

**Department for Business, Energy and Industrial Strategy  
National Minimum Wage Consultation on salaried workers and salary sacrifice  
Response from the Low Incomes Tax Reform Group (LITRG)**

**1 Executive Summary**

- 1.1 As a group of tax specialists with interest and insight into the pay and tax issues facing the low-paid, we welcome the opportunity to respond to this consultation.
- 1.2 Our response largely focuses on the part of the consultation looking at salary sacrifice, given the interactions that exist with a worker's income tax and National Insurance contributions (NIC) position. However, we also make some general comments on the other aspects of the consultation.
- 1.3 We do not have extensive enough experience of the salaried workers rules to know for sure whether any of the proposals would cause any detriment to workers. We recommend that any changes to the legislation taken forward as a result of this consultation are published for consultation, as we are concerned that there might be unintended consequences.
- 1.4 The salaried worker rules are complex and if there is not to be a wholesale review and simplification of them, we recommend that guidance for employers is improved as many may otherwise struggle to comply.
- 1.5 Salary sacrifice schemes are mainly used to take advantage of the beneficial tax and NIC rules that exist where employers provide benefits. Salary sacrifice schemes can therefore be very helpful to employees as they can often save them income tax and/or NIC. However,

currently, you cannot salary sacrifice below the National Minimum Wage (NMW) and as the NMW rises,<sup>1</sup> more and more people are not able to benefit.

- 1.6 Part of the rationale behind the NMW/salary sacrifice restriction is that lower paid workers are at more risk of having their salary pushed below the Lower Earnings Limit (LEL) – that is, the level at which you start accruing entitlement to state benefits under the social security system. However, we think this risk is largely overstated.
- 1.7 In any case, we are not convinced that some of the arrangements that seem to have triggered this consultation (e.g. Iceland’s Christmas Club<sup>2</sup>) and so on, are actually salary sacrifice schemes. We think that workers are just having deductions made out of their net salary. In which case, there is even less likelihood of ‘harm’ as their gross salary is untouched.
- 1.8 Ideally, the NMW Regulations would be rethought to allow those on the minimum wage to participate in salary sacrifice arrangements (as well as to enter into benign arrangements like Christmas Clubs).
- 1.9 In terms of other NMW rules that penalise employers without protecting workers from detriment, the main one that springs to mind is around staff uniforms. If a worker has to pay for an item of ‘everyday’ unbranded clothing to wear as part of a uniform, such as a pair of black trousers, black shoes or a white shirt, the cost incurred must be deducted from their pay to establish whether at least the minimum wage is being paid. Employers seem to get this wrong again and again, somewhat understandably in our view.
- 1.10 More generally, it could be said that HM Revenue & Customs’ (HMRC) approach to compliance and enforcement of the NMW can penalise employers excessively, when compared to the detriment suffered by a worker.
- 1.11 It should be remembered that the NMW Regulations are complex and sometimes difficult for employers to apply. We are not convinced that naming and shaming an employer who has made an administrative error or technical failure, resulting in a small underpayment to workers is the appropriate or correct response.
- 1.12 Supporting employers who want to be compliant so that such problems are prevented in the first place, is a better idea. This would free up resources to deal with engagers at the other (deliberately non-compliant) end of the spectrum, which is where the potential for the most severe and harmful worker detriment must lie.

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<sup>1</sup> <https://www.gov.uk/national-minimum-wage-rates>

<sup>2</sup> <http://about.iceland.co.uk/2018/05/17/hmrCs-iceland-probe-shows-warped-priorities/>

## **2 About us**

- 2.1 The LITRG is an initiative of the Chartered Institute of Taxation (CIOT) to give a voice to the unrepresented. Since 1998 LITRG has been working to improve the policy and processes of the tax, tax credits and associated welfare systems for the benefit of those on low incomes. Everything we do is aimed at improving the tax and benefits experience of low income workers, pensioners, migrants, students, disabled people and carers.
- 2.2 LITRG works extensively with HMRC and other government departments, commenting on proposals and putting forward our own ideas for improving the system. Too often the tax and related welfare laws and administrative systems are not designed with the low-income user in mind and this often makes life difficult for those we try to help.
- 2.3 The CIOT is a charity and the leading professional body in the United Kingdom concerned solely with taxation. The CIOT's primary purpose is to promote education and study of the administration and practice of taxation. One of the key aims is to achieve a better, more efficient, tax system for all affected by it – taxpayers, advisers and the authorities.

