



DAVEY'S Locker



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Severance benefits

Funding method is crucial

by Tony Davey

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'Tis the season for severance, courtesy of the current economic climate. If you receive a termination of service award (termed a 'severance benefit' in the Income Tax Act), various concessions apply, provided that your (ex) employer didn't fund it through an insurance policy.

The award is taxed under the retirement fund table (R315 000 exempt, the balance up to R630 000 at 18%, the balance up to R947 000 at 27%, and any excess at 36%. (Included are benefits from retirement funds.)

The following requirements must be satisfied:

- the amount must be paid for the relinquishment, termination, loss, repudiation, cancellation or variation of an office or employment or of an appointment;
- the payment must be made reasonably contemporaneously with the termination of employment or office; and
- any one of the following three situations must apply: (1) the exemption is obviously intended, exclusively, for employees or office holders who have come to the end of the employment road, so to speak, so that the award will not be exempt unless they have attained the age of 55 years; (2) the relinquish-

ment of employment or office must be due to sickness, accident, injury or incapacity through infirmity of mind or body; or (3) the employee's services are terminated owing to the employer's ceasing to carry on his trade or because the employee has become redundant; in addition, the employee must have become redundant owing to his employer having effected a general reduction in personnel or a reduction of personnel of a particular class.

The tax concessions will not apply if the employee or office holder at any time held more than 5% of the issued shares or members' interest in the employer company or close corporation, or if the severance benefit was funded by an insurance policy.

Herein lies the inequity. Thanks to the specific wording of the definition of a 'severance benefit', if the award from the employer is funded from cash reserves or an investment, the concessional tax treatment applies, but not if a policy was the funding medium.

So much for level playing fields in the taxation of savings.

