ATO Phoenix Strategy – Ordering the Phoenix 21/11/2023

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Hello everybody and welcome to today's webinar... Oh, we seem to have lost part of our title, ATO-Ordering the Phoenix. Okay. My name is Susannah Gynther from Wolters Kluwer, CCH Learning, and I will be your moderator for today. Apologies for that. I just thought I had my title wrong, but I did not. Okay. A few quick pointers before we get started. In the handout section, you'll find the PowerPoint slides for today's presentation. If you're having sound problems, please check your settings in the audio section on the GoToWebinar panel. Try to toggle between audio and phone. Just a reminder that within 24 to 48 hours, a notification for the e-learning recording will be emailed to you.

You can ask questions at any point during the presentation by sending them through the questions box. I will collate those questions and ask them at the Q&A towards the end of today's presentation. CCH Learning also offers a subscription service which many people have termed Netflix for professionals. It provides members with access to our entire library of recordings, as well as live webinars for a competitive flat fee. That's for over 500 hours of content. For CPD purposes, your viewing is logged automatically.

Your presenter today is Bruce Collins, founder and principal solicitor of Tax Controversy Partners. Bruce is the founder and principal solicitor at Tax Controversy Partners, currently helping clients to solve all types of tax issues with the ATO and SROs. Before moving into private practise in 2017, Bruce worked for over 35 years in the tax office, a third of his time as a senior executive in what is now Client Engagement Group covering most ATO functions. Bruce was the leader of the technical and case leadership area in private wealth for several years prior to leaving the ATO, as well as having previously been the strategic and technical leader for many of the ATO's compliance programmes. Bruce led the Secretariat for the Inter-Agency phoenix Forum, co-chaired with ASIC, and was the risk owner for the ATO's Phoenix Risk and led the Phoenix Task Force at the ATO from 2012 to 2015. I'll now hand you over to Bruce to commence today's presentation.

Bruce Collins:

Hopefully people can see the screen. It should all be good. So yeah, look, we're going to talk today about what is meant by phoenixing, the risk areas that the ATO and other agencies focus on, what constitutes illegal phoenixing as opposed to legitimate liquidations, the ATO's detection strategies, the covert and tax crime audits that get conducted of suspected phoenix operators, penalties for making a false or misleading statement which often accompany phoenix cases, looking at director's liability for phoenix schemes, and director penalty notices and other aggressive or aggressive, assertive maybe is the better word, collection strategies that the ATO are using to deal with the phoenix risk. We'll look at the introduction of the Director Identification Number and its intention to help to combat phoenixing, and then we'll look at some content from various ATO media releases about phoenix cases. A part of their role is to publicise what they're doing to encourage people not to do it. So in other words, to encourage other people to comply by showing what happens when people who are engaged in phoenixing get caught.

We won't go through every slide and every word because there's quite a bit of stuff, particularly in the ATO media release section, but we included those so that they would be informative for people more generally. So before we start, we just want to get an idea of who is in the audience today so I can tailor some of the content accordingly. So the first poll that, Susannah, I'll administer is about whether you're an accountant or a tax agent, a lawyer, a financial planner, a student, or in an other category. So Susannah?

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Thank you, Bruce. So I'll just launch that poll, and if you could please put a click in the radio button next to the answer that best describes who you are, that would be great. And of course, just a reminder, if you do have any questions during the presentation, please put them into the questions pane and we will get to those questions in the Q&A session at the end of the presentation. I'll just give you about five more seconds to get your votes in. All right, let's close the vote and have a look. So 93% of our audience are accountants or tax agents with 7% lawyers. Thank you very much, Bruce.

Bruce Collins:

Thank you for that, Susannah. So am I back now? Yes. So the next poll is actually about whether people are in private practise and have had exposure to ATO compliance cases involving potential phoenixing, whether they're in private practise and have had no such exposure, or people are in public practise, or again, if they're in the other category. So again, if you could just run that for me, Susannah.

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Not a problem. So there we go. So who are you? You in private practise and have had exposure to ATO compliance action, are you, B, in private practise and have had no exposure, C, in public practise, or D, other. So once again, please put a click in the radio button and we will see what we have. I'll give you about five more seconds to get your votes in. Okay, let's have a little look at our audience. So we have 54% who are in public practise. We have 23% in private practise with no exposure. We have 15% who say other and 8% who are in private practise and have had exposure. Back to you, Bruce.

Bruce Collins:

Okay, thanks for that. Yeah, look, that's very helpful. So look, in essence the question of what is illegal phoenixing is probably the most vexed question here. Unlike some areas of the law where you've got a definition, there's no real definition for what illegal phoenixing is. The ATO defines it in their annual report, and I think this is a variation of a formulation that I actually came up with many years ago when dealing with people when I was involved in the Phoenix Strategy for the ATO, but it's about the systematic process of deliberately incorporating and liquidating operating companies with the intent of having the company or companies avoid their obligations to their employees, suppliers, and to the tax system. So it's about systematising it. It's about repetition. It's about intention. So those are the ideas that differentiate bad conduct which might be illegal from the legitimate liquidation of companies as we'll talk about later. There are legitimate reasons why people do need to liquidate. In fact, they're compelled to do so.

