Salary sacrificing: get to grips with rule change

JAMES GERRARD

The new financial year has kicked off and stricter super rules are now in force. During the past few weeks, many people have asked how these changes will impact their salary sacrifice arrangements.

It's a tricky area that is hard to get right as several things can impact the super contribution total at the end of the financial year. Salary sacrifice is a way to contribute to super from your pre-tax salary and remains one of the last tax breaks. This is what you need to know so that you don't get caught out by the new rules.

Until July 1 this year, for those over the age of 50 you could contribute up to $35,000 into super as pre-tax contributions that were taxed at 15 or 30 per cent depending on income levels. A potential problem will now occur for many people this financial year given the pre-tax super cap has decreased to $25,000. Crucially, you must also realise that the pre-tax super limit always includes your employer's 9.5 per cent compulsory contributions.

Salary sacrificing is usually implemented as an automatic deduction organised by payroll. For those previously salary sacrificing up to the $35,000 cap, they will need to contact payroll and request the salary sacrifice amount be reduced to reflect this year's lower cap. Otherwise they may potentially breach the cap if they follow last years' contribution pattern.

In terms of calculating out how much you can salary sacrifice each pay, Nishith Shah, certified practising accountant from SBX Accountants, says one way to do it is to ask your payroll area to crunch the numbers for you. "In some companies, if you ask, the payroll or human resources area will calculate how much you can salary sacrifice into super so that you stay under the cap based on your expected employer contributions. This can be a good approach as you put the onus and responsibility on your employer to get it right for you."

There are several other things to keep in mind when calculating super contributions.

- The 27 fortnight year: Certified practising accountant Luke Star, from Star and Associates, says: "Working out salary sacrifice amounts is not always as straight forward as it seems. For example, if you're paid on a fortnightly basis, in some financial years there will be 27 pay periods instead of 26. So for those who base their salary sacrifice calculations on the usual 26 pay periods, the extra pay period can potentially trip them up and push them over the cap."
- Super payments on bonuses and commissions: Shah says: "Generally bonuses and commissions paid are subject to superannuation payments. As such, if the payments vary in nature, so will the superannuation component, which may throw out the numbers when calculating how much to salary sacrifice. In other cases, some people simply forget to include super on bonuses and commission and end up salary sacrificing too much."
- Super contribution timing: Employers are required to pay super contribution, at latest, one month and 28 days after the end of each quarter. Some pay super each pay period while others pay either monthly or quarterly.

Luke Star says timing issues can affect super caps. For instance, super payments accrued between April to June may only be paid by the company in July, and so they are included in the super cap for the following financial year. This means that the employee does not start the financial year with a nil super cap balance as they may think. At the other end they may end up with cap issues if they are trying to maximise salary sacrificing.

The next move

One simple idea is to keep a close eye on your cumulative contributions in your super fund as the year goes on.

An alternative strategy is to start low and top up later in the financial year. Shannon Bernasconi, MD of WealthO2, which provides technology services in the super sector explains: "We see people salary sacrifice for the first nine months of the year based on a lower self-imposed cap, say 20 per cent below the actual cap. Then in the last quarter of the financial year, they review their cap position and adjust salary sacrificing higher to top up super contributions toward the maximum cap."

If you go over the pre-tax cap, penalty tax is payable on the excess based on your marginal tax rate less an offset to take into account super tax already paid. Sydney-based adviser Richard Johnsson says: "If you're on a high income and exceed the $25,000 cap, you could lose up to 47 per cent of that super contribution to tax."

Penalty taxes on super can be a mixed blessing for others as it may be as a result of their employers paying them above the minimum super required. Known as the maximum contribution base, it affects high-income employees who earn over $211,040 per year.

Star says: "For these people, their employers can choose to limit their 9.5 per cent super contributions to $20,048.80 regardless of their actual income received. In other words, for someone who earns $300,000 employment income, the employer can choose to pay 9.5 per cent super on it which would equal $28,500, or can limit super contributions to the maximum contribution base amount of $20,048.80."

