Phoenix activity involves the ‘deliberate, systematic, liquidation of a company to avoid the payment of liabilities, including employees’ wages, superannuation, outstanding taxes and business creditors. The company then ‘rises from the ashes’ conducting the same business free from all debts under a new or similar identity.

Fraudulent phoenix activity typically occurs when individuals use limited liability companies to accumulate debts that are usually owed to the Australian Taxation Office (ATO), then liquidate the companies concerned and then carry on the same business through a newly formed company. The effect is that in almost all cases the companies placed into liquidation, have no assets.

Fraudulent phoenix like activity isn’t a new phenomenon and was associated with the ‘bottom of the harbour’ tax avoidance schemes prevalent in Australia during the 1970s. The Victorian Parliament Law Reform Committee (VPLRC) tabled a report in 1994 which had several recommendations dealing with and detecting phoenix activity. This report was the catalyst for the ATO to launch the ‘Phoenix Project’ in 1998, with a focus of tracking companies involved in fraudulent phoenix activity.
The early focus of government efforts on fraudulent phoenix activity was within the construction and building industry, specifically in New South Wales. However, other industries where labour costs are high are also greatly affected by this type of activity. The start of the 2007 global financial crisis increased phoenix activity in other industries where companies were seeking to gain a cost advantage over their competitors.

The size of the problem of fraudulent phoenix activity is difficult to estimate but appears to be substantial. In March 2010, the Assistant Treasurer Nick Sherry said that the ‘latest estimates show phoenix activity may be ripping up to AUD 600 million form the national revenue base’. The cost of phoenix activity is estimated between AUD 1.78 billion and AUD 3.19 billion per year, representing a significant amount of lost revenue each year.

Phoenix activity in many of these labour industries was borne out through sham contracting where the employer disguises an employee’s relationship as a client or an independent contractor. Through sham contracting, employers can avoid paying annual leave, sick leave and other associated entitlements if the company becomes insolvent.

This article explains and investigates fraudulent phoenix activities in Australia, the nature of the problem and its size. Phoenix activity is prevalent in the area of unremitted employees’ superannuation guarantee contributions. The Commonwealth Government has increased its efforts to combat fraudulent phoenix activities however this article proposes new measures to combat fraudulent phoenix activities, specifically in relation to unremitted superannuation contributions and through improved online reporting relationships between the Australia Tax office and compliance of companies.

This article also highlights the consequences of fraudulent phoenix activities whereby employees can lose their superannuation entitlements, creditors cannot recover their money and the government loses on non-payment of taxes, superannuation, workers’ compensation premiums and long service leave contributions. The effect of phoenix activity has further implications on the broader community, as more of these people will need to seek government assistance in the form of aged pensions when they retire.
PHOENIX ACTIVITIES AND SUPERANNUATION ENTITLEMENTS

1. INTRODUCTION

The ‘phoenix’ in Greek mythology is described as a mythical bird of great beauty reputed to live for 500 or more years. When the phoenix reaches the end of its lifespan, it builds a nest and burns itself on a funeral pyre, emerging from the ashes as a new phoenix that replicates its previous lifespan.\(^1\) The phoenix is associated with the sun and symbolises immortality, resurrection and life after death. To ‘rise like a phoenix from the ashes’ means to emerge renewed after an apparent disaster or destruction,\(^2\) which can be associated in a legal context to a ‘phoenix company’ where insolvent businesses start up again under a new or similar identity.\(^3\)

This article explains and investigates fraudulent phoenix activities in Australia, the nature of the problem and its size. Although the Commonwealth Government has increased its efforts to combat fraudulent phoenix activities, this article argues that more is required to be done. Phoenix activity is prevalent in the area of unremitted employees’ superannuation guarantee contributions, which is the focus of this article.

The structure of this article is as follows. The first part describes what fraudulent phoenix activity is, including an examination of industries where such activities have taken place. The second part discusses the effect that fraudulent phoenix activity has on employees’ superannuation guarantee contributions. Lastly, this article proposes a new system to

combat fraudulent phoenix activities in the area of unremitted superannuation contributions.

2. **WHAT IS FRAUDULENT PHOENIX ACTIVITY?**

Fraudulent phoenix activity involves company directors abusing the protection afforded by the corporate form by deliberately and systematically liquidating a company to avoid the payment of tax liabilities, such as those arising from employee wages, superannuation contributions and business creditors. This is usually achieved by directors of limited liability companies accumulating debts, then liquidating the companies concerned and later reinstating the same business under the guise of another company free of those debts, with the new company being controlled by the same directors. According to the Australian Taxation Office (ATO), in almost all cases which involve fraudulent phoenix activity, the entities placed into liquidation have no assets, with the added possibility that some of these companies may have been technically trading for some period whilst insolvent.

