TR 94/D35 - Income tax: capital gains: treatment of compensation receipts

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Draft Taxation Ruling
Income tax: capital gains: treatment of compensation receipts

other Rulings on this topic

IT 2328; IT 2561; TD 14; TD 15; TD 31; TD 57; TD 92/130; TD 93/44; TD 93/82; TD 93/178; TD 93/235; TD 93/236

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DTRs may not be relied on by taxation officers, taxpayers and practitioners. It is only final Taxation Rulings which represent authoritative statements by the Australian Taxation Office of its stance on the particular matters covered in the Ruling.

What this Ruling is about

1. This Ruling considers the capital gains tax (CGT) consequences for the recipient of an amount received as compensation, and whether the amount should be included in the assessable income of the recipient under Part IIIA of the *Income Tax Assessment Act 1936* (the Act).

2. This Ruling does not consider:

- the general application of subsection 25(1) or paragraph 26(j) to the recipient;
- the application of subsection 51(1) to the payer;
- the CGT implications for the payer; or
- amounts received for the grant of easements (other than involuntary easements), profits à prendre and licences. This is covered in detail in Taxation Ruling IT 2561 and in Taxation Determinations TD 93/235 and TD 93/236. To the extent of any inconsistency with IT 2561 or those Determinations, this Ruling prevails.

Key terms

3. For the purposes of this Ruling the following terms are used:

Underlying asset

the asset that, using the 'look-through' approach, is the asset that is disposed of or has suffered permanent damage or has been permanently reduced in value because of some act, happening, transaction, occurrence or event which has resulted in a right to

seek compensation from the person or entity causing that damage or loss in value or against any other person or entity.

If there is more than one underlying asset the relevant underlying asset is the asset which leads directly to the payment of the amount of compensation. For example, if a taxpayer receives an amount of compensation for the destruction of his or her truck, the truck is the underlying asset.

Compensation receipt

includes:

any amount (whether money or other property) received by a taxpayer in respect of a right to seek compensation or a cause of action, or any proceeding instituted by the taxpayer in respect of that right or cause of action, whether or not

- in relation to any underlying asset;
- arising out of court proceedings; or
- made up of dissected amounts.

Look-through approach

the process of identifying the most relevant asset. It requires an analysis of all of the possible assets of the taxpayer in order to determine the asset to which the compensation amount is most directly related. It is also referred to in this Ruling as the underlying asset approach.

Permanent damage or reduction in value

does not mean everlasting damage or reduced value, but refers to damage or a reduction in value which will have permanent effect unless some action is taken by the taxpayer to put it right.

Total acquisition costs

costs covered by subsection 160ZH(1), e.g. original cost of acquisition, or the costs of capital improvements.

Right to seek compensation

the right of action arising at law or in equity and vesting in the taxpayer on the occurrence of any breach of contract, personal injury or other compensable damage or injury.

Undissected lump sum compensation receipt

any amount of compensation received by the taxpayer where the components of the receipt have not been and cannot be determined or otherwise valued or reasonably estimated.

Taxation adjustments

any additional amount of compensation (e.g. a 'top-up') calculated to cover any income tax (including CGT) liability that may arise in respect of the compensation receipt. This amount may be determined and received at the time of the compensation receipt or at any other time.

Exemplary or punitive damages

any amount awarded by the courts or agreed to by the parties over and above the amount required to restitute the plaintiff (taxpayer) for the damage suffered.

Involuntary easement

an easement, right or restriction which is compulsorily granted to a government or government authority.

Received

includes entitled to receive.

Notional asset

the asset which is deemed to be created and disposed of under subsection 160M(7).

Ruling

Compensation in respect of the disposal of an underlying asset

4. If an amount of compensation is received by a taxpayer in respect of the disposal of an underlying asset, or part of an underlying asset of the taxpayer, the compensation represents consideration received on the disposal of that asset. In these circumstances, we do not consider that the amount is consideration received for the disposal of any other asset, such as the right to seek compensation.

5. It follows that if the underlying asset disposed of was acquired by the taxpayer before 20 September 1985, the receipt of the compensation has no CGT consequences for the taxpayer. If the underlying asset was acquired by the taxpayer on or after 20 September 1985, a net capital gain or loss may arise on the disposal. Refer to Examples 1 and 2 in this Ruling.

Compensation for permanent damage to, or permanent reduction in the value of, the underlying asset

6. If an amount of compensation is received by a taxpayer wholly in respect of permanent damage suffered to a post-CGT underlying asset of the taxpayer or for a permanent reduction in the value of an underlying asset of the taxpayer, and there is no disposal of that underlying asset at the time of the receipt, we consider that the amount represents a recoupment of all or part of the total acquisition cost of the asset.

7. Accordingly, the total acquisition costs of the post-CGT asset should be reduced in terms of subsection 160ZH(11) by the amount of the compensation. No net capital gain or loss arises in respect of that asset until the taxpayer actually disposes of the underlying asset. If, in the case of a post-CGT underlying asset, the compensation amount exceeds the unindexed acquisition costs (including a deemed cost base) of the underlying asset, the excess is considered to relate to the disposal of the right to seek compensation and an immediate CGT liability may arise.

8. The adjustment of the total acquisition costs effectively reduces the original amount of expenditure or cost by the amount of the recoupment as if that amount had not been incurred. This means that indexation is not available in respect of the recouped amount.

9. If the underlying asset which has suffered permanent damage or a permanent reduction in value was acquired by the taxpayer before 20 September 1985 or is any other exempt CGT asset, the receipt of the compensation by the taxpayer has no CGT consequences.

Compensation for excessive consideration

10. If a taxpayer is compensated for having paid excessive consideration to acquire an asset, the amount referable to the overpayment is considered to represent a recoupment of all or part of the original acquisition cost of the asset in terms of subsection 160ZH(11). Refer to Example 3 in this Ruling.

Exempt assets

11. If an amount of compensation is received in respect of an underlying asset which is exempt from CGT (e.g. a principal residence or an asset acquired before 20 September 1985) there are no CGT consequences. However, if there is no asset which has been permanently damaged or permanently reduced in value, if the requirements of subsections 160M(6) or (7) are satisfied, and the consideration is received by the taxpayer in respect of the disposal of the newly created or notional asset, being the most relevant asset, a taxable net capital gain may arise.

Compensation for an involuntary easement

12. If an amount of compensation is received by a taxpayer for the grant of an involuntary easement which causes a permanent reduction in value of the land, that amount will be treated as compensation for the permanent reduction in the value of the land as a direct result of the grant of the easement. The compensation may be applied to reduce the total acquisition cost of the land. Refer to Examples 4 and 5 in this Ruling.

Determining the relevant asset

13. If the compensation relates directly to more than one asset, it is necessary to determine the most relevant assets and to apportion the compensation between those assets (subsection 160ZD(4)).

Apportioning the compensation receipt

14. If the amount of compensation is received by the taxpayer partly in respect of permanent damage suffered to, or a permanent reduction in the value of, an underlying asset of the taxpayer, that part of the receipt that represents a recoupment of part of the costs or expenditure incurred in respect of the underlying asset reduces the total acquisition costs, and a CGT liability may arise in respect of any excess amount.

15. The costs and expenditure incurred in respect of the underlying asset of the taxpayer can only be reduced to zero. If the recoupment exceeds the total acquisition costs of the underlying asset the excess is attributable to the disposal of either the right to seek compensation or a notional asset, and a CGT liability may arise. Refer to Examples 6 and 7 in this Ruling.

Disposal of the right to seek compensation

16. If the amount of compensation is not received in respect of any underlying asset, and there is no notional asset in respect of which the amount is received, the amount relates to the disposal by the taxpayer of the right to seek compensation. Accordingly, any capital gain arising on the disposal of that right is calculated using the cost base of that right. Refer to Example 8 in this Ruling.

Disposal of a notional asset

17. Generally, as the amount of compensation is received by a taxpayer in respect of either the disposal of an underlying asset or the disposal of the right to seek compensation, subsection 160M(7) does not apply to the compensation payment. If the amount does not relate to either the right to seek compensation or any underlying asset, subsection 160M(7) may apply to the amount received. Refer to Example 9 in this Ruling.

Undissected lump sum compensation amount

18. If the amount of compensation received is an undissected lump sum, the whole amount is treated as being consideration received for the disposal of the right to seek compensation. Refer to Example 11 in this Ruling.

Exemption for personal wrong or injury

19. Compensation received by an individual for any wrong or injury suffered to his or her person or in his or her profession or vocation is exempt from CGT under subsection 160ZB(1). Refer to Examples 12, 13 and 14 in this Ruling.

20. If the individual components of a lump sum compensation amount have not or cannot be determined or reasonably estimated, no part of the amount can be said to relate to any personal injury of the taxpayer. Accordingly, the exemption which would otherwise be

available under subsection 160ZB(1) will not apply to any part of the compensation amount. Refer to Example 15 in this Ruling.

21. Compensation received by a company or trustee for any wrong or injury suffered by the company or trust does not fall within the scope of the exemption provided by subsection 160ZB(1).

Roll-over relief

22. Sections 160ZZK and 160ZZL may provide roll-over relief in certain cases where an amount of money or a replacement asset is received as compensation or as an insurance payment for the disposal of an asset or part of an asset by way of the compulsory acquisition, loss or destruction of, or damage to, that asset.

Preventing double taxation

23. Subsection 160ZA(4) protects from the application of Part IIIA that part of any amount of compensation which also represents income under subsection 25(1) or the other general income provisions of the Act.

