

A guide for employees

Salary sacrifice and pension (including bonus sacrifice)

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Did you know that salary sacrifice (also known as salary exchange, SMART Pensions and Smart Pay) can provide you with an opportunity to increase your pension contributions without affecting your net income (this is the income left after you've paid tax and national insurance contributions)?

What is salary sacrifice?

A salary sacrifice scheme is an arrangement between you and your employer in which you agree to a reduction in your salary or bonus, and in return you receive a benefit. The benefit here is a contribution by your employer of an equivalent amount into your pension. This way you can save on income tax and both you and your employer can save on national insurance contributions (NIC).

The sacrifice is achieved by varying your terms and conditions of employment as you're giving up your contractual right to future cash payments of the amount sacrificed.

Advantages of salary sacrifice for you

- Salary sacrifice can be used to maintain your level of pension savings and see an increase in your net take home income.
- Or, salary sacrifice can be used to boost your pension savings while leaving your net take home income unchanged.
- You can save NIC of 13.25% of the amount sacrificed on earnings above the primary threshold (£12,570 for tax year 2022/23). For any earnings above the upper earnings limit (£50,270 for tax year 2022/23) your NIC saving will be 3.25%.
- Your earnings that would be taxed can be sacrificed into pension contributions which aren't taxed.

- It provides you with a tax-efficient way to save for your retirement.

Depending on your circumstances there may be disadvantages to salary sacrifice and it's important you understand these.

We explain these in 'What you need to be aware of about salary sacrifice' later in this guide, and it's important you read this section.

How is salary sacrifice arranged?

Strict rules apply to salary sacrifice to protect both you and your employer. The following factors laid down by HM Revenue & Customs (HMRC) for salary sacrifice need to be met:

- Your terms and conditions of employment need to be revised.
- This revised contract must state that you're entitled to a lower cash payment and separately a benefit (in this case an enhanced employer pension contribution) as a result of a sacrifice.
- The agreement between you and your employer must refer to the benefit being given in exchange for the sacrifice.
- Only your entitlement to future salary can be sacrificed and this must be done before it's treated as received for tax purposes.

The information contained in this guide is based on Aviva's interpretation of current legislation, taxation law and HMRC practice for the 2022/23 tax year, which may change in the future.

The value of any tax relief depends on your financial circumstances.

A guide for employees – salary sacrifice and pensions

The purpose of this table is to demonstrate the amount by which your net (take home) income increases under salary sacrifice whilst maintaining the same total pension contribution.

You can also choose to use the savings generated by salary sacrifice to increase your pension contribution which would mean that your take home income would be the same.

This is just an example calculation and how much you save will depend on by how much you choose to reduce your monthly pay.

| Basic rate tax payer | | |
|---|----------------------|-------------------|
| | Non salary sacrifice | Salary sacrifice |
| Annual salary | £30,000 | £28,500 |
| Monthly salary | £2,500 | £2,375 |
| Employee contribution before tax relief | £100 | £0 |
| Employee contribution after tax relief added | £125 | £0 |
| Tax | £290.50 | £265.50 |
| National Insurance | £192.46 | £175.89 |
| Take home pay* | *£1,917.04 | *£1,933.61 |
| Employer contribution | £125 | £250 |
| Total invested per month in pension | £250 | £250 |
| Employer monthly NI saving which they may choose to re-invest in your pension | £0 | £18.81 |

***Take home pay is £16.57 per month greater under salary sacrifice**

| Higher rate tax payer | | |
|---|----------------------|-------------------|
| | Non salary sacrifice | Salary sacrifice |
| Annual salary | £60,000 | £58,500 |
| Monthly salary | £5,000 | £4,875 |
| Employee contribution before tax relief | £100 | £0 |
| Employee contribution after tax relief added | £125 | £0 |
| Tax | £952.67 | £902.67 |
| National Insurance | £422.62 | £438.56 |
| Take home pay* | £3,504.71 | *£3,533.77 |
| Higher/Additional tax relief reclaimed via self-assessment | £25 | |
| Final net income allowing for higher rate reclaim | *£3,259.71 | £3,533.77 |
| Employer contribution | £125 | £250 |
| Total invested per month in pension | £250 | £250 |
| Employer monthly NI saving which they may choose to re-invest in your pension | £0 | £18.81 |

***Take home pay is £4.06 per month greater under salary sacrifice (after allowing for the higher rate tax relief that is claimed through self-assessment in the non salary sacrifice scenario).**

Please note, the examples in this guide aren't appropriate for Scottish tax payers.

