

Review into the Tax Office's administration of the Superannuation Guarantee Charge

Submissions of:

Australian Council of Trade Unions
Industry Super Network
Industry Funds Credit Control
Australian Institute of Superannuation Trustees

ACTU



Industry
Super
Network



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Introduction

The modern superannuation system in Australia has served working Australians and the economy well. The unique compulsory retirement savings system is a key foundation of Australia's retirement system. There are currently a number of reviews relating in whole or part to the superannuation system. These joint submissions highlight the simple fact that for many Australians the greatest impact on the level of their retirement savings will be the non-payment of the correct superannuation entitlements.

This submission is made jointly by the Australian Council of Trade Unions (ACTU), The Industry Super Network (ISN), Industry Funds Credit Control (IFCC) and the Australian Institute of Superannuation Trustees (AIST).

The parties to these submissions have been involved in enforcement of superannuation guarantee entitlements since the commencement of the superannuation guarantee and welcome the opportunity to make these submissions.

These submissions offer a number of proposed solutions to an ongoing problem impacting on the retirement savings of millions of Australians.

1. Statistics on non-compliance

There is limited public information on the extent of employer non-compliance with their SG obligations.

ATO data

During the late 1990s, the ATO also conducted annual surveys of SG compliance based on a statistical survey of employers. The surveys found that 27-28% of employers were non-compliant with their SG obligations, including 1% of employers who wholly failed to pay any superannuation contributions for their eligible employees. The average shortfall was \$300 per employee.¹ By 2007-08, the average shortfall had risen to \$1814 per employee.

According to the ATO, the non-compliant employers are 'usually small businesses with less than 10 employees, whose failure to pay generally extends over several years'.²

According to the ATO employers in hairdressing and beauty, engineering design and consulting, and building and industrial cleaning are at a higher risk of not meeting their superannuation obligations.

The recent introduction by the ATO of a superannuation guarantee charge statement and calculator tool is a welcomed one, intended to assist employers to calculate their obligations

¹ Statutory Declaration of Graeme Robert Wilkinson (Acting Assistance Commissioner of Taxation) (20 September 2002) Royal Commission into the Building and Construction Industry, exhibit 1517.

² AO Compliance Program 2002-03

and for employees to establish whether they have a right to superannuation and the level of superannuation.

Extrapolating from these figures, we can estimate that:

- More than 500,000 employees are not receiving their full superannuation entitlements. (If we assume that the average private sector business employs 6 employees,³ and that there are about 840,000 employing businesses,⁴ and that 30% of businesses are non-compliant).
- More than \$900 million is outstanding in unpaid superannuation entitlements. (If we assume a shortfall of \$1,800 per employee.) This compares to \$3.5 billion in unpaid income tax.⁵
- More than 50,000 employees are working without accruing any superannuation. (If we assume that 1% of private sector businesses wholly fail to make SG contributions.)
- Fewer than 5% of employees who have not received their full superannuation entitlements make a complaint to the ATO.

Industry data

Industry Funds Credit Control Pty Ltd (‘IFCC’) manages superannuation arrears for a wide range of industry superannuation funds, including AustralianSuper, REST, CBUS, CARE, MTAA, HIP, AMIST and CLUBPLUS. Together, these funds hold 4.5 million accounts, or nearly 20% of the 24 million public and private superannuation accounts in Australia.⁶

According to their databases, in 2008/2009 there were almost 430,000 superannuation accounts in arrears (up from 310,000 in 2005/06)⁷. Approximately 75% of these employers employed fewer than five employees (according to their last return).

It should also be noted that many employees who are entitled to superannuation guarantee payments simply do not enter the system. This applies to employees paid cash in hand, those who work a combination of cash in hand and taxable shifts and those employees for whom superannuation guarantee payments have never been paid.

Not every employer with a fund in arrears has technically breached its SG obligations. For example, an employer’s legal obligations are satisfied by mailing a cheque to their employees’ superannuation fund, even if there is no covering letter identifying the employees in respect of whom the payment is made. Many small businesses are in arrears (but technically compliant with the law) because of this phenomenon.

³ ABS, Small Business in Australia (2001) cat 1321.0, 6.

⁴ ABS, Counts of Australian Businesses, Including Entries and Exits (June 2003-June 2007) cat 8165.0, 6.

⁵ ATO Annual Report 07-08, 45.

