Income Tax on Gambling: Recent Developments

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Introduction

The general perception among professional gamblers and tax practitioners is that gambling winnings are not subject to income tax. However, historically, the courts have admitted the possibility that such winnings could be taxable. In recent times, certain types of professional gambling have come ever closer to taxable activities (e.g. spread betting, systematic card playing). In 2010 I wrote of how the Australian Tax Office determined that an individual who spent a week spread betting was subject to income tax on his winnings.[1] Understandably, this created uncertainty for gamblers and their professional advisers. This article considers the law in this area and a recent decision of the UK Court of Appeal that has brought some welcome clarity.

Some preliminary points worth noting are:

- Gambling proceeds are subject to betting duty at 1%.
- Section 613(2) of TCA 1997 states that winnings from betting are not chargeable gains. There is no similar provision in respect of income tax.
- The badges of trade were formulated in the context of the acquisition and disposal of assets and are applied in

1 See Paul Brady, "Risky Business – Income Tax on Gambling", *Irish Tax Review*, 23/3 (2010), 103.

situations involving the exploitation of property rights or the provision of professional services.[2]

Before considering the UK position, it is working reviewing the approach in two other common law jurisdictions – Canada and Australia.

The Canadian Approach

In the Canadian case of *Le Blanc v The Queen*,[3] two brothers who played sports lotteries on a massive scale from their living room were held to be not liable to tax on their winnings. This was so notwithstanding the very systematic and methodical approach that they adopted. Expert evidence was presented showing that there was no reasonable prospect of their profiting from the venture. Therefore, it could not be regarded as a trade. The court concluded that the intervention of Parliament was required for gambling winnings to be subject to income tax.

The Australian Approach

The Australian courts have admitted the possibility of gambling winnings being subject to income tax.[4] They have attempted to articulate a method of analysis to determine the issue. A number of factors are identified. Is the behaviour businesslike? Is it for profit or pleasure? Does it reward skill and judgement, or does it depend purely on chance? However, to date, the Australian courts have been hesitant to hold gambling winnings liable to tax.

It was in this context that the Australian Tax Office (ATO) reached its own (non-judicial) decision that an individual who took a week off work to engage in spread betting was liable to income tax on his winnings.[5] In the ATO's opinion, spread betting was closer to the skill end of the chance-to-skill spectrum.[6]

The UK Approach

The 1925 UK High Court case of *Graham v Green*[7] is usually taken as the starting point for analysis of UK case law in this area. It involved a man who bet on horses on "a large and sustained scale" and made his living from it. In his decision, Rowlatt J distinguished a gambler from a bookmaker. The latter is: "organising an effort in the same way that a person organises an effort if he sets out to buy himself things with a view to securing a profit by the difference in their capital value in individual cases."

However, in relation to the gambler who places bets with the bookmaker:

> *"These are mere bets…I do not think he could be said to organise his effort in the 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…I think all you can say of that man, in the fair use of the English language, is that he is addicted to betting. It is extremely difficult to express, but it seems to me that people would say he is addicted to betting, and could not say that his vocation is betting.*
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> *The subject is involved in great difficulty of language, which I think represents great difficulty of thought. There is no tax on a habit. I do not think 'habitual' or even 'systematic' fully describes what is essential in the phrase 'trade, adventure, employment or vocation'."*

At about the same time, the UK Court of Appeal gave its decision in *Cooper v Stubbs*.[8] Mr Stubbs was a cotton merchant who speculated on future cotton prices – buying and selling contracts but never actually taking delivery. While, to the average person, his activities would appear to be gambling, the enforceable nature of the contracts he entered into meant that he was, nonetheless, engaged in a trade that was liable to income tax. To the detriment of tax advisers for decades to follow, the judges expressly reserved their opinion on what the tax treatment would have been had the contracts not been enforceable.