Goodwill

24. A temporary fluctuation in the value of goodwill does not represent either permanent damage to, or a permanent reduction in the value of, the goodwill. Accordingly, it is not appropriate to adjust the cost of the goodwill in terms of subsection 160ZH(11) in these circumstances.

Interest

25. Interest awarded as part of a compensation amount is assessable income of the taxpayer under the general income provisions. If the taxpayer receives an undissected lump sum compensation amount and the interest cannot be separately identified and segregated out of that receipt, no part of that receipt can be said to represent interest. In that case the whole amount relates to the disposal of the right to seek compensation.

Taxation adjustments

26. Taxation adjustments are considered to be additional amounts received as a result of or in respect of the disposal of an asset.

Date of effect

27. This Ruling applies to years commencing both before and after its date of issue. However, the Ruling does not apply to taxpayers to the extent that it conflicts with the terms of a settlement of a dispute agreed to before the date of issue of the Ruling (see paragraphs 21 and 22 of Taxation Ruling TR 92/20).

Outline of this Ruling

28.

A	**Actual disposal of the *underlying asset.*** Includes a disposal of part of the underlying asset. This also includes loss or destruction of part or all of the underlying asset. The taxpayer uses the general disposal provisions of Part IIIA, including any roll-over relief and exemption. **Sections 160M and 160N**
B	**No disposal of the underlying asset; *permanent damage* to, or *permanent reduction* in the value of, the underlying asset and the receipt does not exceed the total acquisition costs of the underlying asset at the time of receipt.** This requires a reduction of the total acquisition costs for so much of the amount received as represents compensation for the permanent damage or permanent reduction in value. **Subsections 160ZH(11) and 160ZD(4) (dissection basis)**

C	**No disposal of the underlying asset; *permanent damage* to, or *permanent reduction* in the value of, the underlying asset and the receipt exceeds the total acquisition costs of the underlying asset at the time of receipt.** CGT may apply to any excess over the total acquisition costs as consideration for the disposal of the right to seek compensation or the notional asset. **Subsection 160ZD(4) (dissection basis)**
D	**No disposal of the underlying asset; disposal of the *right to seek compensation*.** Consider this under the general disposal provisions. In some cases an exemption may be available. **Section 160A (pre and post amendment), paragraph 160M(3)(b) & subsection 160ZB(1)**
E	**Act, transaction or event not covered by A, B, C or D.** Subsection 160M(7) will apply. **Subsection 160M(7) (pre and post amendment)**

Explanations

General concepts

29. Part IIIA applies to include in the assessable income of a taxpayer net capital gains made on the disposal of assets.

30. If a change has occurred in the ownership of an asset, subsection 160M(1) deems the change to have effected a disposal and an acquisition of the asset. Subsections 160M(2) and (3) extend the scope of 'a change in the ownership of an asset'. One effect of these provisions is that a change in ownership of an asset may occur without there being a corresponding acquisition of the asset.

The asset

31. 'Asset' is defined in section 160A as any form of property and includes, among other things, a chose in action, and any other right, whether or not proprietary in nature and whether or not legally enforceable (paragraph 160A(a)). It is clear that the right to seek compensation is an asset for the purposes of the definition in section 160A.

32. The Explanatory Memorandum accompanying *Taxation Laws Amendment Act (No 4) 1992* stated, at 55:

> 'Not all things often referred to as "rights" will be assets for CGT purposes. To be an asset, a right must be recognised and protected by law - a court of law or equity will assist in enforcing it. Personal liberties and freedoms, such as the freedom to work or trade or to play amateur sport, are not legal or equitable rights and accordingly will not be assets for CGT purposes. [But this does not mean that money or other consideration received in relation to personal liberties and freedoms can not be taxed under the CGT provisions...]...
>
> Accordingly a legal right of a personal character which is not capable of assignment, such as the rights under a contract of personal services, will be an asset. Other examples might include the rights of a party to a restrictive covenant or exclusive trade tie agreement, and the rights of a sporting club under an agreement that a sportsperson play for that club.'

33. We consider that the right to seek compensation is an asset for the purposes of the CGT provisions.

Before the 25 June 1992 amendments

34. The issue is whether the right to compensation was an asset for CGT purposes prior to the amendments.

35. The UK CGT legislation has generated a number of cases where the definition of 'asset' has been considered.

36. In *O'Brien (Inspector of Taxes) v. Bensons Hosiery (Holdings) Pty Ltd* [1980] AC 562, the court held that any legally enforceable right that can be turned to account is an asset for the purposes of the UK CGT legislation. In that case the taxpayer argued that its rights under a service contract with an employee did not constitute an asset. Lord Russell of Killowen concluded, at 739:

> 'If, as here, the employer is able to exact from the employee a substantial sum as a term of releasing him from his obligations to serve, the rights of the employer appear to me to bear quite sufficiently the mark of an asset of the employer, something which he can turn to account, notwithstanding that his ability to turn it to account is by a type of disposal limited by the nature of the asset.'

37. *Whiteman on Capital Gains Tax* (4th ed), after an analysis of the UK case law, states at 100 that:

> '...it is hard to resist the conclusion that, in appropriate circumstances, the right to sue for damages (or indeed for any other form of relief) is an asset in respect of which a gain may be realised.'

38. On the basis of Australian case law there is some difference of opinion as to whether a right to compensation would have been an asset for CGT purposes prior to the amendments. One of the first significant cases on this issue is *Hepples v. FC of T* 91 ATC 4808; (1991) 22 ATR 465. In that case there was some limited analysis of the meaning of 'asset' (in the context of applying subsections 160M(6) and 160M(7)), and, in particular, the width of the phrase 'any other right' for the purposes of the definition of asset in section 160A.

39. In the Full Federal Court Gummow J concluded (90 ATC 4514; (1990) 21 ATR 62):

> 'In the case of a contract for the provision of personal services the person for whom the services were to be tendered might, in the case of a breach, have a right to damages or, in a particular case, seek an injunction to restrain breach of a negative covenant...But one would treat the plaintiff in such a case as pursuing legal and equitable rights which fell short of any form of incorporeal property and fell outside...the definition of "asset".'

40. The High Court in *Hepples* did not fully explore the meaning of 'asset' or 'any other right' except as they related directly to the application of subsections 160M(6) or 160M(7). Indeed, the reasoning of the court is conflicting in some respects.

41. Gaudron J accepted the concept of the rights under the contract being an asset (91 ATC at 4828; 22 ATR at 488):

> 'The right of the appellant's employer...to enforce the promise of the appellant is an asset within the ordinary meaning of that word and as defined in section 160A of the Act. That asset was created by the making of the promise and...there is no difficulty in treating the making of that promise as the disposal of the asset.'

42. It is clear that there remains some uncertainty on the question of whether 'asset' is limited to proprietary interests. Even if it is so limited, there is judicial authority suggesting that a right to sue is a proprietary right.

43. McHugh J in *Hepples* suggested that a right to sue is a proprietary right once it is vested in the grantee. His Honour observed in his judgment (91 ATC at 4840; 22 ATR at 502):

> 'When a person creates a right in another person to sue him or her, the grantor does not dispose of any asset of his or her own. The personal right to sue is never vested in the grantor, even momentarily. It is only when the right to sue is vested in the grantee, and not before, that it bears the character of a proprietary right.'

44. In *Georgiadis v. AOTC* (1994) 119 ALR 629, the High Court considered whether the right to sue was property for the purposes of paragraph 51(xxxi) of the Constitution.

45. The case involved the question of whether a provision in employee compensation legislation is a law with respect to the acquisition of a right for a purpose in respect of which the Parliament has power to make laws within paragraph 51(xxxi). In determining the question the court was first required to determine whether the plaintiff had any property which was affected by the Act. Mason CJ, Deane and Gaudron JJ, said at 632:

> '..."property" as used in paragraph 51(xxxi) extends to "every species of valuable right and interest including ...choses in action", "money and the right to receive a payment of money". Clearly, a right to bring an action for damages for negligence is a valuable right.'

46. Brennan J concluded, at 638:

> '...if the plaintiff's rights against the Commonwealth were proprietary in nature, the extinguishment of those rights by section 44 would amount to an acquisition of property...What, then, is the nature of a claim in negligence for damages for personal injury?
>
> A plaintiff's claim in negligence causing personal injuries is a chose in action, as the Court of Appeal decided in *Curtis v. Wilcox* ([1948] 2 KB 474). In that case it was held that a wife's claim for damages for pre-nuptial negligence was part of her property for which she was entitled to sue her husband pursuant to the *Married Women's Property Act 1882 (UK)*. Although such a cause of action is not assignable, their Lordships rejected the

> argument that assignability is the test of whether a claim in negligence was a chose in action, and, in my respectful opinion, rightly so. It is not by reason of its nature that such a claim is not assignable; it is for reasons of public policy that the courts have held that such a claim is not assignable, thereby avoiding the evils of champerty.'

47. The right to sue in relation to a breach of contract seems to be proprietary in nature. In *Loxton v. Moir* (1914) 18 CLR 360, Rich J at 379 noted:

> 'A right to sue for a sum of money is a chose in action, and it is a proprietary right.'

48. In the context of these decisions we consider that there is sufficient authority to support our conclusion that the definition of 'asset' before the amendments of 25 June 1992 extends to cover the right to seek compensation.

Exempt assets

49. If the relevant asset is an exempt asset for the purposes of Part IIIA, the receipt of an amount of compensation in respect of the disposal of that asset continues to be exempt from CGT. If the amount of compensation is received in respect of permanent damage to, or a permanent reduction in value of, an exempt underlying asset of the taxpayer, the compensation will continue to be exempt from CGT.

