

	<b>NOTICE TO EMPLOYERS – PAYE</b>	<b>Document #</b> AS-NT-09	<b>Revision #</b> 0	<b>Effective</b> 01.03.2006
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**Notice No 1 of 2006 — 14 January 2006**

**TOPIC: LEGISLATION CHANGES RELATING TO MEDICAL SCHEME CONTRIBUTIONS AND EXPENSES**

The Minister of Finance proposed a reform of the tax treatment of medical scheme membership and health care costs in his budget speech on 23 February 2005. This proposal will be incorporated into the Income Tax Act (IT Act) through the Revenue Laws Amendment Bill, 2005, which has been passed by Parliament and will be promulgated within the next few weeks. These proposed amendments will become effective **from 1 March 2006**.

**1. FRINGE BENEFIT - EMPLOYER PAYS CONTRIBUTIONS TO MEDICAL SCHEME [Par. 2(1) & 12A of the 7<sup>th</sup> Schedule to the IT Act].**

The existing “**2/3**” rule falls away with effect from 1 March 2006.

The calculation of the taxable fringe benefit where the employer pays the contributions of an employee to a medical scheme (excess above the 2/3's) has been amended by applying a monetary cap that takes into account the number of beneficiaries covered by the medical scheme membership.

The taxable fringe benefit is so much of the contributions paid by the employer as exceeds the following monthly capped amounts:

- R500 for employee only;
- R1 000 for employee and one dependant only; or
- R1 000 for employee and first dependant plus R300 for every additional dependant thereafter.

See Example 1 below.

This taxable fringe benefit must be taken into account as remuneration for employees' tax purposes. It is also deemed to be paid by such employee in terms of the new section 18(5) of the IT Act and is therefore considered to be contributions paid by that employee.

However, where an employee is 65 years or older, no taxable fringe benefit must be taken into account.

**2. CONTRIBUTIONS TO A MEDICAL SCHEME THAT MAY BE TAKEN INTO ACCOUNT FOR EMPLOYEES' TAX PURPOSES [Par 2(4)(e) of the 4<sup>th</sup> Schedule of the IT Act]**

Employers will be allowed (at their option) to take into account, before calculating the employees' tax liability of an employee, **contributions paid by that employee to a medical scheme**.

The amount that may be taken into account for this purpose, is the following -

- **Employee 65 years or older:** The **total contributions** made by the employee (in respect of himself or herself, his or her spouse and any dependant) to a registered medical scheme in respect of which proof of payment has been furnished to the employer;
- **Employee under 65 years:** So much of any contributions made (including deemed to be made) by the employee (in respect of himself or herself, his or her spouse and any dependant) to a registered medical scheme (in respect of which proof of payment has been furnished to the employer) as does not exceed –
  - **the capped amount** applicable to the relevant employee (R500 for employee only; R1 000 for employee and one dependant only; or R1 000 for employee and first dependant plus R300 for every additional dependant thereafter),
  - **reduced by** any contributions paid by the employer not included in the remuneration of such employee.

See Example 2 below.

**3. FRINGE BENEFIT - EMPLOYER PAYS MEDICAL COSTS [Par. 2(j) and 12B of the 7<sup>th</sup> Schedule to the IT Act]**

Where an employer paid medical costs in respect of any medical, dental and similar services, hospital services, nursing services and prescribed medicine of an employee, his or her spouse, child, other relative or dependant, such payments are regarded as taxable fringe benefits and were previously reported under code 3808 – Payment of an employee's debt. This benefit has now specifically been inserted into the IT Act and must in future be reported under a new code 3813 – see par. 4 of this notice.

This taxable fringe benefit must be taken into account as remuneration for employees' tax purposes. It is also deemed to be paid by such employee in terms of the new section 18(5) of the IT Act and is therefore also considered to be costs paid by that employee. Employers are however required to split the costs between two reporting codes namely, 4024 and 4485 – see par. 4 of this notice.

This benefit will not be regarded as taxable under certain circumstances and should be reported under a new code 4487 – see par. 4 of this notice. These

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circumstances are listed under the proposed paragraph 12B(3) of the Seventh Schedule – see the Revenue Laws Amendment Bill, 2005, for full detail.

**4. CODES FOR TAX CERTIFICATE [IRP 5 / IT 3(a)] PURPOSES**

The following **new** income, deduction and information codes for purposes of issuing employees' tax certificates are effective from 1 March 2006 (2007 year of assessment).

