The Taxation of Employment Law Awards and Settlements - Nothing to be frightened about - This is about the nuances of words not mere sums.

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INTRODUCTION

When you mention the word "tax" to some Employment Lawyers and Practitioners it sometimes feels as if you have rabbits caught in the headlights of a car - transfixed. For others the fear in their eyes is sometimes thinking you have asked them to jump out of a plane without a parachute.

Let me be clear, tax is law. It is about applying the law to certain facts. It is no different than reading Section 6 of the Unfair Dismissal Acts or Section 15 of the Organisation of Working Time Act. It is about the law. It is not about "mere sums".

Unlike other areas of law, there is "no equity in tax". Tax follows the law. As Employment Law practitioners we are used to legislation which like the Terms of Employment (Information) Act sets compensation as is "fair and reasonable" there is no such test in tax. Either something is taxable or it is not. There is no "fair" or "reasonable" test. There is no "equity" in tax.

An employee either receives an exemption or a relief or they do not. There are no "grey" areas. Tax is "black and white".

A scoundrel may obtain a tax exemption or allowance while a saint may not. To that extent and to that extent only, Practitioners need to amend their thought processes.

THE APPROACH TO TAX

To be fair, most Solicitors and employers and employee representatives are prepared to discuss tax issues. Unfortunately, the majority of Barristers seem to resile on the basis that tax has nothing to do with them.

If your approach in cases is fight everything, never settle, never go into mediation and that when any decision issues you send it to your client with note to say: "My engagement is finished. I am not accepting any further engagement about this case. You deal with it from here" then possibly you can get away with this approach of not considering tax.

Unless you understand the basics you can get a result where your client either pays too much tax, fails to get a relief, or exemption or is caught with a tax liability which would legitimately have been avoided. You cannot wash your hands of tax. Tax is an integral part of any settlement or decision. Get is wrong and you create a tax liability for somebody.

EMPLOYERS AND EMPLOYEES

Tax planning is as important for employers as it is for employees. Some think it is only relevant to employees. It is not. If an award or settlement is subject

to tax and employer has employer's PRSI to pay in addition to the amount payable to the employee. Therefore, the difference an employer has to pay on an award of €15,000 (or settlement) which is subject to tax is €1,612.50 as an additional cost.

MEDIATION - Why you should consider it? -or- Why €15,000 can be worth more than €20,000?

If acting for either employers or employees, you should consider mediation in the WRC. It costs nothing. It is not a sign of weakness to attend. You may get the case resolved. Many employer's actually just want to tell somebody they are "good people" and then they are prepared to settle. Some colleagues forget that. Equally there are some employees who just want to be able to get it out that their employer was a "bad employer" and then they equally are prepared to settle. Again, this is an issue that some colleagues overlook.

I would advise that you would consider settlements earlier. The earlier the settlement the less the costs to both sides. This helps to keep a settlement cost down for employers. For employee representatives an Unfair Dismissal award is taxable. There are exemptions but they are limited and this will be discussed later in the paper. Many believe that if an award is stated to be compensation then it is exempt from tax. In the case of Unfair Dismissal cases, or claims under the Payment of Wages or any issue relating to loss of earnings, for example, an equal pay claim, it most definitely is not exempt from tax.

If you settle for example an Unfair Dismissal claim, you can claim the tax free termination exemption being the €10,160. In addition, you can claim a sum of €765 for each completed year of service. This has advantages for both employers' and employees' representatives. The reality is that an Unfair Dismissal award is taxable. There are certain exemptions. However, the element that is taxable for the employee will be taxed at 40% tax and 8% USC will be deducted from what the employee receives. For employers there is the employer's PRSI of 10.5% on the entire amount.

For the purposes of discussing issues going forward in this paper, I thought it would useful to possibly set out an example. I am going to look at a case which results in an award where an employee received an award of €20,000 in an Unfair Dismissal case and then when the same case is looked at where it is settled for €17,000 and what the position is.

Employer		**Employee**	
Award	€20,000	Award	€20,000
PRSI	€2,100	Tax Exemption	€10,925
Cost	€22,100	Taxable	€9,075
		Tax at 48%	(€4,356)
		Balance	€4,719
		Add Exemption	€10,925
		Employee Receives	€15,644
		Fees	(€4,000)
		Employee Net	€11,644

Let us take a case if the case settles for €17,000 and again the employee only has one-year service.

