Update on Handling ATO Debt Strategies 15/05/2024

CCH Learning:

Hello everybody and welcome to today's webinar, an Update on Handling ATO Debt Strategies. I'm Susannah Gynther from Wolters Kluwer CCH Learning and I will be your moderator for today.

A few quick pointers before we get started. If you're having sound problems and can 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 on your GoToWebinar panel. And shortly after the session, you will receive an email letting you know that the 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.

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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 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 hand you over to Bruce to commence today's presentation.

Bruce Collins:

Okay, so hopefully everyone can see my screen at the moment. So today, we'll be talking about the ATO's focus on small business and private wealth debt collection strategies. It's an important area for practitioners because of the fact that there are so many cases which the ATO's actioning at the moment and the ways in which they're actioning have changed. So, we'll talk about the ATO's statutory powers to collect debts and the framework that supports those powers. And we'll also talk about the ATO as a general creditor, using the powers that every creditor has to pursue their debts, because they intersect and overlap. But remembering that the commissioner of taxation has a strategic advantage built in, baked in if you like, to the tax system, and we'll see how that applies.

Now, there's been quite a lot of scrutiny, a review, and our stakeholder feedback process is happening. So, we'll talk about what they're finding and what comments have been made in areas that are maybe hotspots that are reflected in those items of feedback and those concerns about the ATO's debt collection strategies.

And we'll talk about strategies in response to the ATO strategies about how to better manage engagement with the ATO on the management of taxpayer related debts, particularly those affecting small businesses and private groups, because as I said, there's a lot of activity happening there and the ATO has changed the ways in which they're doing it in a number of different ways.

So, before we start, it's always a good idea to understand the audience, and I know people who have been to any of my sessions, will probably be getting a bit bored with this question, but we just want to know whether you're an accountant, or a lawyer, a financial planner, a student, or in the eponymous other category.

So, turning back to Susannah to just run that poll quickly.

CCH Learning:

Certainly. So, I'll just launch that poll, and if you could please put a click into the radio button next to the answer that best describes you, that would be really great. And just a reminder, of course, if you do have any questions throughout the session, please put them into the questions pane and we will get to those questions in the Q&A at the end of the session.

So, I'll just give you about five more seconds to get those votes in.

Thank you very much. So, we're going to close the vote and have a little look. Okay, so 95% of our audience is an accountant or a tax agent, with 5% being lawyers.

Back to you, Bruce.

Bruce Collins:

Thanks for that Susannah. And then, there's another poll as well, just asking whether people are in private practise with experience in tax-related debts, or in private practise with no such experience in tax-related debts, or in public practise, including at the ATO. Couple of sessions lately we've had almost a majority of people from the ATO, which just allows us to tailor the [inaudible 00:05:58]. And if people have had a lot of experience, it's nice to know that that is the case. And if they've got no experience, we can tailor it according to that as well. So, if you're in private practise with experience in ATO debt, in private practise with no experience, in public practise, or again the other category. Back to you Susannah.

CCH Learning:

Thank you, Bruce. So, I'm just launching that again. So again, please put a click into the radio button which best describes your situation.

And once again, a reminder, if you do have any questions today, 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 give you five more seconds to get those votes in.

Thank you very much. I'm going to close and let's have a little look at the answers. So, we have 60% who are in private practise with experience, we have 24% in private practise with no experience, and 16% in public practise. Thank you very much.

Back to you Bruce.

Bruce Collins:

Okay, thanks very much for that. It gives me the opportunity to sort of tailor things I'll say to cover the audience. Much appreciated.

Now, the ATO's obligation to collect debt is set out in the public service management framework, Public Governance and Performance Accountability Act. So, the idea is that the commissioner as an agency head is required to gather tax debts and to collect money for government, which is a pretty obvious thing, but it's always nice to focus on it. Now, part of that strategic ownership of the debt system is to monitor what's happening with the debt book owed by the ATO, or the series of debt books and the composition of those debts over time. So, between 2019, 2023, collectible tax debt rose from 2.65 billion to 50.2 billion. That's a big increase.

Now, collectible debt for businesses accounts for 90% of that, not surprisingly, because most of the assessments raised are actually for businesses, are the ones which aren't paid by withholding. For individuals, most of the money that comes in for individuals is coming in through the withholding system. So, the composition of the total collectible debt at the moment is small to medium enterprises, unpaid activity statement debt of about 23 billion. And SMEs, unpaid superannuation guarantee debts of 1.8 billion.

But the government has given the ATO extra money to pursue small business and private group debts. And so, not surprisingly, you get ATO spokespeople like Vivek Chaudry, the Deputy Commissioner of Taxation for Lodgement and Payment. He gave a speech last year in relation to the ATO's return to stronger debt collection approaches.

When they talk about stronger, it's actually about a combination of more activity, and it's also a combination of the use of their powers more firmly. And we'll talk about what a firmer action strategy looks like, which is a terminology the ATO sometimes uses. And the ATO is aiming to create a more level playing field between businesses that comply with their lodgement and payment obligations and those that don't. So, those who aren't paying their debts on time are effectively using the tax officers, either a bank or they're actually trying to evade payment at all. So, delaying payment is one thing, but permanently stopping payment is another entirely.