50. While the underlying asset may be exempt from CGT, an amount received by the taxpayer in relation to an act, transaction or event for the purposes of subsection 160M(7) (both before and after the amendments) may represent consideration received in respect of the disposal of the notional asset created by that subsection. In these circumstances that compensation amount will be subject to Part IIIA.

51. In adopting this view we have taken into account the general scheme and intent of Part IIIA. If the actual disposal of an asset would not give rise to a capital gain or loss (for instance, because the asset is a pre-CGT asset, or is otherwise exempt) a compensation receipt in respect of its disposal or a permanent decrease in its value should also be exempt.

Determining the relevant asset

52. The particular asset in respect of which an amount of compensation has been received by the taxpayer may be:

1. an underlying asset (analysed in situations A, B and C; paragraphs 85 to 101);

2. a right to seek compensation (analysed in situations D and E; paragraphs 102 to 111 and 118 to 123); or
3. a notional asset, in terms of subsection 160M(7) (analysed in situation E; paragraphs 112 to 117).

The underlying asset approach

53. In determining which is the most relevant asset, it is often appropriate to adopt a 'look-through' approach to the transaction or arrangement which generates the compensation receipt. We regard this concept as the most appropriate basis on which to determine whether any capital gain arises on the disposal of any asset of the taxpayer.

54. Warner J in *Zim Properties v. Procter (Inspector of Taxes)* [1985] STC 90; 58 TC 371 applied this look-through approach in determining from which asset the settlement sum was derived. His Honour considered that the choice of which was the most relevant asset depended on the 'reality of the matter'. There, the taxpayer had contracted to sell certain property. However, the buyer was able to repudiate the contract because the taxpayer could not show good title to the property. The taxpayer then sued its solicitors for negligence and was awarded an amount of compensation against them for that negligence.

55. Warner J held that the settlement amounts paid by the solicitors were not derived from the real estate but were derived from the right to sue, which was itself an asset.

56. It is important to note that, in *Zim Properties,* there was no disposal of the real estate.

57. In *Case Z21* 92 ATC 218; *Case 7870* (1992) 23 ATR 1162, the AAT (PW Johnston, Deputy President, AAT) accepted that $165,000, received on the termination of a management agreement, was compensation for loss of future earnings, and therefore assessable income. The amount was received as compensation for the repudiation of the agreement, and was paid to avoid paying damages arising as a result of the termination of the agreement. The AAT found that the receipt stood in the place of damages to compensate for the loss of future profits, and not for the loss or destruction of the facility or business asset which the company would have exploited to earn those management fees.

58. Although it was considered that it was not strictly necessary to do so, the Tribunal also made some observations about the application of the CGT provisions. The Tribunal expressed the opinion that the

relevant asset was the right of the company to receive management fees while the agreement continued.

59. In Taxation Determinations TD 31 and TD 57, which deal with the receipt by a taxpayer of insurance proceeds and compensation for uninsured items respectively, we have used the concept of looking through the transaction that gave rise to the compensation receipts to the most relevant asset relating to the receipts. In both situations, we consider that the loss or destruction of the asset which generates the right to seek compensation, either under an insurance policy or from some other source, is the most relevant transaction or event producing the right to receive compensation.

60. Accordingly, we consider that it is for the loss or destruction of the underlying asset that compensation is received, rather than for the disposal of the rights arising from that loss or destruction. Only if the insurance or settlement proceeds do not relate to the disposal of part or all of any underlying asset is it necessary to consider the policy rights or the right to seek compensation as the relevant asset.

61. More recently, in *Carborundum Realty Pty Ltd v. RAIA Archicentre Pty Ltd and Graeme McDonald* 93 ATC 4418; (1993) 25 ATR 192, Harper J suggested that the compensation receipt should be linked to the underlying asset in determining whether the plaintiff had received any capital gain. In that case Harper J found that the defendant was liable to pay damages as compensation for the defendant's negligence in inspecting and reporting on the condition of a residential property owned by the plaintiff.

62. The statutory scheme of Part IIIA, as demonstrated in the roll-over provisions for involuntary disposals in sections 160ZZK and 160ZZL, reinforces the validity of this underlying asset approach.

63. In concluding that the underlying asset is the most relevant asset to which an amount of compensation relates, the taxpayer must be able to show that the compensation receipt has a direct and substantial link with the underlying asset. If an asset has not been disposed of and has not been permanently damaged or permanently reduced in value by the happening or event which generated the amount of compensation, the taxpayer will not be able to demonstrate that link. It follows that the compensation cannot be directly related to that asset. In those cases, the most relevant asset may be the right to seek compensation, or the notional asset.

Apportioning the compensation receipt

64. If the compensation receipt relates to more than one relevant asset, the compensation needs to be apportioned between those assets. Similarly, if the amount is received in respect of a number of heads of

claim (for example, lost profits, interest and punitive damages), the amount also needs to be apportioned between the items.

65. Subsection 160ZD(4) provides:

> 'where any consideration paid or given in respect of a transaction relates in part only to the disposal of a particular asset, so much of that consideration as may reasonably be attributed to the disposal of the asset shall be taken to relate to the disposal of the asset.'

66. This provision allows receipts to be allocated between the relevant assets. If the taxpayer allocates amounts between different assets on a reasonable basis we will generally accept that basis of allocation. If the taxpayer does not allocate the amounts, or the basis of allocation is not reasonable, the Commissioner may decide the basis of allocation.

Disposal of an asset

67. Subsection 160M(1) provides that a change in the ownership of an asset is a disposal of that asset for the purposes of Part IIIA. In many cases the disposal of an asset is by way of contract, with the disposal time being determined in accordance with subsection 160U(3). The loss or destruction of an asset or part of an asset also constitutes a disposal of the asset or that part of the asset (section 160N). The time of disposal is at the time of the loss or destruction in terms of subsection 160U(9).

68. Paragraph 160M(3)(b) refers to a change in the ownership of an asset being a chose in action or any other right on the cancellation, release, discharge, satisfaction, surrender, forfeiture, expiry or abandonment, at law or in equity, of the asset. If the relevant asset is the right to seek compensation, paragraph 160M(3)(b) applies on the granting by a court of a judgment debt in favour of the taxpayer, or by the taxpayer entering into a settlement offer with the defendant. There is a release, discharge or satisfaction of the right, and therefore a disposal of that right.

69. Although there is a disposal of the asset by the taxpayer on the judgment in the taxpayer's favour, the right to seek compensation does not result from any disposal by the grantor (i.e. the payer) of any right to the grantee (i.e. the taxpayer). Rather, the right to seek compensation is vested in the grantee by operation of law (per McHugh J in *Hepples*).

70. Following the amendments to section 160A and subsection 160M(6), of course, an asset created by a person and vested in another on creation is deemed to have been acquired and owned by the grantor immediately before the vesting in the grantee.

Disposal consideration

71. Subsection 160ZD(1) provides that the amount of consideration in respect of the disposal of an asset is the amount or sum of the amounts that a taxpayer has received **as a result of or in respect of** the disposal. In certain circumstances the market value of any property received as consideration is taken into account in determining the total consideration amount.

72. The words 'as a result of or in respect of' have the widest possible meaning of any expression intended to convey some connection or relation between the two subject matters to which the words refer. In these circumstances the relevant subject matters are the disposal and the money or other property received as consideration. It follows that most insurance or settlement proceeds would be received as a result of or in respect of the disposal of an underlying asset, and would constitute consideration received in respect of the disposal of that underlying asset.

73. In *Carborundum* Harper J found that, while there would be a disposal of an asset by the plaintiff, there was no consideration receivable by the plaintiff. His Honour concluded (93 ATC at 4424; 25 ATR at 199):

> '...generally speaking, consideration is something given, by agreement, in return for something else. It has no place where, as here, the plaintiff will obtain the amount of its judgment debt by compulsory exaction from someone who has not agreed to pay it and who will receive nothing as a quid pro quo.'

74. His Honour went on to say (93 ATC at 4425; 25 ATR at 200):

> 'In this case, the amount of money which the defendant must pay in order to eliminate the judgment debt will not be received by the plaintiff "as a result of or in respect of the disposal" of that debt. When received, that amount will **effect** the disposal of the judgment debt - and will do so without there being anything received by the defendant (or given by the plaintiff) in return' (emphasis in original).

75. With respect, we consider that the words 'as a result of or in respect of the disposal' are wide enough to apply to the disposal of the chose in action. In terms of paragraph 160M(3)(b), the 'cancellation, release, discharge, satisfaction, surrender, forfeiture, expiry or abandonment, at law or in equity' of the chose in action occurs in return for the payment of the judgment debt. We consider that there is

sufficient nexus between these two events to satisfy the requirements of section 160ZD.

76. We also consider that, if an amount is received to 'top-up' an amount of compensation for any potential CGT liability, that top-up amount represents part of the consideration received by the taxpayer 'as a result of or in respect of ' the disposal of either the underlying asset, or the right to seek compensation, as the case may be.

77. Similarly, the application of the underlying asset approach means that an amount of compensation received to supplement the disposal proceeds received by a taxpayer (e.g. as a result of a claim for negligence) on the disposal of the underlying asset also represents consideration received 'as a result of or in respect of ' the disposal of the underlying asset.

Recoupment of cost amounts

78. The cost base of an asset is determined in accordance with section 160ZH. That section, broadly speaking, provides that capital expenditure incurred by the taxpayer in connection with the acquisition of an asset, and including the capital costs of holding and maintaining the taxpayer's interests in that asset, form part of the cost base of the asset. In certain cases a taxpayer may be deemed to have incurred expenditure for the purposes of determining the cost base of the taxpayer's asset. Where the asset is held for at least twelve months before its disposal by the taxpayer, the cost base is adjusted for inflation for the purpose of calculating a capital gain.

