



## Taxation Law update May 2009

### Employer super guarantee obligations Warning warning Will Robinson!

by Dung Lam and Peter McCrohon

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#### The trap

In these recessionary times when cash flow is tight and businesses are scrambling on occasion to pay creditors, wages, rent, borrowing costs and the tax man, it is often a temptation not to pay or to defer the payment of employees' superannuation guarantee ("SG") contributions since such payments do not appear to be as pressing. This temptation can prove to be irresistible – in the short term – and then in the longer term - because there is no regular reporting obligation imposed on employers by the Superannuation Guarantee (Administration) Act 1992.

Over the last few months a number of clients who were behind in the payment of their SG contributions have found themselves on the wrong end of a Tax Office audit or have received an 'unexpected' default assessment<sup>1</sup> from the Tax Office. Faced with a substantial tax bill we have assisted them in dealing with the Tax Office in respect of the amount of SG Charge payable, the amount of penalties imposed (seeking a remission of the whole or part of such penalty) and payment terms.

MBP Legal warns against deferring the payment of SG contributions in light of the penalties which arise on a failure by an employer to make SG contributions for its employees.

In this publication we deal with an employer's SG obligations. As usual with tax and superannuation law, everything is technical. We suggest employer clients read this publication carefully.

Please feel free to forward this email to your friends, clients and associates if you believe that they will find the information interesting.

#### What are an employer's SG obligations?

Generally, an employer is required to make SG contributions by the 28<sup>th</sup> day after the end of a quarter (i.e. 28 July, 28 October, 28 January and 28 April). The size of the SG contribution which must

<sup>1</sup> Pursuant to section 36 of the SGAA.



be made by an employer in respect of each employee is broadly 9% of an employee's ordinary time earnings.

## What happens when an employer does not meet their SG obligations?

Where an employer fails to make SG contributions by the required due date, then the employer is required to pay a SG Charge **and the employer must lodge a SG Charge Statement** by the 28<sup>th</sup> day of the second month after the end of the relevant quarter (i.e. 28 August, 28 November, 28 February and 28 May).

If an employer fails to lodge a SG Charge Statement then this failure to lodge results in an automatic penalty arising equal to 200% of the SG Charge as discussed below (this is in addition to the SG Charge).

Continued non lodgement by an employer will often result in the Tax Office issuing a default section 36 assessment based on the Commissioner's estimate of the true SG Charge liability. **The employer then has the arduous task of preparing a formal objection (required under the Taxation Administration Act 1953) and must substantiate any decrease in the SG Charge. The objection must be prepared carefully and there is a strict time period in which the objection must be prepared. If you have received a default assessment then we recommend that you contact us immediately.**

## What is the SG Charge?

The SG Charge is **greater than** the SG contribution amount that an employer is initially required to pay to meet their SG obligations. Broadly, the SG Charge is equal to

- the amount of the SG contribution shortfall; plus
- an interest component and an administration component.

The interest component is calculated at the rate of 10% per annum on the SG contribution shortfall and is calculated from the beginning of the quarter in which the shortfall occurred up until the date when the SG Charge is required to be paid.

**The additional sting in the tail of paying the SG Charge is that it is not tax deductible.**

This contrasts with SG contributions which are broadly tax deductible where the contributions are made to a complying superannuation fund, and are made in respect of an employee who is either under the age 75 years or is covered by an industrial award.

Accordingly, if you fail to meet your SG contribution obligations not only are you buying yourself an increased liability and extra administrative costs in having to lodge a SG Charge Statement but you are also losing a valuable tax deduction!

## Should you make out of date SG contributions?

If you are late with your SG contributions then MBP Legal recommends that you **not** make out of date contributions to your employees' superannuation funds, but rather you should take care to pay the SG Charge and lodge the SG Charge Statement by the relevant due



date. The ATO will then, after deducting a portion for administration costs, forward the remaining SG Charge to an employee's superannuation fund for their benefit.

Until recently the golden rule was an employer should **never** make out of date contributions to its employee's superannuation fund, where it missed a SG contribution deadline. This was because, until very recently, the superannuation guarantee law did not generally recognise the payment of late SG contributions.

