IT 245 - Defence Force Retirement And Death Benefits Act : bounties and gratuities

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TAXATION RULING NO. IT 245

DEFENCE FORCE RETIREMENT AND DEATH BENEFITS ACT : BOUNTIES AND GRATUITIES

F.O.I. EMBARGO: May be released

REF

*** NOTE: THIS RULING HAS BEEN MODIFIED BY IT 2243

H.O. REF: J49/164/32 F251 DATE OF EFFECT:

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F.O.I. INDEX DETAIL

REFERENCE NO:	SUBJECT REFS:	LEGISLAT. REFS:
I 1101041	DFRDB FUND	25
	GRATUITIES	26(d)
	LUMP SUM PAYMENTS	
	TERMINATION OF EMPLOYMENT	
	RE-ENGAGEMENT OF SERVICE	

PREAMBLE Consequent upon the proposed replacement of section 42A of the Defence Force Retirement Benefits Act with Regulation 19 of the Defence Force (Bounties and Gratuities) Regulations as the authority for payment of "advances" against gratuities, it has been necessary to review previous rulings concerning the liability to tax of ex-members of the Defence Forces Retirement Benefits Fund on amounts received on retirement.

2. Broadly, a member who, on completion of a term of engagement, re-enlists for a further term is, by virtue of section 42A(1) of the D.F.R.B. Act, entitled to payment of a specified amount unless he elects not to receive that payment. Where the member does not make the election and receives the payment before discharge, the amount so received is taxable in full in the year of receipt. Such a payment is clearly a benefit to which an eligible member becomes entitled under the D.F.R.B. Act and, as no debt is created at the time of payment, it is not considered to be in the nature of a loan but rather a receipt in the nature of a gratuity, or part of a gratuity, assessable in full in the year of receipt.

RULING 3. It is considered that payments made under Regulation 19(1) and (2) will be essentially the same in character as those paid under section 42A(1) with the result that they will be taxable in full in the year of receipt.

4. The provisions of Regulation 19(6) and the amendment of section 42 of the Defence Force Retirement Benefits Act 1948-1971 effected by section 22 of Act No.82 of 1973 will, however, operate to alter the deductibility for income tax purposes of any repayments made by a member in consequence of being entitled to retirement pay or a pension. Previously, a

repayment by this class of member to the DFRB Fund of amounts received in terms of section 42A restored full pension rights to the member. In these circumstances, it was accepted that the repayment was a contribution to a superannuation fund for the personal benefit of the member and therefore qualified for deduction in the year the repayment was made in terms of section 82H of the Income Tax Assessment Act.

5. Under present circumstances, however, it is clear that repayment of an amount, whether received under section 42A or Regulation 19(1) or (2), will not affect the member's retirement pay entitlement under the Defence Force Retirement and Death Benefits Act 1973. The repayments cannot, therefore, be accepted as being for the personal benefit of the taxpayer in terms of section 82H of the Assessment Act. Moreover, the repayments will not be made to a superannuation fund and, in cases where Regulation 19(6) applies, will not be contributions under the Defence Force Retirement and Death Benefits Act which will qualify for deduction under proposed amendments to section 82H of the Assessment Act.

6. In the circumstances, repayments made under Regulation 19(6) or in terms of the present section 42A will not qualify for deduction under the income tax law as it now stands or in the form it will take when amended to cater for the change in the retirement benefit scheme whereby members' contributions are payable to Consolidated Revenue in lieu of a superannuation fund.

7. Payments made under Regulation 19(1) and (2) may be applied against the benefit due to a member on completion of his service if he is not entitled to a pension (Regulation 19(6)). Amounts deducted from a gratuity on retirement in terms of Regulation 19(6) will not qualify for deduction for income tax purposes.

8. Where, on retirement, a member is only entitled to a refund of his contributions to the Fund no part of the amount so received will fall to be included in his assessable income. However, the question whether payments consisting of a refund of contributions, together with an additional amount by way of gratuity (where the ex-member is not entitled to a pension) constitute a retiring allowance subject to tax, falls to be determined from the statutory provisions relating to the Fund. In the generality of cases, where an amount is paid as one indivisible sum it is subject to tax to the extent of 5 percent of the lump sum. It would seem that under the proposed legislation a refund of an ex-member's own contributions and the gratuity paid on retirement are regarded as two separate and distinct sums. Consequently, the amount received on retirement as a refund of contributions should be treated as not being subject to tax. However, 5 percent of the separate gratuity paid will be assessable under section 26(d) of the Assessment Act.

COMMISSIONER OF TAXATION