As a Matter of Interest...

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You are probably aware that interest has been receiving increased attention from the Tax Office in recent times; especially interest included in awards of damages and interest on early payments or overpayments of income tax.

Awards of damages
In September 1996, the Federal Court considered the assessability of interest included in awards of damages in the case *Whitaker v FCT* (96 ATC 4823).
That case involved a lady who had an eye operation which went wrong and who later sued her surgeon and was awarded damages. In that damages award were two components of interest: pre-judgement and post-judgement interest. The Court had to decide whether these amounts were genuine interest or whether they merely formed part of the damages awarded as compensation because damages for any wrong or injury suffered by a taxpayer to his or her person are exempt from capital gains tax pursuant to section 160ZB.

The Court held that both the interest components of the damages awarded were assessable as ordinary income and did not form part of the calculation of the quantum of damages.
Accordingly, Mrs Whitaker was assessable to income tax on these components of the damages awarded.
The results of this case will have to be borne in mind whenever determining the quantum of damages sought in a suit. It is interesting to note that if this case had of been settled out of court, the undissected lump sum received by Mrs Whitaker would most likely have been treated as entirely consisting of capital and therefore exempt from income tax.

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Interest on early payments or overpayments of tax
Many people are not aware that the Tax Office pays interest. The rates paid change every six months. For the six months ended 31 December 1996 the rate paid was 7.5% per annum and the rate currently being paid (to 30 June 1997) is 6.5%.

These rates are higher than the 5% or so currently being paid by banks on deposits.

The Tax Office will pay you interest when:-
- you pay your tax bill more than two weeks early; your assessment is amended resulting in an additional refund; or
- your refund is issued late by the Tax Office.

Some people are therefore deliberately paying their tax bills early to receive a better rate of return on their money than would be received from a bank.
Where the entitlement to interest arises because you have paid early, the interest must be calculated manually (as it is "too hard" for the Tax Office system to calculate) and either claimed as a credit on the next tax return or requested by cheque from the Tax Office. You can request a cheque from the Tax Office where the amount of interest is at least $5.00. Don't forget that interest received from the Tax Office is still assessable income and must be disclosed in your next tax return.

Income matching system
For some time now, investors have been required to quote their tax file numbers when opening bank accounts or making certain other investments. You should be aware that this quotation of tax file numbers is used by the investment bodies concerned to report to the Tax Office the interest paid.

After your tax return is keyed in at the Tax Office, the Tax Office computer adds up all the reported interest for your tax file number and matches it to the amount of interest declared in your tax return. If the amounts reported are greater than what is in your tax return, a letter requesting explanation is automatically generated. If you do not reply within one month, an amended assessment (including penalties) is raised.

You should therefore be particularly careful to declare all your interest income when preparing your income tax returns later this year.