SUBMISSION: SCHOLARSHIPS AND BURSARIES AWARDED TO EMPLOYEES AND RELATIVES OF EMPLOYEES

Dear Madam,

Please find enclosed the SAICA National Tax Committee’s submission on bursaries awarded to employees and relatives of employees.

Legal background to the issues raised in this submission

Section 10(1)(q) of the Income Tax Act, No 58 of 1962 (the Act) provides for the exemption of scholarships or bursaries. This exemption applies in certain circumstances only when the scholarship or bursary was provided to employees and relatives of employees (this is covered in the proviso to section 10(1)(q)).

If the scholarship or bursary is granted to assist an employee the exemption will only be available if it is a requirement that the employee will reimburse the scholarship or bursary if he or she fails to complete his or her studies (unless this is due to death, ill health or injury.
With respect to a scholarship or bursary granted to a relative of an employee, the exemption will only be available if the remuneration derived by the employee does not exceed R100 000 during the year of assessment and only the first R10 000 of the scholarship or bursary will then be exempt.

It is not disputed that South Africa is still experiencing a skills shortage.

**Factual description of the issues**

Background information

Many employers provide bursaries and study loans to up-skill and develop employees and to assist relatives of employees to study and become skilled.

Employers are often committed to the continuous development of their employees and associated relatives. This contributes to the continued increase in education levels across the nation and should be encouraged by government in order to lessen the burden on the already over-extended education departments and tertiary institutions.

There are however a number of challenges that employers face in this arena. These are discussed further below.

1. **Monetary amounts**

**Legal nature of the issue**

The monetary amounts used in section 10(1)(q) have seen little adjustment for inflation since its introduction in 1992 (1992: R36 000 and R 1 200 respectively, 1997: R50 000 and R1 600, 2002: R60 000 and R 2000, 2006: the R2 000 was adjusted to R3 000 and then in 2008: R100 000 and R10 000).

**Factual description of the issue**
The monetary amounts in section 10(1)(q) do not take the increase in the cost of education in South Africa into account. The low remuneration value is limiting the availability of the benefit to very few individuals. The employers would provide bursaries but the result for employees will be that they will be taxed on a fringe benefit and therefore they cannot afford this benefit. Most employees will therefore not provide this assistance.

**Proposal**

The monetary amounts in section 10(1)(q) should be revised in line with inflationary changes. One option is to link the remuneration level to the annually changing Basic Conditions of Employment earnings threshold, currently R183 008. Another option would be to link it to the lowest tax bracket currently R160 000.

It should also be considered to remove the R10 000 limit in its entirety.

2. **The concept of “remuneration”**

**Legal nature of the issue**

The R100 000 amount in section 10(1)(q) refers to remuneration. Remuneration is not defined for purposes of the section and must therefore take its normal meaning. It is a very wide definition and will for instance include variable payments, discretionary payments and lump-sums.

Interpretation Note 66 confirms this and states that ‘The word “remuneration” refers to the amounts payable by the employer to an employee for services rendered or by virtue of employment ...It is clear, therefore, that the meaning of remuneration in this regard is not “remuneration” as defined in paragraph 1 of the Fourth Schedule to the Act.’

Section 10(1)(q) specifically refers to remuneration for the year of assessment.

**Factual description of the issue**

The problem that employers face is that it is unclear at what point remuneration for purposes of section 10(1)(q) is to be determined. The following practical problems illustrate the point:
• Changes in enrolment periods – If enrolment starts at the beginning of the year of assessment (1 March), the employer may have a very good idea of the remuneration for the year whereas enrolments in other months, the employer would not know what the remuneration for the year could be.
• Promotions / increases during the year may mean that the remuneration threshold will be exceeded during the year which will trigger tax consequences for the recipient of the employee. This must be an unintended consequence as the employee will have to pay tax on a tax free fringe benefit at time of award.
• Unexpected overtime or performance bonuses will trigger tax on a bursary awarded earlier in the year.

For example:

Employee A is on a R90 000 remuneration package. She therefore earns approximately R5 500 after employer contributions. Her daughter is studying at UNISA and is a recipient of a R9 000 bursary from her (Employee A’s) employer.

Based on the current scenario, the bursary is exempt from tax and is not a fringe benefit.

Should Employee A become entitled to a significant amount of overtime in one period or receive a discretionary bonus, the bursary which has been exempt form tax for most of the year will now become subject to tax.

This becomes a practical payroll issue and requires a continuous monitoring process to determine when the remuneration exceeds the monetary amount (the R100 000 remuneration limit) which is administratively burdensome. It is creates uncertainty for the employees concerned as for a part of the year a scholarship or bursary that was been exempt from tax becomes subject to tax during the year. The tax that results from this may have a significant impact on the employees’ net pay.
Many employers do not have the resources to manage full bursary schemes or to fund payments upfront to institutions or to manage approval processes in time for registration dates to be met.

Proposal

It is suggested that section 10(1)(q) is amended to allow the employer to determine the application of the exemption based on the fact that the employer is satisfied that at the time the award is made, the remuneration of the employee for the year of assessment is not expected to exceed the monetary amount for that year.

It is also proposed that remuneration for purposes of this section is defined more narrowly than in the Fourth Schedule by restricting remuneration to the cost to the employer and excluding any lump sum payments, share gains and variable payments.

3. Method of payment

Legal nature of the issue

Section 10(1)(q) does not stipulate the manner in which the scholarship or bursary is to be awarded or funded. The Interpretation note refers to “financial or similar assistance granted to enable a person to study” and then provides some examples of what a bona fide scholarship or bursary would include. It specifically states that “a reward or reimbursement of study expenses ... after completion of studies” will not qualify for the exemption and then deals with study loans.

Factual description of the issue

The following challenges are experienced by employers:

- The law does not stipulate how the award or funding is to be made and the Interpretation Note is too restrictive. This prevents many employers from implementing bursary schemes.

The Interpretation Note does not take into account commercial realities. Other payment methodologies used in practice include the creation of a staff loan or the reimbursement of expenses incurred particularly in cases where payment to the institution cannot take place in
time for registration and the employee is forced to fund the upfront payment themselves to guarantee a position. The following scenarios explain the problem:

- The provision of a loan to further studies does not in itself constitute a taxable benefit; however, the waiver of such a loan on completion of studies does create a taxable event.
- The payment of fees directly to an institution does not constitute a taxable benefit; however, payment to the employee to reimburse for expenses paid to the same institution does create a taxable event.

For many employers, the award of scholarships or bursaries is an *ad hoc* function and the current practice does not provide the employer with flexibility in payment options.

**Proposal**

It is proposed that where the true nature of the payment, in whatever form, is for the purpose of enabling an employee or relative of an employee to enable or assist a person to study then the section 10(1)(q) exemption should apply. The proposal is in essence that other mechanisms of funding should therefore be permitted.

National Treasury should be encouraging employers to fund these studies as it eases the burden on the state in terms of education as well as for future social grants as more individuals will be qualified to earn a liveable wage.

Please do not hesitate to contact us, should you have any questions regarding the submission.

Yours faithfully

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