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6 Ibid.
PHOENIX ACTIVITIES AND SUPERANNUATION ENTITLEMENTS

Fraudulent phoenix activities are not a new phenomenon. In fact, fraudulent phoenix activities can be associated with the ‘bottom of the harbour’ tax avoidance schemes prevalent in Australia during the 1970s. Companies with tax liabilities would use the bottom of the harbour schemes by stripping the companies of their assets, which would then be sold or transferred to an entity that would not be able to pay the tax liability. These transactions were achieved by a promoter (such as a lawyer or accountant) who would assist the owners by transferring the assets from the old company to a new company, with the business continuing in the new company. The old company was then sold to the promoter for the value of the profit, less a commission (such as 10%). The promoter would then find someone with limited means who had no knowledge and no interest in looking at the books to sell the company to, and would keep the commission.9

Metaphorically, the company once stripped was sent to the ‘bottom of the harbour’ by transferring the company to someone that had no interest in its past history, or to someone who had limited means. Many companies avoided tax in the 1970s as it was not clear whether tax avoidance was illegal. The Crimes (Taxation Offences) Act 1980 (Cth) made these tax evasion schemes illegal.10

Concerns in relation to fraudulent phoenix activity can be traced back as far as 1994, when one of the first reports

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emanated from the Victorian Parliament Law Reform Committee (VPLRC).\textsuperscript{11} That Committee recommended that the laws should be tightened when dealing with the disqualification of directors of companies, more resources should be allocated to detect phoenix activity and for prosecution of offenders, increase public awareness that it is a serious offence, improve the way information is collaborated between regulators, and to enact laws to freeze assets so that creditors who have a claim can access them.\textsuperscript{12}

This report was the catalyst for the ATO to launch the ‘Phoenix Project’ in 1998, with a focus of tracking companies involved in fraudulent phoenix activity by allocating more staff to collaborate with other agencies.\textsuperscript{13} The Australian Government has since established the Inter-Agency Phoenix Forum in 2013, so that key government agencies can share, identify and deter fraudulent phoenix activity.\textsuperscript{14} The ATO has established project teams to focus and manage specific areas of risk arising from areas such as superannuation debts and phoenix companies.\textsuperscript{15}

\textsuperscript{13} Ibid 414.
\textsuperscript{14} The members of this Forum are: The Australian Crime Commission (ACC); Australian Federal Police (AFP); Australian Securities and Investments Commission (ASIC); Clean Energy Regulator (CER); Department of Education, Employment and Workplace Relations (DEEWR); Department of Sustainability, Environment, Water, Population and Communities (DSEWPaC); Fair Work Building & Construction (FWBC); Fair Work Ombudsman (FWO); and the ATO. See specifically, Australian Taxation Office, Australian Government, Inter-Agency Phoenix Forum <http://www.ato.gov.au/General/Gen/Inter-Agency-Phoenix-Forum>.
\textsuperscript{15} Inspector-General of Taxation, Australian Government, Review into the Tax Office’s Small Business Debt Collection Practices – Summary
PHOENIX ACTIVITIES AND SUPERANNUATION ENTITLEMENTS

From 1999 to 2005, the ATO raised around AUD 335 million in tax and penalties from its phoenix project.\(^{16}\)

With the collapse of many prominent businesses in the 1990s, the Commonwealth Government enacted Part 5.8A of the *Corporations Act 2001* (Cth). This was designed to protect the entitlements of a company's employees from agreements and transactions entered into with the intention of defeating recovery of those entitlements. Part 5.8A sets out the entitlements subject to legislation and whose entitlements are protected under s 596AA\(^{17}\), while s 596AB “prevents the recovery of the entitlements of employees of a company or of significantly reducing the amount of the entitlements of employees of a company that can be recovered”.

Part 5.8A is narrow in its scope and application. In particular, s 596AB prescribes that it has to be proven that the directors intentionally prevented or significantly reduced the amount of employee entitlements. As there are significant costs involved in litigation, it might discourage employees or a liquidator to try and attempt to go to court under Part 5.8A, as the requisite intention is difficult to prove.\(^{18}\) Employees of phoenix companies will not be protected under Part 5.8A because the company is deliberately stripped of assets before going into liquidation, thus making the employees ineligible for employee protection. Employees or the liquidator would have to


\(^{18}\) Ibid 13.
go to court, and as there are significant costs involved in litigation, employees or a liquidator may not go to court.\textsuperscript{19}

The early focus of government efforts on fraudulent phoenix activity was within the construction and building industry, specifically in New South Wales. Fraudulent phoenix activity is not limited to the building and construction industry.\textsuperscript{20} It is also involved in other industries where labour costs are high, including labour hire, employment, security, road transport, hospitality, manufacturing, fruit harvesting and the cleaning industry.\textsuperscript{21} Due to the global financial crisis, phoenix activity has spread to other industries where businesses are seeking to gain a cost advantage over their competitors. Entities in the building, construction, and textile industries may be expected to have a greater tendency to engage in fraudulent phoenix activities as those sectors have relatively low barriers to entry. These companies that are involved in phoenix activities can undercut their competitors when tendering as they do not anticipate fulfilling their tax obligations.

