



EMPLOYMENT  
LAWYERS  
ASSOCIATION

P.O. BOX 353  
UXBRIDGE UB10 0UN  
TELEPHONE/FAX 01895 256972  
E-MAIL [ela@elaweb.org.uk](mailto:ela@elaweb.org.uk)  
WEBSITE [www.elaweb.org.uk](http://www.elaweb.org.uk)

## **HM Treasury Call for Evidence on Remuneration Practices**

### **Response from the Employment Lawyers Association**

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# **ELA RESPONSE TO HM TREASURY'S CALL FOR EVIDENCE ON REMUNERATION PRACTICES**

## **Introduction**

The Employment Lawyers Association ("ELA") is an unaffiliated and non-political group of specialists in the field of employment law and includes those who represent and advise both employers and employees. It is therefore not our role to comment on the political merits or otherwise of proposed legislation, rather we make observations from a legal standpoint.

ELA's Legislative and Policy Committee is made up of both Barristers and Solicitors who meet regularly for a number of purposes including to consider and respond to proposed new legislation.

A working group was set up by the Legislative and Policy Committee of ELA under the chairmanship of Stephen Ratcliffe to consider and comment on HM Treasury's Call for Evidence on Remuneration Practices. Our response is set out below. A full list of the members of the working group is listed at the end of this paper.

### **1. Do you agree with the definition and composition of remuneration set out above?**

Broadly, yes. There is of course no formal or universal definition and the specific practices will differ between companies. Some employers may view 'remuneration' in the narrower sense of cash or cash equivalent (e.g. salary, bonus, car allowance, pension contribution), excluding non-monetary benefits or other perks like medical insurance or share schemes.

### **2. Are there additional forms of remuneration that you consider are relevant to current practice?**

In the case of senior employees, employers sometimes enter into agreements for the payment of guaranteed termination payments, which effectively form part of the executive's overall remuneration "package".

### **3. Are there benefits in kind or other payments that should not be treated as remuneration for tax and/or National Insurance purposes?**

ELA considers that this category of payments would primarily consist of incidental expenses or costs incurred in connection with employment or the carrying out of duties. This could include, for example, company cars provided for business use only, the cost of required equipment and tools, required professional memberships, and travel and subsistence payments.

### **4. Where applicable could you provide evidence of typical remuneration practices for the categories set out below. Any data you can provide to illustrate the breakdown for your organisation would be welcome.**

#### Sectors

- Financial services

Remuneration is typically made up of salary, with a bonus potential based on individual and company/division performance, which is often significant. In addition, employees typically receive company pension payments (or an allowance in lieu), private medical insurance, holiday in excess of statutory minimum, and family-friendly leave at enhanced rates of pay.

On occasion, employees also receive share incentives or other long-term incentives, and this has become more prevalent following increased regulation of pay in the financial services sector.

- Manufacturing

Remuneration is typically made up of salary, some element of bonus (especially for more senior employees), shift allowances or premia for overtime or additional duties (e.g. first aider payments), company pension contributions, and enhanced holiday. There is often a distinction between the amounts paid to shop/manufacturing employees (where rates of pay and work or time-based allowances or premia are more common) versus managers or executives who may receive additional benefits or bonuses. Company cars or allowances for mobile or more senior employees are common. Site-based benefits also more common in this industry e.g. on site occupational health facility, canteen.

### Regions

Other than salary weighting (e.g. London weighting), we are unaware of significant variations as between regions.

### Types of Worker

Zero hours contract, temporary or contingent workers would tend to receive a more limited package of salary and benefits, though this can be subject to legal challenge in the event that part-time staff receive less than the pro-rata value of a full-time staff member's package.

### Types of Employer

Larger employers tend to provide a broader range of non-cash benefits such as private medical insurance, canteens, gyms, childcare vouchers, cycle to work schemes, workplace counselling or healthcare, and concierge services. Multinational employers will often seek to provide a standardised remuneration package, offering a similar range or level of benefits globally, although allowing for local variations as a matter of law or practice.

5. **What are the most significant changes you have seen to remuneration practices over recent times? Have you seen certain forms of remuneration become more or less popular over time? What has driven these changes: in particular what role has the tax system played?**

ELA has seen an increase in the range of payments and benefits provided. A wider range of benefits has been combined with a move away from purely salary-based packages, to provide employees with a package of benefits that is intended to be competitive. In particular, start-up companies are more likely to offer a more flexible package of benefits, such as homeworking arrangements and flexible hours, in return for a reduced salary. These arrangements, though not strictly "remuneration", may be considered to be part of the overall package used to entice employees into employment and to retain existing staff.

