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FEDERAL BUDGET 2011 - ALERT

GOVERNMENT TARGETS PHOENIX ACTIVITY AND COLLECTION OF UNPAID SUPERANNUATION

OVERVIEW

- Federal Budget measures aim to expand ATO powers to collect unpaid superannuation debts to target phoenix activity
- Extended powers may impact directors, employees, secured and unsecured creditors
- Director penalty regime extended to superannuation liabilities
- Under certain circumstances, recovery actions for unreported liabilities exceeding three months to be commenced without required 21 day notice period
- Directors and associates potentially to be denied personal tax credits for unpaid company tax
- New powers effective 1 July 2011

CHANGES THAT YOU NEED TO KNOW ABOUT

In Tuesday's Budget, the Federal Government confirmed that the further collection powers of the Australian Tax Office ("ATO") will come into effect from 1 July 2011 in the following ways:

- the director penalty regime will be extended to superannuation guarantee amounts, making directors personally liable for their company's failure to pay employee superannuation;
- the ATO will be given the power to commence recovery against directors under the director penalty regime, without providing a 21 day grace period, for certain unpaid company liabilities that remain unreported after three months of becoming due; and
- in certain circumstances, directors and associates of directors will be prevented from obtaining credits for withheld amounts in their individual tax returns where the company has failed to pay withheld amounts to the ATO.

While these measures are aimed at deterring phoenix activity, they should further encourage directors to ensure companies promptly remit all statutory liabilities.

ATO'S EXISTING POWERS

These measures extend the means currently available to the ATO in collecting outstanding tax debts. The ATO's existing powers include:

- the ability to issue a notice requiring compliance within 21 days or directors may become personally liable for any accrued and unremitted withholding taxes, such as PAYG tax deducted from employee's wages;
- the ability to require the payment of a security bond for prospective tax liabilities where the ATO has determined that grounds exist to warrant such security; and

- the ability to issue garnishee notices effectively against a company, such as on the company's debtors and the company's bank account, requiring the payment of monies directly to the ATO.

IMPACTS ON STAKEHOLDERS

The potential for directors to become personally liable for outstanding superannuation guarantee amounts is likely a positive for a number of stakeholders including:

- **employees:** the new measures encourage directors to ensure timely payment of superannuation. However, if such amounts do remain outstanding another avenue now exists from where those monies can potentially be recovered, namely the personal assets of directors. This is particularly relevant given that outstanding superannuation in an insolvency is not presently covered by the Federal Government's existing employee safety net, the General Employee Entitlements and Redundancy Scheme ("GEERS");
- **secured creditors:** any outstanding superannuation represents a priority claim with respect to floating charge assets. These measures should discourage the accumulation of large employee superannuation claims by a company and accordingly minimise the potential quantum of priority employee claims, which rank ahead of those of a secured lender when floating charge assets are available. However, this may also have the consequence of directors requesting support from financiers to fund superannuation liabilities at short notice; and
- **unsecured creditors:** encouraging directors to ensure that superannuation claims which rank ahead of unsecured claims are not accrued, or to act more quickly where such potential claims are accruing, may lessen the impact on and exposure of unsecured creditors in an insolvency.

The ATO's ability to commence recovery proceedings under the director penalty regime without 21 days notice with respect to unreported debts older than three months has the potential to immediately impact the liquidity and cash requirements of a company, or precipitate a company entering into a formal insolvency regime. It also makes company directors automatically and immediately personally liable for certain statutory liabilities.

Additionally, the combined measures will likely further discourage directors deferring payment of superannuation and taxes in favour of other liabilities and commitments in times of financial stress. This may make superannuation and tax liabilities a more prevalent consideration when formulating financial forecasts, determining funding requirements and assessing the ability to successfully turn around a financially distressed business.

While expected to be welcomed by creditors and the broader community, the measures impose further onerous personal obligations and liability on directors, including where there is no intentional engagement in phoenix activity.

Directors can take steps to mitigate their potential personal liability for outstanding taxes and superannuation, including:

- keeping proper and accurate records and accounts;
- ensuring tax and superannuation liabilities are accurately assessed and statutory returns prepared on time;
- ensuring lodgement and remittance status are regularly reported to directors;

- ensuring all taxes and superannuation are paid on time;
- formally informing the ATO where a temporary delay in return lodgement or remittance will occur and seek a formal extension; and
- where a company is not in a financial position to meet tax or superannuation liabilities or complete returns, act early and seek independent advice regarding available options. Options may include implementing an informal workout plan with input from key stakeholders such as the ATO and financiers, or appointing a voluntary administrator.

While awaiting full details from the Federal Government, overall these measures enhance the ATO's arsenal for curbing phoenix activity and recovering tax debts and outstanding superannuation. However, they place a significant onus on directors to ensure a company's compliance with respect to statutory liabilities, or risk personal liability.

HOW TAYLOR WOODINGS CAN HELP

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 directors to act in a way that appropriately discharges their duties.

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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