So, the aim of the ATO's management of their debt is always to focus on a combination of the current liabilities being paid and then to have work done to rehabilitate the taxpayer, to get them back to where they should have been on their past debts. So, the idea of most payment plans is to try to raise the liabilities from the taxpayers progressively, but then to collect everything within the last cycle.

So, if it's a quarterly obligation, like [inaudible 00:10:19] activity statement, liabilities, they want to make sure the people are effectively back, are on deck within the payment period of 90 days. And if it's an income tax cycle, then they're aiming for 12 months. Now, that can actually be very hard for businesses to do if they've had an adverse event, that means that they suddenly can't pay their debt. They often can't pay it within a month or two, so that can be difficult for them. And the ATO's view on that, according to what Vivek said, was to effectively argue that some businesses need to stop trading if they can't pay their liabilities, rather than allowing them to accumulate more liabilities over time that don't get paid. So, that snowball is rolling down the hill and gathering more and more debt. They want to make sure that that's not happening, so they try to take action more promptly as a result.

Now, the COVID period isn't mentioned here, but it's worth mentioning. The ATO took its foot off the accelerator pretty much entirely. In fact, put the brakes on to a large degree during COVID. And from 2022 onwards, they put their foot back on the accelerator and they've been gathering momentum since then and they've been trying to catch up on the amounts of liabilities that were sitting in the debt books, which as it's talked about here, has risen quite significantly. So, it's now actually a question of how firm they're being and what they're doing in those strategies, which we'll talk about next.

Now, the current focus areas for the ATO according to their public statements are on unpaid super guarantee. And the super guarantee amounts are effectively a replicate of the obligation to pay super on behalf of the employees. The ATO regards super guarantee as effectively trust monies that have been taken from the employee's entitlements, which had to be paid to the superannuation fund of the relevant employee, and haven't been. It shouldn't be viewed by businesses as being a buffer or a sort of cash flow working capital amount that they can keep and use.

So, the ATO is taking increasingly firm actions against employers in respect of those things, including some of the tools we'll talk about in more detail later, like garnishees, directions to pay, director penalty notices, and the disclosure of tax debts to taxpayers. And in some cases, prosecution action. For instance, for non-compliance with the direction to pay or in relation to other types of misconduct that are associated with those unpaid superannuation guarantees, like phoenix conduct and things like that.

There's also been, as a concomitant sort of issue arising from the ATO's extra money to do the reviews under the private wealth programmes, the Top 500 and the Next 5,000, and their other compliance work through the Tax Avoidance Taskforce and the Serious Financial Crime Taskforce and things like that. They've been raising a lot of liabilities against entities as a result of review and audit action.

Now, there's a priority on the part of the ATO for those debts to be pursued more quickly and more firmly than they were previously. I had a couple of clients just in the last week, both of whom had had assessments raised against them as a result of ATO audit action, which was done covertly. They were getting debt collection calls within two weeks of the assessments issuing, before they were actually due and payable, and looking to see about payment arrangements or checking to see when the amounts would be paid. Of course, we're lodging objections and that'll make the debts disputed, and therefore, affecting what action the ATO is likely to take. But that shows a change in tone. That would've been regarded as unusual before COVID, during COVID unheard of, and now it's more routine for significant debts in the millions. So, there's a lot of that sort of follow-up back there.

Now, the next category is refund fraud, and anybody who gets involved in a case that involves refund fraud should expect a very rough ride from the ATO, whether it's about operation protocol, the GST fraud case, or it's another form of identity fraud. Anybody who's trying to get refunds by fraudulent conduct is going to expect to get the strongest possible use of ATO debt collection powers, both in terms of the statutory powers we'll talk about as well as the commissioner's general powers as creditor and the associated powers that apply for criminal investigations like proceeds of crime action and things like freezing orders are being applied. Added to that is something called a departure prohibition order, where if somebody is subject to a tax related liability, they can have their ability to depart the country prohibited. And those powers mean that when you get to the airport you discover that your passport flags a red sort of flashing light and suddenly federal police officers descend upon you and tell you you're not allowed to leave. And that's not a great experience for people who are maybe not aware of that DPO being issued.

Controversially, the ATO is also focusing very significantly on aged debts. Now, there's a four-year programme focusing on public and multinational groups and privately owned groups with debts over 100K, but also debts for those categories that are overdue for more than two years, even if they're not above 100K. Now, those debts are being pursued through a variety of firmer action strategies, and the types, we'll talk about during this presentation. So, it's worth recognising that those amounts will be pursued.

Now, that overlaps with the criticism we'll talk about later about the robotax programme, as it was dubbed by the media, wanting to draw a correlation, maybe a false correlation between what was happening and the Robodebt scandal. But the important thing is that those aged debts can be ones that were previously announced to be what used to be called sometimes colloquially written off. That actually meant that they were regarded as being uneconomical to pursue at a point in time. And the ATO, under the PGPA, is obligated to revisit that periodically.

And I note that there's a greater discretion being discussed now after the budget announcements around whether the commissioner should have greater powers to decide on what to do with some debts, to have a discretion about it greater than the ones that were previously provided under the tax act, Tax Admin Acts in particular, but also affecting the interaction with that PGPA, which tells the commissioner as an agency what he's supposed to do under the public sector management framework.