## **3 Salaried workers (Questions 1 to 8)**

- 3.1 We make some general comments in relation to these consultation questions.
- 3.2 ***The inclusion of additional payment cycles (Questions 1 to 5)***
- 3.2.1 With the caveat that we do not have extensive experience of the salaried workers rules, we cannot see that amending the NMW Regulations to include additional payment cycles and fixing the definition of the calculation year for employers would cause any detriment to workers.
- 3.3 ***The calculation year (Questions 6 & 7)***
- 3.3.1 We would suggest that aligning the calculation year with the tax year would be sensible, as there is generally a peak of payroll related activity at this time anyway. We trust any changes will be communicated with employers and that good, clear guidance will be made available so that they understand how to apply the rules in practice. Guidance should cover commonly encountered scenarios, such as what happens in cases where an employee starts just before the end of a calculation year.
- 3.4 ***Inclusion of overtime and pay premia (Question 8)***
- 3.4.1 We are concerned that the inclusion of overtime and pay premia in the definition of pay for basic hours could be detrimental. Without seeing the proposed changes in legislation, it is difficult to comment, but it strikes us that this could open up the possibility of employers using pay premia to disguise an otherwise lower pay rate. Could this not then cause distortive hiring practices on the part of some engagers, as between salaried workers and time workers, given time workers will not have pay premia counted as part of their minimum

wage pay?<sup>1</sup> We recommend that any such proposed change to the legislation is itself published for consultation.

### 3.5 ***Further comments relating to salaried workers***

3.5.1 We see that the consultation document notes on page 5 that there has been feedback from businesses that the existing rules are complex. We agree that the rules are indeed complex and this seems to be backed up by the fact that the Low Pay Commission recently identified salaried workers as being at high risk of underpayment.<sup>2</sup> Ordinary employers, particularly small and micro employers without specialist HR/payroll support, are likely to struggle to understand them.

3.5.2 There are two possible solutions to this: either the rules are too complicated and a wholesale review is required (with a view to simplification); or the associated information and guidance requires significant improvement, so that people can really understand them. As the former does not seem to be an option at present, with this consultation instead proposing to adjust the existing rules, improvements to guidance are therefore essential.<sup>3</sup>

## 4 **Salary sacrifice**

4.1 ***Question 9 – Do you have any evidence that the salary sacrifice offer has been withdrawn or restricted in the last 12 months as a result of National Minimum Wage requirements?***

4.2 To start with, we would like to clarify what we understand by the term salary sacrifice. Under a salary sacrifice arrangement, an employee is able to swap cash salary for non-cash benefits.<sup>4</sup> The idea is that because no income tax and NIC is payable on the amount of salary that is swapped for the non-cash benefit, they can be in a better position overall than if they merely purchased the benefit from their net salary independently. (We include employer pension contributions in the general term ‘non-cash’ benefits, as although these are ‘cash’

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<sup>1</sup> Regulation 10(j) National Minimum Wage Regulations 2015:  
<https://www.legislation.gov.uk/ukxi/2015/621/regulation/10/made>

<sup>2</sup> <https://www.gov.uk/government/news/low-pay-commission-report-on-non-compliance-with-the-minimum-wage>

<sup>3</sup> We give a specific example of the current poor standard of guidance on the salaried worker rules in our response to the Director of Labour Market’s 2019/20 call for evidence:  
<https://www.litrg.org.uk/latest-news/submissions/180926-call-evidence-uk-labour-market-enforcement-strategy-201920>

<sup>4</sup> Salary sacrifice is a contractual arrangement and the ‘sacrifice’ is achieved by varying the employee’s terms and conditions of employment relating to pay.

payments, they are made to a pension plan with a view to the worker obtaining a deferred benefit from them – i.e. they are not of immediate ‘cash’ value.)

