Reye and his wife commenced receiving age pensions in 2001 and 2000 respectively and, upon the policy maturing in November 2001, Reye received a lump sum of $63,486. The sum comprised of $28,306, representing total premiums paid, and $35,180 which represented the total accumulated bonuses over 25 years. Centrelink decided to treat the latter sum as 'income' for a period of 12 months from February 2002, which resulted in a reduction in age pensions for the ensuing 12 months. The SSAT affirmed Centrelink's decision.

The issue

The AAT needed to determine whether the bonuses accumulated in the years prior to receipt of age pension were 'income' for the purposes of the social security law. If that was so, consideration needed to turn to whether the sum could be disregarded as an 'exempt lump sum'.

The law

Section 8(1) of the *Social Security Act 1991* ('the Act') broadly defines 'income' to include 'an amount earned, derived or received by the person for the person's own use or benefit'. Section 1073 provides for certain lump sums to be assessed over an ensuing 12-month period. Section 8(11) permits the Secretary to deem an amount or class of amounts as an 'exempt lump sum' with the following note:

> Note. Some examples of the kinds of lump sums that the Secretary may determine to be exempt lump sums include a lottery win or other windfall, a legacy or bequest, or a gift — if it is a one-off gift.

Discussion

The AAT commented that the definition of 'income' was indeed very broad and encompassed almost all money received, subject to the specified exemptions. The AAT thought the exclusion of the component representing total premiums paid was 'probably obvious' (Reasons, para. 9), but the position in relation to accumulated bonuses was not so clear.

It was submitted by Reye that the matter should be approached in exactly the same way it would have been if Reye had opened an interest bearing account and made periodic payments to it. Upon first applying for age pension, the balance would have been treated as an asset with only interest earned thereafter being 'income'. The Department submitted that there was a public policy requirement to direct public expenditure to those in actual need. Furthermore, there was no point in comparing bonuses to interest on bank accounts as such amounts were taxed in the year they accrued, but bonuses were not so treated.

The AAT did not accept the Department's submission:

> Whilst the Tribunal accepts that people should use their own resources before they call on public expenditure, the provisions of the social security legislation do not require them to be totally destitute before they get a benefit. The rate of payment of benefits is governed by an assets test and an income test. Those tests allow pensioners to have a certain amount by way of assets without affecting the rate of payments. The income test only relates to income received during the period when the pensioner is receiving a pension, not to income that was received when the pensioner was not receiving a pension. As noted above, not all monies received are treated as income for the purposes of calculating pensions.
>
> The fact that bonuses which accrue on an endowment policy are not declared as income, and no tax is payable on them, is irrelevant so far as this review is concerned. There are numerous examples of situations where people may increase their assets without paying tax on the increase ...

(Reasons, paras 14,15)

The AAT took a contrary view about 'income':

> It is the view of the Tribunal that in the case of Mr. and Mrs. Reye, that part of the lump sum which Mr. Reye received on the maturity of his insurance policy, which represented premiums plus bonuses accrued up until either of them began to receive social security benefits, represented part of his assets at that date and none of it was 'income' for the purposes of the Act. Consequently, the bonuses accrued prior to receipt of benefits was not '*ordinary income*' for the purposes of calculating the rate of payment of pensions.

(Reasons, para. 16)

Having reached that conclusion, the AAT decided it unnecessary to consider whether the amount was an 'exempt lump sum' for the purposes of s.8(11).

Formal decision

The AAT set aside the decision under review and directed that the portion of the lump sum which represented bonuses accumulated prior to 23 June 2000 was not 'income' for social security purposes.

[S.L.]

Age pension: meaning of 'loan'; relevance of financial hardship to waiver

SMART and SECRETARY TO THE DFaCS (No. 2002/293; 2002/294)

Decided: 22 December 2003 by D.G. Jarvis.

Background

Mr and Mrs Smart ran a furniture-making business in partnership for many years. They did not take profits, instead reinvesting funds back into the business. In 1990, they created W.L. & J.E. Smart Pty Ltd ('Smart Company') and a loan account was created to reflect the sale of the business, which included property, to Smart Company. A sum of $350,000 was also created as 'goodwill'. Mr and Mrs Smart successfully applied for age pensions on 18 April 1996 and disclosed they were self-employed and owned shares. Furthermore, they advised the business had ceased operating on 17 January 1996 when the building and equipment were destroyed by fire. The business was not revived, although the applicants' son continued to work in a 'hobby' capacity and continued to lodge tax returns. Although indicating in the original claim that a loan to the company existed, the applicants failed to do so in response to questions on subsequent review forms. Centrelink became aware of the erroneous assessment in 2001 and levied debts in the sums of $28,926.64 each.

The issue

The AAT was required to decide whether the indebtedness of Smart Company to the applicants was a 'loan' for the purposes of s.1122 of the *Social Security Act 1991* ('the Act'). If that was so, the Tribunal needed to decide if debts existed and whether there was any basis for waiver.

The law

Section 1122 of the Act provides as follows:

> 1122. If a person lends an amount after 27 October 1986, the value of the assets of the person for the purposes of this Act includes so much of that amount as remains unpaid but does not include any amount payable by way of interest under the loan.

