TR 95/35 - Income tax: capital gains: treatment of compensation receipts

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This ruling contains references to repealed provisions, some of which may have been rewritten. The ruling still has effect. Paragraph 32 in TR 2006/10 provides further guidance on the status and binding effect of public rulings where the law has been repealed or repealed and rewritten. The legislative references at the end of the ruling indicate the repealed provisions and, where applicable, the rewritten provisions.

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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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*This Ruling, to the extent that it is capable of being a 'public ruling' in terms of Part IVAAA of the **Taxation Administration Act 1953**, is a public ruling for the purposes of that Part. Taxation Ruling TR 92/1 explains when a Ruling is a public ruling and how it is binding on the Commissioner.*

What this Ruling is about

Class of person/arrangement

1. This Ruling applies to a person who receives an amount as compensation. It considers the capital gains tax ('CGT') consequences for the recipient of the amount, 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, profits à prendre and licences - these are covered in detail in Taxation Ruling IT 2561 and in Taxation Determinations TD 93/235 and TD 93/236.

Key terms

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

Compensation receipt

A compensation receipt, or compensation, 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.

Exemplary or punitive damages

Exemplary or punitive damages include any amount awarded by the Court or agreed to by the parties over and above the amount required to restitute the plaintiff (taxpayer) for the damage suffered.

Exempt asset

An exempt asset is:

- an asset which is excluded from Part IIIA;
- an asset whose disposal is excluded from Part IIIA; or
- an asset whose capital gain or loss on disposal is excluded from Part IIIA.

Look-through approach

The look-through approach is 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.

Notional asset

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

Permanent damage or reduction in value

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.

Received

Received includes entitled to receive.

Right to seek compensation

The right to seek compensation is 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. A right to seek compensation is an asset for the purposes of Part IIIA. The right to seek compensation is acquired at the time of the compensable wrong or injury, and includes all of the rights arising during the process of pursuing the compensation claim. The right to seek compensation is disposed of when it is satisfied, surrendered, released or discharged.

Taxation adjustments

A taxation adjustment is any additional amount of compensation (e.g., a 'top-up') calculated to cover any income tax liability (including CGT) 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.

Total acquisition costs

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

25 June 1992 amendments

The amendments to section 160A and subsections 160M(6) and (7) made by the *Taxation Laws Amendment Act (No 4) 1992*, effective on and from 26 June 1992.

Underlying asset

The underlying asset is the asset that, using the 'look-through' approach, 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.

Undissected lump sum compensation receipt

An undissected lump sum compensation receipt is 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.

Ruling

Compensation for the disposal of an underlying asset

4. If an amount of compensation is received by a taxpayer wholly 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 consider that the amount is not consideration received for the disposal of any other asset, such as the right to seek compensation. Refer to Example 1 in this Ruling.

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. Refer to Example 2 in this Ruling. If the underlying asset was acquired by the taxpayer on or after 20 September 1985, a capital gain or loss may arise on the disposal.

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 a post-CGT 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 costs 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 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 total unindexed acquisition costs (including a deemed cost base) of the underlying asset, there are no CGT consequences in respect of the excess compensation amount.

8. The adjustment of the total acquisition costs effectively reduces those costs by the amount of the recoupment as if those costs had not been incurred. This means that indexation is not available in respect of the recouped amount. Refer to Examples 3 to 6 in this Ruling.

9. Compensation received by a taxpayer has no CGT consequences 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.

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 represents a recoupment of all or part of the total acquisition costs of the asset in terms of subsection 160ZH(11). Refer to Example 5 in this Ruling.

Disposal of the right to seek compensation

11. If the amount of compensation is not received in respect of any underlying asset, 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.

12. The cost base of the right to seek compensation is determined in accordance with the provisions of section 160ZH. The consideration in respect of the acquisition of the right to seek compensation, for the purposes of paragraph 160ZH(1)(a), includes the total acquisition costs incurred as a result of which the right to seek compensation arose. Refer to Example 9 in this Ruling.

Disposal of a notional asset

13. Generally, the amount of compensation is received by a taxpayer in respect of either an underlying asset or the disposal of the right to seek compensation (created and disposed of in accordance with subsection 160M(6) after the 25 June 1992 amendments). Accordingly, subsection 160M(7) does not apply to the compensation. If the amount does not relate to either the underlying asset or the right

to seek compensation, subsection 160M(7) may apply to the amount received. Refer to Examples 7 and 10 in this Ruling.

General concepts

Exempt assets

14. If an amount of compensation is received in respect of an underlying asset which is an exempt asset (e.g., a principal residence or an asset acquired before 20 September 1985) there are no CGT consequences. However, a taxable capital gain may arise if:

- there is an exempt underlying asset which has not been disposed of, or permanently damaged or permanently reduced in value;
- the requirements of subsections 160M(6) or 160M(7) are satisfied; and
- if the consideration is received by the taxpayer in respect of the disposal of the newly created or notional asset, being the most relevant asset.

Determining the relevant asset

15. 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

16. If the amount of compensation is received by the taxpayer partly for permanent damage suffered to, or a permanent reduction in the value of, an underlying asset of the taxpayer, that part of the receipt which represents a recoupment of part of the total acquisition costs incurred in respect of the underlying asset reduces the total acquisition costs.

17. The total acquisition costs 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 there are no CGT consequences in respect of the excess recoupment. Refer to Examples 3 and 6 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 Examples 12 and 13 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 14 to 17 in this Ruling.

20. Exemption under subsection 160ZB(1) is available if the taxpayer receives compensation in an undissected lump sum which relates wholly to the personal wrong or injury suffered by the taxpayer. Refer to Example 17 in this Ruling.

21. However, if compensation is received by a taxpayer in a lump sum paid in settlement of a number of claims, including a personal injury claim, and its individual components cannot be determined or reasonably estimated, no part of the compensation can be quantified as relating to the personal injury of the taxpayer. Accordingly, the exemption under subsection 160ZB(1) does not apply to any part of the compensation. Refer to Examples 12 and 13 in this Ruling.

22. 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

23. Sections 160ZZK and 160ZZL may provide roll-over relief if 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

24. 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

25. 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

26. 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. If the compensation cannot be dissected it is likely that the whole amount relates to the disposal of the right to seek compensation.

Taxation adjustments

27. 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

28. 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 taxation dispute in relation to an assessment of the taxpayer, where the settlement was 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

Compensation receipts

29.

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.** 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; 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), subsection 160M(6) (post-amendment), paragraph 160M(3)(b) and subsection 160ZB(1)**
D	**Act, transaction or event not covered by A, B, or C.** Subsection 160M(7) will apply. **Subsection 160M(7) (pre and post amendment)**

Explanations

General concepts

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

31. 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

32. '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 legal or equitable (paragraph 160A(a)).

33. 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.'

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

Before the 25 June 1992 amendments

35. Is a right to seek compensation an asset for CGT purposes before the amendments of 25 June 1992? This question has generated significant comment and discussion, although there is little judicial authority directly on point in Australia.

36. The United Kingdom capital gains tax legislation has generated a number of cases where the definition of 'asset' has been considered. 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 573:

> '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 whether a right to seek compensation is an asset for CGT purposes before the amendments. It is clear that there remains some uncertainty on the question 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.

39. One of the first significant cases on this issue is *Hepples v. FC of T* 91 ATC 4808; (1991) 22 ATR 465, which considered whether the right to work was an asset for the purposes of Part IIIA. 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.

40. In the Full Court of the Federal Court of Australia, Gummow J said that the words 'any other right' did not mean 'rights' in some popular and non-technical sense. His Honour concluded (90 ATC 4497 at 4514; (1990) 21 ATR 42 at 62):

> 'In my view, the content of para. (a) of sec. 160A is all forms of incorporeal property, not personal rights which do not answer that description. Further, 'incorporeal property' plainly is a technical term and that consideration supports the conclusion that it is not attached to the expression 'any form of property' in sec. 160A so as to stretch the reach of that expression to personal rights.'
>
> '...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".'

41. Gummow J further concluded (90 ATC at 4517; 21 ATR at 66):

> 'In my view, rights which are not proprietary in character ... whether because they are personal rights or because they are 'rights' merely in some popular sense, are not 'assets' within the meaning of sec.160A of the Act.'

42. Lockhart J commented, however, (90 ATC at 4508; 21 ATR at 55):

> 'I do not find it necessary to discuss in detail whether a relevant asset is an asset of a proprietary nature or may be a human right or a right to work or a right to trade. I am satisfied that, like subs (6) that precedes it, subs (7) is talking about rights of a proprietary nature...'

43. According to the Full Federal Court the essential characteristic of an item of property is that it can in some way be assigned, transmitted or turned to account with a third party. The following examples of items which are not proprietary in nature were suggested:

- the right to know;
- the right to privacy;
- constitutional and statutory guarantees which give rise to individual causes of action;
- the right or freedom of trade;
- the right or freedom to work;
- an equity to have the Court rectify a contract of personal services;
- a right to sue for unliquidated damages in tort for personal injury;
- rights which by virtue of statute cannot be assigned (e.g., the right to compensation under the *Trade Practices Act* for false or misleading conduct);
- the benefit of a contractual obligation where the identity of the person performing the contract is crucial to the contract (as in a contract for personal services);
- future property; and
- contingent interests which had not yet vested (e.g., the right of a discretionary object to a distribution of income that is contingent on the exercise of a power of appointment by a trustee).

