



HM Revenue  
& Customs

# Consultation on salary sacrifice for the provision of benefits in kind

## **Consultation document**

Publication date: 10 August 2016

Closing date for comments: 19 October 2016

<b>Subject of this consultation:</b>	Limiting the range of benefits in kind (BiKs) that attract income tax and National Insurance contributions (NICs) advantages when they are provided as part of salary sacrifice and flexible benefit arrangements.
<b>Scope of this consultation:</b>	To explore potential impacts on employers and employees should the government decide to change the way the benefits code applies when a BiK is provided in conjunction with a salary sacrifice or flexible benefit scheme.  Employer pension contributions, employer-provided pension advice, employer-supported childcare and provision of workplace nurseries and cycles and cyclist's safety equipment provided under the cycle to work scheme will remain unaffected by this measure.
<b>Who should read this:</b>	The government is interested in hearing from everyone with a view on this subject, including employers who operate salary sacrifice and flexible benefit arrangements, their representatives, trade organisations and any other interested parties.
<b>Duration:</b>	The consultation will run from 10 August 2016 to 19 October 2016.
<b>Lead official:</b>	Alex Raisen, HMRC.
<b>How to respond or enquire about this consultation:</b>	Written responses to the consultation can be addressed to: Employment Income Policy Team, Room 1E/08, 100 Parliament Street, London, SW1A 2BQ or e-mailed to: <a href="mailto:employmentincome.policy@hmrc.gsi.gov.uk">employmentincome.policy@hmrc.gsi.gov.uk</a>
<b>Additional ways to be involved:</b>	Meetings will be arranged with external representatives. If you are interested in attending a meeting to put forward your views, please contact the Employment Income Policy team at the address listed above.  If you require a version of this consultation document in Braille or in Welsh then please contact the Employment Income Policy team using the details shown above.
<b>After the consultation:</b>	The government will publish details of the consultation responses and expects to make an announcement at Autumn Statement 2016 on decisions made in light of those responses. Any policy changes are expected to feature as part of Finance Bill 2017.
<b>Getting to this stage:</b>	This consultation follows announcements that the government remains concerned about the growth of salary sacrifice arrangements and their fairness on the tax system.
<b>Previous engagement:</b>	Following Autumn Statement 2015, the government undertook an evidence gathering exercise. Responses have informed its approach and the government is now considering limiting the range of benefits that attract income tax and NICs when they are provided as part of salary sacrifice or flexible benefit schemes.

# Contents

	Foreword	4
1	Introduction	5
2	Background to the proposal	8
	Results of evidence gathering	9
3	Proposed approach	10
	Affected legislation	11
	Benefits in kind which would retain their current tax treatment under salary sacrifice	12
	Implementation	13
	Compliance	13
4	Summary of consultation questions	15
5	The consultation process: how to respond	16

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## Foreword

Whilst the majority of employees are rewarded mainly with cash remuneration, the provision of benefits in kind is a long-standing component of reward packages. Such remuneration packages are now offered in many different forms, often including a mixture of cash and benefits in kind, such as pension contributions and company cars.

The way in which benefits are provided has also evolved, with a growing market for flexible benefit packages, often combined with salary sacrifice arrangements. This growth represents an increasing cost to the Exchequer and creates an uneven playing field between employees and employers who use such arrangements and benefit from the tax advantages, and those that don't. We want employers to continue to offer benefits to their employees, but need to balance this with the interests of all taxpayers.

The government indicated its concern about the rising costs of salary sacrifice at Summer Budget 2015. At Autumn Statement 2015, we announced that we would undertake evidence gathering to better understand the main drivers influencing the use of salary sacrifice. HM Treasury and HM Revenue and Customs invited contributions from a wide range of stakeholders and worked with the Chartered Institute of Payroll Professionals to survey its members. I am grateful to all those who participated in that exercise.

At Budget 2016 the government announced that it is considering limiting the range of benefits that attract income tax and National Insurance contributions advantages when provided as part of a salary sacrifice arrangement.