79. Subsection 160ZH(11) provides:

> 'In determining the cost base, the indexed cost base or the reduced cost base to a taxpayer of an asset, **account shall not be taken** of the amount or value of any part of the consideration paid or given by the taxpayer, or of the amounts of any costs or expenditure incurred by the taxpayer, in respect of which the taxpayer has been recouped, or is entitled to be recouped, by any person' (emphasis added).

80. The term 'recouped' has its normal meaning. The *Macquarie Dictionary* defines 'recoup' as to obtain an equivalent for; compensate for; to regain or recover; to return an amount equal to; to reimburse or indemnify. We therefore consider that an amount of compensation can represent a recoupment of costs in certain cases.

81. The use of the words 'account shall not be taken of' suggests that the recouped expenditure or cost may be completely disregarded in determining the cost base of the asset. Further, the determination of the cost base, indexed cost base or reduced cost base of an asset is

required to be made at the time of disposal of the asset. It is only at that point that the relevant cost calculations can be made.

82. If the taxpayer receives a recoupment of part or all of an amount which has been included in the total acquisition costs of his or her asset, the costs need to be adjusted to exclude the recouped amount. The adjustment effectively reduces the original amount of expenditure or cost by the amount of the recoupment, as if the recouped amount had not been incurred. Accordingly, for the purposes of indexation, this 'adjusted' cost base applies and is subject to indexation from the time of incurring the original expenditure or cost to the time of disposal of the asset by the taxpayer.

83. Although subsection 160ZH(11) requires a taxpayer to exclude from the total acquisition costs of his or her asset any recouped amount, the provision does not deem there to be any disposal of the asset or any part of the asset by the taxpayer at the point of receiving the recoupment (unlike the deemed disposal mechanism contained within section 160ZM, for example).

84. Accordingly, if the amount of recoupment exceeds the taxpayer's total acquisition cost at the time of the compensation receipt, the effect of subsection 160ZH(11) is to reduce the cost to zero. It follows that the whole consideration received on a later actual disposal of that asset by the taxpayer will be a taxable capital gain. The excess of the recoupment over the cost in these circumstances does not represent a taxable capital gain derived from the disposal of that asset. The excess recoupment represents consideration received on the disposal of another asset, such as the right to seek compensation or a notional asset, and may result in an immediate CGT liability.

Compensation receipts: disposal of the underlying asset

When is the asset acquired?

85. The time of acquisition of the underlying asset is determined by section 160U linked with the normal operation of section 160M.

What is the cost base of the asset?

86. The cost base of the underlying asset is determined by section 160ZH.

When is the asset disposed of?

87. If the relevant asset is the underlying asset a disposal of the asset will occur when there is a change in the ownership of the asset or of part of the asset in terms of subsection 160M(1). This may alternatively occur when the asset or part of the asset is lost or destroyed in terms of section 160N. If the asset was acquired on or

after 20 September 1985, any consideration received in respect of the disposal is taken into account in determining whether there is a net capital gain or loss arising on the disposal.

88. The time of disposal is determined by the normal operation of section 160U.

What is the consideration on disposal?

89. The consideration on disposal of the underlying asset is determined by the normal operation of section 160ZD.

What are the CGT consequences?

90. If the underlying asset was acquired by the taxpayer before 20 September 1985, there are no CGT consequences. If the underlying asset was acquired on or after 20 September 1985, a net capital gain or loss may arise on the disposal or part disposal of the underlying asset.

91. An example of the underlying asset approach is to be found in *Tuite v Exelby* 93 ATC 4293; (1992) 25 ATR 81. In that case, Wenmar Stockfeeds Pty Ltd (Wenmar) operated a stockfeed business. Its shareholders were Mr and Mrs Tuite and Mr and Mrs Exelby. In May 1989 the Tuites purchased the business from the Exelbys, and the terms of sale included restraints on the Exelbys from being directly or indirectly involved with the same kind of business for two years after the sale. At about this time the Exelbys arranged for a company to be established (Cradex Pty Ltd) which operated in competition with Wenmar. In determining the question of compensation, Shepherdson J found that there had been breaches of the covenants. His Honour said, at 93 ATC 4299; 25 ATR 91:

> 'If the contract had been performed Cradex would not have existed and been trading in competition with Wenmar at 19 June 1991...[T]he first plaintiffs are entitled to damages for the reduction in the capital value of the shares in the Wenmar business'.

92. He awarded $808,940 for the reduction in value of the shares and $323,130 for lost profits. He also allowed an additional amount of $517,191 for the anticipated CGT liability on the amount attributable to the shares.

Compensation receipts: no disposal of underlying asset; permanent damage to or permanent reduction in value of the underlying asset and the receipt does not exceed the total acquisition costs of the underlying asset at the time of receipt

When is the asset acquired?

93. The time of acquisition of the underlying asset is determined by section 160U linked with the normal operation of section 160M.

What is the cost base of the asset?

94. The cost base of the underlying asset is determined by section 160ZH. If the compensation receipt is paid **wholly** for the permanent damage to, or permanent reduction in value of, the underlying asset, that receipt should be applied to reduce the total acquisition costs in terms of subsection 160ZH(11). If the compensation payment is paid **partly** for the permanent damage to, or permanent reduction in value of, the underlying asset and partly for some other purpose, the compensation payment should be apportioned between the different amounts, and the total acquisition costs adjusted accordingly.

95. The adjustment of the costs effectively reduces the original amount of expenditure or cost by the amount of the recoupment as if the recoupment had not been incurred. It follows that indexation is not available in respect of the recouped amount.

96. The cost adjustment should occur at the time of disposal of the asset. Normal indexation rules will then apply from the relevant times for each component of this adjusted cost base.

When is the asset disposed of?

97. As discussed earlier, if the compensation is received wholly for the permanent damage to, or permanent reduction in value of, the underlying asset, that receipt should be applied to reduce the total acquisition costs in terms of subsection 160ZH(11). There is no disposal of the underlying asset at that time.

What is the consideration on disposal?

98. There is no disposal of the underlying asset at this time.

What are the CGT consequences?

99. The total acquisition costs of the asset are reduced in terms of subsection 160ZH(11).

Compensation receipts: no disposal of underlying asset; permanent damage to or permanent reduction in value of the underlying asset and the receipt exceeds the total acquisition costs of the underlying asset at the time of receipt

100. The compensation receipt will be divided into two parts. An amount equal to the total acquisition costs of the underlying asset, at the time the compensation is received, is treated as in situation B (paragraphs 93 to 99).

101. The excess of the compensation receipt over the cost base of the underlying asset is treated as a receipt in respect of the right to seek compensation (see paragraphs 102 to 111) or in respect of a notional asset (see paragraphs 112 to 117) as is appropriate.

Compensation receipts: disposal of the right to seek compensation.

When is that asset acquired?

102. The asset, being the right to seek compensation, is acquired at the time the damage or injury occurs. In a personal injury claim, for example, it is generally at the time the personal injury or wrong occurs. In a breach of contract claim, it is generally at the time of the breach of contract.

103. It has been argued that a contract which clearly anticipates a breach by one of the parties to the contract and specifies the nature and extent of any remedies on breach generates rights at the time of entering into the contract. In these cases both parties effectively agree that the breach will not void the contract but will simply bind them to behave or perform one other aspect of the original contract.

104. We consider that, notwithstanding these specific arrangements, the rights arising on the breach of contract are merely contingent unless and until the breach occurs. It is at that point that the rights to a remedy arise in the injured party.

What is the cost base of the asset?

105. The cost base of the right to seek compensation is determined by section 160ZH. The cost base is generally limited to incidental costs such as legal fees. Legal fees and charges connected with the proceedings and incurred during the course of proceedings may be included in the cost base of the asset in terms of subsections 160ZH(1) and (5). Subsection 160ZH(9) cannot apply to give the taxpayer a deemed market value cost base as the taxpayer did not acquire the asset from another person, or because the provision is specifically excluded from applying.

When is the asset disposed of?

106. For the purposes of subsection 160M(1) the right is disposed of when the taxpayer agrees to a release, discharge, satisfaction or surrender of his or her right to seek compensation. This is generally at the point of settlement of the claim, whether in the course of court proceedings, or in an out of court arrangement. The time of disposal is generally determined by subsection 160U(3) to be the time of entering into the settlement agreement.

What is the consideration on disposal?

107. The consideration on disposal of the right to seek compensation is determined by the normal operation of section 160ZD. The amount settled on or the amount ordered to be paid by the court represents the consideration received on disposal.

What are the CGT consequences?

108. If the right was acquired by the taxpayer before 20 September 1985 there are no CGT consequences. If the right was acquired on or after 20 September 1985, a net capital gain or loss may arise on the disposal of that right, depending on the cost base of the asset.

109. In many cases there is an underlying asset and a right to seek compensation. Determining the most relevant asset depends on whether the underlying asset has been permanently damaged or permanently reduced in value. If the underlying asset has not been affected in that way and there is no disposal or part disposal of the underlying asset, the compensation must be received for the surrender of the right to seek compensation.

110. Another possible view is that the legal process of resolving and enforcing these types of claims gives rise to the acquisition and disposal of a multiplicity of rights. This view may be correct when considered in an overly strict legalistic sense. In any event, if there is a series of acquisitions and disposals, each of which arguably has a cancelling effect as one right is replaced by another right of comparable value, a capital gain or loss is unlikely to result.

