momentum

	Preferred compensation	Alternative employee benefit structure
Purpose	To retain and incentivise selected employees over a medium to long term	
Investment choices	Endowment policy (Flexible Endowment Option), or Collective investment schemes (Flexible Investment Option)	
Investment structure	**Flexible Endowment Option** The employee is the policyholder and life insured. The employer is the premium payer. The employee registers a collateral cession in favour of the employer against the policy. **Flexible Investment Option** The employee is the investor. The employer is the premium payer. The employee will register a collateral cession in favour of the employer against the investment.	**Flexible Endowment Option** The employer is the policyholder. The employee is the life insured. The employer is the premium payer. **Flexible Investment Option** The employer is the investor. The employer is the premium payer.
Service agreement	A service agreement is entered into whereby the employer gives the employee a salary increase to fund the endowment's contribution as well as the additional tax burden that will be incurred due to the increase. This agreement will prescribe the timeframe associated with the benefit scheme. The agreement creates a debt in favour of the employer equal to the lesser of the salary increases or the fund value of the endowment policy or the market value of the investment - the endowment policy/investment is ceded to the employer as security for this debt. If the employee leaves the service of the employer before the end of the agreed time period, the employer will be entitled to claim payment against the policy/investment in terms of the security cession.	A service agreement can be entered into whereby the employer undertakes to pay the employee a bonus at a predetermined future date. The value of the future benefit is generally quantified in terms of the monthly contribution made by the employer and limited to the actual maturity value of the policy/the market value of the investment at that time. If the employee leaves the service of the employer prior to the agreed date, the employee forfeits all rights to the benefit.

	Preferred compensation	Alternative employee benefit structure
Income tax implications iro the premium	**Flexible Endowment Option and the Flexible Investment Option** The employer will increase the salary of the employee and the employer will qualify for a tax deduction under section 11(a). The increase will be part of the employee's gross income and fully taxable. Therefore the increase should be equal to the contribution plus tax payable on that contribution.	**Flexible Endowment Option** The employer will pay the policy premium. The premium will be included in the gross income of the employee as a fringe benefit in terms of the Seventh Schedule. The employer will enjoy a tax deduction in respect of the premiums paid in terms of section 11(w)(i). **Flexible Investment Option** The employer will not qualify for a tax deduction and the investment is made with after tax funds.
Income tax implications in the policy during the investment term	**Flexible Endowment Option** The insurer is liable to pay tax on the income and capital gains realised in the endowment policy according to the five fund approach. As an individual is the policyholder, the funds will be allocated to the individual policyholder fund. In this fund income is taxed at 30% and capital gains are taxed at an effective rate of 12%. No exemptions or exclusions apply within the policyholder funds. **Flexible Investment Option** All interest and dividends earned on the investment will accrue to the investor, the employee and will be part of gross income. The individual's interest and dividend annual exemptions will apply. Where units are sold and a capital gain is realised, the individual will be liable for the capital gains tax which has a maximum effective rate of 18%. The individual will enjoy the annual exclusion of R40 000.	**Flexible Endowment Option** The insurer is liable to pay tax on the income and capital gains realised in the endowment policy according to the five fund approach. Where a company or close corporation is the policyholder, the funds will be allocated to the company policyholder fund. In this fund income is taxed at 28% and capital gains are taxed at an effective rate of 22.4%. No exemptions or exclusions apply within the policyholder funds. **Flexible Investment Option** All interest and dividends earned on the investment will accrue to the investor, the employer and will be part of gross income. No interest exemption applies to companies or CCs. Where units are sold and a capital gain is realised, the employer will be liable for the capital gains tax which is an effective rate of 22.4%. No annual exclusion applies in the case of a company or CC.

	Preferred compensation	Alternative employee benefit structure
Income tax implications on the maturity value	**Flexible Endowment Option** When the policy matures, the employer will cancel the collateral cession, as provided for in the agreement, and the maturity value will be payable to the employee tax-free as it is seen as a capital receipt. As the policy is paying out to its original beneficial owner (or that person's nominee or beneficiary in the case of death) no capital gains tax will be payable. **Flexible Investment Option** At the agreed date, the employer will cancel the collateral cession on the investment and the employee will be entitled to withdraw the market value, which will result in the sale of units. Where a capital gain is realised on the sale of units, the employee will be liable for capital gains tax on the taxable capital gain at a maximum rate of up to 18%. The employee will enjoy the annual exclusion of R40,000.	**Flexible Endowment Option** When the policy matures the proceeds will be payable to the employer. As the amount will be included in the gross income of the employee, it is not included in the gross income of the employer. The amount paid to the employee will be part of the employee's gross income, however, it will be exempt in terms of section 10(1)(gG)(ii) if all the contributions that was paid into the policy was included in the employee's gross income as a fringe benefit. **Flexible Investment Option** At the agreed date the employer will have to realise the investment to fund the amount due to the employee. This disposal of units can result in a capital gain that will be subject to capital gains tax in the hands of the employer at an effective rate of 22.4%. The employer will then make a payment to the employee to settle the obligation as contained in the service agreement. This payment will qualify as a tax deduction for the employer under section 11(a) – as an expense incurred in the production of income. The employee will receive the incentive from the employer which will be treated as gross income and it will be fully taxable in the hands of the employee.

