

Salary sacrifice to super

Introduction

A way to boost retirement savings and reduce your tax bill is to salary sacrifice into superannuation. This practice is popular as people have become aware of the need to accumulate funds for retirement and that superannuation represents a tax-effective vehicle for savings. There are some facts however that you should consider prior to sacrificing your income into super.

How does salary sacrifice work?

In general terms, you enter into a superannuation salary sacrifice agreement (SSA) with your employer to forego a nominated amount of income in return for which your employer will make a contribution of that amount to your super fund on your behalf.

Instead of the income being taxed at your marginal tax rate (plus Medicare levy), the monies paid into super will be taxed at 15% on entry. Further, while accumulating, your investment earnings in super are taxed at only 15%. The effect of ongoing contributions and compounding returns in a concessional tax environment is an enhanced financial position at retirement.

How much can you salary sacrifice?

While in theory it may be possible to salary sacrifice 100% of an employee's salary, several issues affect the amount of superannuation that can be or should be contributed.

Contribution caps

Concessional contributions (which include superannuation guarantee (SG) and salary sacrifice contributions) are capped at \$50,000 per annum per person; with a limit of up to \$100,000 applying for those turning age 50 at any time up until 2012.

Amounts contributed above the limits will be subject to a penalty tax of 31.5% (which is in addition to the 15% contributions tax); and will also count towards the non-concessional (personal) contribution limit. Employees will need to monitor their contributions to ensure the caps are not exceeded.

Employer limits

The ability to salary sacrifice is at the discretion of the employer. Though most employers attempt to accommodate each employee's wishes, some still limit how much (if any) they allow to be placed into superannuation.

Employers can claim a tax deduction for the full amount of a super contribution made on behalf of an employee.

Superannuation guarantee

When you reduce your salary under a SSA it removes the legal obligation of your employer to pay superannuation guarantee (SG) contributions at your pre SSA level of salary. While most employers will continue to pay contributions based on the higher salary level, this should be confirmed with your employer in advance of entering a SSA.





Maintaining salary package entitlements

In reducing your salary through a SSA you should also ensure that the SSA preserves your entitlements to bonuses, leave payments and possible redundancy or termination packages.

Confirmation that your pre salary sacrifice base salary is to be used for the calculation of these entitlements should be documented as part of the SSA.

Other considerations

Access to funds restricted

It is important to remember that all contributions into super are preserved. That is, you will not be able to access the funds until you meet a condition of release, such as permanent retirement over age 55.

Taxation on withdrawal

Upon their withdrawal, salary sacrificed contributions may be subject to further tax. While there is no tax on lump sums and pension income for those over age 60 years, there will be tax implications for those making withdrawals from super prior to reaching age 60.

Alternative investments and structures

Investing in super can allow you to diversify your investments. However salary sacrificing into super means forgoing the opportunity to invest in other types of investments, through other legal structures or paying down debt (eg home loan). The differences should be quantified and appreciated.

Who would it suit?

The taxation benefit of salary sacrificing comes from comparing your marginal tax rate with the 15% tax rate applied to the contribution. It follows then that those with a higher marginal tax rate will generate a greater benefit.

Salary sacrificing would also suit:

- Those accumulating retirement savings over a period of time
- Those with excess income
- Combined with a transition to retirement income stream, it can provide a better income-tax position.

Salary sacrifice to super needs to be considered on an individual basis, so please talk to your financial planner.

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