111. We consider that the underlying asset approach requires the ascertainment of the most relevant asset in determining whether there has been any capital gain.

Compensation receipts: disposal of a notional asset

Pre-92 amendments

When is that asset acquired?

112. The relevant asset, being the notional asset deemed to be created in terms of subsection 160M(7), is acquired immediately before the relevant act, transaction or event occurs, and not when the consideration is received by the taxpayer. The relevant act, transaction or event is the breach of contract or the personal injury or wrong. Alternatively, it might be the commencement of proceedings, the obtaining of judgment, or the reaching of a settlement.

What is the cost base of the asset?

113. The cost base of the notional asset is limited to incidental costs (e.g. legal fees) of its disposal and does not include any costs referable to the underlying asset (paragraph 160M(7)(d)).

When is the asset disposed of?

114. The notional asset is disposed of at the time of the relevant act, transaction or event.

What is the consideration on disposal?

115. The consideration on disposal of the notional asset is the compensation receipt.

What are the CGT consequences?

116. A capital gain arises on the disposal of the notional asset.

117. As subsection 160M(7) applies subject to the other provisions of Part IIIA, if there is permanent damage to or a permanent reduction in the value of the underlying asset, subsection 160ZH(11) applies in precedence to subsection 160M(7).

Post-92 amendments

118. In practice it is unlikely that the new subsection 160M(7) will apply as it is subject to the other provisions of Part IIIA and in most cases those provisions will apply. If subsection 160M(7) does apply, the consequences are similar to those outlined in the analysis in paragraphs 112 to 117 of this Ruling.

119. One of the consequences of the amendments of 25 June 1992 to section 160A and subsection 160M(6) is that an asset which is created by a person and on its creation is vested in another person now falls within the provisions of subsection 160M(6).

When is that asset acquired?

120. The effect of paragraph 160M(6A)(a) and subsection 160U(6) is that the creator of the asset is deemed to acquire the asset and to have owned it immediately before the vesting time. At the vesting time, the taxpayer acquires the asset from the creator and is deemed to commence to own the asset (paragraph 160M(6B)(a) and subsection 160U(6)). The vesting time is generally at the time of creation (e.g. at the time of breach).

What is the cost base of the asset?

121. The effect of paragraph 160M(6A)(c) is to limit the cost base of the asset of the taxpayer to the value of money or property given as

consideration for the creation of the asset. This will generally be a nil amount.

When is the asset disposed of?

122. The newly created asset is disposed of by the taxpayer on the release, discharge, satisfaction, or surrender of his or her right to seek compensation (paragraph 160M(3)(b)).

What is the consideration on disposal?

123. The consideration on disposal of the newly created asset is the settled sum or judgment debt received on settlement.

Undissected lump sum compensation amounts

124. Whether a receipt constitutes income or capital in the hands of the taxpayer depends on the circumstances of the receipt and the reasons why it was paid to the taxpayer (*FC of T v. Slaven* 84 ATC 4077; 15 ATR 242). In that case the Federal Court was required to consider the nature of an amount of compensation received by the taxpayer following a motor vehicle accident. The court (Bowen CJ, Lockhart and Sheppard JJ), in concluding that the amount was paid as compensation for loss or impairment of the taxpayer's earning capacity, stated (84 ATC at 4085; 15 ATR at 252):

> 'It is the character of the receipt in the hands of the taxpayer as recipient that must be determined'.

125. The courts have also emphasised that there is a clear distinction between the character of a payment and how it is calculated or quantified (for example, *Tinkler v. FC of T* 79 ATC 4641; (1979) 10 ATR 411) and that the method used:

> 'may provide a quite misleading guide to the character of the payment' (Deane and Fisher JJ, in *Tinkler*, 79 ATC at 4648; 10 ATR at 418).

126. It has been argued that the mere fact that compensation has been awarded as a lump sum and has not been dissected into its component elements is sufficient to treat the whole receipt as one of capital. We do not accept this argument. The facts and circumstances surrounding the receipt may enable an apportionment of the lump sum payment on a reasonable basis into its constituent elements.

127. In *McLaurin v. FC of T* (1961)104 CLR 381, the High Court considered the case of a taxpayer who had commenced an action to recover damages caused by a fire originating on the defendant's land. The taxpayer had supplied the defendant with a list setting out particulars of damage. On the basis of its own list of particulars of damage, the defendant offered the taxpayer a lesser amount as a lump

sum in full settlement of his claim, and the taxpayer accepted the sum **without knowing** the basis of calculation of the sum offered. The Commissioner sought to assess the taxpayer on that portion of the lump sum which was of an income nature as based on the defendant's list of particulars.

128. The High Court held that the lump sum was not assessable income because the settlement offer was for a single undissected amount rather than for a total of itemised amounts, and that it would have been unacceptable to determine the character of the receipt in the hands of the recipient by taking into account the **uncommunicated** reasoning of the payer.

129. The court stated that no apportionment is appropriate if the receipt is in respect of a claim or claims for unliquidated damages only and is made or accepted under a compromise which treats it as a single undissected amount of damages.

130. The court said, however, that a single receipt of a mixed nature may be apportioned across the several heads to which it relates and an income or non-income nature may be attributed to those heads of claim. This apportionment may be done if the amount is 'in settlement of distinct claims of which some at least are liquidated (*Carter v. Wadman* (1946) 28 TC 41) or are otherwise ascertainable by calculation (*Tilley v. Wales* [1943] AC 386).'

131. In *Allsop v. FC of T* (1965) 113 CLR 341, the High Court decided that because the settlement amount payable was an entire sum paid by way of compromise of a number of claims, and no part of it could be attributed solely to a refund of permit fees (which would have been assessable), the amount could not be treated as an income receipt.

132. We consider that these cases do not preclude a proportionate approach to identifying and allocating amounts of compensation to the various heads of claim if the taxpayer receives a single undissected lump sum in satisfaction of those claims.

133. In the case of a court ordered lump sum, the court order will indicate whether the sum relates to specific items, or whether it is an entire and undissected sum. In the case of an undissected sum, the particulars of the plaintiff's claim would indicate whether some of the claims satisfied by payment of the compensation sum are for a liquidated amount and whether individual claims can be identified.

134. In the case of a lump sum paid by way of a settlement of claim or under an insurance policy, the settlement documents (e.g. the letters of offer and acceptance) and the terms of the policy respectively are evidence of the matters examined above. Other evidence may equally be relevant to determining the real agreement between the parties.

It must be remembered that the burden of proving the above matters rests on the taxpayer.

135. The Full Federal Court in *FC of T v. Spedley Securities Ltd* 88 ATC 4126; (1988) 19 ATR 938, also considered the assessability of a lump sum amount received as damages. That case involved a lump sum payment to Spedley under a deed of discharge after a $65 million loan agreement was terminated. There was some evidence that Spedley principals were concerned about the effect of the termination on the international reputation of the group. The receipt was expressed to be consideration for the release from the agreement.

136. Spedley was initially assessed on the lump sum on the basis that it represented loss of commission income. The court, in dismissing the Commissioner's appeal, found that part of the receipt represented lost commission, and part represented recompense for the damage to Spedley's reputation. Their Honours (Fox, Fisher and Sheppard JJ) said, 88 ATC at 4129; 19 ATR at 941:

> 'The discharge document relates to all possible claims arising out of the termination. It is in wide and comprehensive terms, plainly going beyond the necessities of the case. What it does do, assuming its effectiveness, is to bar legal proceedings. It does not follow that because a particular matter of complaint could not, or might not, lead to a legal claim, it has no existence.'

137. And, 88 ATC at 4131; 19 ATR at 942:

> '...The point of the present case is that what was received was a lump sum, the ingredients of which were not identified (there may in fact have been no dissection made on either side) but which...included compensation for injury to a capital asset. There is no basis for dissection or apportionment'.

138. In reaching this conclusion, the court emphasised the lack of any evidence presented to it as to the possible apportionment of the amount received by Spedley.

139. If the compensation amount relates to a number of heads of claim, and the taxpayer cannot apportion the amount into its income and capital components (into profits, interest, disposal consideration and other capital amounts, for example), nor can any reasonable estimate of the components be made, we consider that the whole amount must relate to the disposal of the taxpayer's right to seek compensation. The comments of the court in *Spedley Securities* support and demonstrate this conclusion.

140. It follows that if the individual components of the compensation amount cannot be determined or estimated, no part of the amount can be said to relate to any personal injury of the taxpayer. Accordingly,

the exemption which would otherwise be available under subsection 160ZB(1) will not apply to any part of the compensation amount.

141. It is likely that a lump sum compensation amount can be dissected using the information which was available at the time of making the compensation claim. Alternatively, the income and capital components of the lump sum may generally be estimated or valued on a reasonable basis.

142. The principles relating to the assessability of dissected and undissected amounts apply equally to lump sum compensation amounts received in respect of personal injuries claims, whether by way of settlement or under a court order.

Exemption for personal wrong or injury

143. Section 160ZB provides a statutory exemption from Part IIIA for certain types of capital receipts which might otherwise be included in the assessable income of the recipient.

144. Subsection 160ZB(1) provides:

> 'A capital gain shall not be taken to have accrued to a taxpayer by reason of the taxpayer having obtained a sum **by way of** compensation or damages for any wrong or injury suffered by the taxpayer to his or her person or in his or her profession or vocation and no such wrong or injury, or proceeding instituted or other act done or transaction entered into by the taxpayer in respect of such a wrong or injury, shall be taken to have resulted in the taxpayer having incurred a capital loss' (emphasis added).

