How can retirement savings be increased without reducing take home pay?

Making voluntary contributions to superannuation may increase the value of a person's retirement savings and therefore the amount of funds they have at retirement. However some may not be able to afford the resulting reduction to their take home pay.

Who does this suit?	It works like this
This strategy is accessible to certain people who have attained their preservation age[1] and are still working.	A person using a TtR income swap strategy will concurrently: **1. Make voluntary concessional contributions to superannuation. This involves either:** – Entering into a salary sacrifice agreement with their employer whereby the employer contributes part of the employee's salary into their superannuation without deducting the income tax they would otherwise have done on this portion of their salary; or – Personally contributing funds to superannuation, advising their superannuation fund that they intend to claim a tax deduction (subject to various timeframes), then claiming the deduction when they submit their tax return. **2. Commence a TtR account based pension. This involves:** – Moving funds currently inside the superannuation environment from the accumulation phase to pension phase and drawing pension payments of between 2% and 10% each financial year. Once a condition of release is satisfied which generally occurs upon the earlier of attaining age 65, or fully retiring after attaining preservation age, the 10% maximum no longer applies. A tax arbitrage may result, as voluntary concessional contributions are taxed at 15%[2] within the annual limit of $25,000 (2020/21), and the income payments from the TtR pension are tax free if the TtR account holder is age 60 or over. If between preservation age and age 59, the tax-free portion of the pension payment is tax free and the taxable portion is taxed at marginal tax rates with a 15% offset. When the TtR income swap strategy is used correctly, the benefit of this tax advantage is reflected in a boost to the individual's overall superannuation balance.

1. Preservation age: https://www.ato.gov.au/rates/key-superannuation-rates-and-thresholds/?page=11
2. An additional 15% contributions tax applies to very high income earners, broadly those who earn more than $250,000.

Benefit

Increase the value of retirement savings without incurring a reduction to take home pay.

Example

What would be the result of Julia, who is age 62, currently working 40 hours per week earning salary of $80,000 p.a. with $200,000 in her superannuation, utilising a TtR income swap strategy?

The following compares 2 scenarios for Julia:

1. Compulsory superannuation guarantee	– Aside from the compulsory 9.5% superannuation guarantee she receives from her employer, Julia does not currently make any additional contributions to her superannuation. – She cannot afford a reduction to her after tax income of $2,423.58 per fortnight ($63,013 for the year).
2. TtR income swap strategy	– Julia salary sacrifices $669.23 per fortnight ($17,400 per year) which combined with her compulsory 9.5% superannuation guarantee of $7,600 ($80,000 x 9.5%) will fully utilise her concessional cap of $25,000 ($17,400 + $7,600). – Julia uses her $200,000 superannuation to commence a TtR account based pension and draws pension payments of $436 per fortnight ($11,336 per year). – This amount is between her 2% minimum of $4,000 and 10% maximum of $20,000.

For the 2020/21 financial year, the following table compares Julia's current situation with an alternate scenario if she elects to adopt the TtR income swap strategy.

	1. Compulsory superannuation guarantee	2. TtR income swap strategy
Salary	$80,000	$80,000
Salary sacrifice	$0	$17,400
TtR pension payments	$0	$11,336
Income tax (including Medicare)	$16,987	$10,923
After tax income	**$63,013**	**$63,013**
Net contributions to superannuation	$6,460	$9,914
Additional superannuation savings	**$0**	**$3,454**

For the 2020/21 financial year, by adopting the TtR income swap strategy:

- Julia maintains the same take home pay of $63,013 ($2,423.58 per fortnight). This is her salary, minus the amount she is salary sacrificing, plus the TtR pension payments, minus income tax (including Medicare).
- She has increased her superannuation savings by $3,454 ($9,914 - $6,460) which is the overall benefit of the strategy.

In this example, Julia benefits from tax free payments from her TtR as she is over age 60. If Julia was in fact aged 57 and did not have any tax-free component in her superannuation, she would need to draw pension payments of $14,158 to achieve the same take home pay. This would reduce the 2020/21 benefit of the strategy to $632.

As this illustrates, those who are age 60 or over are more likely to benefit from a TtR income swap strategy than those between their preservation age and age 59.

Take note

Prior to commencing a TtR income swap strategy, things for an individual to consider include:

- The impact of adopting a TtR account based pension on their financial situation.
- Ensuring that the $25,000 concessional contribution cap is not breached, otherwise penalties apply. A person's concessional contribution cap includes all of their voluntary concessional contributions (both salary sacrifice and personal contributions claimed as a tax deduction), and the compulsory 9.5% superannuation guarantee received from their employer on their salary.
- If making salary sacrifice contributions, determine whether there are any conditions imposed by the employer and whether this impacts the level of superannuation guarantee otherwise receivable.
- Individuals won't be able to access amounts contributed to superannuation until they satisfy a condition of release.
- Not everyone will benefit from adopting a TtR income swap strategy. A financial adviser will be able to determine whether this is likely to be tax effective and an appropriate strategy based on your personal circumstances.

Need help

For more information on how to save tax effectively for your retirement, please speak to me.

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