⁶ <http://www.apra.gov.au/Statistics/upload/June-2008-revised-Annual-Superannuation-Bulletin1.pdf>

⁷ It should be noted that IFCC figures include some recurring debtors and are in some cases not outstanding superannuation guarantee payments due to the monthly collection of payments.

Extrapolating from the IFCC figures, it seems that there might be 2.4 million (public or private offer) superannuation accounts in arrears in Australia. This figure, representing about a third of the employed workforce, is consistent with the other figures presented here.

Fair Work Ombudsman

The Fair Work Ombudsman (‘FWO’) (formerly the Workplace Ombudsman) has the power to enforce employers’ workplace obligations – including superannuation obligations under workplace awards and agreements — in respect of employers in the federal industrial relations system.

Because of the link between the correct calculation and payment of the employee’s wage, and the proper calculation of the employer’s superannuation liability, it is usually the case that an underpayment of wages automatically results in non-compliance with the employer’s SG obligations. Moreover, the FWO’s enforcement activities demonstrate that employers who deliberately underpay employees often deliberately avoid making superannuation payments to them (in whole or part).

Because of the link between underpayment of wages and non-compliance with SG obligations, we can use the FWO’s data relating to wage underpayment to estimate the level of non-compliance with superannuation obligations.

In March 2009, the FWO completed an audit of the hospitality industry. It found that 34% of employers operating pubs, taverns and bars were in breach of their employment obligations. (The figure was as high as 68% in New South Wales). The majority (83%) of these breaches were underpayment matters, while 17% were breaches of record-keeping obligations, including failure to record ‘the amount of superannuation contribution and the name of the superannuation fund’ on payslips.

Similar results have been found in audits of other industry sectors. These audits confirm the suggestion that approximately one third of employers underpay employees, and therefore fail to meet their proper SG obligations too.

Unions

Unions often receive complaints from members about unpaid superannuation. There are no figures on how many complaints are made, but reports from union organisers would support the notion that at least a third of employers are non-compliant with their SG obligations.

In addition to formal non-compliance, the ACTU is aware that in many industries employers regularly engage workers as sham contractors to avoid their SG liabilities. One independent study suggests that as many as 45% of the workers in the construction industry are sham contractors.⁸

⁸ Michael Wilson, ‘Remedies for Non-Compliance with Legislated Occupational Superannuation Requirements in the Building and Construction Industry’ (June 2004) Report to the Queensland Department of Industrial Relations, 16.

Since July 2008, an employee's notional earnings base is the employee's ordinary time earnings (OTE). Ordinary time earnings are the total earnings in respect of ordinary hours of work and earnings consisting of over award payments, shift loadings, commissions and some bonuses.⁹

At a recent Administrative Appeals Tribunal case, the Tribunal affirmed the Commissioner's declaration that bonus payments by a corporate taxpayer to its employees are considered ordinary time earnings. The Tribunal held that such bonuses must be included when determining superannuation guarantee contributions.¹⁰

It is suggested that many employers are not aware of their changed obligations in relation to the calculation of superannuation and that further educative processes from the ATO will assist employers in meeting these obligations and reduce any penalties that could otherwise be applied.

2. Handling of arrears

Arrears in employees' superannuation accounts may be handled by a wide range of actors, including the employee's union, their superannuation fund, a debt collection agency, the FWO or the ATO.

Although this inquiry focuses on the role of the ATO, it is important to appreciate the context in which the ATO operates, and the other actors involved in the same regulatory space.

Unions

Unions have a statutory right of entry to inspect employer's pay records if an underpayment of superannuation is suspected. However, under Work Choices, a union's right to enforce superannuation payments was removed if the employer made a non-union collective agreement with its workforce, or if it made Australian Workplace Agreements with its employees. As a result, the role of unions in enforcing superannuation payments has been greatly diminished in industries, such as mining, where employers have pursued a strategy of union avoidance.

Even under the new *Fair Work Act*, if an employer makes an enterprise agreement (with or without a union's participation) that is silent on the matter of superannuation, then superannuation loses its status as an industrial issue and neither the union nor the Fair Work Ombudsman have any role in enforcing it.

A further problem faced by unions when enforcing members' entitlements is the fact that the ATO reportedly insists on only dealing with the employee complainant directly, and refuses to deal with their union or other representative.

⁹ See Ruling SGR 94/5 for the Tax Commissioners view on the meaning and scope of 'salary and wages'.

