Federal Court decision

SECRETARY TO DSS v READ
Federal Court of Australia
Decided: 10 March 1987 by Fisher, Spender and Pincus JJ.

This was an appeal from the AAT's decision in *Read* (1986) 33 *SSR* 420. The Tribunal had decided that extra units in a property trust, credited to a pensioner following a revaluation of the trust's assets, did not constitute 'income' for the purposes of the age pension income test. The AAT had stressed the distinction between income and capital receipts, and said that the extra units issued to the applicant were capital receipts.

The legislation
This appeal involved the interpretation of s.6(1) of the *Social Security Act*, which defines 'income' as meaning -

> 'personal earnings, moneys, valuable consideration or profits *whether of a capital nature or not* earned, derived or received by that person for the person's own use or benefit by any means from any source whatsoever, within or outside Australia . . .'

The italicised words were added to the definition following the AAT's decision in this matter, with effect from 27 October 1987.

'Income' includes capital
The Court decided that the s.6(1) definition of 'income' did not distinguish between receipts of income and receipts of a capital nature, as those terms were understood in trusts or income tax law.

This reading of the definition, the Court said, did not depend on but was reinforced by the 1986 amendment. Even without the qualifying phrase, the Court said, the definition was sufficiently broad to include what might otherwise be regarded as capital receipts. Consequently, the value of additional units in a property trust allotted to the applicant was to be treated as 'income' for the purposes of the age pension income test, the Court said.

The Court noted that the rules of the property trust provided for a revaluation of its assets every three years. On that basis, the Court said, Read could expect to receive extra units in the trust every three years. Accordingly, for the purposes of the income test, one third of the value of the extra units issued to her should be added to her income in each of three years.

Formal decision
The Federal Court set aside the decision of the AAT and remitted the matter to the Secretary to the DSS for calculation of the level of pension payable to Read.

Background

Child maintenance: discrimination under the income test

The *Social Security Act's* income test for sole parents has long been regarded as discouraging lone parents from trying to generate extra income, particularly from work. In 1985, for example, the combined effect of the income test and income tax meant that a widow's pensioner (which for present purposes includes a supporting parent's beneficiary) faced an effective marginal tax rate of 62.5% if she or he had private income above $77 a week.

On smaller incomes, the effect was much less severe - because of the tax threshold and because the *Social Security Act* allowed a pensioner 'free income' of $30 a week plus $6 a week for each dependent child: ss.63(2), 64(1)(a). In many ways, of course, this simply increased the disincentive effect of the higher marginal rates which cut in when the lone parent's income exceeded the social security and tax thresholds.

The *Social Security Act* has always provided special rules for dealing with child maintenance payments under its income test. The effect of s.64 was to include child maintenance over $6 a week in the pensioner's income: para.(1)(b). However, the section prevented 'double dipping' by reducing the extra 'free income' of $6 by the amount of maintenance (in most cases where maintenance was being paid, this would lead to elimination of that 'free income'): para.(1)(a).

The net effect of these provisions was to treat child maintenance in the same way as earned income of the pensioner for the purposes of the social security income test. Child maintenance payments were not included in the pensioner's taxable income but, because of the social security income test, there could be a disincentive to a sole parent seeking child maintenance from the non-custodial parent.

The 1985 poverty traps reduction legislation, which came into effect in July 1987, has increased the disincentive effect. The *Social Security (Poverty Traps Reduction) Act* 1985 raised the 'free income' for each dependent child to $12 a week. But the legislation did not change the formula for treating child maintenance as income of the pensioner. That is, child maintenance over $6 a week is still treated as income of the pensioner, although a lone parent receiving income other than child maintenance will have the first $12 disregarded for each child.

Take, for example, two lone parents, each with one child and each receiving widow's pension. The first lone parent receives no child maintenance but has a part-time job which pays her $100 a week. Of this amount, $52 a week will be disregarded ($40 a week for the pensioner and $12 a week for the child) and the balance will reduce the level of the lone parent's pension on the basis of 50c in the dollar - a reduction of $24 a week.

The second lone parent receives child maintenance of $30 a week and has a part-time job which pays her $70 a week. Of the total amount, $46 a week will be disregarded ($40 a week for the pensioner but only $6 of the child maintenance) and the balance will reduce the level of the lone parent's pension on the basis of 50c in the dollar - a reduction of $27 a week.

Why this discrimination against child maintenance? A spokesperson for the DSS has rejected the obvious explanation - that it was a mistake - and insisted that the anomaly is not unintended. Apparently, the explanation is that the DSS is still struggling to develop a coherent policy on child maintenance, following the government's commitment to making non-custodial parents contribute to the support of their children. Until the DSS develops that policy, it does not want to change the child maintenance provisions in the *Social Security Act* - or so the explanation goes. However, this explanation overlooks the fact that, by creating a discrimination between child maintenance income and other income with the 1985 amendments, the child maintenance provisions *have* been changed, even if the change is difficult to understand - let alone defend.

Peter Hanks