IT 2623A - Addendum - Income Tax: repayments of sickness benefits

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Australian
Taxation
Office

TAXATION RULING IT 2623

Income tax: repayments of sickness benefits

ADDENDUM

F.O.I. EMBARGO: may be released

The Tax Law Improvement Project is restructuring, renumbering and rewriting the income tax law in plain language. The Parliament is amending the income tax law progressively to reflect these aims. As new laws come into effect, Taxation Rulings about old laws are being brought into line with them.

In addition to bringing this Ruling into line with the new laws, this Addendum clarifies the administrative policy in paragraphs 15 to 17.

This Addendum amends Taxation Ruling IT 2623 as follows:

1. **Paragraph 1**

   Omit '('the Act')'; substitute '('the 1936 Act')(now section 8-1 of the *Income Tax Assessment Act 1997* ('the Act')'.'

2. **After paragraph 1**
   Insert:
   'Cross references of provisions

   1A. This Ruling refers to sections 6-5 and 8-1 of the Act. Those sections express the same ideas as subsections 25(1) and 51(1), respectively, of the 1936 Act. Paragraph 8-1(1)(a) of the Act expresses the same idea as the first limb of subsection 51(1) of the 1936 Act.'

3. **Paragraph 5**

   Omit 'of the Act'; substitute 'of the 1936 Act'.

4. **Paragraph 6**

   Omit 'of the Act'; substitute 'of the 1936 Act'.

5. **Paragraph 7**

   Omit 'subsection 25(1)'; substitute 'section 6-5'.

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6. **Paragraph 9**

(i) Omit 'the first limb of subsection 51(1)'; substitute 'paragraph 8-1(1)(a)';

(ii) Omit 'the assessable income" of the person who makes the payment'; substitute 'your assessable income"'.

7. **Paragraph 12**

Omit 'subsection 51(1)'; substitute 'section 8-1'.

8. **Paragraph 13**

Omit 'of the Act' (twice occurring); substitute 'of the 1936 Act'.

9. **Paragraph 17**

Omit 'of the Act'; substitute 'of the 1936 Act'

10. **After paragraph 17**

Insert:

'18. The AAT was not asked to consider the effect of the decisions of the High Court in *Cullen v. Trappell* (1980) 146 CLR 1 or *Fox v. Wood* (1981) 148 CLR 438 in *Case* V16; *AAT Case* 4077; *Case* W78; *AAT Case* 5259; or *Case* W86; *AAT Case* 5347. *Cullen v. Trappell* concerns lump sum personal injury compensation components paid in respect of loss of past and future income earning capacity. The decision in *Cullen v. Trappell* is that the amounts are to be calculated net of tax. Therefore, where repayments require a tax inclusive amount to be repaid, the recipient would be undercompensated by the amount of tax previously paid. The High Court, in *Fox v. Wood*, ruled that in those cases where tax had to be repaid, the lump sum personal injury award had to include the tax. In a dissected lump sum, this component is shown as a separate head of claim known as the *Fox v. Wood* amount. Undissected lump sums will not identify this amount but should have included this component in the calculation.

19. The decision of the Queensland Supreme Court of Appeal in *Arndette Pty Ltd (in liquidation) v. Thurlow* (unreported) handed down on 20 August 1996 highlighted a need to specifically address the implications of the *Fox v. Wood* decision in this Ruling. The administrative practice in paragraphs 15 to 17 of this Ruling exists because there is no legislative provision to prevent the anomaly that arises where an amount is assessed, tax is paid on that amount, and the amount is

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subsequently repaid in full leaving the taxpayer out of pocket by the amount of tax paid.

20. This administrative practice does not apply to the recipients of a personal injury compensation lump sum as the recipient of the lump sum should have had the *Fox v. Wood* amount included in the lump sum, and hence, been correctly compensated. This Office will not apply this Ruling in situations where the *Fox v. Wood* amount has not been included in the lump sum and undercompensation results from the repayment, as the anomaly does not arise out of the taxation laws.

21. Paragraph 20 does not apply where a taxpayer has settled a claim in the period between 20 August 1996 and 6 August 1997 relying upon the decision in *Arndette Pty Ltd (in liquidation) v. Thurlow* which precludes the recovery of the *Fox v. Wood* amount. Where this situation arises the taxpayer is able to seek an amendment to prior years, subject to the qualification in paragraph 17, to exclude the repaid amounts from assessable income.

22. Paragraph 17 has a requirement that the amount be 'repaid' before an assessment is reopened to exclude the amount repaid. Where arrangements are in place to ensure that payment occurs (e.g., the employer is deducting an agreed sum from the weekly wages), and repayment is by instalments and has commenced, it is accepted that the amount has been 'repaid' for the purposes of this Ruling.'

Commissioner of Taxation

6 August 1997

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