How to Deal with the ATO on Bankruptcy and Winding Up Cases – What you (and your clients) need to know
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Hello, everybody, and welcome to today's webinar, How to Deal with the ATO on Bankruptcy and Winding Up Cases: What You and Your Clients Need to Know. I'm Susannah Gynther, from Wolters Kluwer, CCH Learning, and I will be your moderator for today. Just a few quick pointers before we get started. If you're having sound problems, and can you hear me, please toggle between Audio and Phone. Hopefully, you can see this instruction on the screen, regardless. If you are looking for your PowerPoint for today's session, it's saved in the handout section of your GoToWebinar panel. And shortly after the session, you will receive an e-mail letting you know that E-Learning Recording is ready to be viewed. You can ask questions, at any point during the presentation, by sending them through the Questions box. I will collect 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 currently helping clients to resolve 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 the client Engagement Group, covering most ATO functions. Bruce was the leader of the Technical and case leadership area in Aggressive Tax Planning, and then, 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 private group, and advisor-focused compliance programmes. In those roles, Bruce was also involved in dealing with many of the most complex settlement and debt collection negotiation cases, for private group and scheme participant cases. I will now pass you over to Bruce, to commence today's presentation.

Bruce Collins:

Thank you for that, Susannah, I'll just share my screen, and make sure it's the right one. Everyone should be seeing this now. Okay, good.

So today, we're going to be talking about ATO debt collection strategies, and how they intersect with the individual and corporate insolvency systems.

Essentially, the ATO has its debt collection strategies, and it has ramped them up a little bit of late. And then, we'll need to talk about how individual insolvency law and bankruptcy works, and what the alternatives are of bankruptcy, and corporate versions of the same thing, how companies are wound up, and what the alternatives to liquidation are.

We'll talk a bit about securities, because securities can be an important part of convincing the ATO not to proceed with either individual or corporate insolvency. We'll talk about the issues for garnishees and director penalty notices, which are powers that the Commissioner specifically has, that most creditors don't have.

We'll talk about the issues that intersect with the objection process, under Part 4C of the Tax Administration Act, and bankruptcy and corporate insolvency processes. We'll also talk about the potential issues when somebody is subject to either a potential bankruptcy, or a corporate insolvency, to actually seek review of some of the decisions that might be involved, under the ADJR Act.

For individuals, there is also some relief for serious financial hardship, but it only applies, really, mostly to income tax-related liabilities in general.

We'll talk about GIC remission requests, and we did a presentation on GIC requests, and payment plan offers, as well. That's two presentations on those, previously, but we'll touch on a couple of issues.

Because it's quite commonly a factor that a substantial amount of the liability may be GIC-related, that is being pursued by the Tax Office. And sometimes, the taxpayer will try and negotiate, at a late stage, a payment plan, to forestall either corporate insolvency, or individual bankruptcy.

Now, we talked about securities earlier in the list, but there's also the questions about how you offer security and when. And there's also a power that public sector agencies have to compromise liabilities owned to the Commonwealth. Effectively, if you owe money to the ATO, the ATO does have a power to compromise. That overlaps with some of the other provisions that specifically apply to individuals and companies, and we'll talk about those.

Now before we kick off, it's always a good idea to find out who's in the audience, and what's going on. So I might just firstly, do a little poll, if Susannah can administer it for us, to find out who the people in the audience are, and whether they are accountants or tax agents, lawyers, financial planners, and students or others. So back to you, Susannah.

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Thank you Bruce. I'll just launch that, sorry, launch that poll. If you could please just put a click in the Radio button that best describes your situation, that would be brilliant.

I'll just give you a few moments to get your votes in, and then we'll close the vote. Okay, I'll just give you five more seconds to get any votes in.

Okay, I'm going to close the vote. And let's have a quick look, shall we?

So 78% are accountants or tax agents, with 22% lawyers. Back to you, Bruce.

Bruce Collins:

Thank you for that, Susannah. The other poll is really just to see what experience people may or may not have had with the ATO, and involvement with bankruptcy or liquidation cases, if they're in private practise, if they've had experience, or if they're in private practise, and they've had no such experience with the ATO in those sort of matters. Or alternately, if you're in public practise including with the ATO.

And the last category is Other, just in case there's somebody else here we aren't expecting. So back to you, Susannah.

CCH Learning:

Thank you, Bruce. I'll just launch this poll. So again, just click in the Radio button that best describes your situation.

A is in private practise, with experience. B is in private practise, with no experience in bankruptcy or liquidation. C is public practise, and D is other.

Just a reminder, of course, if you do have any questions throughout this presentation, please put them into the Questions box, and we will get to those questions in the Q&A session, at the end of the presentation.

I'll just close that vote, and let's have a little look here. So we have 63% in private practise with experience, and 38% in private practise, with no experience. So back to you, Bruce.

Bruce Collins:

Okay, thank you. Well, that's a nice mix of levels of experience, so I'll provide an intermediate coverage of some of these topics, as a result.

Look, the ATO's tax approach with collection of debts is based upon the idea that most people are generally compliant. The pandemic response and the post-COVID landscape have actually left us with issues and concerns for the ATO, and we'll talk about some of the strategies that the ATO is pursuing at the moment, and how they've become harder-edged.

We'll talk specifically about what the current areas of focus in debt collection are, as setting the context for when bankruptcy or corporate insolvency will be on the ATO's agenda for particular taxpayers.