Example monthly payslip

| | | | | | |
|----------------------|------------------|------------------------|----------------|-----------------------|------------------|
| Employee Name | | Employee Number | | Tax Period | |
| | | | | Tax Code | |
| | | | | N.I Number | |
| | | | | N.I Code | |
| | | | | | |
| Payments | | Deductions | | This Period | |
| Description | Cash | Description | Cash | Description | Cash |
| Reference salary | £2,50 0.0 0 | Tax | £265.50 | Taxable Pay | £2,375.00 |
| Salary sacrifice | -£125.00 | NI-EE | £175.89 | | |
| | | | | | |
| | | | | Year-To-Date | |
| | | | | Tax | |
| | | | | NI-D | |
| | | | | Taxable Pay | |
| | | | | NICable | |
| | | | | | |
| Payments | £2,375.00 | Deductions | £441.39 | Net Pay | £1,933.61 |
| | | | | Paid By | BACS |
| | | | | Sort Code | |
| | | | | Account Number | |

The reference salary is your pre-sacrifice salary.

Salary sacrifice shown on a standard payslip as a reduction to salary before tax and NIC.

There is not a set way in which salary sacrifice needs to be demonstrated on a payslip. Much of this will depend on the payroll system your employer uses and whether employee benefits are based on the higher or reduced gross salary.

What you need to be aware of about salary sacrifice

Like any financial decision salary sacrifice is not suitable for everyone. You should be aware of the potential drawbacks and take these into account before deciding.

You need to be aware that salary sacrifice could affect your current or future entitlement to a range of state benefits, including the receipt of tax credits.

If your earnings (after salary sacrifice) fall below a certain limit (currently £6,396* a year), you won't be eligible for:

- statutory sick pay;
- statutory maternity, paternity or adoption pay;
- incapacity benefit;
- jobseeker's allowance (although means-tested benefits may still be claimed).

If you've not paid enough NIC on your income, state pension benefits may also be reduced on retirement.

*2022/23 limits

Salary sacrifice should not reduce your cash pay to below the national minimum wage. This means that if you're working full-time and earn around £15,000 a year or less, you should take care when considering any salary sacrifice scheme.

Any amount that you sacrifice is taken from your pay before tax is deducted. If you're a non-taxpayer (you earn less than your personal allowance), you don't benefit from the tax relief that a taxpayer would receive. If you're paying into a personal pension, it may be more cost effective to pay personal contributions rather than use salary sacrifice, as personal contributions are automatically deducted net of basic rate tax relief regardless of the amount you earn.

Other possible impacts are on your borrowing levels, such as mortgage borrowing, credit card and personal loan limits, income protection insurance benefits and redundancy entitlements.