- 4.3 Salary sacrifice can be particularly efficient where the non-cash benefit is exempt from both income tax and NIC. Even if the non-cash benefit is not exempt from income tax, the employee will normally save Class 1 NIC. This is because on most benefits you do not pay any Class 1 NIC (although the employer pays Class 1A NIC).
- 4.4 However, it is important to note that since 6 April 2017 the ‘optional remuneration arrangements’ rules only allow tax and/or NIC savings in respect of certain approved arrangements, including pension saving, childcare vouchers (subject to certain limitations) and the cycle to work scheme.<sup>1</sup>
- 4.5 We do not have any actual evidence that the salary sacrifice offer has been withdrawn or restricted in the last 12 months as a result of NMW requirements, although we assume that this will be happening on a large scale. This is because as the minimum wage encompasses more and more workers,<sup>2</sup> fewer and fewer of them can use salary sacrifice – because the rules essentially mean that a salary sacrifice arrangement cannot reduce an employee’s cash earnings below the appropriate minimum wage rate.<sup>3</sup>
- 4.6 There are unexpected consequences for those slightly higher up the income ladder too, because an increase in the minimum wage rate may affect their ability to sacrifice salary for things like childcare vouchers.
- 4.7 For example: Neena, 38, works as a cleaner. She generally works around 35 hours a week at £9.50 an hour. At the moment she can give up £55 of her £332.50 weekly pay packet and get childcare vouchers instead (bringing her cash pay down to £277.50 but still above the minimum wage rate of £7.83 per hour) and saving her tax of £11 and NIC of £6.60, a total of £17.60 each week.<sup>4</sup>
- 4.8 When the minimum wage rate for her circumstances goes up to £8.21 in April 2019, Neena would only be able to sacrifice around £45 of her pay for childcare vouchers, saving her £14.40 (£9 in tax and £5.40 in NIC). We do not think that it can be assumed that employers

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<sup>1</sup> FA 2017, section 7 and Schedule 2, see also: <https://www.gov.uk/guidance/salary-sacrifice-and-the-effects-on-payee>

<sup>2</sup> See ‘Coverage’ – page 57 onwards: [https://assets.publishing.service.gov.uk/government/uploads/system/uploads/attachment\\_data/file/759271/National\\_Minimum\\_Wage\\_-\\_Low\\_Pay\\_Commission\\_2018\\_Report.pdf](https://assets.publishing.service.gov.uk/government/uploads/system/uploads/attachment_data/file/759271/National_Minimum_Wage_-_Low_Pay_Commission_2018_Report.pdf)

<sup>3</sup> Benefits in kind (except accommodation) cannot count as part a worker’s pay under Regulation 10(f) National Minimum Wage Regulations 2015: <https://www.legislation.gov.uk/uksi/2015/621/regulation/10/made>

<sup>4</sup> Neena is an existing claimant of childcare vouchers. They closed to new recipients from October 2018.

will keep the pay differential for people like Neena, who earn slightly over the minimum wage rate, when the minimum wage rates are uplifted.

