PKF Francis Clark

Pension salary exchange

A pension salary exchange scheme or pension salary sacrifice, involves an employee agreeing to exchange part of their gross salary for additional employer pension contributions. This results in national insurance savings for both employer and employee.

Pension salary exchange...

...benefits for employers

By implementing a pension salary exchange scheme, as opposed to deducting employee pension contributions from net salary, the employer will see a real cash saving in the form of reduced employer's national insurance contributions (NICs).

There is an effective saving of 15% per £1 sacrificed for each employee taking up the scheme. This is permitted by the tax legislation to encourage pension savings.

The employer's NIC saving can either be retained by the business or can be apportioned between the business and the employee's pension scheme. This means businesses with between 400 and 600 employees could save around £100,000 per year.

There are numerous factors to consider when implementing a salary exchange arrangement. Identifying the right approach for different groups of employees will be a key part of the policy design process.

...benefits for employees

Employees sacrificing salary into a pension scheme don't have to pay employee's NIC on the amount sacrificed. For those earning below the upper earnings limit (currently £967 per week), this could mean an 8% boost to their take-home pay.

Scheme design and communication are key considerations when introducing a pension salary exchange scheme to ensure it is provided only to those who would benefit.

Some of the issues to consider include:

- Employees cannot join a salary exchange scheme if it takes their salary below the national minimum wage
- Tax and NIC savings only apply if the individual is a taxpayer – part-time or seasonal workers therefore may not benefit
- Schemes can impact earnings-related benefits, such as statutory maternity and paternity pay
- Some mortgage companies may only lend on the post-sacrifice income as opposed to a pre-sacrifice reference salary. This is less common now as these schemes have become more popular

If you're interested in introducing a pension salary sacrifice scheme, our specialist team can prepare an illustration of the potential annual savings available based on information from your company accounts. The next step would be to review your existing workforce and their current pension contributions in detail to obtain a more precise estimate.

Basic rate

	Before salary exchange	After salary exchange
Gross salary	£30,000	£28,500
Employee % contribution	5%	0%
Employee pension payment	£1,500	£0
Employee NIC	£1,394	£1,274
Employee NIC saving	**£0**	**£120**
Employer % contribution of gross salary before exchange	3%	8%
Employer NI	£3,750	£3,525
Employer NI saving	**£0**	**£225**
Total contribution rate	8%	8%

In the example above, the employee gives up £1,500 of their salary (5% of £30k). The employer then contributes 8% of their salary instead of 3%. This leads to an NIC saving of

£120 for the employee and £225 for the employer. Additionally, the employee's take home pay increases while the total pension contribution percentage stays the same at 8%.