Accordingly, an employer who made out of date contributions could be liable to pay SG contributions twice – i.e.,

- once being the out of date contributions, and
- then again when they paid the SG Charge levied as a result of the missed deadline.

Late payments in respect of unpaid SG contributions made by an employer will not be classified as SG contributions. Such payments may not always be "lost" and can be treated as an advance payment of future SG contributions provided the payment is for a future SG contribution quarter that is not more than 12 months after the payment is made. However, late payment of an SG contribution cannot be used as an advance payment where the employee has ceased employment. As such and prior to recent amendments to the law, the late payment of SG contributions for departed employees would be lost.

Legislative amendments (generally effective from 1 January 2006) now allow an employer to use out of date contributions to offset a SG Charge liability. However, since offsetting is a formal process that can only be undertaken in certain situations and in the case of offsetting against a SG Charge, involves completing and lodging approved forms with the ATO, MBP Legal generally recommends that a late payer not make out of date contributions and just comply with the SG Charge obligations. Furthermore if there are unpaid SG contributions dating back to before 1 January 2006, there are a myriad of transitional rules relating to offsetting that may apply.

## What if an employer is late in paying the SG Charge and lodging a SG Charge Statement?

Where the SG Charge is not paid by the due date, then an employer is liable to pay general interest charge ("**GIC**") on the SG Charge until it is paid. The GIC applies on a daily compounding basis and changes each quarter. Currently, the GIC is a significantly high 10.16% per annum. The GIC is tax deductible but given its high rate, is an interest expense to be avoided.

Failing to pay the SG Charge can also expose an employer to significant penalties. For instance, an employer who fails to lodge a SG Charge Statement by the due date is liable for a penalty of 200% of the SG Charge. Should the ATO audit an employer and discover that they have failed to meet their SG contribution obligations, then the ATO may separately impose another penalty of 75% of the SG Charge. The ATO has indicated in a Practice Statement that it will generally remit the 200% penalty to nil where an employer lodges SG Charge statements and pays its SG Charge liabilities prior to any action by the ATO. The ATO also indicates that it may remit the 75% penalty where the 200% penalty otherwise applies.



## Links with other employee tax issues

Where an employer has failed to meet its SG contribution obligations for a number of years, the outstanding GIC and the SG Charge liabilities can be considerable. It is noted that there is a link with NSW payroll tax in that where an employer has failed to pay its SG contributions or the resulting SG Charge, then the employer will have underpaid its payroll tax. This is because a SG contribution and a SG Charge are included in the definition of taxable wages, for NSW payroll tax purposes.

Since the SG Charge is greater than the SG contribution which an employer would otherwise have to pay in respect of an employee, not paying SG contributions on time also increases an employer's payroll tax liability.

The link with payroll tax is not to be unexpected since most employment taxes are interrelated. Often a business may get itself into trouble with its employer obligations where it engages contractors. In these financially tight times where there are hiring freezes and cut backs to staff numbers, engaging a contractor may be seen as an easier way of stretching the staff budget.

A business should always ensure that it characterises a contractor relationship correctly and not always assume that a contractor is truly an independent contractor. Should a business wrongly classify a contractor as an independent contractor, rather than as an employee then a cascade of problems may arise not only in respect of SG obligations and payroll tax but also Pay-As-You-Go (PAYG) withholding tax, fringe benefits tax, workers compensation law, employment law and even GST in relation to the payments made to the contractor.

## Take home message

In summary the "take home" message of this update is that an employer should save itself the pain, time and hassle and keep happy employees by meeting their SG contribution obligations.

If you have any superannuation guarantee concerns, MBP Legal can assist in clarifying an employer's superannuation guarantee liabilities and penalty issues. MBP Legal can also provide commercial and tax advice on employee / contractor relationships and tax advice on employer obligations in respect of PAYG withholding tax, fringe benefits tax and payroll tax.

If you have received a default SG Charge assessment from the Tax Office then you need to object otherwise you will be bound by the default assessment. Most default assessments are guesstimates by the Tax Office and often overstate the SG Charge payable. You will also lose the ability to reduce or have remitted any penalties imposed.