



Changes to tax laws expand personal liability of directors

On 29 November 2011, Royal Assent was received for the Tax Laws Amendment (2011 Measures No. 8) Bill 2011 (Tax Act) and the Pay As You Go Withholding Non-compliance Bill 2011 (PAYG Act).

The new legislation makes important changes to tax legislation, which may have serious implications for directors by expanding their personal liability.

The rationale behind the amendments is a strengthening and further defining of obligations of company directors in relation to employee's PAYG withholdings, enhancing the protection of employee superannuation entitlements and combating fraudulent "phoenix company" activity (ie, deliberately placing a company into liquidation or voluntary administration to avoid payment of debt and liabilities, and then reincarnating the business through a different corporate entity).

Existing PAYG withholding and director penalty regime

Directors of companies are obliged under existing Australian tax legislation to withhold certain amounts from payments made to employees under the Pay As You Go (PAYG) withholding regime. Amounts withheld under the PAYG withholding regime are required to be paid to the Commissioner of Taxation (Commissioner) within strict timeframes.

Schedule 1 of the Taxation Administration Act 1953 (Cth) (TAA) imposes penalties on directors of companies who fail to comply with their obligation to remit to the Commissioner their company's PAYG withholding amounts (or estimates of such amounts) (PAYG debt). Non-compliant directors may become personally liable for the amount of PAYG debt under the director penalty regime.

Under the previous regime, the Commissioner was empowered to issue a director penalty notice (DPN) under which a penalty equal to the amount of outstanding PAYG debt of the company could be imposed on a director if the Australian Taxation Office (ATO) did not receive payment of the outstanding amount within 21 days of issue of the DPN. The Commissioner was restrained under the previous regime from commencing proceedings to recover the director penalty until 21 days after the issue date of the DPN to the director.





How will the existing PAYG Withholding regime change?

Key changes introduced under the Tax Act and the PAYG Act include the following.

Removal of the 21 day grace period under the director penalty regime

Once a company's unreported and unpaid superannuation, referred to below, or PAYG withholding liabilities are three months' old, the Commissioner can immediately commence proceedings against directors without waiting for the 21 day grace period — presently imposed under the director penalty regime — to expire.

Director liable to pay PAYG withholding non-compliance tax

Where a company has deducted PAYG from the salary/wages of an employee/director and reports this withholding in the company's PAYG withholding statement, the employee/director becomes entitled to a credit (against the employee/director's tax liability) for an amount equal to the reported withholding, even where the employer does not remit the withheld amount to the Commissioner. New provisions introduced by the PAYG Act give the Commissioner the discretion to effectively remove that director's entitlement to the PAYG withholding tax credit. This is achieved through the imposition of a new PAYG withholding non-compliance tax upon the director, equal in amount to, and which will effectively cancel the benefit of, the credit to which the director becomes entitled.

Associates also liable to pay PAYG withholding non-compliance tax

Associates of a director may also become liable to pay the new PAYG withholding non-compliance tax, so that a benefit an associate may obtain from a PAYG withholding tax credit will also be effectively cancelled where a company's reported PAYG withholding, as to the associate, is not remitted to the Commissioner. Before an associate can be liable, the Commissioner must merely be satisfied that, due to the associate's relationship with the director or the company, the associate knew or could reasonably have been expected to know that the company had failed to duly remit PAYG amounts, related to the associate, to the Commissioner.

An associate of a director is widely defined, by reference to the "associate" definition in s 995-1 of the Income Tax Assessment Act 1997 (Cth) (ITAA97), so as to include partners, a spouse, children and other relatives of a natural person director.

Additional liability for unpaid superannuation

Currently, part of a director's responsibilities is to ensure a company pays superannuation contributions for eligible employees, at a minimum rate of 9% of their annual salary. There is, however, no sanction imposed upon a director for any failure of the company to do so. The new legislation has widened the scope of the PAYG director penalty regime so that directors may become personally liable for their company's unpaid superannuation guarantee charge (SGC).





As with the amendments to the PAYG withholding regime, once the company's unreported and unpaid superannuation liabilities are three months' old, the Commissioner will be able to immediately commence proceedings against directors without waiting for expiration of the 21-day grace period imposed under the previous regime.

The Commissioner's ability under the previous regime to estimate an unpaid PAYG debt has also been expanded to include estimations of unpaid SGC. The ability of the Commissioner to issue an estimate of the SGC will enable the Commissioner to take prompt action (without having to issue an assessment) to pursue directors of companies who have failed to meet their SGC obligations.

How will the new legislation affect directors?

Importantly, there is no requirement in the new legislation that directors or their associates act fraudulently or dishonestly in order to be liable under the director penalty regime. The regime is not directed solely at "phoenix company" arrangements. Directors and their associates will be caught by the legislation if non-payment of a PAYG withholding or superannuation liability has mistakenly occurred (for example, if the amount payable has been miscalculated or if an employee has been incorrectly categorised as an independent contractor as opposed to an employee).

Businesses should ensure that procedures are implemented, or directors should undertake a review of any procedures currently implemented, in order to avoid or limit mistakes giving rise to directors' personal liability.

Directors should seek the appropriate advice to ensure their company's compliance with PAYG and SGC obligations. This is of particular relevance to new directors as the regime will impose the same personal obligations upon them for a company's prior PAYG and SGC debts that remain outstanding 14 days after they become a director if they do not cease to be a director before expiry of that 14 days.

This article was written by



Jonathan Ilbery, Partner
Tel: 9426 6660
jilbery@jacmac.com.au



Joanna Chandler, Solicitor
Tel: 9426 6775
jochandler@jacmac.com.au

This article was first published in the Insolvency Law Bulletin 2012. Vol 12 No 5, page 110