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Assessment of Damages for Overseas Claimants

31 January 2017

VINCENTS

INTRODUCTION

The assessment of losses suffered by an overseas claimant are governed by the same underlying rules as any other claimant; namely a comparison of the notional benefits the claimant would have obtained but for an incident and the actual benefits they have / will obtain as a result of injuries sustained in the incident.

In nearly all instances, the more challenging aspect of assessing losses of an overseas claimant relate to the differences in the underlying components of the benefits received and issues surrounding the taxation and pension systems of the claimant's country of residence.

The recent decision of *Yamaguchi v Phipps & Anor* [2016] QSC 151, which involved a 23 year old Japanese national who was injured on her arrival in Cairns Australia, demonstrated the importance of thoroughly considering a number of issues when assessing the damages of an overseas claimant.

ISSUES THAT SHOULD BE CONSIDERED

Whilst many of the usual principles adopted (eg. career progression etc) will apply when assessing the damages of any overseas claimants, the following notable matters should be considered:

i. Income Tax returns;
ii. Earnings;
iii. Deductions;
iv. Income Tax;
v. Retirement age;
vi. Pension / Retirement System;
vii. Exchange rates; and
viii. Discounts for Contingencies / Vicissitudes.

I deal with the above issues separately hereunder.

INCOME TAX RETURNS

In my experience, whilst Income Tax returns from foreign countries may appear different in form, they generally attempt to capture similar information for their relative taxation authorities, notably the sources of taxable income and relevant deductions.

In Australia, taxpayers are required to lodge individual Income Tax returns; however in many countries there is an option to file "joint returns" with a spouse, which ordinarily provides more tax benefits than filing separate Income Tax returns. In these instances, it is important to identify the components of the taxable income and deductions which relate specifically to the claimant.

EARNINGS

As previously noted, ascertaining the notional and actual / residual earnings of an overseas claimant involves similar principles to that for Australian claimants (eg. career progressions etc).

In my experience when ascertaining a claimant's earnings the following factors should be taken into account:

i. Cultural Issues / Issues particular to certain countries;
ii. Other Benefits; and
iii. Currency Conversions.

Cultural Issues

In Australia, laws exist that are designed to protect the rights of people with disabilities however this is not necessarily the case in other countries. As a result, disability can have a profound impact on the level of earnings or employability of an injured claimant.

Other Benefits

In other countries, benefits other than standard wages / salary can be in a variety of different forms including, but not limited, to:

i. Employer benefits in the form of the provision of additional healthcare and pension benefits;
ii. Regulated bonuses. As an example, some countries have what is known as a 13th salary. In essence this is equivalent to a bonus equal to one month's salary and is ordinarily paid during December;
iii. Unregulated bonuses. As an example, in the United States there is a general expectation of a Christmas bonus; and
iv. Tips.

Currency Conversions

In some, but not all instances, it may be appropriate to use the earnings of a comparable position in Australia in an attempt to ascertain the equivalent earnings in another country.

In making any valid comparisons to earnings in Australia, it is necessary to adjust those earnings to the overseas country equivalent. This procedure is not just simply a currency conversion process, rather an adjustment must be made to take account of the relative purchasing power (i.e. standard of living) in each country.

DEDUCTIONS

Similar to an Australian claimant, when assessing the notional earnings of an overseas claimant it is important to consider the level of deductions to be taken into account in determining (i) the taxable income; and (ii) Income Tax that would be payable on the notional earnings.

With few exceptions, in Australia a taxpayer is required to substantiate and itemise any amounts ("itemised deductions") in order to claim an Income Tax deduction.

In contrast, in many other countries taxpayers have an option to claim deductions based on two different methods, namely the itemised deduction method or what is known as a "standard deduction" method.

The standard deduction is an amount which is stipulated under the relevant taxation regime and may be claimed without reference to any actual cost incurred. In these taxation regimes, taxpayers can claim the method which provides them with the highest deduction.