Employer		**Employee**	
Settlement	€17,000	Settlement	€17,000
PRSI on €2,075	€218	Exemption	(€10,925)
Cost	€17,218	Taxable	€6,075
		Less Legal Fees	€4,000
		Balance Taxable	€2,075
		Tax at 48%	€996
		Balance	€1,075
		Add	€10,935
		Monies received by employee	€12,010

I am simply setting this out as a simple example of a situation where while the benefit to the employee is relatively small, the benefit to the employer is very high.

It is still however a benefit to the employee.

Both the employer and the employee are better off.

The issue of tax and Unfair Dismissal awards is one that comes as a surprise to most. I have had comments like:

"But it was awarded as compensation".

Yes, it was, but Section 123 TCA 97 applies and the exemption in Section 192A TCA 97 does not apply. The tax under Section 123 TCA 97 is subject to the exemptions in Section 201.

The basis of the tax is that it is for lost wages such as Payment of Wages claims, Unfair Dismissal claims, Equal Pay claims or non-payment of holiday pay as examples of awards which are taxable.

If it is for breach of a right such as not getting paid holiday pay in advance (a subtle difference), working too many hours, being dismissed for a ground under the Equality Acts or for compensation for breach of a right then it is not taxable. Unfair Dismissal awards is not a "right" as specified in the exemptions.

If you are acting for an employer and you get it wrong, the Revenue can go back up to 6 years and seek the tax, penalty and interest. In the previous example the tax is not just €4,356 but rather closer to €8,700. When you then take penalties and interest you can be talking about another €16,000.

When acting for an employee, you will have a lot of explaining if a cheque comes in for €11644 when the employee thought that the employee would receive a net sum of €20,000.

SETTLING CASES

In settling an Unfair Dismissal claim or Wages claim or a case that relates to any loss of income as an employer's representative you will want to include that great phrase in any settlement:

"*Without Admission of Liability"*

If acting for the employee, it makes no difference.

However, in a case involving "compensation" such as an equality dismissal or for not having got a document which complies with Section 3 of the Terms of Employment (Information) Act or for working excessive hours as just examples, you cannot use the phrase

"*Without Admission of Liability".*

I will discuss this later in this paper and while technically you can but if you do, you lose the benefit of a settlement being deemed to be tax free.

I have set out examples previously as to how the compensation is taxed in an Unfair Dismissal case. That would equally apply then in one of these cases which is exempt if you use these words as there would be no allowance and it would be, if it was an equality dismissal claim it would be treated as a termination payment. If however it was a claim that an individual was discriminated against, other than in relation to a termination situation, then a settlement of €17,000 will actually be fully taxable.

Net amount received €6,760

This is a significant reduction for an employee. There is a significant exposure for those representing employees. The same applies to those representing employers. The reason is the €17,000 will be subject to 10.5% employer PRSI. Those acting for employers also have the issue that if the tax is not deducted the Revenue can come back for 6 years against the employer.

CONCLUSION

This is the first part of this seminar note and I thought it was relevant to set out in in broad terms at the start and I can deal with it then in more detail in the rest of the paper.

THE RELEVANT TAX LEGISLATION

The starting point in relation to an understanding of the tax treatment of employment law awards and settlements is the relevant legislation.

Section 192 (A) TCA97 was inserted by Section 7 FA2004. This Section was inserted because of the fact that the Revenue in 2003 sought to tax all employment law awards and settlements. A subcommittee of the Taxation Committee of the Law Society (now the Taxation and Probate Committee) met with the Department of Finance. As a result of those negotiations the legislation was implemented and can be simply understood as follows.

If the award relates to a loss of wages such as an Unfair Dismissal claim or a Payment of Wages claim it is taxable

If the award of settlement relates to compensation for breach of a statutory entitlement, which is not wages, it is exempt.

The fact that an award may look like it is an award of wages does not make it taxable. I think it is useful at this stage to give an example.

If an Adjudicator gives an award of 10 weeks wages for breach of Section 11 Organisation of Working Time Act (OWTA) which is a breach of the provision relating to the employee getting an 11-hour break that is exempt from tax as it relates to compensation for the infringement of an employment right.

If the Adjudicator awards 10 weeks wages for an Unfair Dismissal claim that is a payment of a financial loss and is taxable.