This consultation sets out a proposal for future tax treatment of such benefits and encourages views from all interested parties.

**Jane Ellison MP**  
**Financial Secretary to the Treasury**

# Chapter 1: Introduction

- 1.1 Benefits in kind (BiKs) have been part of the employee remuneration landscape for some time. Although they are not offered universally, they are regarded by many employers as a useful tool for rewarding their staff.
- 1.2 Many BiKs are offered in addition to salary, but HMRC has seen a growth in salary sacrifice arrangements in recent years. These are agreements between an employer and employee to change the terms of an employment contract and reduce the employee's entitlement to cash pay in exchange for some form of non-cash BiK. The effect of this, depending on the BiK, is often to reduce the amount of income tax, employee and employer NICs due on the employee's remuneration.

**Example: salary sacrifice savings for a mobile phone contract**

The provision by an employer of a mobile phone to a director or employee for private use is exempt from tax and NICs. Therefore, if it is provided in addition to salary, there is no extra tax or NICs liability. However, where it is provided under a salary sacrifice agreement, there can be savings for both the employer and employee relative to the employee purchasing a phone from their take home pay.

A 24-month contract for a new mobile phone could cost over £1,000. This example shows the amount of tax and NICs saved on a contract of £700 purchased through salary sacrifice by an employee in each income tax band, by an employer, and the overall cost to the Exchequer.

<b>Contract cost: £700</b>	<b>Basic</b>	<b>Higher</b>	<b>Additional</b>
<b>Employee reduces gross salary by</b>	£700	£700	£700
<b>Cost to employee (reduction in net pay)</b>	£476	£406	£371
<b>Employee saves*</b>	£224, 32%	£294, 42%	£329, 47%
<b>Employer saves**</b>	£97, 13.8%	£97, 13.8%	£97, 13.8%
<b>Cost to Exchequer</b>	<b>£321</b>	<b>£391</b>	<b>£426</b>

\* The employee's income tax and Class 1 NICs

\*\* The employer's NICs

- 1.3 Not all employers offer BiKs to their employees. In addition, where BiKs are offered only through salary sacrifice arrangements, employees with earnings at or near the National Minimum Wage or the National Living Wage cannot participate because salary sacrifice arrangements cannot reduce an employee's cash earnings below the National Minimum Wage or National Living Wage rates. Those employees who are not able to participate in salary sacrifice arrangements are at a disadvantage. They have to fund what might otherwise be offered as a BiK from their net pay, whereas others can receive the BiK at a reduced cost at the expense of the Exchequer.

- 1.4 For employers, the provision of BiKs through salary sacrifice arrangements means that although the employees pay for the BiKs, the employer can also gain a tax advantage. Even where there may be some form of administration or management fee for a third party to manage the arrangements, this is likely to be more than covered by the NICs savings an employer may receive. This appears to be one of the reasons that these arrangements have grown in popularity.
- 1.5 Many salary sacrifice arrangements are specifically marketed by promoting the tax and NICs savings employers and employees can enjoy. For example, one provider of salary sacrifice schemes advertises on its website '*...a desirable salary sacrifice scheme that is straightforward and at zero cost to the employer who retains all employer NICs savings generated by the scheme*'.
- 1.6 Some employees are unaware that use of salary sacrifice can reduce the level of contributory benefits such as statutory maternity pay and Jobseeker's Allowance, or reduce the level of occupational pensions which can be referenced to post salary sacrifice levels of remuneration.
- 1.7 HMRC has seen significant growth in these schemes. There has been an increase of a third in PAYE clearance requests from employers for salary sacrifice arrangements between 2009/10 and 2014/15. The government believes that the growth of salary sacrifice has resulted in an increasing cost to the Exchequer due to the loss of tax and NICs. Also, salary sacrifice can artificially increase entitlement to tax credits or Universal Credit.
- 1.8 The government indicated its concern about this cost at Summer Budget 2015. At Autumn Statement 2015, the government reiterated its concerns and said that matters would be considered further. Subsequently, between December 2015 and February 2016, the government undertook an evidence gathering exercise to better understand the use of salary sacrifice.
- 1.9 At Budget 2016, the government announced it was considering limiting the range of BiKs that attract income tax and NICs advantages when they are provided as part of salary sacrifice schemes. The announcement was clear that pension saving, employer-supported childcare and the cycle to work scheme should continue to benefit from income tax and NICs relief when provided through salary sacrifice arrangements. These are benefits that the government specifically wants to encourage employers to provide.
- 1.10 However, the government does not believe that other BiKs, effectively paid for by employees themselves through reductions in gross salary, should be able to be provided by employers at a cost to the Exchequer through salary sacrifice arrangements.
- 1.11 The government recognises that salary sacrifice arrangements are an important part of employers' remuneration strategies. Employers wanting to offer BiKs in conjunction with salary sacrifice will still be able to do so; however, the tax and employer NICs advantages for some BiKs will be reduced. BiKs currently offered on top of salary will not be affected by the proposed changes.

