

Private Business Tax Retreat

David v Goliath: Dealing with ATO Debt and Recovery Action

Presented at the Private Business Tax Retreat on 16-17 February 2023

Shaun Cartoon, FTI
Arnold Bloch Leibler

Andrew Spierings, ATI
Arnold Bloch Leibler

© Shaun Cartoon, FTI & Andrew Spierings, ATI 2023

Disclaimer: The material and opinions in this paper are those of the author and not those of The Tax Institute. The Tax Institute did not review the contents of this paper and does not have any view as to its accuracy. The material and opinions in the paper should not be used or treated as professional advice and readers should rely on their own enquiries in making any decisions concerning their own interests.

Liability limited by a scheme approved under professional standards legislation.

Contents

1. Overview	3
2. Tax Debt and the Commissioner’s Powers.....	4
2.1 Recovering a tax-related liability that is due and payable	4
2.2 General debt recovery powers	5
2.3 Tax-specific debt recovery powers.....	8
3. Managing Tax Debts and Other Measures.....	13
3.1 Undisputed debts	14
3.2 Disputed debts.....	17
4. Small Business Restructuring.....	19
4.1 Eligibility criteria.....	19
4.2 The restructuring process.....	20
4.3 Effect of small business restructuring.....	21

1. Overview

And Saul said to David, Thou art not able to go against this Phillistine to fight with him: for thou art but a youth, and he a man of war from his youth.

And David said unto Saul, Thy servant kept his father's sheep, and there came a lion, and a bear, and took a lamb out of the flock:

And I went out after him, and smote him, and delivered it out of his mouth: and when he arose against me, I caught him by his beard, and smote him, and slew him.

Thy servant slew both the lion and the bear: and [Goliath] shall be as one of them...

- *The King James Bible, 1 Sam, 17:33-36*

In Australia, there are some 250,000 private groups (comprising around 1.1 million entities) plus another 4.5 million small business taxpayers.¹ Together, they are a major segment of the economy and of the tax base. They are also a major part of the \$66.6 billion of tax debt currently owed to the public coffers.²

That tax debt ballooned during the coronavirus pandemic as the Commissioner of Taxation took a more passive stance to support business. Whilst first home buyers turned to the Bank of Mum and Dad, businesses increasingly relied on the ATO Bank for funding as directors prioritised other company and personal debts. The Commissioner, armed with all the coercive powers of the state, has stated that one of his “key priorities” for this year is to address that debt.³ The Commissioner has myriad tools for that purpose, which some taxpayers will experience all too painfully. He is undoubtedly the Goliath of this arena; “a man of war from his youth”.

Most taxpayers are, in comparison, but callow youths. Whether they are Davids or without the divine protection to overcome Goliath, in every case, each taxpayer’s (and sometimes their directors’) debt must be carefully managed. Proper management allows David to carry on the fight over contested liabilities as best he can and other taxpayers to carry on business whilst dealing with their uncontested debt.

In many cases, and whatever the stance in the substantive tax dispute, debt and recovery proceedings are best managed by negotiation and a productive relationship with the Commissioner and his officers rather than an attempt to slay the lion and the bear, or alternatively, to run away and pretend they do not exist. The Commissioner is not in the business of bankrupting Australian taxpayers and, if he can be given sufficient comfort that a debt will ultimately be met, he is usually amenable to arrangements that will allow business to continue. There are a range of options available to the taxpayer to achieve that result.

The authors are grateful to Timothy Graham of Arnold Bloch Leibler for his assistance in preparing this paper. Naturally, all errors remain ours alone.

¹ Australian Taxation Office, ‘Annual Report 2021-22’ (10 October 2022) 4.

² Australian Taxation Office, ‘Annual Report 2021-22’ (10 October 2022) 212.

³ Australian Taxation Office, ‘Annual Report 2021-22’ (10 October 2022) ii.

2. Tax Debt and the Commissioner's Powers

Taxation is by far the principal means by which the Commonwealth raises money, and the Commissioner is charged with procuring that money: some \$515.6 billion of it in the 2021-22 year.⁴ To that end, the law (enacted at the instigation of the government which that money supports) gives him powers that are vast and invasive. The Commissioner's armoury is almost as impressive as the Biblical Goliath:

And he had an helmet of brass upon his head, and he was armed with a coat of mail; and the weight of the coat was five thousand shekels of brass. And he had greaves of brass upon his legs, and a target of brass between his shoulders. And the staff of his spear was like a weaver's beam; and his spear's head weighed six hundred shekels of iron: and one bearing a shield went before him.⁵

2.1 Recovering a tax-related liability that is due and payable

A 'tax-related liability' is any pecuniary liability arising directly under a taxation law.⁶ An amount of a tax-related liability that is due and payable is a debt due to the Commonwealth and is payable to the Commissioner.⁷ The Commissioner, a Second Commissioner, or a Deputy Commissioner may sue in their official name in a court of competent jurisdiction to recover an amount of a tax-related liability that remains unpaid.⁸ Once an assessment is issued, there are few ways for a taxpayer to resist such a suit: the provisions of the tax legislation do not leave any room for the operation of state limitation acts to impose a time limit on recovery in a court⁹ and the decision to commence recovery proceedings cannot be challenged under the *Administrative Decisions (Judicial Review) Act 1977*.¹⁰

A tax-related liability generally becomes due and payable shortly after the Commissioner makes an assessment.¹¹ Even though an assessment may be disputed by way of an objection, review or appeal under Part IVC of the *Taxation Administration Act 1953*, the tax-related liability may still be recovered by the Commissioner.¹² In other words, while a taxpayer is entitled to challenge the assessment, in the meantime, tax must be paid¹³ and there are a range of general and statutory debt recovery powers which the Commissioner can rely upon to ensure that tax is paid. The Commissioner's decision to exercise these recovery powers will generally turn on an assessment of the taxpayer's capacity to repay the debt and the risk that the taxpayer will evade payment.¹⁴

Integral to that assessment, and the course of any recovery action, is determining what assets belong to the taxpayer, i.e., what is "up for grabs". If debt action becomes contentious, it is in the Commissioner's interest for the taxpayer's asset pool to be larger. Assets held in the names of companies or relatives may come under attack as belonging beneficially to the taxpayer, such as the family home whose registered proprietor is a spouse. Those disputes will be familiar to many tax and

⁴ Australian Taxation Office, 'Annual Report 2021-22' (10 October 2022) ii.

⁵ *The King James Bible*, 1 Sam, 17:5-7. Perhaps the modern shield-bearer is the Deputy Commissioner of Taxation.

⁶ *Taxation Administration Act 1953* (Cth) Sch 1 s 255-1(1).

⁷ *Taxation Administration Act 1953* (Cth) Sch 1 s 255-5(1).

⁸ *Taxation Administration Act 1953* (Cth) Sch 1 s 255-5(2).

⁹ *DCT v Moorebank Pty Ltd* (1988) 165 CLR 55.

¹⁰ *Rawson Finances Pty Ltd v DCT* (2010) 189 FCR 189; *Golden City Car & Truck Centre Pty Ltd v DCT* (1999) 56 ALD 177; *Ruddy v DCT* (1998) 82 FCR 337.

¹¹ See, eg, *Income Tax Assessment Act 1997* (Cth) s 5-5.

¹² *Taxation Administration Act 1953* (Cth) ss 14ZZM and 14ZZR; *DCT v Broadbeach Properties Pty Ltd* (2008) 237 CLR 473.

¹³ See eg, *Hoare Bros Pty Ltd v DCT* (1996) 62 FCR 302.

¹⁴ PSLA 2011/18; PSLA 2011/6.

succession planning advisors and, whilst the Commissioner's recent doctrinal challenge to the presumption of advancement failed,¹⁵ questions of resulting trust over family or even business assets will turn on intention and circumstances.

