

DIRECTOR PENALTY NOTICES

UNDERSTAND YOUR PERSONAL EXPOSURE IF YOUR COMPANY FALLS INTO ARREARS WITH THE AUSTRALIAN TAXATION OFFICE



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TOGETHER WE MAKE IT HAPPEN

Who are we?

We are a dedicated insolvency accounting practice with extensive corporate and personal insolvency experience. Our firm is an independent member of HLB International and the HLB Mann Judd National Association – a worldwide organisation of respected accounting firms and business advisors.

We appreciate that managing a struggling business and juggling debt is distracting and stressful. We derive satisfaction and motivation by helping people understand their options and by creating a clear plan to escape a cycle of uncertainty and worry.



Greg is a Partner at HLB Mann Judd Insolvency WA with over 13 years of corporate and personal insolvency experience. Greg is a Registered Liquidator and manages the corporate and personal insolvency appointments managed by the firm.



Kim is a Partner at HLB Mann Judd Insolvency WA. Kim is a Registered Liquidator and Trustee in Bankruptcy with over 35 years of experience specialising in insolvency and reconstruction involving all types of personal and corporate administrations.

WHAT IS A DIRECTORS PENALTY NOTICE?

The Director Penalty Notice (“DPN”) regime is administered by Division 269 of the Taxation Administration Act 1953 (Cth) (“the TAA”).

Directors are legally responsible for ensuring a company meets its taxation and superannuation lodgement and payment obligations.

Under the DPN regime, failure to meet these obligations means directors can be held personally liable for a penalty in an amount equal to the amount that the company should have paid.

The DPN regime has, until recently, only applied to PAYG-w and Superannuation Guarantee Charge (“SGC”) amounts. Laws governing the DPN regime have evolved over the years.

In June 2012, the concept of a ‘lockdown DPN’ was born, making it easier for the Australian Taxation Office (“ATO”) to make directors personally liable for these debts, particularly where lodgement obligations are not complied with;

- From 1 April 2019, the exposure of a director to a lockdown DPN in respect of SGC amounts was changed from three months after the lodgement due date of the SGC statement to simply the day the SGC statements are due;
- Following reforms associated with broader anti-phoenixing measures, a major update has been the inclusion of Goods & Services Tax (“GST”) into the scope of the regime from 1 April 2020, along with Wine Equalisation Tax (“WET”) and Luxury Car Tax (“LCT”).

The DPN regime serves to ensure that directors acquit their lodgement obligations on time and to safeguard against any delays in payment of PAYG-w, SGC and GST.

“DPNs compel directors to lodge and pay company tax liabilities on time. Failure to do so results in personal liability.”
- Greg Quin, Partner

HOW DPNS WORK

In accordance with Division 269 of the TAA, a director becomes liable for a penalty at the end of the same period that the company should have settled its obligations for PAYG-w, SGC and GST. In other words, the ATO does not need to issue a DPN for the director penalty amount to exist. The issuance of a DPN (i.e. the paperwork) is merely notification that enforcement actions are commencing.

The ATO follows a process for enforcement of the penalty by observing a 21 day notice period in which a director can take various courses of action. It is important to note that the 21 day notice period commences on the date of the DPN itself as opposed to the date of receipt by the director.

There are two types of DPN which are explored below.

NON-LOCKDOWN DPNS

Non-lockdown DPNs occur in circumstances where a company has acquitted its BAS and SGC lodgement obligations (or they are not lodged more than three months late in respect of PAYG-w and GST etc - noting that SGC do not have a 'grace period' from 1 April 2019); however payment of the relevant liabilities have not been made.

The issuance of a DPN in these circumstances will give a director options to consider and address within the 21 day notice period as follows:

- Pay the debt
- Place the company into Voluntary Administration
- Place the company into Liquidation

LOCKDOWN DPNS

Lockdown DPNs occur in circumstances where a company has not acquitted its BAS lodgement obligations within three months of their due dates, or its SGC lodgement obligations on time, and payment of the relevant liabilities have not been made.

The issuance of a DPN in these circumstances will not give a director options (other than payment of the debt by the company) to avoid personal liability as is the case with a non-lock down DPN.

It is worth noting that an additional month is granted where a Tax Agent is attending to the lodgements for a company.

In our experience, there are few directors who attend to the lodgement of SGC statements with the ATO in circumstances where superannuation is not paid to the relevant superannuation funds by the relevant due dates. There appears to be a general lack of awareness amongst directors around the matter and the responsibility to lodge SGC statements, resulting in automatic personal liability once the SGC statements become overdue.

