

Directors Beware – Director Penalty Notices

The Taxman Cometh - Again!!!!

As you may have already heard, tucked away in the 2011 Federal Budget were proposed changes to the ATO's ability to make claims against directors of companies for not only unpaid PAYG but also unpaid employee superannuation. Whilst the changes have been earmarked as "Anti Phoenix" legislation, in reality they have broad consequences for any director whose company is behind on payment of either PAYG or employee superannuation.

Director Penalty Notices have been around since 1993, however the changes substantially alter:

- The amounts claimable against a director under the "Director Penalty" regime to now include both unpaid PAYG and employee superannuation; and
- The concept of 21 days Notification of a Director Penalty Notice by the ATO overruled by an **automatic liability** trigger in certain circumstances.

The changes are simply summarised by the following table which is taken from the Explanatory Memorandum to the draft changes in Legislation.

Comparison of key features of new law and current law

Current law	New law
Directors are personally liable for their company's unpaid PAYG withholding amounts after the expiry of an issued Directors Penalty Notice (DPN).	In addition to liability for PAYG withholding amounts, directors are personally liable for their company's unpaid Superannuation Guarantee Charge amounts.
An estimate can only be raised by the ATO in relation to PAYG Withholding liabilities.	In addition to estimating unpaid PAYG withholding liabilities, the Commissioner can estimate a Superannuation Guarantee Charge debt.
<p>For arrears PAYG the Commissioner may issue a Director Penalty Notice and may only commence recovery against the director 21 days after the notice was issued.</p> <p>A director can extinguish their personal liability by causing one of three things to happen within that 21 day notice period:</p> <ul style="list-style-type: none"> • Payment of the debt; • Appointment of an administrator under sections 436A, 436B or 436C of the <i>Corporations Act 2001</i>; or • Beginning the winding up of the company. 	<p>The current law continues to apply where a company's debt to which the director penalty applies is less than three months old or where the debt has been correctly reported before three months from the due day passes. In these circumstances director liability occurs after the service and expiry of a DPN notice.</p> <p>Once the company's "<u>unreported debt</u>" is three months old, the Commissioner can commence proceedings to recover the penalty immediately and, a director's personal liability is only extinguished by payment of the debt or penalty.</p>

<p>Regardless of whether a company has paid PAYG withholding amounts to the Commissioner, its directors like all other company employees are entitled to PAYG withholding credits withheld by the company from a withholding payment made to the director</p>	<p>Where a company has failed to pay PAYG withholding amounts to the Commissioner, the Commissioner has a discretion to reduce a director's entitlement to PAYG withholding credits relating to withholding made from the company. They will therefore be personally liable for any tax due.</p>
<p>A company director's associates are entitled to PAYG withholding credits withheld by the company from a withholding payment made to the associate, such as salary, regardless of whether the company has paid the PAYG withholding amounts to the Commissioner.</p>	<p>Where a company has failed to pay PAYG withholding amounts to the Commissioner, the Commissioner has a discretion to reduce the creditors of a director's associate that relate to withholding payment made from the company.</p>

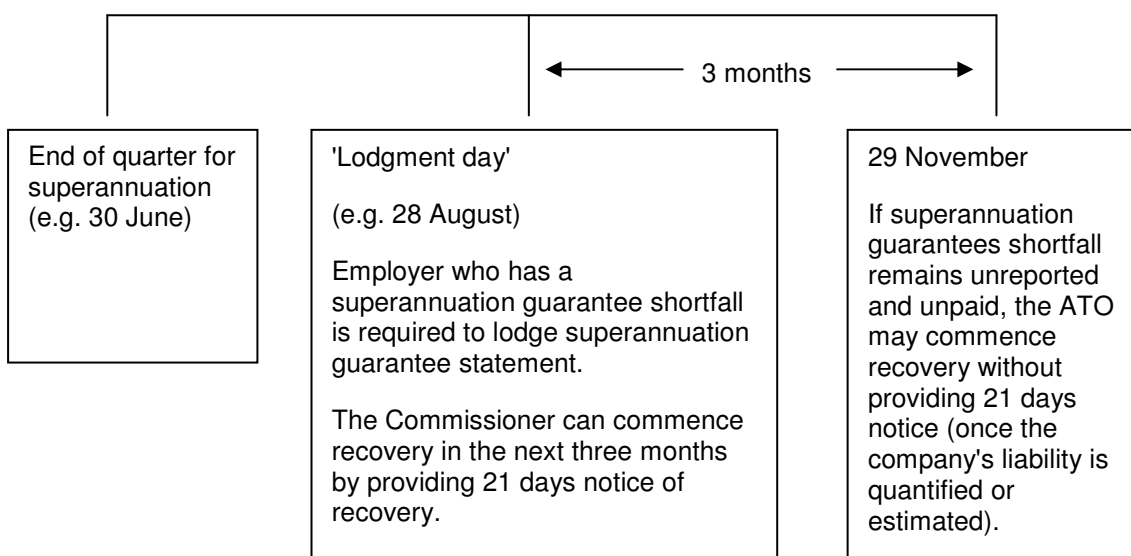
Reporting as opposed to Payment

There is a distinction in the legislative intent between "Reporting a Liability" and "Payment of a Liability". If the relevant lodgments are undertaken, as and when required, to report a liability as being due, but obviously not paid, then the OLD director Penalty Notice regime applies and directors will still have 21 days in which to remedy the position after the service of a DPN.

If a liability is "unreported", after three months of when they were required then an automatic liability for the debts crystallises against the directors of the company.

It is therefore important to ensure that all relevant returns are lodged by the due date even if without payment. Whilst this will not stop the issuance of a DPN with a 21 day action period it will prevent the use of the automatic liability provisions.

They say a picture is worth a thousand words so see the following as an example provided by the Explanatory Memorandum.



No Credit for unpaid PAYG on Directors Returns

These new provisions provide discretion on the part of the ATO to reduce a directors entitlement to PAYG withholding credits in their personal returns where a company has failed to remit the relevant taxes. This is also capable of being used against "Associates" of the director.

Whilst the language of the explanatory memorandum is in terms of "Phoenix" activities it remains to be seen just how broadly these new provisions are applied.

When do the provisions apply from

Whilst the Budget papers made reference to the Law being effective from the 1st July 2011 the Explanatory Memorandum states:

1. The automated DPN provisions "*will apply to all director penalties that are due and payable at or after commencement of these amendments on the day after Royal Assent of the Bill*".
2. The automated DPN provisions also apply to director penalties in existence before the commencement of the new provisions if those penalties were not extinguished before the commencement. To extinguish you must have either paid the penalty or appointed a Liquidator or Voluntary Administrator to the company.
3. The Superannuation Guarantee Charge liability apply if the company is required to lodge a quarterly superannuation guarantee statement to report unpaid and overdue super guarantee shortfall on or after the day on which the amendments commence (i.e. No substantive retrospectivity).
4. The reduction of credits to directors for unpaid PAYG applies from the 2011-2012 income year.

The consultation period for draft legislation has now expired. As to when the legislation will be introduced into Parliament, which starts the process of obtaining "Royal Assent" is unknown however you should assume it will be sooner rather than later.