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Are employees entitled to more?

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In the black; Aug 2002; 72, 7; ABI/INFORM Complete
pg. 67

Strong regulation is required to secure funding for employee entitlements, report VICTORIA WISE and JUDY OLIVER

MUCH HAS BEEN REPORTED RECENTLY about the need to secure employee entitlements, but recent history shows that tangible improvements in this area are very difficult to achieve or retain.

George Lopez, chair of CPA Australia’s insolvency and reconstruction committee reported in Australian CPA (November 2001) on the replacement of the Commonwealth Government Employee Entitlements Support Scheme (EESS) with a new scheme, the General Employee Entitlements Redundancy Scheme (GEERS). Both schemes provide a safety net by which government pays employees their service entitlements and then takes the employees’ place in claims against the insolvent employer organisation. Such schemes are fundamentally inequitable as ultimately they require taxpayers and shareholders to foot the bill for the mistakes, excesses, misdemeanours or incompetence of employers.

Similar arrangements have been proposed in the past. For instance, the Australian Law Reform Commission’s Harmer Report (1988) contained a recommendation that a wage earner (fidelity-type) protection fund be established. In 1999 the NSW government commissioned a feasibility study into the implications of setting up and running a compulsory “national insurance scheme to protect employee entitlements”. The ACTU in 2000 released details of a proposal for a comprehensive national safety net scheme into which a levy on all employers would be paid. These proposals have been met with stubborn resistance from corporate managers who perceive their organisations as being unfairly penalised for the failure of risky or poorly managed businesses. It appears that without compelling regulation, funding of employee entitlements simply will not occur.

IS LEGISLATION THE ANSWER?
In the state of Victoria, local government legislation already exists to ensure that long service leave entitlements are funded. The Victorian local government...
The regulations (VLG) specifically require that assets sufficient to meet long service leave obligations be “restricted” as cash or investments. And until recently (August 2001) the Victorian water industry had a similar regulatory requirement.

In August 2001 the Victorian water regulations were amended to remove the funding requirement. This amendment effectively transferred the insolvency risk associated with deferred long service leave obligations from employers in this industry to their employees. Furthermore, there are balance sheet structural implications as a result of this move. The provision for long service leave remains on the balance sheet but the counterbalancing restricted asset disappears. The revised regulations were silent as to the disposition of the accumulated funds, but it is most likely that they have been transferred back into general working capital accounts of the employer organisations and not retained as a sinking fund to secure employee entitlements.

The VLG regulations compel the funding of the long service leave entitlements of its staff. Over the time these regulations have been in place a huge funding resource has been created. At 30 June 2000 the aggregate was $107 million.

These regulations were subject to a sunset clause in February 2002, and after due consideration the funding requirement was retained. Had the funding requirement been removed, the security of long service leave entitlements of staff in the organisation. It also ensures intergenerational equity as future generations of ratepayers will not have to pay for the costs of providing services to the current generation.

The long service leave liability of the Victorian state departments (second tier of government) was unfunded up to 1 July 1998. Since that date when accrual output management (AOM) was introduced, departments have been funded for long service leave expense through revenue received for the delivery of outputs. This funding is available to departments to pay out long service leave liabilities as they fall due for payment. With the passage of sufficient time and the expiration of the unfunded liability, it is anticipated that a funded liability will accumulate. However, there is no requirement that the funding be held in a dedicated asset account.

**IS THERE ANOTHER SOLUTION?**

Annual leave and long service leave are both examples of deferred wages. This means they are the same in nature as superannuation. The trust funding model introduced so effectively to promote and preserve superannuation entitlements is a mechanism that would work just as

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effectively in securing other employee entitlements.

A highly successful model already exists in the Australian construction industry. The Construction Industry Long Service Leave Act established a trust fund that serves to record the work history of employees and secure the funding of long service leave entitlements. The construction industry is characterised by the transient nature of its employees and in many cases, employers. The trust arrangement accumulates intermittent work histories and compels the employer funding of long service leave entitlements on a regular basis. Hansard (1999) records that it is the preferred model of significant union groups including the Metal Trades Federation of Unions and the Australian Manufacturing Workers Union (AMWU).

The trust funding approach also has some advantages for employers, as it enables them to remove a significant liability from their balance sheets and relieves them of a significant administrative burden. If managed efficiently, employer contributions become marginal once a sufficient pool of accumulated funds has been achieved. So successful has the investing and management of the construction industry fund been, that in Victoria since 1993, employers' contributions have been insignificant.

In April the AMWU took strike action to secure workers' service entitlements against corporate collapses. The strike was in response to an employer's failure to establish a trust fund for the purpose of protecting long service leave entitlements as required under an enterprise agreement. Following the disastrous impact on employees of the Ansett and HIH failures, emotions were running high, and the strike brought Australia's automotive industry to a standstill. In May the AMWU called for a summit to develop an industry plan to protect employee entitlements. It appears likely that unless a satisfactory solution is found, Australian industry will suffer further disruption.

It was suggested at a recent Mercer Global Investment Forum (November 2001) that if government was loath to hold a review of superannuation, the industry might hold its own and put up solutions to vexing problems. Likewise, if government provides other employee entitlement solutions that are unattractive (such as the ESS scheme) then other interested parties may continue to press strongly for their own solutions.

FURTHER READING

- Corporate groups and the duties of directors: protecting the employee or the insolvent employer? David Noakes, Australian Business Law Review, April 2001
- Corporations Law amendments promise better protection for employee entitlements: but do they deliver it? by Lysanne Pelling, Keeping Good Companies: Journal of Chartered Secretaries Australia June 2001
- Employee Entitlements Support Scheme: Insolvency Practitioners' Manual by the department of workplace relations and small business, 2001

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