

# Puzzled By Pensions?

## Salary Exchange Explained



In the last few years, lots of Usdaw members have received announcements from their employers about 'Salary Exchange' arrangements (sometimes called Salary Sacrifice Pensions) which offer an alternative way of paying your regular contribution to the company's pension scheme.

These arrangements do not replace the pension scheme that you are currently in.

They are simply a way of paying your regular contribution to the company's pension scheme which is designed to save you and your employer money.

Salary Exchange is not the easiest thing for companies to explain or for employees to understand. Many employees are instinctively suspicious or fail to understand how taking a cut in pay can actually save them money!

Provided that it is done properly, Usdaw supports the introduction of Salary Exchange arrangements by employers because:

- a. Most members who participate will benefit from a little extra 'take home' pay.
- b. Employers make a larger saving which is offset against the cost of providing good quality pension benefits and encourages them to keep good pension schemes open for longer.

### How Salary Exchange Works

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If you are a member of your company's pension scheme, your employer will pay your regular pension scheme contribution for you.

In exchange, you give up (or 'sacrifice') an amount of your gross pay equal to the amount of your regular pension scheme contribution.

The income tax that you pay stays the same, but the amount of your National Insurance contribution (and the National Insurance contribution that your employer makes for you) goes down.

As a result of paying a reduced National Insurance contribution, your net 'take home' pay goes up by a small amount.

### What Are the Effects of Salary Exchange?

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#### *Pay and Related Benefits*

All of your pay and pay-related benefits (including bonus, overtime, holiday pay, life assurance and so on) and any future pay rises should continue to be based on your previous level of pay before you took part in Salary Exchange.

#### *Company Pension*

If your pension is calculated based on your final salary or career average salary, it should continue to be worked out using your 'pre-exchange' level of pay and so it will not be affected.

#### *Redundancy*

If you were to be made redundant, company redundancy payments should also be based on your 'pre-exchange' level of pay.

#### *Child Support and Court Orders*

Child Maintenance Service (CMS) assessments and Court Orders are usually based on your net pay, which will increase as a result of Salary Exchange. You should contact the CSA, the Citizens Advice Bureau or seek legal assistance if you need more information.

#### *Student Loans*

Student loan repayments are based on gross pay which reduces as a result of Salary Exchange and so your repayment period may be increased.

#### *Mortgage Applications*

Some mortgage lenders will accept a letter from the employer based on your 'pre-exchange' level of pay.

#### *State Pension*

The State Pension was reformed in April 2016 and the new single-tier pension is not salary-related. There is, therefore, no impact on your State Pension if you participate in a Salary Exchange scheme.

### Other State Benefits

Statutory Maternity Pay (SMP) and Statutory Paternity Pay (SPP) may be reduced if you take part in Salary Exchange.

### Additional Voluntary Contributions

If you pay Additional Voluntary Contributions (AVCs) towards your company pension, your employer may also extend Salary Exchange to cover your regular AVC payments.

### Who Isn't Salary Exchange Right For?

- a. Government will generally not allow you to participate in a Salary Exchange arrangement, if you are earning National Minimum Wage or Living Wage.
- b. If you are eligible for means tested State benefits, you could be disadvantaged if you join a Salary Exchange arrangement. Always check with your employer if you think you might be affected.
- c. If you have already reached your State Pension Age, you will no longer be paying National Insurance and so there is no benefit to you from a Salary Exchange arrangement.

If you are in any doubt about joining a Salary Exchange arrangement always check with your employer first.

### Further Information



Usdaw members who have any questions about Salary Exchange, or just about pensions in general, can contact Usdaw's Pensions Section on **0161 224 2804**, email us at [pensions@usdaw.org.uk](mailto:pensions@usdaw.org.uk) or scan the code to ask a question through the website.

### An Example

Below is an example of how somebody who is earning £20,000 a year and contributing 5% of their pay towards their pension can save money by taking part in Salary Exchange:

This person has benefited from a small increase of £80 in the amount of their 'take home' pay.

	Without Salary Sacrifice	With Salary Sacrifice
Gross yearly pay	£20,000	£20,000
Pension contribution	£1,000	N/A
Salary Exchange	N/A	£19,000
Less Income Tax	£1,286	£1,286
Less National Insurance	£593.28	£513.28
Net 'take home' pay	£17,120.72	£17,200.72

This example uses 2026/27 levels of Income Tax and National Insurance.

From April 2029 Government has confirmed it intends to cap the National Insurance exemption for pension contributions at £2,000 a year.

For lower pension savers contributing less than £2,000 a year, there will be no change. However, if you are paying higher contributions your National Insurance saving will be reduced when the legislation is introduced.

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