2014 project that I was involved with Melbourne Law School and Monash Business School identified that there are various classes of conduct, legitimate, legal phoenixing or business rescue, problematic phoenix which might stray into that territory, the illegal type of phoenixing where there's an intention to avoid debts formed as the company starts to fail. So in other words, they change their intention. The illegal type of phoenixing where people are doing it as a business model with that repetition and recurrence, and the complex illegal phoenix activity which is actually like it's taking it beyond a business model to where it's an integrated criminal business model which actually spans usually various entities, various industries, and various types of activity, can sometimes also be associated with organised crime.

Now the way in which these risks play out for the ATO is really about mostly employer obligations, but not exclusively. So employees obviously miss out on wages, superannuation, and other entitlements, and they come with associated non-payment of monies to the ATO for those employment related things like the Pay As You Go withholding, super guarantee, et cetera. It also of course results in a competitive disadvantage for other businesses that are actually paying tax and complying with those obligations. Suppliers and subcontractors are often left adrift in these arrangements, and ultimately the community misses out in revenue, including GST and income tax revenue from those sorts of transactions as well, and those could have all gone towards community services. So the ATO risk profiles using a sophisticated analytics model that risk rates the population of entities in business. It takes the information and stratifies the population and looks for indicators of that recurrence and that intention, and it's supposed to identify those higher risk characteristics and feed them in.

Now they have information about previous liquidations, business addresses, business types and reports from various other agencies, et cetera, such as ASIC and departments responsible for the operation of small businesses and employment obligations and things like that. So all that stuff gets put into the mill and then that plays out of course in other contexts besides the ATO's context. So you've got law enforcement agencies that are concerned with illegal activities generally, and some of that can actually be connections with outlaw motorcycle gangs or other organised crime. But also, of course, if people are evasive enough or fraudulent, they can stray or actually step right over the edge into criminal activity. Of course, you've got the corporate regulation by ASIC where you've got people who are company directors who choose intentionally to evade their obligations as directors, and that can include trading while insolvent obviously. There's also the question about whether registered liquidators or business turnaround specialists are actually facilitating phoenixing.

Now, the same sorts of issues that apply for the ATO in Pay As You Go withholding legal so apply to state revenue offices or Revenue New South Wales or whatever they're called in each jurisdiction, and that's mostly around payroll tax. There's parallel issues for workers' compensation for the various regulators that deal with that, and of course there's the employee entitlement system which is guaranteed by the federal government as well, but virtually any area of regulation can see phoenix operators trying to evade those regulatory restrictions. So if there are restrictions on what they can do, they'll try and evade them. If there are benefits that they can obtain, they'll try to get them in properly and then they'll phoenix the structure in order to try to stop getting caught.

Now the ATO leads the Inter-Agency Phoenix Forum and the Phoenix Task Force and it involves a whole range of agencies, the usual suspects in law enforcement, the Australian Criminal Intelligence Commission I think it's actually called now, the Australian Federal Police, ASIC, obviously the ATO, the Clean Energy Regulator, DEEWR, Department of Sustainability, Environment, Water, Population and Communities, Fair Work Building and Construction, Fair Work Ombudsman. I think in fact the Fair Work Building and Construction might've actually stopped with the changing government. But the two roles of that forum were really to share intelligence and to help coordinate strategies across the different agencies so that they could work together on dealing with this pernicious set of behaviours. Now it also helps to provide governance and relationships with other forums.

Now the idea of illegal phoenixing, as I foreshadowed earlier, is about companies being liquidated, wound up, or abandoned, and then a new company being set up, rising like a phoenix from the ashes to carry on the same business activities but without the debts, without the debts being paid. Now it's worth pointing out that liquidated is obvious. If a liquidator is appointed, somebody looks at the affairs of the company to some degree, but wound up but leads to liquidation, but abandoned is a curious thing, but you see quite a bit of this where people just choose not to pay the ASIC fees and the company gets deregistered, but no liquidator is appointed and no statement of solvency or insolvency has to be prepared by the directors. That's a sneaky way of trying to avoid having that scrutiny and that can be important in terms of progressing these things.

Now, creditors, suppliers, subcontractors, employees don't get paid and the ATO of course is the largest unsecured creditor in the Australian system. So it can really be difficult to see when something is illegal phoenixing or whether it's just that a company becomes insolvent. Not every company flourishes, and as a consequence it means that many of them are going to be in a situation where a company law actually requires them to be liquidated because that's what a company director is obligated to do. So the ATO leads that task force which I mentioned, which has a whole bunch of mechanisms to try to detect these sorts of things and to then coordinate with other agencies who are funded by government through the ATO's budget to work together to try to identify and deal with these potential phoenix operators.