2.2 General debt recovery powers

Judgment debt

A notice of assessment is conclusive evidence that the assessment was properly made and that, except in review or appeal proceedings under Part IVC, the amounts and particulars of the assessment are correct.¹⁶ Similarly, the production of a signed certificate which states that an amount was payable under a taxation law from a specified time is prima facie evidence that the amount was payable from that time and the particulars stated in the certificate are correct.¹⁷ The Commissioner may rely on these provisions to obtain judgment that the amount is payable, which then supports recovery of that judgment debt through general law enforcement processes such as bankruptcy or insolvency, or writs and warrants of execution.

Writs and warrants of execution

The Commissioner may seek to enforce a judgment debt through a writ or warrant of execution or order of seizure and sale.¹⁸ As the name suggests, such an order authorises the sheriff in the relevant jurisdiction to seize and sell the debtor's assets and apply the proceeds to satisfy the judgment debt.¹⁹ The property which may be seized and sold is property owned by the debtor, including property jointly or commonly held with another person,²⁰ but not property held on trust.²¹ The Commissioner will generally consider warrants when it can be established that the debtor has sufficient unsecured assets to satisfy the tax debt, or the tax debtor has equity in real estate.²²

Bankruptcy and insolvency

Having obtained a judgment debt, the Commissioner may seek to recover the debt from an individual taxpayer using the bankruptcy process. He may apply to the Official Receiver to issue a bankruptcy notice against an individual taxpayer, which requires payment of the tax debt within a specified period.²³ If the taxpayer fails to comply with the bankruptcy notice, this will amount to an act of bankruptcy.²⁴ The Commissioner may then present a debtor's petition to the Court, who may then make a sequestration order against the taxpayer upon which they will become bankrupt.²⁵

A trustee in bankruptcy will be appointed to administer the bankrupt's estate. This will have serious implications for the property divisible amongst the creditors, being property belonging to the bankrupt

¹⁵ *Bosanac v FCT* (2022) 96 ALJR 976.

¹⁶ *Taxation Administration Act 1953* (Cth) Sch 1 s 350-10(1) item 2.

¹⁷ *Taxation Administration Act 1953* (Cth) Sch 1 s 350-10(3).

¹⁸ *Federal Court Rules 2011* (Cth) r 41.10; *Court Procedure Rules 2006* (ACT) r 2200; *Supreme Court Rules* (NT) r 66.02(1)(a); *Uniform Civil Procedure Rules 2005* (NSW) rr 39.1, 40.2; *Uniform Civil Procedure Rules 1999* (QLD) r 828; *Enforcement of Judgments Act 1991* (SA) s 7(1); *Supreme Court Rules 2000* (TAS) r 906; *Supreme Court (General Civil Procedure) Rules 2015* (VIC) r 66.02(1)(a); *Civil Judgments Enforcement Act 2004* (WA) s 59.

¹⁹ See, eg, *Supreme Court (General Civil procedure) Rules 2015* (VIC) O 69.

²⁰ *Farrar v Beswick* (1836) 150 ER 608.

²¹ *Caillaud v Estwick* (1794) 145 ER 909.

²² PSLA 2011/18, [169].

²³ *Bankruptcy Act 1966* (Cth) s 41.

²⁴ *Bankruptcy Act 1966* (Cth) s 40(1)(g).

²⁵ *Bankruptcy Act 1966* (Cth) s 43.

at the commencement of the bankruptcy or acquired after this time but before discharge.²⁶ This property will pass to and vest in the trustee on their appointment.²⁷ The trustee will take possession of that property,²⁸ realise those assets,²⁹ and declare and distribute dividends from the proceeds amongst the creditors.³⁰

Similarly, the Commissioner may seek to recover the debt from a corporate taxpayer by winding up the company in insolvency.³¹ The Commissioner may serve a statutory demand on the taxpayer for payment of the tax debt.³² If the taxpayer fails to comply with the statutory demand, the Commissioner may apply to the Court for the company to be wound up in insolvency.³³ The Court must presume the company is insolvent if the taxpayer failed to comply with the statutory demand,³⁴ and may make an order that the company be wound up in insolvency.³⁵

A liquidator will be appointed to the company. Where a liquidator has been appointed, the liquidator will take into their custody or control all the property of the company.³⁶ The court may order that the property of the company vest in the liquidator.³⁷ The liquidator will then collect that property and apply it in discharging the company's liabilities.³⁸ Following this, the Court may order the deregistration of the company and the company will cease to exist following deregistration.³⁹

The Commissioner will consider a number of factors before initiating bankruptcy or insolvency proceedings including the asset position of the debtor, the size and nature of the debt, the future income of the debtor, the risk to the revenue and the cost and likely return of bankruptcy or liquidation.⁴⁰ The secured creditor position of the debtor will also be relevant, as any secured debt ranks in priority to tax debt which is unsecured. The Commissioner will also consider whether bankruptcy would be inappropriate due to special circumstances such as age or ill health and whether the debtor may be required to make contributions from their future income to the bankrupt estate.⁴¹ The Commissioner will usually issue director penalty notices prior to initiating liquidation proceedings,⁴² and is more likely to initiate such proceedings where there has been insolvent trading in order to pursue the directors for breach of duty.⁴³

A further important point, whether for bankrupt individuals or insolvent companies, is that their Part IVC appeal rights are significantly restricted.⁴⁴ There are also questions about whether the bankrupt retains their legal professional privilege or it passes to the trustee in bankruptcy. Although "not beyond doubt",

²⁶ *Bankruptcy Act 1966* (Cth) s 116.

²⁷ *Bankruptcy Act 1966* (Cth) s 132.

²⁸ *Bankruptcy Act 1966* (Cth) s 129.

²⁹ *Bankruptcy Act 1966* (Cth) s 134.

³⁰ *Bankruptcy Act 1966* (Cth) s 140.

³¹ Winding up in insolvency is governed by Part 5.4B of the *Corporations Act 2001* (Cth). This is one of a number of insolvency recovery processes the Commissioner may use to recover a tax debt from a company set out in Chapter 5 of the *Corporations Act 2001* (Cth).

³² *Corporations Act 2001* (Cth) s 459E.

³³ *Corporations Act 2001* (Cth) s 459P.

³⁴ *Corporations Act 2001* (Cth) s 459C(2)(a).

³⁵ *Corporations Act 2001* (Cth) s 459A.

³⁶ *Corporations Act 2001* (Cth) s 474(1).

³⁷ *Corporations Act 2001* (Cth) s 475(2).

³⁸ *Corporations Act 2001* (Cth) s 478(1).

³⁹ *Corporations Act 2001* (Cth) s 601AD.

⁴⁰ PSLA 2011/16, [11].

⁴¹ PSLA 2011/16, [12] and [13].

⁴² PSLA 2011/16, [14].

⁴³ PSLA 2011/16, [16].

