

Chapter 5

The causes of SG non-payment

5.1 Submitters to the inquiry put forward numerous causes behind non-compliance with SG obligations.

5.2 For example, according to a submission by Cbus, SG non-compliance typically has four main sources:

- employer non-compliance (either deliberately or inadvertently);
- use of the cash economy;
- sham contracting; and
- employer insolvency.¹

5.3 The ACTU took a similar approach to considering reasons for SG non-payment and identified four types of employment arrangements in which non-payment is likely to occur:

- 'normal' employment arrangements in which an employer simply does not comply with their SG obligations;
- 'independent' contracting arrangements in which there may be uncertainty about whether genuine contracting is occurring, leading to doubts as to whether a liability for SG exists and if it does, who should pay it;
- cash in hand arrangements; and
- 'new' forms of employment (such as the 'gig economy' or 'in kind' work) which may raise doubts as to whether the SG liability arises, and who should be responsible for it.²

5.4 The ATO collated a range of reasons provided by employers as to why they had not complied with SG obligations. For example, cash flow difficulties were raised in around 70 per cent of cases, with poor record keeping raised in approximately 20 per cent of cases.³ The ATO also stated that other reasons provided by employers for non-compliance included a lack of understanding of the SG legislation (leading to a misunderstanding of obligations); a deliberate strategy to delay or avoid SG obligations as long as possible; or simply choosing not to comply.⁴

1 Cbus, *Submission 48*, p. 9.

2 Australian Council of Trade Unions, *Submission 51*, p. 6.

3 Australian Taxation Office, *Submission 6*, p. 13.

4 Australian Taxation Office, *Submission 6*, p. 13.

5.5 Taking into account all the evidence received by the committee, several factors driving systemic non-compliance with SG obligations were identified. These factors can be broadly categorised as follows:

- compliance challenges stemming from system design and complexity;
- compliance challenges specific to small businesses; and
- industry characteristics leading to a pre-disposition to SG non-payment.

5.6 The problem of employer insolvency was also raised by numerous submitters as a contributing factor to SG non-payment, and this will be discussed in chapter 6.

5.7 This chapter will now turn to examine the salient issues contained within these three categories.

System design and complexity

5.8 The committee received evidence indicating that some aspects of the design and complexity of the SG system increased the likelihood of SG non-payment. A number of submitters argued that the SGA Act was not simple to follow and that the obligations imposed on employers under it were complex.⁵

5.9 Similarly, in its 2015 performance audit of the ATO's activities in promoting compliance with SG obligations, the ANAO observed that some features of the operation of the SG scheme presented practical challenges for employers, employees, and the ATO as regulator. The ANAO stated those challenges could in some cases underpin employer non-compliance with SG obligations.⁶

5.10 However, despite the apparent system complexity, it should be noted that the ATO acknowledged that case officers reported a very high level of employer awareness regarding SG requirements, and that it was rare for an employer to claim they knew nothing about their SG obligations.⁷

5.11 Elements of system design which could lead to SG non-payment include:

- the \$450 per month threshold limit;
- current salary sacrifice arrangements; and
- quarterly payment requirements.

5.12 Administrative challenges arising from the complexity of the system which led to SG non-payment include:

5 For example, see Housing Industry Association, *Submission 28*, p. 2; Council of Small Business Australia, *Submission 33*, pp. 1–3.

6 Australian National Audit Office, *Promoting Compliance with Superannuation Guarantee Obligations*, Audit Report No. 39, 2014-15, p. 15.

7 Australian Taxation Office, *Submission 6*, p. 13.

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- the misclassification of employees; and
 - the difficulty in calculating SG amounts based on the definition of OTE.

5.13 This section will examine each of these five elements in turn.

\$450 per month threshold limit

5.14 To be eligible for SG contributions from an employer, an employee must be aged 18 or over and earning over \$450 a month in OTE. Numerous submitters pointed out that this \$450 monthly threshold missed out a potentially significant number of employees and was too easily able to be exploited by unscrupulous employers.⁸

5.15 ISA asserted that some workplaces use targeted strategies based around this threshold to avoid SG obligations. For example, an employer may deliberately roster staff in ways to keep them under the \$450 threshold, or develop an enterprise agreement restricting the classification of OTE hours, thereby ensuring additional hours worked are overtime and fall outside the SG base.⁹

5.16 The National Foundation for Australian Women (NFAW) was also of the opinion that the \$450 monthly threshold was an anomaly that was being misused, leading to a particular subset of employees not accumulating any superannuation benefits. The NFAW submission stated:

We have been informed that some employers who maintain large casualised workforces may be exploiting this provision in their rostering arrangements. For example women have talked of being employed by several different employers in the same industry, with each employer limiting the hours so that the worker remains under the monthly threshold. We believe that this also affects other groups of workers, including students.¹⁰

5.17 Similarly, Women in Super informed the committee that even without the misuse of minimum monthly earnings figure, the \$450 monthly threshold was likely to disproportionately affect females. This is because women make up the majority of part-time and casual workers, and often work multiple jobs in female dominated, low paid industries (such as nursing, retail and hospitality). The submission also noted that men in similar circumstances would also be adversely affected.¹¹

8 See ISA, *Submission 7.1*; Anglicare Australia, *Submission 22*; National Foundation for Australian Women, *Submission 1*; Council on the Ageing, *Submission 52*; Council of Small Businesses Australia, *Submission 33*; Australian Institute of Superannuation Trustees, *Submission 37*; Women in Super, *Submission 45*; Construction, Forestry, Mining and Energy Union, *Submission 54*.