Section 1237A(1) provides for waiver where a debt arises solely from administrative error and payments are received in good faith. Section

1237AAD permits waiver in 'special circumstances'.

Discussion

The crux of the Department's position was that the applicants obtained a benefit by the creation of the loan. The indebtedness was recorded as a loan in the books and the accounts were certified as correct by the applicants in their capacity as directors. The indebtedness had the quality of a loan as it was being repaid, a fact reflected in accounts from 1990 to 2001.

The AAT formed the view that even if the Department was correct in its submissions, it would not assist in arriving at a correct characterisation of the indebtedness. The AAT referred to *Gordon and Department of Social Security* (1992) 27 ALD 381 where Deputy President Forgie discussed loans being distinguished from other forms of indebtedness. After considering other authorities, the AAT stated:

> On the above authorities and on the material before me, I find that the indebtedness of Smart Company to the applicants did not constitute a '[lending] of an amount' or a 'loan' within the meaning of s.1122 of the Act. In the present matter, Smart Company did not pay any funds to the applicants that were then lent back to Smart Company. No doubt it was intended that the indebtedness would be repaid by Smart Company over time, but that does not alter the character of the indebtedness. Further, the reference in the accounts of Smart Company to the indebtedness as 'loans' did not, in my opinion, alter the character of the indebtedness. The indebtedness represented the unpaid purchase price of the assets sold by the applicants to the company, and the applicants had, in effect, provided vendor finance by not requiring the purchase price to be paid at the time of the transaction.

(Reasons, para. 29)

For completeness, the AAT addressed waiver 'in case I am wrong in my conclusion that the indebtedness is not a loan' (Reasons, para. 31). In relation to s.1237A(1), the Tribunal concluded the matter was not attended by any administrative error.

For the purposes of s.1237AAD, the AAT was satisfied the applicants had not 'knowingly' failed to fulfil their obligations. The AAT considered a number of factors amounted to 'special circumstances', including the goodwill artificially created by the former accountant, Mr Smart's poor education, the fact that the loans (if they existed) were valueless, the applicants' age and poor health, and the fire which destroyed the business.

The AAT considered the Department's submission that the applicants could call upon the family trust, which still retained real estate, to repay an outstanding loan of some $40,000. The Department suggested that fact militated against a suggestion of financial hardship and was a counter to s.1237AAD. The AAT, whilst accepting that the applicants could call upon the trust to repay, stated:

> Certainly financial hardship is often an important element in finding that there are special circumstances that make it desirable to waive the debt. Nevertheless, in Secretary, *Department of Social Security v Hales* (supra) French J said at 162 that the '*exclusion of financial hardship alone as a special circumstance does not mandate its inclusion in the range of matters constituting such circumstances for the purpose of enlivening the Secretary's discretion*'. I accordingly conclude that the absence of financial hardship does not exclude a finding of special circumstances under s.1237AAD(b) of the Act
>
> ...

(Reasons, para. 42)

Formal decision

The AAT directed that age pension entitlements be reassessed on the basis that the indebtedness of Smart Company to the applicants not be included as an asset for social security purposes and that sums recovered from the applicants towards the debts be refunded.

[S.L.]

Assets and income test: loan to trust and trust distributions

BROWN and SECRETARY TO THE DFaCS (No. 2004/48)

Decided: 22 January 2004 by G.A. Barton.

Background

Mr and Mrs Brown's rate of disability support pension and carer payment were reduced on the basis that their assets included an outstanding loan to a corporate trustee and that their income included a trust distribution.

Mr and Mrs Brown were beneficiaries of a family trust. They directed and controlled the corporate trustee which had acquired assets including shares, land and bank deposits using moneys loaned from them.

Prior to the date of claim the beneficiary loan accounts totalled $356,379.70, of which $141,000 had been deposited with a South African bank. Financial statements also showed that $14,232.13 was distributed to them equally by the trust.

The loans were not documented and were interest free.

In February 2001 the trustee paid Mr and Mrs Brown the balance of the moneys held in the South African bank which at this stage was $90,904.03, thus reducing their loan to $262.452.67. The amount of the loan was then taken to be forgiven from May 2001 when Mr Brown produced a balance sheet showing liabilities of the trustee to be nil.

Mr and Mrs Brown were assessed on the basis that they had an annual income of $25,442.62, including the trust distribution previously referred to and deemed income of $11,251.62, based on the asset of the gifted amount $252,452.67, moneys in bank accounts and various shares.

The issues

There were two issues raised by the applicants:

- they argued that any outstanding loan to the trustee should not include the loss of $50,016 made when the South African bank deposit was redeemed.
- that their income should not include distributions made from the trust as deemed income from the trust assets had already been included in their income.

The findings

The Tribunal found that the amount of $50,016 (being the difference between the amount deposited in the South African bank and the amount redeemed) constituted an amount that was unpaid at the relevant time. Consequently this was an amount that must be included in the value of the applicant's assets pursuant to s.1122 of the *Social Security Act 1991* ('the Act').

The applicants argued that the Tribunal should 'look through' the trust structure and view the trustee as an investment agent or manager, such that the South African deposits were an investment, for practical purposes, made by them.

The Tribunal found that it was not open to it to ignore the legal reality of the trust. There was no evidence that the trustee agreed to act merely as an agent.