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# Salary sacrifice amounts and SG changes

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28/11/2019

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From 1 January 2020 employers will also be required to provide superannuation guarantee ('SG') support on the amount of employee salary sacrificed contributions under salary sacrifice arrangements ('SSA'). This article examines this change that was recently made by the *Treasury Laws Amendment (2019 Tax Integrity and Other Measures No. 1) Act 2019* (Cth) ('Act'), which received royal assent on 28 October 2019, to the *Superannuation Guarantee (Administration) Act 1992* (Cth) ('SGAA').

## What is a superannuation salary sacrifice arrangement?

Broadly, a superannuation SSA involves an employee entering into an arrangement with their employer to forego a certain amount of their future salary and wages in lieu of the employer contributing the sacrificed amount into the employee's superannuation fund.

Sacrificed contributions are deductible for the employer and are not included in the assessable income of the employee (subject to the possibility of the employee exceeding their concessional contributions cap).

Salary sacrificed amounts, like other employer contributions, are generally taxed at 15% in the superannuation environment. If the employee's adjusted taxable income including concessional contributions exceeds $250,000 in a financial year, an additional 15% tax under division 293 of the *Income Tax Assessment Act 1997* (Cth) ('ITAA 1997') may apply to the extent the employee's concessional contributions exceed the $250,000 threshold.

A SSA may, in certain cases, prove more beneficial for an employee seeking to boost their superannuation compared to an employee paying tax on salary or wages at marginal tax rates plus levies and then making a personal superannuation contribution.

Note from 1 July 2017, an employee can claim a personal deduction for a concessional contribution even though they derive more than 10% of their income from employee activities provided the deduction does not give rise to a loss. As a result of changes to income tax rules from 1 July 2017, it is now easier for employees to claim a tax deduction for personal contributions they make to a superannuation fund.

Accordingly, personal contributions may be an attractive option compared to salary sacrifice contributions as this allows the employee to derive their usual salary (especially if the employer did not provide any flexibility to salary sacrifice) and then reduce their taxable income by making personal deductible contributions.

However, SSAs are still considered worthwhile due to the reduced administration associated with personal deductible contributions (eg, the notice requirements under div 290-C of the ITAA 1997) and will no doubt continue to be a popular tool for boosting superannuation savings.

## Background on the SG regime

Broadly, the SG regime requires employers to make superannuation contributions for their employees of at least the minimum level of superannuation support set out in the SGAA.

Since mid-2014, the SG rate (ie, the rate applied to the employee's ordinary times earnings ('OTE') to determine the employer's minimum SG contributions) has been frozen at 9.5%. This rate is scheduled to increase to 10% in July 2021 and then will annually increase by 0.5% to ultimately reach 12% by July 2025.

Where an employer fails to pay the minimum level of superannuation contributions on behalf of an employee, as measured on a quarterly basis, the employer is liable to pay the SG charge on their SG shortfall plus certain administrative and penalty amounts.

## The current salary sacrifice SG regime

To illustrate the gap under the current regime, consider the following scenario:

Tony receives a salary from his employer for his ordinary hours of work of $100,000 per annum. His OTE for SG purposes is $25,000 per quarter. Tony would have an entitlement to $2,375 in SG contributions per quarter, which is determined by multiplying $25,000 by 9.5% (the current minimum SG rate).

Tony enters into a SSA with his employer to sacrifice $2,000 each quarter from his salary and wages with the intention that Tony's employer contributes this sacrificed amount to his nominated superannuation fund on top of the employer's mandated SG obligation. Accordingly, Tony expects that the total concessional contributions made on his behalf to his fund will rise to $4,375 per quarter.

Under the current SG regime (ie, prior to 30 June 2020), Tony's employer can use any salary sacrificed super contribution (eg, $2,000 per quarter) to partly satisfy their minimum SG obligations.

Additionally, the employer's mandated SG obligations would be calculated based on an adjusted OTE base which excludes any sacrificed amounts — ie, $23,000 instead of $25,000 (ie, $25,000 minus the salary sacrifice amount) per quarter.

Thus, Tony's employer is only obliged to pay SG contributions of $2,139 per quarter (ie, $23,000 x 9.5% = $2,139), and only $139 of this amount would be on top of his quarterly salary sacrificed amount.

Tony's super account balance is likely to be much less in this scenario than he would expect. Indeed, Tony may not even realise there is any issue and he may not even check on his superannuation fund.

In the report *Overdue: Time for Action on Unpaid Super* released by Industry Super Australia in December 2016, it was estimated that the total amount of unpaid SG for FY2014 would be $1 billion or higher if employee salary sacrifice contributions were excluded.

However, this figure has been contested by others. For instance, in the Federal Government's Superannuation Guarantee Cross-Agency Working Group's interim report released in January 2017, it was suggested that the practice of employer's exploiting this gap in the SG regime was not widespread and the above stated figure of $1 billion is likely to be a very large overestimate.

Nevertheless, the Superannuation Guarantee Cross-Agency Working Group recommended that the gap in the regime be addressed and on 14 July 2017, the then Minister for Revenue and Financial Services, the Hon Kelly O'Dwyer MP, announced that the Government would amend the SGAA to address this issue.