Sham contracting occurs when the employer tries to disguise an employee’s relationship as a client or an independent contractor. This is widespread throughout the Australian economy, though is overly represented in the construction industry. Through sham contracting, employers can avoid paying annual leave, sick leave and other associated entitlements. This leads to workers risking their claim to their entitlements to be paid for the work done. If the company becomes insolvent, the workers involved in sham contracting arrangements are unable to claim their entitlements as a wage earner; instead they can only claim as an unsecured creditor.\textsuperscript{22}

\begin{thebibliography}{99}
\bibitem{19} Ibid 14.
\bibitem{20} Sherry, above n 3.
\bibitem{21} Darmanin, above n 8, 6.
\bibitem{22} Office of the Australian Building and Construction Commissioner, Australian Government, ‘Sham Arrangements and the Use of Labour
\end{thebibliography}
PHOENIX ACTIVITIES AND SUPERANNUATION ENTITLEMENTS

The rise of sham contracting arrangements has propelled an increase in fraudulent phoenix activity. Sham contracting can shift the responsibility for items such as workers’ compensation to the employee, leaving them inadequately compensated. Given the nature of the construction industry as one prone in which serious injuries may arise, this can leave an employee with a significantly reduced income for the rest of their lives. Sham contracting can also have an impact on superannuation by disguising an employee as an independent service provider under a contract; the employer may then fail to contribute to the employee’s superannuation. When these employees retire, greater support from the government is required in the form of the age pension.\(^{23}\)

Chart 1 below shows the comparison of the proportion of labour force classified as employees and independent contractors by industry as at November 2009.\(^{24}\)

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\(^{23}\) Ibid.
\(^{24}\) Ibid 11.
It can be seen in Chart 1 that a high percentage of independent contractors are working in the construction industry, approximately 33 percent, making it the highest across all industries.\textsuperscript{25}

\textsuperscript{25} Ibid.
PHOENIX ACTIVITIES AND SUPERANNUATION ENTITLEMENTS

Phoenix activity also appears to be more prevalent in smaller enterprises that have a turnover of between AUD 2 million and AUD 10 million. This may be due to there being no audit requirement for a small company under the Corporations Act 2001 (Cth). Consequently, any breaches of company law by its directors can go unnoticed by the regulator. By the time the regulator is aware that directors have breached company law it is often too late as there are no assets left in the company to pay its suppliers, employees or taxes.

Directors may also participate in fraudulent phoenix activities to increase their personal wealth by saving on labour costs through the non-payment of superannuation guarantee contributions and non-remittance of Pay as You Go Withholding (PAYGW). Companies also achieve a competitive advantage by using employee superannuation guarantee contributions and taxation monies as a line of credit, thus gaining a competitive cash flow advantage over companies who properly deal with these obligations.

Fraudulent phoenix activities also have a broader impact on the economy, in particular the impact through unremitted employee superannuation contributions, which is the focus of this article. In 2009, it was estimated that phoenix activity results in lost revenue of more than AUD 600 million each year. In 2010, insolvent employers owed the ATO an estimated AUD 600.8 million in superannuation guarantee contributions.

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28 Hayes, above n 7, 7.
charges, which is written off as lost employee retirement savings.\textsuperscript{30}

Whilst the precise size of the problem of fraudulent phoenix activity is difficult to estimate, by all accounts it appears to be substantial. In March 2010, the Assistant Treasurer said that the ‘latest estimates show phoenix activity may be ripping up to $600 million from the national revenue base’.\textsuperscript{31} In February 2013, ATO Acting Second Commissioner Mr James O’Hallaran stated that it has been previously estimated that about 6,000 phoenix companies operate in Australia, a very small percentage (0.31).\textsuperscript{32} However, the cost of phoenix activity is estimated at between AUD 1.78 billion and AUD 3.19 billion per year, which represents a significant amount of lost revenue for the government each year. It is therefore an important issue for the government to address to maintain the integrity of its revenue base.\textsuperscript{33}

2.1 Court Reviews

To conclude this section, it is instructive to examine briefly some of the court cases relating to fraudulent phoenix activities, as this gives further context to the nature and scope of the problem. On 23 April 2010, the Commissioner of Taxation revealed that AUD 200 million in tax liabilities have been identified as a result of the ATO’s focus on fraudulent phoenix activities.

\textsuperscript{31} Sherry, above n 3.
\textsuperscript{33} PricewaterhouseCoopers (PWC), ‘Phoenix Activity: Sizing the Problem and Matching Solutions’ (Report to the Fair Work Ombudsman, June 2012) 1.
activity, with up to nine cases being referred to the Director of Public Prosecutions.\textsuperscript{34}

In February 2013, search warrants were issued to 80 South Australian based labour-hire companies operating in the agricultural industry and the ATO and Australian Federal Police (AFP) were working together to execute warrants for suspected criminal activity within the berry picking and meat processing sectors.\textsuperscript{35}

As noted earlier, in cases of fraudulent phoenix activities, the competitiveness of businesses is distorted due to the fact that phoenix companies enjoy lower-than-market costs. Consequently, they are able to achieve an unfair advantage in the marketplace, which in turn undermines the integrity and confidence of the marketplace, and established processes which are used for insolvency.\textsuperscript{36}

In the last six years there have been an increasing number of cases before the court that relate to fraudulent phoenix activities. In \textit{ASIC v Somerville (No 2)},\textsuperscript{37} the Australian Securities and Investments Commission (ASIC) succeeded in obtaining declarations for breach of directors’ duties under the \textit{Corporations Act 2001 (Cth)} against directors of eight unrelated companies. These companies had a common solicitor (Somerville), who advised and assisted each of those directors in relation to phoenix activities. Similarly, in June 2010, a phoenix

\textsuperscript{34} Australian Broadcasting Corporation, ‘ATO Grilled Over Tax Return Bungle’, Lateline, 23 April 2010 (Andrew Robertson) \textless http://www.abc.net.au/lateline/business/items/201004/s2880640.htm \textgreater . It is not clear why there is apparently a gap of AUD 400 million between the two figures, but it may well be the case that the figure of AUD 600 million includes moneys other than tax liabilities and/or estimates that are yet to be confirmed (with the gap thus possibly representing the difference between actual and potential liabilities).