Now, the other area is around supervising employers with new self-assessed tax debts. Now, one of the things we'll talk about with director penalty notices is there's two sorts of director penalty notices. One of them relates to unreported debts, where their reporting is either not done at all or it's more than 90 days late. So, the idea here is that the ATO is now taking swifter action and applying firmer action strategies to those employers who self-assess but don't actually pay. They used to get a lower priority in a sense because they were reported and they just accumulate. Now, they're trying to deal with it on a more broad basis, by focusing more strongly on those issues, including applying interest and notifying people of interest and implying penalties where applicable.

And there's no idea that payment plans are really in place for genuinely deserving taxpayers rather than being agreed with every employer that asks. And it's there for people who genuinely need financial support rather than to allow the tax system to be a sort of unregulated banking facility for people to use. And one of the things that the government's announced controversially, again, is the idea that GIC and SIC won't be deductible in future years, from 2025 onwards. So, that's actually going to change the landscape quite a bit because I would always say that you shouldn't be paying GIC because of the fact that it's at a high rate. And you shouldn't be paying GIC because it's not only at a high rate, you can't claim it as a tax deduction, which is I think a real change of significant concern.

Now, the ATO has got a range of debt collection powers we'll talk about. Now, some of these are powers that everybody has, the legal action ones in particular, except for the disclosure of tax related business debts. But the idea is that all of these are intended as a combination of carrot and stick, mostly stick in this place. But the idea is that the encouragement of the carrot is that you don't get subject to these if you pay. You don't get subject to as many of these if you have a payment plan. But otherwise, you're going to be hit with the debt stick pretty hard over time.

Now, the initial actions the ATO takes include the imposition of general interest charge on most liabilities. And the general interest charge, as we'll talk about in a moment, is imposed under statute. Then you've got the fact that if you have a credit or refund amount due to you and you've got another tax related liability for some other head of revenue, then the credit allocation rules mean that before you can get your cash, it has to be allocated to the other liabilities, the earliest period liability and the interest charges associated with that early period liability. So, effectively, that means that you won't get any refund while you've got another liability owing, including ones, by the way, that might be disputed. Now, there is a discretion that the commissioner has to be able to provide that refund anyway, but it's rarely utilised and it's regarded as quite a high standard to reach to convince them to make any such decision.

The other thing the ATO can do, as any creditor can do, is they can refer the debts owed to a debt collection agency to act as either a factor or an agent for the collection of the debts. Factoring is if the book of debts is sold to the debt factorer. So, they buy it at a discount effectively, and anything they collect is applied to that. It doesn't tend to happen very much for the tax office, but the debt collection agency acting to collect on the commission's behalf is not uncommon, as we'll talk about. There are differences in how that might play out and perceptions as to what's happening, which contribute to concerns by the community about how that works.

But the firmer action strategies of garnishee notices, DPNs directions to pay, and security bond deposits, which we'll talk about in later slides, and you've got the disclosure of business tax debts if they're more than 100K. I've got to say that in part that particular power is something that might be partly my fault, as I was in the ATO, in charge of the phoenix strategy, and that was one of the recommendations of one of the phoenix reviews into which the ATO had extensive input. But obviously, it was decision government as to what they did.

Now, the disclosure of business tax debts can have a major impact on a business because of the fact that their creditors, their trade creditors will then become aware of things and their financiers will become aware of the liability if they weren't already told. And so, that can lead to sustainability questions and changes to terms of trade.

Now, the legal actions of course include the disclosure of those business tax debts, but they also include bankruptcy notices, creditor's petitions, statutory demands, and winding up action, which are available to all creditors. And the ATO is effectively the largest petitioning creditor for both individuals and businesses in the country. So, as a rule, and despite them saying they're not a big part of the debt system, they are a huge part of the debt system. And so, there's a lot of issues that flow from there.

Now, the initial actions, as I talked about with GIC, it's proposed automatically by the ATO's system. So, it's calculated automatically. But it can be remitted, and sometimes there are manual calculations and sometimes very hard for the tax office to work out what's happening with manual calculations and how they're being treated. We've had cases where it's taken 11 gos for the tax office to be able to tell us what the actual GIC amounts were on the accounts and why they were calculated the way they were, because of manual calculations being done, because of peculiarities in the accounts, the underlying liabilities.

As I mentioned earlier, the credits or refunds are required by law to be allocated to those earliest tax debts, including the interest charges. And the debt collection agencies will be out there acting on behalf of the ATO as well as the ATO lodge and pay call centres. The outbound call centres will be doing outbound phone calls and other contacts with taxpayers. And where there's an external debt collection agency, that can be a bit awkward because if you're contacting the tax office, they share information with the debt collection agencies but not in real time, in a sense. So, you can actually be trying to engage with the tax office on a payment plan or something and then you'll get a call from a debt collection agency that doesn't know about that. I've heard of that happening. RecoveriesCorp is one of the ones on the panel, and I think that's the one that the ATO is using at the moment.

Now, the garnishee notice is a peculiar power that people might be familiar with, but it's an incredibly onerous power. The commissioner effectively has an assessment on foot for some liability, and then the commissioner has the power to garnishee some other entity to pay an amount which may be payable to the entity whose tax-related liability has been assessed. And that can be financial institutions holding bank accounts. It can be the purchaser for a property that's being sold where the vendor is the taxpayer. It can be trade debtors who are trading with the business entity who owes the tax-related liability. And it can also be associated entities who may have transactions with that particular group entity.

