

Submission to Senate Standing Committees on Economics

The impact of non-payment of Superannuation Guarantee – *A self-assessment system that has not worked?*

I am making this submission because I believe that a Senate enquiry is the only thing that will bring to light weaknesses that justify change.

Enforced lodgment, even of nil SGC returns, and utilizing maximum penalty for non-compliance with self-assessment obligations appear to be the big stick solution need for the few employers gaming the system. In addition, normalizing the recording in electronic payroll systems of un or late paid super will help honest business meet their SGC obligations.

Universal Worker Superannuation

The introduction of a universal worker superannuation system (SG) started in the 1990's as a political response to wage increase pressure and higher expectations by workers for living standards in retirement.

The government designed a system that kept its administration costs low. They only are impacted when an employer does not pay the worker's super to the fund. High penalties in the law, make a decision to not pay super, and being drawn into The Superannuation Guarantee Charge (SGC) system, very expensive. SGC is not a tax-deductible expense. Penalty tax of 200% can apply. Interest is charged from the start of quarter not paid.

Per system design, a business will always make the payments fully on time. If they do not, and then do not report their tax liability, and need to be audited a 200% penalty should normally occur. ATO guidelines indicate this is not always happening so the ATO can seek to recover more of the 'worker's super'.

So what weakness is there in this system?

The weakness that this Senate enquiry has identified is non-payment. This weakness is a significant issue now in the media, and in my experience, a systematic condition of our economy when businesses are under high cash-flow or competition and profitability pressure.

I had expected that when the GFC hit SGC return lodgment would sky rocket. But the audit office showed no material increase. From this I have concluded SGC lodgment rates are governed by ATO resourcing levels. Currently indicated to be 170 FTE in their submission, not a big commitment towards reducing a systematic problem.

Another indicator of weakness is how payroll software is designed to deal with non-payment of SG event and tax shortfall calculation. It is my belief that all

business accounting software treat this as a general super liability, undistinguished from the liability that was generated in last weeks pay run.

I would expect that a separate tax liability account would be required in a 'Chart Of Accounts' for unpaid super by due date if SG self-assessment was a normal function element of running a business. Without this account the interest liability cannot be calculated, and the SGC tax obligation is not included in the business books. If not recorded business owners may even miss their SGC obligation or be able to hide it from their bank when they seek to borrow more money to keep the business going.

What is the scale of the problem?

ISA has been driven to do expensive studies that quantify the size of the problem because there is a gap in information due to ATO compliance focus. Unlike the UK the ATO has not believed in the past that public Tax Gap information generates confidence in the tax system.

ISA's interest is in reducing the large cost they carry in chasing up late and non-payment for their fund members. This cost reduces what they can pay to members, being not for profit, upon retirement.

The ATO said to the Senators: "*The ATO's Tax Gap Research program does include Superannuation Guarantee however to date the work has not delivered an estimate of sufficient credibility and reliability. ... Without a reliable estimate of the non-payment of Superannuation Guarantee it is not possible to estimate the fiscal impact.*"

But they also said "*In 2014-15 approximately 880,000 employers made payments of \$85.7 billion on behalf of about 11.7 million employees.*" In response to 20,000 EN they have devoted 170 of 350 FTE compliance staff & overall 500 - 650 FTE over the last few years. "*Cash flow issues are raised in approximately 70 per cent of cases as the reason for non-payment of SG when due. Poor record keeping is raised in approximately 20 per cent of cases. ... Other reasons that are given are that their lack of understanding of some of the complexities ... which leads to a misunderstanding of their obligations ... actively seeking to delay or avoid their SG obligations as long as possible and ... Case officers report a very high level of employer awareness regarding the requirement to pay SG and it is rare for an employer to claim they know nothing about SG. Those few that do usually have only one or two employee or are new to business.*"

The ATO view the problem as "*We speculate that the possible reasons for these behaviours include that employees are not interested or engaged with their superannuation until approaching retirement.*" If this is true then their compliance focused on EN strategy only addresses the 'needs' of over 45 year old workers. The 45+ age correlates with the graph the ATO provided on page 16 of their submission.

The ATO stated, "*\$670.4 million superannuation guarantee charge raised (including penalties and interest)*" principally from the 170 FTE working on SG

compliance. Each worker appears to be generating about \$4 million in SGC. Simply doubling the FTE funding for current compliance practices, I would expect, would double the charge raised. If it this thought experiment was conducted, I believe the SG Tax Gap would not be closed.

Doing more of the same is a costly form of compliance. The cost benefits of big data would not be achieved, and business behaviour not fixed.

So, it seems to me, the ISA estimates are the principle quantification estimate of the problem. The ATO compliance model fails to engage the average work, particularly young and those with low job security.

How to measure the scale of the problem

Using big data, an estimate of the SG Tax gap is possible. The ATO would need to provide two sets of data to the committee for you to do this. They have made public a 2% sample of superannuation and income tax data. In addition to this the Senate Committee needs to request an additional sample that shows 'SG tax compliance' as 'True/False' and/or '\$SG shortfall amount'.

The website www.kaggle.com will even provide specialist data analysts that will compete to make the most accurate estimate. To run a big data estimate a large sub-sample with known compliance is analyzed. The sub-set is split in two. One sub-set gives the compliance info, and this is analyzed to form an algorithm. The algorithm is then tested against the sub-set with the compliance info not given. The algorithm efficiency is ranked by how well it predicts the true SG compliance status. The best algorithm is then run against the 2% sample to estimate the SG tax gap.

The ATO via the SG Compliance work has been collecting SG compliance status on 20,000 employees/employers for years. A good algorithm will give the public what the ATO has declined to do. What is more, it will give the committee a tool to evaluate ATO performance going forward.

A good big data algorithm also will have a known reliability.

Can the ATO do their duty differently?

The ATO has been doing field and desk audits on targeted employers, and the issue of non-payment has not apparently diminished. They have reviewed penalty guidelines to increase or decrease the financial impact, and the issue of non-payment has not apparently diminished. The issue seems to be an intransient business behaviour amongst some employers. Often there is just no money left to pay the SGC at the end of a quarter, 70% of the reason for the SGC gap, or the business does not keep the records they need to lodge a SGC [20%].

I would think that if a past SGC non-compliance event is identified, the ATO should address the repeat risk. They should get an undertaking, or make an order that SGC Returns be lodged for every future quarter, including even nil SGC returns.

SG law seems to allow the Commissioner this power, but if it does not an amendment is needed. This will increase the compliance cost to employers who have been gaming the SG system, but this is justified.

The ATO would then be able to audit any 'false statements' and apply higher penalty rates going forward. The quantification of unpaid SG would then eventually correlate with unpaid SGC.

The ATO provides input into approved software design. They could require that SGC reporting needs to be built into the products used to perform most payroll functioning. This would mean Desk Audits could be quicker, and the un/late paid super shortfall calculated without resorting to complex calculations. A shorter audit turnaround period would allow greater volume, which in turn would increase voluntary compliance with SGC obligations.

The most important step the ATO could do though, is the simplification of the SGC form and lodgment process. This would require the ATO to work together with software designers to come up with simple and efficient options. Making the reporting of the tax obligation simple is a separate issue to paying the tax obligation. It is the thing that the ATO has the most power to correct.

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