\textsuperscript{35} Australian Taxation Office, above n 34.

\textsuperscript{36} Appleby, above n 29.

\textsuperscript{37} [2009] NSWSC 998.
operator, James Soong, was jailed for three years in the Sydney Downing Court for failing to remit to the ATO deducted tax instalments totalling AUD 6.7 million from the wages of employees of two companies that he operated.  

A more recent prosecution in relation to this case was in March 2013 in New South Wales, where Ms Desley Soong was found guilty for not complying with a Security Bond Demand Notice.

Furthermore, the ATO’s Compliance In Focus document for 2013-2014 indicates its plans to tackle medium-sized businesses using fraudulent phoenix activities to avoid financial obligations including PAYG, income tax, GST and superannuation liabilities. The ATO plans to conduct 1,000 reviews and audits and has 2,500 contacts to verify information or provide advice. The ATO will also focus on 150 cases dealing with property developers engaging in phoenix behaviour (which includes in the context failing to report the sale of developments and using liquidation to avoid GST obligations). The ATO has found over 2,000 property developers who have on multiple occasions placed companies deliberately into liquidation to avoid paying GST.

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39 The power enables the ATO to require a company to provide an appropriate tax bond where it is reasonable to expect that the company would be unable to meet its tax obligations and/or would engage in fraudulent phoenix activity. The penalty for non-compliance with a requirement to provide security has been increased from AUD 2200 to AUD 11,000 for individuals and from AUD 11,000 to AUD 55,000 for companies.

2.2 Other Government Efforts to Combat Fraudulent Phoenix Activities

Apart from court cases and ATO reviews, the government has initiated other efforts to combat fraudulent phoenix activities. The Cole Royal Commission was established in 2003 to investigate the occurrence and problems associated with fraudulent phoenix activities, especially in the building and construction industry, mainly involving underpaid workers’ compensation premiums and tax avoidance.41

On 1 November 2005, the Commonwealth Government’s General Employee Entitlements and Redundancy Scheme (GEERS) was revised in order to provide employees from a failed company with an opportunity to claim certain unpaid entitlements. However, employees could recover unpaid entitlements only if the failed company was placed into liquidation, and this might not have occurred immediately.42

In November 2009, the Treasury issued a proposals paper for public comment.43 The paper outlined possible amendments to taxation and company law dealing with matters such as: disqualification of directors; denying companies PAYGW credits; imposing bond provisions; making amendments to the

41 Appleby, above n 27, 3-4.
director penalty regime; and expanding anti-avoidance provisions.\(^{44}\)

In November 2012, GEERS was replaced with Fair Entitlements Guarantee (FEG) legislation. The FEG limitations are the same as GEERS, whereby employees cannot recover unpaid entitlements unless the company has been placed into liquidation.\(^ {45}\) Therefore, employees from a phoenix company that had not received their unpaid entitlements (due to the fact that the company had not been placed into liquidation) were left with no way of receiving their entitlements.

This was resolved by the Commonwealth Government enacting the *Corporations Amendment (Phoenixing and Other Measures) Act 2012* (Cth) (Phoenixing Act) in July 2012. The Phoenixing Act has given ASIC powers to order a company that has been abandoned by its directors to be wound up. The aim of the Phoenixing Act is to be able to facilitate the payment of employee entitlements and to facilitate the publication of corporate insolvency notices.\(^ {46}\) This is important, as it is a precondition under GEERS that an employee cannot receive payment if the employer company is not formally wound up.

The Phoenixing Act aims to remove the current impediments to workers accessing their entitlements under GEERS,\(^ {47}\) as ASIC will now be able to order a company be wound up in several circumstances, such as: the company hasn’t

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\(^{46}\) Commonwealth, Parliamentary Debates, House of Representatives, 15 February 2012, 1342 (David Bradbury).

\(^{47}\) Treasury, Australian Government, *Corporations Amendment (Phoenixing and Other Measures) Bill 2012* (Cth), Bills Digest, No 114 of 2011-12, 28 February 2012, 2-3.
been carrying on a business; hasn’t lodged any documents in the previous 18 months; it is in the best interests of the public if the company is wound up; and if there is no response from the company for six months. This would allow the liquidator of an abandoned company to investigate and report to ASIC possible misconduct by the directors of the abandoned company which has engaged in fraudulent phoenix activity, or if the abandoned company has entered into any uncommercial transactions prior to abandoning the company.48