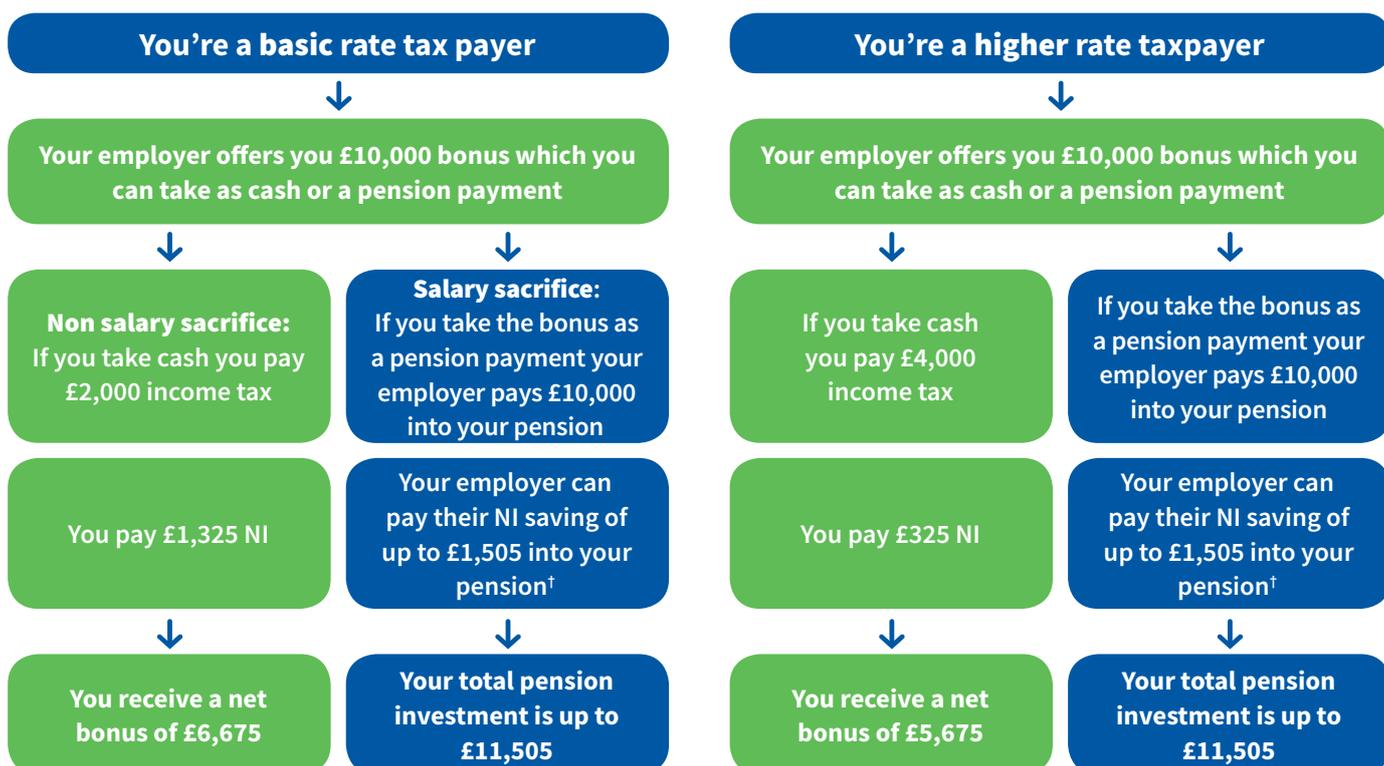
Pay-related benefits, such as overtime payments, life insurance, salary increments and final salary pension benefits, may be calculated on your 'reference' salary, i.e. your salary before the sacrifice. This will depend on what your employer has stated in your employment contract.

Bonus sacrifice

In the same way that you can sacrifice earnings for a non-cash benefit, such as pension contributions, you can also sacrifice some or all of your bonus.

Things to be aware of about bonus sacrifice

- The bonus must be sacrificed before you receive it.
- You cannot change your mind once you've agreed to sacrifice the bonus.
- Bonus sacrifice can also affect your entitlement to state benefits.



[†]Your employer will decide how much of their saving will go into your pension. The maximum amount is 15.05% of the bonus. These calculations assume the employer contributes the maximum amount of their NI saving into your pension.

Questions & answers

If I decide not to opt for salary sacrifice initially, when can I join in the future?

Joining a salary sacrifice scheme is subject to eligibility, the terms and conditions of the scheme, your acceptance of a change to your contract of employment, and the scheme continuing in existence. You'll need to check with your employer if you can join the salary sacrifice scheme at a later date.

Can I withdraw from salary sacrifice at any time?

Subject to the rules of the salary sacrifice scheme of your employer, you can withdraw from salary sacrifice for pension at any time although you'll need to check with your employer to find out when you'll be able to choose salary or bonus sacrifice again.

