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Super concessional contributions: beware of going over the cap

If you are either an employee or a self-employed person and you top up your super by making deductible contributions, you need to be aware of not breaching the annual $25,000 concessional (before-tax) contribution cap. If that happens, your tax bill will increase, not to mention the administrative inconvenience you may face.

As an employee, your employer is obliged to pay you the 9.5% of Superannuation Guarantee Contributions (SGC), which count as concessional contributions. So if you are a high-income earner, especially, with more than one employer (eg, a doctor working for more than one hospital) you could risk going over the limit.

TIP: You could also be in danger of reaching the cap if you're an employee with salary sacrifice arrangements already in place from last year, when the annual concessional cap was higher ($35,000 or $30,000 depending on your age).

Given that the annual cap was lowered to $25,000 – regardless of age – from this year (2017–2018), it's advisable to review your current arrangements and adjust your contribution amounts so you don't inadvertently contravene the new lower cap.

What exactly are concessional contributions?

Concessional contributions are those made to a super fund out of an individual's pre-tax income and are taxed at 15%.

Generally, concessional contributions include:

- *your employer's super guarantee contributions*, that is, the compulsory 9.5% of your salary that your employer puts into your super;
- *salary sacrifice payments* you make to your super fund by entering into a salary sacrifice agreement with your employer;
- *personal contributions* for which a deduction has been claimed (typically if you're self-employed); and
- *insurance premiums and administration fees* when your employer paid those costs to your super fund on your behalf, rather than you having them deducted direct from your super fund.

What happens if your contributions are over the limit?

If you go over the $25,000 concessional contributions cap, whether deliberately or unintentionally, the ATO will send you an excess concessional contributions determination, which indicates that:

- The excess contributions will be included in your assessable income and you will be taxed at your marginal tax rate (plus Medicare levy).
- You will receive a non-refundable tax offset of 15% for your excess concessional contributions. This amount acknowledges the tax already paid by the super fund on those contributions.

TIP: Concessional contributions are taxed at 15% when received by your super fund.

You will need to pay an excess concessional contributions charge (ECC charge) at an approximate rate of 4.70% (the rate is updated quarterly). The ECC charge period is calculated from the first day of the income year to which the charge relates, ending on the day before the day on which payment is due under the first notice of assessment.

Making an election

When you receive the excess concessional contributions determination, you can choose to pay the tax bill from your own money, or use a release authority issued by the ATO to pay the debt using your superannuation money.

Before paying the debt, though, it's a good idea to contact us (or your superannuation fund) to confirm that there have indeed been excess contributions and the ATO determination is correct. There may also be a narrow possibility of challenging the excess based on “special circumstances” – speak to us first to evaluate your position.

The release authority allows you to use up to 85% of the excess concessional contributions from the superannuation fund to cover the additional personal tax liability. The election to release must be made in the approved form within 21 days of receiving the excess concessional contributions determination.

Once you send the election form to the ATO, the ATO will issue an excess concessional contributions release authority to the super fund you have nominated. The super fund must then pay the released amount to the ATO within seven days. This is a short timeframe, so trustees of self managed super funds (SMSFs) should ensure that they have sufficient cash to make these types of payments on time.

TIP: Administrative penalties will apply if you or your super fund fail to make a payment to the ATO.

Talk to us

There are various practical things you can do to keep an eye on your contributions and avoid paying additional charges. Talk to us today to find out more about how your financial situation could affect decisions about your super.

Greater transparency on fees is coming soon

Have you ever wanted greater transparency and comparability in terms of fees and costs you pay to invest in superannuation and managed funds? Well, Australian Securities and Investments Commission (ASIC) may have a solution for you. ASIC has identified inconsistencies with reporting and under-reporting of certain fees as key issues for consumers. From 1 October 2017, most product disclosure statements (PDSs) issued by superannuation funds and managed investment funds should conform to the enhanced disclosure requirements of RG 97.

Generally, under the updated RG 97, PDSs will need to include a standardised fees and costs template, certain additional explanations of fees and costs, an example of annual fees and costs, and a boxed consumer advisory warning. The standardised template should allow you to compare the fees and costs involved with products, quickly and easily, without having to trawl through different sections of the PDS.

In addition to the usual performance fees and management fees, the PDS must also include indirect costs, which are any amounts that may directly or indirectly reduce your return on the product. The indirect costs are usually calculated based on what was paid in the previous financial year and must be calculated and disclosed either separately (for super entities), or as a part of management costs (for managed investment funds).

It is hoped that such increased disclosure will remove hidden costs that can reduce the value of investments by stealth.

To further assist you, the following needs to be transparent:

- a worked example of the application of the fees and costs during a single year’s holding of the product;
- information such as material amounts paid or payable to related parties of the issuer;
- any conflicts of interest; and
- a breakdown of fees and costs.