44. The High Court of Australia in the *Hepples* case 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).

45. Brennan J concluded (91 ATC at 4813; 22 ATR at 471) that the right to trade, like the right to work, is not a form of property. McHugh J (91 ATC at 4841; 22 ATR at 503) also rejected that notion.

46. Gaudron J accepted the concept that the rights under the contract were 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 s.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.'

47. McHugh J suggested that a right to sue is a proprietary right once it is vested in the grantee. His Honour observed (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.'

48. Hill J also considered these issues in *Reuter v. FC of T* 93 ATC 4037; (1993) 24 ATR 527. In that case Mr Reuter entered into a covenant with Rothwells not to sue in relation to the payment of a fee, and in return for granting that covenant Mr Reuter received $8m. Hill J concluded that the taxpayer's right was a personal chose in action against Rothwells for the payment of a fee. His Honour referred to his earlier comments in *FC of T v. Cooling* 90 ATC 4472; (1990) 21 ATR 13, where he said, in relation to the reference in the legislation to an asset (90 ATC at 4486; 21 ATR at 28):

> 'what is comprehended is an item of property or an interest in property rather than rights of a non-proprietary kind.'

49. His Honour went on to say (93 ATC at 4050; 24 ATR at 543):

> 'In part this view was derived from the fact that an asset had to be capable of disposition to give rise to a taxable gain (unless otherwise a deemed disposition arose by virtue of the Statute). Secondly, the words "any other right" and the words "any other form of incorporeal property" in para. (a) of the definition suggested that ... it was only proprietary rights or interest that were included within the definition.'

50. In *Halwood Corporation Ltd v. Chief Commissioner of Stamp Duties (NSW)* 92 ATC 4155; (1992) 23 ATR 158, the Supreme Court considered whether the transfer of transferable floor space was the conveyance of property for the purposes of the stamp duty provisions.

The taxpayer argued that 'any other right or interest' for the purposes of that legislation was limited to proprietary interests, and transferable floor space was not proprietary in nature. Rather, the taxpayer argued, it was a mere expectancy, which did not confer any rights which were enforceable against any other person.

51. Loveday J referred to the tests set out in *National Provincial Bank Ltd v. Ainsworth* [1965] AC 1175 at 1247 per Wilberforce J (92 ATC at 4160; 23 ATR at 163-4):

> 'Before a right or an interest can be admitted into the category of property or of a right affecting property, it must be definable, identifiable by third parties, capable in its nature of assumption by third parties, and have some degree of permanence or stability.'

52. In finding that the transferable floor space is proprietary in nature, Loveday J recognised the commercial reality of the right. His Honour noted (92 ATC at 4161; 23 ATR at 164-5):

> 'The transferee of the transferable floor space has a right recognised by the council to have a development application considered by the council taking into account the existence of the transferable floor space. This is a valuable right not possessed by an applicant for development approval without transferable floor space. The reality is that commerce regards transferable floor space as a proprietary right. The courts should do likewise.'

53. 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.

54. The case involved the question 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.'

55. 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.'

56. Even if it is accepted that a right to seek compensation is a chose in action, it has been suggested that it is a personal chose in action, and, as a personal chose in action is unassignable, it cannot be a form of property. The ability to assign is only one of the features of an item of property. We do not believe that the lack of this ability precludes a personal chose in action from being an 'asset' for the purposes of section 160A. Further, McHugh J in the *Hepples* case appears to accept that a personal chose in action is an asset (refer paragraph 47 above).

57. 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:

> 'The phrase 'chose in action' is used in different senses, but its primary sense is that of a right enforceable by an action. It may also be used to describe the right of action itself, when considered as part of the property of the person entitled to sue. A right to sue for a sum of money is a chose in action, and it is a proprietary right.'

58. In *Provan v. HCL Real Estate Limited & Ors* 92 ATC 4644; (1992) 24 ATR 238, Rolfe J accepted that a compensation receipt could have CGT consequences. He said (92 ATC at 4652; 24 ATR at 245):

> 'But the judgment represents the fruits of the legal action, in respect of a cause of action which did not arise until October 1988.'

Further, he accepted the plaintiff's claim that the plaintiff's right to seek compensation was an asset and that there was a disposal of that asset on the obtaining by the plaintiff of the judgment debt.

59. Deputy President B J McMahon, in *Case 37/95* 95 ATC 331 at 335; *AAT Case 10260* (1995) 31 ATR 1016 at 1023 (on appeal as *FC of T v. Guy*), said that a 'right to sue' is almost by definition a chose in action. A chose in action has been defined as a right of proceeding in a Court of law to procure the payment of a sum of money or to recover pecuniary damages for the infliction of a wrong or the non-performance of a contract (PG Osborn, *A Concise Law Dictionary*).

60. The High Court in *Chamberlain v. DFC of T* 88 ATC 4323; (1988) 19 ATR 1060, when discussing a 'cause of action', in relation to litigation proceedings, cites the judgment of Brennan J in *Port Melbourne Authority v. Anshun Pty Ltd* (1981) 147 CLR 589 at 610 as an example of a decision discussing the imprecision in the words. The words are sometimes used to mean the facts which support a right to judgement, or a right which has been infringed, or the substance of an action as distinct from its form. A right to seek compensation falls within the imprecise use of the words 'cause of action'.

61. We accept that the position is not free from doubt. In the context of these decisions, however, we consider that there is sufficient authority to support our conclusion that a right to seek compensation is proprietary in nature. Accordingly, the definition of 'asset' before the 25 June 1992 amendments extends to cover a right to seek compensation.

Alternative view: the right to seek compensation

62. It has been suggested that the legislative framework of Part IIIA before the amendments supports the exclusion of a right to seek compensation from the definition of 'asset' for the purposes of section 160A. This argument suggests that section 160A defines asset exclusively, to include any form of property. A chose in action or right therefore still needs to be proprietary in nature to fall within the provisions. It is said that this argument is supported by the absence of any specific provision in section 160U to support the timing of acquisition of such a right. Further, it is suggested the fact that both sections 160A and 160U required amendment supports this reasoning.

63. We do not accept that the amendments to sections 160A and 160U are evidence that the sections did not apply to assets such as a right to seek compensation. Rather, the amendments were introduced in recognition of the concerns identified in the *Hepples* case, and elsewhere.

Alternative view: the right as a bundle of assets

64. It has been suggested that the legal process of resolving and enforcing a right to seek compensation 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. The original cause of action is 'replaced' by, or surrendered for, a judgment debt, which in turn is 'replaced' by a fresh or renewed cause of action and judgment debt, until all possible appeal rights have been satisfied.

65. 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. We believe that it is appropriate to consider the right to seek compensation as including the bundle of rights which may be said to arise and be extinguished during the finalisation of the litigation process.

Exempt assets

66. 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 for permanent damage to, or a permanent reduction in value of, an exempt underlying asset of the taxpayer, the compensation continues to be exempt from CGT.

67. 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 (e.g., because the asset is an exempt asset) compensation in respect of its disposal or a permanent decrease in its value should also be exempt.

68. Compensation received by a taxpayer by reason of an act, transaction or event in relation to, or affecting, an exempt underlying asset in terms of subsection 160M(7) (both before and after the 25 June 1992 amendments) may represent consideration received in respect of the disposal of the notional asset created by that subsection. In these circumstances that compensation amount is subject to Part IIIA.

Determining the relevant asset

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

1 an underlying asset (analysed in situations A and B; paragraphs 140 to 152 below);

2 a right to seek compensation (analysed in situation C; paragraphs 153 to 171 below); or

3 a notional asset, in terms of subsection 160M(7) (analysed in situation D; paragraphs 176 to 182 below).

The underlying asset approach

70. 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.

71. 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 for that negligence.

72. 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.

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

74. In *Case Z21* 92 ATC 218; *Case 7870* (1992) 23 ATR 1162, the Administrative Appeals Tribunal (P W Johnston, Deputy President) 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 Tribunal 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.

75. Although it considered it strictly unnecessary 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.

76. In Taxation Determinations TD 31 (Receipt by a taxpayer of insurance proceeds) and TD 57 (Compensation for uninsured items), we have used the approach of looking through the transaction that

gave rise to the compensation receipt to the most relevant asset relating to the receipt. 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.

77. 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 any 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.

78. 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. 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.

79. 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.'

80. 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.

81. 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.

The approach is also supported by subsection 160ZZH(3), which brings within Part IIIA the proceeds of disposal of the interests of an insured in an insurance policy only if the underlying asset to which the policy relates also falls within Part IIIA. If the asset which is damaged, lost or destroyed is an exempt asset, Part IIIA does not apply to the insurance proceeds.

82. 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 is not 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

83. 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 for a number of heads of claim (e.g., lost profits, interest and punitive damages), the amount also needs to be apportioned between the items.

84. 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.'

85. This provision requires the taxpayer to allocate receipts between the relevant assets. If the taxpayer allocates amounts between different assets on a reasonable basis we will generally accept that basis of allocation.

Acquisition of an asset

86. A right to seek compensation is not acquired as a result of any disposal by the grantor (i.e., the payer) of the 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 the *Hepples* case).

87. Of course, following the amendments to section 160A and subsection 160M(6), 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. Therefore, a right to seek compensation is created by the grantor and vested in the grantee.

