

Federal Court decisions

Income test: can losses be deducted from income?

GARVEY v SECRETARY TO DSS Federal Court of Australia

Decided: 18 March 1989 by Spender J. This was an appeal, under s.44 of the *AAT Act*, from a decision of the AAT given on 4 August 1988.

In that decision, the AAT had affirmed a DSS decision to reject Garvey's claim for invalid pension on the basis that his income precluded payment of any pension. The question raised in this appeal was whether the AAT had adopted the correct approach to calculating Garvey's income.

Income from various sources

Garvey and his wife (whose income was to be taken into account under s.3(5) of the *Social Security Act*) had income from several sources. These included his wife's salary from employment of \$23 779 a year, interest on bank and credit union deposits, debentures and shares of \$9204 a year, and rental from four properties (one of which was owned jointly with his wife) of \$16 396 a year.

The total income from these sources was \$47 657. Garvey claimed that he incurred expenses directly related to the rental properties of \$43 365 a year; and he sought to deduct that amount from his total income, leaving an annual net income of \$4292.

Should losses be 'quarantined'?

The AAT had affirmed the approach taken by the DSS, namely that the expenses related to the rental properties could only be deducted from the income related to those properties. The AAT had worked on the basis that each source of income was to be quarantined and that, if one of the sources of income produced a loss, that loss could not be deducted from the other sources of income. On this approach, the combined income of Garvey and his wife would have been \$23 779 (his wife's salary) plus \$9204 (from their investments).

The AAT had said that this result followed from the Federal Court's decision in *Haldane-Stevenson* (1985) 26 SSR 323.

The Federal Court referred to the High Court's decision in *Harris v Director-General of Social Security* (1985) 24 SSR 294, where the majority of the court had said that when determining a person's annual rate of income for the purposes of the income test, it was necessary 'to have regard to the pensioner's sources of income at that time and to define what each of those sources would yield over the period of a year...'. The Federal Court observed:

'In the present case there would be a negative yield from the rental properties. I find nothing incongruous in such a statement or idea. In my respectful opinion, there is no warrant for saying that if the yield from a particular source is negative it is to be ignored in the ascertainment of the annual rate of income.'

(Reasons, p.8)

Purpose of Social Security Act

Spender J then quoted extensively from the Federal Court's decision in *Haldane-Stevenson* (above), including the statement of Davies J that the *Social Security Act* was 'concerned with net earnings, moneys, valuable consideration and profits' and that it was 'the net income from each source which is to be taken into account in the calculation of a pensioner's annual rate of income'.

Spender J said that he did not read these observations as requiring that each source of income should be considered separately and its contribution to income be considered only if there was a positive net income from that source. Such a reading would be at odds with the purpose of the *Social Security Act*, as identified by Davies J, which was to provide for income maintenance.

Spender J noted that *Haldane-Stevenson* had been relied on in several AAT decisions as requiring 'a quarantining of each particular source of income' so that if a source of income actually produced a loss, that loss could not be set off against a profit from another source. These decisions included *Crosby* (1986) 30 SSR 375; *Selimovsky* (1989) 48 SSR 624 and *Shafer* (1983) 16 SSR 159. However, Spender J said that in his opinion the method adopted in those cases had been wrong:

'In my opinion, "income" as defined in the *Social Security Act* means the net income of a person and the rental losses are properly to be taken into account in ascertaining Mr Garvey's income...'

Accepting, as Davies J pointed out in *Haldane-Stevenson* . . . , that the *Social Security Act* is an Act providing for income maintenance, in my opinion the rental expenses have to be taken into account in determining the sum which is available for the maintenance of the pensioner.

An approach which results more closely in the real level of income, as opposed to a result which does not at all reflect the actual capacity of a person to maintain herself or himself.'

(Reasons, p.14)

Spender J said that where a pensioner operated two businesses, one of which produced a profit of \$20 000 and the other a loss of \$20 000 a year, 'it would be a denial of the purpose of the *Social Security Act* to conclude that his income was \$20 000 per year rather than zero': Reasons, p.15.

Problems of segregating 'sources of income'

Spender J said that the contrary view required each source of income to be identified and a notional audit carried out on the receipts and expenditure relating to that source. This could lead to real difficulties in deciding what should be treated as a single or separate source of income:

'is a diverse investment portfolio involving quite different types of investment, to be regarded as a single source of income, or is each particular investment to be regarded as a source of income. The answer to these questions could materially affect the result of the determination of a person's income, if sources of gross income which made a net loss are to be ignored and only sources of gross income which make a net profit are to be considered'.

(Reasons, p.15)

Spender J noted that, in the present case, it might be that Garvey would be affected by the assets test; and that, in any event, the impact of the income test on the pension payable to him would need to be calculated in the light of the principles developed in this decision.

Formal decision

The Federal Court allowed the appeal, set aside the decision of the AAT, and remitted the matter to the AAT 'to proceed in accordance with these reasons for judgment'.

[P.H.]

