1937 *Present :* **Moseley J. and Fernando A.J.**

WALLES *v.* COMMISSIONER OF INCOME TAX.

S. C. (Inty.) 155—Income Tax.

Income tax—Trainer and dealer in racehorses—Stakes won at races—Separate activities—Stakes not liable to tax—Bad debt—Not capable of being deducted within year of assessment—Income Tax Ordinance, No. 2 of 1932, ss. 6 (1) (a), 9 (1) (d), 13 1 (b) and (c), and s. 74.

Where a person who carried on the business of trading in and training racehorses also indulged in the racing of horses for sport,—

***Held,* that the racing of horses did not form part of the business carried on by him and that the stakes won at the races were not liable to income tax.**

Where the assessee claimed the deduction of a debt under section 9 (*d*) of the Income Tax Ordinance and it was disallowed on the ground that it cannot be regarded as incurred within the period for which profits were ascertained,—

***Held,* that the deduction may be claimed under section 13 (*b*) of the Ordinance.**

THIS was a case stated for the opinion of the Supreme Court under section 74 of the Income Tax Ordinance by the Board of Review constituted under the Ordinance.

The assessee was a veterinary surgeon, a dealer and trainer of racehorses, who also indulged in horse-racing from love of sport. His wife also owned a string of racehorses. The Commissioner of Income Tax held that the racing of horses by the assessee and his wife formed part of the business carried on by him and that the stakes won by his wife and himself were liable to income tax.

The assessee also claimed the deduction of a bad debt which he contended became bad within the year preceding the year of assessment which the Commissioner disallowed.

The assessee thereupon appealed to the Board of Review which held that the racing of horses was an activity that formed part of the business carried on by the assessee the profits of which formed part of an enterprise, which is conducted on commercial lines and therefore fell within profits and income under section 6 (1) (*a*) of the Income Tax Ordinance. On the question of bad debt the Board was of opinion that it was not incurred during the period for which profits are ascertained for the purposes of the assessment.

H. V. Perera (with him *E. G. P. Jayatileke* and *N. M. de Silva*), for assessee, appellant.—The points for decision are :—

(1) Is the activity of horse-racing carried on by the appellant and his wife part of an enterprise carried on on commercial lines thus making the profits and income taxable under section 6 (1) (*a*) of the Income Tax Ordinance ?

(2) Is the Board of Review correct in its view of the alleged bad debt ? Person doing a business must do so habitually. There must also be an element of holding out—an invitation to the public to do business. This has been recognized in the two cases of *Graham v. Green*[1], the case of a man who habitually bets, and *Partridge v. Mallandaine*[2], where a bookmaker was held to carry on a business. Although not expressed the distinction seems to be that in the case of the man who habitually bets he is not taxable because there is no holding out or invitation, while in the case of the bookmaker, he invites the members of the public to take bets with him.

[MOSELEY J.— What of a person who only deals with one person—a Government contractor ?]

A holding out is necessary.

In the case of the *Earl of Derby v. Bassom*[3], the Commissioners of Inland Revenue took up the position that where a person combined a business with a hobby the one could be separated from the other and taxed. The Earl of Derby carried on a racing and a breeding establishment. It was conceded that his racing activities were not taxable but he was liable to tax on the fees received by him by the letting of the services of his stallions.

The same principle should be applied in the case of Mr. Walles. He is taxed on his business as trainer and importer of racehourses but his racing activity should be separated from his business. If it is not done he will be entitled to his losses during the bad years.

The House of Lords took up the same attitude in the case of *Glanely v. Wightman*[4].

The test of separability was laid down in the cases of *Commissioners of Inland Revenue v. Maxse*[5], and *Commissioners of Inland Revenue v. Ransom*[6].

On the second point the debt only became bad when the property purchased on the bond was sold. The property was not purchased as a

[1] *9 Tax Cases 209.*
[2] *2 2 Tax Cases 179.*
[3] *10 Tax Cases 357.*
[4] *17 Tax Cases 131.*
[5] *(1919) 1. K. B. 647.*
[6] *(1918) 2 K. B. 709.*

speculation but to realize the debt due to the appellant. The loss therefore was suffered after the property was sold. A debt is bad at a time when the loss is calculable.