In general terms, the ATO has a benefit that the Australian community is amazingly compliant. Worldwide, we're one of the most compliant countries in the world, from a tax perspective. So the majority of payments of are actually made voluntarily, either automatically, through the application of credit, because of the design of the system, things like pay as you go withholding amounts, or alternately, because people just pay.

Now, during the pandemic, obviously, the ATO downshifted radically to collect debt less assertively, let's say, because of the fact they were giving everyone a break, like other creditors, and at the direction of government. So there was a lot of deferral of liabilities, and there were a lot of matters that couldn't be pursued under the government policies that came in, to prevent a flood of insolvencies occurring.

Now, that meant that people were being given free rides, basically, on a lot of their liabilities, during the COVID lockdown periods, in particular, without the normal requirements being met around evidence being provided, and things like that. It was just a general approach that everyone was getting a reasonable deferral.

And a lot of the staff in the ATO were redeployed to other work, so there was fewer people to be doing work on those issues during that period. Now, post-COVID, I mean, COVID's still around, but after the lockdown period, when things became a bit more normal, the problem is that lots of businesses were still suffering financial stress from COVID, and from the rising interest rates, and the increased supply chain costs that arose during that period, and that have continued, since now a lot of businesses were paying late, and the debts were accumulating. And people were not prioritising paying the tax and super liabilities.

They expected that their interest and penalties would continue to be remitted, as they were during COVID, and a lot of people were just playing the ostrich play, and waiting for the ATO to contact them, rather than engaging actively. As a result, debt increased substantially during that period between 2019 and 2023, so it's way up to $50 billion and more now, by the end of 2023.

90% of that total is business debt, and around 33 billion, or 75% of that value, is actually small business debt. So the ATO is concentrating a lot on small business debt, and including in that 33 billion, there's 1.8 billion in unpaid super guarantee charges, which the ATO takes quite seriously, because it's really the employee's money that should be in their super.

Now, the ATO is concerned about that, and they're obviously focusing on these issues, because they want to make sure that the strong compliance culture I talked about doesn't get eroded. They don't want people to be disengaged from the tax system, and they don't want people in general to form the conclusion that other people are getting away with it.

Now, there are problems with cascading debts. The domino principle applies, where if you've got a large, say, building industry player who goes broke, all of their subcontractors, and the people who provide them with supplies, suddenly suffer financial stress because of that.

You can see these sorts of issues playing out with some of the corporate collapses in the building industry lately, for instance. And in the broader economy, if enough of that happens, uncontrollable and uncontrolled insolvencies will then impact the economy negatively, because people won't be able to work, and all of those sorts of things.

The idea is to manage the debt pool in a way which takes into account, which ones can continue trading, which ones are zombies that should be allowed to pass quietly into that sweet dark night, let's say. Now, the ATO is actually now, in my observation, at pre-COVID levels and some more. They are expecting that there'll be on-time lodgement and payment, and they're taking debt collection action.

In observation for myself, and other practitioners with whom I've spoken, and I've spoken to about 50 people about these issues in the last, probably two months, other practitioners are all saying the ATO is acting earlier, and they're more willing to escalate to legal action.

And they're taking a tighter rein on GIC remissions, and they're only considering those remissions in a more limited range of circumstances. They are taking payment plan decisions on the basis of shorter periods being expected, and that 12 months seems to be pretty much the element.

They are focusing on five key target areas, which are, effectively, unpaid super guarantee. And now, there's over two billion outstanding, and the majority of that's in small businesses.

They're concentrating on the ATO audit adjustment pool, where people have been audited, basically. I've had clients being rung the day after the assessment issues by ATO debt, for very significant debts, and trying to engage with the taxpayer the next day.

That was weird, because it was a COVID audit, that one case, where the taxpayers only found out about it on say, the Tuesday. And then, on the Wednesday afternoon, their tax agent's getting a call, chasing up the potential payment of the debt. When you've got millions or tens of millions of dollars outstanding, I mean, the ATO takes it seriously.

They're also focusing, understandably, on refund fraud. So if you get money that you're not entitled to, and the ATO identifies it as a potential refund fraud case, they're going to be all over it.

They're also looking at aged and high value cases. So they're looking at it more than $100,000, and overdue for more than two years, and they're not really entertaining long payment periods, as a result, so they're not giving as many missions to those outstanding cases.

Now, there was, of course, a big fuss, the robotax, as it was called, where people were having their previous debts resurrected, and they're being contacted about things. And there's been a bit of a readjustment on the ATO front, as a result of that. Generally speaking, if you owe a substantial amount of money, the ATO is going to be knocking on your door in the fairly near future, if they haven't already done so.

So clients are coming to practitioners, and raising those issues at the moment. Of course, with employer obligations, and that touches on the unpaid super guarantee issue at the top. The ATO takes very seriously whether people are paying their pay as you go withholding, and their super guarantee obligations.

So if they are self-assessing and lodging, then they are somewhat protected from Direct Penalty Notice possibilities for those liabilities. But they are then going to be subject to the ATO chasing them up pretty quickly thereafter.

Now, it seems as if, from the public statements made by the ATO, and the practical experience that practitioners are relating, that payment plans and GIC remissions are being much more tightly policed than they used to be. Therefore, they're described in this presentation as being an exception rather than the rule.

So people want to try and engage, they want to do it well, and obviously, we've done other presentations on some of those issues, as well. So engage early, engage often.