ASIC has not specifically prescribed the form and content of the standardised fees and costs template, however, RG 97 for MySuper products contains a list of fees and costs, which must be disclosed in the template including the:

- investment fee;
- administration fee;
- buy-sell spread;
- switching fee;
- exit fee;
- advice fees relating to all members investing in a particular MySuper product or investment option;
- other fees and costs; and
- indirect costs ratio (indirect costs paid in the previous financial year over the total average net assets for the relevant financial year).

It is likely that other investment products will need to disclose similar fees and costs information to consumers. Where fees and costs involved may be variable, RG 97 notes that the amount should be shown as a range in the fees and costs template. However, calculations (ie, worked examples) must be based on the highest amount within the range.

At this stage not all PDSs issued after 1 October will have the enhanced disclosure features due to resistance from the industry. ASIC received feedback from across the industry citing challenges to the practical implementation of RG 97 by the deadline, despite six months’ notice since RG 97 was first released in March. In an attempt to placate the industry, ASIC has extended its facilitative compliance approach to fee and cost disclosure. ASIC will also work with an external expert to conduct a review of the reforms contained in RG 97 to ensure the objective of greater transparency for consumers is met in practice.

So transparency is coming, but it will be a slow process.

TIP: Your accountant who is a limited AFS (Australian Financial Services) licensee can provide you with more information and general advice.

Be alert to sham self managed super schemes

Have you been advised to transfer your super to a self managed super fund (SMSF)? Perhaps you have been told that you could withdraw your superannuation early, to pay off debt? Either could be a warning sign of an illegitimate scheme through which you could be in line for a fine, face a jail term and risk your entire super. Here we look at how to avoid such a scheme and what to do if you think you could be caught up in one.

The ATO has warned SMSF trustees to avoid the latest range of retirement planning schemes that deliberately target members who are close to retirement. Such schemes may at first appear legitimate (because they are structured in a way that seems to satisfy certain tax and regulatory rules), but could put members at risk of breaking the law. You might be lured by an offer to access your superannuation early, without concern to the general conditions of release. You could be asked to transfer your super from an existing fund to a self managed super, resulting in high fees and loss of valuable savings.

ATO Deputy Commissioner James O'Halloran has cautioned: "If a taxpayer becomes involved in any illegal arrangement, even by accident, they may incur severe penalties, jeopardise their retirement savings and risk losing their rights as a trustee to manage their own fund."

If you take part in such a scheme you may also be vulnerable to identity fraud, as it will no doubt involve you handing over your personal details. Such fraud may take years to recover from.

Crucially, setting up an SMSF and knowingly or unwittingly accessing your super early may leave you facing a fine of up to $340,000 and a jail term of up to five years, or fines of up to $1.1m for corporate trustees.

TIP: As part of its Super Scheme Smart program, the ATO has released information to highlight the warning signs and risks associated with such contrived schemes (see the ATO Super Scheme Smart webpage at: https://www.ato.gov.au/General/Tax-planning/Tax-avoidance-schemes/Super-Scheme-Smart/).

Latest schemes of concern to the ATO

SMSFs and property development

This type of scheme typically involves an SMSF subscribing for units in a unit trust that enters into a joint venture to develop a property on land owned by another entity (often a related party). The development profits may be split 50/50 between the unit trust and the other entity, despite the fact that the initial contribution by the unit trust to the venture represents less than 50 per cent of the total value. This attempts to channel more of the profits to the concessionally taxed super environment and boost the individual's retirement savings. However, the ATO considers that any eventual income distributed to the SMSF by the unit trust is subject to 45 per cent tax and could result in the ATO revoking the SMSF's complying fund status.

Granting legal life interest over commercial property to SMSF

This scheme is where the rental income from a commercial property is diverted to the SMSF, which is taxed at lower rates while the individual or related entity retains legal ownership of the property. A typical example will involve a small business owner using a deed to grant a life estate interest over business real property to their SMSF. While the value of the life interest is only a proportion of the property's value, the SMSF has full access to the commercial property and 100 per cent of the income it generates. The ATO warns that the rental income received by the SMSF may be subject to 45 per cent tax if the amount paid by the SMSF for the life interest is not a fair market value. This could also have implications for the members' non-concessional contributions cap, pension transfer balance cap, and could breach other rules.

Exceeding the contributions cap to reduce taxable components

Such a situation would arise where an individual deliberately exceeds their non-concessional contributions cap to manipulate taxable and non-taxable components of their superannuation interest upon refund of the excess.

Other suspect arrangements

The ATO is looking at other arrangements regarding the super caps and restrictions that apply from 1 July 2017, including:

- *Deliberate use of multiple SMSFs to manipulate tax outcomes*, eg, switching each of the respective funds between accumulation and retirement phase; and
- *Use of reserves in SMSFs to circumvent the total superannuation balance*, which could be legitimate in relation to legacy pensions, although the ATO believes there are limited circumstances where it is appropriate for new reserves to be established in SMSFs.