UNDERSTANDING THE LEGISLATION

The provisions of Section 192 A TCA97 provides that, with effect from 4th February 2004, compensation awards paid following a formal hearing by a "relevant authority" or a settlement (in certain circumstances) in respect of the infringement of an employee's rights and entitlements under the law are exempt from Income Tax. The exemption does not apply, however, to payments which are in respect of earnings, changes in function or procedures of an employment or the termination of an employment. Saying this, there are exemptions in relation to.

While the commentaries on this piece of legislation seem clear their application in practice is often misunderstood. This misunderstanding is not limited to Solicitors and Barristers. Accountants, in particular staff of Liquidators and Receivers, and even some "Tax Advisors" fail to comprehend the practical effect of the legislation.

Those seeking rulings from the Revenue often ask the "question" the wrong way and therefore an "incorrect" answer is received from the Revenue.

The legislation itself is reasonably simple. It is its application in practice which some confuse.

THE LEGISLATION

Section 192 A TCA97 can be summarised as follows;

1. An award or settlement for the breach of an employment right of an employee or former employee is exempt from tax, provided;

A It is not a payment in respect of remuneration or arrears of remuneration and

B It is not a payment for a change in function or a termination payment.

There are exemptions but I will deal with these later.

However, a termination payment may itself be exempt by Section 201 TCA 97. This I will deal with later.

THE SCOPE OF THE LEGISLATION

The legislation refers to "a Relevant Act". This is an enactment which contains provisions for the protection of employees' rights and entitlements or for the obligation of employers towards their employees. In practice this means any piece of employment legislation. It will include legislation post 2004. Therefore, it would include the Protection of Employees (Temporary Agency Work Act) 2012. The exemption applies for payment under a Relevant Act to an employee or former employee by an employer or former employer after 4th February 2004 in accordance with;

A A Recommendation
B Decision; or
C Determination by a Relevant Authority

A "Relevant Authority" is defined as

A A Rights Commissioner,
B The Director of Equality Investigations,
B (a) An Adjudicator Officer of the Workplace Relations Commission,
B (b) The Workplace Relations Commission,
B (c) The District Court,
C The Employment Appeals Tribunal,
D The Labour Court,
E The Circuit Court, or
F The High Court.

(The Legislation was amended to insert (BA) (BB) and (BC) by the Finance Act 2015)

The exemptions will also apply to a settlement under a mediation process provided for in a Relevant Act and shall be treated as if made in accordance with a Recommendation, Decision or Determination under the Act of a Relevant Authority subject to certain conditions.

Originally, the only "mediation process" provided for under Legislation was Section 78 Employment Equality Acts. The Workplace Relations Customer Service "mediation" process is now provided for under a "Relevant Act". Therefore, such mediation agreements do have the benefit of Section 192 A TCA 97. Such "settlements" are therefore exempt, provided if a decision issued, it would be exempt. This is often overlooked by many.

STRUCTURING SETTLEMENT AGREEMENTS TO BE EXEMPT FROM TAX

The provisions of Section 192A TCA97 also apply to out of Court Settlements. Therefore, the agreement under the WRC could qualify. However, to qualify certain conditions must be met namely;

1. That it is a bona Fide claim made under the provisions of a relevant Act,
2. Which is evidenced in writing, and
3. Which had the claim not been settled by agreement, is likely to have been the subject of a Recommendation, Decision or Determination under that Act by a Relevant Authority that a payment be made. (underlining added).

The first two conditions are met by the WRC mediation. The one that does not is the condition that the agreement certifies that had not the agreement been made it would have been the subject of a Recommendation, Decision or Determination. This condition is set out in Section 192 A (4) (a) (i) (iii). This is the one condition which Solicitors for employers, and especially Barristers, for some reason have the greatest resistance to incorporate into any agreement. It is however a condition precedent to obtain the exemption. If, however, such a provision is incorporated into any such agreement / settlement. No such wording is required in the WRC. Mediation Agreement as any exemption will apply automatically.

The form of words which is sufficient for including in this settlement agreement is as follows.

"the employer and the employee agree that the sum of €xxx is a fair and reasonable settlement sum and that such a sum is likely to have been awarded by an Adjudicator / Labour Court in any claim".

The above provision requires to be inserted. This clause is the one clause that causes the greatest difficulty for employers. There is a preconceived view that any settlement agreement must have the words it is made "Without Prejudice" and "Without an Admission of Liability".

