Week 2 Notes

Ordinary Income- general

Define: "income according to ordinary concepts" and is assessable under s6-5 Income Tax Assessment Act 1997. A gain that is regarded by courts as being an income character will be ordinary income. (*Scott v Commissioner of Taxation, 1935*)

Categories of ordinary income: income from personal services & employment (salary), income from business (firm selling services) and income from property (rent/ dividend)

Prerequisites of ordinary income

NOTE: Must fulfil both prerequisites and characteristics > ordinary income
Gain can't be ordinary income if it's not cash/ cash convertible (*FCT v Cooke and Sherden, 1980*)

1. **Cash/ convertible to cash**

Item to be cash convertible needs to be readily convertible to cash e.g. car, real estate or transferrable holiday
Illegal to sell good > not cash convertible e.g. receipt of cigarettes as it's not illegal to sell w/o license

- *Payne v FCT, 1996*: Free flights as result of frequent flyer points NOT cash convertible as they couldn't be sold
- *Tennant v Smith, 1892*: Free accommodation not cash convertible
- *FCT v Cooke and Sherden, 1980*: Free holiday not cash convertible

Look at s15-2 and s21a if s6-5 doesn't apply

S21A ITAA 1936: Non-cash business benefits as being cash convertible

2. **Real gain to taxpayer**

Ordinary income if receipt is genuine gain (taxpayer is better off)

- Reimbursements for work related loss is NOT a real gain as it's only an reimbursement for an expense incurred on behalf of the employer
- Specific reimbursements are allowances (ordinary income)
- *Hochstrasser v Mayes, 1960*: Employer reimbursed for loss from selling employee's house to relocate for work not a real gain > taxpayer compensated for work-related exp. He was not better off (not a genuine gain)

Characteristics of ordinary income

FCT v Myer Emporium, 1987: Ordinary income despite not fulfilling charac. of ordinary income

1. **Regular/ periodical receipts**

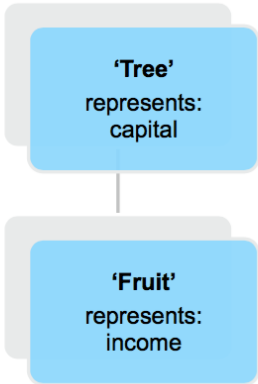
A gain that is regular/ periodic is more likely to be ordinary income than a gain that is paid as a lump sum. If the gain is regular, expected & depended upon for support > ordinary income. E.g. wages

- *FCT v Blake, 1984*: Regular payments > ordinary income
- *FCT v Harris, 1980*: One-off payment > Capital (NOT ordinary income)
- *Keily v FCT, 1983*: Government aged pension > ordinary income
- *Anstis v FCT, 2010*: Youth allowance > ordinary income
- *FCT v Dixon, 1952*: Top up payments (difference between former salary and current salary) > ordinary income

However, someone who receives a lump sum to do a one-off job and a one-off receipt of interest are ordinary incomes.

- *Premier Automatic Ticket Issuers v FCT, 1933*: Lump sum held to be ordinary income
- *Foley v Fletcher, 1843-1860*: Instalments for sale of capital asset > NOT ordinary income

2. Flow concept



Eisner v Macomber 252 US 189, 1920: Fruit & tree concept- tree: taxpayer's ability to work/ contract & fruit: payment for services
E.g. Capital: Appreciation of value of investment property.
Income: Rent of investment property

BOTH traits to be considered for ordinary income

a) Nexus (connection) with earning source
   i. Property e.g. rent has a nexus with property
   ii. Business e.g. firm's profit has nexus with business
   iii. Personal exertion e.g. salarty has nexus with employee providing services
b) Severable from earning source
   - Gain can be extracted w/o affecting the underlying earnings. E.g. Extracting rent has no affect on property
   - However, extracting goodwill from a restaurant will have an effect on the restaurant as it might affect the restaurant's reputation

Personal gifts & inheritances are NOT ordinary income or capital