¹⁰ *Prushka Fast Debt Recovery Pty Ltd and FCT*, AAT August 2008

Many employees lack the resources, ability or understanding of superannuation to adequately pursue their superannuation entitlements.

Fair Work Ombudsman

The FWO has the power to enforce award and workplace agreement provisions that contain superannuation obligations, in respect of employers in the federal industrial relations system. It has powers to enter workplaces, seize documents, and so forth.

However, there are only 200 inspectors for the entire country, and the inspectorate has a policy of not prosecuting underpayments of less than \$5,000 (see FWO Litigation Policy, cl 12.1(ii)). This means that many employers avoid detection and also prosecution.

A further problem is that it also seems that where an employee makes a complaint of underpayment of superannuation, without an accompanying complaint of underpayment of wages, the FWO simply refers the employee to the ATO, even if the underpayment of the superannuation is also a breach of an industrial award or agreement (which is the FWO's responsibility).

A final problem is that, like unions, the FWO loses the power to enforce superannuation entitlements in workplaces where an enterprise agreement is in place that is silent on the question of superannuation.

Superannuation funds

Traditionally, superannuation funds and employers had a closer legal relationship than is now the case. Before the advent of choice of fund legislation in 2005, employers were bound as a participating employer to a particular fund, either through the Trust Deed of the fund, through a separate Participation Agreement, through the industrial awards system, or in the case of public sector funds, through Acts of Parliament.

This closer legal relationship meant that funds were in a stronger position to enforce payment of contributions, the frequency of those payments, and requirements for employers to furnish sufficient information to allow speedy and efficient allocation of contributions to individuals' superannuation accounts.

The advent of choice of fund has significantly eroded, and in many cases eliminated those legal relationships. Consequently, even though many funds' Trust Deeds still provide power for the trustee to forcibly collect contributions, they often lack the legal leverage to do so.

Where some leverage remains available to trustees, the costs of exercising it can be prohibitive. The major fund administrators for the Industry Super Funds (Superpartners and Australian Administrative Services) maintain a database which automatically identifies arrears in superannuation accounts. At first instance, an employer in arrears is sent a reminder letter. If the problem is not resolved within the indicated timeframe, a second reminder is sent. If payment is still outstanding after a further period, the file is sent to a debt collection agency (such as IFCC) for action.

The role of the IFCC is to identify the reason for the apparent underpayment and to recover any moneys owed on behalf of the fund. Most underpayments are remedied voluntarily, although the IFCC pursues approximately 400 employers through the legal system each year. It recovered approximately \$75 million in unpaid superannuation last year.

In performing its compliance work, the IFCC also identifies and attempts to remedy other compliance issues, such as cases where:

- The business has ceased to operate;
- The employee has left employment;
- The employer has changed address; or
- Payments are misallocated (because of the employer's failure to accurately identify employees);
- The employer is claiming to employ fewer people than it does.

In addition to underpayments made in the course of operating, superannuation funds regularly deal with employers who have ceased trading because of insolvency, and have outstanding superannuation obligations. These matters are also referred by the funds to debt collection agencies, such as the IFCC. At any one time, the IFCC runs approximately 4,000 insolvency files. This figure is likely to rise, given present economic circumstances.

The IFCC also regularly encounters problems with 'phoenix companies'. It is usually not cost effective for debt collection agencies to seek to pursue the directors involved, given the high cost of litigation.

The ATO

The history of the ATO's handling of superannuation complaints, as we understand it, is as follows.

Prior to October 1998, the ATO investigated SG compliance on the basis of complaints made by employees and the public. It received and investigated 5,000 complaints per year.¹¹

In October 1998 the ATO changed its compliance approach. It adopted a practice of simply recording complaints on a database, and sending the employer a form letter reminding them of their obligations. Only 'high risk' employers were subject to audits.

In the period from 1998 to 2002, approximately 15,000 SG audits were conducted per year. Those audits revealed an average level of non-compliance (in 2002) of \$10,600 per employer. Almost 700 staff was allocated to the SG compliance unit.

In 2003-04 the ATO experienced 'systems problems' which meant that fewer than 10,000 of the 16,000 SG audits were finalised in that year. In that year, 326 employers were fined for

¹¹ Peter Costello, 'Superannuation: Compulsory Contributions Investigations' (13 May 1999) Answer to Question on Notice 504. *Hansard* 5480.

failing to provide information to the ATO about their SG payments. The average fine was only \$635.

