Housing briefing, March 2025
Use salary exchange effectively to deliver savings

From April 2025, employer National Insurance contributions (NIC) will increase to 15%, and the salary threshold for NICs will decrease to £5,000. These changes should be factored into business plans and budgets. To mitigate the impact of these changes, salary exchange (or salary sacrifice) can be applied to pension contributions. This will reduce NICs for both employers and employees.

What is salary exchange?

Salary exchange makes pension contributions and other benefits more tax-efficient, delivering NIC savings for both employees and employers.

It can be used for member contributions to both Defined Benefit (DB) and Defined Contribution (DC) schemes (but not the Local Government Pension Scheme).

How does salary exchange work?

Salary exchange involves employees giving up part of their salary in return for their employer making a matching pension contribution.

This reduces gross salary, requiring a change in employment terms and potentially affecting other benefits like life assurance cover. Most employers maintain a *reference salary* to address this.

NICs are paid on the reduced salary, saving money for both employers and employees, and increasing employees' net take-home pay.

How to implement salary exchange effectively

Policies: Create a clear blueprint, considering factors such as the National Minimum Wage and periods of leave. Include regular reviews.

Communications: Use webinars, calculators and booklets. Clear messaging is more likely to lead to better implementation and higher take-up.

How much do employers save?

Recurring NIC savings for employers depend on the employee contribution rate and salary exchange take-up. For example, with a payroll of £10m:

NIC savings for employers		Take-up rates		
		0%	20%	80%
Average employee contribution rates	3%	No savings	£9,000 each year	£36,000 each year
	8%	No savings	£24,000 each year	£96,000 each year

Introducing salary exchange on an opt-out basis typically results in significantly higher take-up compared to an opt-in approach.

How much do employees save?

Employee NIC savings depend on salary and contribution rate. For example, with a salary of £35,000, monthly savings vary according to the contribution rate:

Monthly NIC and tax savings for employees	Employee contribution rate		
	3%	8%	20%
Gross pension contribution	**£88**	**£233**	**£583**
Income tax relief	*(£18)*	*(£46)*	*(£116)*
NIC saving from salary exchange	*(£7)*	*(£19)*	*(£47)*
Net pension cost	**£63**	**£168**	**£420**

As shown above, with an 8% contribution rate, salary exchange saves an employee an extra £19 each month. After tax relief, their £233 gross member pension contribution costs just £168.

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