ELA has also seen greater use of individual bonus and share or incentive based schemes, particularly in the financial services sector, where restrictions on cash remuneration (in particular bonuses) have caused employers to consider alternative means of attracting and retaining staff. The tax system, and in particular the tax advantageous nature of some share-based schemes is a significant driving force behind companies' decisions to adopt particular payments or benefits.

Similarly, the tax and NIC advantages to both employee and employer have driven the widespread adoption of salary sacrifice arrangements, such as childcare vouchers and pension contributions. At

the same time, ELA members report a decrease in the use of company car schemes, primarily due to the burden of administration and additional tax cost.

**6. Which of the objectives set out above do employers consider are the most and least important when determining remuneration practices and how does this vary? Are there other objectives missing from this list?**

The objectives of attracting and retaining talent and managing cost are uppermost in employers' minds, in ELA's view. This naturally means that advantageous tax treatment of particular benefits encourages their adoption.

**7. What forms of remuneration do employers think fulfil each of these objectives and why? It would be helpful if you could outline specific forms of remuneration that are used most widely in each case.**

Salary, bonus and cash allowances remain the primary tools to recruit and retain talent. However, bonuses and share incentives are also commonly used for that purpose, particularly in the financial services sector. Bonuses and share incentives are also common means of rewarding performance, and incentivising employees to achieve targets. Long-term incentives in particular are also used effectively as a retention tool, as well as a means to share in the success of the business.

Family-friendly leave policies, childcare vouchers and flexible working arrangements are generally designed to promote wellbeing and to recruit and retain a diverse workforce. Medical insurance, gym membership, cycle to work schemes, and employee counselling services are most commonly used to promote health and wellbeing.

As noted above, tax-efficient benefits such as childcare vouchers or pension contributions made by salary sacrifice are commonly used to help manage costs.

**8. Why are plans involving employment-related securities used in remuneration packages?**

In ELA's experience, the combined benefits of tax efficiency of certain forms of employment-related securities, together with ensuring that employees are fully invested in the business, tend to drive employers to offer share-related benefits. In addition, since such schemes are often long-term, they can be a valuable means of retaining and motivating key talent.

The effectiveness of such schemes in incentivising performance depends largely on the terms on which they are awarded. Save As You Earn (SAYE) schemes which are open to all employees, for example, are less likely to motivate individual performance than share or option awards which are conditional on individual performance. However, such schemes are widespread, and tend to be regarded by employers as an effective way of motivating and retaining staff.

The beneficial tax treatment of certain types of schemes is a significant motivating factor, since absent such treatment employees would in some cases receive no benefit over buying shares on the open market. Tax efficiencies commonly drive an employer's choice of scheme, though this is not universally true, for example where global employers seek to implement schemes which are consistent across multiple jurisdictions.

**9. How far do individuals' preferences drive the packages on offer by employers? How does bargaining power vary according to an individual's status at the firm? What is the take up of different forms of remuneration?**

ELA's experience is that individual preference has only a limited impact on the packages on offer. Whilst employees may be able to negotiate elements of cash payments e.g. salary, the remainder of

the package tends to be set at a corporate level, with bespoke arrangements put in place for only the most senior of staff.

**10. How far are remuneration practices driven by these external factors, in particular what impact does the current tax treatment of different forms of remuneration have on remuneration packages? Are there other factors that are relevant here?**

Legal obligations are of course a significant factor, since employers are in ELA's experience keen to ensure that such obligations are complied with in full. Tax has a more limited impact, since the opportunities to avail of tax-efficient forms of remuneration are necessarily more limited. However, where such efficiencies are available (e.g. salary sacrifice arrangements), take-up is common, and there is a natural tipping point where the provision of such benefits becomes the norm within the relevant industry or business sector.

More generally, market practice, and the local and national job market are also important considerations, as is current and projected future economic conditions for the employer and the economy generally. For multinational employers, global or regional market and cultural factors also play a material role in attracting and retaining international or mobile workers.

Within unionised workforces, the trade union's bargaining power is of course a significant factor in pay setting. Such negotiations still typically focus on cash remuneration rather than on remuneration structures such as share plans and discretionary bonuses where the reward may be perceived to be less guaranteed. Increasingly, trade unions also focus on pension contributions, and on ensuring pay transparency and/or steps to address perceived equal pay issues, as additional negotiating points or trade-offs.