145. We accept that the phrase 'by way of' should be given a wide meaning (*Goldsborough Mort & Co Ltd v. FC of T* 76 ATC 4343 at 4348; (1976) 6 ATR 580 at 586). It is not necessary that the amount received by a taxpayer be described as an amount of compensation. An amount received in an out of court settlement where liability is not admitted by either party still represents a sum received 'by way of compensation' in terms of subsection 160ZB(1).

146. The subsection is also intended to be read widely in considering the types of compensation receipts which fall within its scope. Certainly the Explanatory Memorandum accompanying the original CGT legislation suggests a very wide interpretation of the phrases 'to his or her person' and 'in his or her vocation' by referring to 'insurance monies under personal accident policies', and referring specifically to compensation for libel, slander or defamation.

147. We consider that the terms 'to his or her person' and 'in his or her vocation' should be read as widely as possible to cover the full range

of employment and professional type claims, and include claims for sexual harassment, discrimination, and wrongful dismissal.

148. We have considered the potential width of the exemption in Taxation Determinations TD 14 and TD 92/130. TD 14 considered payments made under accident and health assurance policies, while TD 92/130 considered payments of compensation amounts for defamation, for loss of support following wrongful death, and for the professional negligence of a solicitor in failing to institute personal injury claims. In all of these circumstances the exemption provided by subsection 160ZB(1) applies.

149. Compensation amounts for any wrong or injury suffered by a company do not fall within the scope of the exemption. We consider that the use of 'his or her' in connection with the taxpayer suggests that the application of subsection 160ZB(1) is intended to be limited to taxpayers who are natural persons. Similarly, we consider that compensation received by a trustee in his or her capacity as trustee does not fall within the scope of subsection 160ZB(1). Of course, amounts received by the trustee in respect of the surrender of a personal injury claim of the trustee continue to be exempt.

Roll-over relief

Monetary compensation received - section 160ZZK

150. Section 160ZZK provides roll-over relief in certain cases where an amount of money is received as compensation or as an insurance payment for the involuntary disposal of an asset or part of an asset by way of compulsory acquisition, loss or destruction of, or damage to, that asset. For a pre-CGT asset, the effect of the roll-over relief is to allow a replacement asset to maintain its pre-CGT status. In the case of a post-CGT asset, the provisions allow deferment of any capital gain until such time as there is a disposal of the replacement asset.

151. An asset is deemed to be a replacement asset for the purposes of section 160ZZK if it is used for the same or similar purpose as the original asset. For example, if the original asset was used in a business, then the new asset must also be used, or be installed for use, in that business.

Original asset acquired before 20 September 1985

152. If expenditure of a capital nature has been incurred in repairing or restoring an original asset, that asset will retain its pre-CGT nature. This will be the case even though the capital expenditure may otherwise constitute a separate asset in terms of section 160P (subsection 160ZZK(3)).

Original asset acquired on or after 20 September 1985

153. If, but for section 160ZZK, a capital gain would accrue as a result of an involuntary loss or disposal of an asset, subsection 160ZZK(6) may require that an amount be returned as a capital gain or that adjustments be made to the cost base of the replacement asset.

Note: the application of these roll-over provisions is also discussed in Taxation Determinations TD 15, TD 93/82 and TD 93/178.

Replacement asset received

154. In some cases where an asset is compulsorily acquired or otherwise lost or destroyed, a replacement asset may be received either as compensation or under an insurance policy. If certain conditions are met, section 160ZZL may provide roll-over relief so that a replacement asset will maintain the status and attributes of the original asset. Therefore, the replacement asset for an original asset which was acquired pre-CGT will maintain that status and a post-CGT replacement asset will adopt the cost base of the original asset.

Preventing double taxation

155. Subsection 160ZA(4) is designed to ensure that an amount which has been, or will be, included in a taxpayer's assessable income under the general income provisions is not also assessed as a capital gain. There are two conditions which must be met before the provision can apply:

- a capital gain must accrue to the taxpayer on the disposal of an asset; and
- an amount must have been or will be included in assessable income under the general provisions of the Act **as a result of the disposal of that asset**.

156. The actual application of subsection 160ZA(4) depends on the circumstances of each case. We consider that the words 'as a result of the disposal' extend to protect from double taxation any amount of compensation which also represents income under subsection 25(1) or the general income provisions of the Act.

Goodwill

157. Goodwill is an asset, as defined in section 160A. If a taxpayer conducting a business suffers some damage to his or her business operations, or becomes entitled to receive compensation in respect of that business, some part of the compensation amount may relate to his or her goodwill. In considering the effect on the goodwill it is

necessary to consider whether, as a question of fact, the taxpayer has disposed of part or all of his or her goodwill, or whether there has been permanent damage to goodwill.

158. Goodwill is generally either purchased or created by the taxpayer. Purchased goodwill is generally considered to be acquired at the time when the taxpayer enters into the purchase contract. Created goodwill is acquired when the taxpayer commences his or her business activities (Taxation Ruling IT 2328). If a taxpayer disposes of a business, or an interest in a business, and the disposal includes the taxpayer's goodwill, or an interest in the goodwill, the capital gain on disposal is subject to the specific exemption provided by section 160ZZR.

159. Goodwill of a business continually fluctuates in value and a taxpayer is not entitled to reduce the cost of that goodwill in terms of subsection 160ZH(11) for those temporary fluctuations.

160. In certain limited circumstances a taxpayer may be able to demonstrate that he or she has suffered some permanent damage to his or her goodwill, or that it has been permanently reduced in value by some act or event which has generated the right to seek compensation. In these circumstances the taxpayer is entitled to reduce the total acquisition costs of his or her goodwill by so much of the compensation amount that relates to the permanent damage or permanent reduction in value.

161. It is generally very difficult, however, for the taxpayer to demonstrate that there has been some permanent damage to, or permanent reduction in value of, the goodwill, rather than an actual disposal of some or all of that goodwill, or a temporary fluctuation in the value of the goodwill.

162. It should also be noted that receipts are often attributed to 'goodwill' or to the disposal of goodwill, when in fact they represent a receipt in respect of loss of profits. The actual characterisation of a receipt will, of course, always be a question of fact to be determined in each case.

Interest

163. An award of compensation made to a taxpayer may include an amount of interest. It has been suggested that interest or statutory interest in this context is not interest which is assessable income of the taxpayer in terms of subsection 25(1). Rather, it is claimed that the interest represents a capital amount which is simply part of the compensation amount, and which effectively represents part of the consideration received by the taxpayer on the disposal of either the underlying asset or the right to seek compensation, as the case may be.

164. Interest has been described as 'payment by time for the use of money' (Rowlatt J in *Bennett v. Ogston* (1930) 15 TC 374 at 379). In economic terms, interest is the return or compensation for the use or retention by one person of a sum of money belonging or owed to another. Court rules allow the court to include in a compensation amount interest on the whole or part of the amount for the whole or part of the period to which the judgment relates.

165. Any interest awarded as part of a compensation amount is interest within the general meaning of that term. It represents assessable income of the taxpayer even when the judgment provides only for a single lump sum which would otherwise be a capital receipt (*Federal Wharf Co Ltd v. DFC of T* (1930) 44 CLR 24; 1 ATD 70 and *Riches .v Westminster Bank Ltd* [1947] AC 390).

166. We consider that any amount which is in the nature of interest, and which can be identified as interest, and whether paid as part of the compensation amount or separately, constitutes assessable income of the taxpayer under the general income provisions. It may also represent part of the consideration for the disposal of either the underlying asset or the right to seek compensation. Subsection 160ZA(4) would then apply to prevent any double taxation of that amount.

Taxation adjustments

167. There has been a great deal of conflicting commentary on the issue whether a compensation amount should include an amount to allow for any potential CGT liability of the plaintiff. If a court decides that an amount should be added for tax, questions arise as to the mechanism for determining the amount and timing of any future CGT liability.

168. Recent cases have taken varying approaches to the question of any potential tax liability in relation to the compensation amount. In some cases the courts have used an indemnity arrangement to cover the potential liability, while in other cases the courts have refused to allow any additional amount for that potential CGT liability.

169. In *Tuite*, Shepherdson J sought an undertaking from the plaintiffs that in the event that tax was assessed at something less than the additional amount allowed, they would repay the balance to the defendants.

170. In *Provan*, Rolfe J allowed the plaintiff to be indemnified for any CGT liability which might arise in respect of the compensation amount.

171. In *Carborundum*, Harper J refused to grant leave to amend the original application for damages to include a further amount to cover the CGT liability.

172. In *Namol Pty Ltd v. AW Baulderstone Pty Ltd* 93 ATC 5101; (1994) 27 ATR 181, Davies J also refused to allow an additional amount of damages to reflect any likely CGT liability, and was quite critical of the notion of allowing a contingent amount for the potentiality of CGT liability in respect of the compensation award. His Honour said (93 ATC at 5104; 27 ATR at 184):

> 'I cannot accept that it is in accordance with the ordinary principles of assessing damages to include a contingency of the type proposed by counsel. Ordinarily damages are assessed on the probabilities of the case. But if risks or possibilities have to be taken into account because they are part of the matrix of relevant facts, then a court must do the best it can and will adjust the award to take account of that risk or possibility. It is inconsistent with common law principles to make a conditional order either providing for an additional award should a certain event occur or reducing or providing for a reduction of an award should an expected event not come to pass.'

173. If an additional amount of compensation is awarded to the taxpayer to cover the additional CGT liability which might arise in respect of the total compensation award, that additional amount of compensation is considered to represent additional consideration received by the taxpayer for the disposal of the underlying asset, the right to seek compensation or the notional asset, as the case may be.