If such a clause as set out above is not included the settlement agreement does not gain the benefit of Section 192 A. If it is included then it does have the benefit of Section 192A. Where made "Without Prejudice" or "Without Admission of Liability" no tax exemption. Solicitors and Barristers should instead rely on Non-Disclosure/Confidentiality Agreements. You cannot get the exemption if made "Without Prejudice" or "Without Admission of Liability".

Where a settlement document is entered into there is an obligation on the employer to maintain same for a period of 6 years. Section 192 A (4) (a) (iii) provides that copies must be retained for the period of 6 years.

Sub Section (4) (b) provides that copies of these documents can be requested by the Revenue Commissioners.

I do appreciate that some employers and practitioners have a real difficulty with this condition.

It is not that the settlement would not have been one which would **likely** have been made by for example an Adjudicator but the fact of any admission. The word used is "likely" not "certainly" or any similar word.

There is nothing to stop parties including in a settlement agreement the following.

"It is agreed between the parties that the settlement herein relates solely to case reference xxx and may not be used by either party for the purposes of grounding or defending any other claim under any other Act or at Common Law or otherwise and may not be produced in any other Court, Tribunal or otherwise for the purposes of grounding, supporting, defending or otherwise dealing with any claim by either party against the other party under any other piece of legislation or at Common Law or otherwise whatsoever".

I would say in passing that there is nothing to stop a party settling a matter under for example the Organisation of Working Time Act and then including clause that it resolves all matters between the parties and setting out all the relevant Acts. This is a standard procedure by many Solicitors.

I would be of the view that it is better in those circumstances to provide as follows;

"it is agreed between the parties that the settlement under reference xxx shall be deemed to be in full and final settlement of all claims which the employee may have against the employer and that the employee undertakes not to bring any further claims and to withdraw any other claims already in existence under any of the following pieces of legislation. (And then insert the normal list)".

When a settlement will not be exempt from tax but a Decision, Determination or Recommendation would be.

Section 10 TCA 97 defines connected person

A connected person is "connected with the other person if they are a Husband, Wife or Civil Partner or is a relative or the Husband, Wife, Civil Partner of a relative of the individual or of the individual's Husband, Wife or Civil Partner".

This looks like a bit of a mouthful.

This is additionally so when a relative means a Brother, Sister, Ancestor or Lineal Descendant. In Appendix 1 I have set out Section 10 TCA 97 for those who want the full list. This is different than the exception in say the National Minimum Wages Act Section 5. It may be useful to give an example.

Let us assume that employee A in the previous example is a Sister in Law of the employer and employee B is a Brother in Law of the employer. Employment Acts will not exclude the employees claiming.

Where employee A has a decision from the WRC and employee B has a settlement only.

Even if the settlement with employee B includes the three conditions for the exemption to apply, as set out above, the exemption in the case of a settlement or mediation by virtue of Section 192 (A) (4) (i) is excluded from the exemption. This is because of the fact that employee B is a "connected person". Employee A can receive the Decision exempt from Tax as she will not be relying on the provisions of Section 192 A (4).

Therefore, if you are acting in the case of a relative of an employer it is important for representatives that they proceed the full way for a hearing and get a Determination, Decision or an Order. The provisions of Section 192 A (4) (i) specifically excludes "connected persons".

These is a saving provision. Mediation agreement by the WRC would however be exempt under Section 192 A (3). The restrictions only apply to an out of Court settlement not under a mediation process provided for under a Relevant Act. Therefore, use the WRC. It means you need to consider settlements early. If the case goes to the Labour Court the only way to get the exemption is to get a Decision.

THE TAX TREATMENT OF DECISIONS, DETERMINATIONS, AND RECOMMENDATIONS

The basic distinction between an award or settlement which is exempt and one which is not exempt is a distinction between salary / wages and compensation.

This is the concept which is often misunderstood. The misunderstanding is understandable as employment legislation before an Adjudicator and the Labour Court is denominated as regards compensation on the basis of weeks of wages.

The Maternity Protection Act in Section 32 refers to up to 20 weeks wages. The Unfair Dismissal Act ("UDA") is up to 104 weeks wages. The OWTA is the

same. The first and third Acts are gross wages. The UDA is net wages. Decisions may say in a Terms of Employment (Information) Act case that one week or two weeks wages being €x is awarded as compensation.

