OpRA – A review of the performance

Employment Tax | Tax voice



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Lee Knight provides an overview of the initial impact

The Optional Remuneration Arrangement ("OpRA") rules took effect from 6 April 2017 amid HMRC concerns about the increasing use of salary sacrifice and the perceived connected loss of tax and NIC receipts to the Exchequer.

Almost one year on, and despite the HMRC guidance issued on 20 March 2017, there are still ambiguities within the rules and misunderstandings about how and when the OpRA rules apply.

With the 2017/18 tax year about to end, and the 2017/18 P11D season almost upon us, it is vital that employers identify all arrangements provided under OpRA, and fully consider what the rules mean for them and their employees.

How do the OpRA rules apply?

The OpRA rules apply to:

- any arrangement where an employee or director gives up the right (including a future right) to an amount of earnings in return for a benefit. These are known as “Type A” arrangements; or
- any other arrangement under which an employee or director chooses to be provided with a benefit rather than an amount of earnings. These are known as “Type B” arrangements.

When do these rules apply?

The OpRA rules apply where an OpRA begins from 6 April 2017 or, where an existing arrangement that commenced before 6 April 2017 is modified, varied, or renewed after 6 April 2017.

For most arrangements that commenced before 6 April 2017 and which are still in place on 6 April 2018 (without being modified, varied or renewed between 6 April 2017 and 5 April 2018) the OpRA rules automatically apply from 6 April 2018.

If the pre 6 April 2017 benefit subject to the arrangement is a car with C02 emissions of more than 75gkm, or school fees, or living accommodation, the OpRA rules will not automatically apply until 6 April 2021 (provided the arrangement is not modified, varied or renewed before then).

Example

An employer provides employees with private medical insurance and income protection insurance under a flexible benefits scheme where employees sacrifice salary for benefits. Employees elect for these benefits annually between 1 January and 31 January.

The private medical and income protection insurance benefits are renewed on 31 January 2018 for all employees who have previously taken these benefits. As these

benefits are provided under an OpRA the OpRA rules apply from 31 January 2018, and the ‘higher of’ comparison must be undertaken to value the benefits reportable on the employees’ 2017/18 forms P11D.

Does this only affect salary sacrifice arrangements?

No, crucially the inclusion of Type B arrangements extends the reach of the OpRA rules beyond salary sacrifice arrangements.

Example

An employee is promoted and their employer offers them a choice between a car, and a cash car allowance of £400 per month. The employee chooses the car which is available to him on 6 September 2017. The car has a list price of £22,000 and an appropriate percentage of 20%.

The OpRA rules apply as the employee forgoes earnings of £400 per month in return for a company car. The value of the company car benefit in 2017/18 is the higher of the earnings foregone of £2,800 (i.e. monthly cash allowance £400 x 7 months) and the normal benefit value of £2,566 (i.e. (£22,000 x 20%) x 7/12 months).

The benefit in kind reportable on Form P11D and liable to tax and employer’s Class 1A NIC during 2017/18 is £2,800, not the amount of £2,566 determined under the company car benefit rules.

It is yet to be seen exactly how HMRC will enforce this part of the OpRA legislation.

Are all benefits provided under an OpRA caught?

No, “excluded” and “special case” benefits are outside the scope of the OpRA rules.

Excluded benefits are ringfenced benefits unaffected by the OpRA rules where the previous tax and NIC advantages can continue. These include (but are not limited to) payments by employers into registered pension schemes, childcare vouchers, cycles, and cars with C02 emissions of less than 75gkm. Special case benefits are those benefits where separate legislation already counters the use of OpRAs in conjunction with the use of that benefit (for example in relation to subsidised workplace meals).

The excluded benefit for payments by employers into registered pension schemes can also extend to employer provided life insurance policies, which only insure the lives of employees and directors, and which are registered group life schemes set up under pension legislation. Other employer provided employee insurance policies (such as excepted life and critical illness policies) are caught when provided under an OpRA.

Are benefits that are otherwise exempt from tax and NIC caught?