In such cases, it is important to recognise the difference between the two methods and the impact on the calculation of the claimant's Income Tax payable.

INCOME TAXES

Rates and Types

Ordinarily in calculating an assessment of economic loss, it is necessary to deduct taxation from the loss of income assessed.

Obviously the tax payable will be dependant on the rates and taxation regime of the claimant's residence.

Unlike Australia, in some countries the Income Tax rates are based on a number of factors other than income. Some examples include income taxes based on location (eg. state, canton, municipality or prefectural taxes), social security contributions, wealth and property taxes.

Whilst identifying and applying the relevant rates of Income Tax can be a difficult task, it is important to establish whether any lump sum payment for compensation is taxable in the claimant's country of residence.

Lump Sum Payments

As noted above, the assessment of economic loss ordinarily requires that taxation be deducted from the loss of income.

The principal that taxation should be deducted from a loss of earnings would appear to be founded on the basis that, in Australia, a lump sum compensation payment is exempt from Income Tax (i.e. not assessable as ordinary income)[1] on the basis that:

i. The Supreme Court of Queensland in *Groves* v *United Pacific Transport Pty Ltd and Thompson* (1965) Qd.R. 62 held that personal injuries compensation was 'really awarded for the impairment of the plaintiff's earning capacity that has resulted from his injuries';

ii. In *Atlas Tiles Ltd* v *Briers* (1978) 44 CLR 202, Barwick CJ held that 'earning capacity' was a capital asset;

iii. Accordingly, if a compensation sum is deemed to be capital in nature, then it is necessary to determine whether it is subject to the capital gains tax ("CGT") provisions. In this regard I note that there is an exempting provision[2] which disregards a capital gain derived by a taxpayer from a CGT event where it represents compensation received in respect of personal injury;

iv. The Australian Taxation Office allows the abovementioned exempting provision to apply even if a claimant is unable to dissect the separate components of their compensation; and[3]

v. Accordingly, not to deduct taxation would effectively overcompensate a claimant[4].

The difficulty arises where the claimant will not be a resident of Australia for taxation purposes and the damages will subject to the taxation laws of another country. In such circumstances, it is necessary to research whether any compensation for damages may be subject to taxation by a resident of another country (i.e. will those damages be exempt from taxation as they are in Australia).

In relation to the above, where an exemption does not exist, deducting Income Tax from the loss of earnings calculation and then again on receipt of the damages would mean that the claimant would incur the burden of taxation twice. First on the assessment of the damages, and subsequently on the taxation payable upon the receipt of damages.

[1] Section 6-5 of the *Income Tax Assessment Act 1997* (Cth)
[2] Section 118-37 of the *Income Tax Assessment Act 1997* (Cth)
[3] Example 17 of TR 1995/35
[4] For further information see generally the decision of *British Transport Commission v Gourley* [1956] AC 185 (HL) and *Cullen v Trappell* (1980) 146 CLR 1

In such circumstances, alternative approaches need to considered including, but not limited to, the following:

i. Calculating an additional head of damage for the level of additional taxation that would, in effect, restore the claimant to a position where the primary damages are net of tax;

ii. Seeking an indemnity from the defendant to cover the tax liability (if any) that will accrue as a result of the receipt of the primary damages (this in itself may be subject to taxation); and

iii. Seeking a private ruling from the relevant Taxation Authority as to whether the damages are subject to taxation and, if required, seeking some form of exemption.

RETIREMENT AGE

Whilst the intended date of retirement for any claimant is a question fact having regard to their personal circumstances, there has been a tendency to adopt the pensionable age as being representative of a claimant's likely date of retirement.

In such circumstances, the likely date will depend on the pensionable age in that country and may also be dependent on various factors including, but not limited, to the following:

i. The particular pension system;

ii. Whether the claimant is male or female;

iii. The industry the claimant worked in;

iv. The location the claimant worked in; and

v. The number of children reared by the claimant.

