Bring forward retirement plans

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Executives looking forward to golden handshakes are being advised to bring forward retirement plans due to a change in the tax treatment of employment termination payments (ETPs) that may mean vastly bigger tax bills.

From July 1 if an ETP takes total income to more than $180,000, the tax impost on that part of the ETP above the top tax threshold will be 46.5 per cent. Under the current rules, any ETP – whether part of a redundancy payout or a contractual agreement with an employer – is concessionally taxed. The first $165,000 is taxed at a maximum of 15 per cent for those 55 and over and 30 per cent for those who are younger. Generally amounts above these caps are taxed at 46.5 per cent.

The cap is indexed and will be $175,000 for the 2012-13 tax year. Amounts above these caps are taxed at 46.5 per cent.

The new rules will not apply to "genuine redundancies", says Colin Lewis, head of technical services at ipac Securities. In situations where someone's job is no longer required and they are made redundant, their ETP will continue to be taxed concessionally up to the $175,000 threshold.

Timing will be everything for top earners trying to avoid the extra tax. Taking a payout early in a new financial year, for example, will mean working off a low income base.

As shown in the table, someone earning $150,000 and receiving an ETP of $175,000 will pay almost $40,000 more in tax by retiring late in the next financial year compared to before June 30 this year

"Employees who had planned to retire post July 1, 2012, will need to reconsider their plans and possibly take their retirement this financial year or early in the new financial year when their taxable income is likely to be lower," says John Randall, superannuation tax partner at Deloitte.

ETPs comprise any "extra sums" stipulated on an employment contract, says Louise Biti of adviser Strategy Steps, as well as amounts in a redundancy payout over and above certain tax-free amounts based on years of service.

Unused leave payments are not counted.

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