88. Section 160U sets out the timing of acquisitions and disposals for the purposes of Part IIIA. Subsection 160U(4) provides that in the case of acquisitions or disposals other than under a contract the time of acquisition or disposal occurs at the time of the change in ownership of an asset. Where subsection 160M(6) applies, subparagraph 160U(6)(b)(i) provides that the time of acquisition of the right is the time of vesting. We believe that in the case of a right to seek compensation (where the asset comes into existence and vests in the owner of the asset, other than by acquiring the asset from another person), the time of change in ownership can be the time at which ownership commences.

89. In some cases the taxpayer may receive compensation for more than one related cause of action (e.g., in the *Provan* case, the taxpayer sought damages for negligence and for breach of contract and breach of fiduciary duty). While each separate cause of action is an asset, the right to seek compensation, for the purposes of this Ruling, encompasses all of those related assets. Of course, if the actions are not in any way related, each is an asset which must be considered in terms of the general provisions of Part IIIA.

Disposal of an asset

90. 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).

91. By paragraph 160M(3)(b), a change in the ownership of an asset (being a chose in action or any other right) occurs 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 receipt of the compensation following the granting by a Court of a judgment debt in favour of the taxpayer, or following a settlement entered into between the taxpayer and the defendant. There is a release, discharge or satisfaction of the right, and therefore a disposal of that right.

92. In the *Carborundum* case, Harper J found that paragraph 160M(3)(b) applies when the judgment debt is paid. It is then that the chose in action or the judgment debt is satisfied.

93. In some cases the taxpayer receives compensation consisting of a number of elements (for example, the actual compensation, interest, a taxation adjustment, and exemplary damages). For the purposes of determining the disposal consideration in respect of the right to seek compensation, or the amount which relates directly to the underlying asset for the purposes of applying subsection 160ZH(11), all of the relevant components of the compensation must be taken into account. For the purposes of subsection 160ZD(1), interest and taxation adjustments are as much part of the disposal consideration as the actual compensation component. Of course, for the purposes of determining the assessable income of the taxpayer under subsection 25(1), a different analysis may be necessary. Refer to Example 3 of this Ruling.

Determining the cost base of a right to seek compensation

94. The cost base of a right to seek compensation must be determined in accordance with section 160ZH. Paragraph 160ZH(1)(a) includes in the cost base any consideration in respect of the acquisition of the right. The expression 'consideration in respect of the acquisition of an asset' is defined in subsection 160ZH(4). The broad effect of this drafting device is that where reference is made in Part IIIA to 'consideration in respect of the acquisition of an asset', subject to subsections 160ZH(5) - 160ZH(14), paragraphs 160ZH(4)(a), (b) or (c) may be substituted.

95. The use of the word 'is' rather than 'includes' in subsection 160ZH(4) gives the expression 'consideration in respect of the acquisition of an asset' an exhaustive definition. The word 'is' in its context there has the meaning 'means'. Accordingly, money, property or money and property will only fall within the cost base for the purposes of paragraph 160ZH(1)(a) if it is paid or given by the taxpayer in respect of the acquisition of the asset within the terms of paragraph 160ZH(4)(a), (b) or (c).

96. There are a number of views on the potential width of the expression 'consideration in respect of the acquisition of an asset'. A narrow or strict interpretation of the expression effectively limits its application to the initial purchase cost of an asset. This effectively limits the 'consideration in respect of the acquisition of an asset' to costs or expenditure of a capital nature.

97. The consequence of this narrow interpretation is that any expenditure which results indirectly in the acquisition of the right to seek compensation cannot form part of the cost base of that right

(e.g., a right to seek compensation from a solicitor following negligent advice which results in the taxpayer incurring further expenditure). In effect, the taxpayer does not pay or give any money or property to acquire the right. Rather, the right simply arises as a consequence of the negligent advice. On this narrow view, although it might be said that money or property was paid or given as part of the larger transaction, it was not paid or given to acquire the right to seek compensation (e.g., the right of the taxpayer to claim from the solicitor or the right of the solicitor to claim under an insurance policy or professional indemnity policy).

98. We believe that it is appropriate that a wider view be taken of what money, property or money and property falls within the cost base because it is paid or given in respect of the acquisition of the asset in terms of paragraph 160ZH(4)(a), (b) or (c).

A wider view of 'consideration in respect of the acquisition of an asset'

99. 'Property' for the purposes of subsection 160ZH(4) has its ordinary meaning, albeit within the context of the section, and Part IIIA generally. Refer to the discussion in paragraphs 35 to 61 above.

100. If, in addition to paying money and giving property, something else is provided in acquiring an asset (e.g., an arrangement in the context of family dealings, which is not intended by the parties to create a contractual relationship) which is not in the form of money or property, only the money and property are taken into account for the purposes of determining the cost base of the asset under subsection 160ZH(4).

101. Broadly speaking, money, property, or money and property come within the cost base and are regarded as paid or given in respect of the acquisition of the asset in terms of paragraph 160ZH(4)(a), (b) or (c) if there is some direct and substantial link between the money or property and the acquisition of the asset. In determining whether there is a direct and substantial link, we believe it is appropriate to consider the following indicators:

- the necessity for the payment of money or the giving of property;
- the degree of temporal relationship between the payment of money or the giving of property and the acquisition of the asset;
- the purpose (objective and subjective) of the payment of money or the giving of property;
- the nature of the asset;

- the circumstances of the acquisition of the asset including:
  - parties (e.g., whether money paid or property given to a third party);
  - terms of the contract or agreement; and
  - arising from a wrong or by a lack of consent;
- the extent of causation;
- whether money paid or property given is in proportion to the value of the asset; and
- whether the degree of connection is diminished if money is paid or property is given for multiple benefits rather than solely to acquire the asset (e.g., for services).

102. The question whether a connection or link exists is a question of fact and degree.

103. On this wider interpretation of paragraph 160ZH(1)(a), expenditure or an outgoing forms part of the cost base of a right to seek compensation if there is a direct and substantial link between the expenditure or outgoing and the arising of the right to seek compensation.

104. If the right to seek compensation arises in respect of a monetary loss of the taxpayer (e.g., in respect of a claim for breach of contract, as a result of which the taxpayer must incur additional expenditure) the amount of that loss is included in the cost base of the right to seek compensation for that loss. It is an amount which the taxpayer has paid or is required to pay in respect of the acquisition of the right to seek compensation for having to incur the expenditure.

105. Similarly, if the taxpayer is insured under a contract of indemnity insurance and is liable to pay a claim covered by that policy (e.g., for a claim for negligent advice against the taxpayer), the amount of the claim paid by the taxpayer is included in the cost base of the taxpayer's right to claim against the insurer for indemnity under the policy. Refer to paragraphs 183 to 187 of this Ruling.

Application of the market value rules in determining the cost base of a right to seek compensation

106. If a taxpayer acquires an asset from another person and does not pay or give any consideration in respect of the acquisition, paragraph 160ZH(9)(a) deems the taxpayer to have paid or given as consideration an amount equal to the market value of the asset at the time.

107. The provision, however, does not apply if the acquisition of the asset from a person does not also involve its disposal (for the purposes of Part IIIA) by the person from whom it is acquired.

108. In relation to the acquisition of assets before 15 August 1989, paragraph 160ZH(9)(a) deems the cost base of the asset to be an amount equal to the market value of the asset if 'the taxpayer acquired the asset from another person and did not pay or give consideration in respect of the acquisition'.

109. In *Allina Pty Ltd v. FC of T* 91 ATC 4195; (1991) 21 ATR 1320, the Full Federal Court considered the meaning of the words 'acquired the asset from another person' in circumstances where the taxpayer had sold certain rights to subscribe for BHP Gold Mines Ltd shares granted to it by the Broken Hill Proprietary Co Ltd. The Commissioner included in the taxpayer's assessable income the total amount of consideration received for the disposal of the rights by the taxpayer. The taxpayer argued successfully that it had acquired the rights from BHP for no consideration and therefore it was deemed to have paid or given as consideration an amount equal to the market value of the rights at the time of acquisition (that being the same amount as was realised on the sale).

110. It was recognised by the Court (91 ATC at 4202; 21 ATR at 1327) that property can be acquired by one person without there being any disposition of that property by another person. However, the Court went on to say that the allotment of shares is an act of a company, the capital of which is the source of the allotment. The allottee acquires the shares from the company.

111. In considering a right to sue (e.g., in tort for negligence), McHugh J in the *Hepples* case suggested that a right to sue is a proprietary right once it is vested in the grantee (refer paragraph 47 of this Ruling).

112. While the plaintiff's right to sue is a chose in action and is property, the right is created at the time of the breach of duty or injury giving rise to the cause of action.

113. The circumstances in which a right to sue is vested in a plaintiff differ from those in the *Allina* case. A right to seek compensation is not granted by a person in the same way as an allotment of shares or a grant by a company to a shareholder of rights to subscribe for shares. The right to seek compensation only vests in the plaintiff on, and springs from, the breach of duty or injury. It is not acquired or obtained from another person. It follows that paragraph 160ZH(9)(a) does not apply to deem a market value cost base for the right to seek compensation.

Alternative view: potential application of paragraph 160ZH(9)(b)

114. It has also been suggested that paragraph 160ZH(9)(b) applies to give a right to seek compensation a cost base equivalent to its market value. We do not accept that the consideration given to acquire a right to seek compensation cannot be valued. As a matter of determining the damages necessary to compensate a plaintiff for his claims, the plaintiff, the other parties to a claim (e.g., the defendant or an insurer) or the Court take into account the likely cost or monetary loss suffered by the plaintiff. Paragraph 160ZH(9)(b) does not apply to give a market value cost base to the right to seek compensation.