Examples

Example 1

174. Wally has lived on a 2 hectare property since purchasing it in January 1987 for $300,000. In that time the property has not been used for income producing purposes. One hectare of land is needed by the State Government to complete improvements to the highway which runs alongside the property. The relevant State Authority compulsorily acquires the 1 hectare strip from Wally in May 1994 and commences work on the property at that time. The contract is settled in July and the Authority pays $180,000 as compensation for the acquisition of the 1 hectare strip. Wally has engaged the services of an independent qualified valuer who has estimated the value of the 1 hectare strip in 1987 as $120,000.

175.

Relevant asset:	1 hectare of land
Acquired:	January 1987
Cost base:	$120,000 (being the portion of the total cost of the land that is attributable to the 1 hectare strip)
Disposed of:	May 1994 (under subsection 160U(8))
Consideration:	$180,000
CGT consequences:	Under section 160ZZQ the 1 hectare was nominally part of Wally's post-CGT dwelling and exempt from CGT. However, subsection 160ZZQ(4) operates to impose CGT on the disposal of land when it is disposed of separately to the dwelling. Indexation would apply from January 1987.

Note: Roll-over relief under section 160ZZK may apply.

Example 2

176. Fred purchases from Barney a fossil for $30,000 in July 1994. Prior to Fred's purchase, Dino Inc certifies the fossil as being a fossilised Tyrannosaurus Rex bone. In June 1995 Fred discovers that the fossil is a worthless wood fossil. In July 1995, he returns the fossil to Barney and sues both Barney and Dino Inc for negligence (misrepresentation). Fred agrees to accept $50,000 from Barney in settlement of the claim.

177.

Relevant Asset:	The underlying asset (the fossil)
Acquired:	July 1994
Cost base:	$30,000
Disposed of:	July 1995
Consideration:	$50,000
CGT consequences:	The fossil was acquired at the making of the contract (July 1994) and disposed of when property passed back to Barney (at July 1995). This results in a capital gain of $20,000 on the disposal of the asset by Fred. As the amount
of	compensation received relates to the disposal of the underlying asset, no amount can be consideration received for the disposal of the cause of action. Accordingly, there is no capital gain on the disposal of the legal action.

Example 3

(Variation of Example 2)

178. Continuing on from Example 2, the court holds that the misrepresentation by Barney was innocent and therefore he is not required to pay damages. Fred commences legal action against Dino Inc. Fred has returned the fossil to Barney for nil consideration and incurred $20,000 legal costs for his actions against both Barney and Dino Inc. He obtains judgment against Dino Inc in negligence and receives $70,000 as damages in December 1995.

179.

Relevant asset:	
The underlying asset (the fossil)	the right to seek compensation
Acquired:	
July 1994	June 1994
Cost base:	
$30,000	$10,000 (being the proportion of legal expenses attributable to the right to seek compensation)
Disposed of:	
July 1995	December 1995
Consideration:	
Nil	$40,000 (being $70,000 less the recoupment of $30,000)
CGT consequences:	
The disposal of the fossil occurred at the time it was returned to Barney. The reduction of the cost base to nil means that there are no CGT consequences for Fred. The legal expense incurred in relation to his claim against Barney cannot form part of the cost base of the fossil.	The legal action still relates to the underlying asset, being the fossil. However, the amount awarded represents recouped consideration. The additional $40,000 (which is the excess recoupment) is received in respect of the disposal of the cause of action. This results in a net capital gain of $30,000.

Example 4

180. Wayne purchased a farm in 1988 for $350,000. In 1993 Wayne granted an involuntary easement across one side of the property to the Electricity Authority for power lines and associated plant. Under the terms of the easement Wayne loses all right of access or entry onto that part of his land and it is surrounded by 2 metre high security fencing. For the grant of the easement Wayne receives $80,000. The legal expenses incurred by Wayne total $2,000.

181.

Relevant asset:	The farm
Acquired:	1988
Cost base:	$350,000
Disposed of:	Not applicable as there is no disposal of the farm
Consideration:	Not applicable
CGT consequences:	There is no actual disposal of the land. The total acquisition costs of the property are reduced by $80,000 (less the legal expenses).

Example 5

(Variation of Example 4)

182. If the property was originally acquired by Wayne prior to September 1985 there would be no CGT consequences in relation to the $80,000.

Example 6

183. On 25 August 1987 Benny commenced a delicatessen and cafe business in a NSW beach resort town. In its issue of 2 February 1992 the local newspaper carried an incorrect report that Benny had been fined for infringeing health regulations in the preparation of his food. Benny's sales dropped dramatically, and he was forced to incur substantial expenses for marketing and advertising to reassure his customers that the report was incorrect.

184. On 4 July 1992 Benny informed the paper he had commenced action to sue the paper for defamation, claiming compensation for lost profits, damage to his reputation and for the reduction in the value of his business. On 10 March 1993, before the matter went to court, Benny and the newspaper agreed to settle the matter. In return for Benny ceasing his legal action, the newspaper agreed to publish an

apology and pay Benny damages of $110,000. This payment comprises $60,000 for loss of profits, $20,000 for damage to Benny's reputation and $30,000 for the permanent reduction in the value of the business. Benny's legal costs were $10,000, which were **not** paid by the newspaper.

185.

Relevant asset:	
Goodwill	The right to seek compensation
Acquired:	
August 1987 when Benny commenced the business (see IT 2328)	February 1992 when the report was published
Cost base:	
% of legal costs ($3,000) (being an estimate of the costs related to this asset)	Nil acquisition cost plus % of legal costs ($7,000) (being an estimate of the costs related to this asset)
Disposed of:	
Not applicable as Benny still operates the business and has not disposed of any part of his goodwill	March 1993 being the date Benny accepted the settlement offer

Consideration:	
$30,000, which relates to the reduction in the value of the goodwill of the business, will result in a cost adjustment. Note that the total acquisition costs cannot be reduced below nil. The excess recoupment (being $30,000 less $3,000 costs) relates to the right to seek compensation.	$107,000 (being $80,000 plus the excess recoupment which relates to the damage to Benny's reputation) represents consideration for the disposal of his right to receive compensation.
CGT consequences:	
As Benny still owns the business, the receipt of compensation for the reduction in the value of goodwill will not affect this asset until the business is sold. The total acquisition costs of the goodwill are limited to a proportion of legal costs. This will be reduced by the compensation receipt to a nil amount.	Subsection 160ZA(4) exempts Benny from CGT in respect of that part of the consideration received (being $60,000) on the disposal of the right to seek compensation that is assessable under subsection 25(1). Subsection 160ZB(1) exempts the personal injury component ($20,000). The balance is assessable as a capital gain.

Example 7

(Variation of Example 1)

186. The State Authority is in some haste to acquire the land and therefore offers Wally an extra $50,000 to expedite the process. The contract for the sale specifies that $180,000 is for the acquisition of the land and the extra $50,000 represents an inducement payment.

187.

Relevant asset:	the right to enter on the land (being the right created and vested in the State Authority)
Acquired:	May 1994 (immediately before disposal)
Cost base:	a proportion of the legal expenses relating to the contract (the balance being attributable to the sale of the land)
Disposed of:	May 1994
Consideration:	$50,000
CGT consequences:	Subsection 160M(6) would apply to assess the capital gain. Even if subsection 160M(6) was found not to apply, the capital gain would be assessable under subsection 160M(7); the relevant asset being the notional asset created as a result of the operation of subsection 160M(7).

Note: See Example 1 for the effect of CGT on the other amount.

Example 8

188. On 4 July 1989 Marty acquired a rental property. In January 1990 the property was damaged by fire and Marty decided to sell it. On 15 March 1990 Waldo indicated to Marty that he was willing to buy the property for $200,000. On 20 March 1990 Marty engaged his solicitors Legal Eagles to act for him in the sale. Legal Eagles had also acted for Marty when he purchased the property. On 10 July 1990 contracts were exchanged with a requirement that the sale be settled one year later on 10 July 1991. The sale was not finalised on 10 July 1991 because of a delay in receiving a clearance from one of the local authorities. Waldo later exercised his right under the contract to repudiate the contract and claimed a refund of his deposit.

189. On 24 October 1991 Marty commenced legal action against Legal Eagles seeking damages for their negligence in not ensuring that the certificate was received by the proposed settlement date. On 20 December 1991 Legal Eagles advised Marty they were willing to negotiate a settlement. On 17 January 1992 Marty accepted and received compensation of $95,000 in settlement of his claim against Legal Eagles. At this date Marty had not sold the property.

Note: no part of the $95,000 represents a repayment of the deposit paid by Waldo.

190.

Relevant asset:	The right to seek compensation. The property is not the relevant asset as it was neither permanently damaged nor was its value permanently reduced by the actions of Legal Eagles.
Acquired:	July 1991. In July Legal Eagle's negligent action became apparent.
Cost base:	nil acquisition cost plus legal costs
Disposed of:	January 1992
Consideration:	$95,000
CGT consequences:	Marty will be assessed in the 1992 income tax year on the net capital gain.

Example 9

191. Alf is an interior designer who works from spacious offices, showrooms and workshops attached to his home, with space for customer parking on the premises. The business commenced in 1989 and Alf has a substantial client base and is well known in the industry. Alf's clients generally visit the showrooms to choose styles and approve orders. Early in May 1994 the local council commences road works which block the road on either side of Alf's premises for fourteen weeks. During this time he has no vehicular access to his premises. The council offers Alf $12,000 as compensation for the inconvenience and loss of access. Alf had not sought any compensation from the council; the offer of $12,000 was not solicited. Alf accepts the offer and receives payment on 28 May 1994.