1.12 No employee NICs are due on the vast majority of BiKs. Therefore, in most cases these changes will only apply to income tax and employer NICs.

## Chapter 2: Background to the proposal

- 2.1 Salary sacrifice arrangements normally take the form of an employee agreeing to give up cash remuneration in return for some form of non-cash BiK. Once that salary is given up it is not chargeable to income tax nor is it liable for employee or employer NICs.

### **Example**

An employee's current contract provides for cash remuneration of £40,000 a year with no benefits. The employee agrees with the employer that in future the employee will be paid cash remuneration of £39,500 a year and provided with a BiK valued at £500. The employer operates pay as you earn (PAYE) on £39,500 of salary rather than £40,000.

- 2.2 Increasingly, BiKs are offered under flexible benefit (or 'flexben') arrangements. These normally include an amount of cash salary and an amount which the employee can use to access a range of BiKs up to a certain value. The flexible benefit arrangement can also be structured as a salary sacrifice arrangement. This is the position where the original salary includes the value of the BiKs amount and that salary is reduced by the value of BiKs chosen.

### **Example**

An employee is recruited into a job with a headline salary of £100,000. However, they can exchange up to £10,000 of their salary for non-cash benefits such as private medical insurance or a company car. Their salary is reduced by the value of the BiKs chosen. If the employee selects the maximum value of BiKs allowed, they will be paid a cash salary of £90,000 and the employer must account for PAYE on £90,000 of salary rather than £100,000. If the value of the BiKs taken up is, say, £7,500, the cash remuneration is reduced to £92,500 and that is the amount of salary subject to tax and NICs.

- 2.3 In contrast, an employee may be entitled to a flexible benefits package in addition to an amount of cash pay but with no cash option within that benefits package. The employee can vary the BiKs provided, but have no choice about the level of their contracted cash pay. The government does not wish to capture these sorts of arrangements as the employee has no option to reduce their cash pay in exchange for the BiK. Such BiKs will continue to be taxed and liable for NICs as appropriate under the current rules. However, where an employee is able to trade BiKs for cash pay as set out in the example in the paragraph above, the intention would be for such arrangements to be affected.
- 2.4 For the remainder of this document, references to salary sacrifice should also be read as referring to relevant flexible benefit arrangements in which the employee can exchange cash remuneration for one or more BiKs.

## Results of evidence gathering

- 2.5 The government announced at Autumn Statement 2015 that it would gather evidence on salary sacrifice, including from employers, to inform its ongoing approach. During December 2015 and January 2016, HM Treasury and HM Revenue and Customs engaged with over 85 employers and representative bodies and collaborated with the Chartered Institute of Payroll Professionals (CIPP) to survey its members on the use of, and opinions on, salary sacrifice. The survey received over 200 responses from employers and payroll bureaus.
- 2.6 This research indicated that the use of salary sacrifice is increasing, with a number of employers saying they had deferred introducing new salary sacrifice schemes for the time being because of the government's announcement at Autumn Statement 2015.
- 2.7 The data and discussions showed that the vast majority of benefits supplied through salary sacrifice are employer pension contributions, employer-supported childcare and the provision of cycles and cyclists' safety equipment. Other popular benefits include private medical insurance (which is liable to both tax and employer NICs) and additional annual leave. Growth areas include cars, health screening and the provision of assets such as mobile phones, TVs, computers and white goods.
- 2.8 The government is grateful to all stakeholders who were involved in the evidence gathering process and has used this to inform its proposed approach.

