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Salary exchange guide for **employers**

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With people living longer than ever before, and the cost of living rising each year, your employees' pension savings will need to go a long way to provide for a comfortable retirement. By encouraging your employees to pay into their pension plans through salary exchange, you can help boost their retirement investment whilst minimising some of the costs you incur as an employer.

What is salary exchange?

Salary exchange is an arrangement through which your employees agree to reduce their salary or bonus in exchange for a pension contribution paid by you, their employer.

How does it work in practice?

To see how salary exchange might affect your employees' salaries and pension payments we'll look at an example case,

Steve is paid an annual salary of £20,000. He pays £1,000 (gross) into his pension plan each year and his payments are matched by his employer, taking his total pension payments for the year to £2,000.

- With salary exchange, Steve could stop making payments himself and agree to 'exchange' £1,000 of his salary for a pension payment paid by his employer.
- Steve's employer would reduce his salary to £19,000 and pay the 'exchanged' amount (£1,000) into his pension plan, along with the £1,000 they already pay on his behalf.

	Before salary exchange	After salary exchange
Salary	£20,000	£19,000
Steve's pension payment	£1,000	£0
Employer pension payment	£1,000	£2,000
Total pension payment	<i>Steve will pay lower NICs on his reduced salary which will increase his take home pay. Or, Steve could choose to exchange slightly more salary in order to increase his total pension payments and keep his take home pay the same</i>	

What are the benefits?

For the employer - As an employer, you'll pay lower National Insurance contributions (NICs) on your employees' reduced salaries.

To get an idea of the amount you stand to save, simply multiply the amount your employees pay into the scheme (which, in this example, is the amount we are assuming your employees are exchanging) by the current employer NIC rate of 13.8% for the 2024/25 tax year.



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Average annual employee payment (gross amount)	£1,500
Number of scheme members	100
Total	£150,000
Employer NIC rate	X13.8%
Your annual saving	£20,700

You are free to choose how to use any employer NIC saving. One way to increase scheme take up would be to redistribute some of your NIC saving to your employees to supplement their pension provision.

For the employee

Your employees may pay lower NICs on their reduced salaries. The saving can be used to either:

- Increase their pension payments and keep take home pay the same
- Keep the overall pension payment the same and benefit from increased take home pay
- Increase both their pension payments and take home pay

Our technical guide to salary exchange has explanations on the different ways of setting up a salary exchange arrangement.

Some things to bear in mind

If you're considering setting up salary exchange as a way for your employees to make pension payments, there are some things you need to be aware of. These relate to two key changes:

- A reduction to your employees' annual pre-tax salaries
- Changes to your employees' contracts of employment

Both have implications for you and your employees. You can find a list of issues to consider in our technical guide to salary exchange. Some key points are listed below:

- Your payslips will need to display the amount of salary exchanged.
- HM Revenue & Customs take an interest in how tax and national insurance contributions are affected and they have published a full set of salary exchange guidelines on their website (www.gov.uk/guidance/salary-sacrifice-and-the-effects-on-payee).

We've summarised the main points in our technical guide to salary exchange.

- Your employees' entitlement to statutory benefits and other salary related benefits may be affected by their reduced gross salaries and you'll need to make your employees aware of how they may be affected (the relevant benefits and potential impacts are listed in our member guide).



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- You may want to retain a notional salary for your employees (this is the salary before exchange). By doing so, employees' pre-exchange salaries may be taken into account by mortgage lenders, and when entitlement to other salary related benefits is calculated.

This is based on our understanding of current tax laws. These laws and our understanding of them may change in the future.

Tax treatment will depend on the individual circumstances of each employee and may be subject to change in the future.

Auto-enrolment

At the moment, salary exchange doesn't work seamlessly with the auto-enrolment process. Employers can't make an agreement for salary exchange a pre-condition for auto-enrolment. However, employers can choose to operate salary exchange before or after the auto-enrolment process or use it as an alternative contribution basis to a default, unreduced, basis. Alternatively, employers can look into amending contracts of employment to have the same effect as salary exchange. Employers may need to take expert advice on salary exchange before deciding what they want to do.