Now, insolvency for individuals generally requires that there be a Statement of Claim lodged, which actually includes, in the case of the ATO, liabilities for unpaid tax. Now the way that that works is that they'll usually, for most taxpayers, they'll write to the taxpayer before initiating Statement of Claim, maybe a couple of times.

But if it doesn't get paid, then they're going to be starting to issue a Statement of Claim, which gets served on the individual, at their last known address. Then they are effectively being required to go to court. If the amount repay is not repaid to the ATO soon, then it's quite likely that the ATO will then apply to have that Statement of Claim recognised by the court, and a judgement issued.

Now, generally speaking, it's a prerequisite that you have judgement against an individual before you can seek to bankrupt them. There's some other acts of bankruptcy, like avoiding service or fleeing the country, which can actually trigger potential bankruptcy notices anyway, but generally, there'll be a Statement of Claim, and a judgement obtained first.

Bankruptcy notices then are served, and if somebody doesn't pay the bankruptcy notice, it's like a formal final demand for payment, and that constitutes another act of bankruptcy, of the more routine kind. On an act of bankruptcy being demonstrated by nonpayment, the creditor can seek what's called a sequestration order, which is the formal act of bankrupting somebody.

That also gives the ATO choice of who is the bankruptcy trustee. So there's an advantage, in one sense, to having the taxpayer go bankrupt themselves, and choosing their own trustee. The effect of that is that the bankrupt's assets are then managed by the trustee in bankruptcy. They lose the legal right to manage their own affairs in respect of their pre-sequestration debts, and they become a new legal person, effectively, in respect of their finances.

After the bankruptcy, pre-sequestration belongs to the trustee to manage. Post-sequestration now belongs to the new person, and their debts are generally quarantined between those two statuses, except for the fact that there's rights to pursue the bankrupt individual, in respect what are regarded as excessive salary receipts. Of course, they have to provide information to the trustee.

Now, most bankruptcies end three years and one day after the person is made bankrupt. But it can be extended by application, usually by the trustee, in order for it to go to five or eight years, instead. But that really requires that there be some doubts about the cooperation of the bankrupt individual, and potentially, that there might be assets being concealed, or something like that, that require greater pursuit by the trustee.

Now, there are some alternatives to bankruptcy for individuals, and they're listed here, but I'll go through the slides that follow. If you've got temporary debt protection applications, so you can effectively get 21 days to try and get your affairs sorted out, before unsecured creditors can pursue you. Relatively unusual, but it happens occasionally.

The ATO is more likely to engage with somebody informally during the initial period of a bankruptcy notice, or indeed, a Statement of Claim, rather than going through a temporary debt protection process. But it can still happen.

There's also debt agreements, which are effectively an agreement to pay like a payment plan. This is an agreement to pay a sum the debtor can afford, so it's a bit like a compromise. So it's like a payment plan for a compromise. And the idea is that you have to take into account the degree to which other creditors' interests might be involved, as well, because it's between a debtor and the creditors, rather than just a single creditor. Otherwise, that creditor could be getting an unfair preference. And it can be used to manage tax debts.

But the risk is that the ATO may not agree to such an agreement when offered. Then you're back in the grounds of potentially going through the bankruptcy process.

The more formal process equivalent of that is a Personal Insolvency Agreement, sometimes referred to as a PIA, or a Part 10 arrangement. What happens is that the trustee takes control of the person's property, a bit like an administration for a company, and they make an offer to the creditors.

The creditors are then able to make a decision about whether they accept the offer or not, and the duration of the PIA is then negotiated between the trustee and the creditors, on the basis of the information that comes from the bankrupt or potentially bankrupt individual. Now, you can retain some of your assets through a personal insolvency agreement, in a way which is not like what happens in a bankruptcy.

So if you have a personal insolvency agreement, you can potentially keep your house or your car. That can also happen in compromises, as we'll talk about. So there is a possibility of some pursuit of a debt after a personal insolvency agreement, if it turns out there was fraud, concealment of assets or things like that, as well as the other things that are listed on this slide.

Now, there's another alternative to bankruptcy, which is actually not an alternative to bankruptcy, but it's a way of getting out of bankruptcy. It's called a Section 73 proposal. So effectively, they're offering a Deed of Arrangement, or a Deed of Composition. Now it annuls the bankruptcy.

So the bankruptcy takes place, goes on the register, the person's now an undischarged bankrupt. But they can then facilitate an offer, that is not in relation to property or assets, or money that's held by the trustee. So it's usually funded by third parties, family and friends is quite commonly the way it works.

That money is then offered to the participating creditors. You can set one of these up, and sometimes, the ATO will bite that cherry, and at that second bite. Really, that may actually get a person out of bankruptcy.

We've had a number of cases where there've been Section 73 proposal offers and the ATO has refused them. There are others where they've actually accepted them. It depends on really whether the money is money that they wouldn't otherwise get, because it has to be funds which are not otherwise available to the trustee in bankruptcy. So if the sweetening of the deal is that the third party will pay enough, it can actually sway the Commissioner in the right direction.

Now, companies, it's a bit similar, but the names are different. So the first initiating process is a statutory demand, which has to be served on the company's registered office, as listed with ASIC. It gives 21 days to respond.