## Chapter 3: Proposed approach

- 3.1 The government has considered how to reduce the Exchequer cost of these arrangements and level the playing field between employers who offer these arrangements and those who don't. This section set out the proposal in more detail.
- 3.2 The government proposes to change tax legislation so that where a BiK is provided through salary sacrifice, it will be chargeable to income tax and Class 1A employer NICs, even if it is normally exempt from tax and Class 1A NICs, at the greater of:
- the amount of salary sacrificed; and
  - the cash equivalent set out in statute (if any).

This would mean that where the normal taxable value of the BiK is higher than the amount of salary sacrificed, it would be subject to tax and Class 1A NICs in the normal way.

- 3.3 At Budget 2016, the government stated its intention to exclude a number of BiKs from the policy because it wishes to encourage employers to provide these to employees. Therefore, views are **not** being sought on the following:
- **employer pension contributions;**
  - **employer-provided pension advice based on the recommendations of the Financial Advice Market Review (FAMR);**
  - **employer-supported childcare and provision of workplace nurseries; and**
  - **cycles and cyclist's safety equipment which meet the statutory conditions.**
- 3.4 The Budget also indicated that it was the government's intention that health-related benefits such as cycle to work should continue to benefit from relief when provided through salary sacrifice arrangements. The government has carefully considered the case for carving out other health-related BiKs from the change, but has ruled this out.
- 3.5 Other health-related exemptions for BiKs are in place to ensure that no tax or NICs liabilities arise where employers pay for and provide certain BiKs for their employees, such as health screenings, or because ascribing a value to the cost of the BiK to each employee benefitting may be difficult; for example, workplace gyms. Where these BiKs are provided through salary sacrifice, it is the employee who effectively pays for them, and the employer has, by setting the amount of salary that must be sacrificed, valued the BiK.
- 3.6 This proposal does not prevent employers from providing BiKs to their employees through salary sacrifice, but it will remove the tax and NICs advantages that come from doing so. Employers can still use salary sacrifice if they wish and the taxation of BiKs will be unaffected if offered outside of the salary sacrifice arrangement.

- 3.7 There will be no change where salary is sacrificed in return for intangible benefits that are not taxed and do not rely on a specific tax exemption, such as where salary is sacrificed in exchange for extra annual leave or flexible working hours.
- 3.8 Payroll Giving will not be affected by this change. Where an employer offers Payroll Giving, the employee is able to donate to a charity of their choice from their salary before income tax is deducted. There is no corresponding NICs relief for the employer or employee. The government is aware that some schemes operate through salary sacrifice arrangements to access the NICs relief that would not otherwise be due. The government is therefore considering that in these circumstances both employer and employee NICs should be applied.

**Question 1:** Alongside annual leave, are there any other salary sacrifice arrangements that the government should be made aware of that do not strictly involve receipt of a benefit?

**Question 2:** What are the likely impacts on employers and employees of limiting the scope of BiKs that can obtain tax advantages when offered through salary sacrifice arrangements?

**Question 3:** Are these impacts different, or are there different considerations, for large/small businesses or particular business sectors?

**Question 4:** Are the impacts different for particular BiKs?

**Question 5:** Do you think that the government needs to take any steps to mitigate any negative consequences of this change for employees and employers, such as those who may be locked into salary sacrifice arrangements? If responding, it would be helpful to understand specific examples and factors the government should take into consideration.