It is still compensation for infringement of a right rather than the reimbursement of salary or wages. The difficulty can be caused not by the legislation but rather by the way Decisions are written. Written one way taxable. Written a different way not taxable.

The Equality Tribunal did, if the award is compensation for the infringement of a right, would specify that it is exempt from tax. If it is for example an equal pay claim they would specify that it was subject to tax. They had the advantage of limited legislation unlike the other bodies to be fair to the others.

It is useful at this stage to give possible examples of how difficulties can arise with Decisions.

Let us for example take the following case.

Example

Employee C brings a claim to an Adjudicator under the Organisation of Working Time Act. The claims are under Sections 15 for working excessive hours and in relation to not being paid Public Holidays and Annual Leave. Let us assume that the employee earns €400 a week for a 5-day week. There is one Public Holiday that is not paid with a value of €80 as unpaid wages for that date and one week's Annual Leave not paid with an economic value of €400. The Adjudicator declares;

"I find that the complaint is well founded in relation to working excessive hours contrary to Section 15, Public Holidays and Annual Leave. I award the complainant €10,000 as compensation".

In such cases because the award under three Section were all dealt with as a global figure the entire determination is subject to tax. This means that the employer pays the €10,000 to the employee less tax submitted to the Revenue and PRSI and USC to Social Welfare. The employer is also responsible for €1,075 employers PRSI. The employer must submit and amended P45. The employee then reclaims the tax. The employer has paid an additional €1,075. Let us assume that the Adjudicator deals with the Decision as follows.

The Adjudicators Decision states;

"I declare that the complaints under three Section of the Act in relation to working in excess of 48 hours, public holidays and annual leave entitlements is well founded and is upheld.

I award the sum of €8000 for breach of Section 15.

I award the employee €80 for non-payment of public holidays, €400 for non-payment of annual leave and a sum of €1520 for the infringement of the employees' rights under the Act".

In the alternative as has been set out in the past, it could be provided as follows;

"Redress

Having regard to all the circumstances of this case I award the employee compensation in the sum of €10,000 for the contraventions of the Act which I have found to have occurred. Of this amount €480 is in respect of annual leave and public holiday entitlements. The remaining €9520 is in the nature of a general compensatory amount".

In the first circumstance as set out the entire award as previously stated is subject to tax. In the two latter examples the sum of €480 only is subject to tax with the balance being exempt.

The reason for same is that the Decision clearly sets out that the compensation is compensation for an infringement of a right.

It would be beneficial if the decision added on the words

"In respect of the award of €9,520 same is exempt from tax by virtue of the provisions of Section 192 A Taxes Consolidation Act 1997 as it is compensation for infringement of an entitlement under the Act".

I have seen WRC Decisions with this wording which would not come under Section 192A. You must check the exemption applies.

You may say that it is the same amount being awarded. You are correct in saying that but it is the words that are used in the Decision determine the tax treatment.

Legislation is clear in that any award is subject to tax if it is a payment, however described in respect of remuneration including arrears of remuneration.

In the first example set out above the award of €10,000 includes arrears of wages. It includes remuneration and is therefore subject to tax.

If the employee has ceased employment then S. 201 TCA 97 applies and the employee can claim a refund of tax on the €10,000 or €480.

How the tax treatment of a particular matter may ultimately be dealt with depends on the wording of the Decision. If I can give you one example where the Decision of an Adjudicator would be subject to tax and the Decision of the

Labour Court would be exempt from tax and while I am not giving the parties names I am setting out the wording of the Decision.

Before the LRC where there was a Rights Commissioner the Rights Commissioner held;

"There were X public holidays during this reference period. The shortfall is 39 hours multiplied Y per hour equals Z. There were X annual leave entitlements during this reference period. The shortfall is 78 hours multiplied by Y per hour equals Z.

I order the employer to pay to the claimant compensation in the sum of Z + Z for breaches of Section 21 (1) and 19 (1) of the Act".

The matter was appealed to the Labour Court

The Determination of the Labour Court was as follows;

"The complaint is well founded. The Court awards the complainant the sum of "A" compensation for the infringement of his entitlements under the Act".

The total sum was minimal. However, that is not relevant.

The issue is what is the tax treatment?

Clearly the decision of the WRC was taxable as it is arrears of remuneration.

The Decision of the Labour Court was not taxable as the Labour Court provided compensation for the infringement of the entitlement. However, a Revenue Official might argue as the case involved "arrears" the decision could be deemed to include arrears and is taxable. The value would be preclude any real challenge to a Revenue ruling.