9 ISA, *Submission 7.1*, p. vi.

10 National Foundation for Australian Women, *Submission 1*, p. 2.

11 Women in Super, *Submission 45*, p. 3.

5.18 Anglicare Australia submitted that the threshold alone was detrimental to workers on low incomes, or multiple low sources of income, as it effectively prevented them from building their superannuation balances.¹²

5.19 The Council of Small Business Australia (COSBOA) proposed that the \$450 monthly threshold should be removed, citing the resulting removal of threshold anomalies in the award system as justification.¹³

5.20 Additionally, the Australian Institute of Superannuation Trustees (AIST) asserted that the \$450 monthly threshold should be abolished as it provided an incentive for businesses to retain casual employees on low work rostering in order to avoid SG obligations.¹⁴

5.21 The AIST submission provided three reasons as to why the removal of the threshold is necessary to improve fairness and compliance with the SG system:

- the cost to government would be minimal;
- individuals on lower incomes would have a better retirement outcome; and
- Australia's superannuation coverage, although quite high, is comparatively lower than other systems with mandatory superannuation.¹⁵

5.22 The AIST further argued:

We note that whilst wages have grown, so too has the increasing casualisation of the Australian workforce. As the percentage of Australians holding more than one job increases, so too does the likelihood that at least one job will pay under the threshold. As this, in turn, affects the retirement savings of Australians, we believe that [the] time is right to debate the role that this threshold plays in limiting the retirement comfort of Australians.¹⁶

Committee view

5.23 The committee is of the opinion that the \$450 monthly threshold is out-dated. The committee is aware that while initially the threshold may have minimised the administrative burden for employers of deducting small contribution amounts for lower paid or itinerant workers, technological advances over subsequent years and the capabilities available in the current digital age have simplified this aspect of the SG administrative process, rendering this justification irrelevant.

12 Anglicare Australia, *Submission 22*, p. 3.

13 Council of Small Business Australia, *Submission 33*, p. 6.

14 Australian Institute of Superannuation Trustees, *Submission 37*, pp. 22–23.

15 Australian Institute of Superannuation Trustees, *Submission 37*, p. 21.

16 Australian Institute of Superannuation Trustees, *Submission 37*, p. 23.

5.24 The committee is aware that stakeholder concerns around the adverse impact of the \$450 monthly threshold have been raised in the past. In particular the committee notes that a 1995 report¹⁷ of the Senate Select Committee on Superannuation, as well as a 2001 report¹⁸ by the then Senate Select Committee on Superannuation and Financial Services canvassed the issue and examined the adverse impacts of the threshold on those employed in 'itinerant vocations and professions'.¹⁹ Both reports recommended that the appropriateness of the threshold be examined with a view to change.

5.25 Furthermore, the committee understands that the threshold adversely impacts particular categories of employees, such as women and employees who work in multiple, low paid jobs. The committee is mindful that the increasing casualisation of the Australian workforce will only further contribute to the adverse impacts of the threshold on affected workers.

Recommendation 3

5.26 The committee recommends that the government strongly consider introducing amendments to the SGA Act to remove the \$450 monthly threshold on SG eligibility.

Current salary sacrifice arrangements

5.27 A 2006 ATO ruling (SGD 2006/2) on the SGA Act states that it is allowable for an employee's voluntary salary sacrifice contributions to firstly, reduce the employee's OTE base on which SG is calculated; and secondly, be counted towards their employer's compulsory SG obligation.²⁰ Numerous submitters raised concerns with this arrangement and emphasised it could be exploited by unscrupulous employers to the detriment of employees.

5.28 The AIST set out the ways in which this arrangement adversely impacts employees as follows:

- salary sacrifice arrangements reduce the earnings base upon which SG is calculated, resulting in smaller amounts of SG payable by employers; and

17 Senate Select Committee on Superannuation, *Super Guarantee—Its Track Record*, February 1995.

18 Senate Select Committee on Superannuation and Financial Services, *Enforcement of the Superannuation Guarantee Charge*, April 2001.

19 Senate Select Committee on Superannuation and Financial Services, *Enforcement of the Superannuation Guarantee Charge*, April 2001, p. 99.

20 Australian Taxation Office, *Superannuation Guarantee Determination SGD 2006/2*, 28 June 2006, www3.austlii.edu.au/au/other/rulings/ato/ATOSGD/2006/sgd2006-02/sgd2006-02.html (accessed 21 March 2017).

- salary sacrifice amounts are able to count towards SG amounts, enabling 'double counting' by unscrupulous employers.²¹

5.29 In its submission, the AIST drew attention to that fact that the ATO appears to highlight these effects as a benefit for employers as set out in an excerpt from the ATO website:

For you [employer making salary sacrifice contributions on behalf of employees], salary-sacrificed super contributions count towards your super guarantee payment obligations, which are calculated on your employee's reduced salary. However, the agreement [between the employer and employee setting out the salary sacrifice arrangements] may specify that you continue to pay super at the pre-sacrifice level.²²

5.30 Owing to the effects of the loophole, ISA argued that 'it is incomprehensible that any legislator intended to create this anomaly, and equally astonishing that it has not been addressed in more than a decade.'²³

5.31 Chartered Accountants Australia and New Zealand emphasised that due to SG being deferred wages, it is particularly important that employers do not take advantage of the salary sacrifice loophole:

As compulsory employer super is foregone salary and wages we think employers should not be permitted to reduce their compulsory super contributions because an employee has elected to contribute via salary sacrifice unless this has been clearly established under employment conditions.²⁴

5.32 Similarly, the ACTU characterised the ability for employers to offset SG against voluntary salary sacrifice arrangements as an anomaly with an unfair and detrimental impact on employees if misused by unscrupulous employers.²⁵

5.33 Cbus also identified that even though the majority of employers understood and supported the efforts of their employees to build their retirement funds by providing genuine salary sacrifice arrangements over and above their SG obligations, the salary sacrifice loophole had the potential to be exploited and therefore should be closed. Cbus mentioned that many employees may not even be aware that their employer was legally able to offset SG obligations against voluntary contributions.²⁶

21 Australian Institute of Superannuation Trustees, *Submission 37*, p. 24.

22 Australian Institute of Superannuation Trustees, *Submission 37*, p. 24.

23 Industry Super Australia, *Submission 7.1*, p. v.

24 Chartered Accountants Australia and New Zealand, *Submission 27*, p. 4.

25 Australian Council of Trade Unions, *Submission 52*, p. 9.

26 Cbus, *Submission 52*, pp. 14–17.

5.34 Industry Super Australia also provided an estimate of the number of employees affected by the arrangement:

Under Superannuation Guarantee Determination 2 of 2006, salary sacrifice contributions made by the employee are thus considered employer contributions for the purposes of the SG (and for the purposes of both employer and employee income deductions). ISA estimates that salary sacrifice contributions by 429,200 employees were used to meet the employer SG obligations in 2013-14. This involves \$3.6 billion in salary sacrifice contributions – a huge distortion in competitive neutrality.

