



NEWS WITH CLOUT

Chartered Accountants for Business Recovery & Insolvency Services
April 2005

THE ATO'S 2nd BITE!

We recently came across the practical application of Section 588 FGA of the Corporations Act, which gave all other parties involved a bit of a shock!

The directors thought they were away and sailing. They had been hit with a director's penalty notice under Section 222 AOE of the Income Tax Assessment Act by the ATO, which you will recall gives the directors a number of options in the event of arrears in withholding tax. The directors had 4 choices:

1. Pay the debt; or
2. Go into liquidation; or
3. Enter into voluntary administration; or
4. Do a deal to pay the outstanding debt via instalments.

Something to keep in mind, the directors penalty notices are not only applicable to withholding tax arrears but also to other outstanding taxes.

As is often the case these directors did a deal with the ATO to repay the debt by instalments.

Shortly after they commenced the repayments, it appears they discovered that the financial position of the company was far worse than they had anticipated and that eventual failure was imminent.

They knew that if they closed at that time they would be personally liable for any instalments unpaid at closure, given the directors penalty notice. So they kept trading long enough to pay off the instalments. No doubt they also lived in hope that things may turnaround.

You have no doubt picked up that, by them

doing this they were exposing themselves to a potential insolvent trading action.

After repaying the ATO the company was eventually placed into liquidation which made the end result a little more clear cut than an insolvent trading action, which is notoriously difficult to successfully prosecute.

In this case the Liquidator was successful in recovering an unfair preference against the ATO, as the scenario was fairly clear-cut. The directors were then served with demands under Section 588 FGA, which gives the ATO the right to seek redress from directors for any repayments they are forced to disgorge to the Liquidator.

This is clearly something for advisors to think about when negotiating with the ATO, as a result of director's penalty notices.

Some questions that would be prudent to ask are:-

1. Is there going to be survival?
2. What got them into the position in the first place?
3. What has changed?
4. Would voluntary administration really impact that dramatically on their goodwill?

Remember failure inside 6 months of an instalment plan keeps the directors at risk.

Tough Isn't It!

As ever we are always happy to entertain your enquiries without obligation.



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