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PRACTICE NOTE

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Termination Payments

Introduction

An amendment to the definition of a termination payment has recently been added by the Income Tax Act 2001. The purpose of this Practice Note is to clarify the position following the change to the legislation.

In section 48A(6) of the Income Tax Act 1970 the definition of a termination payment is now as follows:-

"termination payment means a payment which is made, whether in pursuance of any legal obligation or not, either directly or indirectly in consideration or in consequence of, or otherwise in connection with, the termination of the holding of any office or employment or any change in its functions or emoluments, including any payment in commutation of annual or periodical payments (whether chargeable to tax or not) which would otherwise have been made as aforesaid but does not include any payment which is otherwise chargeable to income tax."

This amendment applies in respect of the income tax year commencing 6 April 2001 and subsequent years.

General Treatment Of Termination Payments

Relief is available of up to £30,000 for a termination payment made to an individual.

Whether a payment made to an individual on the termination of his office or employment is subject to the £30,000 relief depends on whether the payment was made by way of reward for services, or whether it is genuinely made to compensate the individual for the loss of employment rights. It is only the latter which will now qualify for the relief.

Examples of payments that still qualify for the £30,000 tax relief include any redundancy payment or payment made on the termination of employment where there is no contractual right to that payment.

Examples of payments that will no longer fall to be treated as termination payments and will therefore not be subject to the £30,000 tax relief in future include the following :-

A payment made as compensation for losing the right to a payment or bonus that would otherwise have been taxable.

A payment where the employer gives notice of termination to an individual and informs the individual that they need not work to the termination date and pays wages attributable to the notice period in a lump sum, this in effect being an advance payment of wages.

A payment made in lieu of notice where there is a contractual right to the payment.

Termination Payments To New Residents

By concession the Division will not pursue any liability to income tax in respect of the payment where a new resident receives a lump sum termination payment in respect of employment outside the Isle of Man. The concession only applies where the employment ceased within one month after the commencement of residence and the termination payment is made within three months of that date.

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Assessor of Income Tax

This practice note is intended only as a general guide and must be read in conjunction with the appropriate legislation. It does not have any binding force and does not affect a person's right of appeal on points concerning their own liability to income tax.

Comments and suggestions for improvements of issued Practice Notes and suggestions for future Practice Notes are always welcome.