

The (tax) benefit of keeping employees incentivised

 By [Graeme Palmer](#)

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Section 11(a) of the Income Tax Act allows a taxpayer to deduct expenditure for purposes of determining taxable income if such expenses are incurred in the production of income. Are expenses incurred in maintaining a content and motivated workforce part of the costs of a taxpayer's income-producing operations? The majority decision of a full bench of the Western Cape High Court in *CSARS v Spur Group (Pty) Ltd* held that they are.



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The Spur Group implemented a Share Incentive Scheme (scheme) in which eligible employees could participate. Spur contributed R48-million to the scheme's trust which amount was claimed as a deduction against its taxable income over seven years in terms of s11(a). The contribution was ultimately utilized for acquiring shares in the Spur holding company which benefited employees. Sars disallowed the deduction which decision Spur appealed against.

Without getting into the details here of what was a complex scheme, it is of interest that the purpose of the scheme was to incentivise employees to participate in the growth of the Spur Group of companies. Instead of making the contribution, Spur could have loaned the monies to the employees to acquire shares, but this may have had the effect of disincentivising the employees, particularly if the share price dropped below the loan amount. As a service-orientated business, Spur required an enthusiastic, committed and competent workforce and participation in the scheme incentivised employees to remain employed with Spur.

For the expenditure (i.e. the contribution) to meet the "in the production of income" test and satisfy the requirements of section 11(a), there had to be a sufficiently close connection or link between it and the income earning operations of the taxpayer. The degree of closeness required for the expenditure to be deductible is determined on the particular facts and circumstances of each taxpayer.

The High Court found that the contribution was disbursed in order to indirectly facilitate the carrying on of the taxpayer's trade. Even if it did not directly benefit the employees, the evidence supported the fact that it incentivised and motivated the participating employees. It was not a requirement that employees benefit directly from the contribution. Spur thus discharged its onus of proving that the expenditure was incurred in the production of income and that there was a sufficiently close nexus between the expenditure and the production of income. Sars may still appeal this decision further to the Supreme Court of Appeal.

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