Something fishy about wages

Jonathan Kaplan is a consultant solicitor with Meerkin & Apel Lawyers in Melbourne and is a NMAS accredited mediator. Jonathan can be contacted on (03) 9510 0366 or 0418 588 855.

The advice and information contained in this article is of a general nature only and is not intended to constitute or replace professional advice.

This month resident legal guru **Jonathan Kaplan** puts the magnifying glass on the ramifications of wage cash payments "off the book".

A recent report in the *Sun-Herald* got me thinking again about the hazards of running a business when making cash payments "off the book", and in that way obtaining some commercial benefit or perhaps even facilitating a benefit for others, though acting illegally.

The report involved a sushi restaurant chain which admitted to the newspaper that it had paid some foreign staff as little as $9.00 per hour (in cash, as alleged by some employees), which is effectively around half the minimum $19.01 to $20.26 wage under the Restaurant Industry Award 2010.

After being contacted by the newspaper about the claims, a director of the chain acknowledged that they had "mistakenly" been paying an incorrect rate due to a "misunderstanding" with some of the managers, but that the payment structure had been "revised". He confirmed that all affected would receive compensation.

The situation is very much a Catch-22. Foreign employees on a working (or student) visa often encounter difficulties obtaining employment as international students. They are then "forced" to accept lower paid jobs with low wages paid in cash.

This seems to be borne out by statements from UNITE, the union that represents fast food and retail workers in Victoria, which visited Melbourne's famous Brunswick Street cafes in a name-and-shame campaign after having received complaints against business owners over the past six months. It was alleged that one business owner was paying as little as $7 an hour!

According to research published by Monash and Melbourne universities in 2008, 60 per cent of international students were working below the minimum wage.

So, the temptation is there for both employers – and for employees unable to find more rewarding employment. Where does this leave you and what are the obvious dangers?

When the Australian Tax Office introduced the GST, it had hoped that it would be more difficult for non-compliant business owners in the so-called "cash economy" to operate on the same basis as they had pre-GST. It has become harder for them but there is clear evidence that the hole has not been plugged. In fact, it seems to be leaking like a sieve.

In order to consider the legal risks and consequences, we need to take a look at the circumstances in which cash might be used to pay wages and in that way highlight the apparent dangers.

I used to own hospitality businesses and often had mates look at me with some kind of envy as an owner of a "cash business". They made it sound quite appealing, but when I explained the legal and commercial consequences of "pocketing" cash or paying so-called "cash in hand" for wages or stock, I saw them nodding in agreement like a toy dog's head in the rear window of an old Volvo.

To run an efficient business it is essential to be able to compare operational percentages and ratios on a monthly basis, and by ripping cash out of the business, performance cannot be accurately tracked or shared with key staff. The hospitality industry is tough enough, and finding the time to ensure that proper records of all your normal business transactions are kept is hard enough, let alone trying to cope with keeping other records to reflect the "real" position.

Let's look at some specific circumstance that might attract the attention of the ATO if you were to be audited.

By paying "cash in hand" you are avoiding PAYG withholding obligations and depriving the ATO of its entitlement.

If the employees are paid cash or partly paid in cash you may not be covered by Work Cover should an employee be injured at their place of employment. Although benefits payable to an injured employee are guaranteed by the Work Cover Authority (in Victoria), the costs of the claim may be recovered from the uninsured employer, not to mention the heavy penalties for not properly covering the particular employee by paying the appropriate premiums.

I am unaware of any public liability insurance policy that affords cover to an employer where the employer could, as a matter of course, have obtained Work Cover insurance. So, where there is a serious injury, you could also be financially ruined.

By paying cash or partly cash to an employee you would be avoiding liability for superannuation contributions on the cash component paid. Should that be discovered, you would be liable for the Superannuation Guarantee Charge (SGC) which includes an interest component plus administration fee in addition to any shortfall. If the shortfall is as a result of making a false or misleading statement, the penalty amount that can be imposed is 75 per cent of the shortfall plus the shortfall itself. The penalty for failing to keep adequate records is also significant. If you enter into an arrangement to avoid liability for the SGC, you may have to pay the charge avoided and a penalty of 50 per cent of the avoided amount. All in all it's a nightmare you could do without.

In any employer and employee relationship you need to be able to exercise proper authority over your employees. Apart from the illegality of doing so, by paying "cash in hand" that authority is severely limited and the ability to deal with that employee objectively would be seriously compromised. In other words, if that employee is guilty of serious misconduct, how would you deal with it bearing in mind the potential for blackmail due to "cash in hand" payments?

> In any employer and employee relationship you need to be able to exercise proper authority over your employees. By paying "cash in hand" the ability to deal with that employee objectively would be compromised.

Paying "cash in hand" also has other wide range implications, such as the subtle effect of pushing up wages. For example, if a wage of $500 per week would yield $400 net of tax to an employee, by paying the employee $450 per week cash would mean that both parties are better off. The result is that you are not paying $100 per week in PAYG. The employee is getting $50 more than he would have received and you are paying $50 less than you would have paid in respect of PAYG.

When the same employee applies for another job paid "on the books", he or she would have to be paid closer to $575 to realise a net of $450 (previously paid in cash). On the assumption that no one wants to contravene the law, if the employee is suitable for the position the new employer would have to pay that amount for fear of losing him in a very difficult employment environment! So the more wages in cash being paid in the industry the more the expectation is of a net wage rather than a before-tax wage. Achieving that by paying cash is an extremely risky business.

Whether or not the sushi restaurant chain had made a mistake or not is irrelevant. The message is quite clear. Apart from the distortion of the financial statements of the business which would affect you when trying to sell the business – which is an issue I constantly have difficulty getting potential sellers to understand – the stakes are high when it comes to illegal practices of paying wages in cash. If you fall into this category it's not too late to revert to conducting a best practice business and to hop off the treadmill of cash wages. You could save yourself many sleepless nights – and probably your business too!