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Speak to a financial adviser who can help navigate the intricacies and financial implications of retrenchment.

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BE SMART WITH RETRENCHMENT MONEY

By Renee Eagar, Certified Financial Planner, Brenthurst Wealth Management

The Covid-19 pandemic has delivered economic hardship in its wake as countries around the world instituted lockdown measures in an attempt to limit the spread of the virus. As a result, massive job losses have become the order of the day, in South Africa and many other countries.

If you were retrenched during this period, there are some significant financial decisions you will need to make that are entirely dependent on your circumstances. Although a stressful and difficult time, it is of great importance to manage the impact on personal finances with caution and guidance.

It is imperative to seek the advice of an expert and experienced financial adviser who can help navigate the intricacies and financial implications of retrenchment.

The first decision to make when you are retrenched, is around the money held in your employer’s pension or provident fund.

A lump-sum pay-out will be considered as a ‘retrenchment benefit’ for tax purposes if your loss of employment is because of your organisation ceasing operations or your skills have become redundant.

Unfortunately, as retrenchment benefits are linked to loss of formal employment, they may only be provided in respect of occupational funds such as pension and provident funds, and not in respect individual retirement annuities.

And while preserving your retirement benefit is always the first option, in trying times such as these there might be no other option to make ends meet.

If retrenched, you have the option to withdraw the capital in your employer's retirement fund, although there are tax implications that need to be considered. Everyone is given a once-in-a-lifetime tax relief of R500 000 on their retirement lump sum, bearing in mind that a retrenchment severance benefit is considered and taxed as a retirement lump-sum benefit.

It is important to bear in mind that the South African Revenue Service (Sars) takes all previous taxable withdrawals, retirement (including retrenchment benefits) and severance benefits you have received into account when calculating tax liability.

There are several ways in which you can preserve the remainder of your retirement benefits including leaving it in your (now former) employer's retirement structure, assuming the fund's rules allow for it, or consider transferring it to a preservation fund where you can have an advisor oversee your fund choice and fund manager allocations and actively manage the portfolio.

PRESERVATION FUNDS are specifically designed to invest pension or provident fund savings into, with the added benefit of making one full or partial withdrawal from the fund before retirement age 55. One limitation of a preservation fund, however, is that you cannot make additional contributions to this fund.

RETIREMENT ANNUITIES are the third option, where you can make a tax-free transfer of your retirement benefits to either an existing or new retirement annuity (RA). An RA allows you to make interval or ad hoc contributions after the fact, although it is important to bear in mind that you will not be able to access these funds until age 55.

If you are fortunate enough to have found new employment, you can preserve your pension fund money by transferring it tax-free to your new employer's pension fund. Please note, however, that there are tax implications if you transfer from a pension fund to your new employer's provident fund, so be sure to get the proper advice.

A 'severance benefit' is essentially the cash payment that your employer pays you because of your loss of employment.

South African law provides that you are entitled to at least one week's pay for each year of completed service, but it is important to check your employment contract as you may be entitled to more.

The tax treatment of a severance benefit is the same as in the case of your retrenchment benefits (i.e. withdrawal from retirement fund), bearing in mind that you will be taxed on a combination of both benefits.



Apart from your severance benefit, you will also receive any monies owed to you in respect of overtime, leave, commissions, incentives, or bonuses. It could be a substantial amount and you need to take extra care on how you preserve or draw from it.

Sars will, therefore, consider the combined value of your severance and retrenchment benefits, with the first R500,000 being tax-free. Thereafter, the next R200,000 is taxed at 18%, the next R350,000 at R36,000 plus 27% of taxable income above R700,000, and any amount over R1.05m is taxed at 36%.

You have several options regarding your severance benefits, and what you do with this money largely depends on your circumstances. If you are likely to need the money in the short term, rather put your cash in an interest-bearing account until you have more certainty regarding your future. Alternatively, you can consider investing this capital into a discretionary unit trust portfolio where it can achieve investment growth over the longer term.

You might also want to use some of this money to settle debt and thereby reduce your monthly repayments, however, it is important to find the right balance between paying off debt and ensuring that you have sufficient cash flow while you are looking for another job.

The stress of retrenchment can be overwhelming and not managing your finances with caution during this time may have a detrimental effect on your future financial situation, which is why the guidance of an advisor is recommended.

Read more about [investment planning](#).

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RENEE is head of the Newlands office. She is a **CERTIFIED FINANCIAL PLANNER®** professional, a member of the Financial Planning Institute of South Africa and is fully qualified to give advice on all investment matters.

Renee has been in the financial services industry for 21 years since 1998 and has worked for institutions namely TMA and Investec Asset Management.

Renee obtained her Higher Certificate in Financial Markets in 2004 and was awarded the **CERTIFIED FINANCIAL PLANNER®** designation in 2006.

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