ISA analysis of the 2 per cent matched sample file indicates that employers are reducing the compulsory contributions of 36 per cent of people who are salary-sacrificing, and the vast majority of people affected by this earn below full-time average earnings. Sixty-one per cent of those affected have incomes under \$ 80,000 a year – and the average impact of this across those who are salary-sacrificing and whose employers are reducing their contributions is, on average, \$3,892 per person.²⁷

5.35 During a public hearing the committee queried whether the multi-agency working group on SG had discussed the issue of salary sacrifice deductions with reference to the 2006 ATO ruling. Mr O'Halloran, ATO Deputy Commissioner for Superannuation, responded that the matter had been discussed.²⁸

5.36 Mr David Denney, Branch Manager in the Department of Employment (also a member agency of the working group), provided further clarification and indicated that from the department's perspective, it was an issue that was being looked at in more detail. He also noted that there was room for greater clarity, particularly as the matter intersected with the Fair Work Act and that there appeared to be some confusion around what employers could and could not do in the area.²⁹

5.37 The Department of Employment provided detailed information in response to a question on notice requesting clarification on situations where it is legal for an employer to reduce their SG obligations:

Section 323 of the *Fair Work Act 2009* (FW Act) outlines when an employer can deduct money from payments to an employee for the performance of work (including superannuation). Subsection 324(1) of the FW Act permits a deduction only if it is:

- (a) authorised in writing by the employee and principally for the employee's benefit;
- (b) authorised by the employee in accordance with an enterprise agreement;

27 Industry Super Australia, *Submission 7.1*, p. 8.

28 Mr James O'Halloran, Deputy Commissioner, Superannuation, Australian Taxation Office, *Proof Committee Hansard*, 3 March 2017, p. 20.

29 Mr David Denney, Branch Manager, Department of Employment, *Proof Committee Hansard*, 3 March 2017, pp. 20–21.

(c) authorised under a modern award or an order of the Fair Work Commission; or

(d) authorised by or under a law of the Commonwealth, a State or a Territory, or an order of a court.

Deductions authorised under both paragraphs (a) and (b) require a separate, express agreement by the employee for each deduction.

Further, a term of an award, enterprise agreement or employment contract will be of no effect if it permits a deduction that is for the benefit of the employer *and* is unreasonable in the circumstances.

Therefore, without an employee's express agreement, an employer cannot use an employee's voluntary superannuation contribution to satisfy any part of their compulsory superannuation guarantee obligation unless the deduction is authorised under (c) or (d). An employer who does use an employee's voluntary contribution in this way without the express agreement of the employee may be in contravention of the FW Act. This is because the deduction would appear to be directly for the benefit of the employer as it reduces their compulsory superannuation guarantee obligation.

However, theoretically there may be individual circumstances where an employee expressly agrees to their voluntary contribution being used to satisfy the employer's compulsory superannuation guarantee obligation as it is principally for the benefit of the employee.³⁰

5.38 The ATO informed the committee that it did not have any data to indicate if, or to what extent, employers were using their employees' salary sacrifice amounts to meet their SG obligations, or to show, if indeed this practice was occurring, what amount of salary sacrifice contributions were being used.³¹ As the ATO stated:

Employers are required to report contributions made under a salary sacrifice agreement as '*Reportable employer super contributions*'. Specific salary sacrifice amounts cannot be distinguished from other items reported under this category, such as additional amounts paid to an employee's superannuation fund as an annual bonus or employee negotiated increases in employer superannuation contributions.³²

30 Department of Employment, answers to questions on notice, 3 March 2017 (received 15 March 2017), p. 1.

31 Australian Taxation Office, answers to questions on notice, 3 March 2017 (received 17 March 2017), p. 1.

32 Australian Taxation Office, answers to questions on notice, 3 March 2017 (received 17 March 2017), p. 1.

5.39 The ATO did note, however, that a broad analysis of the complaints and compliance cases it dealt with did not identify the inappropriate use of the salary sacrifice loophole as an issue brought to its attention.³³

5.40 In addition, Ms Jenny Wilkinson, Division Head from the Department of the Treasury, observed:

We get a few complaints to Treasury about this practice occurring. We are aware that it occurs in places, but we do not get a lot of complaints brought to us. We really do not have a sense of how widespread it is...

But the other thing is, for any individuals who are concerned about their employer using their salary sacrifice contributions to make up their SG, with the changes in arrangements for personal deductions that the government introduced in the last set of superannuation changes, you do need to salary sacrifice in order to get the benefits of making personal deductions to your super. You can now do that as a voluntary personal contribution and still received a deduction through your tax return.³⁴

5.41 ISA put forward a recommendation to 'close the loophole' that allows salary sacrifice contributions made by an employee to be considered employer contributions for the purpose of the SG by amending the SGA Act as follows:

- clarify whether Reportable Employer Super Contributions (RESC) are considered salary or wages for the purposes of the act (section 11);
- clarify that a RESC contribution is not considered a contribution for the purposes of subsection (2) and therefore cannot be used by an employer to reduce the SG charge percentage and SG shortfall (section 23); and
- clarify that a RESC is a component of OTE as defined in subsection (2) (section 23).³⁵

Committee view

5.42 The committee understands the concerns raised by submitters about the possibility of the current salary sacrifice arrangements being misused by some employers in order to reduce or avoid their SG obligations. The committee believes that the SG must be a guaranteed minimum contribution to employees' retirement savings. When employees voluntarily contribute extra funds to their own superannuation savings they should be assured that these amounts are genuinely additional to the SG and not simply reducing their employers SG obligation. Without

33 Australian Taxation Office, answers to questions on notice, 3 March 2017 (received 17 March 2017), p. 1.

34 Ms Jenny Wilkinson, Division Head, Department of the Treasury, *Proof Committee Hansard*, 3 March 2017, p. 22.

35 Industry Super Australia, *Submission 7.1*, p. 8.

this assurance, employees may be disinclined to make adequate provision to their retirement through voluntary contributions.