In 2004-05 there were further 'problems with [its] business systems ... which caused delays' in SG administration. However, 12,700 audits were completed, and 242 employers were fined for not cooperating with the ATO (average fine: \$829).

In 2005-06, the ATO investigated 27,800 employers for non-compliance with SG obligations. Approximately 9,500 employers were found to be non-compliant. However, most of these investigations appear to have been conducted through data-matching or telephone inquiries; it seems that only 3,400 'hard' audits were conducted.¹²

In 2007-08, the ATO investigated more than 20,000 employers for non-compliance with SG obligations. As a result of these investigations, \$381 million in unpaid SG charges were discovered, covering around 210,000 employees (or \$1814 per employee). Just over \$288 million of these entitlements were recovered, leaving a shortfall of \$93 million (or \$443 per employee affected).

The ATO currently employs 1,105 staff (out of 23,303) in its superannuation division, plus 2,343 in its debt division. It is not clear how many staff is responsible for the investigation and prosecution of unpaid SG contributions.

We are told that the ATO's staff are overwhelmed by the amount of work to be done. For example, recently the ATO has asked superannuation funds to stop reporting 'lost super' accounts, because it does not have the resources to process all of those reports.

It is also apparent that the ATO does not have the resources to perform thorough investigations and debt collection activities in the superannuation area. Although tax inspectors have powers to enter premises and seize documents (*Income Tax Assessment Act 1936* s 263), we are told that the ATO's superannuation unit is based in Canberra, and does not send inspectors into workplaces to investigate complaints about superannuation matters. It is also not clear the degree to which the ATO cooperates with the FWO, if at all.

Finally, the IFCC reports that in insolvency cases, it is rare for the ATO to lodge a formal proof of debt in relation to unpaid superannuation amounts. It appears to leave pursuit of unpaid superannuation to the superannuation funds, the employees themselves or insolvency practitioners.

4. Proposed solutions

It is clear from the foregoing material that there is a serious and extensive problem of non-compliance with superannuation obligations. As many as a third of employees, or 2.5 million people, may be affected.

¹² ATO Compliance Program 05-06, 36.

The average shortfall per employee is almost \$2,000 –a significant amount of money for an individual. The loss to the employee is compounded by the fact that unpaid superannuation does not earn any interest for them.

Aggregating these individual losses, it appears that almost \$1 billion in superannuation is being retained by employers, usually as working capital in their businesses, without any compensation to employees for the use of their money in this way.

On 20 June 2002 the Federal Government tabled its response to 16 recommendations made by the Senate Select Committee on the Superannuation and Financial Services report on the enforcement of the Superannuation Guarantee Charge.

A number of the Committees recommendations have been subsequently adopted; however recommendations that were supported or supported in principle have not yet been adopted. For sake of brevity these recommendations have not been reproduced here; we are of the view that further consideration should be given to those recommendations which are yet to be implemented.

Whilst a number of solutions are suggested below it is emphasised that the lack of resources available to the ATO to adequately deal with an underestimated problem is the key item that should be addressed as a matter of urgency.

The table below identifies some of the significant causes of the problem and suggests some solutions:

Problem	Proposed solution
Small employers' lack of awareness about their superannuation obligations.	<ul style="list-style-type: none"> • Additional resources should be directed towards education. Consideration should be given towards requiring a person proposing to start a new employing business to first attend a (free) course to inform them of the obligations as an employer.
Employers deliberately avoiding their obligations, because of the low risk of detection and the lack of tough penalties for non-complying employers.	<ul style="list-style-type: none"> • Underpayment of superannuation should be treated the same as underpayment of wages under the <i>Fair Work Act</i>, and penalised with a fine of up to \$33,000 (for corporations). • Additional resources should be directed towards compliance activities in the superannuation area. The ATO, or the FWO, should conduct a high-profile 'blitz' on superannuation underpayment in the near future, in the interests of general deterrence. • The ATO should cross-match its records on SG non-compliance with its other databases (on GST and PAYG remittances) to identify and prosecute businesses that are flout tax and wages laws. • The ATO currently collects annual returns from superannuation funds detailing contributions made at the individual member level. This material should also be cross-matched to personal tax files to