N. Nadarajah, C.C. (with him *Crossette-Thambiah, C.C.*), for Commissioner of Income Tax.—Section 6 (1) (*h*) of the Ordinance enables the taxation of "income from any other source whatsoever". The stakes won would if not caught up by 6 (1) (*a*) be liable under 6 (1) (*b*). The activity of horse-racing is not an independent or separable activity but is part of assesse's business of training and selling horses. This is a question of fact from which there is no appeal. The test of separability does not apply except to cases of super tax.

The terms business and trade are defined by Jessel M. R. in *Smith v. Anderson* [1].

Supreme Court can under section 74 consider only questions of law. The horses of the appellant were run for purposes of his business. This is a finding of the Board of Review which cannot be overruled. The appellant is not entitled to separate parts of his activity from his business which must be treated as a whole. (*Gloucester Railway Carriage & Wagon Company v. Revenue Commissioner* [2].)

The bad debt is one which cannot be recovered from a debtor. The appellant in entering satisfaction of judgment is deemed to have recovered the amount.

H. V. Perera, in reply.

Cur. adv. vult.

February 17, 1937. MOSELEY J.—

This is a case stated for the opinion of this Court under the provisions of section 74 of the Income Tax Ordinance, No. 2 of 1932, by the Board of Review constituted under that Ordinance.

The assessee, Mr. G. N. G. Walles, is a veterinary surgeon, a dealer in horse fodder and saddling and a trainer of racehorses. He also imports and sells horses. According to his own account, since 1920 he has indulged in horse-racing purely from the love of sport and his racing string now numbers twenty-two. His wife has taken up racing on similar lines and now owns nine horses.

For the year of assessment 1933-1934 the assessee was assessed as having an income of Rs. 35,170. He was dissatisfied with that assessment on two grounds, viz.:—

(1) that the stakes won by horses belonging to himself and his wife are not assessable, and

(2) that no allowance had been made for an alleged bad debt of Rs. 6,535, which debt, he contended, became bad within the year preceding the year of assessment and which, he claimed, should be deducted from the assessment or his income.

The assessee appealed to the Commissioner of Income Tax on these grounds.

In regard to the first ground the Commissioner held that the racing of horses by the appellant formed part of the business carried on by him and that the profits thereof were taxable. He held also that the profits

[1] (*1879*) *L. R. 15 Ch. 247.*

[2] (*1925*) *A. C. 469.*

resulting from the racing of horses belonging to the appellant's wife were profits resulting from an enterprise conducted on commercial lines and fell within the meaning of "profits and income" as defined in section 6 (1) (*a*) of the Ordinance.

In regard to the second point the Commissioner held that the debt of Rs. 6,535 became bad not later than December, 1931, at which date the appellant bought in the property of the debtor. He therefore disallowed the deduction, and the appeal on both grounds was dismissed.

The appellant thereupon appealed to the Board of Review who decided as follows :—

"Upon the evidence and the facts stated in the course of the argument we are of opinion that the racing of horses by Mr. and Mrs. Walles is an activity which forms part of the business carried on by Mr. Walles, the profits from which formed part of the profits of an enterprise which is conducted on commercial lines, and therefore fall within 'profits and income' as defined in section 6 (1) (*a*) of the Ordinance.

"On the question of the 'bad debt' we are of opinion that it was not incurred during the period of which the profits have to be ascertained for the purposes of this assessment. It is accordingly disallowed. The appeal is dismissed and the assessment is confirmed".

The appellant is still dissatisfied and has requested the Board to state a case.

Now the decision of the Board on a question of fact is final, unless, I suppose, this Court should be of opinion that there is no evidence to support such finding. It becomes necessary therefor to examine the finding of the Board with a view to ascertaining the dividing line between the finding of fact and the Board's view of the law which should be applied.

It is somewhat difficult to dissect the finding of the Board on the above lines, but if I may be permitted to paraphrase the finding, it seems to me that the question this Court is invited to decide is whether or not the "activity" of racing horses as carried on by Mr. and Mrs. Walles does, for the purposes of section 6 (1) (*a*) of the Ordinance, form part of the business carried on by Mr. Walles.

I think we may take it as common ground that stakes won by an owner who races purely for sport are not liable to taxation under the above mentioned sub-section or any other provision of the Ordinance.