- **Code 3813** – Taxable fringe benefit in respect of medical costs paid by employer (paragraph 12B fringe benefit);
- **Code 4024** – Medical costs deemed to be paid by employee in terms of section 18(5) only in respect of **employee, his / her spouse and child**;
- **Code 4025** – Medical contribution taken into account for employees' tax purposes;
- **Code 4485** – Medical costs paid by employer in respect of **other relatives or dependants** (not spouse and child / children of employee);
- **Code 4486** – “Capped amount” determined by employer;
- **Code 4487** – Non-taxable fringe benefit in respect of medical costs paid by employer under certain specified circumstances (benefits not regarded as taxable i.t.o. paragraph 12B).

The following **existing** codes remain in place for employees' tax certificate purposes (please note that the definition of code 4005 has been amended):

- **Code 3810** – Medical contributions paid by employer (paragraph 12A fringe benefit)
- **Code 4005** – Medical contributions paid **and deemed to be paid by employee in terms of section 18(5)**
- **Code 4474** – Medical contributions made by employer's

**Validation rules relating to new codes:**

- The value of code 3813 must be equal to the sum total of the values of code 4024 and 4485.
- Code 4005 is mandatory if a value for code 3810 or code 4025 is specified.
- Code 4486 is mandatory if a value for code 4025 is specified.
- The value of code 4025 may not be greater than the value of code 4005.

**CONTACTING SARS**

Details of the amendments to the legislation can be found in the Revenue Laws Amendment Bill, 2005 (Bill 40 of 2005) on SARS website at [www.sars.gov.za](http://www.sars.gov.za) under "Legislation".

Where employers have queries relating to PAYE, SDL and UIF contributions, they should contact their local SARS branch office. Additional information can be obtained on the SARS website at: [www.sars.gov.za](http://www.sars.gov.za)

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### EXAMPLE 1

The following example illustrates the determination of a paragraph 12A fringe benefit.

- a) The number of beneficiaries covered by the medical scheme membership of the employee is 5.
- b) The employer pays R2 200 of the total monthly contributions of R3 594 and the employee pays R1 394.

**Determining the fringe benefit (see paragraph 1 of this notice).**

- Determine the capped amount for fringe benefit purposes (paragraph 12A).
  - i. R1 000 (for member and first dependant) + R300 x 3 (for additional dependants) = R1 900
- Determine the taxable fringe benefit which must be included in the income of the employee.
  - i. Deduct the capped amount from the amount paid by the employer (R2 200 – R1 900) to determine the taxable fringe benefit (R300).
- Determine the contributions paid by the employee (actual and deemed) by adding the fringe benefit as well as the actual portion paid by the employee (R1 394 + R300 = R1 694).

**IRP 5 detail:**

- Code 4005 = R1 694
- Code 3810 = R300
- Code 4474 = R2 200
- Code 4486 = R1 900

### EXAMPLE 2

The following example illustrates the determination of the medical scheme contributions to be taken into account for employees' tax purposes.

- a) The number of beneficiaries covered by the medical scheme membership of the employee is 5.
- b) The employer pays R1 800 of the total monthly contributions of R3 594 and the employee pays R1 794.

**Determining the portion of the contributions to be taken into account for employees' tax purposes (see paragraph 2 of this notice).**

- Determine the capped amount for medical contributions purposes (paragraph 2(4) & section 18).
  - i. R1 000 (for member and first dependant) + R300 x 3 (for additional dependants) = R1 900
- Determine the portion of the contributions to be taken into account for employees' tax purposes (paragraph 2(4)).
  - i. Determine the employee medical scheme contributions (R1 794) as does not exceed –
  - ii. the capped amount applicable to the employee R1 900
  - iii. proviso – reduced by employer contributions not included in employee's remuneration
 

-R1 800	
Contributions to be take into account	R 100

The allowable portion for PAYE purposes of the employee's medical contributions is therefore R 100.

**IRP 5 detail:**

- Code 4005 = R1 794
- Code 4025 = R100
- Code 4474 = R1 800
- Code 4486 = R1 900

Notes:

- As the R1 800 contributions made by the employer is less that the capped amount (R1 900) applicable to the employee, there is NO taxable fringe benefit and NO fringe benefit is therefore included in the employees remuneration – see par. 1 of this notice.
- The R1 694 remaining medical scheme contributions made by the employee and not taken into account for PAYE purposes (R1 794 – R 100) will only be considered for tax deduction purposes with the submission of the annual income tax return.

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### EXAMPLE 3

The following example illustrates the capped amount calculation, paragraph 12A and 12B fringe benefit determination, calculation of medical contributions to be taken into account for employees' tax purposes (paragraph 2(4)), and the reporting of the relevant information on an employees' tax certificate.