	<p>identify non-compliance with SG.</p> <ul style="list-style-type: none"> • The problem of sham contracting should be tackled more vigorously. Consideration should be given to deeming a contractor who performs more than 80% of their work for one ‘client’ to be an employee, for the purposes of the superannuation laws (as is already done in relation to personal income tax: see <i>Income Tax Assessment Act 1997</i>, div 87).
<p>The absence of any requirement upon employers to ensure that sufficient identifying information is provided to superannuation funds to enable the funds to be directed to the correct account.</p>	<ul style="list-style-type: none"> • The superannuation laws should be amended to require employers to provide funds with sufficient information to identify employees. • The law should require, or at least strongly encourage, employers to make contributions and provide information by electronic means. • Requiring sufficient data and providing it electronically could be incorporated into the present Government proposal to assist small employers via the provision of clearing house services. • Action should be taken to ensure standardised forms, electronic and paper, should be developed to assist the remittance of superannuation payments. Standardised electronic protocols should also be adopted to assist this process.
<p>The ease of ‘phoenixing’ to avoid legal obligations;</p>	<ul style="list-style-type: none"> • If a company fails, any ‘phoenix’ corporation (trading in the same type of business, with the same shareholders or directors) should be made strictly liable for the unpaid wages and superannuation liabilities of the failed company. • If a company fails owing wages or superannuation to employees that is not recovered, the directors of the failed company should be banned from managing a corporation in future (see existing section 206D of the <i>Corporations Act</i>).
<p>The multiplicity of accounts held by individuals makes it difficult to direct payments into the correct account.</p>	<ul style="list-style-type: none"> • There should be automatic consolidation of lost superannuation accounts, as is presently being considered by the government. The ISN and AIST have made submissions to Government on this matter. These submissions can be found at http://www.aist.asn.au/Pages/PolResAdv/documents/ISN_AIST_LostMembers_Submission.pdf • The adoption of standardised electronic protocols for the acceptance of SG monies would greatly reduce the level of lost accounts.

<p>The high level of incomplete or inaccurate data resulting in payments not being associated with an account.</p>	<ul style="list-style-type: none"> • The introduction of a requirement that an employer has not fulfilled their SG obligation until such time as they pass on correct monies and sufficient personal details in an appropriate form to allow the identification of the individual and account the monies are intended to be deposited. Including the provision of the correct TNF.
<p>The long gap between payments (quarterly) payments means that significant debts can accrue before arrears are detected and investigated.</p>	<ul style="list-style-type: none"> • The superannuation laws should require payment of superannuation amounts to be made at the same interval as the payment of wages. Under the <i>Fair Work Act</i>, wages must be paid at least monthly.
<p>Employees disadvantaged (because of loss of interest) if payments not made on time.</p>	<ul style="list-style-type: none"> • Employers who make late payments should be required to pay penalty interest into the employee's account, calculated by reference to the return of the fund over the period the funds were missing (provided this figure is positive). • The Commonwealth government should establish a loan fund that superannuation funds can draw upon to credit underpaid accounts with, in the event of the employer's failure to pay contributions on time. If and when a payment is made into the account by the employer (along with interest), the loan can be returned to the Commonwealth, along with any interest accrued.
<p>Unions face difficulties enforcing superannuation underpayment claims</p>	<ul style="list-style-type: none"> • The ATO should recognise the right of unions to act on behalf of members, and to act as agent for non-members (with their consent). See recommendation 6 of the Senate Select Committee on Superannuation and Financial Services report on the enforcement of the Superannuation Guarantee Charge in 2002. • Superannuation should remain an industrial matter that unions can enforce, including through their right of entry, even if an enterprise agreement is made in that workplace which is silent on the matter.

<p>Diminished ability of funds to directly enforce legal obligation for payment of superannuation guarantee</p>	<ul style="list-style-type: none"> • Consideration should be given to means by which funds can play a greater role in follow up of non or short payment of superannuation guarantee payments owed to fund members. It is suggested that is an issue that could be further examined by a working group with representation from the ATO, employers, unions and fund representative bodies.
<p>Lack of follow up by some superannuation funds of non or short payment</p>	<ul style="list-style-type: none"> • In the event that superannuation funds are empowered to pursue non or short payment there should be an associated responsibility that funds make a reasonable and timely effort to do so.
<p>The ATO lacks the resources to tackle the problem.</p>	<ul style="list-style-type: none"> • Consideration should be given to whether enforcement of superannuation obligations should be given to the FWO, or shared between the ATO and the FWO. At the very least, the ATO should consider delegating use of its entry powers to FWO inspectors. • Additional resources should be provided to whichever agency is ultimately responsible for enforcement of superannuation obligations and provision for the ongoing sharing of relevant information.