EXAMPLE OF NON-LOCKDOWN AND LOCKDOWN cont.

The way the figures are set out can be confusing, so it is important that directors liaise with their advisors to properly understand their personal exposure.

Taxation Administration Act 1953

Notice of director's liability to pay a penalty to the Commissioner of Taxation

Superannuation guarantee charge amounts

In exercise of the powers and functions conferred on me as a Deputy Commissioner of Taxation by a delegation from the Commissioner of Taxation (**the Commissioner**) under the provisions of the *Taxation Administration Act 1953 (TAA)* I give you notice under section 269-25 in Schedule 1 to the TAA that you, as a director of **(the company)**, failed to discharge an obligation you have pursuant to section 269-15 of Schedule 1 to the TAA and are therefore liable to pay the Commissioner by way of penalty an amount equal to the unpaid amount of each liability of the company for superannuation guarantee charge in accordance with the *Superannuation Guarantee (Administration) Act 1992*, details of which are set out in the following table:

Column 1 Particular quarter	Column 2 Amount of superannuation guarantee charge	Column 3 Amount the Commissioner thinks is the unpaid amount of the company's liability	Column 4 Unpaid amount of the company's liability notified on or before the end of 3 months after the due day	Column 5 Unpaid amount of the company's liability not notified on or before the end of 3 months after the due day
	\$	\$	\$	\$
01 OCT 2015 to 31 DEC 2015	17,330.31	17,330.31	17,330.31	0.00
01 JUL 2015 to 30 SEP 2015	18,787.41	18,787.41	0.00	18,787.41
01 APR 2015 to 30 JUN 2015	14,485.16	14,485.16	0.00	14,485.16

The penalty in respect of each unpaid amount of the company's liability as detailed in Column 4 of the above table will be remitted if, **within 21 days after the date of this notice**:

- (a) the company complies with its obligation to pay the unpaid amount to the Commissioner; or
- (b) an administrator of the company is appointed under section 436A, 436B or 436C of the *Corporations Act 2001*; or
- (c) the company begins to be wound up (within the meaning of the *Corporations Act 2001*).

The penalty in respect of each unpaid amount of the company's liability as detailed in Column 5 of the above table will be remitted if, **within 21 days after the date of this notice** the company complies with its obligation to pay the unpaid amount to the Commissioner.

Dated this 31st day of August 2018

Robert Ravanello
Deputy Commissioner of Taxation and
Delegate of the Commissioner of Taxation

IMPORTANT POINTS TO CONSIDER

ADDRESS FOR SERVICE

Directors often suspect that important correspondence pertaining to a company will be issued to its registered office; however given the personal nature of a DPN, it is issued to the director's personal address as recorded on the Company's Australian Securities & Investments Commission's ("ASIC") register.

It is not unusual in our experience for a DPN to go unopened for the full 21 day notice period, resulting, in the case of a non-lockdown DPN, personal liability at the expiry of that period.

We have encountered circumstances where family members have filed or misplaced correspondence from the ATO containing a DPN in expectation of it containing 'routine' information, only to discover its true contents at a later time.

The critical point is that directors should open any correspondence received from the ATO, regardless of what they may perceive to be its contents.

We have also observed, in less frequent circumstances, that a DPN can be issued to the office of a company's Tax Agent, as the ATO is empowered to do.

Importantly for Tax Agents, if a client changes their residential address, it is important that the change is reflected at ASIC. Consider the circumstances where a director moves house, you update your internal records for the issuance of invoices for your services etc, and fail to update the ASIC register. Such circumstances could result in reputational damage or potentially worse.

PAST AND NEW DIRECTORS

The potential exposure to a DPN continues despite the subsequent resignation of a director if they did not comply with section 269-15 of the TAA during their appointment as a director.

A penalty for past obligations also applies to new directors after 30 days of coming into office, starting on the date of their appointment. The only way to discharge this personal liability is for the company to enter either voluntary liquidation or voluntary administration within 30 days of their appointment.

It is critically important therefore that individuals intending to become directors therefore must understand the company's taxation lodgement and payment status and history before becoming directors.

DPNs MAY BE BASED ON ESTIMATES

If a company fails to comply with its PAYG-w, net GST and SGC reporting obligations, the ATO may make a reasonable estimate of the respective liabilities and a DPN may be issued based on those estimates.

The estimate is due and payable by the company on the day that the ATO provides notice of the estimated amount.

IMPORTANT POINTS TO CONSIDER cont.

