

14 OCTOBER 2011

ATO ENFORCEMENT POWERS AMENDED – DIRECTORS AUTOMATICALLY LIABLE

PROPOSED LEGISLATIVE CHANGES TO DPN AND SGC REGIMES NOW BEFORE PARLIAMENT

WHAT ARE THE CHANGES?

Under the existing Director Penalty Notice (“**DPN**”) regime, once the Australian Taxation Office (“**ATO**”) has issued a DPN, a personal liability can be created for a company’s director in respect to unpaid Pay as You Go Withholding (“**PAYGW**”) should the company fail to pay any outstanding amounts or appoint an insolvency practitioner within 21 days of the issue of the DPN.

On 13 October 2011, the Federal Government introduced tax legislation designed to protect workers' superannuation and deter fraudulent 'phoenix company' activity. The proposed changes:

- Make directors personally liable for their company's failure to pay employees' superannuation by the inclusion of amounts owing under the Superannuation Guarantee Charge (“**SGC**”) in the DPN regime;
- Enable the ATO to make a reasonable estimate of unpaid SGC where a company fails to meet its reporting obligations;
- Allow the ATO to commence immediate recovery procedures where a company fails to comply with its reporting obligations for a period of more than 3 months and its PAYGW and/or SGC liability remains unpaid. In this circumstance, the ATO will be able to pursue the company’s directors under the DPN regime without issuing a director penalty notice as the liability automatically attaches to the director on the expiration of 3 months after the due date for lodgement; and
- Deny directors (and their associates) entitlement to PAYGW credits (through the imposition of tax) where the company of which they are a director has failed to remit PAYG withholding amounts.

BACKGROUND

The Federal Government’s 2011 Budget which was handed down in May, included proposed amendments to the ATO’s penalty powers in regard to the ability to hold directors personally liable for some employee related company tax debts. The Federal Government’s position is that these changes are necessary to deter fraudulent phoenix activity and protect employees’ superannuation entitlements.

The proposed legislation will allow the ATO to target companies with a poor statutory compliance history and in addition, hold recalcitrant company directors personally liable for the company’s unpaid PAYGW and SGC obligations.

"Fraudulent phoenix activity hurts all sectors of the economy, including workers, creditors, customers, competing businesses and Government. It creates competitive disadvantages for businesses who do the right thing and means payments of workers' entitlements are often neglected", the Assistant Treasurer and Minister for Financial Services and Superannuation Bill Shorten said.

Since the announcement, Taylor Woodings has been following the progress of these changes. Yesterday, the underlying legislation to these proposed changes was introduced into the House of Representatives. The Explanatory Memorandum that accompanies the legislation now provides greater clarity around what the proposed changes will be and how they will operate.

OBSERVATIONS

Our observations of the changes include:

- With the introduction of SGC to the DPN regime, directors can now be personally liable for a significantly higher proportion of a company's unpaid employee related obligations.
- Where a company's PAYGW and SGC remain unreported for in excess of 3 months a director will become automatically liable for the obligation even though they have not received any notice (through the issue of a DPN) for the company's PAYGW and SGC obligations. This contrasts with the current regime where upon service of a DPN, a director has 21 days to pay the debt or appoint an insolvency practitioner prior to becoming personally liable.
- In practice, this will allow the ATO to commence immediate recovery proceedings (in respect to either a reported or estimated amount) which may range from third party garnishee orders to formal judgements through to the commencement of bankruptcy proceedings in order to recover the outstanding debt. The only way for a director to avoid further enforcement action will be to pay the debt.
- Outstanding PAYGW obligations on the date the legislation is enacted will be captured meaning there is a degree of retrospectivity about the changes.
- By imposing a new personal tax – the PAYG Withholding Non-Compliance Tax, the ATO is effectively closing a loophole whereby directors (and in some circumstances their associates) have been able to personally claim PAYGW credits where the company has failed to remit them prior to it being placed into liquidation.
- Financiers should be aware of their customers' statutory compliance history and ensure that their lodgement and payment obligations are up to date. Any failure to do so may create an environment in which the ATO is able to commence recovery action that may create a personal liability for directors which financiers should be aware of when providing finance to directors. Further, where a personal liability attaches, a director's statutory obligations to the company may be conflicted in relation to their own personal interests leading to dysfunctional decision making.
- These proposed changes will provide the ATO with the flexibility and responsiveness to deal with recalcitrant directors by commencing recovery proceedings against the director (in certain circumstances) without further notice.

HOW TAYLOR WOODINGS CAN HELP

Taylor Woodings is an independent, national Chartered Accounting firm providing clients specialist services in Restructuring, Corporate Recovery, Advisory and Transaction Services and Forensic Accounting. With offices in Sydney, Perth, Melbourne and Brisbane, we offer our clients a truly national service.

Businesses with outstanding tax and superannuation debts or general financial and cash flow difficulties must seek independent advice as soon as possible. A failure to take prompt decisive action will diminish the prospects of the business continuing and also increase the likelihood of directors becoming personally liable for the company's debts.

Taylor Woodings specialises in the areas of corporate recovery and related advisory services. We provide advice to directors, financiers and other key stakeholders exposed to businesses in financial distress.

Across all appointments, we work hard to find practical solutions to the challenging situations faced with the aim of maximising the position for all stakeholders.

Taylor Woodings can provide advice with respect to:

- Whether a company is likely to be insolvent or near insolvent;
- What steps can be taken (if any) to avoid the company becoming insolvent; and
- If insolvency cannot be avoided or it appears imminent, assist stakeholders with respect to their rights and obligations.

Should you require any additional information regarding the contents of this newsletter or wish to discuss a specific matter involving a financially stressed business, please contact one of Taylor Woodings' partners in Sydney, Perth, Melbourne or Brisbane.

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