Any benefit which is provided under an OpRA, and which is not an “excluded” or “special case” benefit is caught by the OpRA rules. This applies even where the benefit is normally exempt from tax and NIC. In circumstances where the benefit is normally exempt, the value to be compared with the amount foregone is deemed to be nil.

Example

An employer provides employees with a single health assessment annually. This core benefit is not provided under an OpRA.

Under the employer’s flexible benefits scheme employees can, however, enhance their annual health assessment so that it covers a more comprehensive range of checks. Where the benefit is enhanced this increases the annual cost and this is funded by the employee through salary sacrifice.

Employee A has received the core annual health assessment for many years without enhancing the benefit, but on 31 January 2018, as the employer’s annual flexible benefits window closes, she elects for the enhanced annual health assessment option which increases the cost of her annual health assessment by £600. She sacrifices gross salary of £600 and the single annual health assessment takes place on 31 March 2018.

Before the 2017/18 tax year the annual health assessment for Employee A is an exempt benefit under Section 320B ITEPA 2003. The benefit arising during 2017/18 is, however, the greater of the amount of salary foregone (which is £600) and the taxable value of the benefit (deemed to be nil, as it is otherwise exempt under Section 320B ITEPA 2003). The value of the health assessment benefit to be

reported on the employee's 2017/18 P11D is £600. The employee will pay tax, and the employer will pay Class 1A NIC, on this amount.

This example highlights the need for employers to consider the impact of the OpRA rules and communicate this to employees as soon as possible. This employee has received this benefit for many years without paying tax on it and by enhancing it in this way she is triggering a benefit which she will be required to pay tax on. This tax will not be collected under PAYE during 2017/18 but will impact her tax code, and reduce her take home pay, from the 2018/19 tax year. This will all seem highly counter intuitive to the employee.

What happens where Approved Mileage Allowance Payments are made under an OpRA?

Where employees are provided with mileage allowance payments under an OpRA the mileage allowance payments exemption does not apply and the amount foregone by the employee is treated as taxable.

Example

An employer pays 25p per mile to employees when they use their own cars for business. No employees undertake more than 10,000 miles in a year. The employees can also sacrifice salary equal to 20p per business mile and the employer then tops up the mileage allowance payment to a total amount of 45p per mile. The amount foregone of 20p per mile is caught by OpRA and reportable on the employees' forms P11D.

It is not clear how the NIC should be dealt with in this situation. Section E (mileage allowance payments not taxed at source) of the draft 2017/18 P11D (published by HMRC at the date of this article) is not a Class 1A NIC box. Presumably the employer would therefore enter the 20p per mile for each employee in the Section M Class 1A NIC box.

Are OpRA calculations straightforward?

No not always. This is primarily because the amount of earnings given up is compared to a modified benefit where any amounts made good by the employee are ignored. However, amounts which are made good do then reduce the taxable

benefit which arises. This typically affects benefits where part of the benefit is provided under OpRA and the employee also contributes towards the cost of the benefit in another way.

Example

An employee is provided with living accommodation by their employer. The employer rents the property and pays a monthly rent to the landlord of £1,100 beginning on 10 April 2017. The employee enters into a salary sacrifice arrangement on 8 April 2017 where they sacrifice salary of £1,000 per month, and they also agree to make good a further £250 per month towards the cost of the accommodation which is deducted from their net monthly pay.

The benefit in kind arising for 2017/18 is the higher of the earnings foregone of £12,000 (i.e. £1,000 x 12 months) and the modified value of the benefit being £13,200 (the annual rent paid by the employer). No deduction is made in the comparison calculation for the additional amount made good by the employee in the year (which totals £3,000).

The living accommodation benefit arising during 2017/18 is however £10,200 (i.e. £13,200 less the amount made good by the employee of £3,000).

How does this affect company cars?

Company cars with C02 emissions of more than 75gkm and available for private use are within the scope of the rules when provided under an OpRA. The higher of comparison is the greater of:

- The modified cash equivalent of the benefit; and
- The amount foregone in relation to the provision of the company car benefit.

The modified cash equivalent is the cash equivalent under the company car benefit rules, but ignoring any capital contributions made by the employee and any required payments the employee makes for private use.