	Preferred compensation	Alternative employee benefit structure
What happens if the employee leaves the service of the employer prior to the agreed period?	**Flexible Endowment Option and Flexible Investment Option** The agreement will dictate what happens. It will generally state that a debt will arise, where the employee will owe the employer an amount equal to the lesser of the total salary increases paid to the employee over the time period or the surrender value payable by the policy/market value of the investment at that time. The employer will be entitled to invoke the rights associated with the security cession.	**Flexible Endowment Option and Flexible Investment Option** The agreement will dictate what happens. It will generally state that the employee loses all rights to the benefit and the employer will merely retain the policy/investment until maturity. In the case of the Flexible Endowment Option, it is in the interest of the employer to maintain the premiums on the policy as the cessation of premiums can result in a causal event charge being levied against the policy's fund value. Note – some endowment policies do not have any causal event charges due to the costing structure applicable.
Income tax implications where the employer exercises the rights in terms of the cession	**Flexible Endowment Option** As the policy proceeds will be seen as a repayment of a loan, it will not result in any income tax or capital gains tax consequences to the employer. If however, the employer decides to take full ownership of the policy by way of an outright cession, the maturity value payable to the employer will be subject to capital gains tax as the employer is not the original beneficial owner and therefore the abovementioned capital gains tax exclusion will not apply. **Flexible Investment Option** To exercise the rights in terms of the collateral cession, units will be sold to fund the repayment of the loan to the cessionary (employer). This will result in a potential capital gain in the hands of the employee.	Not applicable as the employer is the investor/policyholder.

	Preferred compensation	Alternative employee benefit structure
What happens if the employee dies?	The agreement will determine what happens. Generally the employer will cancel the collateral cession on the investment, leaving unrestricted ownership in the estate of the deceased employee. **Flexible Endowment Option** As the life insured is deceased the policy will pay out either to the nominated beneficiary (which is reinstated once the collateral cession is cancelled) or to the estate of the employee. **Estate Duty** As the policy is on the life of the deceased employee, the proceeds will be a deemed asset for estate duty purposes and therefore potentially subject to estate duty. **Flexible Investment Option** The executor will deal with the investment in terms of the will of the deceased employee. **Estate Duty** As the investment is property in the estate of the deceased employee, it will be part of the dutiable estate and potentially subject to estate duty.	The agreement will determine what happens and generally it will provide for some form of benefit to be payable to the employee's estate or beneficiaries. **Flexible Endowment Option** As the life insured is deceased, the policy will pay out to the employer. Where the proceeds are paid to the employee's beneficiary or estate, the income tax implications as discussed under the maturity section will apply. **Estate Duty** As the policy is on the life of the deceased employee, the proceeds will be a deemed asset for estate duty purposes and therefore potentially subject to estate duty. **Flexible Investment Option** The investment is an asset of the employer and if payment is due to the employee's estate or beneficiary, the employer will have to realise units to fund the payment. This can result in a capital gain in the hands of the employer. Any payment made to the employee in terms of a service agreement will be tax deductible in the hands of the employer under section 11(a). In the hands of the employee, it will constitute gross income and therefore be subject to income tax in the deceased's estate. **Estate Duty** The net amount paid to the estate of the deceased employee will be property in the deceased estate and therefore potentially subject to estate duty.

What happens if the employer is insolvent?	The agreement will determine what happens in this instance. In general the agreement will determine that the employer cancels the security cession in the event of its liquidation and therefore reinstating the employee as the policyholder/investor without any restrictions. The employee can then decide to continue with the policy or to surrender the policy in which case causal event charges may apply.	The policy is part of the assets of the employer and will fall into the liquidated entity's divisible assets. The agreement will determine what rights the employee has to the policy or investment value upon liquidation of the employer. Where the agreement provides for a claim in favour of the employee, that employee will be a creditor of the liquidated business and will enjoy similar rights as any other creditor.