They can comply with the demand, or they can apply to the court for the demand to be set aside, because it's defective, it's inaccurate, in other words, or a reasonable defence is available for not paying, such as there was a setter of transaction, or a cross-claim. Or indeed, in the case of a tax-related liability, there could be an objection to the underlying liability to which the statutory demand relates.

Now, assuming that there is nonpayment, then the company is assumed to be insolvent, and the creditor can then commence court proceedings to seek winding up. So the creditor applies for a winding up application to the court. The notice is issued, and the debtor is advised that legal proceedings have commenced.

Now, there still exists some options that you can take at that point, before the winding up order is made by the court. In order for there to be a winding up order, and indeed for bankruptcy, somebody has to be willing to take on the role of either trustee in bankruptcy, or the liquidator. So there needs to be a consent to act filed, but the courts in both cases can order somebody from the list to take on the role involuntarily, if you like.

If you have a member's voluntary liquidation, that the directors or shareholders normally offer to pay the liquidator, the same thing can happen with the trustee in bankruptcy. So somebody agrees to pay the fees. It means that the person who consents to act in either role is going to then be funded to do the work.

It doesn't mean they're friendly and controllable by the people that pay them, because they still have a statutory duty, as trustees in bankruptcy, or liquidators, to do the right thing, and conduct inquiries. Essentially, in the case of a winding up order, the liquidator will be appointed, and then, the assets are called in, as they are for the bankruptcy process, and usually, the assets are sold. That pays the creditors in proportion to their claims, a cents on the dollar sort of arrangement.

But costs come out of the cost of winding up, the cost of the liquidator. It doesn't include, obviously, the secured assets of the individual company in either case, but there'll be a calling in of the assets and there'll be a pursuit of any liabilities to the company. So in other words, an asset of the company could include a loan from a director.

One of the things that people don't understand is, if they've got DIV 7A loans, for instance, they're actually assets owned by the company. So if the company's in financial difficulties to put the hands of a liquidator, they can call in those loans.

And suddenly, the individual who thought that they were safe behind the corporate veil, can find that they've also got civil litigation claims against them, in respect of those unpaid debts. The alternative to liquidation is effectively different types of external administration. So you can have a voluntary administration, which leads to a Deed of Company arrangement.

So effectively, if you go into administration, the idea is that you're trying to get to the point where there can be a Deed of Company Arrangement, or a DOCA, offered. There's small business restructuring, and there's receivership over assets.

Now there's a question about standing, and we'll talk about security deposits and garnishees, and Director Penalty Notices, on the way through. But effectively, a voluntary administration, the liquidator, or sorry, the administrator, in this case, takes control of the company.

Now it can save the business, if it's possible to be salvaged. Or it can offer, because of again, external funding, a better return for creditors than if the company had been simply wound up.

Now, if it results in a Deed of Company arrangement, the DOCA itself will provide effectively a schedule for payment or distribution of funds. It has to be proportionate to the interest of each of the creditors. It can actually involve restructuring the business as well. You then have the idea of what results in the completion or termination of the DOCA.

Now, DOCAs can fail. If the creditors don't vote in favour of it, it can fail at that stage. But also, if it's not implemented in accordance with what the DOCA said was going to be done, then it can fail as, well. Then you back in the territory of being potentially subject to liquidation action.

There's also a more recently introduced, somebody called it liquidation light, or administration light, where somebody is appointed as a small business restructuring consultant to take control of the business in a similar fashion to an administrator, to go through the process of developing a restructuring plan, with these conditions about eligibility, as specified in the slide.

During that period, there are protections around not being able to put the company in liquidation. Or do other activities, like seek to enforce personal guarantees, while the small business restructuring process runs its course. It's supposed to take a month, but I've seen ones take longer, and the creditors are usually happy if there's positive progress towards getting them some money.

Now, receivership is a bit different. In one sense, receivership is over the control of assets, which are subject to a security. Really, the receiver's put in place to realise those assets, as part of protecting the interest of the secured creditor. Now, if they get any other money beyond the security interest of their creditor who appointed them, they will obviously be required to distribute that in accordance with the other creditors' rights and obligations.

Now, they can't sell at a fire sale price, which is less than the market value. Now, if you think about it, the market value of something is the willing but not anxious buyer, paying what they're willing and not anxious, or will accept.

But in a fire sale, like a receivership, inevitably, the vendor is going to be acting to secure the interest of the secured creditor. So they're going to be taking into account the time value of money, for however long it takes to sell.

So there's a drivedown in price there, although they're not supposed to sell it less than market value, and the best price reasonably obtainable is not the same as market value. Now, the receivers cover their own costs first, then they pay disbursements to the secured creditor, or creditors, in order of their secured interest. Anything left is paid back to the company or its external administrator, if one's been appointed. So if there is an excess, that's good.

So if you've got somebody who's got a value loan on a real property, if they sell for 95% of what the property was ostensibly worth, there's going to be 25% theoretically available to distribute back. Some of it'll go in costs, but that's the idea of what happens with that.

Now, there are some issues that arise with external administrations. One is that the individual or company change their standing. The individual that no longer has standing, in respect to their pre-insolvency affairs, and the directors of the company lose control of the company, and the liquidator is appointed, instead. The trustee in bankruptcy for individuals, or the company liquidator, takes control, instead.

Now, that means that the person can't initiate legal proceedings, and can't take certain legal actions anymore, because the trustee in bankruptcy, or the company liquidator, is now responsible for the affairs of that particular entity. Now, they are taking action in the interest of creditors, and that means that they may not choose to fund, say, an objection against the liabilities of the taxpayer.

