



## **DIRECTORS BEWARE**

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The Director Penalty Regime ("the Regime") was introduced to give the Australian Taxation Office ("ATO") power to make company directors personally liable for certain unpaid company taxation debts. It is imperative that company directors and their advisors understand the Regime and its operation, in order that they can take steps to avoid personal liability.

In this newsletter, we discuss the operation of the Regime, and most importantly, how director penalties are enforced. We also discuss changes to the Regime introduced on 1 July 2012, which allow the ATO to hold a director personally liable even after an Administrator or Liquidator has been appointed to the company.

## **IMPOSITION OF DIRECTOR PENALTIES**

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A director penalty is imposed on a director where certain company taxation debts remain unpaid at the end of the day on which they become due. A full listing of the taxation debts covered by the Regime can be found in section 269-10 of Schedule 1 to the Taxation Administration Act 1953 (Cth), but the most common taxation debts to which the Regime applies are PAYG Withholding ("PAYG") and Superannuation Guarantee Charge ("SGC"). The Regime also applies to estimates issued by the ATO in respect of these types of taxation debts.

For example, if a company withholds amounts from employee wages in respect of PAYG, the amounts withheld will become payable at a future date, known as the 'Due Day'. If the withheld amounts are not paid to the ATO before the end of the Due Day, then a director penalty, equal to the amount of the unpaid PAYG is imposed on all directors of the company at the time the debt was incurred. The regime also applies to newly appointed or recently retired directors.

## PIERCING THE CORPORATE VEIL - THE ATO AND DPN'S

The Due Day for PAYG is usually the day on which a company's BAS or IAS lodgement is due, and for SGC it is one month and 28 days after the end of each financial quarter. Whilst a director penalty is imposed at this time, the ATO is prohibited from enforcing a director penalty until it has issued a Director Penalty Notice.

The director penalty and the corresponding company taxation debt are concurrent liabilities. If a company pays its taxation debt after a director penalty has been imposed under the Regime, then the director penalty is also discharged to the same extent, and vice versa. (N.B. Discharging of a director penalty is different to remittance of a director penalty, which is discussed below.)

### ENFORCEMENT AND REMITTANCE OF DIRECTOR PENALTIES

The ATO must issue a Director Penalty Notice to a director and allow a period of 21 days before it can bring court proceedings against a director for the recovery of a director penalty. The ATO is only required to send a notice to the address of a director noted in the records maintained by the Australian Securities and Investments Commission, whether or not that address is current. The ATO may alternatively send notice to a director at his or hers registered tax agent's address.

Once a director penalty has been imposed by the ATO, there are three ways in which a director can have that penalty remitted, namely;

1. Causing the company to comply with its obligations to pay amounts to the ATO; or
2. Appointing a Voluntary Administrator to the company; or
3. Having a Liquidator appointed to the company.

Directors should note that these remittance provisions are available prior to the issuance of a Director Penalty Notice by the ATO. It is appropriate for directors to consider exercising these options as soon as they become aware of taxation debts remaining unpaid after the Due Day.

If a valid Director Penalty Notice has been issued, and 21 days has passed since it was issued, the remittance provisions are no longer available to a company director, and either the company or the director must pay the amount due to the ATO.

### LOCK-DOWN DIRECTOR PENALTY NOTICES – THE IMPORTANCE OF REPORTING

If PAYG or SGC remains unreported and unpaid for more than three months after the Due Day, a director is unable to have a director penalty remitted by the appointment of an Administrator or Liquidator. In these circumstances, the ATO must still issue a Director Penalty Notice, known as a 'Lock-Down Director Penalty Notice', and wait the required 21 days. Once the 21 days have passed, a director who receives a 'Lock-Down Director Penalty Notice' must pay the director penalty, or cause the company to pay the corresponding company taxation debt.

It is important to note that the ATO is able to issue a Lock-Down Director Penalty Notice, even after an Administrator or Liquidator has been appointed to a Company, if applicable taxation debts that were not reported to the ATO within three months of the Due Day remain unpaid. The only way to avoid a Lock-Down Director Penalty Notice is to ensure that all company taxation debts are reported to the ATO within three months of the Due Day.

## PIERCING THE CORPORATE VEIL - THE ATO AND DPN'S

### DEFENCES TO DIRECTOR PENALTIES

In the event that proceedings are commenced against a director, there are only limited defences available to company directors. Those defences are:

1. Illness or Incapacity (A director was unable to take part in the management of a company.)
2. All Reasonable Steps (All reasonable steps were taken by a director to comply with his or her obligations, or no such steps were available.)
3. Superannuation Guarantee Charge – Reasonably Arguable Position (A director adopted a reasonably arguable interpretation of Superannuation Guarantee Charge legislation.)

### RIGHT OF INDEMNITY AND CONTRIBUTION

A director that has paid a director penalty to the ATO, is entitled to recover that amount from the relevant company, in the same manner that a person can recover amounts paid under a guarantee of a company debt. A director that has paid a director penalty is also entitled to recover amounts from anyone that was also a director at the time the corresponding company taxation debt was incurred, as if all those directors were joint & several guarantors.

### PAYG WITHHOLDING NON-COMPLIANCE TAX

Whilst not technically part of the Regime, the PAYG Withholding Non-Compliance tax was introduced with Lock-Down Director Penalty Notices. This new tax allows the ATO to deny a director, or their close associates, tax credits in their personal tax returns, where the PAYG Withholding amounts have not been paid to the ATO. If a director has been issued a Director Penalty Notice, then he or she can also be denied credits on their personal tax return, for the

same underlying principle company PAYG debt, in effect causing a director to pay twice at the same time. Of course if such a director does pay both amounts, it would be expected that he or she would obtain the benefit of the denied credits in the following period.

### GARNISHEE ON DIRECTORS' BANK ACCOUNTS

Garnishees allow the ATO to compel payment from a third party that holds amounts due to, or on behalf of, a taxpayer that is indebted to the ATO. Once a Director Penalty Notice has been issued, and the 21 day period has expired, the ATO is entitled to seek a garnishee order against any third party that owes money to, or holds money on behalf of, the relevant director, including a director's personal bank accounts.

### CONCLUSION

The ATO will not hesitate to use the Regime, and in particular Lock-Down Director Penalty Notices as it is the only legislative method by which the ATO can hold a director personally liable for company debts. Directors and their advisors should ensure that timely and accurate financial information is available to facilitate prompt action when a company begins to have difficulty meeting its taxation obligations, or a director risks becoming personally liable.

The introduction of Lock-Down Director Penalty Notices to the Regime means that reporting of taxation debts to the ATO is more important than ever. The looming spectre of a Lock-Down Director Penalty Notice should motivate all company directors to ensure that taxation debts are reported to the ATO on time, regardless of whether they are able to pay the debts being reported. Once the hard deadline of three months past the Due Day has expired, there is nothing a company director can do to avoid personal liability.

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**Without obligation or cost, we are available for an initial consultation. Please contact:**

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