⁴⁴ See, *McCallum v FCT* (1997) 75 FCR 458; *ACN 092 138 442 Pty Ltd v FCT* (2013) 95 ATR 976; *Pitman v FCT* (2021) 113 ATR 852.

the balance of authority seems to favour retention by the bankrupt,⁴⁵ but the process of handing over documents to the trustee raises the very real possibility of waiving privilege.⁴⁶

Freezing orders

The Commissioner may protect his ability to recover by seeking freezing orders over the taxpayer's assets.⁴⁷ Such an order may restrain a taxpayer from removing any assets located in or outside Australia or from disposing of, dealing with, or diminishing the value of those assets.⁴⁸ Such an order may be made where there is a judgment, or the applicant has a good arguable case on a prospective cause of action,⁴⁹ and there is a danger that a judgment will be wholly or partly unsatisfied because the judgment debtor, or prospective judgment debtor, absconds or their assets are removed from Australia or disposed of.⁵⁰

Due to the statutory finality of tax assessments, it appears that in the absence of judgment the Commissioner will generally have a strong prospective cause of action in recovery proceedings.⁵¹ The fact that a taxpayer is incorporated in another country, and their assets are moveable, is relevant but not sufficient to demonstrate there is a risk the taxpayer will dissipate their assets.⁵² There must be facts from which a prudent, sensible, commercial person can properly infer a danger of default if assets are removed from the jurisdiction.⁵³ However, the court may make freezing orders over the taxpayer's worldwide assets, regardless of the efficacy or prospects of enforcing such an order.⁵⁴

Intervening in Family Court proceedings

The Commissioner may intervene in Family Court proceedings where one of the parties has an outstanding tax debt. In property settlement proceedings, the Family Court will generally always have regard to the position of significant creditors.⁵⁵ The Commissioner may, with leave from the Court, intervene in property settlement proceedings.⁵⁶ This may allow the Commissioner to seek asset preservation orders, similar to freezing orders, in relation to the parties to the marriage.⁵⁷ In addition to intervening in property settlement proceedings, the Commissioner may also apply to the Court to set aside property settlement orders.⁵⁸

⁴⁵ *R v Dunwoody* (2004) 212 ALR 103, [25].

⁴⁶ *R v Dunwoody* (2004) 212 ALR 103, [31].

⁴⁷ *Federal Court Rules 2011* (Cth) Div 7.4; *Court Procedure Rules 2006* (ACT) rr 740-745; *Supreme Court Rules 1987* (NT) o 37A; *Uniform Civil Procedure Rules 2005* (NSW) Pt 25 Div 2; *Uniform Civil Procedure Rules 1999* (QLD) r 260; *Supreme Court Civil Rules 2006* (SA) r 247; *Supreme Court Rules 2000* (TAS) r 937B; *Supreme Court (General Civil Procedure) Rules 2015* (VIC) r 37A.02; *Rules of the Supreme court 1971* (WA) o 52A.

⁴⁸ *Federal Court Rules 2011* (Cth) r 7.32(2).

⁴⁹ *Federal Court Rules 2011* (Cth) r 7.35(1).

⁵⁰ *Federal Court Rules 2011* (Cth) r 7.35(4).

⁵¹ *DCT v Gashi* (2010) 27 VR 127, [23] – [24]; *DCT v Hua Wang Bank Berhad* (2010) 273 ALR 194, [15] and [16].

⁵² *DCT v Hua Wang Bank Berhad* (2010) 273 ALR 194, [12] and [56].

⁵³ *DCT v Hua Wang Bank Berhad* (2010) 273 ALR 194, [12].

⁵⁴ *DCT v Huang* (2021) 395 ALR 616.

⁵⁵ *DCT v Kliman* (2002) 51 ATR 58, [30].

⁵⁶ *Family Law Act 1975* (Cth) ss 79, 92 and 4(1)(ca); *DCT v Kliman* (2002) 51 ATR 58.

⁵⁷ *DCT v Kliman* (2002) 51 ATR 58.

⁵⁸ *DCT v Spanjich* (1988) 93 FLR 98; *Mcauley v DCT* 98 ATC 4021.

2.3 Tax-specific debt recovery powers

Debt information disclosure

Generally, it is an offence for a taxation officer to disclose a taxpayer's protected information to another entity. However, in 2019 an exception was introduced allowing taxation officers to disclose the business tax debt information of a taxpayer to credit reporting bureaus in certain circumstances.

Broadly, the exception applies where a taxation officer discloses information, which relates to the tax debts of an entity in a class of entity declared by the Minister, to a "credit reporting bureau" for the purposes of enabling it to conduct credit worthiness reports in relation to that entity.⁵⁹ For disclosures which do not involve updating, correcting or confirming previously disclosed information, the Inspector-General of Taxation must be consulted, and the disclosure cannot be made until 28 days after the entity has been notified in writing.⁶⁰ The notice must explain the information, explain why the entity falls into the relevant class, set out the overdue tax debts, and explain how the entity may make a complaint.⁶¹

A "credit reporting bureau" is an entity recognised by the Commissioner as one which prepares and issues credit worthiness reports in relation to other entities.⁶² The Commissioner is required to publish a list of credit reporting bureaus on his website.⁶³

A taxpayer will fall into the relevant class where it meets the specified conditions.⁶⁴ The entity must be registered on the Australian Business Register, but not as a deductible gift recipient, complying superannuation fund, registered charity or government agency.⁶⁵ The entity must have total tax debts of at least \$100,000 which have been due and payable for 90 days,⁶⁶ excluding tax debts subject to a payment arrangement, or a live debt release application, objection, review, appeal, or complaint with the Inspector-General.⁶⁷ Further, the entity must not have an active complaint with the Inspector-General in relation to the exception, unless after taking reasonable steps the Commissioner does not become aware of the complaint.⁶⁸

Disclosure of information under this exception does not directly facilitate the recovery of the outstanding tax debts. However, it may make it difficult for the taxpayer to access credit, which may have serious financial repercussions for them and their business, particularly the availability of credit and the confidence of existing counterparties. To manage these risks, the taxpayer should ensure it engages with the Commissioner.

Security

The Commissioner may require security for the due payment of an *existing* or *future* tax-related liability.⁶⁹ The reference to a future tax-related liability is extremely broad and includes liabilities which are unknown or unquantified at the time the power to require security is exercised.⁷⁰ It is not conditioned

⁵⁹ *Taxation Administration Act 1953* (Cth), Sch 1 s 355-72(1).

⁶⁰ *Taxation Administration Act 1953* (Cth), Sch 1 s 355-72(1)(e).

⁶¹ *Taxation Administration Act 1953* (Cth), Sch 1 s 355-72(3).

⁶² *Taxation Administration Act 1953* (Cth), Sch 1 s 355-72(7).

⁶³ *Taxation Administration Act 1953* (Cth), Sch 1 s 355-72(8).

⁶⁴ Under s 355-72(5), the Minister may by legislative instrument declare one or more classes of entities for the purposes of the exception. The current legislative instrument is *Taxation Administration (Tax Debt Information Disclosure) Declaration 2019 (TDID 2019/1)*. Cl 6 of TDID 2019/1 specifies the conditions an entity must satisfy to fall into the relevant class.

⁶⁵ TDID 2019/1, cl 6(1)(a).

⁶⁶ TDID 2019/1, cl 6(1)(b).

⁶⁷ TDID 2019/1, cl 6(2).

⁶⁸ TDID 2019/1, cl 6(1)(c).

⁶⁹ *Taxation Administration Act 1953* (Cth) Sch 1 s 255-100(1).

⁷⁰ *Keris Pty Ltd v DCT* 253 FCR 233, [27].

upon facts having occurred upon which the Commissioner could then act to make and notify an objectively correct quantification of the liability.⁷¹ This means the Commissioner can require a taxpayer to give security for a future tax-related liability in relation to a transaction which has not yet occurred.⁷²

The Commissioner may require the taxpayer to give security by way of a bond or deposit, or by any other means that the Commissioner believes is appropriate,⁷³ but must give the taxpayer written notice of the requirement to give security.⁷⁴ The Commissioner's preferred types of securities are mortgages over real property and bank guarantees.⁷⁵ The taxpayer will commit an offence if they fail to give the required security,⁷⁶ and the Federal Court may order a taxpayer to comply with the requirement to give security.⁷⁷ Failure to comply with such an order is also an offence.⁷⁸

Statutory garnishees

The Commissioner may recover a tax debt from third parties by issuing a garnishee notice to an entity who owes or may later owe money to the taxpayer.⁷⁹ These are commonly issued to banks to garnishee the accounts of their taxpayer customers. The third party (e.g., bank) is taken to owe money to the taxpayer where it holds the money for or on account of the taxpayer or some other entity for payment to the taxpayer, or has authority from another entity to pay the money to the taxpayer.⁸⁰ The deeming also operates even if the money is only due conditionally and the relevant condition has not yet been fulfilled.