So, I've seen instances where every entity in a corporate group have been hit with garnishees about prohibiting any payments being made to any of the entities within their group, without the money instead being directed to the commissioner. Sometimes, most frequently, there'll be a percentage sort of amount set rather than being the whole amount for trade debtor transactions or financial institutions, but not always. I've seen amounts just hooted up by the commissioner from the bank accounts of taxpayers.

Now, it's a statutory power that the commissioner has. So, he doesn't need to go to court. The commissioner can just have his staff issue a garnishee. Now, it has to say who the entity is that the liability rests with and how much they owe. The person who receives it has to be a person that the commissioner has reason to believe holds the money, and that they have authority from some other entity to pay the money to the debtor. And if you don't comply with the garnishee, then it's an offence. So, you can actually be prosecuted for it and you can be fined as a result.

Now, one interesting issue which isn't on the slide, is that a garnishee notice survives insolvency. So, if the commissioner issues a garnishee notice against a company and the company becomes insolvent, garnishee notice still applies in preference to other creditors, and same thing happens with bankruptcies. So, rather than the waterfall of insolvency arising and everything then going to all creditors, you can still have a situation where some money goes preferentially to the commissioner. Seen cases where that's happened with employment income, where the employer has been garnisheed in respect of an employee who then goes bankrupt, and the commissioner continues to take money from the garnishee transaction while the person stays with that employer. And in cases like that, the employee has the option to move after insolvency to a new employer, and the commissioner can't reissue a new garnishee, but it's still a bane on the insolvency system and it does give the commissioner preference over other creditors in a way which I think is contrary to policy, but it's the way that the law is interpreted at the moment.

Director penalty notices also exist as a tool. Now, director penalty notice is a surrogate for the liability of the company for one of a few heads of revenue. Pay as you go withholding, GST in more recent years, which has accrued superannuation guarantee charges, and as an adjunct to the goods and services tax, the wine equalisation tax and luxury car tax liabilities. All the directors can get a DPN, and a DPN can be issued for any period that the director was a director while the liability arose or any subsequent period after 28 days when the amount remains unpaid from a previous period. So, it's a good idea if you're going to become a director or your client's contemplating being a director or there's a change of directors, to advise them that they need to check whether there are liabilities subject to a DPN before they accept the appointment. Otherwise, they can end up, as some of our clients have had the experience of going through. That effectively, they become a director and then become liable for the debts for the previous directors failures to actually pay.

Now, the personal liability only accrues when the DPN crystallises, but there are defences against them which arise, but they are difficult to reach. So, DPNs are a bane on being a director. They're actually an incredibly powerful tool that pierces the corporate veil, and they create real problems as a result.

Now, firmer action directions to pay SGC is effectively a notice from the commissioner directing that payment occur. Failing to make the payment is actually a prosecutable offence, with 50 penalty units or imprisonment for 12 months, or both. So, here you've got a direction notice to the employer entity, it's the company, but of course, if the employer is an individual, that means they're directly liable. If they're corporately liable, then the penalty units are, of course, increased because they're higher for a company rather than individual.

So, this can, again, be quite a powerful tool, and the commissioner is are using this tool increasingly to deal with those categories of previously unreported SGC liabilities and also increasingly for reported liabilities that remain outstanding for a longer period.

Security bond deposit is something you won't see very often, but is increasingly, from what I hear, being used. I've seen clients subject to SBDs before, but apparently, the commissioner is using them more frequently at the moment, but it's effectively a power for the commissioner to say, "I believe there will be a liability owed and I'm going to require the entity that owes that or will owe that liability rather to provide security for the payment of that liability." And a couple of the cases involved in the reports to date have included a discretionary trust which has a prohibition in its trust deed from not distributing its taxable income according to the net income of the trust estate calculation, and effectively requiring that trustee to provide a security for an amount which would be assessed against the trustee, which again doesn't make sense, because the trustee is prohibited from actually... Are being left holding a relevant amount of taxable income which isn't distributed to a beneficiary, either express beneficiaries under the discretion or default beneficiaries in the lieu of that discretion not being exercised or failing.

So, there's limited power to review it. And the cases that have been viewed so far have all gone the commissioner's way, and as I said, including ones that I don't think should have, with all due respect to the judges in question making the decision. It seems as if the test under the ADJR, the process review standard there is such that the commissioner is again having the benefit of saying he's got reason to believe, and unless the reasons to believe meet one of the failures for administrative law purposes, like not taking into account reasonable and relevant considerations, or acting unreasonably, those sorts of things, unless you can show that that's happened as overt bias, then the taxpayer is simply going to be assessed on what the commissioner thinks is reasonable. And therefore, the idea is that the security will be therefore payable, which is, I think onerous.

Now, the disclosure of tax related debts I talked about a bit earlier, but it can be only done where there's an ABN, so it has to be business operating. The outstanding debt has to be more than 100K, and it's been overdue for more than 90 days. So, payment arrangements are actually important. So, the ATO shouldn't report one that has a payment plan, but the problem is if you negotiating a payment plan and you don't make what the commissioner regards as an appropriate offer, they can still refer you. And once you're on the credit reporting bureau list, that it's a historical list, so even if the commissioner says, "Okay, we've now got a payment plan subsequently," the report's still there and it still adversely affects the creditability of the business. And therefore, can also affect their financier's willingness to lend and their trade creditor's ability to actually go through that. And of course, there's an exclusion for hardship applications, but hardship only applies to income tax for individuals. So, I don't think it's really going to be much use for most businesses.