In another case the tax treatment of an award by the Labour Court could not have been clearer or more precise.

"Having regard to all the circumstances of this case the Court awards the claimant compensation in the amount of €5000 for the contraventions of the Act which it has found to have occurred. Of this amount €2000 is in respect of arrears of holiday and cessor pay. The remaining €3000 is in the nature of a general compensatory amount".

The case reference is DWT1223.

The €3000 is exempt under S. 192A. The €2000 is subject to tax but as it is "cessor" pay arising on cessation of employment relief under Section 201 is available. Therefore, no tax is payable.

That Decision could not have been clearer for the tax treatment. Because the decision stated "cessor pay" S. 201 is available. Even if it had not it would on the facts of the decision been available but by putting it in the redress section of the decision the tax treatment is clearly and precisely stated.

It is much more beneficial if any amount of remuneration including arrears, holiday pay or public holiday pay or any matter which was in the form of compensation for an economic loss that is quantifiable in euros and cent is separately provided for with any general compensation being separately specified.

At a minimum it would be far more beneficial if Decisions did specify at least claims on a section by section basis. Therefore, the tax treatment would be absolutely clear as regards exempt awards. Therefore, if say arrears of wages and compensation are lumped together only part of an award would be taxable and an exempt award for another section would be exempt.

Payments not covered by the exemption.

I would refer you to Schedule 7.1.27 of the Revenue Tax Manual and the Revenue notice for guidance notes.

Payments not covered can be summarised as follows.

1. Actual remuneration of arrears of remuneration.

This would include a claim for wages under the Payment of Wages Act or an award under the Unfair Dismissal Acts. It would include claims under the Industrial Relations Act and Equal Pay claims under the Employment Equality Acts. It would include a claim for Annual Leave pay or Public Holiday pay under the Organisation of Working Time Act, i.e. actual loss.

It does not include as remuneration or arrears of remuneration an award under the Terms of Employment (Information) Act even if it specifies that it is four weeks wages or a Decision under the Maternity Protection Act awarding an employee 20 weeks wages or an award for infringement of say the OWTA as regards Annual Leave entitlements as opposed to holiday pay. The fact that the compensation is denominated in weeks of wages does not make it taxable.

2. Compensation for a reduction of future remuneration arising from a reorganisation, a change in working procedures will be subject to tax subject to the relief under Section 480 TCA97.

Section 480 TCA 1997 refers to lump sum payments made to an employee as compensation for a change in working conditions. This applies to any payment chargeable to tax under Schedule E (e.g. PAYE) made to an employee to compensate the employee for;

(a) A reduction or possible reduction of future remuneration arising from a reorganisation of the employer's business e.g. a loss of promotional prospects, with attendant loss of possible higher earnings,

(b) A change in working procedures or working method. Examples might be the introduction of new technology or agreed changes in working methods

(c) A change in duties e.g. a machinist agreeing to load raw material or pack the finished product.

(d) A change in the rate or remuneration e.g. the introduction of a higher basic salary and substitution for a basic salary or commission or the cessation of overtime at a higher rate of pay

(e) A transfer of the employer's place of employment from one location to another.

Payments excluded from the relief are lump sum payments made to directors and employees with proprietary interests or part time directors and part time employees. The relief is claimed after the tax year ends. The relief is such as to reduce the total income for the year or assessment to

(a) The income tax which would have been payable by the employee if he / she had not received the lump sum, plus

(b) Tax on the whole of the lump sum computed at a special rate (an effective rate on the payment of 1/3 only of the lump sum paid).

You require to make a written claim and evidence that any of the items have happened must be furnished for example a statement from the employee.

The timing of payments can be significant.

As such structures are put in place to negotiate with employees very often in effect you are dealing with what they are going to receive net into their hand. There is a significant net difference by paying it on 31st December as opposed to 1st January. There is a 1/3 Exemption (subject to certain restrictions) for paying in a year when the charge occurs.

SCSB - Exemption

In dealing with high net individuals who are members of a company pension scheme, there is a provision for them to take out a sum of up to €200,000 exempt from tax. There is a complicated formula to be applied. I do not intend to go into it here today. However, what I would say is that you need to be very

careful in relation to this. It is a lifetime exemption of €200,000. It does mean at times that an employee may not look to take that exemption.