The notice will require the third party to pay the amount owing to the Commissioner in place of the taxpayer.⁸¹ When deciding whether to issue a garnishee notice, the effect the notice might have on the taxpayer's ability to fund Part IVC proceedings and the merits of those appeals are relevant considerations.⁸² The third party will commit an offence if they do not comply with the garnishee notice.⁸³

Where the notice is effective, it creates a statutory charge in favour of the Commissioner which makes the Commissioner a secured creditor of the taxpayer with priority in the event of insolvency.⁸⁴ This is one way that the Commissioner can legitimately "jump the queue" in front of other creditors, even mortgagees of real property.⁸⁵

Estimates

The Commissioner may estimate the unpaid and overdue amount of a taxpayer's pay-as-you-go, superannuation guarantee charge and GST liability to the extent such a liability has not been assessed

⁷¹ *Keris Pty Ltd v DCT* 253 FCR 233, [93].

⁷² *Keris Pty Ltd v DCT* 253 FCR 233.

⁷³ *Taxation Administration Act 1953* (Cth) Sch 1 s 255-100(2).

⁷⁴ *Taxation Administration Act 1953* (Cth) Sch 1 s 255-105.

⁷⁵ PSLA 2011/14, [87].

⁷⁶ *Taxation Administration Act 1953* (Cth) Sch 1 s 255-110.

⁷⁷ *Taxation Administration Act 1953* (Cth) Sch 1 s 255-115.

⁷⁸ *Taxation Administration Act 1953* (Cth) Sch 1 s 255-120.

⁷⁹ *Taxation Administration Act 1953* (Cth) Sch 1 s 260-5(2).

⁸⁰ *Taxation Administration Act 1953* (Cth) Sch 1 s 260-5(3).

⁸¹ *Taxation Administration Act 1953* (Cth) Sch 1 s 260-5(4).

⁸² *Denlay v FCT* (2013) 211 FCR 344, [73] and [75].

⁸³ *Taxation Administration Act 1953* (Cth) Sch 1 s 260-20.

⁸⁴ *Brown v Brown* (2007) 69 ATR 533, [17] citing *Clyne v DCT* (1981) CLR 1, 17-18 and 26-27; *Goodin v FCT* (2002) 169 FLR 282, 289; *FCT v Donnelly* (1989) 25 FCR 432, 436; *Macquarie Health Corp Ltd v FCT* (1999) 96 FCR 238, 255-271; *Goodger v Ayre* (1988) 88 FLR 188, 191-192.

⁸⁵ See, eg, *FCT v Park* (2012) 205 FCR 1.

prior to the estimate.⁸⁶ The amount of the estimate is what the Commissioner thinks is reasonable.⁸⁷ The taxpayer is liable to pay the Commissioner the amount of the estimate, and this liability is separate and distinct from the underlying liability.⁸⁸ This means the Commissioner is able to separately recover an estimate liability, and the estimate liability is a debt provable in bankruptcy or winding up.⁸⁹

While the accuracy of the estimate is irrelevant,⁹⁰ there are a number of ways in which the estimate can be discharged, reduced or revoked. To the extent the estimate liability or the underlying liability is discharged, both liabilities are discharged.⁹¹ The Commissioner may at any time reduce or revoke the amount of the estimate.⁹² In doing so, the Commissioner must have regard to the principles that the estimate is of the unpaid amount of the underlying liability, the purpose of reducing the estimate is to bring it closer to the unpaid amount of the underlying liability, and reductions of the underlying liability after the estimate are dealt with under the discharge provisions.⁹³ The estimate may also be reduced or revoked where the taxpayer provides a statutory declaration or affidavit which demonstrates that a specified lesser amount is the unpaid amount of the underlying liability or that the underlying liability never existed.⁹⁴ The estimate may also be reduced to the extent that a proof of debt in relation to the estimate is rejected,⁹⁵ or to the extent it is paid.⁹⁶

Director penalties

The Commissioner may rely on director penalty notices (**DPNs**) to recover certain tax-related liabilities of a corporate taxpayer from its directors. This regime applies to persons who are “directors” as defined in the Corporations Act (i.e., it extends to de facto and shadow directors).⁹⁷ The provisions impose an obligation on directors to ensure that companies comply with their obligations to pay pay-as-you-go withholding, superannuation guarantee charge, GST, and estimates to the Commissioner by the relevant due day.⁹⁸ Between March and September 2022, over 52,000 DPNs were issued.⁹⁹

Directors issued with a DPN are personally liable to pay an amount equal to the company’s unpaid tax liability. The liabilities of the director and the company are parallel so that the Commissioner can recover against either party, but where an amount is paid or applied to discharge one of the liabilities the other is discharged to the same extent.¹⁰⁰ The director will continue to be liable to the director penalty until the company pays the outstanding amount, or, within the specified time, appoints a voluntary administrator, small business restructuring practitioner or liquidator to wind up the company.¹⁰¹ However, the appointment of an administrator or restructuring practitioner, or winding up, will not relieve the director from penalty where the relevant tax liability (other than SGC) was due over three months before, to the extent that the Commissioner has not already been notified of the liability.¹⁰²

⁸⁶ *Taxation Administration Act 1953* (Cth) Sch 1 s 268-10(1).

⁸⁷ *Taxation Administration Act 1953* (Cth) Sch 1 s 268-10(2).

⁸⁸ *Taxation Administration Act 1953* (Cth) Sch 1 s 268-20(1) and (2).

⁸⁹ *Taxation Administration Act 1953* (Cth) Sch 1 s 268-30.

⁹⁰ *Taxation Administration Act 1953* (Cth) Sch 1 s 268-25.

⁹¹ *Taxation Administration Act 1953* (Cth) Sch 1 s 268-20(3).

⁹² *Taxation Administration Act 1953* (Cth) Sch 1 s 268-35(1) and (3).

⁹³ *Taxation Administration Act 1953* (Cth) Sch 1 s 268-35(5).

⁹⁴ *Taxation Administration Act 1953* (Cth) Sch 1 s 268-40(2) and (4).

⁹⁵ *Taxation Administration Act 1953* (Cth) Sch 1 s 268-45.

⁹⁶ *Taxation Administration Act 1953* (Cth) Sch 1 s 268-50.

⁹⁷ *Taxation Administration Act 1953* (Cth), sch 1 s 269-15(1).

⁹⁸ *Taxation Administration Act 1953* (Cth) Sch 1 ss 269-10 and 269-15(1).

⁹⁹ Tom McIlroy and John Kehoe, ‘Directors Cough up \$2bn Tax Debt after ATO Warning’, *Australian Financial Review* (26 September 2022).

¹⁰⁰ *Taxation Administration Act 1953* (Cth) Sch 1 s 269-40.

¹⁰¹ *Taxation Administration Act 1953* (Cth) Sch 1 ss 296-15(2) and 269-30(1).

¹⁰² *Taxation Administration Act 1953* (Cth) Sch 1 s 296-30(2)-(3).