ALLOCATION OF PAYMENTS

A critical point to consider is the allocation of payments made to the ATO. These matters are dealt with by Division 2 of Part IIB of the TAA and PSLA 2011/20.

Consider the following circumstances:

- A taxpayer has a historical RBA deficit, comprised of GST, PAYG-w, penalties and interest
- A payment plan is in place to address the historical debt and there is a condition that ongoing BASs are lodged and paid on time
- The taxpayer complies, making payment of the agreed monthly amounts and adheres to ongoing lodgement obligations

One might presume that the payment made pursuant to the payment plan would be allocated equally across the respective debts associated with GST, PAYG-w, penalties and interest. One might also presume that the payment of ongoing obligations would be allocated directly to the liability associated with the respective lodgements as they arise.



Net cash	283	
Financing		4,186
Short-term debt		
Maturities of short-term debt	0	(1,000)
Common stock issued	208	660
Common stock repurchased	(1,042)	(5,052)
Common stock cash dividends paid	(1,683)	(1,363)
Net cash used in financing	(2,513)	(6,751)
Investing		
Additions to property and equipment	(498)	(491)
Acquisition of companies, net of cash acquired, and purchases of intangible and other assets	(8,627)	(69)
Purchases of investments	(10,047)	(5,896)
Maturities of investments	6,061	1,836
Sales of investments	7,835	2,603
Securities	(292)	447
Net cash used in investing	(5,568)	(1,570)
Equivalents, end of period	\$ 10,610	\$ 4,023

PSLA 2011/20 and specifically, section 8AAZLE of the TAA, cover the following ground:

- Common law provides that a person who owes two or more debts to the same person, in this case GST, PAYG-w, penalties and interest, the debtor is entitled to nominate that a payment applies to one debt and not another
- In the case of an ongoing BAS payment, it is clear that a payment made corresponds with a specific liability
- If a debtor does not specify where the payment should be allocated at the time of payment, the creditor, in this case the ATO, is entitled to make the decision as to allocation of the payment

PSLA 2011/20 says that the ATO will usually allocate payments in accordance with directions, on the basis that the payment discharges the full amount of the liability.

Having said that, section 8AAZLE of the TAA gives the ATO discretion to allocate payments contrary to directions, specifically in instances “Where an account reconciliation is required to isolate certain components (for example, in the case of director penalty liabilities)”.

PSLA 2011/20 goes on to say that unless there is a valid reason to do so, the ATO policy for allocating a payment for which no direction is received, is:

- All payments will be allocated to the earliest (oldest) debts within an account
- Except where the payment relates to a ‘Listed Payment’

IMPORTANT POINTS TO CONSIDER cont.

ALLOCATION OF PAYMENTS cont.

Listed Payments, amongst other elements, importantly include:

- Arrangements to pay tax-related liabilities by instalments, allocated in accordance with the arrangement, or by default as follows:
 - Net GST
 - Assessed net fuel amounts greater than zero
 - FBT instalments
 - PAYG-w
 - Deferred company and superannuation funds instalments
 - PAYG instalments
 - Administrative penalties, including General Interest Charge for late payment

In summary, the allocation of payments made to the ATO will have a material impact on the issuance of a DPN, and given the discretion afforded by section 8AAZLE, payment directions given to the ATO may have little bearing on DPN risk mitigation.

Having said that, with the recent introduction of GST to the DPN regime, this issue will become less relevant as we move forward.

DEFENCES

There are defences available to directors who are exposed to a DPN liability as set out below:

- The director did not take part (and it would have been unreasonable to expect the director to take part) in the management of the company during the relevant period because of illness or other acceptable reason
- The director took all reasonable steps, unless there were no reasonable steps the director could have taken, to ensure that one of the following three things happened
 - The company paid the amount outstanding
 - An administrator was appointed to the company
 - The directors began winding up the company (within the meaning of the Corporations Act 2001)
- In the case of an unpaid SGC liability – the company treated the Superannuation Guarantee (Administration) Act 1992 as applying in a way that could be reasonably argued, was in accordance with the law, and took reasonable care in applying that Act.

IMPORTANT POINTS TO CONSIDER cont.

RECEIVERSHIP DOES NOT DISCHARGE PERSONAL LIABILITY

The appointment of a Receiver or Receiver and Manager will not extinguish the exposure to a DPN. As noted above, the appointments needed to extinguish a DPN must be Administration (i.e. the appointment of a Voluntary Administrator) or wound up (i.e. the appointment of a Liquidator)

If a company is in Receivership, and a non-lockdown DPN is received by a director, it will necessary to appoint a Voluntary Administrator or a Liquidator within 21 days of the date of the DPN to avoid the personal liability of the said director.