Disposal consideration

115. 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 (emphasis added). In certain circumstances the market value of any property received as consideration is taken into account in determining the total disposal consideration.

116. 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.

Alternative view: application of section 160ZD

117. In the *Carborundum* case, 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.'

118. 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.'

119. 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.

120. 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.

121. Similarly, in applying the underlying asset approach 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.

122. The *Provan* case is an example of a plaintiff receiving additional consideration in respect of the disposal of the asset.

123. This case concerned an action by the owner of a rental property against the real estate agent who sold the property. Following the advice of the agent that there was limited interest in the property, it was not offered at auction. The property was sold for $1.9m, and after the sale the owner discovered that there had been other parties interested in purchasing the property for a higher amount. The owner sought compensation for the loss which resulted on the sale of the property, and sued the agent for breach of contract, breach of fiduciary duty and negligence.

124. Rolfe J found that the plaintiff was entitled to receive damages of $955,450 (plus an indemnity for any additional CGT liability which might arise in respect of the damages award). The damages amount was calculated by reference to the amount that would have been received if the property had been sold at auction. It effectively represented additional consideration received by the owner in respect of the disposal of the property.

Recoupment of cost amounts

125. The cost base of an asset is determined in accordance with section 160ZH. That section, broadly speaking, provides that

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 indexed for the purpose of calculating a capital gain.

126. 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).

127. The term 'recouped' has its ordinary 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 represents a recoupment of costs in certain cases.

128. In using the words 'by any person', subsection 160ZH(11) clearly contemplates that the taxpayer may receive, from someone other than the original vendor of the asset, recoupment of any part of the total acquisition costs incurred by the taxpayer.

129. The use of the words 'account shall not be taken of' suggests that the recouped total acquisition costs may be completely disregarded in determining the cost base of the asset. Further, the cost base, indexed cost base or reduced cost base of an asset is determined at the time of disposal of the asset. It is only then that the relevant cost calculations can be made.

130. If the taxpayer recoups 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 total acquisition costs 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 total acquisition costs to the time of disposal of the asset by the taxpayer.

131. Subsection 160ZH(11) may apply if the taxpayer receives compensation for the permanent damage to, or permanent reduction in the value of, a post-CGT underlying asset. If there is no disposal of the underlying asset at that time, we consider that the compensation is

a recoupment of part or all of the total acquisition costs of the underlying asset.

132. Subsection 160ZH(11) requires a taxpayer to exclude from the total acquisition costs of his or her asset any recouped amount. It 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, for example, the deemed disposal mechanism contained within section 160ZM).

133. Accordingly, if the amount of recoupment exceeds the taxpayer's total acquisition costs at the time of the compensation, the effect of subsection 160ZH(11) is to reduce the costs to zero. The excess of the recoupment over the costs in these circumstances does not represent a taxable capital gain derived from the disposal of that asset. There are no CGT consequences in respect of any excess. It follows that the whole consideration received on a later actual disposal of that asset by the taxpayer will be a taxable capital gain (unless the taxpayer incurs additional expenditure which forms part of the cost base of that asset).

134. The application of subsection 160ZH(11) if the compensation is attributable to an underlying asset which has not yet been disposed of by the taxpayer assumes that the compensation represents a recoupment of part or all of the total acquisition costs which would otherwise form part of the cost base of the underlying asset.

135. If the compensation is received for the actual or anticipated costs of repairing or remedying the permanent damage to the underlying asset, the recoupment in terms of subsection 160ZH(11) is a recoupment of that part of the cost base, rather than a recoupment of any part of the initial acquisition costs. Refer to Example 6 in this Ruling. It follows that if the taxpayer chooses not to incur the expenditure on the underlying asset for which he has been compensated, there is no recoupment which can fall within subsection 160ZH(11). In this situation the right to seek compensation is the most relevant asset in respect of which the compensation has been received.

136. Whether the underlying asset or the right to seek compensation is the most relevant asset in these circumstances cannot be determined until the underlying asset is disposed of by the taxpayer. It is only then that the cost base of that asset can be determined, and it is only then that the taxpayer can determine whether the recoupment under subsection 160ZH(11) is available (i.e., whether the expenditure necessary to remedy the damage to the underlying asset has actually been incurred by the taxpayer).

137. If, on the disposal of the underlying asset, the taxpayer determines that the right to seek compensation is the most relevant

asset, any capital gain or loss in respect of that asset must be considered and brought to account then (being the time of receipt of the judgment debt or settlement proceeds). It may therefore be necessary to go back and reconsider the taxpayer's assessment for the year of income in which that disposal occurred (subject to section 170).

138. Subsection 160ZH(11) may also apply if a taxpayer is compensated for having paid excessive consideration to acquire an asset. The amount referable to the overpayment is a recoupment of all or part of the total acquisition costs of the asset.

139. The *Carborundum* case is an example of a taxpayer receiving compensation for paying excessive consideration to acquire an asset. In that case, Harper J measured the damages by determining the difference between the actual purchase price and the price likely to be sought by a willing but not anxious vendor, being $75,000.

Compensation receipts: disposal of the underlying asset

When is the asset acquired?

140. 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?

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

When is the asset disposed of?

142. If the relevant asset is the underlying asset a disposal of the asset occurs 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 capital gain or loss arising on the disposal.

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

What is the consideration on disposal?

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

compensation may form part or all of the consideration in respect of the disposal of the underlying asset, and may be received by the taxpayer before or after the actual disposal of the underlying asset (e.g., as occurred in the *Provan* case).

What are the CGT consequences?

145. 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 capital gain or loss may arise on the disposal or part disposal of the underlying asset.

Compensation receipts: no disposal of underlying asset; permanent damage to or permanent reduction in value of the underlying asset

When is the asset acquired?

146. 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?

147. The cost base of the underlying asset is determined by section 160ZH. 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 (including the cost of repairing any permanent damage to the underlying asset) in terms of subsection 160ZH(11). If the compensation is received **partly** for the permanent damage to, or permanent reduction in value of, the underlying asset and partly for some other purpose, the compensation should be apportioned between the different amounts, and the total acquisition costs adjusted accordingly.

148. The adjustment of the costs effectively reduces the original total acquisition costs 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.

149. 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?

150. 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?

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

What are the CGT consequences?

152. The total acquisition costs of the asset are reduced in terms of subsection 160ZH(11). The taxpayer will lose the benefits of indexation in respect of that part of the cost base. Refer to paragraphs 125 to 139 of this Ruling.

Compensation receipts: disposal of the right to seek compensation

Before the 25 June 1992 amendments

When is that asset acquired?

153. The asset, being the right to seek compensation, is acquired at the time the damage, monetary loss 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. If a taxpayer chooses to pursue more than one basis of claim (e.g., a claim for negligence and a claim for breach of contract) in respect of a single wrong or breach, the right to seek compensation is acquired at the time of the first actionable wrong or breach.

Alternative view: time of acquisition of the right to seek compensation

154. 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.

155. 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 then that the rights to a remedy arise in the injured party. Indeed, for an action for assault and for some actions for negligence there needs to be an act done by a respondent which could be said to create a right to seek compensation.

156. While the plaintiff's right to seek compensation is a chose in action and property, we consider such a right is created, in an action for negligence or assault in tort, when the breach of duty or the assault occurred.

What is the cost base of the asset?

157. The cost base of the right to seek compensation is determined by section 160ZH. 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. Refer to paragraphs 106 to 114 of this Ruling.

When is the asset disposed of?

158. 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 (paragraph 160M(3)(b)). This is generally at the final 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 and receiving the compensation.

Alternative view: the disposal of a right to seek compensation

159. A chose in action is a right of proceeding in a Court of law to procure the payment of a sum of money or to recover pecuniary damages for the infliction of a wrong or the non-performance of a contract.

160. In the *Guy* case, Deputy President McMahon expressed the view that on commencement of proceedings in a Court, the right to sue becomes a former right and is subsumed into the Court proceedings. The case concerned an agreement to settle proceedings for breach of contract in which damages were sought. Mr McMahon went on to say that it was not until an order was made by the Court that there was a legal obligation to pay a sum of money in consideration of foregoing the right to sue and that, under the circumstances, he did not consider that there was disposal of the right to sue.

161. In the *Chamberlain* case**,** the High Court dealt with a matter in which the Commissioner sued the appellant on a cause of action for which he received judgment. Without seeking to have that judgment set aside or otherwise impugned on the ground that it had been entered into by mistake, the Commissioner then sought to sue again in respect of the same cause of action. Although this matter dealt with the doctrine of *res judicata*, the Court did give some guidance on what it considered happens to a right to sue.

162. Deane, Toohey and Gaudron JJ (88 ATC at 4327), formed the view that when the Commissioner obtained a judgment of the Court the cause of action on which he relied merges, thereby destroying its independent existence, for so long as that judgment stands. There is an inference that for so long as the Commissioner chooses not to challenge the judgment, he is considered to be satisfied with the order of the Court and has no further right to sue. Dawson J said (88 ATC at 4328):

> 'Once a cause of action has merged in a judgment it no longer exists to found another action.'