The director may escape liability by raising one of three limited defences:

1. that, because of illness or for some other good reason, it would have been unreasonable to expect the director to take part, and the director did not take part, in the management of the company at the relevant time;¹⁰³
2. the director took all reasonable steps, or there were no reasonable steps that could have been taken, to cause the company to comply with its obligation, appoint an administrator or small business restructuring practitioner, or cause the company to begin to be wound up;¹⁰⁴ or
3. where the director penalty relates to superannuation guarantee charge, that the penalty resulted from the company adopting a reasonably arguable position and taking reasonable care.¹⁰⁵

These defences are notoriously difficult to prove, and the director bears the burden of proof in relation to the matters necessary to establish the satisfaction of the defence of illness or reasonable steps.¹⁰⁶

For a director to rely on either the ‘illness or some other good reason’ or the ‘all reasonable steps’ defence, they must establish the defence for the entire period. In other words, they have to either establish that it would be unreasonable to expect them to participate in the management of the company due to illness or some other good reason, or that they took all reasonable steps and that no further reasonable steps could be taken, for the entire period the directors are under their obligation.¹⁰⁷

For the purposes of establishing the ‘illness or some other good reason’ defence, the courts have set a high bar as to what constitutes a good reason. The cases illustrate a litany of reasons which were not “good reasons” for non-participation in the management of the company, including where the director was under the mistaken belief they had resigned their position,¹⁰⁸ and where the director believed others were responsible for the financial affairs of the company.¹⁰⁹ Even if there is a good reason the defence may fail on the evidence, for example where there is evidence that the director has actually participated in the management of the company.¹¹⁰

The courts have set a similarly high bar for the ‘all reasonable steps’ defence. The defences (a) to take all reasonable steps and (b) that no reasonable steps could be taken are cumulative and not mutually exclusive.¹¹¹ In effect, this means the director must exhaust all reasonable steps until there are no further steps which could be taken, and that this must be established for the entirety of the relevant period. Further, the conduct of directors is to be judged objectively, such that the position must be reasonable having regard to the existing circumstances of which a director is aware or ought to be aware.¹¹²

Departure prohibition orders

The Commissioner has broad powers to prohibit a taxpayer from departing Australia by issuing a departure prohibition order (**DPO**). He may do so where they are subject to a tax liability and the Commissioner believes that is desirable to do so to ensure they do not depart without discharging the

¹⁰³ *Taxation Administration Act 1953* (Cth) Sch 1 s 269-35(1).

¹⁰⁴ *Taxation Administration Act 1953* (Cth) Sch 1 s 269-35(2).

¹⁰⁵ *Taxation Administration Act 1953* (Cth) Sch 1 s 269-35(3A).

¹⁰⁶ *Taxation Administration Act 1953* (Cth) Sch 1 s 269-35(4). See, eg, *DCT v Saunig* (2002) 55 NSWLR 722; *Canty v DCT* (2005) 63 NSWLR 152.

¹⁰⁷ *DCT v George* (2002) 55 NSWLR 511; *Snell v DCT* (2020) 350 FLR 328; *Canty v DCT* (2005) 63 NSWLR 152.

¹⁰⁸ *DCT v Robertson* (2009) 234 FLR 35.

¹⁰⁹ *DCT v Lawson* [2017] VSC 789.

¹¹⁰ *DCT v Lawson* [2017] VSC 789.

¹¹¹ *Canty v DCT* (2005) 63 NSWLR 152, [38].

¹¹² See, eg, *DCT v Moss* (2002) 50 ATR 542; *Canty v DCT* (2005) 63 NSWLR 152.

liability or making satisfactory arrangements to discharge the liability.¹¹³ Where the Commissioner makes such an order, it remains in force unless and until revoked or set aside by the court.¹¹⁴

For the Commissioner to make a DPO, the recoverability of the tax liability must be affected by the departure of the taxpayer from Australia.¹¹⁵ As Einfeld J said in the case of Geoffrey Edelsten's DPO in the late 1980s:

*In other words, it is only the possibility or likelihood that the taxpayer's departure from Australia would adversely affect the revenue that there should be under this Act a restriction on the right of an individual in a free society to travel without bureaucratic impediment. The power to issue a DPO may not be exercised penally or for other purposes.*¹¹⁶

In every case, the Commissioner must consider whether the departure of the person will make it less likely that the tax liability will be discharged or that the Commissioner's ability to recover will be impaired.¹¹⁷ It appears that if the taxpayer has sufficient assets in Australia to meet their obligation, then the physical presence of the applicant would be redundant to the Commissioner's ability to recover.¹¹⁸ Further, the ability of the Commissioner to recover in a foreign jurisdiction is a relevant consideration.¹¹⁹

The Commissioner must revoke a DPO where the taxpayer discharges their tax liabilities and their future tax liabilities will be wholly discharged or completely irrecoverable, or where their existing tax liabilities are completely irrecoverable.¹²⁰ He may also revoke a DPO at his discretion.¹²¹

In some circumstances, the Commissioner may authorise the taxpayer to depart from Australia whilst maintaining the DPO. He will do so where he is satisfied that the person will return to Australia within an appropriate period and is either satisfied the tax liability and future tax liabilities will be discharged or be completely irrecoverable¹²². He will also do so where the taxpayer has given security, departure should be allowed on humanitarian grounds, or where refusal to allow departure would be detrimental to the interests of Australia.¹²³

¹¹³ *Taxation Administration Act 1953* (Cth) s 14S(1).

¹¹⁴ *Taxation Administration Act 1953* (Cth) s 14S(2).

¹¹⁵ *Skase v FCT* (1991) 32 FCR 206, 210-211.

¹¹⁶ *Edelsten v FCT* (1989) 20 ATR 238, 242.

¹¹⁷ *Troughton v DCT* (2008) 166 FCR 9, [22].

¹¹⁸ *Bakri v DCT* (2017) 104 ATR 773, [45].

¹¹⁹ *Bakri v DCT* (2017) 104 ATR 773, [46].

¹²⁰ *Taxation Administration Act 1953* (Cth) s 14T(1).

¹²¹ *Taxation Administration Act 1953* (Cth) s 14T(2).

¹²² *Taxation Administration Act 1953* (Cth) s 14U(1)(a).

¹²³ *Taxation Administration Act 1953* (Cth) s 14U(1)(b).

3. Managing Tax Debts and Other Measures

So, faced with that vast and terrifying power, what is a humble David to do?

The taxpayer should *not* approach the issue as the fictional Mr Pottifer did:

I think the reason lay partly in [Mr Pottifer's] idea of immortality, but I think too it belonged to his war against the Inland Revenue. He was a great believer in delaying tactics. "Never answer all their questions," he would say. "Make them write again. And be ambiguous. You can always decide what you mean later according to circumstances. The bigger the file the bigger the work. Personnel frequently change. A newcomer has to start looking at the file from the beginning. Office space is limited. In the end it's easier for them to give in." Sometimes, if the inspector was pressing very hard, he told me that it was time to fling in a reference to a non-existing letter... after a few years of Mr Pottifer, [the inspector] was quite liable to have a nervous breakdown.¹²⁴

As we have seen,¹²⁵ a taxpayer who has been assessed to tax is obliged to pay the outstanding amount whether or not they are disputing the assessment under Part IVC. Naturally, not every taxpayer (indeed, perhaps very few taxpayers faced with amended assessments) will be able to pay the tax straight away and there are cases where the Commissioner's pursuit of the assessed tax debt places severe strain on a taxpayer's business or deprives them of the resources with which to conduct Part IVC proceedings. This is especially so in cases of deemed income or "dry" tax events (i.e., events where a tax liability arises but there is no corresponding in-flow of cash that would otherwise have been available to satisfy the tax liability). It is therefore critical that the debt recovery process is managed in such a way that allows the taxpayer to pursue their Part IVC rights and, ideally, keep operating their business or avoid a fire sale of their assets.

Generally, the most effective way to navigate these issues is to take a pro-active, collaborative approach to the debt and the Commissioner. A taxpayer that is open and demonstrates that they take the debt seriously is less likely to be a risk of non-payment, which is relevant to the Commissioner's risk-based approach. Similarly, the Commissioner will often ask for information about the taxpayer's financial position, including their assets and liabilities, before deciding whether to accept a payment arrangement or security proposal. Taxpayers should complete this process thoroughly and honestly, lest (aside from the obvious moral and ethical imperative) an irregularity be discovered later on or they are required to present the information in an affidavit, which would result in a major deterioration in the relationship with the Commissioner.

