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AVIVA

Salary Sacrifice and Optional Remuneration Arrangements – FAQ

Employee benefits funded via salary sacrifice have traditionally been a popular and tax efficient method of premium payment particularly in the flexible benefit market.

Our current standard method of premium collection for Group Income Protection (GIP), Excepted Group Life Policies (EGLPs) (including Spouse & Partner (SPLA)) and Group Critical Illness (GCI) is through a salary sacrifice arrangement.

For GIP and EGLPs, the tax advantage has previously been that the employee 'sacrifices' a portion of their salary in exchange for flex top up cover. For GCI the benefit is already treated as a P11D Benefit in Kind therefore the income tax position is broadly neutralised though there are still employee National Insurance savings to be gained.

All references to taxation are based on our understanding of current tax law and HM Revenue and Customs (HMRC) practice. Tax law and practices could change in the future.

What is OpRA?

Optional Remuneration Arrangements (OpRA) is the statutory definition for arrangements where employees have a choice between cash and a benefit – including salary sacrifice.

The OpRA legislation was introduced in Schedule 2 of the Finance Act 2017 as a means of making a number of popular salary sacrifice arrangements less attractive and HMRCs perceived impact these arrangements were having on the public purse.

What changes were introduced?

The main change was the removal of tax advantages previously enjoyed for certain non-cash benefits funded through OpRA. The OpRA legislation creates a charge to income tax and employer contributions (class 1A National Insurance) on the higher of:

- the amount of cash foregone (the amount of salary sacrificed); or
- the modified cash equivalent of the benefit.

In broad terms, this means that many benefits provided tax free outside of an OpRA are taxable within an OpRA.

Are there any exemptions?

Specific products and services that broadly support Government initiatives were excluded from the legislation and will not be affected even if provided via an OpRA:

- Pension saving and Group Life Registered products under registered and qualifying overseas plans (including related pension advice);
- Tax exempt childcare (including qualifying nursery provision and childcare vouchers);
- Qualifying Cycle-to-Work schemes;
- Counselling and other outplacement services;
- Retraining costs;
- Intangible benefits such as the purchase of additional annual leave;

and

- Ultra-low emission company cars (with CO_2 emissions less than or equal to 75 g/km).

How has this affected Group Protection products?

EGLPs and GIP are included in the scope of the legislation. This means that if the employee has foregone salary to secure those benefits, then a benefit in kind will be triggered (normally equal to the value of the salary foregone).

Group Life under a registered pension scheme remains outside the scope of OpRA. Similarly, there is no change to GCI as premiums were already subject to a benefit in kind charge prior to the OpRA legislation (assuming the amount of salary sacrificed was equal to the value of the benefit in kind).

What changes took place for GIP and EGLP?

HMRC states that both products will be subject to a benefit in kind charge on the greater of the amount of salary foregone or cash benefit equivalent. Additionally, Employer National Insurance contributions (NICs) will be payable on the full pre-sacrificed salary though employees will still benefit from paying reduced NICs as OpRA does not extend to employee NIC.

GIP benefit payments are subject to income tax aren't they?

HMRC initially argued that the OpRA legislation potentially gave rise to double taxation, where both the premium and benefit is subject to income tax. Aviva, in conjunction with the Association of British Insurers (ABI), convinced HMRC that this was not correct.

On 15 October 2019, HMRC revised its view and considered that, to the extent that GIP cover is taxable under OpRA, this is effectively the same as the premium being paid from the employee's net pay, and accordingly the proportionate benefit should be tax free. This situation arises when the premiums are partly taxed under OpRA and partly not taxed. The portion of the GIP benefit payments associated with the taxed premiums becomes fully taxable and is subject to NICs. The proportion of the GIP benefit payments linked to the untaxed premiums are not taxable.

On 1 December 2022, HMRC reversed their guidance and asserted their 15 October 2019 interpretation of OpRA legislation was in fact incorrect. They now conclude that any enhanced OpRA premium should **not** be regarded as an employee contribution. Therefore, an element of double taxation will arise where employees enhance their GIP cover by making an OpRA contribution and if they receive claim payments through their employer.