## Affected legislation

- 3.9 Legislation sets out how BiKs must be treated for tax purposes. Section 6 of the Income Tax (Earnings and Pensions) Act 2003 (ITEPA) imposes a charge to income tax on employment income, which includes general earnings. Section 7(5) provides that general earnings includes any amount treated as earnings under the benefits code in Part 3 of ITEPA. However, many BiKs are subject to an exemption from tax. Part 4 of ITEPA sets out all the exemptions.

- 3.10 Generally, the amount treated as general earnings of the employee under the benefits code is determined by reference to the 'cash equivalent' of the benefit. This is usually the cost to the person providing the benefit unless affected by a special rule such as car benefit.
- 3.11 Legislation would change the way that the benefits code in Part 3 and the exemptions in Part 4 apply when a BiK, other than those whose treatment would remain unchanged, is provided in conjunction with salary sacrifice.
- 3.12 Where an employee is provided with a non-exempt BiK in conjunction with salary sacrifice, the cash equivalent of the BiK would equal the greater of the cash equivalent of the BiK as specified in the benefits code, or the actual amount of the salary sacrificed by the employee.
- 3.13 Where an employee is provided with a tax-exempt BiK in conjunction with salary sacrifice, the exemption would no longer apply. The cash equivalent of the BiK, treated as general earnings of the employee, would equal the greater of the taxable value of the BiK specified in the benefits code (if the exemption had not applied), or the amount of salary sacrificed by the employee.
- 3.14 For NICs, the majority of BiKs attract a Class 1A (employer only) NICs liability. The Class 1A NICs treatment of the BiK will continue to follow the income tax treatment following any change.

**Example**

In September 2016 employer A and employee X agree a salary sacrifice arrangement. Employee X earns £25,000 annually and agrees to sacrifice £600 for workplace parking.

Employee X agrees to a £50 a month reduction in their salary for a period of 12 months. Until 5 April 2017 there will be no tax or Class 1A NICs due on the cost of the workplace parking because this is subject to an exemption from tax under s237 of ITEPA.

From 6 April 2017, the exemption under s237 of ITEPA will be dis-applied and there will be a taxable BiK equal to the amount of salary sacrificed. In addition, a corresponding Class 1A NICs liability will arise for the employer on that same amount.

**BiKs which would retain their current tax treatment under salary sacrifice**

- 3.15 As announced at Budget, following any change, certain exempt BiKs would retain their existing tax treatment under Part 4 ITEPA with the same treatment for Class 1A NICs. These are:
- The exemptions for childcare vouchers in Chapter 6 at sections 270A to 270B as long as the conditions in sections 318B to 318D were met;
  - The exemptions for employer provided pension contributions in Chapter 9;

- The exemptions for employer-supported childcare in Chapter 11 – section 318 (workplace nurseries) and sections 318A to 318AA as long as the conditions in sections 318B to 318D were met;
- The exemption for cycles and cyclist’s safety equipment in section 244;
- The new exemption announced at Budget 2016 for employer-provided pension advice arising from the recommendations of the Financial Advice Market Review (FAMR) will also be excluded from this measure. The exemption will be implemented from 6 April 2017 through secondary legislation under s210 ITEPA (power to exempt minor benefits).

**Question 6:** Do you consider that the approach proposed for legislation would work as intended?

**Question 7:** Are there any consequences the government has not considered in proposing to legislate in this way?

## Implementation

3.16 The government’s intention is to proceed with these changes through legislation in Finance Bill 2017. This would be subject to technical consultation as part of the normal draft Finance Bill process.

3.17 It is the government’s intention that the legislation would take effect from 6 April 2017.

**Question 8:** Would this timeline present employers with difficulty, for example with updating payroll software?

**Question 9:** Are there any other changes that employers would need to make?

## Compliance

3.18 Following any change, employers would be required to report any BiKs provided through salary sacrifice to HMRC in the same way as other taxable BiKs that they already report. This could be through the P11D process or by voluntary payrolling. The BiKs would also need to be reported on form P11D (b) for Class 1A NICs.

