**AAT Bookkeeping Guides**
**Payroll Deductions**

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On occasions, a manager is faced with a need to deduct money from an employee’s pay particularly in situations where the employer seeks to recover money which they believe the employee owes to them.  This practice is strongly regulated under legislation, notably, the Fair Work Act 2009 (the Act).  There are very specific provisions in the Act as to when an employer can make deductions from an employee's wage or salary.

It is important for employers to understand their obligations. In this article we review some of the circumstances and the rules that apply.

**What is my key responsibility as an employer in relation to pay?**

The Act requires an employer to pay an employee amounts owing to them in full in relation to the performance of work, except where **authorised** deductions may be made from an employee's wage/salary, incentive based payments, bonuses, allowances, and similar and only if the deduction is **authorised in writing** by the employee and the deduction is **principally for the employee’s benefit** (e.g. a salary sacrifice arrangement).

**When can I make deductions?**

The Act permits the employer to make deductions where:

* the deduction is authorised by the employee in accordance with an enterprise agreement,
* the deduction is authorised by or under a modern award or an order of the Fair Work Commission, or
* the deduction is authorised by or under a law of the Commonwealth, a State, or a territory, or an order of a court (e.g. income tax deductions, a deduction made for the purposes of child support by the Department of Human Services, or a garnishee court order).

Any written authorisation from an employee **must clearly specify** the amount of the deduction and allow for the employee to cease this authority at any time in writing.

**When am I unable make deductions?**

In addition to the circumstances mentioned elsewhere in this update, employers are prohibited from requiring employees to spend any part of their payment (wages) in relation to the performance of work where the requirement is unreasonable.  For example, where employees are required to wear a particular brand or type of clothing and are required to purchase that clothing, then that requirement has to be reasonable to be enforceable and not to be in breach of the Act.

**What about mentioning deductions in a contract of employment?**

Many employers believe that an employment contract provides sufficient authority to permit deductions.  Sadly, this is not the case as the Act does not grant this type of authority.  The key danger is that upon termination, some employers believe they can deduct monies from the employee’s final pay that the employee maybe owing (e.g. a store account or leave that is overdrawn). This means that although it is common practice for contracts of employment to contain terms which may expressly allow an employer to make deductions, such terms do not generally comply with the Act.  Simply, if an employer relies on such a contractual term, and the employee later disputes the deduction, the employer may not only have to repay the amount to the employee but may be prosecuted and fined.

**What if a deduction is "for the benefit of the employer"?**

It is important for employers to recognise that deductions for an employer's (or a related party's) benefit must be authorised by a modern award or enterprise agreement (or if relevant a contract of employment), otherwise the employer cannot lawfully make a deduction.

An example of terms that will have **no effect** include reducing an employee’s pay where the employer considers the employee has performed substandard work.  Another example is deducting the value of replacing a damaged or broken item from an employee’s wages.

Even if a modern award or enterprise agreement (or even, a contract of employment) contains an authority to make a deduction, the Act provides that the authorisation will have no effect (making the deduction unlawful) if the deduction:

* is directly or indirectly for the employer's (or a related party's) benefit and it is unreasonable in the circumstances; and
* has not been agreed to in writing by a parent or guardian of the employee, where the employee is under 18.

**Are there examples of reasonable deduction for the employer’s benefit?**

The regulations of the Act help by providing examples deductions from wages for the benefit of the employer to be considered reasonable include a deduction of health insurance fees made by an employer that is itself a health fund, and a deduction for a loan repayment made by an employer that is itself a financial institution.

A deduction which is to recover costs directly incurred by the employer as a result of the employee's voluntary private use of particular property of the employer, whether the use is authorised or not.  Examples include:

* the cost of items purchased on a corporate credit card for personal use by the employee;
* the cost of personal calls on a company mobile phone, and
* the cost of petrol purchased for the private use of a company vehicle by the employee.

However, although these deductions will be considered reasonable, the deduction must still first be authorised by a modern award or enterprise agreement a written agreement or if relevant, a contract of employment.

**What about a deduction for employee clothing?**

In addition to the circumstances mentioned elsewhere in this update, employers are prohibited from requiring employees to spend any part of their payment (wages) in relation to the performance of work where the requirement is unreasonable.  For example, where employees are required to wear a particular brand or type of clothing and are required to purchase that clothing, then that requirement has to be reasonable to be enforceable and not to be in breach of the Act.

**Deductions related to resignation: What happens if an employee does not give the required notice if they resign?**

An example of a common modern award provision, that provides for a permissible deduction for the benefit of the employer without written authorisation from the employee, is the following clause in relation to the notice of resignation required to be given by an employee:

*The notice of termination required to be given by an employee is the same as that required of an employer except that there is no requirement on the employee to give additional notice based on the age of the employee concerned.* ***If an employee fails to give the required notice the employer may withhold from any monies due to the employee on termination under this award or the NES****, an amount not exceeding the amount the employee would have been paid under this award in respect of the period of notice required by this clause less any period of notice actually given by the employee.*

**What if my business sustains damage because of an employee’s actions?**

Importantly, employers cannot automatically make a deduction from an employee's wages/salary or other payments in the following circumstances:

* to recover the cost of repairs or the insurance excess where an employee damages the employer's property during the course of employment,
* to recover the shortfall of a cashier at the end of the day in their register, or
* if an employee continually arrives late for work or leaves early.

**What if an employer mistakenly overpays an employee?**

An employer can only deduct money from payments to an employee to recover an overpayment if allowed by an industrial instrument (for example, an enterprise agreement or modern award), legislation or court order.  Despite this, an employee and employer can agree to a deduction, if the reason for the overpayment was simply due to a payroll error.  This agreement would need to be in writing showing clear dates of application and when deductions will cease.

**In summary**

The issue of payroll deductions needs careful attention by every employer and the above brief outline details payroll deductions in limited circumstances only.

We reiterate that employers should be cautious in simply seeking to rely on any general deduction wording in employment contracts.  Despite such contractual wording, an employee's written authorisation of a specific amount will still be required (unless the deduction is properly authorised by an industrial instrument, legislation or court order).

**Needing more help or assistance?**

If you would like assistance with managing deductions from employee’s wages or salary or you are not sure how to handle an overpayment mistake, please contact our team of advisors at AB Phillips, Monday to Friday between 9:00 am and 5:00 pm AEST by phone on 1300 208 828 or by email: advice@abphillips.com.au.

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