

## Salary Sacrifice - The Basics

### What is Salary Sacrifice?

In a salary sacrifice arrangement an employee gives up the right to part of the cash remuneration due under their contract of employment. Usually the sacrifice is made in return for the employer's agreement to provide them with some form of non-cash benefit.

Although salary sacrifice is not a new idea, it has grown in popularity in recent years as more and more employers realise the tax and National Insurance savings they can generate through operating such a scheme. In fact, our research indicates that the majority of UK companies who have employee benefits (72.63 percent) have implemented salary sacrifice, which represents a huge growth since 2005.

Salary sacrifice schemes also prove popular with employees as it enables them to also make tax and National Insurance savings on valuable lifestyle benefits.

### Which benefits can operate in this way?

The principal benefits which can operate under a salary sacrifice arrangement are:

**Pension** - Although more popular (and simple) with defined contribution, it is also possible to turn a defined benefit scheme into a salary sacrifice scheme.

**Childcare vouchers** - Since 6th April 2006 the first £55 spent on the cost of providing the childcare vouchers to employees has been free from both income tax and National Insurance, provided the qualifying conditions below are met:

- That the childcare voucher scheme is generally available to all employees where the scheme operates;
- That employees can only use the childcare vouchers to pay for childcare that has been registered or approved.

**Cycle to work scheme** - Employees can save up to 50 percent on the retail price of a bicycle through a combination on savings on income tax, VAT and National Insurance contributions. The scheme is part of the Government's "Green Transport Plan" designed to encourage healthier travel and to reduce pollution and congestion. The cycles can also be used for leisure provided that they are mainly for travelling to and from work.

#### Note:

The March 2006 budget saw the announcement that tax exemptions for one of the most popular salary sacrifice benefits, the home computer initiative (HCI), was to be removed from 6th April 2006.

## Implementing a Salary Sacrifice scheme

Implementing a salary sacrifice scheme requires careful planning and thought. In particular, you should be aware of the following:

- It will be necessary to change an individual's terms and conditions of employment if they decide to take advantage of a salary sacrifice benefit;
- Salary sacrifice must not bring the employee's hourly wage below the minimum wage level. In addition, as it reduces an employee's cash pay, salary sacrifice can have an effect on earnings and related benefits such as the state pension, statutory maternity pay and statutory sick pay. The most significant consideration for state benefits will be if cash income falls below the lower earnings limit;
- Be aware of the additional administrative complexities should an employee undertake multiple sacrifices (for example an employee chooses childcare vouchers and to purchase a bicycle);
- Salary sacrifice may affect other salary driven benefits such as life assurance or disability insurance);
- The need to keep the Inland Revenue informed;
- It requires very careful communication to ensure that employees understand the implications;
- Due to the complexity of the calculations required, it is difficult and burdensome to run salary sacrifice on a paper basis.