- 4.9 **Question 10 – What do you regard as the main reasons that workers opt in to salary sacrifice schemes?**
- 4.10 We think that income tax and NIC efficiency will be one aspect – however as stated in para 4.4, the government has recently limited the range of benefits that attract income tax and/or NIC advantages when provided as part of salary sacrifice arrangements.
- 4.11 Saying that, we question whether the arrangements that seem to have triggered this consultation (e.g. the issues with Iceland’s Christmas Club, widely reported in the press) are true salary sacrifice schemes. We think employees in such schemes are probably making a regular payment via a deduction from their *net* (after tax and NIC) pay, rather than contractually reducing their salary. They then receive a lump sum, which comprises the total amount that they had paid in over the year to spend how they wish. Therefore these types of schemes have no effect whatsoever on the gross pay of the workers and are just voluntary savings schemes (in fact, they seem quite similar to the sidecar savings scheme that NEST are currently trialling).<sup>1</sup>
- 4.12 Workers may opt into things like Christmas Clubs because it helps them save, or because it gives them access to the employer’s goods and services at a discounted price. In the current economic climate, such benefits will be very welcome in terms of helping workers’ pay go a little further each month.
- 4.13 **Question 11 – What, if any, risks to workers’ pay do you think are presented by salary sacrifice schemes? (please use examples if you can)**
- 4.14 Salary sacrifice arrangements involve an employee altering their work contract to give up a portion of their earnings. This may present risks such as affecting the ability to borrow money; and future calculations of pensions, redundancy pay, statutory maternity pay, paternity pay, and shared parental pay. However, these risks can be managed by an employer making sure a worker fully understands the implications of the scheme.
- 4.15 One of the main concerns about allowing the lowest earners to sacrifice salary has been the risk of their pay dropping below the point at which entitlement to contributory benefits is triggered (the LEL). In 2018/19, this is £116 per week or £502 per month. In 2019/20, it will be £118 per week or £512 per month.
- 4.16 In practice, this is becoming less and less likely to occur, given the fact that the minimum wage rates are rising much faster the LEL.<sup>2</sup> For example, any person, aged 25 or over, working just 16 hours a week on the minimum wage of £7.83 (in 2018/19) would still earn

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<sup>1</sup> <http://www.nestinsight.org.uk/nest-insight-launches-sidecar-trial/>

<sup>2</sup> The LEL has been £113 (2017/18), £116 (2018/19) and is going up to £118 in 2019/20. The National Living Wage has correspondingly been £7.50, £7.83 and is going up to £8.21 in 2019/20.

£125.28.<sup>1</sup> Even if earnings did drop below the LEL, National Insurance credits might be available to effectively restore entitlement – for example, National Insurance credits are given to claimants of child benefit for a child under 12.<sup>2</sup> If credits were not available then there still might not be a significant problem depending on how many qualifying years the person has already accrued and their future potential to make up any gaps.

- 4.17 Taken together with the fact that salary sacrifice can only be used to gain a tax/NIC advantage in a limited number of circumstances now anyway (as a result of the HMRC restrictions set out in para 4.4), this means that we think the NMW Regulations should be rethought to allow those on the minimum wage to participate in these arrangements.<sup>3</sup> In our opinion, many lower earners (possibly female<sup>4</sup>) would be able to afford to salary sacrifice, taking into consideration their overall household income, if they had the opportunity to do so.
- 4.18 With the correct information about whether and how a reduction in their pay through a salary sacrifice arrangement might affect their entitlement to benefits and so on, employees should be able to make their own sensible decision. Saying that, there would be nothing to stop the government building in a safeguard to stop salary sacrifice pushing an employee's salary below the LEL to ensure their contributions record remain protected.<sup>5</sup>
- 4.19 In summary, we think the 'risks' to the low-paid of using salary sacrifice are largely overstated. This is even more so for the Christmas Club type schemes, if they are not actually true salary sacrifice schemes but are simply deductions from net pay. The only real downside to these schemes for the employee is that their overall pay is lower during the savings period. But our understanding is that they opt into it voluntarily, can opt out of it at any time and the money is held on a bare trust by the employer<sup>6</sup> until they draw it out – it is hard to see how it is exploitative.
- 4.20 Nevertheless, we understand that HMRC's view is that such deductions from pay reduce the amount the worker is taken to have received under Regulation 12 of the National Minimum

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<sup>1</sup> A 21 to 24 year old person on the £7.38 rate per hour, would also meet the LEL at 16 hours a week.

