

# Reconsidering your pension contributions

**Increases to National Insurance Contributions (NICs) from next April have made employee pension contributions less attractive.**

That headline is not one you might expect to see from a financial adviser, but there is some solid logic behind it. Consider Jane who works in Leeds, earns £40,000 a year and makes net contributions to her employer's workplace pension of £2,000 annually (equivalent to £2,500 once basic rate tax relief is included):

To earn £2,000 net, Jane must receive £2,941.18 of gross pay:

Gross pay	£2,941.18
Employee NICs @ 12%	(£352.94)
Income tax @ 20%	(£588.24)
Net pay	£2,000.00

In addition, Jane's employer will have to pay 13.8% NICs on her gross pay – another £405.88.

So, the total cost of putting £2,500 into Jane's pension is £3,347.06.

The alternative is for Jane and her employer to agree to a salary sacrifice arrangement under which she forgoes £2,941.18 of salary and in return has £3,347.06 paid into her pension by her employer – a gain of 33.9% over the personal contribution route. In practice, the benefit may be slightly less as some employers levy an administration charge for salary sacrifice arrangements.

From April 2022, when NIC rates rise by 1.25% for employer and employee, Jane's potential gain increases to a maximum of 37.9%.

In this instance, higher rate taxpayers gain less because their marginal NIC rate will normally be less (2% in 2021/22, rising to 3.25% from 2022/23). Do the math and the benefit is 17.7% in this tax year and 21.6% thereafter (the figures in Scotland are marginally higher because its higher rate is 41% rather than 40%).

Despite the obvious appeal of the option, if your employer offers salary sacrifice for pension contributions, you should always seek financial advice before agreeing to a sacrifice arrangement. There can be disadvantages to salary sacrifice stemming from lower gross pay. If your employer does not offer salary sacrifice, then you may want to ask why...

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