The Corporations Amendment (Similar Names Bill) 2012 (Cth) was proposed by the former Labor government to regulate the use of similar names as an early indicator to prevent fraudulent phoenix activity, however it only addresses the issue if the company uses the same company name as the old company. It does not appear to apply to the use of a similar business name,49 or prevent incorporation of a company using a similar name that was used by the failed company.50 At the time of writing, the Bill had not been enacted. Notably, in the context of fraudulent phoenix activity, the Bill imposes liability only for the debts of the new company, not the debts of a failed company. This is inconsistent with the Government’s intentions to combat phoenix activities, as the creditors of the failed company would have been caused harm from the fraudulent phoenix activity of the directors in contrast to the new company.51

New reporting requirements in the building and construction industry have been introduced to reduce sham contracting and

48 Explanatory Memorandum, Corporations Amendment (Phoenixing and other Measures) Bill 2012 (Cth) 6.
50 Anderson, above n 12, 427.
51 Ibid.
create an alert system for fraudulent phoenix activities. From 1 July 2012 it has been compulsory for anyone carrying on a building or construction business to report details of payments made for the supply of ‘building and construction services’. The Regulations provide a list of related services that require reporting for building and construction businesses and the explanatory statement provides examples that satisfy the definition of ‘building and construction services’. The ATO can now use the reported information for data matching to detect contractors who have either not lodged income tax returns or have not reported all of their income.

In 2012, further reforms were implemented that extend the director penalty regime to make directors personally liable for their company’s unpaid superannuation guarantee amounts. This change was designed to ensure that directors cannot avoid possible penalties by placing their company into administration or liquidation when PAYGW or superannuation guarantee contributions remain unpaid and unreported three months after the due date. In some instances, the new reforms make directors and their associates liable to PAYGW non-compliance tax where the company has failed to pay amounts withheld to the Commissioner of Taxation (Commissioner). These measures have been criticised by many, including some debt collectors who have opined that these reforms were ‘useless in that all they

52 Taxation Administration Amendment Regulation 2012 (No. 1) (Cth).
53 Athanasiou and Gioskos, above n 32, 3.
54 Tax Laws Amendment (2012 Measures No. 2) Bill 2012 (Cth).
did was to give priority to the ATO. They did nothing for other creditors’. 56

Despite Government efforts, particularly over the preceding six years, to combat fraudulent phoenix activities, they have unfortunately increased. An area that urgently requires Government attention is the effect of fraudulent phoenix activities on employees’ superannuation entitlements, which is the next focus of this paper.

3. IMPACT OF FRAUDULENT PHOENIX ACTIVITIES ON EMPLOYEES’ SUPERANNUATION ENTITLEMENTS

Australia has a three-pillar system for retirement which comprises of: a means-tested age pension benefit funded by current taxpayers; compulsory savings through the Superannuation Guarantee system funded by employer contributions; and voluntary superannuation funded by personal and government co-contribution (if eligible). 57 Superannuation is an important feature of the Australian economy. It is a significant source of savings for Australian taxpayers and, with an ageing population, superannuation increasingly plays an important part to ensure that the Australian population can enjoy financial security in their future. Superannuation also ensures that the government can reduce its financial burden through age pension benefits and employees can save for their retirement by not having to rely on the age pension benefit. Employees are able to use their superannuation contributions as income.

According to the Australian Prudential Regulation Authority (APRA), contributions to June 2013 totalled AUD 115.3 billion. Contributions from employers were AUD 77.5 billion, whereas contributions from members were AUD 36.5 billion and other contributions, such as government contributions and spouse contributions, totalled AUD 1.3 billion. The total superannuation assets to the year end of June 2013 increased by 15.7 per cent from AUD 1.40 trillion to AUD 1.62 trillion.

Employers are required by law to pay Superannuation Guarantee contributions of 9.25% (as of 1 July 2013, increased to 9.5% as of 1 July 2014) to an employee’s superannuation fund within 28 days of the end of the quarter, representing a proportion of an employee’s salary or wage.

If the employer does not make the contributions to the superannuation fund within the required time, then the employer is required to complete a Superannuation Guarantee Charge (SGC) statement and pay the SGC. The SGC is calculated by adding the super guarantee shortfall amounts to a nominal interest at 10% per annum and an administration fee of AUD 20 per employee. Notably, the onus is on the employer to submit the form and inform the ATO that they have not paid the superannuation amounts to the employees’ superannuation fund. This creates a situation where some employers will not be disposed to informing the ATO, especially if they have been involved in fraudulent phoenix activities.

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PHOENIX ACTIVITIES AND SUPERANNUATION ENTITLEMENTS

When a company is engaged in fraudulent phoenix activities, unremitted superannuation could be lost and employees can lose their benefits, thus affecting an employee’s superannuation savings. As the onus is on the employer to inform the ATO, it could be months (or longer) before any shortfall is discovered and the assets of the employer in this time could be removed from an old company and allocated into a new company. Unremitted superannuation funds deducted from employees of the old company would be used in the formation of the new company, which could be considered as theft. The loss of superannuation entitlements from an employee’s perspective can be understood from a 2012 report on how a 57 year old pilot of Air Australia lost his compulsory superannuation contributions and other contributions he had made whilst salary sacrifying as much as AUD 3,000 a month towards superannuation. He said, ‘To me it is theft. The money was shown to have been deducted from my salary on my payslips but it never reached the superannuation fund, it never arrived. Where did it go? It looks to me to be fraudulent.’