One last thing: One of the few flaws in salary sacrifice — the fact employers could sidestep some of their obligations in relation to compulsory contributions when an employee used the process — is no longer going to be an issue as the government has moved to close this loophole. This is a very good development and not a moment too soon.

James Gerrard is the principal and director of privately owned Sydney financial planning firm FinancialAdvisor.com.au

Brycki's money is on robo-advice

MY WAY

It makes investing simpler, says the Stockspot boss

RICHARD FERGUSON

Chris Brycki is the man behind Stockspot, one of Australia's first companies to offer what has come to be known as "robo-advice". Stockspot recently made headlines after Graham Tuckwell, the Australian tycoon behind London-based ETF Securities became an investor. Brycki first came to the market's attention in 1999 when as a schoolboy he became one of the youngest winners of a stock competition.

How does robo-advice actually work and how is it different to seeing a regular adviser?

The most important thing when investing is getting your asset allocation right. Not so much picking stocks or when you should be getting in or out of the market. Working out what assets you should be investing in will determine 90 per cent of the variability of your results.

Professionals tend to focus on their own little speciality area like shares. In contrast Robo advice helps people actually focus on the asset allocation side. Costs are also one of the biggest drivers of your returns, so automating it offers a much lower cost.

If you give people too much control over their investments they make mistakes due to behavioural bias. They pull out at the wrong time, they choose the wrong stocks ...

Giving people too much control is a bad thing. We don't encourage our investors to weight their portfolios to particular assets like oil. We also know investors are likely to chase things that have been popular in the past, but that doesn't guarantee they'll do well.

JAMES CROUCHER

Chris Brycki says 'robo-advice has been the fastest growing form of investing'

'My money is invested in Stockspot because I believe index investing is the best way to do business. It has discipline; it takes the emotion out of investing'

CHRIS BRYCKI
FOUNDER & CEO, STOCKSPOT

A lot of younger investors are wary of ETFs on ethical grounds. What is Stockspot doing to tackle that?

It's something that all robo-advice companies are dealing with. We give customers the ability to add "themes" to their portfolio. So we control the core, but consumers have some control over what's added and then we "risk manage" it for them. Some of the themes include ethical shares, dividend shares, and global property.

It must difficult to sell robo-advice to some consumers, especially older investors.

Everyone reads the press and decides they have an edge over the market, that their information is unique. But everyone is seeing the same information and doing the same thing. The only way people learn is by losing money.

How did Stockspot begin?

I founded Stockspot in 2013. My background was as a fund manager at UBS and a couple of hedge funds, and I saw that there was a great opportunity to help consumers make better decisions. And to do it online.

I was working on my own for the first year. I built the project, got partners on board, brought it to market myself. Over the last few years, we've grown to 10 staff.

What was your first big investment?

I started investing when I was 10 or 11. My father gave me $1000 and said, "Chris, pick a stock to invest in." I spent weeks researching and I bought a small mining share which I followed very carefully. I eventually sold it and went to my father for the return. To my shock, he told me he never actually made the investment. It was just an exercise.

So your dad set you up?

He set me up, yeah (laughs). I made the decision then to trust my own instinct, not just my dad.

I entered all the shares competitions in high school and university, so I spent a lot of time trading as a teenager and that led to me joining UBS as a graduate.

Why did you decide to take the risk and jump out of UBS?

From a business perspective, having worked for a big organisation, I saw a tidal wave of change heading towards the industry. It started to realise a lot of it could be automated, they don't need to employ that many people.

A lot of countries are more advanced in this phase than Australia, but I wanted to be on the other side of the change. Personally, I thought it was a great chance to take what I'd learned at UBS and become an entrepreneur.

Are we going to see more advisers move to robo-advice?

That's definitely the trend globally. Around the world, robo-advice has been the fastest growing form of investing. It's a case of two global trends coming together: investors turning to services online and more index investing.

