson accounts but may, for the purpose of supporting his attack upon the assessments, rely upon the accounts wherever the commissioner has accepted their accuracy. It becomes unnecessary to deal further with this assumption which has been strenuously challenged by the commissioner.

I now proceed to deal with the taxpayer's special ground of attack upon the 1925 assessment because of its omission of the deduction of £16,821 (being the total of the sums of £15,500 and £1,321) as being a sum of money paid by the taxpayer in order to purchase a release of the option agreement for the sale of Belfield's Hotel. The actual litigation was a suit for specific performance brought against his wife by Belfield's Hotel Ltd. and Clarke and Whitehead (who had been his financial advisers). There is little doubt that it was through Whitehead, who had prepared some of his income tax returns, that the taxpayer conceived the idea of trafficking in hotels including Belfield's Hotel which was to be sold by means of the flotation of a public company in a transaction from which the taxpayer was intended to derive a large profit. I accept much of the criticism of counsel that the varying accounts of this affair, as given by the taxpayer, are very confusing. But for present purposes it is, I think, reasonable that the taxpayer should be identified with his wife and that the legal position should be regarded as fairly established by the pleadings and decree in the equity suit. In my opinion, if the taxpayer is to be debited with

the gains he derived from his enterprise in acquiring and disposing of interests in hotel properties, the losses incurred in the business must inevitably be allowed by way of deduction. I see no reason for finding that the sale and repurchase of Belfield's itself should not be regarded as within the ambit of the business of "trafficking" in hotel properties and licences on which the taxpayer had embarked. Accordingly I am of opinion that the taxpayer is in respect of the year 1925 entitled to be allowed the deductions specified.

One matter which was shortly referred to before me was the question of the validity of sec. 67 of the Act so far as it authorizes the commissioner to impose penalties by way of additional tax. The argument that this section unlawfully confers judicial power upon a non-judicial officer cannot be supported, and after reference to *Jolly* v. *Federal Commissioner of Taxation* (1) and *Richardson* v. *Federal Commissioner of Taxation* (2) the point was not pressed.

All other grounds of objection to the assessments under review were abandoned at the outset of the hearing before me but there is one aspect of the present litigation which it is only fair to mention. The question whether a taxpayer should in justice be visited with the payment of additional tax is one upon which an appeal from the commissioner's discretion lay, not to this court but to the board of review. But in considering whether the case was an appropriate one for the infliction of the maximum penalty, the commissioner was necessarily restricted by the facts as they then appeared to him and he had none of the assistance to be derived from such an investigation as had to be undertaken before me. Accordingly, if the matter of penalty is again raised either before the commissioner or a board, an important point may well be, not whether the profits of the taxpayer's business of racing and of hotel trafficking were profits derived from business for that question is answered against the taxpayer by my findings in this appeal; but whether the taxpayer, in omitting to include the amount of such profits in his return, acted in the belief that they at least were no part of his assessable income. It is not to be supposed for a moment that the aggregate profits of these businesses covered all the deficiencies of the return. But something is to be said for the view

(1) (1935) 53 C.L.R. 206. (2) (1932) 48 C.L.R. 192.

H. C. OF A. 1935-1936.

TRAUTWEIN v. FEDERAL COMMISSIONER OF TAXATION.

THE KING v. FEDERAL COMMISSIONER OF TAXATION; EX PARTE TRAUTWEIN. [No. 2.]

Evatt J.

that the omission of betting gains was due to the taxpayer's misunderstanding of a provisional departmental ruling as to the question of betting and that the taxpayer may, as he asserts, have acted upon the once fairly widely accepted notion that profits from sale of property interests were not taxable as income. I should add also that my findings that the taxpayer carried on these activities by way of business is based upon a general conspectus of transactions which was not available either to the taxpayer or to the accountants who prepared his returns. No doubt there are other aspects of the situation which may be regarded as telling against the taxpayer's conduct, but I think that it is only fair to make the above observations.

I desire to express my thanks to counsel in helping me unravel the tangle of this troublesome and complicated affair. I am particularly indebted to Mr. *Lamb* whose searching and relentless cross-examination of the taxpayer was not only invaluable to me but revealed the *modus operandi* of racing men with something of the dogmatism that often accompanies full knowledge.

The result is that each of the six appeals before me will be dismissed. In respect of the year 1925 I express the opinion that the assessment should be reconsidered upon the footing that the taxpayer is entitled to a deduction of £16,821 in respect of the payments made in connection with the Belfield's Hotel litigation. Therefore the application for mandamus need not be dealt with and I stand that matter over generally.

As to costs, the taxpayer must pay the costs of the proceedings before me, and the taxing officer will treat the six appeals upon the footing of their having been consolidated. There will be no order as to the costs of the reference of questions of law to the Full Court or of the mandamus proceedings relating to the year 1925.

Appeals dismissed.

Solicitors for the appellant and applicant, *A. R. Baldwin & Co.*

Solicitor for the respondent, *W. H. Sharwood*, Commonwealth Crown Solicitor.

J. B.