In a subsequent case the UK courts determined that a golf club professional who played and bet on games after hours was not liable to income tax on his gambling winnings as there was no sufficient association with his normal duties and the

2 John Ward, *Judge: Irish Income Tax* (Dublin: Tottel Publishing, 2007), 493.
3 [2006] TCC 680.
4 *Brajkovich v Federal Commissioner of Taxation* [1989] 89 ATC 5227.
5 Interpretive Decision 2010/56; see http://law.ato.gov.au/atolaw/index.htm.
6 In the author's opinion, this decision was incorrect under Australian law and was possibly an attempt to provoke a judicial ruling on the issue.
7 [1925] 2 KB 37.
8 [1925] 2 KB 753.

gambling lacked organisation.[9] Separately, a casino owner who played cards in his own casino was held liable to income tax on his gambling winnings as the gambling formed part of his business.[10] Thus, a connection with an existing trade will render gambling winnings taxable.

The *Hakki* Decision

I was recently consulted by a professional gambler who was engaged in systematic online poker playing. He sought advice on whether his winnings were subject to tax. While investigating the issue, I chanced upon a UK Court of Appeal decision from April 2014: *Hakki v Secretary of State for Work & Pensions*.[11]

The first point to note about the *Hakki* decision is that it was not a tax case. Mr Hakki was a professional gambler who was sued for failure to pay child maintenance. The court had to determine whether his gambling winnings constituted "earnings" for the purposes of the relevant child support legislation. That legislation equated "earnings" to "taxable profits" for income tax purposes. In other words, if the winnings were subject to income tax, they were to be taken into account in determining child support. The same case law and principles applied to determining both.

Mr Hakki played poker in casinos on average three to four days a week. On any given day, he would stay in the casino as long as it took to achieve his target for the day and then leave. He would select opponents whom he was most likely to beat. He appeared in a televised poker competition, reached the final and won a prize. He also appeared in magazines about poker. He was known in the poker community as Tony, "the Hitman", Hakki.

In delivering the major judgment of the court, Longmore LJ reviewed the UK case law to date. In relation to *Graham v Greene* he noted Rowlatt J's comparison between a bookmaker and a gambler and recited the passages quoted above. He stated: "This authority has now stood for many years and I would certainly not in 2014 wish to question it, even though it can be said that the Court of Appeal in *Cooper v Stubbs* left the matter open."

Longmore LJ noted that there was undoubtedly a dividing line between taxable and non-taxable gambling. He was also persuaded that it is possible to conceive a case in which a gambler's winnings might be taxable (e.g. where they are associated with an existing trade).

However, Longmore LJ did not believe that Mr Hakki had a sufficient organisation in his poker playing to make it amount to a trade (or a business), let alone a profession or vocation. This was so notwithstanding the frequency with which he played, the self-control he exercised and his deliberate selection of opponents. There was no "element of fecundity", merely frequent and successful playing at cards. There would have to be evidence of much more by way of organisation before Mr Hakki could be said to be making earnings from any gainful employment.

Application in Ireland

If a similar question came before the Irish courts, there is no apparent reason why the *Hakki* decision would not be followed. There is very little divergence in legislation between the UK and Ireland, and the same fundamental principles apply. *Hakki* was a unanimous decision of the UK's Court of Appeal. It is the last case in a line of decisions stretching back 90 years. In my client's case, the Revenue Commissioners have accepted this reasoning.

Conclusion

Other than cases where the gambling is ancillary to an existing business, it is difficult to conceive of circumstances where gambling winnings would be subject to income tax. It may be said that the arm of the tax gatherer reaches far[12] but not as far, it seems, as the professional gambler. To alter the position, the Irish courts would need compelling reasons to depart from the approach adopted by our neighbours. Alternatively, legislative intervention would be required.

9 *Down v Compston* [1937] 2 All ER 425.
10 *Burdge v Pyne* [1970] 1 All ER 467.
11 [2014] EWCA Civ 530.
12 Per Rutledge J, *Commissioner of Internal Revenue v Flowers* [1946] 326 US 465.