Maybe an example would help. You have an employee who has a settlement of €200,000. The length of service he has in the company is such that he would be entitled to take out the full €200,000 exempt from tax. Let us assume that he has 30 years service in the company which would mean that he can take under the basic exemption €33,600. To take the basic exemption he cannot take the enhanced exemption of €200,000. It cannot get both. It may therefore appear that of course you would go for the €200,000 but possibly you would not. If the employee was age, say, 63 years of age and would be due to retire and could take monies out of his pension scheme in 2 years time, then in those circumstances taking the €200,000 now would mean that the €200,000 could not be taken in 2 years time and he would lose the benefit of the €33,600. If he takes the €33,600 now, in respect of the €200,000 settlement he would pay tax on a large portion of same but can claim the €200,000 in 2 years time. The issue of SCSB is way outside the issues I believe that any Solicitor is capable of reasonably advising on. If you see a settlement agreement which uses the phrase SCSB or the phrase Standard Capital Superannuation Benefit and that a settlement could be taxed under same, it would be my strong advice that you advise the employee to get clear and definitive tax advice and pension advice before signing up to any agreement with that clause in it.

If a person is not a member of an occupational pension scheme. Where individual is not a member of a occupational pension scheme and the individual has not claimed any relief under Section 201 in the previous 10 years and is not a member of an occupations pension scheme then the employee is entitled to seek an additional payment, being an increased exemption of €10,000 on top of the basic standard exemption of 10 months together with €765 for each completed year of service.

Wages and Arrears of Wages

Claims under the Payment of Wages Act for non-payment of wages are clearly arrears of remuneration.

A claim under Section 18 of the Organisation of Working Time Act where the employee can claim that they were available to work but were not paid where the award would be 25% of the amount which they would otherwise have received is clearly wages and is taxable. Compensation in addition to this for breach of the Act is not wages and is not taxable.

Awards under the Unfair Dismissal Legislation are wages. The reason for this is the terminology of the legislation itself. The maximum award which can be awarded under the Unfair Dismissals Acts is 104 weeks loss. The legislation refers to loss. Therefore, the tax treatment follows the legislation.

There are a number of confusing aspects on this. Under Payment of Wages Legislation and the Unfair Dismissal legislation. The awards are "net" wages. In respect of a claim under Section 18 of the Organisation of Working Time Act it would be the gross amount. In addition, under Section 18 of the Organisation of Working Time Act an Adjudicator or the Labour Court could award up to two years wages as compensation and the tax treatment will depend on the wording used by the Adjudicator or Labour Court. In respect of the Payment of Wages or Unfair Dismissal Act claim it will always be net wages. This does not mean however that all wages are taxable. This may appear a contradiction.

Example

Employee D has 1 year service. He is dismissed. He was not paid his last 3 weeks wages. He was not given Minimum Notice. His gross wages was €500 per week. His net was €400.

The Adjudicator awards €1200 under the Payment of Wages Act for Unpaid Wages and €500 for Minimum Notice (Minimum Notice in Gross). In addition, a sum of €5000 is awarded under the Unfair Dismissal Acts.

On appeal the Decision is upheld by the Labour Court. At first sight all awards are "wages" and are taxable. This seems logical. However, this is not the position. Section 201 TCA 97 will exempt the Unfair Dismissal Act award as it is less than €10,160. The Minimum Notice Payment will also be exempt. The reason for this is that it is a termination payment. The wages of €1200 is taxable and subject to employers PRSI. It is not a termination payment so S. 201 does not apply.

A claim for wages or a claim for breach of contract for non-payment of wages in the Circuit Court or High Court will always be taxable. A payment which is a termination payment will get the benefit of section 201 TCA 97 subject to the threshold. The threshold amount is €10,160. There is also an additional sum of €765 for each complete year of service in the employment in respect of which the payment is made. It is complete years. Therefore, if an employee has 1 year and 11 months service they will get the additional €765. If they have 2 years and 1 month they get an additional €1530.

While it is not strictly speaking part of the seminar the issue which has never really been determined by anybody is what are "net wages".

Example

Let us assume there are two employees who are higher level employees. They are employed for one year. The base exemption applies. They are paid €200k per annum gross. The net for employee A is €150k per annum and for employee B €130k. Employee A maximises every relief that she can under the Taxes Acts while employee B does not.