163. Accordingly, we consider that when the parties enter into an arrangement to settle a matter, the right to recover pecuniary damages is satisfied or surrendered. When a Court order is given the right is satisfied at law. In both cases the requirements of paragraph 160M(3)(b) are satisfied.

What is the consideration on disposal?

164. 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?

165. 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 capital gain or loss may arise on the disposal of that right, depending on the cost base of the asset.

166. In many cases there is both 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.

After the 25 June 1992 amendments

167. One of the features of the 25 June 1992 amendments 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?

168. 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 (i.e., for a right to seek compensation this is at the time of breach).

What is the cost base of the asset?

169. The cost base of the asset of the taxpayer is determined in accordance with section 160ZH, and includes the sum of money and the market value of property given as consideration for the creation of the asset. Refer to paragraphs 94 to 105 of this Ruling.

When is the asset disposed of?

170. 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?

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

Interaction between the underlying asset and the right to seek compensation

172. The cost base of the underlying asset cannot be finally determined until the disposal of the asset by the taxpayer. It is only then that the various requirements of subsection 160ZH(1), and of the cost base rules generally, can be identified and satisfied.

173. The underlying asset approach allows any consideration received in respect of the right to seek compensation to be attributed

to the underlying asset, where the underlying asset is the most relevant asset. Certain items of expenditure incurred by the taxpayer in the course of pursuing the damages claim, or in order to remedy the damage or injury, may relate most directly to the underlying asset, or to the right to seek compensation or may relate to both assets equally.

174. In determining the cost base of the underlying asset (to calculate the capital gain or loss on disposal, or to determine whether an adjustment of the cost base is required under subsection 160ZH(11)) or of the right to seek compensation, the expenditure or outgoings incurred by the taxpayer must be allocated to the most relevant asset. That expenditure should be allocated to the asset to which it most directly relates. The capital costs of repairing the damage to the underlying asset, for example, are most directly attributable to the cost base of the underlying asset, in terms of paragraph 160ZH(1)(c) (assuming that all of the requirements of that provision are satisfied). The legal costs connected with pursuing the right to seek compensation are most directly attributable to the right, and should be included in the cost base of the right. This may mean that the taxpayer incurs a capital loss on the disposal of the right to seek compensation.

175. If the costs relate to both assets, the costs should be apportioned between the two assets on a reasonable basis. For example, the costs of obtaining professional valuations in respect of a damaged underlying asset, which are used in the course of pursuing a claim for compensation may relate equally to both assets and should be apportioned between the two assets.

Compensation receipts: disposal of a notional asset

Before the 25 June 1992 amendments

176. Where the conditions of subsection 160M(7) are satisfied, the subsection deems the disposal of a new notional asset.

When is that asset acquired?

177. 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?

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

When is the asset disposed of?

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

What is the consideration on disposal?

180. The consideration on disposal of the notional asset is the compensation.

What are the CGT consequences?

181. A capital gain arises on the disposal of the notional asset. 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).

After the 25 June 1992 amendments

182. 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 176 to 181 of this Ruling.

Compensation received under a policy of insurance

183. Compensation received under a policy of insurance also relates to a right to seek compensation. On taking out a policy, an insurer enters into a contract under which it agrees to indemnify an insured against claims made against the insured for liability arising out of their negligence (e.g., as the operator of a motor vehicle, or as the provider of negligent advice). If the negligence of the insured results in injury or loss to a claimant which is covered by the policy, the claimant has a right to collect in damages from the insured, and the insured has a right under the policy to compel the insurer to meet the claim.

184. Ordinarily, this is done by the insurer making the payment directly to the claimant. The payment by the insurer to the claimant in

these circumstances discharges the liability of the insured to the claimant and also satisfies the obligations of the insurer under the policy.

185. The insured's right of indemnity under the policy is an asset, and for the purposes of this Ruling, falls within the definition of a right to seek compensation. This right of indemnity is acquired by the insured when the triggering event of the policy occurs (e.g., the motor vehicle accident). The payment of the claim by the insurer results in the disposal of the right of the insured in terms of paragraph 160M(3)(b). Under paragraph 160D(1)(a), the payment by the insurer directly to the claimant is deemed to have been received by the insured and paid by the insured to the claimant, in order to satisfy the insured's obligations.

186. The cost base of the right to seek compensation is determined in accordance with section 160ZH. Refer to paragraphs 94 to 105 of this Ruling. We consider that the amount which the insured is required to pay to the claimant forms part or all of the total acquisition costs of the right of the insured to seek compensation under the indemnity from the insurer.

187. The consideration in respect of the disposal of the claimant's right to seek compensation from the insured, and of the insured's right to seek compensation from the insurer, is the amount paid out by the insurer, adjusted by any additional amounts received by either the claimant or the insured (e.g., where the policy provides for the insured to pay the first part of the claim directly to the claimant).

Undissected lump sum compensation amounts

188. 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; (1984) 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'.

189. 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 the *Tinkler* case, 79 ATC at 4648; 10 ATR at 418).

Alternative view

190. 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.

191. 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.

192. 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.

193. 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.

194. 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).'

195. 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.

196. 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.

197. 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 may help to determine whether some of the claims satisfied by payment of the compensation are for a liquidated amount and whether individual claims can be identified.

198. 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.

199. *FC of T v. Spedley Securities Ltd* 88 ATC 4126; (1988) 19 ATR 938, concerned the assessability of a lump sum amount received as damages. The Full Federal Court concluded that the effect of a settlement is to finalise the cause of action. 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.

200. 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.

201. 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. We consider that the decision in the *Spedley* case (that is, that there was insufficient information to permit a dissection of the lump sum) is based on the particular facts, and is not likely to be commonly applied.

202. In *FC of T v. Northumberland Development* 95 ATC 4483; (1995) 31 ATR 161, Davies J said (95 ATC at 4483; 31 ATR at 164):

> 'It is not in dispute that a sum or sums received as compensation for the compulsory acquisition of property can be dissected or

apportioned into capital and income elements if there is an appropriate basis for doing so.'

203. If the compensation relates to a number of heads of claim, subsection 160ZD(4) requires the taxpayer to apportion the compensation on a reasonable basis to each of those claims. If the taxpayer cannot or does not make a reasonable estimate, valuation or calculation of the amounts which are reasonably attributable to each claim, we will make that allocation using the information which is available in relation to those claims.

204. If the compensation is unable to be allocated on any reasonable basis (for example, because there is insufficient information on the claims made or the basis of acceptance of the compensation) we consider that the whole amount of compensation must relate to the disposal of the right to seek compensation.

205. The Court in the *Spedley* case accepted that an effective discharge document signed by the taxpayer on settlement of all possible claims arising out of the termination bars any further legal proceedings. It effectively represents the surrender or satisfaction of the right to seek compensation.

206. It follows that if the compensation relates to a number of heads of claim, or causes of action, but the individual components of the compensation cannot be determined or estimated, no part of the compensation can be said to relate to any particular claim. If, for example, the total claim includes elements for some personal injury of the taxpayer the exemption which would otherwise be available under subsection 160ZB(1) does not apply to any part of the compensation.

207. Of course, if the taxpayer can show that all of the separate heads of claim relate to the personal injury of the taxpayer, and that there are no other non-personal injury elements of compensation within the total claim, the exemption under subsection 160ZB(1) continues to apply to the compensation.

208. It is likely that some information is available when a compensation claim is made which can be used to dissect a lump sum amount of compensation. Alternatively, the components of the lump sum ordinarily are able to be estimated or valued on a reasonable basis.

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

Exemption for personal wrong or injury

210. 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.

211. 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).

212. We accept that the phrase 'by way of' should be given a wide meaning (*Goldsbrough 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 (e.g., as a result of conciliation) where liability is not admitted by either party still represents a sum received 'by way of compensation' in terms of subsection 160ZB(1).

213. 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 defamation.

214. 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 discrimination, harassment and victimisation (or any directly related claims) arising out of State and Commonwealth anti-discrimination legislation, and wrongful dismissal.

215. 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. Draft Taxation Ruling TR 94/D20 also considers compensation for personal injury and makes it clear that damages in this context are generally received for the loss of earning capacity (and for claims such as future care costs) rather than for loss of

income. In all of these circumstances the exemption provided by subsection 160ZB(1) applies.

216. Compensation for any wrong or injury suffered by a company does 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.

217. Exemption under subsection 160ZB(1) is also available for an undissected lump sum compensation amount which is received by a taxpayer wholly in respect of the personal injury of the taxpayer. Refer to paragraph 207 of this Ruling.

Alternative view: application of section 160ZB(1)

218. It has been suggested that the exemption available under subsection 160ZB(1) does not extend to cover an amount of compensation received by the taxpayer in respect of an illness or disease.

219. 'Injury' is not defined in Part IIIA. Most of the case law in this area considers the meaning of the word 'injury' in the context of a person's working environment. The term is generally defined in the legislative enactments and in a number of jurisdictions the definition includes 'disease'. The key phrase in early workers' compensation legislation was 'personal injury by accident'. No reference was made to 'disease'. However, in interpreting the meaning of 'injury' the Courts included 'disease' (for example, *Innes or Grant v. G&G Kynoch* (1919) AC 765; *Martin v. Manchester Corporation* (1912) 106 LT 741; 28 TLR 344.)

220. Subsection 160ZB(1) does not require that an injury result from an accident; it only requires the fact of injury. We consider that the exemption provided by that subsection extends to cover compensation received by a taxpayer for an illness of the taxpayer.