Now, disputing a Director Penalty Notice becomes very, very difficult if a company goes into liquidation. If the individual director is actually the one who is going to be subject to a DPN, then they are better off pursuing that objection process before you get to liquidation, rather than allowing liquidation to occur, and then, being unable to contest the value of the assessments underlying the DPN.

Now that means that there might also be the need to indemnify, that is, paying money, or cover their costs of the pursuit of that particular dispute with the ATO, and that could include both objection and AAT litigation.

We've seen many cases where those are factors. And it can be quite tricky if the liquidator of a company, for instance, won't pursue such an objection, as to what the director then is left able to do.

Now, the ATO has a unique power, which I've mentioned previously in other presentations, to require a taxpayer to provide security. Now, this is not something that most creditors have, as a power.

These security bond deposit demands are actually a power to think and require that that security be offered. It's subject to a whole bunch of, as the Commissioner might reasonably believe appropriate tests. So it's quite a sweeping power, and all the court cases so far shown that it can be used in quite a, I don't think I'd use the word "cavalier," but quite a discretionary fashion.

It's a power that I understand from other practitioners, and in our experience, seems to be becoming more widely used than it previously was. If that's the case, then this is something, that we have to watch that space. Now this can happen during the preparatory phase prior to a liquidation of a company.

So the ATO might, instead of liquidating, serve a notice requiring a security to be provided. Now, the other end of the spectrum is that the taxpayer may decide to offer security, and that can actually be something offered as a sweetener to get a payment plan.

The Commissioner can suggest security be offered, if they've identified assets to which security might attach. So the effect of offering such security is that if the taxpayer defaults, the ATO has referenced that security, and that can mean that there can be some tricky tactical issues for the taxpayers to consider, about whether they're actually forfeiting rights that wouldn't otherwise be surrendered, particularly under personal guarantees.

But the benefit is that winding up costs can be avoided, and the court process can be stopped, if security is sufficient. And then there is a subsequent meeting of such payment plan.

Now, it can actually be something, as well, where it can be offered during the course of negotiations of a dispute. So if you're objecting, sometimes, the ATO will request what's called a 50-50 arrangement, to actually have 50% of the tax paid, as a way of giving a holding position. Now, not everybody can do that, because they don't have 50% of the tax sitting around in their bank account.

They don't want to go and borrow it, because they may not have to pay it in the end. So therefore, offering security over an asset can be an alternative to doing that in ways which allow the taxpayer to continue to trade accordingly, while resolving such a dispute.

Now, the ATO also has the power to garnishee third parties who owe money to an individual or a company, or indeed, a trustee of a trust. Now, the requirement is that there must be a debt which is due and payable.

The person who served with the garnishee must be holding money, which is, or will become payable, to the taxpayer who owes the debt. Now weirdly, our garnishees survive the insolvency of the taxpayer. So an earlier garnishee continues to prevail after an individual, say, goes into bankruptcy.

I've seen cases where employee individuals who are getting more than the threshold for requiring contributions to be made to the bankruptcy, have actually had garnishees, in place and the money's taken out. But I've also seen once where somebody with a very low income has actually received such a garnishee, requiring 30% of their gross salary to be paid in to the ATO, instead of going to their bank account.

And then, when the person tries to go bankrupt in order to mitigate that, those debts, the ATO continues to collect the money from their employer, straight out of the gross amount. The only alternative that a taxpayer in that situation has, by the way, is to change employers after they're bankrupted, which means that they lose their employment status, and continuity of any benefits.

So it's quite a serious thing, but the case law is clear on that, in relation to bankruptcy. Now, the idea is that the ATO says they won't take garnishee action on disputed debts. So if there's a dispute via objection or appeal, then they won't be taking that action. But that doesn't mean they won't already have taken action, by the time the person seeks to object or appeal, and the ATO may continue to enforce that garnishee subsequently.

So it's better to engage early, to lodge your objections or disputes as early as possible, to forestall such garnishee action, because the garnishee is quite a powerful tool. It can be issued, not just to banks and financial institutions, it can be issued to the purchaser for real estate transaction, requiring them to pay money to the ATO.

And I've seen sales go off, because the taxpayer gets spooked, sorry, the purchaser gets spooked, because of the taxpayer's liabilities. And I've seen asset sales, like sale of businesses, go bad, for the same reason. So it can actually be a negative experience, under the circumstance.

It can be served on an associate, so that if there's a corporate group, and the ATO is concerned enough about it, they'll garnishee everything going. I've seen 12 garnishees issued on entities within a corporate group, in respect of all of the entities in the group, other than the entity to whom the debt relates, just in case any of them are going to make payment to that entity.

Now, I've mentioned Director Penalty Notices already, but they're parallel concurrent obligations, in respect of GST and other indirect taxes, pay as you go withholding, and super guarantee liabilities. Now, the idea is that those are not the liability of the company. They're a penalty for the company not having paid those amounts.

We've done presentations on DPNs, and I'm sure we'll do others in future, but the idea is that the commissioner can recover from the directors, as well as the company, and that liability to recover continues to apply for lockdown DPN liabilities, at least after the company is placed into liquidation, or another insolvency process.

So there's an incentive, therefore, to get a Deed of Company arrangement up for a company, or to otherwise negotiate for a payment by the company, to be made to extinguish the liability. This stuff can make life very complicated for directors, when those things occur.