Nobody has ever described how "net" is arrived at. Whether it is actual or notional.

Saying this, let us assume the Adjudicator awards each 1 year's net wages.

Employee A receives €150k. Employee B receives €130K. This is their "net" loss. However, both awards will be subject to tax. Employee A is taxed on €150,000 less €10,925. Employee B is taxed 130K less €10,925.

As the "employee" will have no tax credits for their tax will be deducted at 40% plus 8% USC (as over €70,044) would be an effective rate of 48% on the Net award. The employer will pay 10.75 for employee A and for employee B but on different amounts as employees PRSI.

The two employees could seek a refund of the tax or they may be able to avail of the other exemptions.

It does however seem unfair to one employee who had put in place for example VHI, put in place permanent health insurance, may have invested in a home and being able to obtain mortgage relief and may have purchased a bike to cycle to and from work where tax relief would have been available that that employee would be deemed to have a higher net than an employee who just took the money at the end of the month and made no provision for their future. I am simply raising it that there would appear to be an argument under the legislation that net wages would be a notional rather than an actual net being calculated on the basis of the tax treatment of the individual as if they were an individual simply claiming the basic allowances. In the example above there would a significant difference between two employees if one is married and has a working spouse and the other Single that is an issue which is going to have to be determined at some stage.

Conclusion of the Tax Treatment

There is an old adage in taxation that;

"Taxation follows the law".

By this I mean that the tax code will apply to a payment to an individual depending on how it is categorised under the law.

Again, I think it might be useful to give an example.

Let us assume there are two employers.

Both employers sell their business. The business transfers under the Transfer of Undertaking Regulations

Employer A writes to an employee as follows.

"Now that your employment has transferred under the Transfer of Undertaking Regulations to the new employer I would like to thank you for all your work over the years and now that you are finished working for me I would like to make a gift to you of €3000 in appreciation of your work and to thank you for your assistance in the transfer of the business over to your new employer".

The second employer sends the following letter;

"I would like to make you a gift of €3000"

The first payment is subject to tax as it relates to a change in conditions.

The second payment is a gift and it's completely exempt under the Capital Acquisitions Act. this is not an Act you could deal with but it shows there is no equity in tax.

Both employers may have intended to make a gift simplicitor. The nuances of words will determine the tax treatment.

I give the above as a simple example of how the categorisation of matters will determine the tax treatment. If there is a settlement that is put in place under the Payment of Wages Act, The Organisation of Working Time Act, the Maternity Protection Act, the Employment Equality Acts and the National Minimum Wage Act and a global figure is inserted in the settlement agreement the entire will be subject to tax.

If it is split up between the various Acts only the Payment of Wages and the National Minimum Wage Act settlement elements only will be subject to Tax.

For employees it is important so as to maximise the amount of money that they receive now.

For employers it is equally important so as to minimise an unnecessary cost of 10.75% PRSI charge. Where there is no liability to pay it but incorrect structuring of a settlement could cause it to be payable.

When considering a settlement, you must always consider Section 201 in respect of any payment which is subject to tax.

If the exemption applies then the employee receives the award without tax and PRSI having been charged. The employer avoids unnecessary cost of 10.75% PRSI charge.

If you have a claim under all of the above Acts this is not a reason for lumping everything under one of the exemption sections. For example, the Employment Equality Legislation or the Organisation of Working Time Act.

A settlement must be "bona fide".

It is certainly useful for a representative of an employer particularly to set out the rationale as to why a particular settlement might have been put in place.

For example. You could have a situation of a claim under the Organisation of Working Time Act. If you are acting for a large employer it may well be that a defence which would be acceptable for the owner of a small corner shop might not suffice for a claim by a significant employer and the level of compensation might well be different. It is therefore useful to specify why a particular award was recommended to an employer. When considering settlement, it is a settlement or an employment law award it is imperative to, look at section 192 A TCA 97 firstly to see if it is exempt. It is then necessary to look at the other exemptions such as section 201 as a fall-back position. Section 192 A TCA97 is not a catch all solution to pay tax free by lumping everything under an "Exempt Act".

CONCLUSION

Many years ago, myself and a man called Ken O'Brien wrote a book entitled "Payroll and Taxation for Employers". Our working title was "The complete cure for insomnia".

I hope the talk today has not caused you to go to sleep. I do hope that it simply has alerted you to the problems which need to be addressed.