3.19 HMRC would enforce compliance with any new rules as part of its ongoing employer compliance programme.

3.20 Employers can continue to seek clearances for salary sacrifice schemes from HMRC in the usual manner.

**Question 10:** Are there any other compliance considerations which HMRC should be aware of?

## Chapter 4: Summary of consultation questions

**Question 1:** Alongside annual leave, are there any other salary sacrifice arrangements that the government should be made aware of that do not strictly involve receipt of a benefit?

**Question 2:** What are the likely impacts on employers and employees of limiting the scope of BiKs that can obtain tax advantages when offered through salary sacrifice arrangements?

**Question 3:** Are these impacts different, or are there different considerations, for large/small businesses or particular business sectors?

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**Question 9:** Are there any other changes that employers would need to make?

**Question 10:** Are there any other compliance considerations which HMRC should be aware of?

## 5. The Consultation Process

This consultation is being conducted in line with the Tax Consultation Framework. There are 5 stages to tax policy development:

- Stage 1 Setting out objectives and identifying options.
- Stage 2 Determining the best option and developing a framework for implementation including detailed policy design.
- Stage 3 Drafting legislation to effect the proposed change.
- Stage 4 Implementing and monitoring the change.
- Stage 5 Reviewing and evaluating the change.

This consultation is taking place during stage 2 of the process. The purpose of the consultation is to seek views on the detailed policy design and a framework for implementation of a specific proposal, rather than to seek views on alternative proposals.

### How to respond

A summary of the questions in this consultation is included at chapter 4.

Please send written submissions addressing the questions and issues raised in this consultation paper before 19 October 2016, by e-mail to [employmentincome.policy@hmrc.gsi.gov.uk](mailto:employmentincome.policy@hmrc.gsi.gov.uk) or by post to:

Alex Raisen  
Employment Income Policy Team  
Room 1E/08  
100 Parliament Street  
London  
SW1A 2BQ

The consultation will run for 10 weeks from 10 August 2016.

Paper copies of this document or copies in Welsh and alternative formats (large print, audio and Braille) may be obtained free of charge from the above address. This document can also be accessed from [HMRC's GOV.UK pages](#). All responses will be acknowledged, but it will not be possible to give substantive replies to individual representations.

When responding please say if you are a business, individual or representative body. In the case of representative bodies please provide information on the number and nature of people you represent.

## Confidentiality

Information provided in response to this consultation, including personal information, may be published or disclosed in accordance with the access to information regimes. These are primarily the Freedom of Information Act 2000 (FOIA), the Data Protection Act 1998 (DPA) and the Environmental Information Regulations 2004.

If you want the information that you provide to be treated as confidential, please be aware that, under the FOIA, there is a statutory Code of Practice with which public authorities must comply and which deals with, amongst other things, obligations of confidence. In view of this it would be helpful if you could explain to us why you regard the information you have provided as confidential. If we receive a request for disclosure of the information we will take full account of your explanation, but we cannot give an assurance that confidentiality can be maintained in all circumstances. An automatic confidentiality disclaimer generated by your IT system will not, of itself, be regarded as binding on HM Revenue and Customs (HMRC).

HMRC will process your personal data in accordance with the DPA and in the majority of circumstances this will mean that your personal data will not be disclosed to third parties.

## Consultation Principles

This consultation is being run in accordance with the government's Consultation Principles. Some stakeholders who previously provided responses have been invited to discuss this consultation face to face.

The Consultation Principles are available on the Cabinet Office website:  
<http://www.cabinetoffice.gov.uk/resource-library/consultation-principles-guidance>

If you have any comments or complaints about the consultation process please contact:

John Pay, Consultation Coordinator, Budget Team, HM Revenue & Customs, 100 Parliament Street, London, SW1A 2BQ.

Email: [hmrc-consultation.co-ordinator@hmrc.gsi.gov.uk](mailto:hmrc-consultation.co-ordinator@hmrc.gsi.gov.uk)

**Please do not send responses to the consultation to this address.**