Now, the legal actions part of the equation is of course where people go to court or threaten going to court. Now, if somebody is subject to an ATO statement of claim, that is actually automatically disclosed to the credit reporting bureau. So, even though it's not reported by the commissioner, the amount is actually on public record and can be accessed by those credit reporting bureaus.

Now, if there's a judgement interest amount that's owed, it'll be regarded effectively as a penalty. So, it creates a problem with tax deductibility, but it's also a problem with this amount being known to be on the record for the business's sustainability over time.

Now, bankruptcy notices follow judgement having been obtained against an individual. And after receiving a notice, that taxpayer has 21 days to actually pay or agree to a payment plan. If not, then the ATO can file a creditor's petition, a sequestration order petition to make the taxpayer bankrupt. Now, that can be opposed if you've got a genuine dispute on foot. The ATO doesn't like you raising genuine disputes late in the piece, but you can still try. And if you have a client in that situation, it's a good idea to get legal advice to actually pursue that.

You'll need legal representation as soon as it's in court anyway, unless people want to try and represent themselves, which is a difficult task for the illegally and uninitiated.

You've got creditor's petitions which are actually done obviously through the process to get that sequestration order for individuals. And the parallel process for a company is the statutory demand process, where the company gets a statutory demand, again, requiring payment within 21 days or the negotiation of a payment plan. And after that 21 days, then the ATO as a creditor can actually seek winding up action by applying for a creditor's petition for winding up. And a liquidator has to accept the gig as being consenting to act as the liquidator of the company in that case. And generally, that will involve selling off the assets to pay the company's creditors. It can very rarely result in a deed of company arrangement being agreed, but the usual is simply to take in the assets of the business and sell them to pay the creditors a dividend. And shareholders, while they might be creditors, they're usually at the end of that queue.

Now, the feedback at the moment on the ATO's debt collection approaches and government debt collection in general includes a report released a few weeks ago by the Commonwealth Ombudsman, the ACT Ombudsman, the Inspector General of Taxation and Tax Ombudsman, which is a guide on how government should notify people about their debts. So, the idea is that it should notify why the debt is arisen, being transparent and accountable. That's transparent and accountable, by the way, not transparent and accountant. Apologies for that typo.

The what should actually say what the debt is and how it arose. It should provide clear information for requesting review or waiver of the debt and also for negotiating payment arrangements. It should provide help for people to get more information or deal with their issues. And the cycle should be that the government agency in question should learn from their feedback and experience and improve their processes to better address the why, what, and how, and the provision of help to people affected by their debt collection powers. It's common sense, but it is actually very salient for what the ATO does, and I think there's still some lessons that the ATO can learn to improve their management of the system. Some of the things we've talked about.

Now, the strategies to better deal with the ATO in terms of managing debts is that it's better to communicate with the ATO about a debt as it arises and as it's being pursued. As early as possible is better, but whenever it becomes relevant is what's required. If the ATO doesn't feel you're engaging effectively with them, then they'll go firmer action more quickly and debts will be then subject to things like credit reporting bureau referrals and other firmer action strategies along the way.

Now, it's also important to recognise if you've got a debt which is accruing, where that you know that the client's going to have to pay, it'd be a really good idea for the ATO to be engaged with as soon as the debt arises. Now, as I mentioned earlier, for some types of audit related liabilities that have been raised, the ATO might be proactive, but for others that are self-assessed, they may not be. So, getting on the front foot can help to mitigate the issues with GIC accruing and enable payment plans to be in place right from the start.

Now, there are some challenges with payments plans, as we'll talk about in a moment, but effectively, it's an issue where you need to stay current on all of your lodgements and the ATO won't entertain a payment plan until someone's up-to-date with their lodgements, and that all future liabilities need to be paid as they're emerging rather than gathering up the snowball rolling down the hill, or amount of liabilities. So, you'll be in default of a payment plan if you don't meet a current lodgement or pay a currently accruing debt.

Now, there's the compromise of debt option that is an important one in the system, that needs to be considered, but it's sort of like the line of last resort. It's like the attempt to deal with the issue by offering the commissioner a lump sum payment rather than them going through the insolvency process, particularly for individuals subject to bankruptcy, but also at times for small businesses run through entities in some circumstances.

Now, there is a request for release for serious hardship, but it really only applies to income tax and related penalties and interest. But if you're genuinely unable to pay the amount, and you're an individual, and it's income tax, it's well worth having a go at the release from the tax debt for serious financial hardship. But it's a high standard to meet, and if you've been systemically non-compliant in the past, the ATO will resist that. And the AAT in reviewing such a decision is likely to be critical of those past histories. And of course, there's the question about the small business restructuring, we'll talk about.

Now, payment plans, you really need to have a payment plan in place to pay over time. Anybody can negotiate one. The GIC still accrues and needs to be paid during the life of the payment plan. It can sometimes be, maybe even frequently, may be remitted at the end in part or in whole, but you require convincing evidence of the reasons why the debt arose through circumstances outside the taxpayers control to succeed in GIC remissions in those sort of cases.