Now it's very common. In fact, it's probably almost one of the defining characteristics of phoenixing that there'll be dummy or puppet directors who are secretly being controlled by the people behind the scenes who are the puppet masters for that. They're called de facto directors, and those people are hard to detect because of the fact they're using these puppets or dummies to actually conceal their identity and their involvement with the company structure. You'll often see those people continuing to pursue negotiations with customers of the company as if they're a director, even though they are in some cases prohibited from being directors, either from disqualification or other reasons.

Now, not all phoenix-like activity is illegal. So when an entity fails, it's a deliberate design feature in the company law system that they have the ability to start again, and people can have a series of pieces of bad luck without intending to be phoenixing, so it's hard to differentiate in a sense from the bad ones from the people that just have bad luck. But repeated resurrection of companies and the moving on of the assets into new iterations of that company can actually be highly problematic, and that's the reason that phoenixing is dealt with in the way it is. Now the ATO as a creditor will obviously be chasing things.

Now it's really important to recognise that on the first occasion it's hard to say somebody's phoenixing. So if somebody's not liquidated a company or caused it to be deregistered, then it might be an incipient potential phoenix but it's not an actual phoenix at that point. Once they've done it several times, it becomes easier to see. Repetition in that sense tends to indicate that either they're really bad business people or they're doing it as part of an intentional plan.

So the idea that companies can be liquidated and then people can start again is of course a key feature of the system, but there are instances where people can be prohibited from engaging in the role of company directors by disqualification, and so again, that's something that is applied in more serious cases. Of course, if somebody is personally bankrupted for something like a director penalty notice, which we'll talk about later, that also complicates the scene a bit.

Now the ATO has access to a huge pile of information and its people are probably aware. The idea at the moment is that as artificial intelligence and data analytics become more sophisticated, it leads to greater insights being available for government in particular who have access to all of that information to then see trends and patterns that wouldn't otherwise have been detectable without those sophisticated computer analysis and prediction models. So all of this stuff goes into the mix and what comes out is a map of who appears to be engaging in phoenix behaviour and what might be done in a stratified and segmented fashion to try to apply strategies to deal with them, the most serious of which involve law enforcement action or coordination with other agencies, but some of which will be nudge strategies and letters being sent out to people to prompt them to comply and to warn them of the adverse consequences of not doing so.

The ATO of course also uses the task force model as a mechanism to exchange information to detect and to address, that should be various forms of tax crime, by the way, that's a typo. So the ATO has the power to disseminate information, but when it does, it carries some risks. So sometimes they can disseminate information they shouldn't or where it's unlawful, sometimes agencies send information to the ATO that is unlawfully disseminated, so that needs to be carefully considered. In some cases you'll find that that's a problem. Now, law enforcement agency information sharing, generally aside from the task force for the phoenix task force which is a defined one, can still be very useful to detect various forms of tax crime and other forms of non-compliance. Of course, the ATO feeds back the results of its own compliance activities, its reviews and audits, into the system, and those can include covert audits where in fact they're auditing somebody and the person doesn't know they're being audited, and that happens in the more serious types of cases where the ATO suspects more serious forms of non-compliance.

Now that can actually be a bit of a dartboard where the ATO starts with a central figure and then they go out from there to map their relationships with business associates, family members, and things like that. I've seen cousins and second cousins caught up in the web of ATO audit activities where, because they have that family association and they have some transaction with the central figure, they end up then being caught in the net and getting treated fairly harshly as a result. So where a covert audit happens, sometimes the only indication that a taxpayer has is that they get a position paper or even an amended assessment without any foreshadowing of it whatsoever, and sometimes the money is then garnisheed of their account in order to stop them sort of doing anything to dissipate their assets.

Now, tax crime audits, including phoenix audits, therefore have a tendency to proceed on the basis that the information that causes the concern is strongly negative. So in other words, it looks to the ATO like the people are engaged in very bad behaviour. Now that can be wrong, frankly. The impression that the ATO has can actually be incorrect, and it's very, very hard once an agency starts rolling the snowball down that hill to actually get them to stop before it turns into a complete avalanche that flattens a client. And so it's very difficult to provide a contrary narrative which is convincing, but it's very important to try.

Now there are some fundamental issues that apply when somebody is actually subject to such inquiries and starts getting asked questions. You can't refuse to comply with a notice. There's no privilege against self-incrimination so you have to answer the questions that are asked under notice. But if you're asked questions in a criminal investigation, then they can't use the coercive powers, they have to run in parallel. The auditor can ask those questions under notice, provided it's for the purpose of the audit, but they can't conversely use that information for the criminal investigation or criminal prosecution of the person who has given the coerced statement. So the ATO will then usually rely upon other information, including law enforcement information, for the purposes of that criminal investigation.

Now, ultimately, at the end of the day, as we've talked about in other presentations, the ATO has the dice stacked, loaded very powerfully in their favour because they can rely upon the statutory burden of the taxpayer having to prove that the assessment is excessive in any subsequent challenge. In other words, the onus shifts to the taxpayer having to prove the negative rather than the ATO having to prove the positive.