Recommendation 4

5.43 The committee recommends the government introduce amendments to the SGA Act to ensure that an employee's voluntary salary sacrificed superannuation contributions cannot count towards the employer's compulsory SG obligation, nor reduce the OTE base upon which SG is calculated.

Quarterly payment requirements

5.44 Numerous submitters informed the committee that the current quarterly payment regime of the SG system was a contributing factor to the non-payment of SG. These submitters recommended that SG payments be made more frequently, in alignment with an employee's normal pay cycle.

5.45 As outlined in chapter 2, employers are generally required to make SG contributions to the complying superannuation fund of the employee's choice four times per annum.³⁶

5.46 ISA argued that the risk of SG non-payment is compounded by the quarterly payment system. As such, ISA recommended that the SGA Act be amended to require that SG contributions be paid on at least a monthly payment cycle, and preferably in alignment with wage and salary payments, before 1 July 2018.³⁷

5.47 CPA Australia observed that the current quarterly payment requirements (with payment due within 28 days of the end of a quarter) made it difficult for the ATO to effectively monitor payment. CPA Australia also stated that the payment requirements made it difficult for employees to identify and reconcile whether the appropriate amount of SG had been paid into their nominated fund when the quarterly payments do not align with their regular salary payments.³⁸

5.48 Similarly, the Institute of Public Accountants noted that research from its membership indicated that employees had difficulty monitoring their employer's SG compliance, in part because of the lack of transparency around when SG was actually paid into their superannuation funds.³⁹

36 Australian Taxation Office, *When to pay super*, www.ato.gov.au/Business/Super-for-employers/Paying-super-contributions/When-to-pay-super/, (accessed 2 March 2017). Note: There are some exceptions to this requirement in that some awards may require SG to be paid monthly.

37 Industry Super Australia, *Submission 7.1*, p. 16.

38 CPA Australia, *Submission 32*, p. 2.

39 Institute of Public Accountants, *Submission 31*, pp. 2–3.

5.49 Cbus also asserted that the quarterly payment requirements created a significant risk of non-compliance and impeded the prompt detection of non-compliance when it did occur. Cbus informed the committee that in order to address this and facilitate the early detection of arrears, the Cbus Trust Deed provides that participating employers make superannuation payments on behalf of their employees monthly, by the first day of the following month. As such, employers, upon joining Cbus, enter a contract accepting these payment terms. Cbus concluded that 'superannuation should be treated the same as wages and paid congruently' and recommended real time payment and reporting of SG be implemented.⁴⁰

5.50 The Council on the Ageing (COTA) emphasised that the administration of wages and entitlements now takes place in an environment far more technologically advanced than that in which SG was introduced in 1992. As such, the quarterly payment dates, which may have been appropriate in the early 1990s when most payments would have been processed manually, were now outdated.⁴¹ As the COTA submission outlined:

The electronic transfer of payments and much more digitally sophisticated accounting and reporting systems open the potential for well-designed, secure, timely and efficient forms of SG payment that better serve the interests of both the employer and the employee. There is no longer an administrative argument for withholding the SG payment from an employee for several months.⁴²

5.51 COTA recommended the payment of SG in real-time, and noted that paying SG alongside or close to wage payments would leave no room for confusion about whose money it was, potentially encouraging better compliance.⁴³

5.52 United Voice pointed out that under the Fair Work Act, wages must be paid at least monthly. It went on to argue that aligning superannuation contributions with pay cycles would reduce the gap between payments, make it harder for employers to fall behind on payments, and make it easier to detect non-compliance.⁴⁴

Committee view

5.53 The committee recognises that the current quarterly SG payment requirements outlined in the SGA Act create a significant risk of non-compliance and also hinder the prompt detection of SG non-payment.

40 Cbus, *Submission 48*, pp. 2–3, 7.

41 Council on the Ageing, *Submission 52*, p. 5.

42 Council on the Ageing, *Submission 52*, p. 5.

43 Council on the Ageing, *Submission 52*, p. 5.

44 United Voice, *Submission 66*, p. 25.

5.54 The committee believes that the current technological solutions available to businesses regarding payroll and other related activities mean that a more frequent schedule of SG payments would not place an undue administrative burden on businesses.

Recommendation 5

5.55 The committee recommends that the government strongly consider introducing amendments to the SGA Act to require SG to be paid at least monthly, and preferably in alignment with regular pay cycles.

Misclassification of workers

5.56 The misclassification of workers in employment or contracting arrangements was an issue identified by several submitters as a factor contributing to SG non-payment.

5.57 Generally speaking, if a worker is classified as an employee, their employer has the liability to pay SG. However, if a worker is classified as a contractor, this is not the case. However, it can be complicated for an employer to correctly classify their workers for SG purposes, particularly as the definition of an employee in common law differs from the expanded definition provided in the SGA Act.⁴⁵

5.58 As the IGT pointed out:

There are inherent difficulties associated with the employee/contractor distinction which stems from its common law definition of 'employee' with no determinative factor. There are a number of factors which have to be considered relative to each other, making a determination very much reliant on the facts of each case.⁴⁶

5.59 The misclassification of a worker as a contractor, rather than an employee, can therefore lead to SG entitlements not being paid.

