

## Tax on termination payments: HR guide

[Call 0203 797 1264](tel:02037971264)

[CLICK HERE TO DOWNLOAD THE GUIDE](#)

### Tax on termination payments and exemptions

It is a common misunderstanding that all **termination payments** qualify for a £30,000 **tax** exemption. The exemption only applies if the payment is not otherwise chargeable to income tax.

#### What is the payment for?

Generally, contractual payments will be subject to income **tax** and national insurance contributions (NICs).

Other payments relating to the termination of employment may only be liable to tax on the amounts exceeding £30,000 and may be completely exempt from NICs.

This general distinction is not very helpful though because there are a number of exceptions.



## Examples of termination payments

Payments for restrictive covenants, which prohibit competitive activity, and confidentiality are subject to tax and NICs.

Payments for retirement are also subject to tax and NICs.

Genuine redundancy payments, even if they are paid under a contractual redundancy policy, do, however, attract the £30,000 tax exemption.

Also, payments to employees on account of their disability or injury – providing certain conditions are met – are completely exempt.



## Notice pay

All pay corresponding to notice is subject to deductions for income tax and NICs. This has been the law since 6 April 2018.

The previous position was that if there was no payment in lieu of notice clause (PILON) in the employment contract and the employer paid out and asked the employee to leave, income tax and NICs would not, generally, be due. Any sum in excess of £30,000 would be taxable, though not subject to employer or employee NICs' deductions.

It is now irrelevant whether an employee has a PILON in their contract. All sums corresponding to earnings for notice are subject to tax and employer and employee NICs.

Under the new rules, if an employee is paid in lieu of some or all of his or her notice period, the employer must deduct income tax and employee NICs from, and pay employer NICs on, the employee's post-employment notice pay (PENP).

HMRC has provided updated [guidelines](#) on using the formula to calculate PENP.

From 6 April 2020 employer NICs will be due on the balance of any qualifying termination payments over £30,000.



## Use of PILONs

Some employers have deliberately not included a PILON in contracts so that there is more flexibility in structuring an exit deal. However, if no PILON is included and the employer pays the employee in lieu of notice, the employer would be at risk of breaching the contract. An employee could then argue that any [restrictive covenants](#) in the contract are no longer enforceable because of the breach.

Since employers will no longer benefit from a PILON-free contract, PILONs should be included in contracts. This will avoid risk of a breach for paying in lieu of **notice** and not being able to enforce restrictive covenants.

This guide is for guidance only and should not be relied upon for specific advice.

**Matt Gingell**

Specialist Employment Lawyer London

<https://www.mattgingell.com>

---

If you need any advice on **tax and termination payments** or have other employment law queries please do not hesitate to [contact](#) me on [0203 797 1264](tel:02037971264).

Do check [mattgingell.com](http://mattgingell.com) regularly for updated information.