



DAVEY'S Locker



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Termination of employment awards

All that glitters is not gold

by Tony Davey

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The draft Taxation Laws Amendment Bill, 2010 proposes legislative amendments giving effect to the intent stated in the February *Budget Review* (83 TSH 2010).

The objective of the amendments is to align the tax treatment of lump-sum payments received by retrenched employees, whether emanating directly from an employer or through withdrawal from a retirement fund.

Withdrawal-benefit amendments in 2009 provided that a lump-sum withdrawal benefit from a retirement fund arising upon retrenchment would qualify for the special retirement-table concessions, including the R300 000 exemption, which is cumulative of previous retirement awards arising after 1 October 2007.

A retrenchment award paid directly by an employer (as distinct from a retirement fund lump-sum withdrawal arising upon retrenchment) currently qualifies only for a R30 000 tax exemption under s 10(1)(x) of the Income Tax Act. The proposed amendment, effective as from March 2011, is to merge such awards for tax purposes into the retirement fund dispensation, with the effect that such employer-provided awards also qualify for the R300 000 exemp-

tion and the special retirement-table rates thereafter.

Since the retirement-table concessions are cumulative and hence aggregated, a retrenchment award will reduce the balance of the retirement fund tax-free benefit. This proposed concession is thus fool's gold for employees who are also members of a retirement fund—the previous combined exemption was R330 000.

On the other hand, employees of smaller firms who are not members of an employer-sponsored retirement fund registered under the Pension Funds Act will nevertheless benefit from an employer award of R300 000 tax free, instead of only R30 000.

The proposed amendments further provide that termination-of-service awards granted by an employer (termed a 'severance benefit') other than upon retrenchment (that is, upon attainment of age 55, sickness, accident, injury, physical or mental incapacity) will also qualify for the R300 000 tax-free benefit and the special retirement-table rates.

The proposed amendments to s 11(w), dramatically curtail the tax deduction of premiums paid by an employer under an insurance policy funding a deferred-compensation arrangement.

In essence, unless the benefit payable under the policy arises solely by reason of death, disablement or severe illness of an employee or director (or in qualifying commercial circumstances, such as the use of insurance as debt collateral), the s 11(w) tax deduction will no longer be available, with effect as from 1 January 2011.

In other words, long-term sal-

ary-structuring arrangements, known in insurance jargon as 'deferred compensation', which are employer-funded, will, as from 1 January 2011, no longer qualify for the insurance premium tax deduction. In my view, the amendment will put an end to such schemes, other than those maturing upon death or disability.