**11. How much flexibility is there in the packages offered by employers and at what stage in an individual's career are these more or less likely?**

It is ELA's experience that formal flexible remuneration structures, whereby employees may trade off certain benefits against each other or may receive cash payments instead, are relatively uncommon, and tend to be limited to larger employers. Such employers tend not to restrict such structures to staff at particular stages in their career, but rather offer such packages to all or a majority of the workforce.

However, ad hoc or individualised flexible remuneration structures are sometimes put in place for senior staff, in particular those approaching retirement, where there may for example be benefits in receiving additional cash allowances rather than pension payments which may put the employee over the lifetime allowance.

**12. What kinds of remuneration are usually offered flexibly or on a voluntary basis? How do these arrangements work in practice?**

In practice, employees are provided with a fixed allowance, which may be taken as cash in the form of salary or which may be used to pay for a variety of benefits such as private medical insurance, additional holiday, life assurance, childcare vouchers, or additional pension contributions. Such insurances are often available to employers at a rate far cheaper than would be available on the open market, thereby providing a potential incentive to take such benefits rather than the cash equivalent.

**13. Why are flexible or voluntary packages provided and what is the take up of these? How does this vary across the workforce?**

In ELA's experience, such packages are offered for a range of reasons similar to those noted in Question 6, including retention of employees, employee wellbeing, promoting diversity, tax efficiency, and cost savings. Take-up of benefits instead of cash varies considerably. Though some employers report a greater take-up of non-cash benefits the older the employee, this is by no means

universal, and lifestyle factors such as the employee's marital or family status appear to be as likely to motivate benefits choices.

14. **What forms of remuneration are commonly offered through salary sacrifice arrangements? Does the difference in valuation of benefits for tax purposes play a part in which ones are offered?**

In addition to childcare vouchers, pension contributions and cycle to work schemes, it is common to offer the ability to "purchase" additional holiday, additional insurance or, in some cases, benefits such as car club driving hours, via salary sacrifice arrangements.

15. **Why are these salary sacrifice arrangements in place; how far are tax and National Insurance considerations important? Where possible, please provide evidence to quantify this.**

Again, such arrangements are offered for a range of reasons similar to those noted in Question 6, of which tax efficiency is only one. Tax efficiency is commonly the primary driver behind employee take-up of benefits such as childcare vouchers and cycle to work schemes, since there is no other benefit to be gained from them. Similarly, it is a significant driver in employers choosing to make pension contributions via salary sacrifice, though often those benefits are shared with or entirely given over to employees via enhanced pension contributions, as a further form of incentivisation and good employee relations practice.

16. **Do you see a distinction between salary sacrifice arrangements and arrangements where benefits in kind that are automatically provided on top of salary are sacrificed for a cash alternative? How far and tax and National Insurance, as well as other factors, drivers for these arrangements?**

From the employee's perspective, there is little difference, since both provide a form of flexibility in the remuneration to be received. However, tax and national insurance benefits are a material factor in both an employee's decision as to whether to take up that flexibility, and an employer's decision as to whether to offer such options.

17. **How do you expect remuneration practices to change in the future? What are the contributing factors to this? Are there areas of the tax treatment of remuneration that the government should explore further?**

Though cash salary will remain the most significant factor in remuneration strategy, ELA anticipates a general trend towards greater flexibility, and the provision of additional lifestyle benefits. As with the increase in e.g. workplace canteens, on-site gyms and childcare, in recent years, employers will often be driven by the introduction of new benefits by their competitors in industry, and the wider cultural acceptability of, for example, homeworking and other flexible working arrangements, to constantly evolve their remuneration structures to remain competitive.

ELA considers that the Government should consider further amendments to the tax treatment of measures put in place to support modern flexible working practices, such as childcare support, and payment for the costs of maintaining a home office, for example. In addition, the Government may wish to consider incentivising employers to offer health and welfare benefits such as medical insurance and employee counselling services, which would appear to assist employees to maintain their attendance at work. Finally, beneficial tax treatment of share schemes is to be further encouraged, since employers often value the ability to provide favourable securities benefits to staff so as to encourage employee loyalty and buy-in to the commercial aims of the business.

**ELA Working Group**

Stephen Ratcliffe, Baker & McKenzie LLP – Chair

Bernadette Daley, Cummins Ltd. Law Department

Emma Dickinson

Kevin Gude, Wragge Lawrence Graham & Co

Gitali Melvin, Nuffield Health