The problem is that the pilot would not have been able to detect the non-remittance of his superannuation contribution.

In the paper *Combating the Phoenix Phenomenon: An Analysis of International Approach*, the extent of the effect is described as follows:

It is possible for an employee to work in the same factory, with the same machinery, for the same management, in ostensibly the same business, over the course of the employee’s working life, with no immediate realisation that the business has been perpetually phoenixed… Essentially the employee appears to be in continuous employment. However

the employee’s superannuation benefits will be significantly reduced as a result.\(^\text{62}\)

To get a sense of the scale of this issue, ASIC Insolvency statistics released on 16 October 2013 reveal that the following amounts of superannuation were unremitted for the year 2012-13: total number of complaints was 9,253; over AUD 1 million of unremitted superannuation in each of the 17 external administrations of companies or groups of companies; between AUD 250,000 and AUD 1 million of unremitted superannuation in each of 113 external administrations of companies or groups of companies; and between AUD 100,000 and AUD 250,000 of unremitted superannuation in each of 382 external administrations of companies or groups of companies.\(^\text{63}\)

This amounts to a minimum loss of AUD 83.45 million in lost employee superannuation entitlements reported in one year of external administrations, ie 2012-2013. Figure 1 below summarises unpaid employee entitlements (superannuation).


PHOENIX ACTIVITIES AND SUPERANNUATION ENTITLEMENTS

Figure 1: Initial External Administrators’ Reports by Unpaid Employee Entitlements (Superannuation), Annual Percentage


Unfortunately, this has a domino effect on the whole community given that when employees lose their pension entitlement, they tend to look towards their government for assistance. This can eventually result in increased reliance on the aged pension and thus impose a greater burden on the Government and the taxpaying community at large. In February 2010, the former Assistant Treasurer Senator Nick Sherry, in an interview with ABC Radio National, sympathised with employees who lose their superannuation entitlement because of phoenix companies, where he said:

And of course that really does hurt, not only do you lose your wages or possibly annual leave, you lose part of your future retirement income. I have to say, the whole area makes me particularly angry, but when you are also effectively denying a person part of their

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64 Ibid.
retirement income it really does get my blood boiling, I have to say.\textsuperscript{65}

4. **ARE EXISTING REGULATORY MECHANISMS EFFECTIVE?**

In light of the preceding discussion, the issue that needs to be addressed in relation to unremitted superannuation is to investigate whether current laws and regulations that are in place are sufficient mechanisms to ensure that the non-remittance of superannuation contributions does not occur, or is stopped from occurring for more than the next reporting period.

A summary of the current laws and regulations in place include: firstly, employees have a right to submit a complaint concerning unremitted superannuation arising under the superannuation guarantee legislation to the ATO, by using the form entitled, ‘Employee Notification of Insufficient Employer Contributions’, commonly called ‘ENs’.\textsuperscript{66} The efficacy of this mechanism is predicated on an employee having knowledge of contributions not being paid, or being able to act on this issue in a timely manner before the company responsible to remit the contributions is liquidated. The practical reality is that many employees may not know for some time whether their superannuation contributions have or have not been remitted and when and if they find out, their employer company may already have been liquidated. Employees may not understand what their entitlements are.

Secondly, the Superannuation Guarantee Charge (SGC) aims to penalise employers that fail to remit employees’


PHOENIX ACTIVITIES AND SUPERANNUATION ENTITLEMENTS

superannuation to their nominated fund or default fund. The SGC for an employer who does not pay the superannuation contribution to the employees fund or default fund for the quarter will be calculated at 10% from the beginning of the quarter and the employer will also have to pay a non-tax deductible administrative fee of AUD 20 per employee, per quarter.

Third is GEERS, a safety net scheme of last resort to assist employees for unpaid entitlements. Fourth, a director penalty regime enacted in Division 269 of Schedule 1 to the Taxation Administration Act 1953 (Cth) to deter directors from using amounts withheld from workers instead of paying them to the ATO or superannuation funds. It is intended to make directors think twice as they will be personally responsible if the company does not meet its tax obligations or goes into liquidation because the company cannot meet the obligations.

67 Superannuation Guarantee Charge Act 1992 (Cth).

98 JOURNAL OF AUSTRALIAN TAXATION
This paper argues that the above laws and regulations are not sufficient to detect non-remittance of superannuation contributions for the following reasons. Firstly, as noted, the SGC legislation operates by placing the onus on the employers who have not remitted the superannuation to voluntarily report this information to the ATO. Secondly, although employees can make a complaint to the ATO using the ENs, many employees would not realise that these unremitted contributions exist until it is too late. Furthermore, many employees are concerned that if they query their employer about their SG entitlement, or lodge a complaint with the ATO, then they could either lose their job or will no longer be given work.\footnote{72}{Inspector-General of Taxation, Submission to the Assistant Treasurer, \textit{Review into the ATO’s Administration of the Superannuation Guarantee Charge}, March 2010 (IGT Report).} This ignores the fact that they can check their remittances online directly using the superannuation fund in many cases, although this is valid only if the superannuation fund has online services.

