Dear Sir/Madam

CALL FOR COMMENTS: DRAFT INTERPRETATION NOTE – LONG SERVICE AWARDS

We refer to the call for comments on the Draft Interpretation Note on Long Service Awards (‘DIN’). Set out below please find the SAICA National Tax Committee’s submission comments.

Specific comments

Clause 4.1 – General Rule
The last paragraph of clause 4.1 refers to “…an asset at less than its’ actual value…”. The apostrophe in the word its’ is incorrect and should be removed.

Clause 4.2 – Nature of asset awarded
The DIN states that the term “money” is excluded from the scope of paragraph 2(a). The current practice adopted by most employers is to grant long service awards in cash. It is proposed that the tax-free amount, if this incentive is to be effective to the workforce, be
aligned with this practice and permit this exemption against long service awards granted in cash.

**Clause 4.3 – Unbroken period of service**

1. The first paragraph is directly from the Act, but it may be helpful to users to have an example of what is meant by “all assets awarded to the employee for long service during the year of assessment”.

2. Paragraph 5(4) of the Seventh Schedule (and the DIN) defines “long service” as an initial unbroken period of 15 years’ service, thereafter 10 years.
   - It is submitted that the long period in service requirement of 15 years (and thereafter 10 years) is an exceptional amount of time for the average South African taxpayer to be engaged in unbroken service to one employer.
   - This requirement is also inconsistent with the current Labour Law requirements which permit certain breaks to be taken from employment without affecting the “unbroken service” condition for labour purposes. The Labour Law deems an employee to be in continuous service should an employee resign and be re-employed within 6 months of the employee’s resignation.

The 15 years (thereafter 10 years) requirement presents challenges in that, for example, the unbroken period will not be met if the employee had during the initial or subsequent periods terminated his/her services with the employer for at least one day.

**Example**
The employee is employed on 1 April 1997
His services are terminated on 1 March 2009
The employee is re-employed on 2 March 2009.
He receives a 15 years long service award in May 2012.

**Result**
This award is fully taxable as the 15 years initial period of service was broken for a day.
3. In addition, employment records are not always readily available and it places an enormous administrative burden on employers to ensure that long service awards are correctly treated for employees’ tax purposes.

**Suggestion:**
It is proposed that the definition of “long service” be aligned to the practice currently prevailing, i.e. the tax incentive for long services be permitted every 5 years. This could be done on a “tranche” basis, for example, the existing tax-free amount of R5 000 could be split to R2 500 for the first 5 years and the remaining R2 500 for the next 5 years etc.

4. Although paragraph 5(4) of the Seventh Schedule does not explicitly require that the periods of unbroken service must be with the same employer and that the periods may not, for instance, have been served partly with an associated institution in relation to the employer, it is submitted that this is implied by the definition of ‘employee’ in paragraph 1 of the Seventh Schedule. We are therefore in agreement with the view expressed in the DIN. We however recommend that the DIN is expanded to deal with this aspect in more detail.

**Clause 4.4 – Consideration**
1. The following words should be inserted at the end of the last sentence of this paragraph to provide further clarity: “reduced by the lesser of R5 000 or the cost to the employer of all assets awarded to the employee for long service during the year of assessment as discussed in 4.3 above”.

**Clause 4.5 – Gift vouchers**
1. The DIN clarifies that a gift voucher constitutes an asset falling within the scope of paragraph 2(a) of the Seventh Schedule. We agree with this view.

2. We submit that this is a change in the practice generally prevailing that gift vouchers are akin to cash and therefore do not qualify for the long services award exemption. We recommend that the reason for the change in view is explained in the DIN.

3. One of the examples given in Example 3 refers to a Musica voucher. We submit that it may be unwise to use a legitimate/real business name in the DIN.
Other comments

1. We note that the DIN does not address the issue of a reimbursement as it applies to a long service award. For example, where an employee who has been employed by a company for an uninterrupted service of 15 years is given the flexibility of purchasing his/her own asset in recognition of his/her long service. Once the employee has purchased the asset he/she then provides the receipts to the employer and is reimbursed.

   Whether the employer purchases an asset and presents it to the employee or the employee purchases the gift and is refunded by the employer, ownership vests in the employee. Will such a reimbursement enjoy the same tax-free limit of R5 000 as offered by paragraph 5(2)(b) of the Seventh Schedule?

   Our view is that a reimbursement of this nature should attract the same tax treatment as a gift voucher in terms of paragraph 5(2)(b) of the Seventh Schedule. As in both instances, there is never an intention for ownership to vest in the employer at any point.

2. We recommend that the DIN be expanded to include a discussion of the treatment of VAT as it applies to “cost to employer”. In terms of section 18(3) of the VAT Act, the granting of fringe benefits to employees is deemed to be a supply made by a VAT vendor in the course or furtherance of his enterprise (excluding exempt supplies, zero rated supplies and supplies of entertainment). This enables a VAT vendor to claim an input deduction where an asset is acquired to give to an employee (except for the above exclusions). Therefore in terms of section 23C of the Income Tax Act, the VAT input has to be removed in the determination of the cost or the market value of the asset.

   It is submitted that the DIN does not address the fundamental shortcomings of the legislation in retaining talent in the global market. The tax legislation in respect of long service awards needs to be amended to address this issue. One would expect, for example, that the monetary amount (R5 000) would have been adjusted over the years to take inflation into account.

   We welcome SARS to engage with us to make submissions to redraft the legislation.
Please do not hesitate to contact us, should you have any questions regarding the above.

Yours faithfully

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