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Finance ministry circular on redundancy payments

The finance ministry has issued a circular on employee redundancy payments, dealing essentially with the question of income accumulation in a single tax year.

A lumpsum payment in compensation for loss of future income received by an employee may rank as “extraordinary” income. If the payment meets the criteria, the employee’s tax charge is five times the incremental tax on one-fifth on the amount. This relieves him from an excessive burden from the progressive rate scale, that would be borne, were he to be required to tax a single redundancy payment in the year of receipt. It is therefore dependent upon actual receipt of the entire amount within the same tax year. The finance ministry has now issued a circular explaining the concept in more detail. Points worthy of note are:

- A privileged redundancy payment compensates for loss of future income. A settlement payment for entitlements already earned or existing, such as salary arrears or untaken holiday, does not rank for the relief.
- The entire redundancy payment must be made within the same tax year. However, a second payment of not more than 5% of the main amount made earlier or later will not be considered harmful. Spreading the payment over two years will also be accepted, if necessary to relieve unusual hardship for the employer or employee.
- Granting or altering a pension promise on the occasion of redundancy will not affect the tax treatment of the compensation payment as “extraordinary” income.

Keywords

extraordinary income, income accumulation, redundancy