Note: it is likely that subsection 25(1) would apply to assess this payment as income. However, the application of subsection 25(1) and consequently the application of subsection 160ZA(4) has not been considered for the purposes of this example.

192.

Relevant asset:	the notional asset created as a result of the operation of subsection 160M(7)
Acquired:	May 1994
Cost base:	nil
Disposed of:	May 1994
Consideration:	$12,000
CGT consequences:	Subsection 160M(6) would not apply as no asset has been created and subsequently vested in the local council. Alf has no right to demand payment; the council has made a public relations gesture in offering the payment. Subsection 160M(7) would apply to assess the capital gain of $12,000. The elements of the provision are satisfied: • the business has been affected by an act of the local council being the blocking of access to Alf's premises; • Alf has received $12,000 as a result of that act; and • the money was received to compensate for the council's exclusive use of the area.

Example 10

(Variation of example 9)

193. Alf and the local council enter into an agreement regarding Alf's loss of access. Under this agreement the council has exclusive use of the car park and the driveways on the premises and Alf will receive a payment of $12,000. Alf incurs legal expenses totalling $1,000.

194.

Relevant asset:	Alf's right to use the car park and access the premises
Acquired:	May 1994
Cost base:	$1,000
Disposed of:	May 1994
Consideration:	$12,000
CGT consequences:	Alf creates an asset by entering into the agreement with the local council. The asset is not in the form of corporeal property and the asset vests in the local council. Therefore subsection 160M(6) would apply and there is no need to consider subsection 160M(7).

Example 11

195. Alison, while on holidays at a beach resort in December 1992, was photographed in a compromising situation. The photographs were published in January 1993. Her four year contract as a children's television personality was due for renewal in February 1993. However, the contract was not renewed. Alison sued the photographer and the magazine for professional embarrassment and humiliation, breach of privacy and loss of future income. In so doing, she incurred legal costs of $30,000. The court awarded her $500,000 as an undissected lump sum compensation payment in full settlement of all of her claims. Alison is not able to make any reasonable apportionment against the separate heads of claim.

196.

Relevant asset:	The right to seek compensation.
Acquired:	At the time of publication of the photographs
Cost base:	Legal fees of $30,000 incurred in making the claim
Disposed of:	On judgment (obtaining the judgment debt)
Consideration:	$500,000
CGT consequences:	As the amount awarded was undissected, no part can be said to relate to any personal injury suffered by Alison. Accordingly, the whole amount represents consideration for the disposal of the right to seek compensation. Therefore no part of the $500,000 will be exempt in terms of 160ZB(1). If the amounts had been dissected by the court, or if Alison were able to provide a reasonable apportionment between the income and non-income amounts, the compensation for professional embarrassment and humiliation and breach of privacy would be exempt by virtue of subsection 160ZB(1).

Example 12

197. On 8 August 1989 David disturbed two prison escapees who were attempting to break into his car. He suffered serious head injuries as a result of being bashed by the men and spent 3 months recuperating in hospital. The escapees were later recaptured, found guilty of the assault and sentenced to an additional 2 years in jail.

198. In March 1991 David applied for and was awarded $30,000 compensation under the *NSW Victims Compensation Act 1987* for his pain and suffering resulting from the assault. Marina, David's wife, also received $20,000 compensation under this Act. She was able to establish that the fear she now had of driving a car alone was attributable to the bashing her husband had received and was therefore entitled to compensation for the loss of enjoyment of life.

199.

Relevant asset:	The right to seek compensation
Acquired:	August 1989
Cost base:	nil acquisition cost plus legal costs
Disposed of:	March 1991
Consideration:	David: $30,000 Marina: $20,000
CGT consequences:	Both David and Marina will be exempt under subsection 160ZB(1) as the compensation relates to their personal injury.

Example 13

200. In preparing for the wedding of her daughter, Patricia ordered three limousines to take the bride and groom and their families to the wedding and to the reception. On the day of the wedding only one car arrived, dirty and unserviced, and the families were required to find other ways of getting to the church on time. After hiring taxis they arrived late and dishevelled, Patricia having ripped her dress in getting into the taxi. Patricia sued the limousine company for personal damages. In awarding her compensation the magistrate awarded special damages of $10,000 in addition to the value of the torn dress and the travel costs, as a reflection of the special nature of the ruined event.

201.

Relevant asset:	The right to seek compensation. It is considered the whole of the amount of compensation relates to the disposal of that right.
Acquired:	At the time of the damage
Cost base:	Legal fees incurred in making the claim
Disposed of:	On judgment (obtaining the judgment debt)
Consideration:	$10,000 plus the other amounts
CGT consequences:	A net capital gain which will be subject to the exemption provided by subsection 160ZB(1).

Example 14

202. Arwen, an employee of Ferret & Son Pty Ltd, leaves the company when she is sexually harassed by a workmate. Arwen complains to the company and seeks compensation for the humiliation and indignity she has suffered. In return for signing an agreement in which she surrenders any rights she may have against the company, Arwen receives from the company an amount of $26,300. The payment is calculated on the basis of 3 months salary, including long service and annual leave entitlements. Arwen incurs legal fees of $6,500 in making this claim. At the time of receiving the payment Arwen is on paid leave.

203.

Relevant asset:	the right to seek compensation for the personal injury
Acquired:	at the time the harassment occurred
Cost base:	legal fees of $6,500
Disposed of:	on entering into the agreement with the company
Consideration:	the total amount received. While the amount of compensation was calculated by reference to her salary level, no part of the amount received is considered to constitute salary.
CGT consequences: be	a net capital gain of $19800, which will then subject to the exemption provided by subsection 160ZB(1). Accordingly, no part of the compensation will be subject to CGT.

Example 15

(Variation of Example 6)

204. The same facts as in Example 6 except that on 10 March 1993 Benny simply accepts a lump sum of $100,000 to settle the matter without any reference to the components of the payment. Benny does not provide a reasonable break-up of this payment, and does not furnish particulars of his claim for compensation.

205.

Relevant Asset:	The right to seek compensation
Acquired:	February 1992
Cost Base:	nil acquisition cost plus legal costs
Disposed of:	March 1993
Consideration:	$100,000
CGT consequences:	Benny will be assessed in the 1993 income tax year on the net capital gain. As no part of the compensation can be attributed to personal injury, the exemption under subsection 160ZB(1) is not available. If Benny had apportioned the lump sum amount on the basis of the amounts claimed by him as compensation, and this basis was reasonable, the apportioned amounts would have been treated for CGT purposes as in Example 6.

Example 16

206. Steven (the landlord) and Ken (the tenant) argue about the renewal of a commercial lease on the cessation of the current lease. Ken believes that after numerous conversations with Steven about the lease there clearly exists a verbal agreement for the lease to be extended. Steven is of the opinion that there is no such agreement. After Ken incurs $50,000 legal expenses in fighting for the continuation of the lease, Steven accepts that an agreement exists and pays Ken $40,000 in respect of his legal costs. The settlement documents provide that the new lease will start from the cessation of the current lease.

207.

Relevant asset:	New lease
Acquired:	At the time of entering new agreement
Cost base:	$10,000 (expenses of $50,000 less the recoupment of $40,000)
Disposed of:	No disposal
Consideration:	Not applicable as there has been no disposal at this point
CGT consequences:	The expenditure incurred on legal expenses relate to the acquisition of the new lease. The $40,000 received by Ken is a reimbursement of the acquisition costs and results in a reduction of the total acquisition costs. When the new lease expires there will be no consideration for the disposal of the lease. This will result in a capital loss of $10,000 for Ken.

Example 17

208. In 1990 Norm decided to sell his shop which he had rented since acquiring it on 15 December 1987. On advice from his real estate agent, Big City Realty, he agreed to them selling the property by auction. Before the auction took place Big City Realty advised him that there had been little interest shown in the property and that it would be unlikely that the auction would generate a reasonable sale price. He was also advised that the Pampered Pet chain was interested in purchasing the shop, but not by auction. On 6 April 1990, before the auction took place, Norm exchanged contracts with Pampered Pets to purchase the shop for $500,000. Norm later discovered that Pampered Pets had been willing to purchase the shop at the auction and that a sale price of greater than $500,000 would have been obtained.

209. Norm sued Big City Realty claiming damages, interest and costs as a result of their alleged breach of fiduciary duties. The court accepted that Big City Realty had breached its fiduciary duties and on 8 August 1991 awarded Norm $225,000 damages comprising $195,000 net additional proceeds that Norm would have received had the sale gone to auction and $30,000 punitive damages.

210.

Relevant asset:	
The property (shop)	notional asset created by the operation of the former subsection 160M(7)
Acquired:	
December 1987	August 1991
Cost base:	
Indexed cost base at time of sale plus % of legal costs	% of legal costs
Disposed of:	
April 1990	August 1991
Consideration:	
$695,000 (section 160ZF does not apply to increase the consideration by the amount of the damages - see TD 93/44. However, paragraph 160ZD(1)(a) provides that the $195,000 damages be included in the consideration, as the court by its decision has ruled in effect that Norm was entitled to have received consideration of $695,000 from the sale rather than the $500,000 price negotiated by Big City Realty.	$30,000
CGT consequences:	
Norm's net capital gain will be recalculated to reflect the increase in consideration from $500,000 to $695,000. His 1989/90 income tax assessment will be amended to include the additional amount of capital gain.	The former subsection 160M(7) will apply as the event occurred prior to 26 June 1992. Norm will be assessed in the 1991/92 income tax year on the excess of the punitive damages over the % of legal costs.

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