PENSION / RETIREMENT SYSTEMS

Traditionally, Courts in Australia have developed a “rule of thumb” approach in an attempt to simplify the calculation of loss of superannuation or pension, by applying a percentage to the past and future losses of income. Currently this would appear to be in the order of 11.33% of future losses.

While the “rule of thumb” approach provides for a convenient and simple method of assessment, in nearly all circumstances it leads to over or under compensation due predominantly to the variance in tax rates applying to income and superannuation.

Notwithstanding the above, it should be noted that many countries have pension systems which are vastly different to that of Australia, both in the manner in which pensions are calculated and the applicable rates.

Accordingly, the assessment of losses of pensions should not be ascertained with reference to a “rule of thumb” approach, but instead with reference to the actual system existing in the country in which the claimant resides.

EXCHANGE RATES

When the claimant resides overseas, the judgment for heads of loss such as past and future economic loss will normally be calculated and awarded in the claimant's currency of residence.

However, there will be heads of loss that will be expressed in Australian dollars, notably the assessment of general damages and any special damages. In such cases, the question will arise as to what is the appropriate exchange rate to use?

In *Yamaguchi v Phipps & Anor* [2016] QSC 151 it was decided that past losses should be converted using the average historical exchange rate from the date of accident to the trial date, and the rate should be based on commercial rates as distinct from the Reserve Bank of Australia rate.

CONTINGENCIES / VICISSITUDES

In many matters in Australia, the Courts have adopted deductions for vicissitudes of approximately 15% from the head of loss.

In some countries (notably Scandinavian countries), the rates of Income Tax are relatively high and specific contributions from the claimant's income are used to fund generous social security schemes which confer benefits including, but not limited to, the following:

i. Redundancy;
ii. Financial hardship;
iii. Disability;
iv. Retirement; or
v. Being forced to leave an industry.

Having regard to those social security schemes, the following relevant matters / impacts may be applicable:

i. Ordinarily an allowance is made for contingencies / vicissitudes in order to take account of items (i), (ii) and (iii) above;
ii. The provision of any benefits of this nature would, prima facie, reduce the level of contingencies / vicissitudes which relate to the claimant's earnings; however
iii. It is often difficult to ascertain the precise level of any reduction in the level of contingencies / vicissitudes which relate to the claimant's earnings.

In such cases it is important to acknowledge that the "standard" deduction for contingencies / vicissitudes of 15% may not be appropriate and a lower rate may be more appropriate.

CONCLUSION

When it comes to undertaking an assessment of losses suffered by an overseas claimant it is important that legal representatives are fully aware of the issues and unique circumstances which are likely to impact any claim.

In nearly all instances the more challenging aspect of assessing losses of an overseas claimant relate to the differences in the underlying components of the benefits received and issues surrounding the taxation and pension systems of the claimant's country of residence.

In my experience, any simple approach which does not take account of the issues about the claimant's residency and the impact thereof is likely to materially misstate the level of damages.

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ABOUT THE AUTHOR

Michael is a director in Vincents Chartered Accountants' Forensic Accounting unit. He is a Chartered Accountant and also possesses a Bachelor of Commerce.

His primary area of expertise is the calculation of economic loss resulting from personal injury disputes, dependency / compensation to relatives claims and the cost associated with modified motor vehicles. He has in excess of 19 years of experience as a forensic accountant.

Michael is the author of numerous papers including "Agreed statistical tables for loss of financial dependency in Australia" and "Personal Consumption Percentages in Australia – Current Tables for 2015".

Michael has prepared Overseas Assessments for persons who are residents of:

Austria, Bangladesh, Belgium, Canada, China, England, France, Germany, Hong Kong, India, Indonesia, Ireland, Israel, Japan, South Korea, Malaysia, New Zealand, Norway, Pakistan, Papua New Guinea, Republic of Mauritius, Serbia, Singapore, South Africa, Sweden, Switzerland, Taiwan, United Arab Emirates and the United States of America.

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