

When the grim reaper comes knocking

“there is always death and taxes: however, death doesn't
get worse every year” – author unknown

Based upon our recent experiences, it would appear that the Australian Taxation Office (“ATO”) is becoming much more aggressive in relation to the collection of overdue PAYG and taxes. More particularly, we have:

- noticed an increase in the number of winding up applications filed by or on behalf of the ATO.
- been provided with copies of notices issued by mercantile agents engaged by the ATO to recover debts that had only recently become overdue.
- met with directors who have been served with a Director Penalty Notice (“DPN”) pursuant to Section 222AOE of the Income Tax Assessment Act.

This aggressive attitude adopted by the ATO will in all probability impact adversely on thousands of Australian businesses already suffering from poor cash flow.

According to an article which appeared in The Australian newspaper on 20 May 2010, credit reporting agency, Dunn & Bradstreet, has reportedly downgraded the risk profiles of almost 80,000 companies after watching payment terms deteriorate in the first quarter of this year. The expectation is that many of those businesses are now more likely to experience financial distress over the next year.

In light of the foregoing, we thought it timely to comment upon the weapons in the ATO's arsenal for the recovery of taxation liabilities owed by corporate debtors.

Director Penalty Notices

A discourse on DPN's is outside the scope of this newsletter. Suffice to say that a director in receipt of a DPN has fourteen days from the date of the notice in which to cause the company to undertake one of the following alternative courses of action:

- discharge the debt in full, or
- enter into an arrangement with the ATO for the payment of the debt, or
- appoint an Administrator or Liquidator to the company.

If the director(s) fail to comply with the DPN by not causing the company to undertake one of the alternatives set out above within the specified time period, then each director is liable to pay by way of penalty an amount equal to the unpaid debt.

The DPN is a powerful weapon that should focus the attention of the directors on addressing the problems affecting the financial position of their company. Directors who neglect to deal with a DPN could face personal financial consequences that could be significant. Yet notwithstanding this, we have encountered a number of directors who for a variety of reasons have ignored a DPN whilst others have convinced themselves as to the viability of their businesses and accepted personal liability totally ignoring the advice of their accountants and/or solicitors. We do not monitor what later happens to those that we meet, however in some cases it has been brought to our attention that the outcomes have been disastrous for those concerned.

It is therefore vital that directors maintain a working knowledge of the financial position of the company under their control particularly when it comes to cash flow and the incurring of taxation and other liabilities. The reality is that a company under financial stress will often defer payment of taxation liabilities thus preserving cash for other outgoings considered more vital. This approach may well ease cash flow constraints short term. However the unpaid taxation liabilities remain and will continue to accrue. In our experience, directors who proactively seek to address the problem in a timely and considered manner are likely to achieve a more satisfactory outcome as compared to those who seek to find a solution under direct pressure from the ATO.

Statutory Demands

Like any creditor, the ATO can issue a Statutory Demand under Section 459E(2)(e) of the Corporations Act ("the Act") for payment of a debt within 21 days after service. The debtor company must within the time period specified either pay the debt in full or make an application to the Court to have the demand set aside pursuant to Section 459G of the Act. Alternatively, the debtor company can take pre-emptive action by:

- appointing an Administrator. Such an appointment is normally made in circumstances where there is some prospect of a Deed of Company Arrangement ("DOCA") being propounded; or
- appointing a Liquidator to wind up the affairs of the company.

If no action is taken by the directors in response to the Statutory Demand, then almost certainly the ATO will commence winding up proceedings.

There are many and varied reasons why directors fail to respond to a Statutory Demand. In many instances, the companies in question will have ceased to trade and have no assets in which case the directors will often not care if the company is liquidated. Other companies will be trading and have assets. It is not uncommon for directors of these companies to simply ignore the Statutory Demand by putting it into the "to-hard basket". For others, the Demand may not be received. One reason for that might be the failure by the Company to notify ASIC of a change in the address of its registered office.