Australia is a little bit behind in the adoption of both of those. We're well behind places like Britain, the US and Canada in embracing ETFs. And we're also behind on adopting digital services generally.

What should we do to catch up?

We need to make financial services a lot more transparent. Investors are generally quite apathetic and they're even more apathetic if it takes a large effort to figure what they need to do to make the best investments. If we make the industry more transparent, we're likely to encourage more, and better, investing.

What are your current investments?

My money is invested in Stockspot because I believe index investing is the best way to do business. It has discipline; it takes the emotion out of investing.

I don't believe anyone who isn't active trading full time can do it effectively and in a good risk-adjusted way. I was fortunate to buy a property in 2009 in the depths of the financial crisis. I lived it in for a couple of years but sold it to invest the money in Stockspot.

But I do believe that people should have a diversified portfolio. A lot of Australians have too much weighted in one area.

Make the changes to transition to retirement plans work for you

MONICA RULE

Many investors initially wrote off the benefits of transition to retirement income streams after the cutbacks in superannuation concessions announced by Scott Morrison in this year's budget, but they remain very valuable to a segment of the population.

Although earnings from assets supporting a TRIS are no longer exempt from tax, a TRIS is the only way to access your superannuation savings while you are still working. (This is provided you have reached your preservation age, which is the minimum age that you can access your super.)

The preservation age is 55 for anyone born before July 1, 1960; 56 for those born on or between July 1, 1960, and June 30, 1961; 57 for people born on or between July 1, 1961, and June 30, 1962; 58 if you were born on or between July 1, 1962, and June 30, 1963; 59 for those born on or between July 1, 1963, and June 30, 1964; and 60 if you were born after June 30, 1964.

There are limits on the minimum and maximum amounts of TRIS you can access from your superannuation fund each year. The minimum amount is based on your age at July 1 and is a percentage of your TRIS account balance.

Again, the way this all works is through scales.

If you are aged 55 to 64, the minimum amount you can access is 4 per cent. For those aged 65 to 74 the minimum amount is 5 per cent. The minimum amount increases to 6 per cent for people aged 75 to 79; and it is 7 per cent for people aged 80 to 84; 9 per cent for those aged 85 to 89; 11 per cent for those aged 90 to 94; and 14 per cent for anyone 95 or older.

AAP

TRIS remains valuable despite Scott Morrison's changes

If your TRIS begins during the year, then the minimum amount will be calculated on a pro rata basis from the starting date.

The minimum amount is rounded to the nearest $10. The maximum amount is 10 per cent of your pension account balance and this is not calculated on a pro rata basis.

TRIS is paid as a non-commutable income stream, which means you cannot convert it to a lump-sum superannuation benefit until you reach the age of 65 or meet another condition of release.

The key advantage of a TRIS remains in place: you can cut down on your working hours and maintain the same level of total income by supplementing what you no longer receive as salary with a TRIS from your super fund.

You still may continue to make contributions into your fund once you start a TRIS.

You could consider setting up a salary sacrifice arrangement (see today's feature on this page by James Gerrard) by putting your salary into your fund and replacing the sacrificed salary with a TRIS from your fund.

This is really working the superannuation system to your advantage.

Yes, it is complex, but by doing this your fund pays 15 per cent on the sacrificed salary received instead of you personally paying tax at your marginal tax rate, which may be higher.

You will need to consider the new concessional contributions cap of $25,000 a year if you do this.

Another strategy you may consider is to receive a TRIS income stream and recontribute it back into your fund as non-concessional contributions.

This will allow you to increase the tax-free portion of your superannuation savings in your fund.

You will need to consider the new non-concessional contributions cap of $100,000 a year, or if you are under 65 you could use the bring-forward rule and contribute a total of $300,000 in one year or across three consecutive financial years.

This is provided your total superannuation balance is below $1.6 million as at June 30 this year and you do not exceed the non-concessional contribution eligibility thresholds

The bring-forward rules remain in place just like the entire TRIS system remains in place; it's just that the numbers have changed.

Monica Rule is an SMSF specialist.

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