Now, associates who are subject to these sort of processes need to be very careful because if they're faced with a choice about whether they drop their associate, potentially a family member, under the bus or whether they try to hold back information, and the question about incriminating other people is actually more complicated because if you're subject to a notice where they ask you questions about are you associate, then there's no privilege against self-incrimination issue there and therefore the information about that can be used in the subsequent criminal case on the associate, even though you can't use the information about you because you've been compelled to provide that information. So the ATO tends to suspect information provided by taxpayers or even their advisors, so there tends to be a rejection of that without corroboration. So the provision of a contrary narrative will often need to be accompanied by that sort of corroboration.

While it's not a phoenix case, the Melbourne Corporation case and the Anglo-American Gold case that happened the same day are good examples of the discussion about the problems of intragroup transactions not having third party cooperation because the only people involved with it are related parties. Now, the ATO has a tendency for phoenix to consciously use more of its harder edge powers, some of which are specifically designed to deal with phoenix operators. Garnishee notices are one, director penalty notices, moving more quickly towards legal collection processes like statutory demands and winding up notices, and also during liquidation to provide indemnity for the costs of liquidators to pursue investigations. If a company liquidator gets an assetless company, one that actually has no cash and the assets are not worthwhile selling, maybe they've been stripped, maybe the entity was always kept as a shell, the question is that they need to get external funding in order to be able to deal with the investigation because otherwise they don't get paid. So the ATO is one of the key indemnifies in those situations.

Now, the garnishee power is something people are probably aware of and familiar with, but I'll go through a couple of the things. It's a statutory power. The commissioner doesn't need approval from any third party or a court to actually do it. Now it has to be in relation to unpaid tax debts, and it's served on a third party who has an obligation or may have an obligation to pay the taxpayer. So rather than paying the taxpayer, the garnishee requires the other third party to pay the commissioner instead. So the idea here is that it either will be money that is held on account or money that is owed to the taxpayer who is the debtor.

Now a person who doesn't comply with a garnishee is subject to a penalty and the penalty is quite significant, and any payments that they make, every time they don't comply with a garnishee notice, they're actually subject to that offence. So effectively it's a pretty big stick to hit people with, and encouraging somebody or trying to induce somebody not to comply with a garnishee is also an offence in terms of conspiracy or causing somebody to do something which is unlawful under the criminal code. So it's quite a serious power and it's one that can be used.

I've seen cases where every entity in a group and all of their trade creditors and all of their financiers were actually served with garnishees. So every entity was served with a garnishee in respect of every entity in the groups, the other entities in the group's debts. Given that ATO had assessed in the alternative against all of them, it ended up with about 20 of those garnishees in place and that became very complicated, and then of course, all of their debtors, the entities that owed the money and all of their financiers were also hit. So it became quite complicated.

Now, director penalty notices are a key tool specifically designed to deal with phoenix operators and strengthened over time to do it better for the ATO and worse for taxpayers. So the powers apply broadly to Pay As You Go withholding liabilities, superannuation guarantee liabilities and indirect tax liabilities, GST, WET, and LCT in that indirect tax space. Now, the way that works effectively is that a director who had the power at some point in time to cause the amounts to be paid is actually subject to a potential director penalty notice for that period. So each of the directors, if there are multiple directors either at the same time or sequentially, can actually be hit with a DPN. That means that the company is liable for the primary obligation and the directors are actually liable for a penalty for the company not having paid it. The reason for it being built that way is because of the idea that the penalty avoids the idea of multiple collection and incontestable taxes being raised. So it's intended to make it hard for people to argue contrary to having to pay the DPN.

Now each of the entities are jointly and severally liable for the penalty itself, and the company of course is liable for the primary obligation. So there rights and indemnification against other parties if you pay and they're liable, but in practise, they're very complicated to navigate. Now there are different types of DPNs and the broad thing is that there are lockdown DPNs where you basically don't have any other option other than cause the company to pay or for you to pay. Now, lockdowns arise when the liability has been unreported and remains unpaid three months after the due date. Lockdown is therefore bad because you have no option to liquidate or do a small business restructure or place the company into administration which you can do in a non-lockdown context, and it's not uncommon for the other company to have in fact some liabilities that have been reported and some that haven't. But in each case, the debt has to have been outstanding for more than three months.

Now, there are defences for DPN, but they're very tight. There's the health condition or other good reason that prevented a person from participating effectively in the management of the company for the entire period they're a director. And then there's the all reasonable steps defence where they've actually taken all reasonable steps to try to, in a sense, to arrange to have the payments made, et cetera, but they have failed because of circumstances outside their control.

Now, the legal collection of process is actually things that people are probably familiar with, but essentially the ATO is statistically over time the largest petitioning creditor in the Australian debt collection system. Currently, all the feedback I'm getting from insolvency practitioners and ASIC is that the ATO has returned largely to pre-COVID levels of debt collection activity, including initiating processes for both personal bankruptcies and company liquidations. So the idea at the moment is that after waking up from the COVID slumber last year, so sort of March or April in 2022 onwards, they've really been pouring on the heat for these sorts of things.