<sup>2</sup> <https://www.gov.uk/national-insurance-credits>

<sup>3</sup> This could be effected by allowing pay sacrificed for things like pension saving or childcare vouchers to still count as pay for minimum wage purposes.

<sup>4</sup> Where, for example, they are primary carer for a child or children.

<sup>5</sup> Or at least placing an obligation on the employer to advise the employee where their earnings will move to below the LEL by virtue of a salary sacrifice arrangement and what the consequences of this are. (This could even include obtaining something signed by the employee saying 'I confirm I understand'.)

<sup>6</sup> <http://about.iceland.co.uk/2018/05/17/hmrca-iceland-probe-shows-warped-priorities/>

Wage Regulations 2015<sup>1</sup> because they are ‘for the employers’ own use and benefit’ (and they do not necessarily then fall within the limited exemption that exists for deductions for goods and services purchased from the employer).

- 4.21 In terms of the *Iceland* case, we understand that they intend to argue that the deduction should not be defined as for Iceland’s own use and benefit and therefore falls outside of Regulation 12. It would however, save considerable effort all round if the NMW Regulations were altered to expressly allow for such arrangements.

## **5 Compliance – Question 12: Are there any other National Minimum Wage rules which penalise employers without protecting workers from detriment?**

- 5.1 In terms of other NMW rules that penalise employers without protecting workers from detriment, the main one that springs to mind is around staff uniforms. If a worker has to pay for an item of ‘everyday’, unbranded clothing to wear as part of a ‘required’ uniform, such as a pair of black trousers, black shoes or a white t-shirt, the cost incurred must be deducted from their pay to establish whether at least the minimum wage is being paid. Employers seem to get this wrong again and again, somewhat understandably in our view.
- 5.2 It is probably counter-intuitive to employers that they need to essentially reimburse staff for such standard attire, which may well be worn outside the workplace and which the worker may have bought anyway for their own benefit. What if the worker already had such items at home and did not have to purchase anything new?
- 5.3 In addition, the legislation does not set a limit on the amount of the expenditure. This seems to create an unfair situation where the more the worker incurs on ‘uniform’ items, the more the employer has to reimburse in order to be compliant.<sup>2</sup> And what if the worker is casual or only ends up working for a few shifts? This could leave the employer seriously out of pocket.
- 5.4 For those employers who understand the rules and happily reimburse their workers, there is also a practical issue: unless the reimbursement takes place inside the exact pay reference period (or the following one<sup>3</sup>), the worker will still be underpaid. What if a weekly paid worker forgets to bring in the receipt for their purchase?
- 5.5 The rules are quite obscure and, in our view, it is not surprising that employers can get caught out. In fact, tax law and minimum wage rules diverge somewhat on this issue, which will almost certainly be adding to employer confusion. Under tax law, the rules are stricter –

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<sup>1</sup> <https://www.legislation.gov.uk/uksi/2015/621/regulation/12/made>

<sup>2</sup> In practice, we understand that to avoid compliance and enforcement action, employers are only required to have reimbursed a ‘reasonable’ cost of the buying such clothing – but what is reasonable and how many employers understand this?

<sup>3</sup> See Regulation 9(b): <https://www.legislation.gov.uk/uksi/2015/621/regulation/9/made>



disallowing a deduction for tax purposes on such inconspicuous clothing. A deduction can only be permitted for clothing that is recognisably a uniform or part of a uniform.<sup>1</sup>