As Administrators and Liquidators are typically remunerated out of the assets of the insolvent entity (and in the case where a Receiver is appointed, these assets are usually under the control of the Receiver) it may be necessary to indemnify an Administrator or Liquidator for their fees in order to initiate a voluntary appointment - thus avoiding the potential personal liability referred to in the DPN.



DEREGISTRATION & DELAYED ENFORCEMENT

A DPN may be issued after a company is struck off the ASIC register, which is obviously problematic because the company does not legally exist at that point. Once a company is struck off the ASIC register, the appointment of a Voluntary Administrator or Liquidator is not practically available to avoid the potential personal liability referred to in the DPN.

We have also encountered individuals who had received a DPN several years ago (with no recovery enforcement action from the ATO at the time), only to have the ATO to resurrect the recovery and enforcement process referred to in the DPN.

TOPICAL ISSUES

COVID-19

Following the onset of the COVID-19 pandemic in Australia in March 2020, in combination with numerous protective insolvency-centric measures set in motion by the Federal Government (for example, temporary moratoriums dealing with Statutory Demands and 'safe harbour' relief for directors in relation to insolvent trading duties), it appears that the ATO ceased issuing DPNs so as not to cause undue distress to business owners during an already challenging period of time.

Given the DPN regime has been strengthened in favour of the ATO with the introduction of GST (and WET and LCT), and that the ATO will eventually need to 'get back to business' probably in early 2021, it is important that company directors remain cognisant of their company's taxation lodgement and payment obligations, notwithstanding that ATO's relatively understanding stance on tax payments since the advent of the pandemic.

IMPORTANT POINTS TO CONSIDER cont.

TOPICAL ISSUES cont.

Single Touch Payroll

The implementation of the Single Touch Payroll (“STP”) process for all employers now provides the ATO with a significant level of visibility over a company’s PAYG-w and SGC positions.

The STP system therefore empowers the ATO to examine millions of transactions to ensure that SG obligations are met on time.

James O’Halloran, a deputy commissioner at the ATO said, in 2019, “It’s [the STP process] a tangible action which demonstrates our increasing ability to effectively follow up in relative real time apparent late or non-payment of SG.”

Accordingly, the ATO will have ready access to these liabilities, meaning DPNs may be issued far quicker than in previous times.

SGC Amnesty

The COVID-19 related events of 2020 meant that the much touted SGC Amnesty fell out of the spotlight until its recent conclusion on 7 September 2020. There were some calls for the amnesty to be extended given the distractions posed by the pandemic, however no such extension was put in place.

From a company and director’s perspective, the key advantages of making use of the amnesty included:

- The ability to claim a tax deduction for SGC amounts and late payment offsets, on the basis that the SGC liability is paid by 7 September 2020
- Exemption from the substantial Part 7 penalties
- No administration fee component

Most clients have been able to access the amnesty to pay the debts, in full, contemporaneously with the lodgement process. However other clients may need to pay the debt over time.

The ATO was open to payment plan arrangements (on the basis that they were entered into on or before 7 September 2020); however, clients who apply for the amnesty after 7 September 2020 (or default on a payment plan) are then exposed to being disqualified from the amnesty regime. The issue is simple for directors – don’t pay or default on the SGC payment plan with the ATO, and the amnesty is annulled, opening the door to the DPN regime.

E-invoicing

In late 2019, ATO introduced its intention to develop a national e-invoicing system. It is intended that the mandated adoption of e-invoicing will occur by 1 July 2022.

In summary, e-invoicing is intended to:

- Reduce costs
- Mitigate the chances of errors
- Create a more reliable and robust system of security
- Reduce payment times

Management accounting platforms, such as MYOB and Xero, have been consulted on the matter in readiness for its roll out. The system will allow invoices to be sent between systems seamlessly, reducing the need for paper invoicing and subsequent data entry.

The e-invoicing system will give the ATO a far higher degree of discernibility between entities and the ability to data match with greater accuracy when BASs are lodged.

A photograph of a natural rock archway in a desert landscape. The arch is made of reddish-brown sandstone and frames a view of a bright sky. A person is standing on a rocky path leading through the arch. The foreground is filled with more rocks and sparse desert vegetation.

"DPNs are very powerful recovery tools available to the ATO. It is important that directors and advisors understand how they operate."

- Greg Quin, Partner

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