Aviva are disappointed with this outcome and strongly believe that where an employee enhances their cover as part of OpRA, it should not form part of OpRA at all as any claim payments are made to the employer and paid to the employee as earnings through payroll and will be subject to all normal deductions through the PAYE system.

We do not, of course, advocate that customers willingly ignore HMRC's stated current position.

What action should an employer take?

HMRC are allowing a transitional period for employers who have relied on 15 October 2019 guidance.

The HMRC phasing approach is as follows:

- HMRC will not be seeking to reclaim any tax which was not paid from 15 October 2019 to 31 December 2023, provided that the employer can provide evidence that they followed 15 October 2019 guidance. This means that any claim payments for the period 15 October 2019 to 31 December 2023, where the employee enhanced their cover through OpRA, the OpRA contribution will be treated as an employee contribution (and the salary foregone taxed as a benefit in kind) and the corresponding benefits will not be subject to normal deductions through the PAYE system
- Any claim payments from 1 January 2024, where the employee enhanced their cover through OpRA, will no longer be treated as arising from an employee contribution and claim payments will be subject to all normal deductions through the PAYE system.

This is a complex issue, and we recommend that employers seek advice from their Financial Adviser to review their GIP cover provided under OpRA rules. They will be able to provide guidance around what current and future claims are impacted, what communications are needed to employees and ensuring that any employee benefit platform is correctly configured for payroll reporting.

Does this mean that GIP flexible benefit schemes are no longer suitable?

There are many benefits to employees of obtaining additional cover under a flexible benefit GIP arrangement. Aviva maintains the view that, despite the taxation issues surrounding OpRA, an employee being able to enhance their personal level of cover above the core employer funded element can still provide significant value. Each employee's circumstances will be different, but obtaining cover through the workplace provides:

- An ease of application through an employer's chosen flexible benefits platform
- A selection of benefits suited to their individual needs and lifestyle
- In many cases, their cover is not subject to medical underwriting when their benefit is below the free cover level (benefits above the free cover level will be subject to an application and underwriting)
- Ability to flex up or down at policy enrolment dates or following an agreed policy lifestyle event
- Access to a wide range of wellbeing services
- Access to expert early intervention and rehabilitation services to prevent absence occurring or help with a return to work.

What happens where employer funded cover can be exchanged for cash under an OpRA?

If an employee can reduce the level of their employer funded cover in exchange for a cash benefit, the amount of the cash equivalent will be taxable. For example, where an employee reduces core GIP cover from 50% to 35%, with the difference taken as cash. The benefit in kind charge applies on the full employer funded level of cover (in this example, the full employer funded level of cover provided by the employer is 50%) that can be flexed for cash, regardless of whether the employee exercises the option fully, partially or not at all.

What happens where employer funded cover is exchanged for another benefit within a flexible benefit arrangement?

If an employee can reduce the level of their employer funded cover and can only use the cash equivalent to purchase another benefit within the arrangement, then the tax position will be determined by the type of benefit purchased. For example, an employee reduces core GIP cover from 50% to 35% and increases Registered GL from 2 times to 4 times salary no benefit in kind charge will apply.

How do trivial benefits work alongside OpRA?

Trivial benefits are those offered by an employer which are voluntary, irregular and non-contractual. They are not treated as a benefit in kind as long as they come to a value of £50 or less per annum for each employee. This is not intended to include items that are either in the nature of a reward or are contractual. Where benefits in kind are provided as part of a salary sacrifice arrangement they are likely to be contractual and therefore not regarded as "trivial".

Does the OpRA legislation change the position for employees on lower earnings to be able to access flexible benefits?

No, the position remains unchanged. After an employee's salary has been adjusted to reflect the benefit purchased, their pay in the pay period must still be higher than the National Minimum Wage to be eligible to join the scheme.

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