

Christmas cheer: tax on bonuses, exit payments and personal grievance settlements

“With Christmas almost upon us, it is timely to think about the tax consequences of making unusual or one-off payments to employees - such as Christmas bonuses ...”



Fiona Heiford - Senior Solicitor

With Christmas almost upon us, it is timely to think about the tax consequences of making unusual or one-off payments to employees - such as Christmas bonuses and gifts. We also comment on some issues relating to exit and personal grievance payments, although hopefully you won't need to consider these issues in the festive season.

Consideration needs to be given to whether these sorts of payments are taxable and, if so, to whether the agreed amount is the gross payment - meaning that tax is still to be deducted from it - or is it a net payment - meaning that the tax has already been deducted. If it is a gross payment, who is responsible for paying the tax to IRD?

Is the payment taxable?

In most cases, payments to employees are very straightforward. They are usually salary or wages or an extra emolument and the employer is responsible for deducting PAYE and ACC levies and paying IRD and ACC. A Christmas cash

bonus (taxed at the extra emolument rate) falls squarely into this category.

Non-monetary Christmas gifts to employees are also likely to be taxed but as a fringe benefit. However, if the value of the gifts (plus other similar benefits) is below a very low statutory threshold of \$300 per employee per annum, up to a maximum of \$1,800 per employer, they will not be subject to fringe benefit tax.

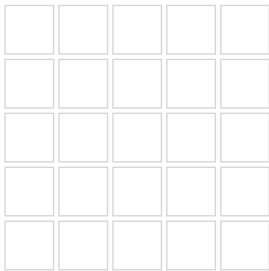
It is only if Christmas gifts are gifts of “personal appreciation”, and not made by virtue of the employment relationship, that the taxman doesn't get his slice of the Christmas spirit - and this is a difficult test to meet especially where Christmas gifts are made to all employees - bah humbug!

Exit payments are also employees' gross income and taxed accordingly. Like Christmas bonuses, they are extra emoluments and the employer must deduct tax (and ACC levies) when making the payment.

Personal grievance payments

A more difficult question arises where a payment is being made in settling a personal grievance. Personal grievance payments usually, but not always, coincide with termination of employment.

If these payments relate to the person's employment, they will be taxable, whether they are ordered by a court or negotiated through mediation or directly by the parties. The payments will be gross income of the employee and subject to PAYE (and ACC levies) and the employer should deduct these amounts before making the payment.



Taxation

There is an exception for payments for humiliation, loss of dignity or injury to feelings (covered by section 123 of the Employment Relations Act 2000). These payments are not taxed because they don't relate to the employment but are damages for treatment suffered. These payments must of course be genuine and reasonable.

Ultimately, if a payment is taxable and the tax is not deducted at source (i.e. by the employer) and paid to IRD, the employee is responsible for the tax. The question then becomes: who is responsible for the penalties and interest? In most circumstances the penalties and interest will be the employer's liability.

The need for clear communication

When you announce to staff that there will be Christmas bonuses of \$2,000, does this mean \$2,000 in the hand or \$2,000 before tax? There is no clear answer and other surrounding facts and circumstances would need to be taken into account. Undoubtedly the best solution is clear and careful communication, spelling out whether

the amount is net of tax or not. Similar issues can arise with personal grievance payments and exit payments, both in terms of whether the amount is net of tax or not and in terms of any apportionment between amounts subject to tax and non-taxable personal grievance compensation payments.

The answer is to consider carefully the tax consequences and communicate your intentions clearly to avoid souring the Christmas cheer.

Merry Christmas!

Advice and information

Our Tax Team can offer advice and information on all areas of tax and GST, including the yuletide implications of special payments. Contact us on the numbers listed below.



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