Roll-over relief

Monetary compensation received - section 160ZZK

221. 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.

222. 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

223. 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

224. 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 - section 160ZZL

225. 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

226. 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**.

227. 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

228. 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 his or her goodwill, or whether there has been permanent damage to goodwill.

229. 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 in respect of the business to which the goodwill is attached. 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, any capital gain on disposal is subject to the specific exemption provided by section 160ZZR.

230. 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.

231. 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 that relates to the permanent damage or permanent reduction in value.

232. 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 that goodwill, or a temporary fluctuation in the value of the goodwill.

233. 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 is, of course, always a question to be determined in each case.

Interest

234. An award of compensation made to a taxpayer may include an amount of interest.

235. The case law in this area is not settled and seems to provide for differing treatment in situations involving damages for the resumption of property or the determination of personal damages, and between pre-judgment interest and post-judgment interest. The Courts also seem to distinguish between an independent right to interest and an incremental allowance which may be calculated in a similar manner to interest.

Alternative view: compensation in the nature of interest

236. 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, 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.

237. 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 compensation interest on the whole or part of the amount for the whole or part of the period to which the judgment relates.

238. Any interest awarded as part of compensation 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).

239. In the *Federal Wharf* case, the taxpayer received compensation on the compulsory acquisition of his property under the *Harbours Act*

1913 (South Australia). The relevant legislation provided for an additional amount by way of interest to be calculated from the time when the Minister entered into occupation, to the time of the payment of the compensation, and provided that the interest would be added to the compensation. The taxpayer argued that the interest component was in substance part of the compensation intended to rehabilitate the taxpayer.

240. Rich J, in considering whether the amount was of a capital or income nature, identified four criteria:

- that the sum was calculated and payable in respect of time;
- that the time started when the owner was deprived of the profitable enjoyment of his property;
- that the time ended with the payment of the compensation which represented the capital of the property; and
- that the interest was calculated on the sum ascertained to represent the capital value of the property of which the owner had been deprived.

241. Applying these criteria, Rich J found that the character of the interest payable under this legislation was that of recompense for loss of the use of the capital during a period of time in which it would earn income.

242. The question of the character of the interest component of a compensation amount has also been considered recently in *Haig v. FC of T* 94 ATC 5002; (1994) 29 ATR 619. The taxpayer's residence was resumed by the National Parks and Wildlife Service, and under the *Public Works Act* (NSW) he was entitled to an amount of compensation which included an amount of statutory interest of $145,660. The taxpayer argued unsuccessfully that the interest component of the compensation did not form part of his assessable income. He also argued that the interest should not be included in the relevant years of income as the original determination of the amount of compensation payable had been overturned and remitted to the Court for determination.

243. Neaves J held that interest payable under statutory provision on the amount of compensation payable for the resumption of real property forms part of the taxpayer's assessable income. Neaves J also held (94 ATC at 5008; 29 ATR at 625):

> 'The fact that the determination of the amount of compensation was required to be reconsidered cannot alter the character of the amounts received by the applicant in the relevant years of income. In the event that, as a result of the redetermination of the amount of compensation properly payable, the applicant is required to repay, and does in fact repay, any part of the

> amounts ... paid to him by way of interest, the question of amendment of the relevant assessments will arise.'

244. In the *Northumberland* case, the Court considered whether an amount forming part of the compensation for the compulsory acquisition of certain coal rights was in the nature of interest. The Full Federal Court distinguished between the steps involved in the calculation of compensation payable in a single lump sum and a sum of interest added to an amount of compensation. After considering the specific terms of the legislation under which the compensation rights arose, the Court concluded that no part of the compensation awarded was in the nature of interest. Rather, it was an amount paid for the acquisition of the capital asset.

245. Davies J also noted (95 ATC at 4485; 31 ATR at 165) that it was unlikely that a Court in this country would hold that an award of pre-judgment interest, forming part of an award of damages for personal injury, constituted an income receipt.

246. It is a question of fact to be determined in each case whether any part of the compensation received by a taxpayer is in the nature of interest. 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 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.

Note: Both the *Northumberland* case and the *Haig* case are currently the subject of further appeals.

Taxation adjustments

247. There has been a great deal of conflicting commentary on the issue whether compensation 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.

248. Recent cases have taken varying approaches to the question of any potential tax liability in relation to the compensation. 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.

249. In the *Tuite* case, Shepherdson J awarded to the plaintiffs an additional amount to cover the estimated taxation liability and sought an undertaking from the plaintiffs that if tax was assessed at

something less than the additional amount allowed, they would repay the balance to the defendants.

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

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

252. 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. His Honour was 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.'

253. 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.

How is an indemnity in respect of additional taxation liability treated for the purposes of Part IIIA?

254. An indemnity is a promise by the promisor that he or she will keep the promisee harmless against loss as a result of entering into a transaction with a third party (*Sunbird Plaza Pty Ltd v. Maloney* (1988) 166 CLR 245 at 254). The person who indemnifies another grants to that other person a right to resort to some property or some fund for the satisfaction of some demand made on them, or to make good a loss which one person has suffered in consequence of the act, default or omission of another. The amount payable is usually fixed by reference to the loss caused by the act, default, or omission.

255. An indemnity can be created by judicial decree (as in the *Provan* and *Tuite* cases), by legislative operation, or by agreement between the parties in an out-of-Court settlement. In the *Provan* case, Rolfe J granted an indemnity to the plaintiff for any CGT liability. In the *Tuite* case, Shepherdson J awarded an additional amount to cover the estimated taxation liability to the plaintiffs, and granted an indemnity to the defendants in respect of any excess.

256. Subsection 160ZD(1) provides the rules for determining the consideration in respect of the disposal of an asset. Paragraph 160ZD(1)(c) provides that if the taxpayer receives as consideration in respect of the disposal of an asset an amount of money and property other than money, the consideration is the sum of the money and the market value of the property. It is therefore necessary to determine whether an indemnity is property for the purposes of subsection 160ZD(1).

257. 'Property' has not been defined for the purposes of Part IIIA. Refer to paragraphs 35 to 61 above for the discussion on property and proprietary rights.

258. An indemnity is a personal obligation to pay, which creates contractual rights in the promisee, and which can be enforced by an action for breach of contract (*Halsbury's Laws of Australia*, Vol 14, at 401026). An indemnifier's obligation is independent of the obligations of the promisor, and is undertaken as a principal. As a contractual promise, an indemnity is a chose in action and assignable at law and in equity (*Loxton v. Moir* (1914) 18 CLR 360).

259. We believe that an indemnity is a form of property for the purposes of subsection 160ZD(1).

260. If the taxpayer receives both an amount of money and an indemnity as consideration in respect of the disposal of an asset, the disposal consideration is the sum of the money and the market value of the indemnity. Once determined, that disposal consideration is then applied to the disposal of the underlying asset, to the recoupment of the cost base of the underlying asset in terms of subsection 160ZH(11), or to the disposal of the right to seek compensation, or the notional asset, as appropriate.

261. Of course, an indemnity is an asset for the purposes of section 160A, and falls within the general provisions of Part IIIA. The indemnity is acquired on the disposal of the right to seek compensation. Its cost base is determined in accordance with subsection 160M(6B). The indemnity is disposed in terms of paragraph 160M(3)(b) when it is satisfied or surrendered in return for the receipt of money payable under the indemnity, or when the conditions of the indemnity have otherwise been satisfied. Alternatively, the indemnity may be disposed of by way of assignment

or by cancellation. A capital gain or loss may arise on the disposal of the indemnity.

Examples

Example 1

262. 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.

263.

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

264. Avery Landowner owns a large tract of land at Burn Creek, which he acquired in 1962. In July 1991, the Commonwealth compulsorily acquired 32 hectares of the land under the *Lands Acquisition Act 1989*. In accordance with the Act, Avery was entitled to receive compensation for the compulsory acquisition. The

Commonwealth valued the land at $600,000, 90% of which was advanced to Avery at the time of the acquisition, pending final determination of the value.

265.

Relevant asset:	The pre-CGT land
Acquired:	1962
Cost base:	Irrelevant
Disposed of:	July 1991
Consideration:	$600,000
CGT consequences:	There is no capital gain or loss. Even though the right to receive compensation for the compulsory acquisition of the land arose post-CGT, the most relevant asset is the underlying land, which is a pre-CGT asset.

Example 3

266. 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 infringing 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.

267. 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.

268.

Relevant asset:	
Goodwill	The right to seek compensation
Acquired:	
August 1987 when Benny commenced the business (see IT 2328)	February 1992
Cost base:	
$1,000, being an appropriate portion of the legal costs	$9,000, being an appropriate portion of the legal costs
Disposed of:	
Not applicable as Benny still operates the business and has not disposed of any part of his goodwill	March 1993
Consideration:	

$30,000, which relates to the reduction in the value of the goodwill of the business, will result in a cost adjustment. The total acquisition costs cannot be reduced below nil. There are no CGT consequences for the excess recoupment.	$80,000
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 $1,000 cost base of the goodwill is reduced to nil. There are no CGT consequences for the excess recoupment.	Benny derives a net capital gain of $71,000 in respect of the right to seek compensation. $20,000 (less a proportion of the legals) of this net capital gain relates to his personal injury claims. Accordingly this part of the capital gain is exempt under subsection 160ZB(1). The balance of the capital gain is likely to fall within subsection 160ZA(4), as the profits component is also assessable under the general income provisions.

