Penfold

How salary sacrifice saves you money

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What is Salary Sacrifice?

Salary Sacrifice is a government-backed scheme to help employers and their workers save on tax by paying into a pension.

Here, an employee effectively ‘swaps’ part of their salary for another benefit, in this case, pension contributions.

The employee agrees to give up a small part of their earnings, reducing their overall salary. These ‘sacrificed’ earnings are then added directly into their workplace pension, ready for their retirement.

Today, only 41% of smaller enterprises offer Salary Sacrifice, compared with 85% of large organisations. For many SMEs, Salary Sacrifice represents a simple way to trim their tax bill while helping their employees keep more of what they earn.

#2

How it works

When an employee agrees to take part in a Salary Sacrifice scheme, they essentially agree to use a small part of their monthly pay for their pension.

Rather than paying a part of their earnings into their pension every month, they get paid less on the agreement that any money they sacrifice goes straight into their pension instead.

They are reducing their monthly take-home pay now in exchange for more money in their pension for the future.

The benefit of doing this is that by reducing the money they receive right now, they owe less tax and get to **keep more of what they earn overall**.

What Salary Sacrifice Looks Like

Here's an example of Salary Sacrifice in action. Rachel works for a small business and earns £50,000 a year.

Before Salary Sacrifice, she paid 5% of her earnings into her workplace pension, with her employer adding a further 3% - that works out as £4,000 a year.

After her pension contributions and tax deductions, her net annual pay was **£34,698.10**

However, with Salary Sacrifice, Rachel could be keeping more of what she earns.

Now, on paper she earns £47,500 a year - she's "sacrificed" the 5% of her salary that she was previously adding to her pension. This contribution comes entirely from her employer.

Her new annual net salary? **£35,029.35.**

She's still adding £4,000 to her pension every year, but by reducing her salary, she's trimmed her tax bill, meaning she keeps hold of **£331.25 extra every year!**

That's money for her, not the government.

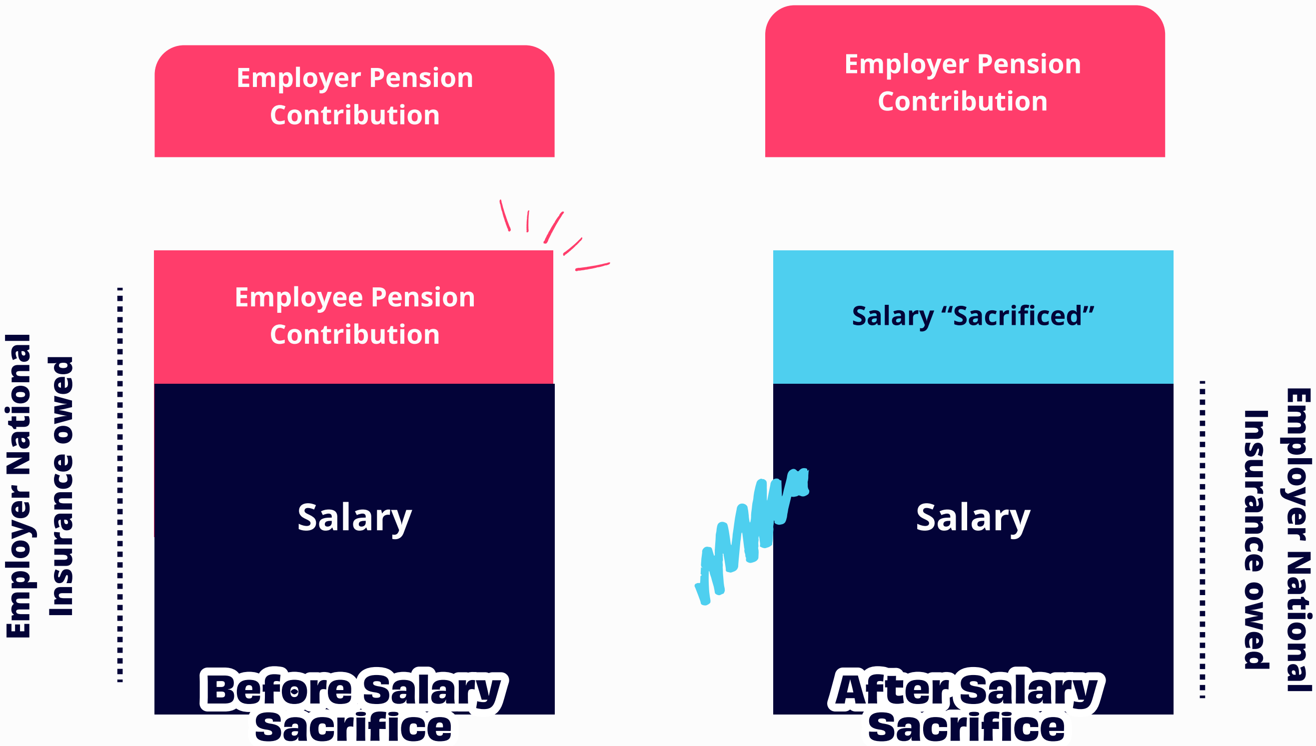
	Before Salary sacrifice	After Salary Sacrifice
Salary	£50,000	£47,500
Personal Pension Contributions	£2,500	£0
Employer Pension Contributions	£1,500	£4,000
Employer National Insurance	£5,335.08	£5,007.33
Employee National Insurance	£5,315.90	£4,984.65
Total PAYE tax owed	£7,486	£7,486
Final Paycheck	**£34,698.10**	**£35,029.35**

#3

How Salary Sacrifice Cuts National Insurance

Because Salary Sacrifice reduces an employee's earnings, you're also reducing the amount of National Insurance your company owes.

