PUZZLED BY PENSIONS?
SALARY EXCHANGE EXPLAINED

Pensions

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

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

They are simply a new 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

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?

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. If your employer operates company sick pay or company maternity pay schemes these should also be unaffected.

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 Support Agency (CSA) 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.

Continued overleaf ...

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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 reference letters

Mortgage reference letters should not be affected because they will be 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) is based on your average pay over a fixed period before you begin to receive it. Exchanged pay won't count as part of your pay for calculating SMP so it may be reduced if you take part in Salary Exchange.

You will lose your entitlement to Statutory Sick Pay (SSP) if your pay drops below the Lower Earnings Limit (£118 a week in 2019/20). You might qualify for Income Support or Incapacity Benefit/ESA instead.

If your pay drops below £30 a week you may lose your entitlement to Maternity Allowance.

Additional Voluntary Contributions

If you pay Additional Voluntary Contributions (AVCs) towards your company pension, Salary Exchange can also be extended to cover your regular AVC payment.

Who shouldn't take part?

The only people who definitely should not take part in Salary Exchange are:

a) People earning the National Minimum Wage (because it is illegal to be paid less than the National Minimum Wage). This will also apply to those being paid the Living Wage.

b) People who earn less than the Lower Earnings Limit (£118 a week in 2019/20) need to check how taking part in Salary Exchange will affect their entitlement to pay-related state benefits (including Basic State Pension, Jobseekers Allowance, Statutory Sick Pay and so on).

Most employers will make sure that anybody who earns less than the Lower Earnings Limit will automatically be excluded from 'Salary Exchange' arrangements.

c) Workers who have reached their State Pension age because they are no longer paying National Insurance and therefore there is no benefit to them.

d) Those receiving childcare vouchers already have their National Insurance contributions reduced. If taking part in Salary Exchange while receiving childcare vouchers means that you will no longer pay any National Insurance it might affect your entitlement to some state benefits. You might be better off opting out of Salary Exchange (because receiving childcare vouchers saves you both tax and NI whilst Salary Exchange only saves you NI).

Further information

Usdaw members who have any questions about Salary Exchange or just about pensions in general can contact the Union's Pensions Section in the Legal Department at Central Office.

Telephone us on 0161 224 2804 or send an email to: pensions@usdaw.org.uk

An example

Below is an example of how somebody, who is earning £15,000 a year and contributing 5% of their pay towards their pension, can save money by taking part in Salary Exchange:

	Without Salary Sacrifice	With Salary Sacrifice
Gross yearly pay	£15,000	£15,000
Pension contribution	£750	N/A
Salary Exchange Pay	N/A	£14,250
Less Income Tax	£350	£350
Less National Insurance	£765	£674
Net 'take home' pay	£13,138	£13,228

This person has benefited from a small increase of £91 in the amount of their 'take home' pay.

This example uses 2019/2020 levels of Income Tax and National Insurance.

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