PMD Financial Advisers

Make your salary go further - package it

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Do you want to increase the value of your total pay packet, reduce your income tax, boost your superannuation savings and take advantage of other tax-effective benefits?

More and more employers are now allowing their staff to take their remuneration as a package of cash and certain other employee benefits that are concessionally taxed, such as superannuation. As a result, you may be able to substantially reduce your tax and/or gain other valuable benefits.

Where's the sacrifice?

Salary packaging is often known as salary sacrifice because you are sacrificing (doing without) a proportion of your take-home salary in order to gain a greater benefit.

You can sacrifice your salary in exchange for additional superannuation, a car lease or payment by your employer of certain other expenses that you would otherwise have had to pay from your after-tax earnings. So with less tax and more benefits, the sacrifice should be worthwhile.

Fringe benefits tax

Before we look at packageable benefits in more detail, let's look at fringe benefits tax (FBT) which is payable on some packaged benefits instead of income tax.

FBT is payable at 49 per cent[1] (equal to the top marginal income tax rate) of the grossed-up taxable value of a benefit. This means that for a benefit to be tax-effective, it must either be exempt from FBT or it must have the FBT applied to only part of the value of the benefit, so that there is still a potential tax saving.

It is important to understand:

- which benefits provide a tax advantage and which do not, and
- how your total income and marginal tax rate will affect your package.

Professional advice is essential. It makes no sense to package a benefit if you will end up paying more FBT and/or other tax than you will save in income tax.

Packaged superannuation

Salary packaging your superannuation enables you to boost your super while paying less tax.

The key advantages of salary sacrificing your super are:

- **lower tax on contributions:** instead of paying income tax of up to 49 per cent before making your contribution, you pay only a maximum of 15 per cent[1] contributions tax and your taxable income is reduced by the amount you sacrifice. If you earn less than $37,000 you may be eligible for the low income superannuation contribution (LISC) from the Government. The LISC refunds the 15 per cent contributions tax you pay on your SG contributions and any salary sacrifice contributions you make.

- **lower tax on investment earnings:** a super fund pays a maximum of 15 per cent on investment earnings compared to the marginal tax rates that apply outside super (up to 47 percent plus the 2 percent temporary budget repair levy).
- **low or no tax in retirement:** when you convert your super from a taxed fund into a retirement income product you will benefit from paying low tax if you have reached preservation age to 59 or no tax if you are aged 60 or over on payments received.

By regularly adding to your retirement savings in super you should end up with considerably more than you can accumulate outside super. Salary packaging is also a good way to build your super savings as you near retirement.

When packaging super makes sense

Taxable income + benefits	Marginal tax rate2	Super tax rate 1	Net tax saving on contribution
$0 to $18,200	0%	15%	Negative
$18,201 to $37,000	21%	15%	6%
$37,001 – $80,000	34.5%	15%	19.5%
$80,001 – $180,000	39%	15%	24%
$180,000 – $300,000	49%	15%	34%
Over $300,000	49%	30%	19%

Packaged car lease

Instead of buying your next car outright, you may be able to arrange a novated lease and pay the lease and full running costs through your salary package.

Depending on your financier, you may be able to choose your own vehicle model, new or used, your own supplier, and negotiate your own price and preferred form of lease payments.

Case study

John and Sarah each have a salary package of $60,000 pa. They each buy a $40,000 car, John through a personal loan and Sarah through a package lease, and each drive about 24,000 km pa.

Sarah is subject to $7,064 pa FBT (for a GST-inclusive employer) on her car's taxable value ($8,000). However, by contributing $8,000 from her after-tax income (employee contribution method) FBT will be eliminated.

Consequently her net take-home pay is about $3,200 higher than John's.

For further details please refer to table on next page.

Packaged work expenses

Work expenses include most of the items you can normally claim as a tax deduction, so they are FBT-exempt. However, when you package certain work-related expenses, you receive your tax back sooner and you may not have to substantiate full business use.

Packageable work expenses could include self-education, professional subscriptions and memberships.

When is packaging not tax-effective?

Non-business items such as mortgage payments, rent and school fees were once frequently packaged. These benefits now incur FBT at the full taxable value so they are no longer tax-effective unless the employer is classed as exempt or rebateable.

Concessional items are normally tax-effective for mid to high income earners but may provide little or no tax savings for low income earners.

Costs of salary packaging

If your employer uses a company that provides a packaging service, there may be an annual administration cost which could vary with the package contents.

You will also need to pay a fee if you seek professional advice on your packaging decision.

How to get started

Firstly, you need to find out if your employer offers salary packaging. Speak to your payroll or HR department. Then, if the benefits set out above seem worthwhile in your circumstances, it is best to seek professional advice.

The car packaging difference	John not packaged $	Sarah packaged $
Gross salary package	60,000	60,000
Total lease and running costs[4]	–	-7,064[4]
Employee contribution	–	+8000
FBT	Nil	Nil
Taxable salary	60,000	52,936
Income tax on salary	-12,147	-9,604
After-tax salary	47,853	43,332
After-tax payments for costs	-15,720	-8,000
Net take-home pay	32,133	35,332

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1. The contributions tax rate is up to 30 per cent for individuals with income over $300,000.
2. Individual tax rates for the year ended 30 June 2017 including Medicare levy and Temporary Budget Repair levy.
3. Assumes registration costs of $500, lease costs of $9,600, insurance $1,500, fuel $3,120, maintenance of $900 and on road costs of $100 less $8,000 in employee contribution to lease and running costs.
4. 7,064 = [(15,720 - 500 - 8,000) /1.1 + 500]

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