It is also important to remember that the Commissioner is not an ordinary commercial counter-party, who would generally be outcome-focused. For the Commissioner, process is as important as the outcome, so that his powers are exercised in accordance with the law and his duty to collect taxes due is properly balanced against his duty to properly manage the tax system.¹²⁶ As a result, it is important to have regard to the Commissioner's current publications on his approach to debt recovery¹²⁷ and for any negotiations and agreement to be principles-based.

¹²⁴ Graham Greene, *Travels with My Aunt* (Vintage Books, 1999) 253-254.

¹²⁵ See, section 2.1 above.

¹²⁶ On the issues involved in this balancing exercise, see, Leibler, Mark, *Tax and the Rule of Law* (Speech, Melbourne Law School Annual Tax Lecture, 23 March 2022) <https://law.unimelb.edu.au/__data/assets/pdf_file/0005/4087391/Mark-Leibler-Paper-Version-Tax-and-the-Rule-of-Law8981853.2.pdf>.

¹²⁷ See, eg, PSLA 2011/4; PSLA 2011/14; PSLA 2011/16; PSLA 2011/17; PSLA 2011/18.

3.1 Undisputed debts

Payment arrangements

The Commissioner is empowered to:

- a. defer the time that a tax is due and payable;¹²⁸ or
- b. permit payment by instalments.¹²⁹

In the former case, the general interest charge (**GIC**) does not apply until the deferred date (if the debt remains unpaid at that time), whereas if instalments are permitted GIC will accrue on the unpaid part from the date the tax was first due and payable.

Deferrals are relatively rare and are intended for “debtors who can demonstrate that they are unable to pay by the due date but have the capacity to pay in full at a particular time in the future”.¹³⁰ Usually a taxpayer will have to demonstrate that payment has or will not be made on time because of circumstances beyond their control such as natural disasters, serious illness, legal impediments (e.g., probate not being granted), or embezzlement of the relevant funds.¹³¹ For example, a deferral was granted to all taxpayers in bushfire-affected postcodes in 2019-20.¹³²

It is important to note that a lodgement deferral and a payment deferral are separate decisions and it is necessary to request both if that is desired.

Instalment arrangements, on the other hand, are more common (although by no means agreed as a matter of course). It is preferable to apply for an instalment arrangement *before* the tax is first due, explaining the reasons it is required and accompanied by an initial payment that the taxpayer can afford to make at that time (or at least by the due date). These demonstrate the taxpayer’s genuine attempt to comply with their obligations as best they can.

The Commissioner will then consider the application in light of the taxpayer’s prior compliance history, their financial position, other recovery options and the circumstances of the case.¹³³ The Commissioner will form a view of the risk to the revenue that the taxpayer will be unable or unwilling to pay and an instalment arrangement “will not be accepted if prospects of recovery in the longer term would be diminished or the revenue would be disadvantaged”. Accordingly, taxpayers should demonstrate that they will be in a position to pay the tax debt, and accrued GIC, at a future point in time.

The Commissioner considers that he may terminate an instalment arrangement where the information provided to him in the application was false or misleading or the taxpayer fails to comply with either the instalment arrangement or their other lodgement or payment obligations.¹³⁴

For many, the Commissioner’s approach to payment arrangements in a post-COVID environment may come as a rude shock. Throughout the pandemic, he was extraordinarily lenient and put in place a range of administrative measures to assist taxpayers experiencing financial difficulty. Taxpayers were

¹²⁸ *Taxation Administration Act 1953* (Cth) Sch 1 s 255-10.

¹²⁹ *Taxation Administration Act 1953* (Cth) Sch 1 s 255-15.

¹³⁰ PSLA 2011/14, [31].

¹³¹ PSLA 2011/14, [32]-[34].

¹³² See, Australian Taxation Office, *Bushfires Affected Postcodes 2019-20* (Web Page, last modified 21 December 2021) <<https://www.ato.gov.au/general/support-in-difficult-times/natural-disaster-support/bushfire-support/bushfires-affected-postcodes-in-2019-20/>>.

¹³³ PSLA 2011/14, [61].

¹³⁴ PSLA 2011/14, [74].

encouraged to approach the Commissioner and he more readily agreed to payment deferrals, allowed changed reporting cycles and granted lodgement deferrals. He was also generally more inclined to remit interest and penalties incurred during the pandemic. With a small number of exceptions, the Commissioner also suspended most debt recovery activity.

However, these administrative arrangements were not automatically put in place and were generally only granted following an application by the taxpayer. Tax debts did not disappear. In the absence of appropriate arrangements with the Commissioner, tax debts continued to crystallise, remain outstanding, and accrue interest. In this sense, many tax debts, and the ATO's debt book more broadly, 'ballooned'. This leniency has since expired and the Commissioner is now looking to recover these accumulated debts. Taxpayers will need to be more proactive in managing their outstanding tax debts in this environment.

Non-pursuit and compromise

The Commissioner may elect to not pursue a debt if it is uneconomical to do so or irrecoverable at law.¹³⁵ In determining whether pursuit is economical, the Commissioner will consider the cost of recovery relative to the size of the recoverable debt, its age and its nature (e.g., the Commissioner is more likely to pursue superannuation guarantee charge because it benefits employees). Similarly, the Commissioner will not pursue debts that cannot be recovered by court action or are the balance left after a bankruptcy or insolvency process.

Alternatively, the Commissioner may compromise a debt by accepting part payment in full satisfaction of the debt.¹³⁶ The object of a compromise is to "secure the highest net return [to the Commonwealth] taking into account considerations of good management and/or administrative common sense" and, therefore, will not be made unless the result is better than the bankruptcy or insolvency process.¹³⁷

The Commissioner will consider a number of principles when deciding whether to agree to a compromise:

- a. he will not accept compromise proposals that offer less than the tax debtor's total net assets in full satisfaction of the debt;
- b. he will not accept compromise proposals unless there is a benefit in doing so over and above that from bankruptcy or insolvency;
- c. he must be able to quantify the tax debtor's total tax debt;
- d. he will neither prejudice other creditors' entitlements nor accept that other creditors can prejudice the Commissioner's entitlements;
- e. he will not consider requests for compromise where this may directly or indirectly impact on other actions involving the taxpayer or other parties;
- f. he cannot accept compromise proposals where the only reason to support the proposal is the taxpayer's hardship (see below regarding serious hardship applications);

¹³⁵ See, PSLA 2011/17.

¹³⁶ *Income Tax Assessment Act 1936* (Cth) s 8; *Public Governance, Performance and Accountability Act 2013* (Cth) s 15; *Public Governance, Performance and Accountability Rule 2014* (Cth) r 11. See also, *Grofam Pty Ltd v FCT* (1997) 36 ATR 493.

¹³⁷ PSLA 2011/3, [14].

- g. he will take into account the taxpayer's compliance history;
- h. he will not accept a compromise with taxpayer who can lodge an agreement under Part IX of the Bankruptcy Act; and
- i. he will not accept a compromise where, within the last five years, the taxpayer has entered into another compromise with the Commissioner, or been a bankrupt or party to certain agreements dealing with bankruptcy or insolvency.¹³⁸

One negotiating option that taxpayers should consider is the surrender of prior year losses in exchange for compromising a present debt.

It must be recognised that the Commissioner's requirements to reach a compromise mean that, if a compromise is agreed, the taxpayer may be or will be close to insolvent. Taxpayers should consider the risks that involves (including to the directors of corporate taxpayers) and the possibility that the compromise with the Commissioner is an unfair preference.¹³⁹

Release for serious hardship

The Commissioner has the power to release an individual or a deceased estate from liability to certain taxes and other liabilities, in whole or part, if the individual or dependants of the deceased (as the case may be) would suffer serious hardship from its payment.¹⁴⁰ When applying for release, it is important that a taxpayer is up to date with their lodgements and has no other outstanding tax issues.

