

Employee flexible benefits schemes - can everyone still benefit?

As the first green shoots of recovery tentatively push their way through the recent wasteland of recession, the thoughts of many an employer will gradually turn from simply cutting staff numbers, to the effective incentivisation and future retention of its remaining quality staff. There is no doubt that schemes which permit employees to select a package of remuneration and benefits which fits with their own lifestyle choices, (i.e. flexible benefits, aka salary sacrifice schemes) are extremely popular with staff. In most cases it is also possible for the employer to save money on the deal!

If this all sounds like a win-win situation, why doesn't everyone do it? Despite recent HMRC announcements intended to 'tighten up' the rules in certain areas, it is important to recognise that the general 'flex' principles remain sound. Therefore this article aims to assist any employer who wishes to consider introducing or enhancing employee flexible benefits. Its intention is to provide an overall perspective on the concept, a realistic analysis of the pros and cons, and a summary of the steps involved, in a flexible benefits project.

Early stages – understand your motivation?

It might sound obvious, but the first step in a 'flex' project is to understand and set out your objectives! Often this will be a combination of two factors; the very laudable objective of saving the company money, and the desire to improve job satisfaction, thereby incentivising and retaining staff. If cost savings are not imperative, then you will need to establish if there is a budget available for the project, or are you hoping that the project can be delivered on a broadly cost-neutral basis?

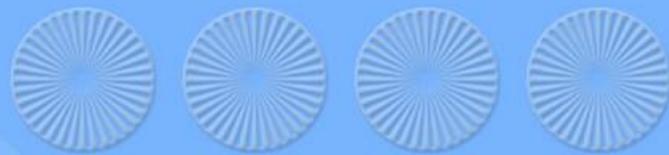
As a starting point, and for a relatively modest sum, you should be able to undertake an initial feasibility study. As well as potential savings, you will need to compile a realistic assessment of the likely implementation costs; there will undoubtedly be some, and the key is to ensure these are accurately estimated and managed. In addition to costs, you will be looking to identify if there are any other 'show stoppers'. We will look at each of these points separately:

Potential savings

In most cases savings will be achieved by an employee converting taxable salary into a benefit in kind that is either exempt, or enjoys a lower effective rate of tax or NIC. However this is not always the case; and some benefits merely provide additional 'lifestyle' choices for staff. Some of the more common benefits within a 'flex' scheme are as follows:

- Flexible pension contributions ; i.e. conversion of employee contributions to employer pension contributions
- Childcare vouchers and crèche facilities
- Bus/cycle to work schemes
- Medical or dental insurance
- Company cars; e.g. extending provision of low cost, low CO² rated cars, to employees who do not normally qualify
- Car Parking provided at or near one's normal workplace
- Holidays, i.e. ability to 'buy' or 'sell' extra days
- Mobile worker subsistence schemes
- Living accommodation
- Employment related training

As a minimum, you (as employer) would usually be looking to save secondary NIC on some of the converted pay. You would therefore want to maximise employee take up, thereby increasing savings.



In addition to employer NIC reductions, it is feasible that additional 'bulk purchase' savings may be generated by the employer (e.g. in relation to company cars, medical and dental insurance etc), however a careful analysis of costings must be undertaken first.

It is also possible that savings can be apportioned between employee and employer in such a way to create additional funding for the employer. However again, careful structuring, and employee buy in, is required.

Particular care is of course needed to ensure that each arrangement is not open to HMRC challenge. The detailed rules in each area are outside the scope of this article; however it is worth mentioning that the following employee benefit areas have recently been the subject of further HMRC or Treasury 'clarification':

- **Childcare vouchers:** In England the less formal 'approval' scheme has recently been withdrawn, and childcarers must now be registered with Ofsted in order for the childcare itself to qualify.

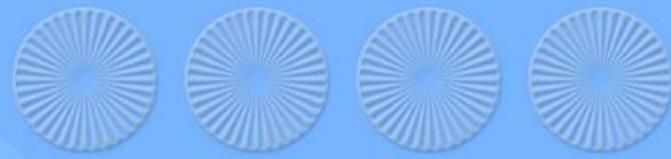
Another factor here is the intention to limit relief to the basic rate from 2011. HMRC has recently announced some fairly convoluted rules which would apply from April 2011, amongst other things requiring the employer to 'assess' how much tax relief the employee can get (unless the employee has already signed up before April 2011 in which case they may continue to enjoy any higher rate tax relief). This assessment would take account of income at the *start* of the tax year, and the proposals include some rather complex rules on what constitutes income for this purpose (e.g. it would include basic wages and taxable benefits in kind, but not bonuses, overtime, or salary sacrifices)?

Employers already running such schemes may want to ensure maximum staff take up prior to April 2011, i.e. to obtain protected relief status. However employers, who have not already introduced childcare vouchers, may have to weigh up more carefully the additional reporting requirements, before implementing this option.

