Planning for redundancies – tax issues

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Termination payments

Old Rules

Contractual or customary PILONs subject to tax and NI and non-contractual PILONs capable of being paid free of tax (up to £30,000) and free of NI (with no limit)

New Rules (April 2018)

Distinction between contractual and non-contractual PILONs now removed and all payments employee expected to earn during notice period subject to tax and NI

Do the maths…

Post-employment notice pay ("PENP") is calculated using the formula below:

$((BP \times D) \div P) - T$

'BP' is the employee's basic pay in respect of the last pay period of the employment ending before the date that the employee serves their notice or, if notice is not served, the last date of employment ("the trigger date").
"Basic Pay" is the total employment income the employee receives, or has the right to receive (even if they give up that right – for example, a salary sacrifice into a pension scheme) in their last pay period before the 'trigger date' but this generally excludes non-standard payments such as, for example, any amount received by way of overtime, bonus or commission due.

'D' is the number of calendar days in the post-employment notice period. This is essentially the notice period that has not been worked so is defined as the period in days between the employment ceasing and the earliest lawful termination date.

'P' is the number of calendar days in the employee's last pay period so this will be 7 days or 30 days depending on whether the employee is paid weekly or monthly. Special rules can apply to "simplify" the calculation where the employee is paid monthly and the notice period is expressed in months.

'T' is intended to capture any amounts of the RTA which have already been taxed.

If the amount given by the formula is negative then take the amount of PENP to be nil and if the amount given by the PENP formula exceeds the total amount of the termination payment, the PENP is capped at the total amount of the RTA.

Termination payments

Old Rules

Non-contractual payments tax free up to £30,000 and free of employee's and employer's NI with no limit

New Rules (April 2020)

£30,000 exemption remains for non-contractual amounts (other than PILONs) but payments in excess of this limit subject to employer's NI (Class 1A) but not employee's NI

This change has been delayed 3 times by Brexit discussions pushing the NI legislation to the back of the queue

Termination payments

Current Rules

Foreign Service rules can exempt entire termination payment with no limit (e.g. employment less than 10 years with 75% foreign service qualifies for exemption in full)

New Rules (April 2018)

Foreign Service rules abolished

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Termination payments

<u>Current Rules</u>
Exemption for payments towards "injury" can apply to "injured feelings"

<u>New Rules (April 2018)</u>
Exemption for "injury" excludes payments for "injured feelings"

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Termination payments

- Make sure you understand the rules in force when you are dealing with terminations as they have changed a lot in the last couple of years
- Don’t assume that the Employment Lawyer will be able to advise on the PENP calculation – it is still not well understood

Other tax matters to consider

- If someone ceases to be employed part way through a tax year and doesn’t work again that year, they will be due a tax refund
- Will your people set up on their own as a freelancer? If you support this, what help can you give them?
- Will you engage your former staff on a freelance basis after you have made them redundant?
- Have you provided equipment to your employees being made redundant that you will not be collecting?

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