HIGHER PAID EMPLOYEE CONTRIBUTIONS INFORMATION FOR PAYROLL

Higher paid local government employees may exceed the concessional contributions cap due to the higher contributions required under the Local Government Act.

What are concessional contributions?

Concessional contributions are super contributions from income that tax has not already been paid on. They include employer contributions, salary sacrifice contributions and contributions claimed as a tax deduction. Concessional contributions are subject to 15% contributions tax on entry to super.

An additional 15% tax applies to concessional contributions if an employee's total income is more than $250,000. Total income is defined in a similar way to that for Medicare levy surcharge purposes.

Concessional contributions cap

The Australian Government caps concessional contributions. The annual concessional contributions cap is currently $25,000 for all individuals.

Carry-forward concessional contributions

It is possible to carry forward unused concessional contributions cap space amounts from 1 July 2018, if you have a total superannuation balance of less than $500,000 at the end of 30 June in the previous year. Unused amounts are available for a maximum of five years, and will expire after this. This means some employees may contribute more than $25,000 annually and not breach the contribution cap.

What happens if an employee exceeds the cap?

Concessional contributions above the cap will be taxed at the employee's marginal tax rate plus an excess contributions charge. The Australian Taxation Office (ATO) will send a notice detailing the employee's liability for additional tax and the charge. To pay the liability, your employee can elect for release of up to 85% of their excess concessional contributions to the ATO (15% contributions tax has already been paid). The ATO will refund any excess contributions released above the employee's liability. You can find out more from the ATO website at www.ato.gov.au.

Which employees are likely to exceed the concessional cap?

Those on higher salaries and with accumulation accounts (or defined contribution accounts) are most likely to exceed the concessional contributions cap. Higher employer contribution rates apply to local government employees under the Local Government Act, and this, combined with the requirement to make member contributions (with the option to salary sacrifice) increases the likelihood of exceeding the cap. You can work out if an employee is likely to exceed their cap by doing this calculation:

Concessional cap

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Total contribution % rate*

***Employer contribution rate plus salary sacrificed member contribution rate e.g. 12% + 6%**

If the result of this calculation is less than your employee's annual salary it is likely they will exceed the concessional contributions cap. Any extra contributions the employee salary sacrifices or claims a tax deduction for also count toward the cap.

What are my employee's options?

The Local Government Act allows employees who will exceed the cap to limit concessional contributions to the amount of the cap and take any additional amount as salary.

Employers can form an agreement with their higher paid employees regarding the employer and member contribution rates that apply. This arrangement cannot be used to reduce an employee's super contributions below the concessional contributions cap for the year. Contributions can only be reduced to the cap.

The legislation specifically prescribes that the 'amount of the reduction must be paid by the employer to the employee as salary'. This means that the employee's total employment cost (TEC) remains the same with less being paid into super and correspondingly more paid as salary.

This legislation does not apply to members with a Defined Benefit account.

Do the superannuation guarantee rules apply?

Employers must still meet the minimum quarterly superannuation guarantee (SG) contribution requirements. This is 9.5% of ordinary time earnings, with the option to restrict contributions to the maximum contribution base based on a salary of $57,090 per quarter (for 2020/21).

Also, ensure you consider that with less of the employee's TEC being paid in super, their salary will increase. Your SG obligations are based on the increased salary.

Can't we just stop contributions once the cap is reached?

You will still need to meet SG contribution requirements each quarter, at a minimum. This means you can't stop contributions completely for an entire quarter or longer period. If a contribution cap agreement is implemented during a financial year, this measure will help but may not stop the employee from exceeding the cap.

Over a full financial year, this measure should stop the employee from exceeding the cap (unless they make voluntary salary sacrificed superannuation contributions).

Would it help if employees made their contributions after tax?

If employees choose to make their member contributions from after-tax pay, these would not count towards their concessional cap. Instead, they would count towards the annual non-concessional contributions cap, which is much higher and capped at $100,000 for the current financial year. The tax implications of this decision depend on the individual's personal circumstances. An additional consideration is the potential impact on the employee's take-home pay.

Employers cannot advise employees on the potential tax implications of applying the relief. LGIAsuper offers single issue financial advice on contributions at no additional cost to members and our representatives are available to talk to your employees.

How do I work out what the contribution rates will be?