5.60 The Housing Industry Association (HIA) reiterated this point arguing that one of the core challenges for businesses in the residential construction industry was determining which workers were eligible for the SG, as distinguishing between employees and independent contractors for the purposes of superannuation was a complex and difficult task.⁴⁷

5.61 HIA elaborated on the issue:

...the extended definition of 'employee' in section 12(1) of the SGA Act deems certain individuals to be employees for superannuation guarantee purposes, even though they would otherwise be outside the scope of the

45 Australian Council of Trade Unions, *Submission 51*, p. 6.

46 Inspector-General of Taxation, *Submission 21*, p. 11.

47 Housing Industry Association, *Submission 28*, p. 3.

SGA Act. In particular, section 12 (3) of the SGA Act deems a person that 'works under a contract that is wholly or principally for the labour of the person' to be an employee for superannuation law purposes.

The ATO has issued Superannuation Guarantee Ruling 2005/1 (SGR 2005/1), which sets out the Tax Office's view on when a contractor falls within the expanded definition of an employee. Drawing on the common law the ruling sets out three principal tests when a contractor will be considered an employee. These are if the contractor:

- is remunerated wholly or principally for their labour and skills
- performs the work themselves
- is not paid to achieve a result.⁴⁸

5.62 HIA concluded that while the SGR 2005/1 ruling provides a degree of guidance, as does the ATO's decision tool, there remains 'considerable uncertainty about who is an employee and who is a contractor for superannuation purposes.'⁴⁹

5.63 However, it should be noted that in addition to instances of accidental misclassification of workers due to system complexity, it is not unknown for unscrupulous employers to deliberately misclassify employees as contractors in order to avoid paying entitlements such as SG. This practice is known as 'sham contracting'.⁵⁰

5.64 The CFMEU submitted that sham contracting arrangements were rife in the construction industry, and that there were substantial cases of non-payment and underpayment of SG as a result of this practice.⁵¹

5.65 Furthermore, as pointed out by the AIST, the prevalence of sham contracting arrangements was singled out as a significant systematic risk in the IGT's 2010 report, given that it potentially affects those individuals most reliant upon SG as a source of retirement income.⁵²

5.66 The IGT informed the committee that businesses and workers could benefit from further assistance to determine the status of workers at an early point in the employment relationship. On this front, the IGT suggested that the existing ATO online tool, the Employee/Contractor Division (ECD) tool, which currently assists businesses to determine whether they have an SG liability, could be expanded to facilitate use by workers as well. The IGT observed that 'such expansion, along with

48 Housing Industry Association, *Submission 28*, p. 3.

49 Housing Industry Association, *Submission 28*, p. 3.

50 See also National Foundation for Australian Women, *Submission 1*, p. 3.

51 Construction, Forestry, Mining and Energy Union, *Submission 54*, p. 4.

52 Australian Institute of Superannuation Trustees, *Submission 37*, p. 5.

early promotion and integration with other ATO tools will better inform all parties of potential superannuation obligations and entitlements.⁵³

5.67 Another initiative put forward by the IGT which would provide a higher degree of certainty for workers on their status as either employees or contractors is a Voluntary Certification System (VCS). The ATO's current private binding advice and administratively binding advice framework is only available to businesses. As the IGT elaborated:

The VCS would, in effect, be an extension of the existing ruling and advice framework but would be based on information provided independently by each party. Similar systems exist in the United States ((US) and Canada where either the worker or business may request a binding determination from the Internal Revenue Service or the Canada Revenue Agency respectively.⁵⁴

5.68 The IGT further detailed:

The VCS would be expected to overcome the inability of workers to obtain relevant binding advice on their status and for both parties to independently submit their facts for consideration. Similar to the expanded ECD tool all parties could be encouraged to use it as soon as possible so that, from the outset, employers are clear when they have to pay the SG amounts and employees are aware of their entitlements.⁵⁵

Committee view

5.69 Given the complexity of classifying workers correctly for SG purposes, and the impact of a misclassification on the SG entitlements of an individual, the committee believes there is a need for enhanced mechanisms that provide greater certainty to workers and their employers on SG entitlements and obligations.

5.70 Guided by the potential solutions suggested by the IGT, the committee is of the opinion that the ATO should look to provide an administratively binding advice framework available not only to businesses, but also to workers.

Recommendation 6

5.71 The committee recommends that the government investigate options to extend the ATO's current private binding advice and administratively binding advice frameworks to make them available to workers as well as businesses.

53 Inspector-General of Taxation, *Submission 21*, p. 11.

54 Inspector-General of Taxation, *Submission 21*, pp. 11–12.

55 Inspector-General of Taxation, *Submission 21*, p. 12.

Difficulty in determining SG amounts

5.72 The difficulty employers faced in determining the correct amount of SG to pay employees was cited by numerous submitters as a factor behind SG non-payment.⁵⁶

5.73 SG is currently calculated upon the amount of Ordinary Time Earnings (OTE). For the purposes of this SG calculation, OTE are defined as the salary or wages paid to employees for their ordinary hours of work. As the ANAO explained in its 2015 performance audit report:

OTE can include over-award payments, allowances, bonuses, commissions, and paid leave. Overtime payments are excluded unless an employer is unable to separately identify overtime amounts. Lump sum payments to an employee on termination in lieu of unused leave entitlements, such as sick leave, recreation and long service leave, are also excluded from the definition of OTE for SG contribution purposes.⁵⁷

5.74 The AIST submitted that the calculation of the SG for all stakeholders would be greatly simplified by basing the calculation on gross remuneration, rather than OTE. This is because under the current system, it is often unclear whether a payment counts as OTE. As the submission stated:

OTE unfortunately only captures some of the many payments that can be paid to employees as part of their work. OTE does not incorporate overtime, whether or not this is regularly worked, nor does it incorporate paid parental leave.

It is not always clear whether a payment forms part of OTE. In Superannuation Guarantee Ruling SGR 2009/2, the Commissioner of Taxation considered 24 different types of employer payments (with some of these further broken down into sub-types) and only concluded in 14 cases that these formed part of OTE.⁵⁸

5.75 The AIST went on to detail:

OTE is presently inconsistent with different income definitions used for thresholds for SG-related taxation and offsets such as the Low Income Superannuation Tax Offset (LISTO) and Division 293 tax which are based on a gross remuneration equivalent, being taxable income adjusted to include reportable fringe benefits, superannuation contributions and investment losses.⁵⁹

56 See Housing Industry Association, *Submission 28*; Australian Institute of Superannuation Trustees, *Submission 37*; Council of Small Business Australia, *Submission 33*.

