

Transition to retirement and salary sacrifice

What is it?

This strategy involves directing part of your salary into superannuation and replacing that salary with income from a transition to retirement (TTR) income stream. The TTR income is funded by your existing super balance. To implement this strategy you must have reached what is referred to as your preservation age (currently 55) and be eligible to salary sacrifice into super.

What are the benefits?

- A TTR and salary sacrifice strategy may reduce the level of income tax paid due to the difference in your marginal tax rate (which may be as high as 46.5%) and the super tax rate of 15%.
- The investment earnings on your super balance (that is used to support the payment of your TTR income stream) are tax free.
- You are able to cease the income stream and salary sacrifice contributions and roll your super balance back to accumulation phase.

How does it work?

The tax saving arises because part of your salary, that would ordinarily be taxed at your marginal tax rate, is directed into super where it is subject to contributions tax at a reduced rate of 15%. Your income requirement is supplemented by drawing additional income in the form of a TTR income stream.

The level of tax payable on the super income stream will depend on a number of factors including your age and the specific taxation components of your TTR income.

Where you are aged over 60 you will not pay any tax on the super income stream. Where you are aged between 55 and 59 the taxable portion of the income stream will be subject to a 15% tax offset.

The higher the marginal tax rate of the individual the greater the tax saving that is achieved as a result of this strategy. The strategy is maximised where you are age 60 or over as a result of the tax free status of super benefits.

Are there any restrictions?

Lump sum withdrawal

Despite having the ability to receive your super balance as an income stream, you should be aware that, generally, you do not have the ability to make lump sum withdrawals until you permanently retire or reach age 65.

Minimum and maximum drawdown

The level of income you must draw each year from your TTR income is set between a minimum of 4% and a maximum of 10% of your account balance.

Contribution caps

For those who are age 50 in a financial year, concessional contributions (which include superannuation guarantee (SG) and salary





sacrifice) are capped at \$50,000 per person per annum up until 30 June 2012. After this, the concessional contributions cap will be reduced to \$25,000 per annum (indexed).

Amounts contributed above the cap 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 contribution cap.

Tips and traps

Superannuation guarantee

When you reduce your salary under a salary sacrifice agreement (SSA) it removes the legal obligation of your employer to pay 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 into 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.

Strategy in action!

Sally is 55 years old, earning a gross salary of \$150,000 and has accumulated \$400,000 in super. Prior to implementing the strategy Sally's net income is \$103,300 (this is the level of income required to fund her living expenses).

Sally is able to retain the same level of income when implementing a TTR and salary sacrifice strategy by electing to salary sacrifice \$34,942 into super and withdrawing \$28,000 from her TTR income stream. The tax saving (personal and contributions tax) by implementing this strategy is \$1,702 in the first year.

If Sally were aged 60 she would be able to contribute \$36,500 to super and still maintain her net income. Under this scenario the total tax saving would be \$8,943 due to the TTR income being tax free in her hands.

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How to Contact Centric Wealth Advisers Ltd

Level 2, 7 Macquarie Place
Sydney NSW 2000
PO Box R1851
Royal Exchange NSW
1225
Tel 02 9250 6500
Fax 02 9252 2702

Level 27, 150 Lonsdale
Street
Melbourne VIC 3000
Tel 03 9639 4848
Fax 03 9639 4343

Level 8, 120 Edward
Street
Brisbane QLD 4000
GPO Box 915
Brisbane QLD 4001
Tel 07 3230 6555
Fax 07 3221 2145

Level 1, 8 Phipps
Close, Deakin
Canberra ACT 2600
PO Box 3637
Manuka ACT 2603
Tel 02 6281 1477
Fax 02 6281 1476

www.centricwealth.com.au

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