Are there any restrictions on eligibility for salary sacrifice?

There are certain restrictions on eligibility. At any time during your employment your gross pay must not fall below the national minimum wage or national living wage rates, either before or after the salary sacrifice reduction. The rates from 6 April 2022 are:

- £6.83 for those aged 18–20
- £9.18 for those aged 21–22
- £9.50 for those 23 and over

You aren't able to sacrifice statutory maternity, paternity, adoption pay or sick pay. If you've already joined the scheme before taking maternity, paternity or adoption leave, you'll receive statutory maternity, paternity or adoption pay in full and employer contributions will be maintained at the level they were prior to you taking the leave, including the amount you would have been sacrificing. While in receipt of statutory sick pay, employer contributions will be based upon your sick pay received at the percentage agreed under your salary sacrifice agreement.

How will salary sacrifice affect my tax credits?

Tax credits are benefits for families with children and working people on low incomes. The amount of tax credits you receive depends on your total family income and your own family circumstances.

HMRC administers tax credits and for more information on how salary sacrifice could affect the amount of tax credits you receive, call the tax credits helpline on **0345 300 3900**.

If I work additional hours, what rate will I get paid?

Your terms and conditions of employment with your employer will show whether your overtime pay is based on your salary before or after sacrifice.

If I apply for a mortgage, a loan or similar financial transaction, what should I quote as my earnings?

You should quote your revised gross pay (following salary sacrifice). If you decide to opt for salary sacrifice to boost your pensions savings, generally your net spending income will remain unchanged. However, your gross pay will be

reduced due to salary sacrifice and this may impact your ability to qualify for a mortgage or loan.

What happens if I take unpaid leave?

While you're taking unpaid leave, you won't be able to participate in a salary sacrifice agreement. Any employer's contributions can usually continue to be paid into your pension; however, they aren't bound by law to do this.

What is the effect of salary sacrifice on how much I can pay in?

You can pay as much as you want into a pension scheme, however, HMRC puts a limit on the total amount you can pay before a tax charge is payable. For the 2022/23 tax year this annual allowance is £40,000. If you've flexibly accessed any of your pensions you'll usually be subject to a reduced allowance of £4,000 (2022/23) tax year in respect of your money purchase pension savings.

If you earn more than £200,000 in threshold income (2022/23), your annual allowance may be reduced and a 'tapered annual allowance' may apply. From 9 July 2015 any new or renegotiated amounts sacrificed from pay have been included when determining threshold income. This prevents the use of salary sacrifice to avoid the tapered annual allowance. If you're a high earner and you think this may affect you, please speak to a financial adviser.

For more information please visit: **www.gov.uk/tax-on-your-private-pension/annual-allowance**

Where can I get independent financial advice?

If you don't already have a financial adviser, you may be able to find one using the contact details below.

Unbiased: **www.unbiased.co.uk**

You may be charged for any advice from an adviser.

What are the charges for joining the salary sacrifice scheme?

You'll need to check with your employer if there are any costs associated with salary sacrifice.

Can I sacrifice any redundancy payment?

Yes, you should be able to sacrifice all or part of a redundancy payment, if your employer provides this facility. Any amount sacrificed is classed as an employer contribution and does not attract tax relief. As the first £30,000 of redundancy pay is normally free of both tax and NI, there are few benefits to sacrificing this amount. Any amount over £30,000 is subject to income tax at your normal rate, though again there should be no NI liability. You could therefore save income tax on any amount sacrificed over £30,000. This means that the benefits of sacrificing redundancy pay aren't as clear cut as with salary or bonuses. You should take professional advice before making a decision. You may be charged for this advice.

For more information on redundancy payments, visit the HMRC website at:

www.gov.uk/calculate-your-redundancy-pay

If you're ready to take advantage of salary sacrifice, please contact your employer.

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 **0345 602 9221**

 **ngp.questions@dgaviva.com**

 **aviva.co.uk**

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