	Member & depend.	Monthly capped amount <b>4486</b>	Total contributions	Employer's portion <b>4474</b>	Employee's portion	Par 12A benefit (contrib.) <b>3810</b>	Employee's medical contributions <b>4005</b>	Par 2(4) deduction <b>4025</b>	Par 12B benefit (costs) <b>3813</b>
Mar	5	R 1 900	R 3 594	R 1 800	R 1 794	0	R 1 794	R 100	
Apr	5	R 1 900	R 3 594	R 1 800	R 1 794	0	R 1 794	R 100	
May	5	R 1 900	R 3 594	R 1 800	R 1 794	0	R 1 794	R 100	R 250 <sup>1</sup>
Jun	6	R 2 200	R 4 836	R 1 800	R 3 036	0	R 3 036	R 400	
Jul	6	R 2 200	R 4 836	R 1 800	R 3 036	0	R 3 036	R 400	
Aug	6	R 2 200	R 4 836	R 1 800	R 3 036	0	R 3 036	R 400	
Sep	6	R 2 200	R 4 836	R 1 800	R 3 036	0	R 3 036	R 400	
Oct	6	R 2 200	R 4 836	R 1 800	R 3 036	0	R 3 036	R 400	
Nov	6	R 2 200	R 4 836	R 2 400	R 2 436	R 200	R 2 636	0	R 4 500 <sup>2</sup>
Dec	5	R 1 900	R 3 594	R 2 400	R 1 194	R 500	R 1 694	0	
Jan	5	R 1 900	R 3 594	R 2 400	R 1 194	R 500	R 1 694	0	R 220 <sup>3</sup>
Feb	5	R 1 900	R 3 594	R 2 400	R 1 194	R 500	R 1 694	0	R 130 <sup>4</sup>
<b>Total</b>		<b>R24 600</b>	<b>R50 580</b>	<b>R24 000</b>	<b>R26 580</b>	<b>R1 700</b>	<b>R28 280</b>	<b>R2 300</b>	<b>R5 100 <sup>5</sup></b>

#### Notes:

- Employer paid costs of doctor in respect of the employee's child.
- Employer paid cost of prescribed medicine in respect of the employee's mother-in-law.
- Employer paid costs of hospital in respect of the employee's spouse.
- Employer paid costs of prescribed medicine in respect of the employee's stepchild.
- The paragraph 12B fringe benefit must be split between costs in respect of the employee, his / her spouse and child (code 4024) and other relatives and dependants (code 4485).

#### Employees' tax certificate (reporting):

- Code 3810: The amount by which the employee portion of the contribution exceed the capped amount (paragraph 12A amount) must be reported as a taxable fringe benefit (**R1 700**).
- Code 3813: The amount of the costs paid by the employer in respect of the employee, his / her spouse, child and other relatives must be reported as a taxable fringe benefit (**R5 100**).
- Code 4005: The amount of the employee's own contributions as well as the deemed contributions (code 3810) must be reported (**R28 280**).
- Code 4024: The amount of the deemed expenses of the employee paid by the employer, only on behalf of the employee, his / her spouse and child must be reported separately (**R600**).
- Code 4025: The amount of the contributions taken into account, by the employer at his option, for purposes of calculating employees' tax, must be reported (**R2 300**).
- Code 4485: The total amount of the deemed expenses of the employee paid by the employer, only on behalf of the other relatives of the employee, must be reported (**R4 500**).
- Code 4486: The amount of the monthly determined "capped amount" must be reported (**R24 600**).
- Code 4474: The amount of the employer's contributions must be reported (**R24 000**).

#### Rules to be applied:

- Determine the capped amount per month (code 4486)**  
Allow R500 for member, R500 for first dependant and R300 for each additional dependant thereafter.
- Determine the taxable fringe benefit - paragraph 12A (code 3810)**  
Where the employer's contribution exceeds the "capped amount", the excess contribution is equal to the taxable fringe benefit (excluding employees 65 years or older).
- Determine the medical contributions paid by the employee (code 4005)**  
The contributions actually paid by the employee (employee portion) plus the value of code 3810 (contributions deemed paid by employee) must be added.
- Determine amount of medical contributions to be taken into account for PAYE purposes – par 2(4) (code 4025)**  
Determine the result of 4486 – (4474 – 3810);
  - If the result is greater than the value of 4005, the allowable deduction is the value of 4005.
  - If the result is less than the value of 4005, the allowable deduction is the result amount.