Now, when you get a statutory demand, the thing is you should engage with the other creditor, in this case the ATO. It's harder to set aside a statutory demand after the fact, but you can do so where there's a sound basis and an explanation for why the statutory demand should be set aside. In opposing a winding up notice for a company, if you have a genuine dispute, it's obviously a rationale for why it should be opposed, but the raising a dispute late in the piece is something the ATO's recently called out as being a potentially negative behaviour, and they choose in most cases to oppose the opposition and to pursue the winding up. So it's better to do it as early as possible, but you can deal with it at the last minute in emergencies which we've done in cases as recently as the last couple of weeks, but it's better to have a sound objection.

Now, one problem you do have, and it's not mentioned on the slide, but is that once a company is placed in liquidation, the previous controllers lose the power to pursue an objection against the liabilities and those liabilities might be the reason that the company is then placed in liquidation. Now, that can be very complicated and can make it very difficult, therefore, for somebody to challenge a DPN because the DPN revolves around the liabilities raised for the company, but if the company is then in liquidation, you can no longer control the company if you're a director to cause it to object, and therefore it's hard to pursue in that circumstance unless you retake control of the company which is a procedural nightmare.

Now, as I mentioned earlier, the ATO chooses to indemnify liquidators for the cost of investigations. Now, this puts the commissioner in a weird position and sometimes one where I think that there's a risk of impropriety in the sense that being both petitioning creditor who has an interest in the liquidation being pursued and also indemnifying the liquidator for their activities, it can also almost mean that the commissioner ends up remote controlling, in one sense, the actions of the liquidator. Now that may involve the commissioner releasing information to that liquidator that would be protected information for the purposes of Division 355. So in other words, information that shouldn't be disclosed except for a proper purpose and there's no hole carved in the secrecy provisions allowing for that dissemination.

There's the course of duties exception, and some might argue that in the course of the duties of an ATO debt officer, they're releasing that information for the purposes of supporting the ATO's role as creditor, but I think that's a pretty slippery slope when you look at things. But the aim of such indemnification is actually to see whether there were related party dealings or adverse behaviours of directors in terms of their conduct that could be challenged, and sometimes the company can pursue the directors or shareholders or associated entities in that way to try to recover money, and the ATO can subrogate its claim against the company by pursuing the claim of the liquidator. In other words, it can actually trace the money and then try to follow that money through to where the alleged benefit actually flowed.

Now, there are other things that can happen to directors as well. A director can actually become liable for a tax offence committed by the company where they caused the company to actually do that under Section 8Y. There's also the Crimes Taxation Offences Act which creates criminal offences for fraudulently evading a range of taxes administered by the ATO, and there's the Crimes Taxation Offences Act then interacts with 8Y to make the director personally liable for the taxes. It doesn't tend to happen a lot, but it is actually a bit of a nightmare for the relevant director when it does occur. In a related issue, there's also the Binetter case that's cited here that the director there was alleged to have entered into a tax evasion scheme on behalf of the company and was therefore found, in that case, to be potentially liable to compensate the liquidators for the tax debt that had therefore been incurred and not met. There's also the potential claw backs that are available on related party dealings through the company law system.

Now, insolvent trading is obviously a key factor, are the liquidation risks for these matters. If you actually engage in insolvent trading, you're in breach of 588G of the Corporations Act. The director can be made personally liable for company debts incurred while the company was trading insolvent, and of course the liquidators in conducting their investigation can make an adverse report to that effect, and that can actually result both in clawing back of those transactions as well as the potential for seek to disqualify the director for future terms based upon that misconduct.

Now there's also a relatively recent provision which I was partly involved with back in the day having created. I didn't create it personally obviously, but it was something that was recommended as one of the phoenix recommendations, and effectively 588FE(6B) of the Corporations Act deals with what are called credit toward defeating dispositions. So a liquidator can apply to court to void the disposition or they can also apply to ASIC to make an order undoing the disposition. It hasn't been used an awful lot. There's only been a couple of cases, but it's only been in for a few years now, and I think that there's going to be scope for this to be a more frequent factor in the system. Clearly it's intended to provide additional tools in the arsenal of dealing with potential phoenix operators, and it was clearly recommended and implemented as part of the phoenix strategy by government.

Now, the capacity to act as a director in the future can actually rise in two contexts broadly. If somebody is a director and they're made bankrupt, they cease to be able to be a director. They're disqualified until the period of bankruptcy elapses, but of course, as I mentioned, ASIC can actually disqualify somebody from being a director. While that can be challenged, it's very hard for a director to actually succeed in such challenges.

One of the problems with directorships historically has been the fact that the data on the company's register was very fragmented in one sense. So my middle name's William, so I could be Bruce William Collins, I could be Bruce Collins, I could be Bruce W. Collins, I could be B. Collins, I could be B.W. Collins. So any one of those could be on the company's register recording me as a director, but how can you tell it's the same me rather than being another Bruce William Collins, like the King's Council who is in fact an ex-judge and a well-known barrister who ran a royal commission on the building construction industry in New South Wales. So which of us is it that is actually on the register? So the introduction of the Director Identification Number was to actually deal with that by providing a unique identifier which is used to differentiate the Bruce William Collins' from the others and to actually show which one's which.

