Understanding the risks and implications of fraudulent underpayment of wages and employee entitlements

By Robin Tarr, Partner, McGrathNicol

A growing number of high profile large Australian companies have been on the receiving end of adverse media attention alleging the deliberate underpayment of employee entitlements. The fallout from these allegations has resulted in significant financial impact not to mention the often unavoidable lasting reputational damage for entities directly or indirectly caught up in such conduct.

Underpayment of workers’ entitlements undermines the trust of customers and disenfranchise and demoralise workers.

Undesirable conduct by a company’s supply chain partners, franchisees or service contractors and subcontractors accused of underpaying their own people can result in ‘guilt by association’.

Executive management should assign responsibility for ensuring compliance and demonstrate commitment to its staff by communicating a strong ‘tone from the top’ message.

Australia’s workplace regulatory agency, the Fair Work Ombudsman’s investigation into allegations of significant underpayment of wages across much of the franchise network of one of Australia’s leading convenience retailers, 7-Eleven found contravening behaviour, that was ingrained within the franchise network.¹

The Fair Work Ombudsman’s investigation was foreshadowed by alarming whistleblower reports alleging a range of serious systemic misconduct including, workers being paid for half the hours worked, deliberate falsification of wage records to facilitate the underpayment, workers not being paid for training and the suggestion that complaining migrant workers were threatened with reports to immigration for working excessive hours in breach of visa conditions.

Who is affected?

The characteristics of the 7-Eleven scandal is not uncommon in various economic sectors for example, hospitality, retail, agriculture, and security services where workers employed under franchise or similar models are vulnerable to exploitation due to their age, social standing and/or immigration status.

However, not all instances can be categorised as fraudulent underpaying entitlements. Australia’s complex system of award and agreements can lead to employers unintentionally or unknowingly underpaying their employees.

To explain, in some cases the undesirable conduct by a company’s supply chain partners, franchisees or service contractors and subcontractors accused of underpaying their own people, results in ‘guilt by association’ resulting in the cloned exposure to the same reputational damage. While ignorance may be put forward as a
defence for deliberate underpayment, it really isn’t a plausible excuse. In summary, if your business partners are caught up in it, invariably your business is at risk of being ‘tarred with the same brush’.

This scenario highlights the importance of ‘building, living and breathing’ a culture of compliance and strong internal governance.

Building a strong compliance framework to mitigate the risk

The financial impact and other consequences from fines and penalties, legal and other professional services fees and to costs associated with retrospectively recalculating are invariably significant.

Therefore, it is of utmost importance for both employer and employee to identify and remedy any flagged instances of underpayment of wages as quickly as possible in order to avoid the human harm that comes from underpayment and the penalties that may far exceed the original short payments.

Whether directly or unknowingly involved, employers need to understand what their obligations are and build a robust governance framework designed to prevent a culture of underpaying employees…

Implementing strategies to prevent underpayment of employee entitlements

The foundation for preventing the conduct is through the development of a compliance framework that firstly articulates a company’s broad obligations under law and under internal arrangements regarding remuneration of all of its employees.

The framework will document the manner in which the company engages and contracts with third parties. Requesting third parties to subscribe to codes of conduct, building ‘right to audit clauses’ into contracts and agreeing to regular reporting protocols will assist companies with accessing timesheet, payroll and other remuneration records and get to the bottom of suspected improper conduct by third parties.

Undertaking sufficient and reliable due diligence of business partners to ensure that the contractors that represent your brand do the right thing by paying their own employees everything they are entitled is sensible preventative governance designed to mitigate reputation risk due to the conduct by third parties. It is recommended that executive management assign responsibility for ensuring compliance and demonstrate commitment to its staff by communicating a strong ‘tone from the top’ message.

Detecting underpayment scandals

A key methodology to detect misconduct in the workplace is through the traditional receipt of whistleblower reports from internally or externally managed hotlines. The whistleblower regime in Australia is currently under review with some robust changes anticipated to legislation regarding the protection of whistleblowers at the end of 2017.3 These changes in effect will provided whistleblowers with greater protection from the risk of reprisal and will hold those responsible for reprisals to account.

In summary the following is expected.

• The definition of a whistleblower will be extended to include former officers, former employees, former contractors and subcontractors. In effect, a larger pool of people associated with an entity through their current or former roles will be provided with protection from reprisal under the proposed changes.

• Whistleblowers may make reports anonymously through a third party, for example a lawyer. This proposed change will provide whistleblowers with an added layer of protection and an added sense of confidence to report sensitive matters like concerns around wage entitlements.

• Changes are likely to signal the introduction of financial reward in some form for whistleblowers for credible information of misconduct. Similar legislation in the USA² has achieved success with the disclosure of prominent misconduct matters.

• There will be mandatory requirements for companies to implement internal processes to facilitate effective whistleblower protection.

The application of traditional data analytics continues to play a pivotal role in the detection of fraud and misconduct of any nature. Accordingly, it is recommended that organisations at risk of exposure to underpayment of employee entitlements consider implementing a data analytics model combining traditional analytics, or advanced predictive analytics that examines historical payroll data highlighting anomalies consistent with indicators of wage fraud that may be subjected to further inquiry. Similarly, applying online analytics across social media platforms for example, will provide stakeholders at affected companies with a realistic summary of employee sentiment. This information can be used to enable corrective measures to minimise damage promptly.
Developing a response strategy

In the event that allegations or concerns around the underpayment of entitlements are made, organisations involved may wish to roll out a response strategy that will include:

- directives for communicating with effected employees and their representative
- communication with legal representatives and other professional services specialists
- methodology to recalculate and repay entitlements to effected employees
- guidance for engaging with the Fair Work Ombudsman.

There is no grey area

In conclusion, the lives of underpaid exploited employees, their families and the broader economy will continue to suffer as long as companies fail to place their employee entitlements ahead of profits and financial targets — there is no grey area in this regard.

The obvious lessons to be learned from matters investigated by the Fair Work Ombudsman for businesses of all sizes across vulnerable sectors in Australia is that the financial and reputational risk implications are far reaching.

Demonstrating commitment to setting the right culture, communicating strong tone from top management and developing a sound governance structure and compliance framework will minimise these risks.

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Notes

2. Parliamentary Joint Committee on Corporations and Financial Services Whistleblower Protection — September 2017