National Insurance Contributions (Employer Pensions Contributions) Bill – Briefing Ahead of Second Reading

This Bill gives effect to the policy announced in the Budget, of restricting the NIC savings from employees paying their pension contributions via salary sacrifice to an annual cap of £2,000.

The debate at second reading is an important opportunity for MPs to consider the claimed advantages and potential drawbacks of applying a cap in the future.

This briefing note mainly considers the merits of the underlying policy of capping the NIC savings on salary sacrificed pension contributions, though it also discusses some potential improvements to how it is proposed to apply.

Key points:

- Most of the yield from this measure would come from employer NICs. It will have a significant impact on the minority of organisations affected. They will pass most of the cost on to their employees through lower pay or pension contributions.
- Capping the benefit of salary sacrificed pension contributions affects workers at every level, and not just the highest earners.
- The estimated yield is unlikely to be achieved, after employers and trade unions work to mitigate the impact, it will hardly be worth putting the cap into effect.

This policy will mostly affect ordinary workers

At least 70% of the yield from this policy will come from increased employer NICs. This is on top of the historic increase in employer NICs in April.

Like April's increase in employer NICs, the vast majority of the impact will be passed on to employees through lower wages or pension contributions.

Recent opinion polling shows that this policy is one of the least popular of all the Budget 2025 measures.

This will not mainly impact higher earners

It is suggested, including by the Chancellor in her Budget speech, that this policy is targeted at higher earners, or that salary sacrifice is abused by people in the financial services industry using it to put their bonuses into pensions. This is incorrect.

Data published by HMRC in July showed that less than 10% of the NIC savings from salary sacrificed pension contributions accrued to those earning over £50,270.

The main reason that higher earners accrue a relatively low proportion of the benefits of salary sacrifice is that their marginal NIC rate is only 2%.

The low marginal rate of NICs for higher earners means that, for example, the savings for employees contributing 5% are higher for someone on £30,000 a year than £100,000.

A cap would affect employees on relatively low earnings. Many Prospect members contribute 6% to their pension, and at that rate everyone earning over £33,333 would be impacted. We have already seen evidence that even some apprentices could be affected by this policy due to the high pension contributions present in the best apprenticeship programmes.

We have already seen that most of the impact falls on employers who are expected to pass this on to employees through lower pay and pensions (and not just for higher earners).

Exchequer Impact of the policy is probably overstated

The cap is primarily a revenue raising measure, if it did not contribute significantly to the Chancellor's headroom against her fiscal targets, it is unlikely to have been a priority for inclusion in the Budget.

Because of the operation of the fiscal rules for Budget 2025, it is the estimated yield in 2029-30 (£4.8bn) that was most relevant to the impact of the policy on the Chancellor's headroom.

But actual yield could fall well short of £4.8bn in 2029-30, and this would greatly undermine the case for a cap:

- £1.6bn of the estimated yield in 2029-30 relates to the anticipated impact of employees switching to Relief At Source (RAS) schemes. There is no obvious basis for anticipating a significant shift to RAS schemes due to capping the benefits of salary sacrifice.
- The impact of behavioural responses by employers could be significantly higher in practice: eg the Budget documentation does not mention new starters (and nearly 50% of affected employees by April 2029 will have started after the Budget).
- This policy primarily affects larger employers who are more likely to have unionised workforces. Unions and employers are already in discussions about how to respond to these changes. The OBR fails to consider this point when assessing the likely behavioural impact of these changes.

Practical difficulties with the policy

NICs operates on a pay period and a per job basis. The Budget documents about this measure indicate that it will be an annual cap for each taxpayer. The mismatch between the bases for NICs and the proposed cap will be difficult to navigate.

The estimated one-off impact of £20m and continuing average annual costs of £30m for employers could significantly underestimate the difficulty of dealing with:

- End of year reconciliations (particularly where pension contributions are uneven and the same contribution could result in different savings depending on when it is made).
- Attributing permitted NIC savings in each pay period between different employers, where employees change job or have multiple jobs.

Suggested revisions to the Bill

The Bill provides for the cap to be increased by regulation. But there should be an automatic indexation provision to protect against the level of the cap losing a significant proportion of its value over time.

Parliament should consider whether a cap of £2,000 is reasonable, or if a higher cap would be more appropriate. There should be no provision for regulations that could reduce the cap in the future.