Now everybody who is a company director now has to have one. If they don't, they've committed an offence. It was introduced gradually, and the Modernising Business Registers project, which has lapsed now, was responsible for introducing that regime and the ASIC and the ATO jointly sort of managed it. It is intended to provide a mechanism to link the directorships and to deal with accordingly.

So there's a few case studies here. I'm not going to go through all of them in detail but I'll just skip through them, but these are drawn from the ATO website. So what you tend to find is that there's a lot of phoenix activity in the building construction industry, in the road transport industry, the cleaning industry, and the security industry, anywhere where there's a lot of labour. So here you've got a classic one where there was the alleged phoenix operator dealt with through the Phoenix Task Force and it resulted in like a million bucks being paid to keep things running. So the credit terms were also changed here, so there's a bit of a systemic response to that as well. Now, building construction industry one, this one resulted in a whole bunch of cash being found and also identified more than $1.6 million in unpaid tax debts, and these sorts of things are pretty much the... I suppose it's the bread and butter of the phoenix sort of work.

Labour hire is a continuing issue because effectively it's actually prudent for a company structure to have several different companies that have different parts of the business segmented for asset protection reasons. So you can have an asset-owning entity and you can have an operating entity and then you can have a labour-providing entity. So that trilogy of entities is pretty common and it makes sense. You can also have labour hire providers who provide labour to third parties. So that labour entity can actually be set up for legitimate reasons, or it can actually be phoenixed, or it could be set up to be constructively phoenixed over time. So if they are doing that, if they're actually phoenixing, then they get a competitive advantage over honest businesses that are out there doing the right thing. Sometimes if it was accidentally stepping into the phoenix space, they can be drawn back and become compliant, and this example talks about one and the $2 million that were repaid, a benefit to the system as a result.

Now, property developers are, if you like, a very frequent flyer in the phoenix space. Not every property developer by any means is phoenixing and not everybody who has a bad project is phoenixing, but there are a fair number of businesses in the building construction industry that are actually operated by phoenix operators, and this apparently was one of them, and they had the appointment of shadow directors, falsification of bank statements, unauthorised withdrawal of funds, basically embezzlement from a company, and this one was actually quite a substantial one by the look of it. So it is important to recognise that there was a substantial amount of money involved and there were very substantial consequences for the people involved once they were caught.

Now, this guy, David Iannuzzi, was disqualified from practising as a registered liquidator because of a very systematic non-compliance, and as the court said in dealing with the challenge to that action, it was a pretty poor showing more generally, and it demonstrated that he wasn't a fit and proper person which is the test for being a liquidator. Now, there's also some ATO media releases here about things. This one is actually about people conspiring to defraud multiple labour hire firms in the vineyard, fruit and vegetable grower and mid-processing industries. Again, labour hire, labour-heavy industries are the ones where this tends to be most prevalent, and there were very substantial amounts of money involved in this. So the key thing is that mostly the money flows through to the individuals and they live their lives through it, and usually they're living on the unpaid tax or super guarantee amounts. This one seemed a bit more than usual, so it does seem like it was a more significant scheme in some ways than the usual ones which tend to have people cutting into the margin. This one seems to have cut pretty heavily into the bone.

Now in the ATO annual report which, look, I read the annual report, I'm a tax geek, so I go through and I pick out the bits that are relevant to this sort of stuff, and here you see that the Tax Avoidance Taskforce has done some things, but the Serious Financial Crime and Phoenix Task Force and the Shadow Economy, they're all dealing with these sorts of issues and they've raised substantial amounts in liabilities and in cash collections.

So it's a continued area of focus to the ATO where they very heavily invest in this because they got special resourcing from government, and that includes what people may not realise is phoenix focus which is a lot of the warning letters, nudge letters which are sent to people to try to encourage them to comply, and the engagement visits where some businesses are visited by the ATO, and also the reviews and audits that are focused on these sorts of activities. They're all part of an integrated strategy differentiating using that risk model to apply resources in a targeted way to try to deal with this risk. The more serious matters get a heavier hand and the more extensive but are not as serious matters get more of the lighter touch until they get bigger, in which case they then end up with a heavier hand.

Now the registry services, the Australian Business Registration Service is clearly one of the initiatives that helps to identify and deal with phoenix operators, and particularly the support for the Director Identification Number regime I talked about earlier. But the ATO is the leader of the Phoenix Task Force as well as being a lead agency for Serious Financial Crime and the Shadow Economy, and it also does things with Illegal Tobacco Taskforce things as well.

So overall, the ATO does a whole bunch of things in relation to phoenix, and some of them are ones that we'll talk about now. So they share information. They get information from other agencies and other agencies get information from the ATO, and this actually talks about the number of referrals to different agencies about these matters. So the other agency can ask for information about an entity or an individual or both from the ATO or the ATO can initiate information flowing from their... Set up these processes when the legislation for the Phoenix Task Force was introduced. You can see that there's continued flows each year in relation to these other agencies. It goes onto the next page and it goes onto the next page. So there's quite a bit of stuff in there that actually goes through what that information flow looks like.

