



# momentum

## Preferred compensation

One of the most valuable assets of any business is its employees, especially those with the relevant knowledge, skills and experience.

### The risk

A high staff turnover is a costly business risk as it results in loss of productivity, intellectual property, employment costs and training costs. Therefore it is important for a business to retain and motivate its employees.

### The solution

The business can implement a preferred compensation scheme. This is an incentive scheme for valuable employees. The purpose of the scheme is to motivate and retain good employees. It rewards key employees with tax-free bonuses every five years and eliminates the cost of staff turnover and reduced productivity.

### How the plan works?

The employee effects an endowment policy on his/her own life. The employer increases the employee's remuneration to allow for the payment of the full premium, with after-tax funds. The employer enters into a service agreement with the employee whereby the employee undertakes to remain in the employer's service for a minimum period of five years. The policy, which is owned by the employee, is ceded to the employer as security for his/ her undertaking. The employer is contractually bound to cancel this cession either prior to maturity or after five years (or any other term as agreed to by the parties) or upon the death of the employee. Upon the cancellation of the cession the employee has the unconditional ownership of the policy. The employee can then make a withdrawal from the policy, which will be tax-free. Where the policy matures the proceeds will also be payable to the employee tax-free. If the employee does not fulfill the contractual obligation, the employer will be entitled to the policy in terms of the security cession. The employer will be entitled to the proceeds in the policy (as provided for in the agreement) and the proceeds will be payable to the employer tax-free.

### Benefits to the employer

1. This is a unique way to retain employees securing the service of key employees for at least 5 years;
2. The total amount paid by the employer is tax deductible, as it is part of the remuneration of the employee; and
3. Should the employee not remain in the service of the employer for the specific time, the employer is protected as a result of the security cession.

## Benefits to the employee

1. The employee receives a tax-free benefit for long service;
2. The security of the benefit is provided by the service agreement;
3. This is a forced saving, making provision for future needs easier to the employee; and
4. This does not affect any tax benefit due to any other retirement funds or deferred compensation scheme.