Now, there's a bunch of tax specific options that rise, when dealing with late stage insolvency matters. I'll go through the slides, rather than reading the list.

The first is, if there's a genuine available ground to object to a decision that can actually be subject to objection, then it's a good idea to object, before you get to insolvency. And in relation to arguing the Statement of Claim that remains unpaid, or a statutory demand that remains unpaid, shouldn't result in winding up of a company, or the sequestration of an individual.

It's very, very important to try to do that early, so as to stop the loss of control I talked about earlier, because only the trustee in bankruptcy or liquidator can do it after the appointment of an external administrator. Now, the requirement must be that an objection has to address why the relevant amount of the liability, which is subject to the claim, it should not be payable.

Now usually, an objection is going to be in respect of the liability to which the legal action relates. Sometimes, it could be something else in relation to another amount, that would actually cause the amount subject to the liability, to be paid like a credit, or an offset.

Somebody has to lodge an objection in the approved form, specifying grounds. They have to do it within time, but the ATO may not be willing to actually permit an extension of that time. Now, the ATO may not stay their collection action. They can, and have, in cases I've seen, instead pursued collection, while there was a dispute on foot. And courts are reluctant to disturb that power, unless there's good grounds to do so.

Interestingly, well, the Commissioner will usually agree, 99 point something percent, there are cases where they regard it, that the objection or AAT litigation, as being spurious or frivolous, effectively, a delaying tactic. They may therefore not take action to exercise the discretion to give extra time to lodge.

The AAT, for small business matters, now has power to stay collection action, while an AAT application is on foot for the liability. And I understand, from the legislation for the new administrative review tribunal, that it will actually have that power retained. But it's only for small business matters, so it doesn't necessarily cover the circumstances for everybody.

I've just talked about this slide unintentionally, but the idea is that the Commissioner can exercise that discretion, but we are seeing a reluctance to grant such an extension late in the collection process, such as immediately pre-insolvency. So you have to have persuasive explanation as to why it's been delayed, and the ATO may not be that happy with it, but you can always go to the AAT, to appeal against such a decision.

I've mentioned earlier that there is relief potentially available, for serious financial hardship that would arise, as a result of the collection of debts. Now, generally, those debts are limited to income tax-related, income tax-sourced penalties, and related interest charges. Now, there's a practise statement that articulates what to do with these sort of decisions.

The AAT is actually generally a little bit more receptive to these applications than the ATO, but not all the way. They quite commonly refer to the Practise Statement as authority for why they're refusing to exercise the power. Now, the serious hardship is actually the idea of people being left without the basics of life, accommodation, food, clothing, medical supplies, or a reasonable education for themselves and their dependents. So the discharge of that is actually sensible and reasonable.

Part of the problem with these, though, is going to be that you sometimes have the circumstance that the person's caused the debt to remain while they've paid other creditors. The ATO, and indeed, the AAT, doesn't take that thing kindly.

Now, in order to qualify for this, you actually have to provide all the relevant information. All activity statement and income tax returns need to be lodged, and up to date. And then, there are no other amendment requests, or outstanding tax disputes on foot. So this is the last ditch application for those types of liabilities for which you can get on serious financial hardship. It doesn't include, by the way, indirect taxes, or superannuation guarantee charges.

So if you've got a small business operator, or a DPN liability, you can't apply for serious financial hardship for those. There is no general power. It's a specific one for income tax.

And also, there can't be any outstanding claims for compensational damages which have been sought against the ATO, such as for a maladministration, or something like that. They have to be finalised first.

Now, GIC remission requests, I've mentioned a bit already, but effectively, the taxpayer can try to request complete remission of the interest charges, on the basis of their special circumstances. Now, doing that late in the piece will actually have two sort of effects. Firstly, there's the prospect that the ATO will agree to remit, in whole or in part, which reduces the total liability.

Now, the preconditions have to be met, and this isn't a session on GIC remissions, but effectively, people can argue that the delay in payment wasn't their fault, or if it was fault, their fault, in one sense, it was fair and reasonable to remit where the person's taken reasonable steps to mitigate, or has mitigated the effects of the circumstances that led to the delay in payment.

Now, remission of GIC is a discretion. It's a reviewable discretion in the ADJR sense, but not always that great a thing to seek, because you can be up for costs in ADJR, as we'll talk about in a moment. There's a Practise Statement on this, which people should read, or indeed, watch the presentation we did on these issues.

Payment plans, you can request a payment plan, and negotiate with the ATO, and this is effectively the process people are probably reasonably familiar with, based upon the audience, but it's important to get the evidence right. And if you are trying to do it at the late stage of pre-insolvency, the ATO is going to take a harder look at it than otherwise would be the case.

Having all this documentation in train, in a short period of time, is going to be difficult. So the ATO may not be willing to take a payment plan at that late stage.

If it's a possible, going through a personal insolvency agreement process might be a better option for an individual, or a data company arrangement sort of structure, for a company, but covering the same sorts of issues as this does, anyway. Now, security, of course, is an important factor in these cases, to maybe even make it a precondition for the ATO to agree to a payment plan.

Voluntary offered securities or personal guarantees are another way of trying to forestall the ATO taking that final collection action. But you've got to remember that personal guarantees, I believe, what would otherwise be personal guarantees for a company's debts, or personal guarantees offered by a third party for the taxpayer's debts, open up the person who offers the securities assets to be effectively captured by the ATO, if the taxpayer doesn't pay the liabilities under a payment plan or offer.

