SMART Pay Guide

Q. What is SMART Pay?

A. SMART Pay (also referred to as salary sacrifice or salary exchange) is a tax efficient way for you to make your pension contributions because they are deducted from your gross pay before you pay tax and national insurance.

In simple terms, you will get the same amount paid into your workplace pension as making contributions from your after-tax pay (the more traditional method) but your take home pay will increase.

Q. What will this mean to me?

A. Your salary will be reduced by an amount equal to your gross pension contribution. This is a contractual change. The employer pension contribution will increase by the same amount as your salary reduces. This is where the saving in tax and national insurance is made.

SMART Pay alters how your employer will deduct your pension contributions and therefore participating in SMART Pay is a variation to your Terms and Conditions of employment.

SMART Pay cannot reduce your earnings below the National Minimum Wage; and if this were to occur, you will no longer be able to participate in SMART Pay and will revert back to having your pension contributions deducted from your after-tax pay.

Q. What are the benefits for me?

A. By participating in SMART Pay, the amount of salary you exchange to an employer pension contribution is no longer subject to tax and national insurance.

This means that your take home pay will be higher whilst the total contribution to your workplace pension remains the same – because of the tax saved. The savings are greater for basic rate taxpayers because they pay national insurance at a higher rate than higher and additional rate taxpayers.

Q. I'm a higher rate taxpayer – how will this affect me?

A. If you are a higher (or additional rate) taxpayer, you have to reclaim any higher rate (or additional rate) tax relief you are due by completing a tax return or writing to (or calling) HMRC.

Under SMART Pay you will no longer have to do this (but you should advise HMRC that you are no longer due the tax relief so that they adjust your tax code accordingly). Higher and additional rate tax relief will be applied at source, which ensures that no one can forget to reclaim any tax relief due from HMRC.

If you are on the edge of the higher or additional rate tax bands, you may find you fall into a lower tax band through SMART Pay.

Some state benefits are subject to gross earnings limits, e.g., Tax-Free Childcare or 30-hours free Childcare. SMART Pay may mean you fall under government limits and become eligible for such schemes, as a result in the reduction to your gross earnings.

Q. How do I know if SMART Pay is right for me?

A. If you are unsure about participating in SMART Pay, you should seek advice. The primary concern for most employees is related to applying for a mortgage because of the adjustment to their contractual salary. To mitigate this, HR can issue a letter showing your pre-exchange salary. Your pre-exchange salary will generally be shown on your payslip.

Q. Will other salary related benefits be affected?

A. Although your contractual salary will be reduced for the purpose of your pension contributions, it will not impact any other salary related benefits, such as a group life assurance scheme, overtime payments, bonus payments linked to your salary or any future salary increases etc., as all of these are based on your pre-exchange salary.

Example: if your current gross basic salary is £25,000 and after SMART Pay it reduces to £24,120, for the purposes of calculating a group life assurance benefit the pre-exchange salary of £25,000 is used.

Q. What if I don't want to participate in SMART Pay?

A. You can elect to 'step-out' of SMART Pay if you believe it is not right for you. This means that you won't benefit from any tax or national insurance savings - and if you are a higher rate taxpayer, you will need to reclaim any higher rate tax relief direct from HMRC.

Q. Is there any impact on tax credits?

A. SMART Pay will not normally reduce any tax credits you receive. If you are in receipt of Universal Credit, Working Tax Credit or Child Tax Credit and have any concerns, please call the Tax Credit Helpline on 0345 300 3900 before making your decision to participate or 'step-out' of SMART Pay. If you are in receipt of any other benefits, please check with the relevant local authority to find out if there will be any impact.

Q. What happens if I have a student loan?

A. Student loan repayments are only deducted where monthly pay, which is subject to tax, exceeds the relevant threshold. As SMART Pay reduces the amount of pay that is subject to tax, the amount of student loan repayments you make may reduce. If earnings fall below the threshold, no student loan repayments would be made.

Q. What is the impact on my State Pension?

A. Entitlement to the new State Pension is based on the number of 'qualifying years' in an individual's working life rather than the amount of national insurance paid.

Q. What if I'm over state pension age?

A. If you are over state pension age you do not pay any national insurance, and therefore you will make no saving. However, you will still automatically be included in SMART Pay unless you choose to 'step-out.'

Q. What happens if I go on Maternity / Paternity / Adoption leave?

A. Statutory payments will be calculated on your SMART Pay earnings and therefore will be lower if you participate in SMART Pay. During the period you receive statutory payments, the employer pension contributions will be based on your pre-leave earnings.

Q. What happens if I go on sick leave?

A. Statutory payments will be calculated on your SMART Pay earnings and therefore may be lower if you participate in SMART Pay. During the period you receive statutory payments, you will not participate in SMART Pay and your pension contributions will be deducted from your after tax pay.

Q. Is there a minimum level of salary for SMART Pay?

A. You will not participate in SMART Pay if your SMART Pay salary falls below the National Minimum Wage (NMW). It is also recommended that you don't participate in SMART Pay if you're not paying tax and national insurance.The maximum pension contribution you can exchange is 10% of your gross pay, without referring to HR.

Q. Can I 'step out' of SMART Pay in the future?

A. It is possible to 'step-out' of SMART Pay in the future if you experience certain 'lifestyle' events, such as marriage, divorce, birth of a child, etc. If this is the case, then you should contact HR.

This is for guidance purposes only. It is recommended that you seek professional advice if you are unsure that SMART Pay (salary exchange or salary sacrifice) is suitable for you.