57 Australian National Audit Office, *Promoting Compliance with Superannuation Guarantee Obligations*, Audit Report No. 39, 2014-15, p. 34 (footnote 49).

58 Australian Institute of Superannuation Trustees, *Submission 37*, p. 7.

59 Australian Institute of Superannuation Trustees, *Submission 37*, p. 7.

5.76 HIA noted that from its observations, employers often experienced confusion about what constituted OTE, particularly in regard to overtime. HIA mentioned other anomalies which caused confusion; for example, if an employer fails to make the correct SG contributions on time and is subject to the SG charge for the shortfall, the shortfall is not based on OTE, but on the broader definition of salary or wages, which might include overtime. HIA also identified that different rules for terminating employees also created confusion.⁶⁰

5.77 The Construction, Forestry, Mining and Energy Union (CFMEU) pointed out that many of its disputes around SG arose due to a conflict over what constitutes OTE. The CFMEU also argued that for hourly employees in industries such as manufacturing, construction and transport, OTE bears little relationship with the actual earnings.⁶¹

5.78 COTA argued that basing SG off gross remuneration would work to simplify SG calculation for employers and employees, and 'properly reflect the intent that SG is a deferred consistent percentage of employee remuneration'.⁶²

5.79 The committee received evidence from the Finance Sector Union of Australia (FSU) and the Commonwealth Bank of Australia (CBA) outlining a situation where the complexity of determining the correct amount of SG resulted in a significant number of CBA part-time employees being underpaid their SG entitlements.

5.80 In 2009, the ATO issued an update to Superannuation Guarantee Ruling SGR 2009/2 which deals with the definition of OTE and superannuation payable to employees. The CBA subsequently obtained advice that set out that under that ruling, SG was not payable on additional hours or overtime worked by part-time workers.⁶³ As a result, part-time CBA employees were not paid SG on any additional hours they worked that were paid at single time hourly rates.⁶⁴

5.81 The FSU raised concerns with the CBA about this practice over several years, as part-time CBA employees indicated that working additional ordinary hours (above those initially specified in their contracted hours) was a relative frequent occurrence. However, the initial response from the CBA was that the payment for those hours did not constitute OTE as envisaged by the SG legislation.

5.82 The CBA informed the committee that it had reviewed its position in light of a number of case studies brought to its attention by the FSU in early 2017, and that it would now be paying SG on additional single time hours worked by part-time CBA

60 Housing Industry Association, *Submission 28*, pp. 5–6.

61 Construction, Forestry, Mining and Energy Union, *Submission 54*, pp. 14–15.

62 Council for the Ageing, *Submission 52*, pp. 8–9.

63 Commonwealth Bank of Australia, *Submission 55*, p. 1.

64 Finance Sector Union of Australia, *Submission 34*, p. 3.

employees. CBA also outlined that it had commenced an internal review of the additional work hours and pay records of all current and former part-time employees for the past eight years in order to identify and rectify instances of unpaid superannuation.⁶⁵

Committee view

5.83 The committee acknowledges the frustrations of stakeholders in the SG system with the current complexity in calculating SG amounts. The committee is aware that this complexity can cause difficulties for employers and may be a contributing factor to SG non-payment.

5.84 The committee is also mindful that any change to the base on which SG is calculated could have wider implications on the tax and superannuation frameworks, and that any move to change the way in which SG is calculated would need to be carefully considered.

Recommendation 7

5.85 The committee recommends the government review the definition of Ordinary Time Earnings for the purposes of SG obligation calculations and undertake an examination on the wider implications of any potential changes.

5.86 The committee considers that such a review be undertaken with a view to avoid any future situations similar to those experienced by part-time employees of the CBA.

Compliance challenges for small businesses

5.87 The committee received evidence that small businesses face particular compliance challenges that can lead to higher rates of SG non-payment.

5.88 According to the Office of the Australian Small Business and Family Enterprise Ombudsman (ASBFEO), small businesses are collectively Australia's biggest employers, providing 44 per cent of total employment. However, small businesses generally have limited administrative resources to navigate the complexities involved with the administration of employee superannuation entitlements.⁶⁶

5.89 ATO analysis of the characteristics of SG non-compliance concluded that it appears to be more prevalent among micro and small businesses. The ATO considered that this may form part of a broader picture of non-compliance, with such employers

65 Commonwealth Bank of Australia, *Submission 55*, p. 1.

66 Office of the Australian Small Business and Family Enterprise Ombudsman, *Submission 29*, p. 1.

also failing to withhold employee's income tax, paying wages in cash, or incorrectly treating employees as contractors.⁶⁷

5.90 The ATO submission stated:

Some 97 per cent of reports of unpaid super made to the ATO were against small business employers and this same group accounted for around 98 per cent of the liability raised by the ATO.⁶⁸

5.91 JobWatch agreed with the ATO's assessment that small business employers are particularly prone to non-compliance with SG obligations. JobWatch also informed the committee that most of the complaints they received in regard to SG non-payment originate from small business employees and low wage workers with largely insecure working arrangements.⁶⁹

5.92 Cash flow pressures were identified by numerous submitters as a challenge to small businesses that drove or created a pre-disposition to SG non-payment.

5.93 For example, the Australian Chamber of Commerce and Industry stated that small business cash flow was a major contributor to missed payments, and that cash flow was an endemic problem for many small and micro businesses.⁷⁰

5.94 The Australian Restructuring Insolvency and Turnaround Association noted:

Self-reportable amounts payable to the ATO can become an easy source of 'funding' when a business enters some form of financial distress. By failing to report, the obligation or debt can become hidden and there is a perception that the outstanding amount will remain unidentified until such time as business improves and the amount can be paid. It is often the case that business does not improve and amounts continue to accrue and remain unpaid, and often unreported.⁷¹

5.95 As the Office for the ASBFEO submitted:

For small business, cash flow is king and non-payment of the Superannuation Guarantee must be seen in context as symptomatic of perennial resource limitations and cash flow difficulties experienced by small business.⁷²

67 Australian National Audit Office, *Promoting Compliance with Superannuation Guarantee Obligations*, Audit Report No. 39, 2014-15, pp. 14–15.