The simplest way to work out how much to contribute on behalf of an individual is to calculate the dollar amount of contributions for each pay period. Based on 26 fortnightly pay periods, the calculation will be:

If salary and super contributions are paid fortnightly:

$25,000
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Number of pay periods in a year

$25,000 ÷ 26
= $961.53 per fortnight

Alternatively, if your payroll system requires a percentage figure you can use the calculation below for one year:

$25,000 ÷ salary

Example based on a salary of $150,000:

$25,000 ÷ $150,000 = 0.166
0.166 x 100 = 16.6%

The legislation does not specify what type of contributions this lesser percentage should be applied to although LGIAsuper would prefer that as far as possible the employer contribution be made in full and any additional contribution be made as standard member contributions.

Continuing with the example, you could make 12% as employer contribution and 4.6% as salary sacrificed standard member contributions. If this approach will not work for you, you can call us to discuss other possible solutions. Salary sacrificed contributions count towards the employer SG obligation. You should encourage your employee to obtain tax advice if they are unsure of the implications of this choice.

What if the employee wants to reduce contributions partway through the year?

The calculation for a part year, where the employer has already made concessional contributions in the year to date, is much more complex.

Considerations for part years:

- Employees can reduce their contributions to the concessional contributions cap but no lower.
- Take into account contributions already made during the current financial year.
- Ensure the minimum SG amount is contributed in each remaining quarter. This is 9.5% of ordinary time earnings, with the option to restrict contributions based on a salary of $57,090 per quarter (for 2020/21).
- If the calculated amount for the remainder of the year does not meet the minimum SG contribution, you will need to make the minimum SG contribution for that employee, even if it means they will exceed the cap.
- Ensure you calculate your quarterly SG obligation based on the employee's increased salary (which results from less dollars being paid into super).
- Ensure that the employee's TEC does not reduce as a result (as required by the legislation).

What if employees are making other voluntary contributions to super?

You cannot take into account any voluntary contributions your higher-paid employee is making when reducing contributions to the cap. The only contributions that can be reduced under this relief are the compulsory contributions mandated under the Local Government Act.

Any other salary sacrificed super contributions, personal contributions for which a tax deduction has been claimed or contributions from other employers, also count towards the concessional cap but cannot be addressed by this relief.

What do I need to do?

If an employee is likely to exceed the concessional contributions cap due to employer and standard/compulsory contribution rates, discuss the option to reduce their contributions.

If you reach an agreement, you should ensure it only benefits the employee to the extent that they reach the concessional cap.

It could be part of an employment contract, a form or letter — as long as it is signed by both parties and provides the following information:

- employee's name
- employee's superannuation fund
- date the agreement comes into effect and ends
- dollar amount of the contributions to apply
- period the amount of contributions will apply to.

See over the page for some suggested wording. Please note that this is a guide only and it is important to confirm the wording of the written agreement with your taxation and legal advisers.

The agreement will need to be revised if the concessional cap changes.

What if our systems can't do this?

We understand that payroll systems may not be able to automate this solution. We encourage you to determine ways you may be able to offer this to employees who request that their contributions be reduced to the cap.

You may consider manually calculating superannuation contributions for the small number of employees who wish to participate.

Any questions? Our team of Relationship Managers are available to assist with any questions relating to contribution caps. They can also meet with higher salaried employees and assist by providing information on contribution cap agreements. Please call **1800 444 396** to arrange a meeting today.

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Suggested wording for written agreement

Amend or redraft as you need - this is a suggestion only and it is important that you confirm the wording of the written agreement with your taxation and legal advisers.

Written agreement to reduce concessional contributions to the cap

I, <employee name>, request <employer name> to limit my superannuation contributions to $25,000 for the year ended 30 June 2020.

The agreement starts from the first pay run after <start date>.

I understand that if I begin this agreement partway through the year I may still exceed the cap as a result of contributions already made and required minimum superannuation guarantee contributions.

Contributions are currently based on my salary of <$salary>.

This agreement applies to the current financial year and future financial years, until I instruct my employer to cease and revert to the contribution rates prescribed in the Local Government Act, or until the contribution cap changes.

OR

This agreement applies only to the 2020/21 financial year, after which contributions will revert to the contribution rates prescribed in the Local Government Act.

Employee name

Superannuation Fund

Employee signature

Employer/manager name

Organisation name

Employer signature

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