

NO TERMINAL PAY WITHOUT BURS' NOD: By Jonathan Hore

Retrenchments are never a pleasant experience and they negatively affect people both economically and socially. On the tax side of things, one needs to know that no employer must pay terminal payments to an employee or ex-employee without clearance from BURS. In today's article, I want to analyse the tax implications that arise from payments made on retrenchments. In this article, words importing the masculine shall be deemed to include the feminine.

THE CONCEPT

An interesting aspect is that the Income Tax Act does not define the term 'retrenchment package' but refers to the Employment Act. To avoid much legal jargon, let me use the definition made by the Business jargons website which states that retrenchments occur, 'when an organization aims at reducing its one or more business operations with the view to cut expenses and reach to a more stable financial position.' Whilst most of us associate retrenchments with the cutting down of employees, the term has a wider meaning and includes cutting down other businesses or operations, with the aim of containing costs or improving profitability. To keep things simple, we will concentrate on the retrenchment of employees.

BURS' clearance

Every employer should get BURS' approval to pay the terminal payments due to his employees by making an application in a prescribed form called ITW 6A. This is a requirement of the Income Tax Act and the reasoning behind it is for BURS to enforce collections of tax and filing of returns with as little effort as is possible. In any case, every employee wants their money when they are terminated and chances that they will clear their tax debts are high as there is a catch; the bucks.

If the employee owes BURS either unpaid taxes or outstanding tax returns, the ITW 6A clearance is declined. This technically means that the employee will not get paid his terminal payments and that puts him under immense pressure to resolve any outstanding tax issues. It must be noted that if an employer does not obtain BURS' concurrence on such payments, the taxman can in fact take them to task for failing to comply with the tax laws. This requirement is enshrined in the Fifth Schedule of the Income Tax Act and must always be adhered to. Having addressed this compliance matter, you may want to know how retrenchments are treated, from a tax perspective. I will analyse that in more detail below.

Tax treatment

The tax treatment of a retrenchment package is contained in section 32 of the Income Tax Act, which states that, 'where an employee receives a retrenchment package, one third of the amount received in money or money's worth or equivalent of the threshold, whichever is greater, shall be exempt from tax and at the option of the Commissioner, the remaining two thirds thereof may be deemed to have accrued at the time it is payable...' My apologies if it seems I am bombarding you with legal jargon but I thought one quote from the Act wouldn't hurt.

If an employee gets a retrenchment package, the first one third of the package escapes tax whilst the remaining two thirds suffer tax. For example, if such employee gets P 300 000 on retrenchment, the first P100 000 is exempt from tax whilst the balance of P 200 000 is subjected to tax, specifically PAYE. This treatment is similar to that accorded to gratuities and severance pay, which are also terminal payments.

Well folks, I hope that was insightful. As Yours Truly says goodbye, remember to pay to Caesar what belongs to him. If you want to join our Tax Whatsapp group or know more about our 9 Tax e-books, send me a text on the cell number below.