It was urged before us by Counsel for the Commissioner that the racing of horses was an inseparable part of the appellant's business as a trader in horses, and he relied upon the appellant's evidence to the effect that "he imported racehorses, trained them, ran them in races and sold them ; sometimes at a profit and at others at a loss". It was pointed out, no doubt with truth, that the winning of a race enhances the value of a horse and that therefore the running of a horse with a view to winning races was part and parcel of the business of trading in horses.

Does, however, the business of trading in horses negative the possibility of the same person engaging in racing from the love of sports ?

A number of authorities were cited by Counsel for the appellant. I shall refer to a few.

In the case of *Earl of Derby v. Bassom* [1], it was held that where a person kept a racing and breeding establishment as a hobby and also let out to others the services of his stallions, he was liable to pay income tax on the fees received for such services. The facts are on a converse footing to those existing in the case before us, but the case is authority for the proposition that where a commercial proposition is carried on in conjunction with a hobby the profits from the former are taxable.

In *Commissioners of Inland Revenue v. William Ransom & Son, Limited* [2] it was held that where two businesses carried on by the same person were taxable on different bases, and it was possible for the Commissioners to separate one from the other, there was nothing in law to prevent them from doing so. Sankey J. in the course of his judgment said :—

"I can conceive of cases where the two branches of the business of a person or a company are so interlaced that it is impossible to separate them, and, although I express no definite opinion upon the point, it may be that in those circumstances, if the main branch of the business is subject to excess profits duty the whole business is subject to the duty on the ground of the impossibility of separating the main branch from the rest of the business. There, again, the decision would depend very much on the facts of the case. The case where an individual carries on two separate businesses, of which one is liable to the duty and the other is not, is a simple one, but it might be more difficult to arrive at a decision where the one business is ancillary and incidental to the other in such a way as to make them nearly inseparable . . . . "

The principle of severance of businesses was approved in *Commissioners of Inland Revenue v. Maxse* [3].

If I am right in my comprehension of the question which we are asked to decide, I am unable to arrive at any conclusion other than that the pursuit of horse-racing as carried on by Mr. Walles, and *a fortiori* as carried on by Mrs. Walles, forms no part of the business of trading in and training horses. In my view therefore the stakes won by horses belonging to Mr. and Mrs. Walles are not assessable.

We now come to the matter of the alleged bad debt. This was in respect of an account for horse fodder supplied to Mr. Coomber which amounted to Rs. 11,172.89. To secure this sum Mr. Coomber executed a mortgage bond which Mr. Walles put in suit on March 23, 1931. Decree was entered on May 8, 1931, and on December 22 of the same year, Mr. Walles bought in the property for Rs. 7,100 (appraised value) subject to three mortgages. On May 23, 1932, Mr. Walles sold the property for Rs. 45,000. After paying off the three mortgages he had a balance left of Rs. 4,497.58 in his hands. He is therefore still Rs. 6,675.31 out of pocket in respect of Mr. Coomber's debt.

Mr. Walles claims that this amount became a bad debt at the date of the realization of the mortgaged property, *i.e.*, within the year preceding the year of assessment, and should therefore be deducted from the assessment of his income.

The Commissioner, on the contrary, held that it became bad not later than December, 1931, when the appellant bought in the property. The

[1] *42 Times Law Reports 380.* [2] *(1918) 2 K. B. 709*
[3] *(1919) 1 K. B. 647.*

Board of Review contended themselves with expressing the opinion that it was not incurred during the period of which the profits had to be ascertained for the purposes of this assessment.

Now, it does not appear that any steps have been taken to recover the balance due from Mr. Coomber since December, 1931, and unless and until such steps are taken, I do not know how it can be said that the debt is bad. That the date of realization bears no relation to the date at which the debt becomes bad is evidence when it is appreciated that Mr. Coomber's debt would have remained even though the property had realized, for the sake of argument, Rs. 100,000. It seems to me therefore that the claim for deduction is premature and on this point the appeal must fail.

It is, however, apparent that in connection with the realization of the debt the appellant has suffered a pecuniary loss. He bought the property in for Rs. 7,100, and after paying off the money due under the three mortgages the balance remaining in his hands was Rs. 4,497.58. There was therefore a loss on the transaction of Rs. 2,602.42. This loss became apparent on May 23, 1932, and it may be that the appellant is entitled to a deduction in respect of this amount under section 13 of the Ordinance.