National Insurance tax is calculated on gross salary - before any deductions. Reducing an employee's 'on paper' salary means you'll owe less in employer National Insurance contributions.



Using Sarah's example, rather than paying National Insurance on £50,000 a year, you're now taxed on £47,000 a year. Remember, you're still paying the same amount in pension contributions.

Here's the main takeaway. You've just saved your business **£327.75 a year** simply by switching schemes. And that's only for one employee.

The bigger your team (and the more your employees earn), the more you save.

Company Size	Yearly NI Savings (Based on £50,000 average salary)
50	£16,387.50
100	£32,775
250	£81,937.50

This saving reflects the upcoming National Insurance tax increases, currently scheduled for 2023.

#4

Benefits for your team

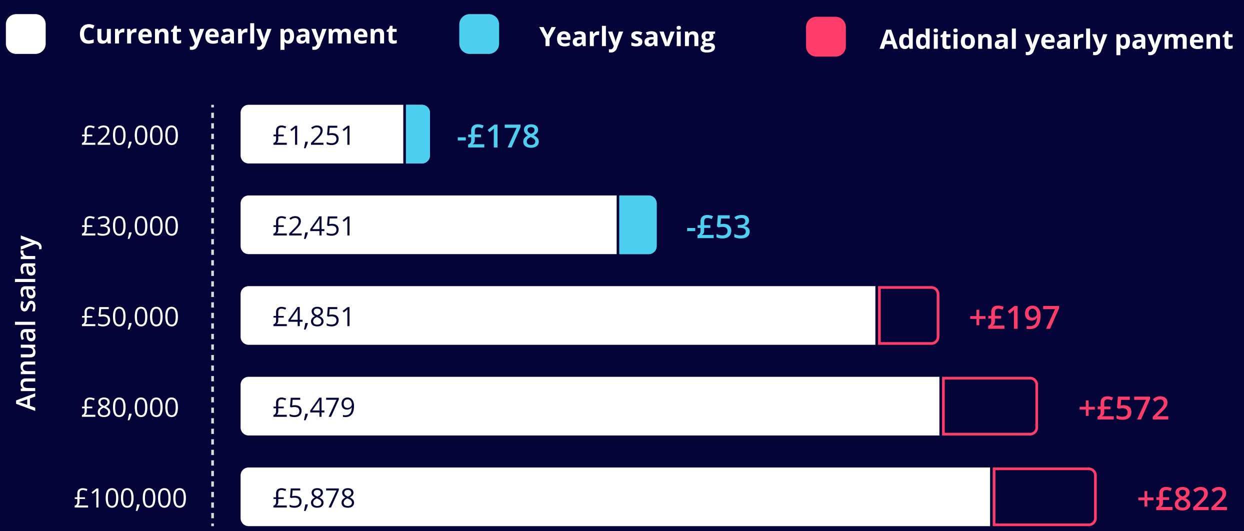
As we touched on earlier, Salary Sacrifice is a great option for helping your employees keep more of what they earn.

Here are the **main 3 advantages** of Salary Sacrifice for your team.

- Regular payments into their pension - including extra from you
- Reduces their tax bill - increasing how much of their money they get to keep
- Tax relief is applied automatically - meaning they won't have to claim it from HMRC themselves

How much more will employees pay?

National Insurance set to increase by 1.25 on the pound*



***Increase would become a separate "Health & Social Care Levy" from April 2023**

Source: gov.uk

#5

Salary Sacrifice VS Net Pay

You may be familiar with the idea of employee pension contributions being paid pre-tax, before Income Tax and National Insurance deductions. This is known as the 'Net Pay' approach. Salary Sacrifice is a little different.

With 'Net Pay' your employees pension contributions still come from their salary. Their yearly earnings don't change, they just use a percentage of their income to pay into their pension.

For Salary Sacrifice, technically the employee doesn't pay anything into their pension. All contributions come from the employer, supported by the employee's sacrificed earnings.

It's a small difference that doesn't affect how much goes into their pension - but has a big impact on how quickly tax relief is added to their pot. No more waiting for HMRC.

#6

Things to keep in mind

While Salary Sacrifice can be a fantastic way to effectively increase your earnings, it will have an impact on anything that is linked to an employee's salary.

Here are a few things that may affect your decision to switch to a Salary Sacrifice scheme.

Low Income

You won't be able to use Salary Sacrifice where it would reduce an employee's earnings under minimum wage.

Salary-Based Benefits

Any life insurance or loan applications that are linked to salary may also be affected. Typically you can provide a lender with a letter/statement explaining that your employee is part of a Salary Sacrifice arrangement - but it might be worth double checking if you're applying for a loan/mortgage.

Maternity Pay

Typically statutory maternity pay is calculated based on average weekly earnings so could be reduced if your overall salary is reduced.