Now, I've belated the point about meeting future lodgement and payment obligations. So, I won't do that again, because... And any future tax credits or refunds will be automatically applied under the allocation rules to the paying off of the earlier debts that accrued. If it's under 200K generally speaking, but not always, the payment plan can be set up online or by phone by the taxpayer or tax agent. The exception is, of course, if there's legal action on foot, it's possible that you won't be able to do that because there'll be some sort of stopper on the system. I saw one of those recently.

Now, interest free payment plans are available for first offenders and small businesses for overdue activity statement amounts, but the eligibility requirements are pretty strict.

Now, the compromise of debt, as I talked about, it's a tool of last resort, and the ATO is reluctant to do it organizationally, because it's exercising a power outside of the tax provisions they normally administer. It's actually under the PGPA to do that and only need a certain number of people in the ATO are authorised to agree to compromises. Now, effectively, you're going to have to have gone through a whole bunch of other hoops before you get there, and they won't agree to a compromise if there's any dispute, which is curious, because a disputed debt, I would've thought is still a debt. So, if someone made a compromise offer as part of trying to deal with it, it would be effective as a means of trying to resolve the total dispute. But the commissioner thinks that it has to be a crystallised debt, which is no longer uncertain before he'll exercise that power.

Waiver or release for hardship applications haven't been finalised, or the taxpayer could lodge a Part IX Bankruptcy Act application to similar effect. So, if the person's been made bankrupt or party to a Part IX or a Part X insolvency agreement within the last five years, then again, the commissioner won't agree to compromise. So, for first timers, it's generally worth having a look at, but you have to show that you're genuinely unable to pay, you have to provide a statement of financial position, and you have to do a whole bunch of argumentation to convince the commissioner to go that way.

Now, the small business restructuring processes are still relatively new. It was introduced broadly during COVID as a result of previous recommendations to government, but got off to a bumpy start, but it's actually now got the ball rolling on it, and effectively it's a business that's viable but struggling because of temporary circumstances. So, the restructuring process involves insolvency practitioner taking a gig, so the practitioner then is engaged and they work with the directors to come up with a plan to put to creditors within 20 days notionally. That's more of a bade within aspiration than always occurring. And then after that, the creditors have the option within 15 days to vote approving or rejecting the plan. Now, the plan can undergo for up to three years. So, effectively, it can't go any longer than that, but it may be completed sooner, depending on the terms of the plan.

Now, the comparison here, and this is something the commissioner has to consider in all these cases, is the comparison between what the commissioner would get from insolvency. So, in the case of a company, that's insolvency via liquidation, so what would they get as a dividend after liquidators administration fees for running the liquidation are taken out and looking at obviously what happens after the secured creditors get their payments.

The ability of the company to make the payments, and obviously also the compliance history of the taxpayer and the group entities. So, if the group has been recurrently non-compliant, it's less likely that the creditor being the commissioner will consider what those particular group entities have offered now, which might be built upon a history of having been systemically creating liquidating entities over time.

Now, one of the things that people need to consider in both deciding to liquidate a company or in relation to a small business restructure is the fact that directors and shareholders in the company are likely to have positive balance loan accounts. Positive balance in the sense that the taxpayer in question owes the company money.

Now, that is an asset of the company which can be pursued through the process of liquidation. So, in other words, if you liquidate the company, then the commercial return that's compared here is considering the hypothetical return to liquidation, it also means that the directors might actually, or the shareholders rather, might actually be paying money into the company or pursued by the company's liquidator in respect of those particular liabilities.

Now, the issue here is that those loan account amounts therefore, [inaudible 00:46:15] loan accounts in particular, can suddenly be pursued by somebody in liquidation, and that's a factor that needs to be taken into account in calculating that hypothetical return from such a hypothetical liquidation.

There's also the fact that the creditors need to consider whether there may have been potential breaches of the Corporations Act. And again, that goes towards the liquidator's role to identify and potentially investigate any possible breaches of the obligations of directors under the Corporations Act, including 588G, for trading while insolvent and things like that. So, there might be other remedies available for creditors which they need to consider as an alternative to going through the smallest restructuring process.

Now, what's not on here is actually a slide on another option, which is obviously to put the company into administration and try to achieve a deed of company arrangement. In a sense, it's a similar sort of process to, but less structured, to the small business restructuring option. So, in the case of an administrator, the administrator stands in the shoes of the other company for the purposes of arranging the deed of company arrangement and putting it to the creditors. And there's a process of negotiation with that, where somebody is going to put money in, it may be the company's going to put the money in, but quite routinely, it's one of the shareholders who's putting money in, which wouldn't otherwise be available to the creditors of the company, including the commissioner, if there were to be a liquidation. So, the tipping of extra money can also occur in bankruptcy matters as well, because there's a parallel Part IX arrangement to avoid bankruptcy, where you can sort of make an offer or you can do a personal insolvency agreement under Part X of the Bankruptcy Act.