In light of these practical difficulties, it is submitted that a different system of detection is required. Anderson and Hardy suggest that ‘the fact that all employers are, or should be, taxpayers, with identifying numbers, means that the ATO has an advantage in knowing about these employers. It has the computing capacity to track people and payments.’\footnote{73}{See, for example, ATO, \textit{Prepare and Lodge – Data Matching} (28 June 2013) <http://www.ato.gov.au/Tax-professionals/Prepare-and-lodge/Tax-Time-2013/Before-you-lodge/Data-matching>. The ATO reports that ‘Last year we cross-referenced information reported in tax returns against over 600 million transactions provided to us by third parties to identify omitted income and incorrectly claimed offsets’. See also ATO, \textit{How We Check Compliance – Data Matching} (22 October 2014) <http://www.ato.gov.au/General/How-we-check-compliance/Matching-data-from-many-sources>; Australian National Audit Office, \textit{Australian Government, The Australian Taxation Office’s Use of Data Matching and Analytics in Tax Administration}, (2014) 16(1) 99.}
PHOENIX ACTIVITIES AND SUPERANNUATION ENTITLEMENTS

Assistant Treasurer Nick Sherry agrees that the approach should be to try and minimise the non-payment of superannuation and other employee entitlements at its base, rather than using taxpayers’ funds to reimburse the employees for lost entitlements.74

Former Assistant Treasurer Bill Shorten has also stated that reforms are needed and that employees should receive information on their payslips when the actual amount of superannuation has been paid into their account, and they should be informed if regular payments cease by quarterly notification from their superannuation fund.75 He also indicated that more information about employees’ superannuation payments, including salary sacrificed payments, should be given to employees in a timely manner. This is in line with the Government’s recommendation in the Stronger Super76 report that:

Employers will receive additional information from superannuation funds to assist them with managing their superannuation payments. Specifically, superannuation funds will be required to provide employers and employees with electronic notification if regular superannuation payments are not being made.77

4.1 Possible New Regime

In 2011-12 the ATO received 19,400 complaints from employees regarding the reported unpaid superannuation of

74 ABC Radio National, above n 68.
75 Former Assistant Treasurer and Minister for Financial Services and Superannuation, Commonwealth of Australia 2010.
77 Shorten, above n 75, 9.
AUD 103.9 million, which has a significant effect on their retirement balances. The problem with the current system is that the ATO is alerted only after three months and 28 days from the time the employer has not paid the SG to the superannuation fund, and only if the employer completes the SGC statement notifying the ATO that all or some of the superannuation contributions to the employees’ super funds have not been made. The onus is on employers, and in some cases the employers do not fill in the forms and notify the ATO, especially if they are engaged in fraudulent phoenix activities.

Companies with cash flow problems may also have a tendency not to pay employees’ superannuation contributions. Sometimes these companies use employees’ superannuation money for their cash flow needs, with the intention of reinstating the borrowed monies from employees’ superannuation deductions as soon as the cash flow improves. In some cases the companies never repay the borrowed amounts from employees’ superannuation deductions, and as a result employee payslips will show amounts of superannuation paid, which has not been paid into their superannuation fund.

In many cases the directors of the company may deliberately not pay superannuation contributions to employees’ superannuation funds as the company has gone into liquidation.

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79 Represents the cut-off date after the end of each quarter that employers are to remit the superannuation contributions to their employees’ superannuation fund.
or transferred the business to another company, thereby partaking in fraudulent phoenix activities. In these cases, the employees will most likely not receive their superannuation contributions.

Although the ideal situation would be for companies to report to the ATO if they are generally having difficulty in paying the superannuation contributions, in which case the ATO could extend the time for payment, it is unlikely that employers using fraudulent phoenix activities will follow this course of action. If the companies are somehow forced into reporting to the ATO, then the ATO could monitor the situation, and a solution could be found earlier rather than later. In these cases employees could be notified in a timely manner that their employer has not deposited their salary sacrifice money and superannuation contributions into their superannuation funds, and that the ATO is aware of it and is monitoring it. A suggestion of how to force company directors to report to the ATO could include personal liability for the non-payment and a penalty for the company. This way, the incentive would be for employers who are having difficulty to report to the ATO.

As the responsibility is currently on employers, some employers may do the right thing by reporting unpaid superannuation contributions to the ATO. However many employers may not do the right thing and the unpaid superannuation contributions may remain unnoticed for many months. When the employee realises the failure to make superannuation payments, it is often too late. One way to deter companies from not paying superannuation funds is an early detection mechanism. This could be created by legislating for the employee superannuation contribution amounts to be paid monthly instead of quarterly, with payment cut-off dates (28 January, 28 April, 28 July and 28 October of each year) into the superannuation fund, and the employee to be notified of the payment when it has been actually deposited into the employee’s account in the superannuation fund. This
notification to the employee can be made electronically, and easily accessible to the employee at little or no cost. This could alert employees to make a complaint to the ATO in a more effective and timely manner, and the matter could be investigated before the company forms a new company. Some superannuation funds offer an online account system where the employee can monitor the superannuation deposits by their employer and match it with their payslips. However, most employees are not aware that their superannuation fund has this facility. There is also no obligation on the part of the superannuation fund to automatically notify the employee to register for the online account.

