

Gratuity advances trigger tax penalties

It is general practice that gratuities are accessed at the end of an employment contract and by nature, they are terminal payments. However, it often happens that some employees access the gratuities through various forms, including getting advances against their gratuity and receiving monthly gratuity payments. These arrangements are put in place by employers but they have possible tax implications, which need to be considered.

It often happens that some employers choose to pay the gratuities to employees on a monthly basis and still apply the 33.33% tax exemption. Whilst that appears to be an innocent arrangement, it has the effect of distorting the whole gratuity concept. Put simply, a gratuity is paid whenever a contract is terminated or when it is terminated and then renewed. Paying the gratuity on a monthly basis gives the impression that the employer terminates and renews the employees' contract on a monthly basis, which is rather unusual. The effect of such an arrangement is that the gratuity loses its nature and therefore becomes taxable in full. The employee also loses on the tax exemption whilst the employer may be exposed to tax penalties and interest due to incorrect tax treatment of the gratuities.

Some employers have arrangements where employees access their gratuities in the form of advances. This then casts doubt on the tax treatment of such gratuity as it is solely supposed to be accessed at the end of the contract. Whilst there is nothing in black and white from BURS on this matter, our view is that any gratuity that is accessed before the contract ends is not eligible for the 33.33% tax exemption as its nature is distorted. This could also be an issue of contention in case of a tax audit by the taxman.

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