Winding Up Proceedings

The serving of a winding up summons will certainly focus the attention of the directors especially if the business conducted by the company is considered to be viable. In these circumstances, the directors will urgently seek advice as to their options under the Act. By that stage, the options are not what they were.

One option might be to attend Court and oppose the application to wind up. However, as the Statutory Demand has expired, there is a presumption of insolvency pursuant to Section 459C(2)(a) of the Act. Therefore, if the directors want to oppose the application, then they will have to satisfy the Court that the company is in fact solvent and that there is some compelling reason why it should not be wound up. Proving solvency can be difficult and the process is likely to be costly.

The directors may consider they have the option of pre-empting the ATO by appointing their own Liquidator. However, pursuant to Section 491 of the Act, a company cannot be wound up voluntarily if an application has been filed to wind up the company in insolvency. Therefore this is not an option available to the directors.

Another option available to the directors is to appoint an Administrator to take charge of the affairs of the company. Whilst technically possible, there is a complication. Pursuant to Section 440A of the Act, the Court is to adjourn an application to wind up a company already in administration, if the Court is satisfied that the continuation of the administration is in the interest of creditors.

The complication arises from the interpretation of the phrase "the Court is satisfied". In our experience, this means that there will need to be evidence put before the Court that will lead the Court to conclude there is a real likelihood that a DOCA will be propounded and that the return under the proposed DOCA will be greater than if the company was wound up. From a practical point of view, it is not always possible to settle upon the likely terms of a DOCA within the time left before the winding up application is heard. In addition, the costs of attending Court and presenting a case can be significant.

In light of the foregoing, it is imperative that Statutory Demands are dealt with within the stipulated time period as this keeps all options open to the debtor company thus giving it the best chance of achieving an optimum outcome.

In the event a company is wound up by order of the Court, then all is not lost. Pursuant to Section 482 of the Act, the Court has the power to stay or terminate the winding up. For such an order to be made, the applicant which is usually the directors, will need to satisfy the Court that the company is solvent and should be allowed back into the market place.

Section 260-5 Notices

Another weapon available to the ATO is the issuance of a notice (commonly referred to as a “garnishee”) pursuant to Section 260-5 of the Income Tax Assessment Act which allows the ATO to collect monies from third parties in satisfaction of taxation liabilities due by other entities.

We dealt with this subject matter in a newsletter issued in April 2006, a copy of which can be found on our web site. For the purposes of this newsletter, all we can state is that we have not encountered any such notices over recent times.

Conclusion

The team at O’Brien Palmer is committed to assisting our contacts help their clients understand and navigate the complex realms of insolvency. As part of that commitment, we would be pleased to answer any of your questions regarding our services. We also offer a complimentary and obligation free initial consultation to establish the nature of the problem and the manner in which we can be of service.

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A Time For Action

Early intervention is the key to avoiding financial disaster. Our experience over many years has proved that survival prospects are increased and losses minimised when the right advice is obtained immediately upon the identification of a problem. Swift, decisive action by our experienced and trusted team of professionals is crucial to a successful outcome.

The Firm

O'Brien Palmer is a specialist practice with national affiliations, focusing on corporate & personal insolvency and business consulting. We adopt an innovative and commercial approach to each matter and offer a dedicated point of contact with a senior team member to ensure that every assignment is given the attention it deserves.

Our Services

Corporate Insolvency

- Voluntary Administration
- Deeds of Company Arrangement
- Receiverships
- Court Liquidation
- Members, and Creditors, Voluntary Liquidations

Personal Insolvency

- Bankruptcy
- Part X / Personal Insolvency Agreements
- Trustee appointments pursuant to Section 66G of the Conveyancing Act

Business Consulting

- Business Viability Reviews
- Prelending/Refinancing Reviews
- Security Reviews
- Management Reporting
- Cash-Flow Management
- Turnaround and Growth Strategies

Without obligation or cost, we are available for an initial consultation.