

CLIENT UPDATE

■ ■ CORPORATE INSOLVENCY

■ ■ RESTRUCTURING

■ ■ FORENSIC ACCOUNTING

Be aware - Director Penalty Notices are on the come back!

Recent Australian Taxation Office (ATO) publications have quoted that ATO collectable debt was \$12.2 billion at 30 June 2009, with \$6.5 billion of this owed by 706,000 businesses with a turnover of less than \$2 million. By January 2010 the amount of debt subject to an ATO payment arrangement may have grown to \$14.2 billion.

This growth in debt is attributed to the effect of the global economic slowdown, and now that economic conditions are recovering, we are seeing a return in favour by the ATO of using Director Penalty Notices ('DPNs') to recover outstanding debt.

What is a DPN?

The ATO has the power to collect outstanding taxes, being deducted amounts under the PAYG provisions, by making Directors personally liable for a 'penalty' for the same amount as the unpaid tax. These provisions create a liability to the ATO in the name of the Director.

Each Director of a company becomes separately liable for the full amount of the penalty.

A Director is made liable by the issue of a DPN that requires a Director to take one of 4 specific actions within 14 days of issue. Failure to comply with the DPN will result in the Director becoming personally liable for the debt.

How to avoid liability?

The 4 actions a Director can take to avoid liability are:

- Pay the debt in full;
- Enter into an instalment arrangement to repay the debt;
- Appoint a Voluntary Administrator; or
- Appoint a Liquidator.

The 14 days is a strict time limit. The ATO has no discretion to extend this period.

Problem Areas

A DPN does not have to be served in the same way as legal proceedings. The ATO only needs to give notice and this can be done 'by leaving it at, or sending it by post to, an address that appears from [ASIC or ATO] documents to be, or to have been within the last 7 days, the person's place of residence or business'.

So, Directors and their advisors must be vigilant to ensure that Director addresses are up to date on the ASIC file or run the risk that a DPN notice may be issued and expire without the Director's awareness.

The 4 choices are actually more limited than they appear. An instalment agreement may take longer than 14 days to negotiate and execute. Directors may not even be aware that this option exists until they receive the notice and then may not understand what it means. Further, there is no certainty that the ATO will accept any proposal made by the company.

What if the company has been deregistered prior to issuance of the DPN?

This is not a defence; the ATO still have the power to issue a DPN.

What should you do?

Act immediately! If the company is solvent, it should pay the tax.

Directors of companies that cannot pay the tax usually decide to appoint a liquidator, by way of Creditors Voluntary Liquidation, or a Voluntary Administrator. Either can be done quite quickly by Heard Phillips.

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Tips on Managing Credit

As businesses deal with the effects of last year's financial crisis, it is important for Directors to consider and respond to factors that may reduce their companies' ability to recover quickly.

Those areas are:

- Inability to obtain bank support when it is needed;
- Inability to repay old suppliers in a timely fashion and obtain new stock; and
- Inability to repay overdue interest-bearing debt.

We comment more as follows.

Don't ignore your Bank

A company's banker is a vital stakeholder in the wellbeing of any company. A banker's support by providing debt funding to match business needs underpins a company's survival.

It is likely that last year's trading has resulted in financial statements that don't appear as healthy as Directors would like. Don't hide this from your banker. Financial statements are a key document to assist with their management of an account, but ensure that when trading performances are disclosed, there is a proactive explanation of plans to restore profits and cash flow strength.

Negotiate with overdue creditors

Suppliers, like bankers, are critical stakeholders in the company.

Many suppliers who are faced with overdue accounts often resort to issuing stop credit notices and formal demands that can impact negatively on a company's capacity to trade.

We recommend that Directors negotiate and document formal repayment arrangements with key suppliers for overdue debts.

This has a twofold effect; both parties can plan their cash flows and therefore better manage credit risk by formally negotiating delayed payment terms with suppliers. Directors can then avoid the inference that debts were not being paid as they fell due.

Don't use credit cards

We increasingly see evidence of Directors using personal credit cards to finance their companies.

Credit cards are expensive and inappropriate forms of finance for a company's working capital funding and will tie the company into debt repayment that often increases with the cost of interest as quickly as it can be repaid.

Not only can cheaper finance be found, but credit cards are inevitably personal liabilities of Directors and their use exposes a Director to a high risk of personal insolvency if the company defaults on the card payments.

Try to refinance credit card debt urgently and take advantage of lower interest rates and payment obligations.

If Directors or advisers have any questions regarding Director Penalty Notices or managing credit, please contact us.

About us

Heard Phillips aims to be the first choice for critical SME insolvency, restructuring and forensic accounting matters in South Australia.

Our firm seeks to deliver superior quality outcomes for clients through our credible and reliable practitioners, who take pride in displaying the highest level of respect to all stakeholders.