And the realisation costs are borne by the taxpayer, and there's obviously going to be a whole bunch of lower values for a forced sale, as we talked about earlier. Now, personal guarantees, as I said, are bad, in one sense.

So anybody contemplating a personal guarantee I strongly suggest should be getting legal advice, that says that they've either received it, legal advice, in the personal guarantee form the ATO uses, or that they have declined to do so. But I think everybody must get one, because of the fact that if they don't get legal advice, they can be wandering into a situation where they just don't realise that Mum or Dad might lose their house.

Or the spouse of the company shareholder might lose their house, because they're offering that personal guarantee over their asset. Or indeed, they themselves could be bankrupted, if they've offered a personal guarantee that is actually a general guarantee, as opposed to a security over a particular asset.

Now, compromises is the last major issue I want to talk about, in terms of this presentation. Now, compromise is a bit like a data company arrangement, or a personal insolvency agreement, or indeed, a Section 73 arrangement to compromise.

It's effectively the ATO negotiating to accept a lesser amount in the circumstances of the taxpayer. Now, the ATO will only look at the balance left, after every other power has been considered.

So this is truly your last ditch. I say, normally, if you've got income tax debt, you go serious hardship relief before you do compromise, but sometimes, you go straight there.

I've had one case where we actually put a compromise in, and then, the ATO came back and said, "Well, why don't we compromise the majority, but we'll do the relief for serious hardship first, before we apply the [inaudible 00:52:18] to the residue?" I said, "If you want to do that, that's fine."

Now, all disputes have to be decided before you can get to the compromise option. The compromise power is again, set out in the Practise Statement, and there's some issues with how it actually works, but it's a power that's not used as widely as people might expect. But it is used in appropriate cases, in some circumstances, so there are some issues that people should consider with pursuing a compromise offer.

Now, the conclusion I would have in these matters is that it's better to engage early, and engage often with the ATO. Leaving it until the last moment, the eleventh hour, or at a minute before midnight, is not the best way to avoid becoming insolvent, and being either bankrupted or liquidated.

Now, if you find you've got a client that's in that situation, though, that's the time that you really need to get your skates on, and engage with the ATO as quickly as possible. Now, that engagement has to then explain to the ATO person in Litigation and Legal Services, dealing with the insolvency proceeding, why the delay occurred, in actioning it so far, and how the taxpayer intends to deal with the underlying debts. What's the proposal, or the series of steps that they intend to undertake?

If you don't do those things, you will then find that you are really up the creek without the proverbial paddle, I suppose, is the way to frame it. And you have no real leg to stand on in trying to oppose the ATO getting the release they're seeking, which is going to be bankrupting the individual, or liquidating the company.

Now, if you do need assistance with these sort of cases, and if it's in litigation, by the way, you should be helping the taxpayer to get legal representation, rather than having them turn up by themselves. Because they can turn up by themselves, but they'll usually fail that.

And of course, tax agents can't appear in court, unless they're holding a Practising Certificate. So these are matters which should involve tax lawyers to provide that assistance, in understanding what all of these options mean. But helping people to represent themselves, you need to give them the ammunition, but they still need to be able to fire their bullets.

Now, there's a bunch of source links at the end of this presentation which take you to material on all of the things we've talked about. So when you actually have time, feel free to have a look at that. But in the meantime, we might open up for questions. Susannah?

CCH Learning:

Thank you very much for that presentation, Bruce. We will be spending the next few minutes taking questions, so please, just a reminder, to please type them into the Questions pane. To give you some time to type up those questions, I will mention our upcoming webinars.

I'll just change the slide, so everyone can see them. Coming up on the 18th of June, we have, Building a Resilient Brain With Mindfulness.

On the 19th, we'll be looking at Equalising Spouse Super Balances. On the 20th, we start our carbon accounting, with Setting the Organisational and Operational boundaries.

On the 25th, we're going to be Reading the Deed: Effective Trustee Resolutions. And on the 25th, we have our monthly Tax Technical Update for June. Also, on the 26th, we have Section 8-1 General Deductions.

Simple, isn't it? If you're interested in those, or any of our sessions, please head to our website, have a look, and see what is right for you. So let's have a little look and see if we have any questions today.

I have a question from Sarah. Sarah is asking, "Why has the ATO hardened their approach to collection cases?"

Bruce Collins:

Okay, well, I think there's three reasons, the way I'd categorise it. One is that the debt amounts that are owed have increased. And the ATO has an obligation, under the legislative framework for government, to manage the debts which are payable to the Commonwealth. So they're required by statute to actually manage the debt pool, and because it's risen, they've had to harden their approach accordingly.

Secondly, government has funded the ATO with additional money to undertake increased collection activities, to address the growing debt, and to raise money for government coffers, given that we're still suffering with a bunch of government debt, that what needs to be paid off over time.

The third reason, though, I think, actually has to do with that maintenance of voluntary compliance or willing participation that I opened up with. If the ATO did not take action to properly manage the debt pools, the people that do pay voluntarily would actually have a disincentive to continue to do so.

In other words, if the ATO is not taking the appropriate action, and is seen not to be taking the appropriate action to collect debt, then community confidence will be eroded, and voluntary compliance or willing participation will reduce. So they've got an obligation, legislatively, they've been given extra money, but they're also, I think, just doing what would be wise to keep the system ticking over in a healthy fashion. But they are definitely taking that harder edge, in our observation.