- 5.6 We wonder whether, to make the situation a bit more balanced for both the employer and employee, the NMW position should be brought closer to the tax law approach. Perhaps items of clothing could be recognized for minimum wage purposes, if they are branded or if the requirements to buy non-branded items are specific and excessive. At the very least, we think more could be done to highlight and clarify such points of divergence between tax law and minimum wage law like this with employers.
- 5.7 More generally it could be said that HMRC's approach to compliance and enforcement of the NMW can penalise employers excessively compared to the detriment suffered by a worker.
- 5.8 It is stated in the consultation document that the NMW Regulations are in place to ensure fairness and to protect workers from excessively low pay. These are principles we wholeheartedly agree with.
- 5.9 However, it should be remembered that the NMW Regulations are complex and sometimes difficult for employers to apply (beyond the salaried worker rules). The burden of trying to understand the minimum wage rules in relation to things like sleep-ins, travel time and costs, equipment, tips, training, etc. can be disproportionate – certainly for small and micro employers – and it is not surprising to us that there can sometimes be administrative errors or technical failures.
- 5.10 The resulting underpayments are often small and, of themselves, probably do not cause significant worker detriment. We are therefore not convinced that naming and shaming<sup>2</sup> an employer who has made an innocent administrative error or technical failure, resulting in, say, an £154.48 underpayment across a workforce of 19 (meaning average arrears of £8.13 per worker<sup>3</sup>) is the appropriate or correct response.
- 5.11 Supporting employers who want to be compliant, so that problems are prevented in the first place, is a better idea. Currently there is an overall lack of guidance and assistance to help employers understand and comply with their responsibilities (and not just around salaried workers). We think that the challenges employers face are best illustrated by looking at this case study.
- 5.12 *A trustee of a homecare-providing charity has recently been in touch with us. He evidently takes the welfare of his staff seriously and, having read our website section on issues for paid*

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<sup>1</sup> <https://www.gov.uk/hmrc-internal-manuals/employment-income-manual/eim32475>

<sup>2</sup> For example, <https://www.gov.uk/government/news/record-22400-minimum-wage-workers-to-receive-millions-in-backpay>

<sup>3</sup> See entry 230 on July 2018's list: <https://www.gov.uk/government/news/record-22400-minimum-wage-workers-to-receive-millions-in-backpay>

*care workers, wanted to clarify the rules around ‘costs’ of travelling between clients (he was unaware that there was a minimum wage implication until he read our material – itself quite worrying).<sup>1</sup>*

- 5.13 *He first looked for some official guidance on the matter, however could not find any with sufficient clarity to reassure him as to what was required. (Note, neither the GOV.UK<sup>2</sup> nor the more detailed BEIS guidance<sup>3</sup> flags that unreimbursed travel expenses reduce pay for minimum wage purposes, let alone how to quantify them, for example, if using one’s own vehicle, is it just the cost of the fuel or can some account be taken of wear and tear or other running costs?)*
- 5.14 *He then rang ACAS who said that they did not think the minimum wage legislation covered travel expenses but that ‘HMRC “owns” NMW so you had better ask them’. The trustee then phoned HMRC who said, ‘we only deal with tax so here’s a number to call for minimum wage guidance’ ... the number was ACAS.*
- 5.15 On the basis that most employer non-compliance does not stem from deliberate and flagrant disregard for the law, but is rather the result of confusion or misunderstanding, we think more should be done to support employers who want to be compliant. This would free up resources to deal with engagers at the other (deliberately non-compliant) end of the spectrum, which is where the potential for the most severe and harmful worker detriment must lie.

LITRG

27 February 2019

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<sup>1</sup> The rules basically say that their pay must average out at or above the minimum wage, once the following are factored in: the time they spend in the client’s home; time spent travelling between their different clients during the day; and their associated out-of-pocket expenses.

<sup>2</sup> <https://www.gov.uk/national-minimum-wage/employers-and-the-minimum-wage>

<sup>3</sup> [https://assets.publishing.service.gov.uk/government/uploads/system/uploads/attachment\\_data/file/726432/calculating-minimum-wage-guidance-july-2018.pdf](https://assets.publishing.service.gov.uk/government/uploads/system/uploads/attachment_data/file/726432/calculating-minimum-wage-guidance-july-2018.pdf)