Taxpayers need to meet a high bar for relief. The Commissioner takes the view that "serious hardship" means that paying the liability "would result in a person being without the means to afford basics such as food, clothing, medical supplies, accommodation or reasonable education".¹⁴¹ He applies three tests to establish whether this is the case:

- a. the income/outgoings test – a consideration of current income against outgoings and the prospect of those factors changing in the future;
- b. the assets/liabilities test – an assessment of the equity available to meet tax obligations (importantly, the Commissioner generally excludes an interest in the family home); and
- c. other relevant factors – such as the likely length of hardship, compliance history, steps taken to pay debts and any factors which may indicate manipulation of circumstances like disposing of assets or preferential payment of other debts.

Those tests are also accepted by the AAT.¹⁴²

Even having established that the taxpayer will suffer serious hardship, the Commissioner retains a discretion whether to grant relief.¹⁴³ This permits a wider consideration of the circumstances, including whether the taxpayer has been the "author of his own misfortune" through extravagant spending or otherwise being involved in the events leading to the tax liability being unpaid.¹⁴⁴

¹³⁸ See PSLA 2011/3.

¹³⁹ See, eg, *Smith v DCT (No 2)* (1997) 75 FCR 339. See also, PSLA 2011/3, [32]-[34].

¹⁴⁰ *Taxation Administration Act 1953* (Cth) Sch 1 ss 340-5, 340-10.

¹⁴¹ PSLA 2011/17, [8].

¹⁴² See, *Ballintine v FCT* (2021) 113 ATR 738, [15].

¹⁴³ *Powell v Evreniades* (1989) 21 FCR 252, 264.

¹⁴⁴ See, eg, *Ballintine v FCT* (2021) 113 ATR 738; *Rasmussen v FCT* (2013) 95 ATR 155.

A taxpayer who is dissatisfied with the Commissioner’s decision not to release them for hardship may object under Part IVC.¹⁴⁵

Ministerial waiver

The Finance Minister (and not the Commissioner) also has a power to waive debts due to the Commonwealth.¹⁴⁶ Naturally, this is rare.

The Commissioner recommends to the Minister whether to accept the waiver application. That is more likely to be supported where there is an inequitable result for which there is no other remedy.¹⁴⁷

3.2 Disputed debts

The processes outlined at section 3.1 above are also appropriate for disputed debts. In addition, there are other avenues more suited to the context of tax disputes.

50/50 arrangements

When there is a dispute concerning the underlying tax debt under Part IVC, the first port of call in any debt arrangement with the Commissioner is usually a “50/50 arrangement”. That is, the taxpayer will pay all undisputed debts and half of the disputed primary tax that has been assessed and in return the Commissioner will defer recovery action of, and remit half of the GIC on, the unpaid balance until the tax dispute is determined.¹⁴⁸

Whether a 50/50 arrangement will be offered is always subject to the Commissioner’s risk assessment and they will not be offered in the case of superannuation guarantee charge.

If a 50/50 arrangement has been in place at the objection stage, it will usually be extended for any further appeal to the Court or tribunal, unless a “substantially similar case” has been decided in favour of the Commissioner.¹⁴⁹

GIC incurred is allowable as a deduction¹⁵⁰ and remitted GIC is assessable as a recoupment.¹⁵¹ The Commissioner advises that taxpayers who are party to a 50/50 arrangement should claim the full GIC amount as a deduction in the year it is accrued and return the GIC remitted in the year the dispute is determined.¹⁵²

Taxpayers who wish to settle the underlying tax dispute should consider whether paying half of the disputed primary tax may influence settlement negotiations. It is a simple, yet perhaps unfortunate, feature of psychology that a person is unlikely to bargain away what they already hold. Whatever the qualities of the office of Commissioner, his officers are mortal with very human minds, and a taxpayer should anticipate that entering a 50/50 arrangement may indirectly anchor settlement negotiations.

¹⁴⁵ *Taxation Administration Act 1953* (Cth) Sch 1 s 340-5(7).

¹⁴⁶ *Public Governance, Performance and Accountability Act 2013* (Cth) s 63.

¹⁴⁷ PSLA 2011/17, [16]-[17].

¹⁴⁸ PSLA 2011/4, [27]-[28].

¹⁴⁹ PSLA 2011/4, [33]-[35].

¹⁵⁰ *Income Tax Assessment Act 1997* (Cth) s 25-5(1)(c).

¹⁵¹ *Income Tax Assessment Act 1997* (Cth) s 20-25(2A).

¹⁵² PSLA 2011/4, [38].

Other security arrangements

As an alternative to the 50/50 arrangement, the Commissioner may accept security over property in return for deferring debt recovery action whilst a dispute is on foot. Generally, this is more appropriate for taxpayers with significant assets to cover a tax debt but without the liquidity to pay the half required for a 50/50 arrangement. However, it does not necessarily enjoy the concessional GIC treatment that a 50/50 arrangement does.

Voluntary security is also often an effective way of having garnishee notices or freezing orders withdrawn by or with the consent of the Commissioner. However, we reiterate our comments that the value of security voluntarily given may have an indirect impact on any later settlement negotiations.

The Commissioner's preferred forms of security are mortgages over real property or bank guarantees (from the taxpayer or third parties).¹⁵³ All secured property has to be located in Australia and the taxpayer will be expected to meet all costs of the security and in connection with secured property.¹⁵⁴ The security arrangement will be documented in a deed.

Security arrangements can also be put in place in conjunction with payment deferrals or instalment arrangements for undisputed debts, although they are less suited to those cases where the Commissioner expects payment to be timely.

Combating DPOs and DPNs

DPOs and DPNs are usually deployed in cases where the Commissioner considers that there is a higher risk to the revenue. The obvious solution is to pay the whole tax debt, although this may not be possible. By at least taking steps to pay down tax debts and/or provide security, and in so doing demonstrating their co-operation, the risk assessment factors can shift in the taxpayer's favour and the Commissioner may be prepared to withdraw those notices.

In the case of DPOs, the taxpayer can challenge the decision to issue the DPO in the Court¹⁵⁵ or the refusal to either revoke the DPO or issue a departure authorisation certificate in the tribunal.¹⁵⁶ The challenge in the Court is principally against the "reasonable grounds" upon which the Commissioner based his decision to issue the DPO,¹⁵⁷ whereas the tribunal will remake the Commissioner's decision having regard to the matters detailed in s 14T or s 14U as relevant.

In the case of DPNs, a director may attempt to rely on one of the defences discussed above, although these are notoriously difficult to make out sufficiently.

The director can also:

- a. have the company pay the tax liability;
- b. appoint an administrator or small business restructuring practitioner; or
- c. appoint a liquidator to wind up the company.

Although, it must be recognised, this is hardly "combating" the DPN and more of an abject surrender.¹⁵⁸

¹⁵³ PSLA 2011/14, [87].

¹⁵⁴ PSLA 2011/14, [83].

¹⁵⁵ *Taxation Administration Act 1953* (Cth) s 14V.

¹⁵⁶ *Taxation Administration Act 1953* (Cth) s 14Y.

¹⁵⁷ *Poletti v Federal Commissioner of Taxation* (1994) 52 FCR 154, 159-160.

¹⁵⁸ The taxpayer should take heart that it is not the shortest action in history: the Anglo-Zanzibar War lasted for 38 minutes on 27 August 1896.