CCH Learning:

Thank you very much for that, Bruce, and I hope that helps you with your question there, Sarah.

I had a question from Michael. Michael was asking, "How can an advisor know if there are sufficient grounds for an objection, if they are engaged late in the piece, like just before insolvency?"

Bruce Collins:

That's a really good question. Because essentially, if you're only engaged at the eleventh hour, it's going to be hard to work out what the grounds for an objection might be. If there's an ATO initiating document for, say the assessments, if they're ATO-created, then getting a copy of the reasons for decision, and having a look at it is probably a really good start. That's what we do.

If it's self-assessed liabilities, then there's probably not a lot of prospect of there being grounds for objection, unless the taxpayer has discovered, subsequently, some drastically different circumstance that they weren't aware of. I have seen cases where they've discovered embezzlement at the last moment, which meant that amounts that they thought were being received as income, or as receipts for GST, were actually not paid to them because they were stolen. And that's a ground that stands independently of the previous self-assessments that might have been filed by the taxpayer.

Also, there's carryback loss issues for income tax, as well. So there might be some circumstances where there'll be grounds that are in addition to whatever the ATO might have already done, but mostly, it'll be based upon what the ATO has said in audit adjustments, where you have grounds to object.

So referring to the accounts, and trying to work out whether they were self-assessed liabilities, or liabilities that arose because of ATO audit action, would be my first port of call, and then, to analyse any such ATO documents which are available. Now, sometimes, if you've been engaged late in the piece, you can ask for an adjournment to allow you to ask the ATO for copies of any such documents.

Because I've seen cases where, say, the taxpayer doesn't have a copy of the Director Penalty Notice, or the taxpayer doesn't have a copy of the audit adjustments. Therefore, in order to be able to do that, or the objection decision, in order to be able to analyse that, the advisor needs more time.

But again, those would be cases where there'll be a lawyer involved, or the taxpayer will be having to explain to the court themselves, if they're self-represented, that they need more time to address that issue, and the ATO are likely to oppose those, which is why having a tax lawyer involved is a good idea in such circumstances, to be able to argue more persuasively, based upon a knowledge of what the issues are likely to be.

But tax agents might be able to find out about the objection issues pretty easily by looking at the ATO documents, if they can get access via the portal, once they're appointed. Tax lawyers like me, I don't have access to the portal, so I have to ask the taxpayer to give it to me, or ask their tax agent to give it to me, or ask the ATO to give it to me. So in any of those cases, it becomes a bit more time-consuming.

CCH Learning:

Thank you very much for that, Bruce. I hope that helps you there. Michael.

I had a question from David. David was asking, "What are the biggest risks for directors regarding DPNs, in cases where the companies are in pre-insolvency litigation?"

Bruce Collins:

Well, I think that, again, that's a good question. Because essentially, if the company goes into liquidation, then the director will lose control of the ability to challenge the underlying liability, or indeed, other liabilities that could actually cause that liability to be paid. That means that they've got a real incentive to try to progress that objection as quickly as possible, and to use the making of that objection as grounds to say there's a genuine dispute on the underlying liability, to prevent the company being placed into liquidation.

Now, that can be done if you can get a liquidator who's going to be appointed. They can agree in advance to pursue the objection, and if the director is willing to indemnify them, that can still work. But if the company's paced into liquidation without such an arrangement in place, it's not certain, but quite likely, that the liquidator won't choose to pursue the relevant dispute.

If they don't, then there's only the DPN defences available to the director, and those DPN defences are pretty hard to reach. Whereas, an objection, you require the grounds and the supporting evidence.

And again, once the company's placed into liquidation, some of that evidence becomes harder to get, as well as the grounds not being pursued by the liquidator. So it can actually become quite difficult to pursue, if the company goes into liquidation, so there's a real incentive to try and pursue things earlier.

And DPNs, in that sense, one of the defences against a DPN is to place the company into liquidation, if it's a non-lockdown transaction. That protects the taxpayer. You've got a mixture of lockdown and non-lockdown DPNs.

What you can find is that the other relevant liability that's a lockdown DPN, won't be defeated or defended against by placing the company into liquidation. That liability continues, so there's a bit of a swing and a roundabout here.

If you try and place the company into liquidation administration, or a small business restructure, in order to address the non-lockdown amounts, you'll then be leaving yourself vulnerable for not being able to dispute the lockdown amounts. So trying to deal with it before doing that can be a judgement as to which is the best play.

Again, seeking expert advice in those cases can be a really good idea, by calling somebody like our firm, to talk about what might be the best options, because there are time limits. You've got 21 days to put the company into some form of insolvency management for them, non-lockdown amounts.

But then you've got to factor in what the prospects of success for an objection are on the lockdown amounts, to work out which one's better. Hope that helps.

CCH Learning:

Thank you very much for that Bruce. So I do hope that helps you there, David.

Well, that does bring us to the end of our questions for today, but if you do have further questions, Bruce's details are there on the screen, so please, feel free to reach out.

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 shortly after today's session, you will be e-mailed when enrolled into the E-Learning Recording, which can be watched multiple times, and you'll have access to the PowerPoint, transcript, and a CPD Certificate.

I would very much like to thank Bruce for the session today, and to you, the audience, for joining us. We 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, [inaudible 01:05:44].