Now all of that stuff has to be approved by a senior executive. It doesn't mean that they have to stamp every one, but they have to approve the flow, and at one stage, I was one of those senior executives. The point is that overall the information flows both ways and some of that information, by the way, might be a huge pile of data about millions of entities. Some of it might actually be a specific query about one entity or one individual. So there's a bit of peas and pumpkins here in terms of the size of the relevant flows.

Now, the ATO Phoenix Task Force results overall have been pretty substantial in terms of its effects as it talks about here. The collection might be 107 million, it says so on one media release, but it says 108 million in the annual report. It's resulted in 2,500 referrals of suspected illegal phoenix activity that came in through the Tax Integrity Centre. It's done 567 disclosures to other agencies, and it's raised over its life from back when it started more than $2.1 billion in liabilities, and every year it collects north of a hundred million. So it's a substantial part of the ATO's total programme.

Now, back in 2015, there was a report that actually talked about the insolvencies in the building construction industry. I actually gave evidence to that committee back in the day, and the idea that company directors are regarded as optional to pay their taxes and comply with tax obligations. So I think that should be mild, by the way, rather than milk. Again, apologies, it's a typo. But essentially the idea is that this led to a range of recommendations which have now flowed through into legislation, and so what we've got now is a slightly different situation than the one that existed back in 2015, but it's still an ongoing problem and there's still going to be activity on it.

Now, if your client is subject to phoenix inquiries, you've got to consider whether it's beneficial to make a disclosure. There are penalties applicable to many of the obligations, the liabilities that are involved, so it's possible that you might want to get a shortfall penalty remission by making a disclosure. But also if your client's not involved in phoenix conduct, they might be peripheral to actual phoenix conduct or it might just be a legitimate insolvency, then it's important to provide a consistent and compelling narrative, to actually provide a convincing argument as to why the ATO is wrong in being concerned that the client is phoenixing.

Now if you provide that narrative early in the piece, that's great. If in fact you didn't understand or the client didn't understand the nature of the ATO inquiries, you might need to correct the record later on and do it again in a convincing fashion and provide corroborational support for the assertions that are made. If your client is subject to information collection activities and notices and things like that, sometimes you might need to challenge those notices and to do so in a way which doesn't lead your client to be viewed as being a negative player.

But getting legal advice on these cases, I can't emphasise too much, is beneficial. If you don't get support for you as practitioners, you can't properly support your clients. As a consequence, you can end up with very negative outcomes for the client and perhaps for you as an advisor if you were involved in any of the transactions in any fashion. So there's also the question about whether you pull a record and discharge a client if you form the impression that they are in fact themselves engaging in phoenixing and lying to you, but that's a different question as well. But otherwise, we might open up for questions now, Susannah.

CCH Learning:

Thank you very much for that, Bruce. Yes, we will be opening up for questions and we will spend the next few minutes taking questions. So just a reminder to please type them into the questions' pane. To give you some time to type those up, I will mention our upcoming webinars. Okay, so coming up, we're looking at Preparing Clients for Pre-filing Mediation of Property Matters, and tomorrow we will have our Division 7A update. On Thursday, we're looking at Legally Assisted Mediation and the Role of Lawyers. We'll also be Preparing and Participating in Negotiations next week, as well as our monthly Tax Technical Update for November, and we'll also having some Insights on the Managing of Termination of Employment. If you are interested in any of these sessions, please head to our website at wolterskluwer.cchlearning.com and have a look and see if they are right for you.

So let's have a little look at our questions. Okay, so I have a question from Sarah. Sarah is asking, "A client has come with some sketchy looking accounting books and they've asked me to be their tax agent moving forward. However, the directors have incurred multiple tax debts, and despite following up I've now been asked to liquidate the company and open a new company. What do I do?"

Bruce Collins:

Well, there's three risk areas there that I think worth exploring. Firstly, taking on a new client, there's always a due diligence process that every firm should do in terms of their uptake of a new client. Sometimes you need to say no, but if you don't originally and then you get indication subsequently that they're bad actors, you ask questions to test that hypothesis. If you find that they are in fact acting improperly, then you need to make a call to protect your own firm. If you're an employee, obviously raise it with your principals, but if you're a sole practitioner, you need to make your own call, or in fact, if you're a principal in a firm. But if they have in fact incurred liabilities through poor business practise or adverse economic circumstances, it's perfectly legitimate for them to liquidate and set up a new company. As I said, doing it once might be all right. Doing it multiple times might start to look fishy.