Australia’s superannuation investment is approximately AUD 1.4 trillion and AUD 9 billion a year in inflows, with over 400 superannuation and investment managers competing to manage the funds. With so many funds, an online account system could be made compulsory by legislating for all superannuation and manager funds to compulsorily set up an online account for individual employees. The system could also include an automatic email alert if the payments from the employer have suddenly stopped so that employees can be vigilant about their superannuation contributions from their employers.

Another solution could be for the ATO to make it compulsory for businesses to complete a form for Superannuation Contributions similar to the Business Activity Statement (BAS) for the collection of GST. The ATO has a tax file number (TFN) for every taxpayer (including companies) and for all employees that could be matched up with the superannuation and manager funds. Under this arrangement, a

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(2014) 16(1) 103
monthly contribution from the employer to the superannuation fund could require a superannuation contribution form to be lodged with the ATO 14 days after the end of the month. If employers do not lodge the form, they could then encounter a late penalty notice. This would encourage an employer to seek an extension from the ATO in the event the company is having cash flow problems and difficulties in paying the superannuation contributions. This would also alleviate employers using employees’ superannuation contributions and salary sacrifice monies deliberately and fraudulently for the company’s business. Although another reporting requirement may increase business accounting work flow, such a burden can be justified as this affects employees’ superannuation contributions, leaving them with significantly less money for retirement.

The regulatory authorities could also better handle the problem of unpaid superannuation. The Australian Prudential Regulation Authority (APRA), the Fair Work Ombudsman (FWO), the ATO, and the superannuation and manager funds and businesses, should work together to ensure that the employee superannuation contributions and salary sacrifice monies of employees are protected. This could be achieved by more detailed information being shared between APRA, ATO, FWO, and superannuation funds and businesses. By drawing up a memorandum of understanding, co-regulatory mechanisms or mutual understandings between agencies on how they should share the information gathered, and how they should work together to improve technology, could be attained. The *Tax Laws Amendment (Confidentiality of Taxpayer Information) Act 2010* (Cth) allows the ATO to provide information that may assist ASIC to pursue actions against directors engaged in fraudulent phoenix activity repeatedly.\(^8^2\) This could be extended

\(^8^2\) Robyn Erskine (on behalf of the Insolvency Practitioners of Australia), Submission to the Senate Standing Committee on Economics, Comments Regarding the Proposed Tax Laws Amendment (2011 Measures No. 8) Bill 2011 and the Pay As You Go
so that agencies work together to improve the way information is gathered and shared amongst them, and encourage co-ordinated campaigns and cross-training of employees. ASIC could also be involved in the sharing of information as they look after the financial markets and they would be aware of the involvement of directors with insolvency matters. This information about directors could be passed on.

The FWO obtains very useful information through its investigations into the compliance of employers with record keeping, payslip obligations and minimum wages, and this could be forwarded to the ATO, as this is something that the ATO does not investigate. Superannuation contributions could be made electronically rather than by cheque (as currently happens in some cases). The ATO has the ability to track all taxpayers with their TFN, thus giving them an advantage to know about the employers, and is able to track whether or not payments have been made. For example, with the PAYG system the ATO can observe if the employer has failed to pay the PAYG payments. If a system similar to the PAYG was implemented then the ATO could be the recipient of the superannuation contribution payments and then forward these payments to the appropriate superannuation fund provider. Even though this will create an administrative obligation to the ATO, it is a way of ensuring that employers make the required payments in time, and that employees’ superannuation contributions are be better managed and monitored. As such, it is recommended that the ATO looks after superannuation contribution payments and keep track of whether or not the contribution payments have been made, just like the PAYG system.

83 Anderson and Hardy, above n 66, 185.
84 Ibid.
85 Ibid 184.
5. Conclusion

This article submits that there is a need for appropriate measures to be put in place to combat fraudulent phoenix activities, specifically in relation to unremitted superannuation contributions. This article also highlights the consequences of fraudulent phoenix activities whereby employees can lose their superannuation entitlements, creditors cannot recover their money and the government loses on non-payment of taxes, superannuation, workers’ compensation premiums and long service leave contributions. This in turn places a higher burden on the broader community, as more of these people will need to seek government assistance in the form of aged pensions when they retire.

The following means could achieve this:

- Working on changing the legislation to make the payment of superannuation contributions compulsory. If for some reason the employer is unable to meet their responsibilities, they need to alert the ATO as soon as possible so that a solution can be worked out. Currently, it takes nearly four months for the ATO to be advised that employers are not fulfilling their responsibilities.

- It could be introduced that the non-compliance of company directors would result in a penalty for the company and a penalty personally for the directors.

- Increasing the frequency of superannuation payments to monthly will allow for early detection of non-compliance.

- Making superannuation contribution statements similar to the BAS system compulsory for companies could be a better way to ensure superannuation is paid on time. This would also allow employees to seek help.
in the form of an extension if the company is having difficulty in meeting payments.

- Better communication and liaison between all regulatory authorities by the drawing up an agreement to keep each informed and alert if a company is failing to meet the requirements.

- The online account system could be made compulsory so as to protect employees’ superannuation guarantee contributions, where non-payments are automatically detected through the use of computing systems and appropriate government agencies and employees are notified. It would also allow employees to take some responsibility in managing their own accounts.