A couple of additional points to bear in mind are that (i) as mentioned in the March 2010 Budget, the general requirement for childcare to be 'available to all' will not be breached if the only exclusions are for staff for whom salary sacrifices would take them below the National Minimum Wage level, and (ii) the existing exemption for workplace nurseries will continue in its present form after 2011 (i.e. unrestricted in amount of relief provided that the nursery itself is a qualifying one)

- **Bus travel to and from work:** HMRC recently stated its view that any provision must be limited to identified bus services rather than covering a local network of routes. This change of opinion effectively tightens the rules for new schemes (though limited continued relief may be available for schemes established before December 2009).
- **Cycle to work schemes:** Recent HMRC guidance reminds us that the relevant exemption only applies where the cycle is generally available to all staff, and care is needed if excluding certain categories of staff.
- **Canteen arrangements:** The government has confirmed its intention to legislate against situations where the canteen exemption is utilised in conjunction with a salary sacrifice; previously HMRC's opinion has been that salary sacrifice is a matter of employment law and does not therefore impact on the availability of particular exemptions. In practice we believe that limited numbers of employers have implemented such arrangements, and the move is unlikely to cause widespread concern.

If you require further clarification on any of these points, please contact Employment Tax for Business.



Potential costs

Having identified savings, you will also want to think about potential costs. These tend to fall into three categories:

- External consultancy costs; whilst the larger accountancy firms and specialist benefit consultancy houses may offer significant expertise, their costs should not be underestimated (six figure fees are common for larger projects).
- Systems costs; these may arise for instance if your existing payroll or payslips cannot fully cope with the proposed changes, or you require the new process to be delivered and available to staff electronically e.g. via your intranet.
- Internal staffing costs; resources will be needed in the initial roll-out (key stakeholders may be brought together from HR, finance, IT, and payroll departments, as well as staff side representatives). There will also be a certain amount of ongoing resource needed – e.g. to process 'in year' changes, staff queries, or to deal with any annual renewal option period.

Show stoppers

Finally within this initial feasibility phase you will want to think about whether there are any other 'show stoppers' i.e. fundamental reasons why any part of the scheme cannot work? As well as the previously mentioned tax/NIC, and systems issues, you may want to look at wider documentation such as employee contracts and pension scheme rules to ensure there is nothing contradictory here.

What happens next?

An employer who decides to proceed would then undertake the following processes:

Scheme design

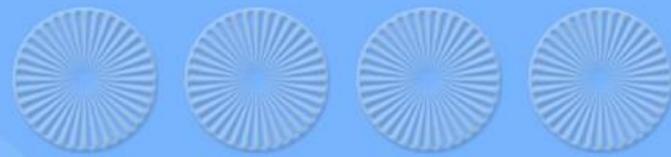
The detailed design process would include factors such as:

- Meetings between stakeholders to agree timescales and Key Performance Indicators i.e. to establish by what objective measures the scheme can be considered a success?
- Engaging with and assessing suitability of any external suppliers, e.g. childcare voucher providers.
- Deciding which employees to include or exclude e.g. with reference to relatively low paid or temporary staff (availability of some tax exemptions may depend on this).
- Determining how the scheme will actually be rolled out to staff, and whether it is feasible to automatically include employees for certain benefits (i.e. so that they would have to personally 'opt-out' if they wished to be excluded).
- How each salary sacrifice may apply to particular circumstances, e.g. new starters, leavers, maternity leave, long-term absences etc.
- Drafting of scheme documentation including wording of employee 'salary sacrifice' agreements and other employee literature.
- Payroll and payslip issues – dealing with the effect of salary sacrifice on other payroll elements such as shift allowances, overtime etc, & confirming design of revised payslips.
- Preparation of scheme rules as guidance to ensure ongoing effective operation.

Implementation

The actual implementation process would include:

- Finalising and issuing documentation to staff.
- Dealing with HMRC tax clearances; often the scheme will have to be implemented initially on a 'pilot' basis, as HMRC does not normally issue 'pre-transaction' clearances. This must be taken into account when setting timescales.



- Any new IT or payroll processes going live.
- Further communications with staff; which may involve publicity, literature, employee helplines, and presentations (to staff side, managers, HR staff etc). The intention would be to ensure smooth implementation and maximum take up.

Follow up reviews

It is usually advisable to undertake internal reviews post-implementation, i.e.:

- To check actual take-up statistics etc against Key Performance Indicators and to agree any potential improvements.
- Agreeing the terms of further employee literature, considering introduction of any new benefits etc, e.g. at annual renewal dates.
- Periodically assessing the 'success' of the scheme and ensuring that in practice it is working in line with the scheme rules, e.g. after an initial period and at the annual renewal program, checking that subsequent aspects (e.g. annual pay rises) are being calculated and demonstrated on payslips effectively, and that HMRC clearances remain effective etc.

Conclusion

Flexible benefits or salary sacrifice schemes do need very careful consideration before implementation. In our experience, it *is* possible to genuinely improve overall employee remuneration packages, whilst ensuring tax compliance and generating significant savings (or at the very least, for the employer to 'break even'). However an effective feasibility study must be conducted first.

Of course one way to significantly limit external fees is to engage with an adviser who can provide an experienced consultancy service, fully equivalent to the 'Big-4' accountants, but at a small fraction of the costs. If you wish to discuss this possibility, without obligation, please contact Employment Tax for Business.

Contacts

If you would like to comment on the contents of this document, or would like to discuss how we can assist with your needs, please contact:

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