So, all of these things are effectively trying to make an offer to the commissioner so that the commissioner will accept something which will be less than 100%, which will cause the commissioner to then back off and allow the entity to either avoid bankruptcy if they're an individual or the entity to continue to trade. Now, the nuclear option in all of these cases, if none of those things happen, is that the individual can be made bankrupt and a trustee's appointed. Or the company's placed into liquidation and a liquidator's appointed. In both of those cases, the relevant taxpayer that previously controlled the activities, whether it's the individual who's now bankrupted or the directors of the company that's now liquidated, they lose control of decision making. They no longer have standing to pursue challenges to their underlying liabilities.

So, one thing that happens in relation to these strategies is that if you want to do an objection to a case which is subject to bankruptcy or liquidation, you need the trustee in bankruptcy or the liquidator's agreement to do the actual objection process. So, it's better to do objections before getting to the point of insolvency rather than after, because not always will the trustee in bankruptcy or the liquidator in a company case agree to pursue such an objection. So, their liabilities can't be challenged. And going back to the DPN context, that also creates a particular issue for a company placed into liquidation, where there's a DPN liability because it's no longer possible for the director who's subject to the DPN liability to then cause the company to challenge those liabilities. The underlying liabilities for GST, pay as you go withholding, super guarantee, luxury car tax, or wine equalisation tax.

So, these options which are about trying to avoid those bankruptcy or liquidation have that collateral benefit, that they also allow the challenging of those particular liabilities if that's the appropriate step to take.

But anyway, we might open up the questions now, Susannah, if you like.

CCH Learning:

Thank you very much for that, Bruce. Yes, we will be opening up for questions. I will just take that back. Excellent.

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. Sorry, there, just waiting for my slides to move along there. So, you can see the upcoming webinars. So, we're looking at tax and motor vehicles, including electric vehicles, this afternoon. We're also going to be looking tomorrow at transition to retirement pensions, the 2025 boom, and the traps within. On the 21st of May, we'll have our May tax technical update for the month. And on the 22nd, we're going to be discussing advisory board essentials, the what, why, and how. On the 28th of May, we're going to be looking at those 2024 year-end conversations for all SMSF clients and also looking at agile mindset and mental fitness. If you are interested in these 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 at our questions. Sorry, I'm just going to make this a little bigger so I can see. Okay, see all the questions. So, we had a question here from Stuart. Stuart was asking, "What if you're in a black hole with a client, that is, they are well behind in their lodgement obligations. We know the consequences are going to be an issue after lodgement. How do you deal with the ATO? Their initial response is fines, GIC, and an unhelpful hotline. It can be quite overwhelming."

Bruce Collins:

Look, I acknowledge that's all absolutely true. I think it depends on the size of the group. If they're a larger group and they're in arrears on their lodgements, you can expect the ATO to be taking action more coherently as a result of the Top 500 and Next 5,000 programme for private groups. But there's lots and lots of smaller groups that aren't in that category. Engaging with the ATO collectively can be harder because they deal with smaller groups entity by entity. If you've got a taxpayer that might have maybe one to five entities, probably a self-managed super fund, an employer entity, maybe an asset-owning entity, and maybe an operating entity, and then the individual's concerned, if they're all in arrears, then they're going to have problems engaging with the tax office separately. So, having a coherent strategy to try to get them back on track can be important.

But the risk is that as the liabilities start to hit the ATO systems as you get them lodging the earlier outstandings, both tax return, our lodgements and activity statement lodgements, is that those debts will start to be actioned. And then, once the debts start to be actioned, you might see an uptick in the lodgement enforcement activity as well, as the ATO starts to wake up to the fact that this group is non-compliant. And so, I've seen cases where people were trying to do the right thing, maybe even change tax agents to someone who said, "Well, this is a complete mess. We need to get you back on board," and they've started to lodge the earliest first, and then they start to get hit with harder action strategies from the ATO while they're trying to get back into engage with the system. So, writing to the tax office in that circumstance and requesting escalation can be a really good idea.

If the debts are big enough and the matters are complicated enough, it sometimes also can be a good idea to get external legal assistance from a firm like ours, not just specifically ours, but I mean a firm like ours. Because if it's big enough and significant enough, the ATO's actions will start to get harsher and harsher pretty quickly, and that experience can be adverse to the rehabilitation of the taxpayer and their re-engagement with tax and super system. But as advisors, our job is to try and help people to comply. That involves them getting back on deck with their lodgements and their payment obligations.

I have one client, for instance, who had bought a couple of rental properties and had been paying them off in preference to paying the tax office, hadn't been lodging for a long time. And as a result, they've had to look at refinancing their existing loans and redrawing money so they could pay the huge amounts of tax that they ended up having to pay as a result of meeting their lodgement obligations. And that's helping them to forestall the ATO and making them bankrupt and taking those rental properties in total. The equity that was available under those properties was quite significant because of the preferential repayments that have been made, and the value of the properties had gone up over time while the person was outstanding in their lodgement obligations, outstanding in the sense they weren't outstandingly good, they were outstandingly bad.

So, it can actually cause people to have to refinance things to actually meet those payment obligations, but that can be necessary. And alternatively, maybe it's better they go bankrupt or become, in fact, insolvent as a company and go into liquidation. If they can't pay their debts, ultimately, that's what's going to happen. But if you go to the tax office and engage with them constructively, collectively on a group, you'll have a better chance of arranging things than you will if you're trying to do it piecemeal, and the ATO just starts swinging according to whatever that hits their system from day to day.