Example 4

269. 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 an 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.

270.

Relevant asset:	New lease (section 160ZU)
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 relates 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. If there is no consideration on expiry of the lease Ken will incur a capital loss of $10,000.

Example 5

271. In May 1987 Lauren purchased land from Andrew for $150,000 on the basis that the local council had approved the land for subdivision. In October 1993 Lauren lodged a development application with the council. She was advised a month later that the original approval for subdivision was refused due to inaccurate information submitted by Andrew. Lauren sued Andrew for damages and in February 1994 received $15,000 compensation.

272.

Relevant Asset:	Land
Acquired:	May 1987
Cost Base:	$135,000 (total acquisition costs less the recoupment)
Disposed of:	Not applicable - Lauren still owns the land
Consideration:	$15,000 which relates to the reduction in the value of the land, and which is applied to reduce the total acquisition costs
CGT consequences:	The cost base adjustment is made to the unindexed total acquisition costs of the asset at the date compensation was received.

Example 6

273. Ken owns a rental property which he bought in May 1988 for $100,000. In July 1992 Dave, an employee of the Roads Authority (RA), was being trained in the use and operation of a steamroller. Dave, being a conscientious and diligent employee, decided to try out a few of his newly learned manoeuvres. Unfortunately, this took him past and through Ken's house. This resulted in severe damage to two of the front rooms of the house, and a partial collapse of the roof. Ken's tenants escaped without harm, by diving out of bed and out of the house. Ken is not insured against the damage.

274. In March 1993, Ken was awarded $50,000 in damages for his claim against the RA for negligence (the amount awarded to Ken related solely to the damage actually incurred). In April 1993, he spent $50,000 in repairing the damage to his house.

275.

Relevant asset:	The rental property
Acquired:	May 1988
Cost base:	$100,000 ($50,000 indexed from May 1988, and $50,000 indexed from April 1993)
Disposed of:	Not yet disposed of by Ken
Consideration:	$50,000 (applied to the total acquisition costs of $100,000)
CGT consequences:	There is no capital gain or loss at the time of the receipt of the compensation. At that time the total acquisition costs of the property were $100,000. This is reduced by the compensation, then later increased by the expenditure on the property.

276. What if Ken spent $50,000 in repairing the damage to his house before he received the compensation? Assume that the expenditure was incurred in February 1993, and in April 1993, Ken was awarded $50,000 in damages for his claim against the RA for negligence (the amount awarded to Ken related solely to the damage actually incurred).

277.

Relevant asset:	The rental property
Acquired:	May 1988
Cost base:	$100,000 (all indexed from May 1988)
Disposed of:	Not yet disposed of by Ken
Consideration:	$50,000 (applied to the total acquisition costs of $150,000)
CGT consequences:	There is no capital gain or loss at the time of the receipt of the compensation. At the time of receiving the compensation the total acquisition costs of the property were $150,000. The compensation relates most directly to the $50,000 expenditure incurred in February 1993, and in terms of subsection 160ZH(11), that expenditure is reduced by the recoupment.

278. What if Ken was awarded more than $100,000 for the damage to the property? Assume that Ken was awarded $115,000 in damages for his claim in March 1993 (the amount awarded to Ken related solely to the damage actually incurred). In April 1993, Ken spent $50,000 in repairing the damage to his house.

279.

Relevant asset:	The rental property
Acquired:	May 1988
Cost base:	$50,000 (indexed from April 1993)
Disposed of:	Not yet disposed of by Ken
Consideration:	$115,000 (applied to the total acquisition costs of $100,000)
CGT consequences:	There is no capital gain or loss at the time of the receipt of the compensation. At the time of receiving the compensation the total acquisition costs of the property were $100,000. This is reduced by the compensation to nil, then later increased by the expenditure on the property. There are no CGT consequences for the excess recoupment.

Example 7

280. 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.

281. 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.

282.

Relevant asset:	
The property (shop)	The 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. 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 before 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.

Example 8

283. On 4 July 1989 Marty acquired a rental property. In January 1990 Marty decided to sell the property. 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.

284. 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.

285.

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 (when 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

286. The Newco Superannuation Fund, relying on advice from its legal advisers, B Co, has been lodging taxation returns on the basis that it is a complying fund. Due to certain irregularities in its accounting and taxation records, amended assessments are raised against the super fund which it pays in February 1994. In April 1994, the fund commences legal action against its advisers, seeking to recover the additional tax liability and penalties, being $60,000. In June 1994 the fund receives $60,000 plus an amount to cover the legal costs of the fund from B Co.

287.

Relevant asset:	The right to seek compensation from the advisers
Acquired:	February 1994
Cost base:	The amount of additional tax and penalties plus any legal costs incurred in pursuing the claim against the advisers
Disposed of:	June 1994
Consideration:	$60,000 plus legal costs
CGT consequences:	There is no capital gain or loss

Example 10

288. 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.

289.

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 199
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 goodwill has been affected by an act or event (the local council blocking access to Alf's premises); • Alf has received $12,000 as a result of that act or event; and • the money was received to compensate for the council's exclusive use of the area.

Example 11 (Variation of example 10)

290. 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.

291.

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 12

292. 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, and the television show was cancelled. Alison also owned the production company which produced the television show. Alison sued the photographer and the magazine for professional embarrassment and humiliation, breach of privacy, loss of income, and reduction in the value of her shares in the production company. 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.

293.

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
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 $470,000 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 heads of claim, the compensation for professional embarrassment and humiliation and breach of privacy would be exempt by virtue of subsection 160ZB(1).

Example 13 (Variation of Example 3)

294. The same facts as in Example 3 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.

295.

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 3.

Example 14

296. 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.

297. 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 assault on her husband and was therefore entitled to compensation for the loss of enjoyment of life.

298.

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:	The amounts paid to both David and Marina will be exempt under subsection 160ZB(1) as the compensation relates to their personal injury.

Example 15

299. 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 damaged 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 ($1,500), as a reflection of the special nature of the ruined event.

300.

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 plus the costs of the dress, the limousine, and the taxi fares
Disposed of:	On judgment
Consideration:	$10,000 plus $1,500
CGT consequences:	A net capital gain which will be subject to the exemption provided by subsection 160ZB(1).

Example 16

301. Arwen, an employee of G Co, 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, and resigns from the company. 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, which commenced at the time of the harassment.

302.

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 and receiving the payment
Consideration:	The total amount received
CGT consequences:	A net capital gain of $19,800, which will then be subject to the exemption provided by subsection 160ZB(1). Accordingly, no part of the compensation will be subject to CGT.

Note: part of the amount may represent assessable income in terms of the general income provisions.

Example 17

303. Ruth Jones is a pedestrian who was badly injured when hit by a motor vehicle driven by Joe Smith. Ruth was a dancer with a promising career ahead of her. As a result of her injuries, she was unable to continue dancing, and required extensive physiotherapy in order to walk again. Joe was insured by the Emu Insurance Company which made a lump sum payment under that policy to Ruth of $1 million to cover all of her claims for loss of earning capacity, non-pecuniary loss, and hospital and other care costs. This amount is not dissected and there is no information available to Ruth to permit a dissection of the amount into its components.

304.

Relevant asset:	The right to seek compensation for the losses arising from the injury suffered
Acquired:	At the time of the injury
Cost base:	Legals and medical costs
Disposed of:	At the time of settling the claim against Joe and the insurance company
Consideration:	$1 million
CGT consequences:	The net capital gain will be wholly exempt under subsection 160ZB(1). Even though Ruth cannot estimate or otherwise determine the elements of the compensation, she can prove that the whole amount relates only to the right to seek compensation for the personal injury.

Example 18

305. Joe Bloggs is the driver of a vehicle which, in June 1994, is involved in an accident which causes substantial personal injury to a pedestrian, John Smith. Joe Bloggs has compulsory third party insurance with Ostrich Insurance Company. John sues Joe for $5 million for negligence and damages suffered. Following lengthy negotiations between the insurer and John's legal advisers, Ostrich Insurance agrees to pay a lump sum compensation amount of $3.5 million to John. This is paid in July 1995, when John signs a settlement agreement releasing both Ostrich Insurance and Joe from any further liability in respect of the accident.

306.

Relevant asset:	Joe's right to seek indemnity from Ostrich Insurance under the insurance policy
Acquired:	June 1994
Cost Base:	$3.5 million paid to John by Ostrich Insurance (ignoring any legals)
Disposed of:	On entering into the settlement agreement with John (July 1995)
Consideration:	$3.5 million, being the amount received from Ostrich Insurance and paid directly to John
CGT consequences:	No capital gain or loss arises for Joe (ignoring any legals)

Example 19

307. 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.

308.

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 (July 1995). This results in a capital gain of $20,000 on the disposal of the asset by Fred. In effect, the amount of compensation received relates to the disposal of the underlying asset, and no amount can be consideration received for the disposal of the right to seek compensation. Accordingly, there is no capital gain on the disposal of the right to seek compensation.

Example 20 (Variation of Example 19)

309. Continuing on from Example 19, 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.

310.

Relevant asset:	The underlying asset (the fossil)
Acquired:	July 1994
Cost base:	$50,000 ($30,000 initial cost plus $20,000 legal costs)
Disposed of:	July 1995
Consideration:	Nil
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 expenses incurred in relation to his claim against Barney form part of the cost base of the fossil. There are no CGT consequences in respect of the excess recoupment.