4. Small Business Restructuring

When all else fails, and the Commissioner cannot be persuaded to refrain from recovering a tax debt the taxpayer is unable to meet, the taxpayer will have to seriously consider administration, liquidation or similar processes. This paper is not intended as a detailed review of the law of insolvency or bankruptcy, which is its own area of specialisation. For our purposes, it is sufficient to summarise it thus: it is very, very bad, not least of which because it severely limits the taxpayer's ability to object to an assessment or appeal an objection decision.¹⁵⁹ However, there is a new process available that warrants some discussion.

Since 1 January 2021, there has been a simpler debt restructuring option open to eligible small businesses in addition to processes already available to insolvent or potentially insolvent companies. In the midst of the coronavirus pandemic, the government announced measures to allow small businesses to restructure their debts with the help of professionals and protections from creditors and other action, whilst still under the control of their directors. Complementary rules for more streamlined liquidation processes were announced at the same time. Between them, the reforms covered around 76% of businesses subject to insolvencies.¹⁶⁰

4.1 Eligibility criteria

Only companies governed by the *Corporations Act 2001* (Cth) may access the small business restructuring regime. They must also meet the following criteria:

- a. total liabilities must not exceed \$1,000,000 (excluding employee entitlements);¹⁶¹
- b. no director (or person who was a director in the last 12 months) was a director of another company that has been the subject of restructuring or simplified liquidation in the last seven years;¹⁶² and
- c. the company has not been the subject of restructuring or simplified liquidation in the last seven years.¹⁶³

If eligible, a company may begin the restructuring process by resolving that, in the opinion of the directors, the company is or is likely to become insolvent and to appoint a "small business restructuring practitioner". There are particular requirements to qualify as a small business restructuring practitioner and ASIC maintains a list of the people qualified.¹⁶⁴

¹⁵⁹ See, *McCallum v FCT* (1997) 75 FCR 458; *ACN 092 138 442 Pty Ltd v FCT* (2013) 95 ATR 976; *Pitman v FCT* (2021) 113 ATR 852.

¹⁶⁰ Treasury, 'Insolvency Reforms to Support Small Business Recovery' (Media Release, 24 September 2020).

¹⁶¹ *Corporations Act 2001* (Cth) s 453C(1)(a); *Corporations Regulations 2001* (Cth) r 5.3B.03(1).

¹⁶² *Corporations Act 2001* (Cth) s 453C(1)(b); *Corporations Regulations 2001* (Cth) r 5.3B.03(2). There is an exception for related companies that commence the restructuring or liquidation processes within 20 business days of each other: *Corporations Regulations 2001* (Cth) r 5.3B.03(4).

¹⁶³ *Corporations Act 2001* (Cth) s 453C(1)(c); *Corporations Regulations 2001* (Cth) r 5.3B.03(3).

¹⁶⁴ See, Australian Securities & Investments Commission, *Insolvency Statistics – Series 4A Registered Liquidator List* (Web Page, first published 1 November 2016) < <https://asic.gov.au/regulatory-resources/find-a-document/statistics/insolvency-statistics/insolvency-statistics-series-4a-registered-liquidator-lists/>>.

4.2 The restructuring process

The restructuring practitioner will work with the directors of the company to develop a restructuring plan to pay the company’s creditors (including the Commissioner) on a *pari passu* basis.¹⁶⁵ The directors are required to assist the restructuring practitioner, and it is a strict liability offence to fail to do so, with a penalty of 120 penalty units¹⁶⁶ (currently \$33,000).

The restructuring plan must be put to the company’s creditors within 20 business days, although that can be extended for 10 business days by the restructuring practitioner or for any period by the Court.¹⁶⁷ In that time, the company must ensure that it is substantially compliant with its obligations to pay employee entitlements and lodge returns, notices or other documents under the taxation law.¹⁶⁸

Amongst other things, the plan states the amount of liabilities outstanding for each creditor and the proportion they will be paid. This offers an opportunity for a creditor to dispute the relevant amount, and the *Corporations Regulations 2001* (Cth) include provisions concerning those disputes.

Creditors have 15 business days to vote on whether to accept the restructuring plan,¹⁶⁹ deciding by majority. Each creditor’s voting power is determined by the value of the debts they are owed and related creditors’ votes are disregarded.¹⁷⁰

Example 1

Creditor	Value of Debt	Votes For	Votes Against
Independent Creditor A	\$20,000		20,000
Independent Creditor B	\$5,000		5,000
Independent Creditor C	\$15,000	No vote received	
Commissioner of Taxation	\$30,000	30,000	
Related Creditor A	\$10,000	Interest disregarded	

In this example, the restructuring plan would be accepted with 54.5% of the vote (30,000 / 55,000). Note that the votes not received and the related creditor’s debt are not counted for the purposes of both the numerator and denominator when calculating a percentage.

A recent ASIC review of small business restructuring, reflecting on its first 21 months of operation, showed that there were 78 proposed restructuring plans, of which 72 were accepted (92%), and that the Commissioner was a creditor in 89% of those 72 cases.¹⁷¹

¹⁶⁵ *Corporations Act 2001* (Cth) s 453E.

¹⁶⁶ *Corporations Act 2001* (Cth) s 453F.

¹⁶⁷ *Corporations Regulations 2001* (Cth) r 5.3B.17.

¹⁶⁸ *Corporations Regulations 2001* (Cth) r 5.3B.24.

¹⁶⁹ *Corporations Regulations 2001* (Cth) r 5.3B.21.

¹⁷⁰ *Corporations Regulations 2001* (Cth) r 5.3B.25.

¹⁷¹ Australian Securities & Investments Commission, ‘Review of Small Business Restructuring Process’ (Report No 756, January 2023) 5-6.

4.3 Effect of small business restructuring

The most significant aspect of small business restructuring, at least in comparison with other processes available to distressed companies, is that the company remains in the control of its directors during the process.¹⁷² The company can continue to enter into transactions in the ordinary course of business, or other transactions with the approval of the restructuring practitioner or pursuant to court order.¹⁷³ The *Corporations Regulations* provide that a transaction to satisfy an admissible debt, the sale of all or part of the company's business and the payment of dividend are not transactions in the ordinary course of business.¹⁷⁴ Unauthorised transactions are void¹⁷⁵ and directors can be ordered to pay compensation where a void transaction results in loss to the company or another party.¹⁷⁶

The small business restructuring process also offers some important protections, similar to other restructuring processes:

- a. processes to wind up the company or appoint a liquidator will be put on hold if the Court considers it in the best interests of the creditors;¹⁷⁷
- b. secured creditors and owners of property leased to the company are restricted from enforcing their rights, unless with the consent of the restructuring practitioner or leave of the Court;¹⁷⁸
- c. proceedings against the company or its property are stayed (including claims from unsecured creditors), unless with the consent of the restructuring practitioner or leave of the Court;¹⁷⁹
- d. enforcement processes against the company are suspended, without leave of the Court;¹⁸⁰ and
- e. guarantees of the company's liabilities given by directors or their relatives cannot be enforced, without leave of the Court.¹⁸¹

¹⁷² *Corporations Act 2001* (Cth) s 453K.

¹⁷³ *Corporations Act 2001* (Cth) s 453L(1)-(2).

¹⁷⁴ *Corporations Regulations 2001* (Cth) r 5.3B.04.

¹⁷⁵ *Corporations Act 2001* (Cth) s 453L(5).

¹⁷⁶ *Corporations Act 2001* (Cth) s 453M.

¹⁷⁷ *Corporations Act 2001* (Cth) s 453Q.

¹⁷⁸ *Corporations Act 2001* (Cth) s 453R. For the circumstances in which secured creditors may still proceed see *Corporations Act 2001* (Cth) Ch 5 Pt 5.3B subdiv F.

¹⁷⁹ *Corporations Act 2001* (Cth) s 453S.

¹⁸⁰ *Corporations Act 2001* (Cth) s 453T.

¹⁸¹ *Corporations Act 2001* (Cth) s 453W.