68 Australian Taxation Office, *Submission 6*, p. 27.

69 JobWatch, *Submission 26*, p. 4.

70 See Australian Chamber of Commerce and Industry, *Submission 49*, pp. 5–6.

71 Australian Restructuring Insolvency and Turnaround Association, *Submission 23*, p. 1.

72 Office of the Australian Small Business and Family Enterprise Ombudsman, *Submission 29*, p. 3.

5.96 Similarly, the IGT submission noted:

...the ATO has observed that in 70 per cent of cases where it investigated non-payment of SG entitlements, the reason for non-compliance was 'cash flow issues'. Indeed, non-payment of SG entitlements is an indication of financial difficulties that a business may be experiencing and may expose its creditors to financial risk of which they may be unaware.⁷³

5.97 Dr Tess Hardy, a lecturer in employment law, and regulatory compliance and enforcement at the University of Melbourne argued:

I think that, where the great bulk of unpaid superannuation is due to cash flow problems, that is a red flag for the economic drivers of non-compliance. It is not as a result of a lack of education or ignorance. And that means that more education, more tweets, more Facebook posts—all of this social media—are, in my view, wasted energy to some extent because they are not going to address some of the fundamental drivers, which are cash flow economic problems faced by small businesses.⁷⁴

5.98 CPA Australia submitted that poor business-to-business payment culture had a detrimental impact on the cash position of small businesses, which could in turn drive the non-payment of SG.⁷⁵

5.99 CPA Australia also drew the committee's attention to the issues paper for the Payment Times and Practices inquiry that was being conducted by the ASBFEO.⁷⁶

5.100 The issues paper stated that evidence from Australia indicated large businesses were using their bargaining power to extend their payment times to suppliers while reducing or keeping payment terms for their customers shorter, allowing them to 'unlock' their working capital and improve their cash conversion cycle at the expense of suppliers. The paper recognised:

Late payments and extended payment times have significant impact on the SME [small and medium enterprises] subject to these conditions. These businesses usually have small, if any, cash reserves and are dependent on a fast cash flow cycle to maintain solvency... SMEs also are often forced to pass on the delay in payment to their suppliers as well as delay payments for other legal obligations (i.e. superannuation) and to government entities.⁷⁷

73 Inspector-General of Taxation, *Submission 21*, p. 3.

74 Dr Tess Hardy, private capacity, *Proof Committee Hansard*, 14 March 2017, p. 6.

75 CPA Australia, *Submission 32*, p. 1.

76 CPA Australia, *Submission 32*, p. 1.

77 Australian Small Business and Family Enterprise Ombudsman, *Issues Paper – Payment Times and Practices – February 2017*, http://asbfeo.gov.au/sites/default/files/ASBFEO_Issues_Paper.pdf (accessed 21 March 2017).

5.101 The ASBFEO's *Payment Times and Practices* report was publicly released in April 2017. The report observed that late payments had a significant impact on the cash flow of the businesses owed the outstanding debt, thereby forcing them to find other ways to finance the short fall in their working capital. The report made a number of recommendations, including that industry codes be developed to regulate business-to-business transactions to include best payment practices, including set payment times. The report also recommended that the government should encourage the adoption of technology solutions to assist businesses to streamline administrative tasks and facilitate prompt payment practices.⁷⁸

5.102 The Office of the ASBFEO also detailed in its submission that interim results of a survey of over 500 small businesses indicated that almost 50 per cent experienced late payments on approximately half of the bills owed to them, with one in four businesses experiencing an average payment delay of between 31 and 60 days past their payment terms. In addition, one in five respondents stated that late payments forced them to delay paying staff salaries, benefits and superannuation contributions.⁷⁹

Committee view

5.103 Although recognising that some small businesses face unique challenges (such as cash flow problems) that may impede their ability to comply with SG obligations, the committee is strongly of the view that employees' SG entitlements should not be used as a cash flow tool, particularly without their knowledge or consent.

5.104 The committee is aware that the ATO is implementing the Cash Flow Management Program, a new initiative for small businesses which focuses on helping employers better understand and manage their cash flow. The committee understands the program has been designed by the ATO and Price Waterhouse Cooper Indigenous Consulting, in consultation with tax practitioners, accountants, bookkeepers and small businesses.⁸⁰

Recommendation 8

5.105 The committee recommends the government consider further initiatives that will assist small business employers in managing their cash flow responsibly in order to provide them the best possible chance of fulfilling their SG obligations.

78 Office of the Australian Small Business and Family Enterprise Ombudsman, *Payment Times and Practices Inquiry – Final Report*, April 2017, pp. 4–6, www.asbfeo.gov.au/sites/default/files/ASBFEO_Payment_Times_and_Practices%20Inquiry_Report.pdf (accessed 21 April 2017).