Example 21 (Variation of Example 1)

311. 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.

312.

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) applies to assess the capital gain. Even if subsection 160M(6) did not 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 22

313. XYZ (an accounting firm) is sued by its former client, BCD Ltd, over work done in carrying out a due diligence examination of a company acquired by BCD Ltd in June 1991. The company was acquired for consideration of $19m, which BCD Ltd now believes was excessive.

314. XYZ and BCD Ltd reach an out of Court settlement in March 1994, under which XYZ pays to BCD Ltd $1 million as compensation for the excess consideration paid to acquire the shares in the company, and in full settlement of all claims that BCD may have against XYZ or any of its principals. XYZ also incurs legal costs of $500,000 in defending the claim and in reaching the settlement.

315. XYZ has professional indemnity insurance coverage and their insurers agree to meet the full amount of the settlement including all legal costs, after adjusting for a deductible amount of $250,000. Under the terms of this agreement the insurers pay an amount of $750,000 directly to BCD Ltd in June 1994, and the balance of the legal costs ($500,000) to XYZ. At the same time XYZ pays the balance of the agreed settlement amount, $250,000, to BCD Ltd.

Consequences for BCD Ltd

316.

Relevant asset:	The shares acquired in the company
Acquired:	June 1991
Cost base:	$18 million (adjusted under subsection 160ZH(11))
Disposed of:	Not applicable. There has been no disposal by BCD Ltd of the shares.
Consideration:	Not applicable
CGT consequences:	There is no disposal of the underlying asset. The cost base of the shares is reduced by the recoupment (being $1 million).

Consequences for XYZ

317.

Relevant Asset:	The right to seek indemnity from the professional indemnity insurer
Acquired:	When the insurable event occurred (June 1991)
Cost Base:	The amount required to be paid to BCD Ltd plus the legals incurred in defending the claim ($1.5 million).
Disposed of:	At the time of entering into the settlement agreement (June 1994)
Consideration:	$1.25 million
CGT consequences:	A net capital loss of $250,000 may arise.

Note: XYZ may be able to claim the total of the amount to be paid to BCD Ltd and the legals costs as deductible expenditure under subsection 51(1). Further, the compensation received from the insurer may represent assessable income of XYZ under either subsection 25(1) or paragraph 26(j).

Example 23

318. Jill Jones invites her friend Mary Mills, to her home for dinner. Unfortunately, it is a dark and stormy night, and her friend slips and falls on Jill's front driveway. Mary suffers a broken leg, and on advice from her lawyer brother, decides to end her friendship with Jill and sue her for $10,000.

319. Jill does not have any insurance and therefore has no right of indemnity for any potential loss. In July 1995, before the matter gets to Court, the parties agree to a settlement under which Jill pays Mary $8,000 in full settlement of her claims.

Consequences for Mary

320. Mary derives a net capital gain of $8,000 (ignoring any legal costs) which relates wholly to her personal injury and is therefore exempt under subsection 160ZB(1).

Consequences for Jill

321. Jill has paid an amount of $8,000 to satisfy Mary's claims for compensation. That payment, however, does not relate to the acquisition of any asset by Jill. Accordingly, there is no capital loss in respect of the payment.

Example 24

322. On 30 September 1985 X Co entered into an agreement with Y Co to purchase for $3m a development site for the construction of a block of home units. The contract was based on Y Co's representations that the zoning permitted such a development. X Co's solicitor settled the purchase without checking the zoning certificate. When X Co lodged a development application, the zoning certificate showed that there was no such zoning and the site was subject to a restrictive heritage conservation order. By this time, Y Co had been liquidated. X Co sued its solicitor for damages.

323. X Co provided evidence at the hearing that the land was worth $1m, and would have been worth $4m at the time of entering into the contract had the zoning been as represented. X Co obtained $3.5m in damages from the solicitor, and the solicitor's insurers paid this amount on 30 September 1993. X Co's legals totalled $30,000. The award for damages did not include any additional amount for any potential taxation liability. The land was later sold by X Co on 31 December 1993 for $1m.

324.

Relevant asset:	The land
Acquired:	30 September 1985
Cost Base:	Nil (total acquisition cost of $3,030,000 reduced by the recoupment of $3,500,000)
Disposed of:	30 September 1993
Consideration:	$3.5 million, applied to the cost base
CGT consequences:	A net capital gain arises on the later disposal of the land for $1m

Example 25

325. Doctor Joseph is a GP with a small local practice which he acquired in 1972. In March 1991, one of Joseph's patients suffers from Joseph's professional negligence, and successfully sues Joseph for malpractice, receiving from Joseph in December 1991 an amount of $100,000. Joseph pays out the agreed settlement sum to his former

patient, and seeks recovery of that amount under the terms of his professional indemnity insurance policy. The insurance company pays out $100,000 to Joseph under the policy.

Consequences for the former patient

326.

Relevant asset:	The right to sue for malpractice
Acquired:	March 1991
Cost base:	Any legal costs connected with the claim. It may also include the costs of taking remedial action (e.g., additional surgery, etc).
Disposed of:	On entering into the settlement agreement with Joseph (December 1991)
Consideration:	$100,000
CGT consequences:	A net capital gain may arise which is then subject to the exemption under subsection 160ZB(1)

Note: subsection 25(1) may apply to assess any income components.

Consequences for Joseph

327.

Relevant asset:	The right to seek indemnity under the insurance policy
Acquired:	March 1991
Cost base:	Any legal costs connected with the claim. It also includes the payment to his former patient.
Disposed of:	On entering into the settlement agreement with his former patient (December 1991)
Consideration:	$100,000
CGT consequences:	No capital gain or loss arises

Note: there may be consequences under the general income tax provisions for the payment and the insurance recovery.

Example 26

328. Alex is a highly successful security consultant, running a business he commenced in 1982. In 1991, at the age of fifty, he decides to retire and sells his consultancy business to Simon, a colleague and former employee. The contract for sale includes a restrictive covenant, which effectively prohibits Alex from operating or being involved with any form of security operation within 500 km of his former business for a period of five years from the date of the contract.

329. In March 1993, Alex joins with his son to establish Nightwatch, a security service for the homes, shops and businesses in his local area. Simon successfully sues Alex for his breach of the covenant, and seeks damages on a number of heads of claim (including lost profits and the reduction in value of his goodwill). The Court awards damages of $10,000 for the breach of the covenant, but does not accept that there has been any damage to Simon's goodwill. Simon is also granted an injunction against Alex which effectively restrains his activities for the balance of the covenant term.

330.

Relevant asset:	The right to seek compensation for the breach of the terms of the covenant
Acquired:	March 1993
Cost base:	Any legal costs connected with the claim
Disposed of:	On judgment by the Court
Consideration:	$10,000
CGT consequences:	A capital gain or loss may arise. The rights under the covenant continue, and could not be said to be permanently damaged or reduced in value by Alex's breach of the covenant.

Example 27

331. Al is the manager of Chicago Shoe Company's major outlet. In February 1991 Al embezzles $2 million from moneys held in trust by Chicago Shoe Company for another associated company. Chicago Shoe Company discovers the loss and takes immediate action to recover the money. The company takes action against Al, Darcy Financial Services (their financial advisers) and the Polk Insurance Company. As a result of this action Chicago Shoe Company agrees to settle the claims and receives a total of $2.9 million in May 1993 ($1 million from Al, $700,000 from Darcy and $1.2 million from Polk).

332.

Relevant asset:	The right to seek compensation in respect of the theft
Acquired:	February 1991
Cost base:	$2 million plus legal fees
Disposed of:	On settlement (May 1993)
Consideration:	$2.9 million
CGT Consequences:	Chicago Shoe Company will be assessed on a net capital gain

Note: The loss cannot be claimed as a deduction under either section 71 or subsection 51(1) as it is capital in nature and not an inherent risk of carrying on the business of retail selling.

Example 28

333. Stephen is a junior executive with a company. As his home is in an area not serviced by public transport, he has acquired a car which he uses to travel to and from the office. On Saturday 1 April, Stephen parks his car at the local shopping mall's car park. While Stephen does his shopping, out in the car park Megan misjudges the width of her four wheel drive vehicle (complete with bull bar) and causes significant damage to Stephen's car. The damage requires his car to be off the road for several weeks, during which time Stephen is forced to travel to and from work by taxi.

334. Stephen takes action against Megan to recover the cost of repairs to his car together with the cost of the taxi travel to and from work to the extent that the cost exceeds his normal cost of travelling. On 25 June his action is successful and he later receives damages, which are clearly defined under separate heads in the award entered in the Court.

335.

Relevant asset:	The right to seek compensation
Acquired:	1 April
Cost base:	The additional costs of the taxi travel to and from work to the extent that the cost exceeds his normal cost of travelling
Disposed of:	25 June
Consideration:	That part of the payment which is specified in the award to be in respect of his claim for taxi fares

CGT Consequences:	The amount received for the cost of repairs will have no CGT consequences as the underlying asset (the car) is not an asset for CGT purposes. The amount received as reimbursement for the taxi fares should produce no capital gain or loss (consideration received equals cost base).

Note: Any amount specified in the judgment as received for his inconvenience or personal suffering would be exempt under subsection 160ZB(1).

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