In view of these findings the appeal is allowed, the assessment made by the Board is annulled, and the case is remitted to the Board for revision of the assessment as set out above. The appellant, having succeeded on the main issue, will be entitled to a refund of the sum of Rs. 50 deposited by him under section 74 (1) and will also be entitled to his costs of this appeal.

FERNANDO A.J.—

I agree, but would like to add the following:—It was argued before us that in this case, the Board had found against the appellant on the facts, and that the question, whether the racing of horses was a part of the business of the appellant was itself a finding of fact. In view of the provisions of section 74 of the Ordinance, it is, in my opinion, the duty of the Board to set out separately their decisions on the facts, and the questions of law, if any, that arise. The decision in this case as set out by the Board is that " the racing of horses by Mr. and Mrs. Walles is an activity which forms part of the business carried on by Mr. Walles ". The contention for the appellant before the Board as well as before us was that the racing of horses by him and his wife was done purely for sport, and it was contended that the profits of such racing were not liable to be taxed as in England, and as admitted by both parties in the case of the *Earl of Derby v. Basson.*[1] Now it was open to the Board to find that in fact, the racing of horses by Mr. and Mrs. Walles was not done by them for sport, but was a commercial enterprise; that the racing of horses was part of the business of importing and selling horses as contended by Counsel for the Commissioner, and that the horses that they raced were not, as contended by the appellant, the exclusive property of Mr. and Mrs. Walles kept by them for the purpose of racing, but only some of the horses which had been imported by them for the purpose of sale. Such a finding would be a finding of fact, and it may be that in view of

[1] *Times Law Reports 380.*

sub-section (5) of section 74, this Court would not interfere with any such finding of fact. On the other hand, it was open to the Board to find that the racing was done for sport, that the horses kept for racing were other than the horses that were imported and sold, but that nevertheless, the racing done by Mr. and Mrs. Walles was an activity forming part of a business carried on by Mr. Walles, in which event their finding would no longer be a finding of fact but a finding of law, and it would be open to this Court to consider whether such a finding would be correct in law.

Counsel for the Commissioner stated that even on a finding of fact, it was open to this Court to interfere if in fact such finding was not supported by the evidence before the Board. It is clear from the order made by the Board that certain evidence was recorded when the inquiry took place before the Board. The record of that evidence has not been placed before us as such, but in the case stated, there are certain extracts from the evidence of Mr. Walles. If we are to assume that these extracts were the only evidence before the Board, then the question would arise whether the Board was justified in holding that the evidence of Mr. Walles that he raced horses for sport was not true, if in fact they did arrive at such a finding.

The appellant spoke of a number of horses which were owned by him, and which were kept by him for the purpose of racing. He also stated that there was another string of horses belonging to his wife also kept for racing. If these horses were kept for racing, and if the appellant's evidence that he engaged in racing for sport is to be accepted, then it is difficult to see how the stakes won by these horses could form part of the business carried on by Mr. Walles. It is admitted that Mr. Walles trained horses which belonged to others than himself and I do not think it is suggested that the stakes won by such horses would also be a part of the profit of Mr. Walles's business. I cannot see any reason why Mrs. Walles's horses would be in a different position to those owned by other owners who engaged the services of Mr. Walles as trainer. For these reasons I agree with my brother whose judgment I have had the advantage of reading, that the stakes won by horses belonging to Mr. and Mrs. Walles are not assessable.

It was also argued for the appellant that he should be allowed a deduction in respect of a bad debt of Rs. 6,535.

That sum was apparently claimed as a deduction under section 9D of the Ordinance as a bad debt incurred in the business. I agree that the debt due to the appellant from Mr. Coomber cannot be regarded as a bad debt incurred within the period of which the profits were being ascertained but I agree that the sum of Rs. 2,602.42 was clearly a loss incurred by the appellant on May 23, 1932, and would be a deduction allowable under section 13B or C of the Ordinance. I do not think it necessary to say anything more on this point, and the Board of Review will no doubt have this matter in mind when they fix the final assessment on the appellant.

Appeal allowed.

25/38