CCH Learning:

Thank you for that, Bruce. I do hope that information helps you, Stuart. I have a question from Jono. Jono is asking, "From what date will taxpayers be denied deductions on GIC interest and charges?"

Bruce Collins:

I think that it's the '26 financial year. So, it starts on the 1st of July 2025, is my understanding, but I must admit that I'm going to write an article on that fairly soon, but I haven't gone back and reviewed all of the history of the announcement, but it's a pretty bad thing for the system, in my opinion. I'm actually quite critical of that as an option.

The reason that the ATO would've been in favour of that is probably because of the fact that GIC effectively accruing becomes a liability the person can claim, even if they don't pay it. So, it's a bit like the ATO imposes a penal rate of GIC and it actually reduces the amount of income tax that the client has to pay that year, even if they don't pay it. And therefore, if they remit it later, it becomes an income event, because it's a recruitment of a deductible expense, but it's a weird mismatch. I can understand why they were concerned about it, but I don't think that the solution that they've chosen or government's chosen as a result of whatever representations were made is the right one. So, it's quite a tricky policy issue, but I don't think this is the right reflex to solve it.

CCH Learning:

Thank you for that, Bruce. I hope that helps you there, Jono.

I had a question from Nick. Nick was asking, "Was there a mention of the small business restructuring process?"

Bruce Collins:

I think that question might have come up earlier, because it was like the last slide. So, yes, there was. If you have a look at that slide, it outlines the options. The ASIC website contains quite a useful articulation of how the small business restructure process is supposed to work. And as I mentioned earlier, it was quite clunky when it started, because not a lot of practitioners were prepared to do it for five grand, which was an unrealistic estimate of what was actually on the table. The work that's necessary is not dissimilar to putting the company into administration, for which the normal fee would be somewhere between 30 and 40,000 for a moderate sized entity, and might be as low as 20,000 for a smaller entity, but it's nothing like 5,000.

So, in practise, it seems like the fees for these are more like five to 10 rather than being less than five, which is what the government originally thought would happen for some, no readily apparent reason. But it's actually quite a useful thing. The numbers of those are rising as practitioners and businesses are more across how it works and more willing to do it. We've got a few cases at the moment where they're involved in such restructures and they're constructively engaging through that process with the ATO.

CCH Learning:

Thank you for that, Bruce. And I hope that helps you, Nick.

I also have another question from Jono. Jono was asking, "What is the guidance for taxpayers or companies who have received a statutory demand and wind up actions?"

Bruce Collins:

Okay, well, that's very important. If you get a statutory demand, jump on it straight away. Do not let it run out. Try and engage with the tax office on it. Statutory demand is not actually going to court, but it's the precursor to going to court. So, at that point, I'd suggest lawyering up, going to a firm such as ours or others to get assistance in dealing with it, because after the statutory period elapses, then they can actually apply for a winding up order thereafter, and that takes you to court. And at that point, you'll need an appearance from a legal practitioner to represent the client. It's also important, if you get a statutory demand, to identify what is happening with the underlying liabilities and whether they're challengeable. Sometimes you can find that a statutory demand is based upon estimate assessments for things like pay as you go withholding or super guarantee, and they may be wrong.

They may be duplicating amounts between periods or between entities and a group. They can also be just wrong from the perspective that the people are not employed by that entity at all. They can actually be somewhere else in the chain of transactions, particularly if there's an agency argument applying for either pay go or super guarantee purposes. So, you can have two or three entities all being subject to the same assessments, and then the ATO starts issuing statutory demands to each. And there's a rule in general terms that the commissioner can only take collection action against one entity for any amount of tax. But there's also a counter argument that the ATO sometimes relies on, that each of those liabilities is separate, and therefore, they're not doing alternative assessments, because each entity in the chain may be liable. I don't buy that particular argument myself, but I've had it argued to me on cases.

But jump on it quickly, review to see whether there's any chance of challenging it, and otherwise engage constructively with the ATO to try and get a payment plan, because the next stage is winding up applications, and that's the pathway for the business to be potentially insolvent.

The other option you have if you get a statutory demand, of course, is to go into administration, a small [inaudible 01:02:16] restructure prior to that liquidation stage.

And the third option that you have is to go into a member's voluntary liquidation. But for that to succeed, you have to have a statement of solvency, a declaration of solvency made by the directors. And in that context, if you believe the company's insolvent and needs to be liquidated, it means that the company can't be solvent, it must be insolvent. And it's hard, therefore, to give declaration of solvency. So, you're usually better off either allowing the commissioner to tip it into liquidation. Or have one of the directors who may be a shareholder take creditors action against the company to sue for the debt that they are owed by the company in order to do that, or get some other associate to do it as a way of sidestepping that issue of not being able to do a member's voluntary because you can't be solvent.

CCH Learning:

Thank you for that, Bruce. And I hope that helps you there, Jono. And just to let you know, Stuart, who was our first question, he says, "Thank you for your answer."

Well, that does bring us to the end of our questions for today, but if you do have any other questions, Bruce's details are 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 shortly after today's session, you will be emailed when you're enrolled into the E-learning recording, which can be watched multiple times, and you'll have access to the PowerPoint transcript, and of course your 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 so much everyone.