## The new SG regime

The changes to the SGAA effective from 1 January 2020 ensure that:

- employer contributions made as part of a SSA do not count toward the amount of SG contributions that an employer is required to make in order for them to avoid an SG shortfall/charge; and
- salary sacrificed super contributions do not reduce the employee's base earnings used to calculate an employer's SG obligations.

The Act introduces a number of new provisions to the SGAA to implement this change. In particular, the Act inserts a new interpretation provision in s 15A of the SGAA, titled 'Interpretation: salary sacrifice arrangements', which contains the following:

**15A Interpretation: salary sacrifice arrangements**

Salary sacrifice arrangement

(1) An arrangement under which a contribution is, or is to be, made to a complying superannuation fund or an RSA by an employer for the benefit of an employee is a ***salary sacrifice arrangement*** if the employee agreed:

(a) for the contribution to be made; and

(b) in return, for either or both of the following amounts to be reduced (including to nil):

(i) the ordinary time earnings of the employee;

(ii) the salary or wages of the employee.

(2) If an amount mentioned in subparagraph (1)(b)(i) or (ii) is reduced under a salary sacrifice arrangement, the amount of that reduction is:

(a) if ordinary time earnings for a quarter are reduced—a ***sacrificed ordinary time earnings amount*** of the employee for the quarter in respect of the employer; and

(b) if salary or wages for a quarter are reduced—a ***sacrificed salary or wages amount*** of the employee for the quarter in respect of the employer.

Excluded salary or wages

(3) In working out the amount of a reduction for the purposes of subsection (2), disregard any amounts that, had they been paid to the employee (instead of being reduced), would have been excluded salary or wages.

(4) For the purposes of this section, excluded salary or wages are salary or wages that, under section 27 or 28, are not to be taken into account for the purpose of making a calculation under section 19.

In determining an employer's SG shortfall for an employee for a quarter, the following new formula is used (SGAA s 19(1)):

$$\begin{array}{c}\text{Quarterly salary or wages base,}\\ \text{for the employer in respect of the employee,}\\ \text{for the quarter}\end{array} \times \frac{\begin{array}{c}\text{Charge percentage for}\\ \text{the employer}\\ \text{for the quarter}\end{array}}{100}$$

In calculating 'quarterly salary and wages base' in the above formula, the Act includes the following definition in the SGAA:

***quarterly salary or wages base***, for an employer in respect of an employee, for a quarter means the sum of:

(a) the total salary or wages paid by the employer to the employee for the quarter; and

(b) any sacrificed salary or wages amounts of the employee for the quarter in respect of the employer.

Thus, under the new law, an employer must include any sacrificed amount to work out their SG obligation to the employee (and therefore any applicable SG shortfall). This ensures that an employee's SG obligations are calculated on the employee's pre-salary sacrifice base and not on the employee's reduced salary and wages (ie, post-salary sacrifice).

Further, under the changes to s 23(2) of the SGAA, an employer's SG charge, which arises if they have not met their mandated SG obligations, will only be reduced if the employer makes a contribution other than a sacrificed contribution. A sacrificed contribution means 'a contribution to a complying superannuation fund or an RSA made under a SSA'.

## The scenario under the Act

Revisiting the scenario above with Tony, the following will occur under the Act from 1 January 2020:

Tony's quarterly salary or wages is $25,000. Tony enters a SSA with his employer and sacrifices $2,000 to super per quarter.

For Tony's employer, the formula in s 19(1) of the SGAA provides that in working out the employer's SG shortfall, it is now calculated in respect of Tony's quarterly salary or wages base which in turn is worked out by totalling Tony's total salary or wages for the quarter, $23,000, plus any sacrificed amounts for the quarter, $2,000, which equals $25,000.

Tony's employer would be required to pay the full amount of $2,375 in minimum SG contributions per quarter based on his OTE remuneration on top of any sacrificed amounts made on Tony's behalf pursuant to his SSA. If the employer were to make quarterly SG contributions less than $2,375, Tony's employer would have an SG shortfall.

The new provisions make it clear that salary sacrifice amounts cannot be used to reduce an employer's mandated SG obligations from 1 January 2020.

## Review and conclusions

From 1 January 2020, the above measure will ensure that any salary sacrificed superannuation amount is included in each employee's SG calculation. It is therefore recommended that employees and employers examine their current documentation and arrangements to determine what changes are needed.

The following considerations should be borne in mind:

- How future scheduled increases to the SG rate are to be handled (ie, will the employer pay in addition to the salary and wage amount under the employment contract or is the additional SG amount part of the employee's total remuneration package which may reduce salary and wages or other benefits?). Many employment contracts do not integrate that well with the SG regime especially with the legislatively enshrined SG increases which will rise to 12% from mid-2025. In particular, you should check whether the employment contract and SSA are appropriately drafted and do not conflict with each other.
- Are the remuneration and SSA documents consistent with the current (reduced) contribution caps and other superannuation changes (eg, will an employee run up a division 293 additional 15% tax on some or all of their concessional contributions if they exceed the $250,000 threshold).

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This article is for general information only and should not be relied upon without first seeking advice from an appropriately qualified professional. The above does not constitute financial product advice. Financial product advice can only be obtained from a licenced financial adviser under the *Corporations Act 2001* (Cth).

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21 November 2019

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