TD 92/D208 - Income tax: if an employee is paid by a dishonoured cheque, can he or she claim a deduction for a bad debt under section 63 of the Income Tax Assessment Act 1936?

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Draft Taxation Determination

Income tax: if an employee is paid by a dishonoured cheque, can he or she claim a deduction for a bad debt under section 63 of the *Income Tax Assessment Act 1936* ?

1. No, a salary or wage earner operates on a cash receipts basis and, by definition, can never have a bad debt for taxation purposes. As a consequence, he or she cannot claim a deduction under section 63.

2. However, this does not mean that the employee will be assessed on income that he or she has not actually received. Salary or wage income is only assessable when it has been derived, and salary or wages are only derived when paid. In *Tilley v Official Receiver in Bankrupcy* [1960] 103 CLR 529 at 535 Kitto J, in an observation on payment by cheque, stated that ' There can be no doubt that the acceptance of a payment by cheque implies, if there be nothing to the contrary, an agreement that it shall be considered as payment, subject to the condition subsequent that if the cheque be dishonoured it shall no longer be so considered.' In *Mackenzie v Rees* [1941] 65 CLR 1 at 15, Dixon J expressed a similar view.

3. In a New Zealand case, *Ullrich v Commissioner of Inland Revenue* [1963] 13 ATD 321 at 323, Perry J stated that an amount is derived by a person only where it has been ' credited in account or reinvested or accumulated or capitalised or carried to any reserve, sinking or insurance fund or otherwise dealt with in his interest or on his behalf.' His Honour reviewed the authorities on the subject of payment by cheque and concluded that they ' establish that the giving of a cheque is payment conditional on its being met '.

4. Accordingly, where salary or wages are paid by dishonoured cheques, there is no payment of salary, and hence no derivation of income.

Example: An employee receives a cheque on 29/6/92 for $500, which he includes in his tax return. On 20/7/92 the cheque is dishonoured. The employee cannot claim a deduction for a bad debt, but may amend his return to reduce his assessable income by $500.

Commissioner of Taxation
12/11/92

FOI INDEX DETAIL: Reference No.

Related Determinations:

Subject Ref: bad debts; employees

Legislative Ref: ITAA 63

Case Ref: Tilley v Official Receiver in Bankrupcy [1960] 103 CLR 529; Mackenzie v Rees [1941] 65 CLR 1; Ullrich v Commissioner Of Inland Revenue [1963] 13 ATD 321

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