



Chain of consequences: income tax, NICs and auto-enrolment

The impact of the interaction of 2019/20 changes to income tax, NICs and auto-enrolment levels will have a marked effect on net pay.

Increases to auto-enrolment levels have been timed with the usual indexation process for the personal allowance, income tax and NIC bands. This can mask the effects on take home pay, in particular of the rise from 2% to 5% for auto-enrolment contributions for many employees from April.

What this means in practice to different taxpayers is demonstrated below.

How does it work?

The following examples are based on the personal allowance of £12,500 for 2019/20 and lower, primary and upper earnings limits of £6,136, £8,632 and £50,000 respectively.

Employee automatic enrolment pension contributions are assumed to be 3% of band earnings in 2018/19 and 5% in 2019/20, adjusted for all available tax relief (based on tax rates for UK excluding Scotland).

Take three employees in a firm in England at different earning levels:

- 1. Tom is on his second job, earning £27,000 a year (close to average weekly earnings).***
- 2. Claire is his manager and earning £50,000 a year (at the UK excluding Scotland higher rate tax threshold).***
- 3. Ash is Claire's colleague in another department, earning £60,000 a year.***

Tom earning £27,000 a year

	2018/19	2019/20
Basic rate tax	(£27,000 - £11,850) @ 20% = £3,030.00	(£27,000 - £12,500) @20% = £2,900.00
NICs 12%	(£27,000 - £8,424) @ 12% = £2,229.12	(£27,000 - £8,632) @12% = £2,204.16
AE (net of 20% tax relief)	(£27,000 - £6,032) @ 2.4% = £503.23	(£27,000 - £6,136) @4.0% = £834.56
Total deductions	£5,762.35	£5,938.72
Change in net pay		-£176.37 (-0.83%)

Tom will end up with £620.70 more in his pension once his employer's higher contribution is taken into account, but with £176.37 less to spend.

Claire earning £50,000 a year

	2018/19	2019/20
Basic rate tax	(£46,350 - £11,850) @ 20% = £6,900.00	(£50,000 - £12,500) @20% = £7,500.00
Higher rate	(£50,000 - £46,350) @ 40% = £1,460	NIL
NICs 12%	(£46,350 - £8,424) @12% = £4,551.12	(£50,000 - £8,632) @12% = £4,964.16
NICs 2%	(£50,000 - £46,350) @2% = £73.00	NIL
AE (net of tax relief)	(£46,350 - £6,032) @1.8% = £725.72	(£50,000 - £6,136) @4% = £1,754.56
Total deductions	£13,709.84	£14,218.72
Change in net pay		-£508.88 (-1.40%)

Claire's salary means she will no longer benefit from higher rate relief on her pension contributions and she sees a significant change in her net pay. Over £1,490 more goes into her pension, but her net pay drops by nearly £43 a month.

Ash earning £60,000 a year

	2018/19	2019/20
Basic rate	(£46,350 - £11,850) @20% = £6,900.00	(£50,000 - £12,500) @20% = £7,500
Higher rate	(£60,000 - £46,350) @40% = £5,460.00	(£60,000 - £50,000) @40% = £4,000
NICs 12%	(£46,350 - £8,424) @12% = £4,551.12	(£50,000 - £8,632) @12% = £4,964.16
NICs 2%	(£60,000 - £46,350) @2% = £273.00	(£60,000 - £50,000) @2% = £200
AE (net of 40% tax relief)	(£46,350 - £6,032) @1.8% = £725.72	(£50,000 - £6,132) @3% = £1,315.92
Total deductions	£17,909.84	£17,980.08
Change in net pay		-£70.24 (-0.17%)

Ash benefits from higher rate relief on contributions, which strangely means that his reduction in net pay is closer to Tom's than Claire's, while his increased total pension contributions before tax relief are the same as Claire's.

Squeezed in the middle

Each of them will find their take home pay affected, but Claire, the middle earner, suffers the biggest loss because:

- > Her gross contribution rate increases by 66%;
- > She loses higher rate tax relief on all her pension contributions;
- > She is caught by the full increase in the AE contribution upper limit of £3,650; and
- > She also suffers the same £3,650 increase in the upper earnings limit for full rate (12%) NICs.

It's always worth ensuring that you understand your exact position when it comes to the intricate interaction of your tax and pension contributions.