SHERIDANS
CHARTERED ACCOUNTANTS

FACT SHEET
Director Penalty Notices

What are they?

Companies are obligated to report and pay to the Australian Taxation Office ("ATO") amounts due under the PAYG withholding regime and the superannuation guarantee charge ("SGC") provisions. If companies fail to comply with those obligations, the ATO's Director Penalty Notice ("DPN") regime causes the imposition of a penalty on the director(s) of such companies, making them personally liable for the amount(s) that should have been paid by the company.

The ATO has a number of techniques for collecting business tax debts including statutory demands and garnishee orders, and the ATO's statutory DPN regime is a powerful inducement to directors not to ignore unpaid PAYG and superannuation in their business.

Importantly, the DPN regime allows the ATO to impose personal liability on company directors without the delay or expense of taking legal action.

History

In 1993 the DPN regime was introduced (replacing the priority previously given to the ATO) to assist the ATO to recover certain company tax liabilities. At its inception, the new regime related principally to unpaid PAYG withholding tax obligations.

With effect from 1 July 2010, the DPN provisions were amended. However, a second set of amendments was enacted on 27 June 2012 which effected a major revision of the DPN provisions.

The relatively recent strengthening of the DPN provisions dramatically increased the scope of the DPN regime and director personal liability.

In particular, a director of a company may now be held personally liable for unpaid superannuation contributions if the company fails to comply with its superannuation guarantee obligations.

How does the DPN regime work?

Where a company fails to pay its PAYG withholding and SGC debts, the DPN regime makes the director liable to a penalty at the end of the day the company is due to meet its obligation. The ATO does not need to issue any notices or take any action to create the penalty; it is automatic as soon as the debt is not paid by the due date. The ATO, however, must not commence proceedings to recover a director penalty until 21 days after a DPN is issued to a director.

If the PAYG and/or SGC liabilities have been reported, then any DPN issued will be the 'old style' notice that gives directors 21 days to act to get the penalty remitted and avoid personal liability.

A director penalty is remitted in these circumstances if, within 21 days, any of the following things happen:

- the company pays the debt;
- a voluntary administrator is appointed; or
- the company is placed into liquidation.

However (and most importantly), where ***three months has elapsed*** after the due day for lodgement, and ***the underlying liability remains unpaid and unreported***, the director penalty is not remitted as a result of placing the company into administration or liquidation. This means the company must pay the debt or if it cannot, the director must pay.

In other words, remission of a director penalty is only a possibility where the company reported the relevant liability to the ATO within three months of the due date for lodgement.

The new DPN regime enables the ATO to take action for all PAYG withholding liabilities and SGC debts that remain unreported from 29 June 2012.

The legislation acts retrospectively in respect of PAYG withholding liabilities, so the new DPNs can include PAYG withholding liabilities incurred prior to 29 June 2012 that have remained unreported for more than three months.

The new DPNs will not include unreported SGC liabilities prior to 29 June 2012.

The new DPN amendments are designed to change the behaviour of directors. In the past, some directors attempted to ignore tax and superannuation debts by not complying with lodgement and payment requirements. Under the current regime there is a strong incentive for directors to cause companies to report liabilities for PAYG and SGC to the ATO within the three month period.

The DPN regime is now fairly complex and timing is critical.

What do directors need to do?

Fundamentally, directors must ensure that proper financial records are maintained for the company.

Directors must then:

(a) Increase their monitoring and awareness of the company's taxation and superannuation liabilities, and act promptly when problems arise.

(b) Ensure that PAYG withholding and superannuation amounts are reported and remitted to the ATO within the required timeframes.

(c) Seek immediate advice from an insolvency practitioner at the first sign of trouble.

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Director Penalty Notices - Related issues

Where are notices sent to?

The DPN is sent to the director's address as listed in the company records maintained by ASIC.

The ATO may also send a copy of the DPN to the director's registered tax agent. This gives the ATO an additional means of bringing the penalty to the director's attention. The ATO is not required to send a copy to the registered tax agent and failure to do so does not affect whether the ATO has given the director actual notice.

Directors should ensure their address details are correct with ASIC.

21 day notice period

The ATO must issue a DPN and wait until the end of the 21 days after issuing the notice before commencing formal proceedings. The DPN is "given" on the day when it is posted by the ATO.

Incoming directors

Newly-appointed directors will incur director penalties equal to all the company's unpaid PAYG withholding liabilities and any unpaid SGC relating to the June 2012 quarter or later.

These penalties cannot be avoided unless within 30 days of becoming a director, either the company pays the liabilities or enters into voluntary administration or liquidation.

It appears that the new director's penalties remain even if the new director resigns within the first 30 day period, unless the company's liabilities are paid or the company enters voluntary administration or liquidation.

After a director has been a director for three months, penalties for amounts that were unreported for more than 3 months and remain unpaid cannot be discharged through administration or liquidation.

New directors must do their due diligence regarding unpaid PAYG and superannuation liabilities prior to accepting appointment. After appointment it could well be too late to avoid personal liability.

Estimates

The ATO can estimate how much PAYG withholding or superannuation it reasonably believes a company has failed to pay and give notice to the company of such estimate.
The estimate becomes payable in its own right as a separate and parallel liability with the actual shortfall. A director becomes liable for a penalty in the amount of the estimate if it is not paid on its due date i.e. a DPN can be issued for the estimate of the PAYG withholding or superannuation liability.

Within 7 days after the estimate is given, the director may give a statutory declaration specifying the unpaid amount of the underlying liability.

Defences

A director is not liable for a director penalty where the director can establish that:

(a) Because of illness or for some other good reason, the director did not take part (and it would have been unreasonable to expect the director to take part) in the management of the company.

(b) The director took all reasonable steps to ensure that one of the following three things happened:

- the company paid the amount outstanding.
- an administrator was appointed to the company.
- the directors began winding up the company.

(c) None of the above steps at (b) were available to the director.

In addition, a director may not be liable with regard to unpaid SGC if they can establish that the company treated the SGC Act as applying in a way that could be reasonably argued was in accordance with the law, and took reasonable care in applying the SGC Act to their affairs.

The provisions allow for a 60 day period to raise a defence.

Right of indemnity and contribution

Under the legislation, a director who pays a liability of the company has a right of indemnity and contribution from the company and its other directors who were also liable to pay the penalty.

ATO indemnity

Under S.588FGA of the Corporations Act, directors are liable to indemnify the ATO for any preference payments recovered by a liquidator relating to payments of PAYG.

A director tempted to contribute their own funds to a company and have it enter into a payment arrangement with the ATO, may find they pay the amount twice: once to the company so it can pay the ATO and again to the ATO when the liquidator recovers the preference.

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