If the amount foregone by the employee is greater than the modified cash equivalent, then a deduction for any capital contribution is made from the resulting benefit. The deduction is given by multiplying the capital contribution (up to the £5,000 maximum) by the appropriate percentage of the company car. A deduction is

also given for the employee’s private use contribution.

Example

An employee is provided with a company car in the 2017/18 tax year in return for sacrificing £430 of salary per month (or £5,160 per year). The car has a list price of £25,000 and an appropriate percentage of 20%. The employee makes a capital contribution of £2,000.

The modified cash equivalent is £5,000 as the capital contribution is ignored. This is compared with the amount foregone of £5,160. The amount foregone of £5,160 is greater, so this amount is used in determining the company car benefit. The company car benefit for 2017/18 is £4,760 being £5,160 less £400 (i.e. the capital contribution of £2,000 x 20%).

The amount foregone may not always be this straightforward. Page two of HMRC’s Employer Bulletin 68 states, when referring to data which will be recorded on the form P46 (Car), that only amounts foregone in respect of the car are included in the higher of comparison. Amounts foregone for fuel, maintenance or servicing are ignored.

This has not been widely publicised by HMRC and causes ambiguities. For example, how does this work where there is a choice between a company car and a car allowance, and the employee chooses the car? Should the cash allowance foregone in the higher of comparison then be adjusted, on a just and reasonable basis, to reflect only the cost of the car and exclude the maintenance and servicing costs? If so, can this only be done where it is specifically stated that part of the allowance given up related to the car and part related to other costs? Or can this adjustment to the cash allowance foregone in the comparison calculation be made on a just and reasonable basis? HMRC have not published any firm guidance on this issue. In the absence of such guidance, unless official agreement is obtained from HMRC, this is likely to be an area which is open to HMRC challenge.

Where there is an OpRA in respect of a fuel for a company car, the OpRA legislation applies and the higher of comparison must be made when calculating the car fuel benefit for the tax year.

Example

An employee has a company car with an appropriate percentage of 17% which is available for the entire 2017/18 tax year. The car is not provided under an OpRA. The employee enters into a salary sacrifice agreement where they sacrifice £350 per month in return for all car fuel being paid by the employer. The cash equivalent of the fuel benefit is £3,842 (the fixed amount of £22,600 multiplied by the appropriate percentage of 17%). The salary foregone of £4,200 (£350 x 12) is higher and so the value of the car fuel benefit during 2017/18 is £4,200.

What does this mean for employers?

Employers who have registered to payroll benefits provided under OpRAs during 2017/18 should have already considered how and when the OpRA rules apply to those benefits. The correct value of the OpRA benefit, ascertained in the 'higher of' comparison, should have already been taxed via the payroll where the OpRA rules are triggered. Where flexible benefits are payrolled, this might be, for example, from when the flexible benefits scheme renews during the 2017/18 tax year. Many employers' flexible benefits schemes will have renewed in January 2018.

There are subtle changes to the draft 2017/18 P11D published by HMRC to reflect the OpRA rules but these changes are barely noticeable and are likely to be missed by many employers. Employers who have not registered to payroll benefits provided under OpRAs should identify which benefits are affected, from when, and how this will change the way they report benefits on their 2017/18 P11Ds. Getting this wrong could have big consequences and lead to unexpected liabilities and HMRC penalties. It could be that benefits are reported on P11Ds for the first time, and/or that the taxable value of benefits previously reported increases. Where this results in increased tax liabilities for employees this should be communicated to employees as soon as possible. Increased employer NIC liabilities should also be reflected in budgets.

Under the OpRA rules, there is an increasing need for employers to consider benefit reporting on an employee by employee basis from 2017/18. The requirement to report a single benefit type could be different across the workforce depending, for each employee, on whether all or part of that benefit was provided under an OpRA, when that OpRA commenced, and when it was modified, varied, or renewed.

Given the above complexities and ambiguities, operating reasonable care to comply with these rules is key. The tax and NIC treatment of benefits has just got a lot more complex.