But the other point is though that the directors need to understand that they may become personally liable to those classes of liability that you need a director penalty notice on, and in addition, they need to be aware that if they have engaged in insolvent trading, they can be opened up anyway. If they're avoidable transactions which have occurred through related party dealings, advising them of those things and saying, "Well, if you liquidate, you do realise that your liquidator is going to ask questions about A, B, and C." That doesn't mean they shouldn't liquidate, but they need to be aware of the consequence. So either ditch the client or navigate them through the process and advise them because you're supposed to advise them of the consequences of their actions so that they are able to make informed consent as to what they do then.

CCH Learning:

Thank you for that, Bruce. I do hope that helps you there, Sarah. I have a question from Junie. Junie was asking, "For a genuine insolvency liquidation when a company has a GST debt and cannot generate income to repay the GST debt, will the ATO issue a DPN to recover the GST from the director or directors?"

Bruce Collins:

Generally, yes. The thing is if there is a genuine liability, however it arose, then the ATO is quite likely to seek to apply a DPN a fair amount substantial. That can happen even if you liquidate the company. If it was reported late in a lockdown DPN context, then the ATO can and will pursue it. If there's a genuine dispute over the amount, that's a different thing because they won't issue a DPN generally while there's a dispute over the liability, but if DPN gets issued and the company isn't yet liquidated, you're faced with a fork in the road as to whether you dispute it or you instead, if it's a non-lockdown DPN, you actually liquidate the company in order to protect the director while leaving the liability on the company. So it's, again, a fork in the road.

CCH Learning:

Thank you very much for that, Bruce. I do hope that helps you there, Junie. I have a question from Michael. Michael was asking, "Can I report another agent who I think has been helping a client in illegal phoenix activities?"

Bruce Collins:

Yeah, absolutely. The Tax Integrity Centre that I mentioned earlier in the presentation is actually the [inaudible 00:59:12], as it used to be called colloquially, to report suspected instances of bad conduct, but also there's no reason why you can't make a report to the tax practitioners board as well. So if you find somebody who you believe is engaging in adverse conduct contrary to their legal obligations, I think it's perfectly legitimate to do so. The only question you have is whether you're using confidential information related to the client to actually do so. Sometimes what happens is client moves from agent A to agent B, agent B says Agent A has done the wrong thing and then the client's going to be the one who carries the can for that particular instance. It may indicate that the agent A is systemically a bad actor, either because of incompetence or because of collusion with people to try to evade or defraud, but it is actually, again, a question about what's in the best interest of your clients.

You are in fact sharing, if you share information about the client, confidential information which you're prohibited from sharing under the Tax Agent Services Act if you're a tax practitioner or under your relevant legal obligations as a legal practitioner under whichever state or territories rules you have. But as an officer of the court, if you're a lawyer, you've got a positive obligation which may supersede the obligation not to provide confidential information so you're actually, again, in a bit of a fork in the road thing. I'd suggest a call to the ethics area in your relevant state or territory if you're a lawyer in that situation. But generally speaking, if you can do it without dropping the client into the bucket, I think that that's actually the appropriate thing to do to try to deal with bad actors.

CCH Learning:

Thank you very much for that, Bruce. I do hope you helps you there, Michael. I also do have a question from Wayne. Wayne was asking, "My client has been diligent with paying their tax obligations, but has had bad luck with contractors and has now liquidated three companies. They've retained their employees and assets. Is there anything that I or they need to be worried about?"

Bruce Collins:

That's a really good question, and it goes to a point I made earlier. It's the narrative. If adverse economic headwinds, particularly say in the building construction industry, you get this domino principle where head contractor goes bust, subcontractor goes bust because head contractor's gone bust, sub-subcontractor is then under a cloud because they can't continue to operate when they don't get paid the money that they were going to get paid by the subcontractor. Now at that point, they need to liquidate. That doesn't mean they need to stop practising their trade, but it does mean that they are going to need an explanation.

So the ATO is quite receptive to those sorts of issues, and if you explain that stuff to the ATO, they will normally take it in account in their subsequent decisions, not always, but generally, and if they don't, you need to escalate to a higher level in the ATO. But if it happens repeatedly, then again, it starts to look worse. So if they've done it three times, that can be quite complicated in terms of the way in which that narrative would have to be provided to the ATO. There's an old saying that once might be an accident, twice misfortune, but three times smacks of enemy action. So the more frequently it occurs, the more likely it is somebody's going to draw an adverse inference from it.

CCH Learning:

Thank you very much for that, Bruce. So there you go, Wayne. Something to think about. Well, that does seem to bring us to the end of our questions today, but if you do have any further questions, Bruce's details there on the screen so please reach out and I'm sure that Bruce will be able to help you. So in terms of next steps, I would like to remind you all to please take a moment to provide your feedback when exiting. We've asked you a couple of questions about today's webinar, so it's really important for us to hear your opinions. It's also a reminder that within 24 to 48 hours you will be enrolled into the e-learning recording which can be watched multiple times, and have access to the PowerPoint transcript, any other supporting documentation, and a CPD certificate. I would very much like to thank Bruce for his session today, and to you, the audience, for joining us. We do hope to see you back online for another CCH Learning webinar very soon. Please enjoy the rest of your day. Thank you very much.

Bruce Collins:

Thanks a lot, everyone.