Make the most of your **pension savings**

An employee guide to salary exchange

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. You can choose to add these 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.

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 the savings and benefits of using salary exchange for an employee called Sam.

! 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 £25,650, and the exchanged amount of £1,350 is added to the existing £810 employer contribution.
- The value of Sam's total pension contributions stays the same. As a result of paying less income tax and NICs on his reduced salary, his take home pay increases by £162 to £21,082.

Case study	Before salary exchange	After salary exchange
Salary	£27,000	**£25,650**
Employee		
Pension contribution	£1,350*	£0
Income tax payment	£2,900	£2,630
NIC	£2,100	£1,938
Employer		
Pension contribution	£810	£2,160
Employee benefit		
Total pension contributions	£2,160	£2,160
Employee take home pay	£20,920	**£21,082**

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

ADDITIONAL TAKE HOME PAY AFTER SALARY EXCHANGE

£162

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 2020/21 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 your pension contributions could provide higher tax and NIC savings.
- 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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