Make the most of your **pension savings**

An employee guide to salary exchange - Employer NIC (National Insurance Contributions) savings reinvested

ROYAL LONDON

By paying into a pension, you're already taking the right steps to save for your future. Your pension savings are invested to help them grow. Another way to make your money work harder could be to **take advantage of the benefits of salary exchange.**

What is salary exchange?

You've probably heard of salary exchange, sometimes referred to as salary sacrifice, but may not be familiar with what it is.

Put simply, it's an agreement between you and your employer, where you agree to exchange part of your gross salary or bonus for a pension contribution.

It works in the same way as other salary related benefit schemes, for example company car, cycle to work and childcare voucher schemes. It's a tax efficient way to make pension contributions into your pension plan.

What are the benefits?

The main benefit is that you and your employer pay less National Insurance Contributions (NIC) and you pay less income tax. Your employer can choose to reinvest their savings. You can choose to add your savings to your pension contribution or your take home pay. Your options include:

- Using the tax and NIC savings to **increase your contributions** and keep your take home pay the same.
- Using the tax and NIC savings to **increase your take home pay** and keep your pension contributions the same.
- In addition to either increasing contributions or take home pay you can also make additional tax and NIC savings by exchanging any contractual or discretionary bonuses you receive.
- Your employer also saves on their NIC and they can choose to **reinvest** some or all of their own NIC savings into your pension plan.

Is salary exchange right for everyone?

There are some things to think about, please see the 'Some things to consider' section on the next page.

How does salary exchange work?

We've used a case study to illustrate the effect on a salary and pension contribution by exchanging part of a salary of £27,000.

The case study on the next page shows how an employee called Sam has chosen to use his tax and NIC savings to increase his pension contributions.

! Investment returns are never guaranteed. So while your savings could grow, their value can also go down. This means you could get back less than what you pay into your plan.

Sam (the employee) is paid an annual salary of £27,000. He pays 5% (£1,350) into his pension and his employer pays 3% (£810). So the total yearly pension contribution is 8% (£2,160) before any salary is exchanged.

- Sam's agreed to exchange part of his salary, his employer adds the exchanged amount to the existing employer pension contribution.
- This means Sam's salary is reduced to £25,411.76, and the exchanged amount of £1,588.24 is added to the existing £810 employer contribution, **along with any NIC saving his employer has chosen to reinvest.**
- The employee benefit shows that Sam's take home pay remains the same at £20,942.16, however **as a result of paying less income tax and NICs on his reduced salary his total pension contributions have increased by £457.42, from £2,160 to £2,617.42.**

Case study: All tax and NIC savings are reinvested into the pension plan	Before salary exchange	After salary exchange
Salary	£27,000	**£25,411.76**
Employee		
Pension contribution	£1,350*	£0
Income tax payment	£2,886	£2,568.35
NIC	£2,091.84	£1,901.25
Employer		
Pension contribution	£810	£2,617.42
NIC	£2,506.08	£2,286.90
Employee benefit		
Total pension contributions	£2,160	£2,617.42
Employee take home pay	£20,942.16	**£20,942.16**

*Because 20% tax relief is given on Sam's pension contribution, the actual cost to Sam is £1,080.

EXTRA PENSION CONTRIBUTION EACH YEAR AFTER SALARY EXCHANGE

£457.42

If you would like more information and a personalised statement, please contact your employer.

All figures are based on tax and NI rates for the 2021/22 tax year.

Some things to consider

To help you decide if salary exchange is right for you, here are some things to consider:

- You won't be able to exchange part of your salary if it drops below the National Minimum Wage or National Living Wage afterwards.
- Your yearly pre-tax salary will reduce by agreeing to exchange part of your salary, which can affect your entitlement to things such as statutory and salary related benefits.
- Salary exchange used to affect how much you could borrow for a mortgage, however most lenders will now typically lend against a pre-exchanged salary.
- Tax treatment depends on your own circumstances and any changes could affect how much you save in the future.
- If you're a higher rate taxpayer, you will effectively receive tax relief at your highest rate of tax because your pension contribution is taken from your gross salary.
- Salary exchange may not be suitable if you earn more than £240,000 with a tapered annual allowance. If this applies to you, you could incur additional annual allowance tax charges.
- The rules about salary exchange may change in the future. If you're not sure if salary exchange is right for you, talk to a financial adviser.

If you don't already have a financial adviser, you can find one in your area by visiting royallondon.com/find-a-financial-adviser. Advisers may charge for their services – though they should agree any fees with you upfront.

Royal London
1 Thistle Street, Edinburgh EH2 1DG
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