79 Office of the Australian Small Business and Family Enterprise Ombudsman, *Submission 29*, pp. 2–3.

80 Australian Taxation Office, *Submission 6*, p. 19.

Industry and workforce characteristics

5.106 Evidence received by the committee indicated that instances of non-payment of SG occurred more frequently in certain industries, owing to workforce characteristics inherent to them. These characteristics included low wages and insecure work patterns. These at-risk sectors included the construction, transport, hospitality, accommodation and cleaning industries.⁸¹

5.107 The ATO acknowledged that there are particular industries where SG non-compliance was high:

From an industry analysis perspective, the top four industries from which reports are received by the ATO are from Accommodation and Food Services, Construction, Manufacturing and Retail Trade. These four industries represent approximately 50 per cent of the audits and reviews undertaken.⁸²

5.108 The Textile, Clothing and Footwear Union of Australia also identified the textile, clothing and footwear (TCFUA) industry as being at high risk for systemic SG non-payment. The TCFUA submission noted:

The reasons for this are many and varied, but the TCF sector is generally characterised as being highly award dependent, low paid and subject to widespread non-compliance of minimum safety net wages and conditions. These factors would appear to predispose certain sectors to high rates of non-compliance with award superannuation and/or SG obligations.⁸³

5.109 The TCFUA further observed:

In the TCFUA's experience, such chronic non-payment and underpayment by employers is conscious and deliberate, rather than a result of ignorance of obligations. Put bluntly, the payment of superannuation is commonly not considered a financial priority for many TCF businesses, but rather still viewed as something discretionary or not necessary to the act of employing staff. The decision to delay (or not pay at all) employee superannuation is seen as a legitimate cash flow solution or an interest free loan in the form of employee entitlements.⁸⁴

5.110 The CFMEU emphasised that the building and construction industry faced an ongoing crisis in relation to the systemic non-payment and underpayment of worker entitlements, and that non-compliance with SG obligations was widespread. Its

81 See Industry Super Australia and Cbus, *Overdue: Time for action on unpaid super*, November 2016, pp. 7-8; as well as Australian National Audit Office, *Promoting Compliance with Superannuation Guarantee Obligations*, Audit Report No. 39, 2014-15, pp. 14-15.

82 Australian Taxation Office, *Submission 6*, p. 4.

83 Textile, Clothing and Footwear Union of Australia, *Submission 50*, p. 4.

84 Textile, Clothing and Footwear Union of Australia, *Submission 50*, p. 5.

submission noted that for the period 1 January 2011 to 31 December 2016, the New South Wales branch of the CFMEU Construction Division recouped over \$13 million for members for the non-payment or underpayment of SG.⁸⁵

5.111 Anglicare Australia noted that the groups most likely to be affected by unpaid SG contributions are women, young people, and people on low incomes. These groups are also the same individuals likely to be engaged in insecure work.⁸⁶ Employees from culturally and linguistically diverse backgrounds are also more likely to be vulnerable to SG non-payment due to their overrepresentation in insecure or casual jobs.⁸⁷

5.112 Dr Hardy commented on industry characteristics which are systemic drivers behind SG non-compliance:

There are a range of drivers [of SG non-payment] in my view. It can arise in industries which have been identified by the ATO and the Fair Work Ombudsman. Those industries which are highly competitive and have high labour costs generally result in a highly casualised workforce characterised by large numbers of young workers or migrant workers. The way in which labour costs may affect the profit or sustainability of small businesses within those industries tends to perpetuate noncompliance. So that is one driver – the industry.⁸⁸

5.113 Dr Hardy also explained the ways in which the fragmenting of organisations could lead to non-compliance with the SG and other workplace obligations:

The other, which I have explored in my work under the Fair Work Act, is the way that the fragmentation of organisations can also lead to noncompliance... I am referring to franchising as an obvious example; the other is of course complex corporate groups – supply chains, labour hire. They are all examples of the way in which the splintering of organisations can drive noncompliance because the smaller businesses at the end of the supply chain or the franchisees within a broad franchise network have limited control over the way in which they manage their business – the price paid for the services or goods that they supply. The one thing they can control is labour costs, and that tends to drive a race to the bottom. They engage in unlawful behaviour because they perceive that they cannot survive as a business in any other way.⁸⁹

5.114 Anglicare Australia argued that unprecedented growth in insecure work had led to workplace conditions for employees which left them more vulnerable to the effects of SG non-payment:

85 Construction, Forestry, Mining and Energy Union, *Submission 54*, pp. 5–6.

86 Anglicare, *Submission 22*, pp. 1–2.

87 Textile, Clothing and Footwear Union of Australia, *Submission 50*, pp. 2–3.

88 Dr Tess Hardy, private capacity, *Proof Committee Hansard*, 14 March 2017, p. 6.

89 Dr Tess Hardy, private capacity, *Proof Committee Hansard*, 14 March 2017, p. 6.

An increasing number of people are stuck in precarious employment situations, characterised by unpredictable or fluctuating income, irregular hours, uncertainty over the length of employment arrangement, a lack of basic rights and entitlements, and a lack of power to negotiate wages and conditions.⁹⁰

5.115 Anglicare Australia also noted that those most affected by unpaid SG are the same groups as those most likely to be affected by insecure work, and emphasised the need to address the problem now:

This is a direct link that cannot be ignored, both because of its disproportionate effect on people who will have the least income in retirement, and because it clearly points to an issues that is going to affect more people into the future as these economic changes progress. We need to address this now to avoid a much greater problem as the next generations enter retirement.⁹¹

Committee view

5.116 The committee is concerned that the increasing casualisation of the Australian workforce could lead to a rise in SG non-payment. As such, the committee is supportive of proposals (such as the removal of the \$450 per month threshold mentioned earlier in this chapter) that eliminate an incentive for the unnecessary casualisation of the work force.

5.117 The committee is also of the view that it is crucial for the government to consider legislative changes that work to combat the compliance challenges that arise from an insecure, casualised workforce characterised by a large number of fragmented organisations and supply chains.

5.118 As such, the committee urges the government to consider the merits of amending the SGA Act to extend liabilities of unpaid SG to corporate entities, similar to the expanded accessorial liability provisions for franchisors and holding companies in relation to unpaid wages, as proposed in the Fair Work Amendment (Protecting Vulnerable Workers) Bill 2017.

Recommendation 9

5.119 The committee recommends the government consider amending the SGA Act to extend liabilities of unpaid SG to corporate entities, similar to the expanded accessorial liability provisions for franchisors and holding companies in relation to unpaid wages, as proposed in the Fair Work Amendment (Protecting Vulnerable Workers) Bill 2017.

90 Anglicare Australia, *Submission 22*, p. 1.

91 Anglicare Australia, *Submission 22*, p. 1.

