Illegal Phoenix Activity: Practical Ways to Improve the Recovery of Tax

Helen Anderson*

Abstract

Illegal phoenix activity generally involves closing one debt-laden company and continuing its business through another company minus those debts. Its propensity to cause losses of federal revenue has recently been highlighted by the Australian Government Treasury announcement of a suite of measures to combat it. However, there is already an extensive array of legislative and administrative tools that are available against illegal phoenixing. This article considers both the existing and proposed measures and makes some practical suggestions to improve the recovery of tax. However, solutions are not found exclusively in tax law and its administration. Since illegal phoenix activity is facilitated by the creation and demise of companies and their controllers are regulated by the *Corporations Act 2001* (Cth), suggestions are made regarding corporate law and its administration by the Australian Securities and Investments Commission.

I Introduction

The ability of the Australian Taxation Office ('ATO') and state revenue offices to collect taxation is inevitably impacted by the form of the entity that owes the obligation.[1] This article[2] takes a slice of those entities — Australian registered companies — and considers how deliberately contrived corporate insolvency affects tax-debt recovery. In particular, it concentrates upon illegal phoenix activity as a device to out-manoeuvre the ATO's attempts to recover tax from micro and small companies. Illegal phoenix activity has recently been the focus of policy announcements by the Minister of Revenue.[3] The most significant proposals made

* Professor, Melbourne Law School, University of Melbourne, Victoria, Australia. The research reported in this article was funded by the Australian Research Council: DP140102277, 'Phoenix Activity: Regulating Fraudulent Use of the Corporate Form' (Chief Investigators: Helen Anderson, Ann O'Connell, Ian Ramsay, Michelle Welsh).

1 For statistics as to the different kinds of taxpayer entities that exist, see ATO, *Statistics* (11 January 2018) <https://www.ato.gov.au/About-ATO/Research-and-statistics/In-detail/Taxation-statistics/Taxation-statistics-2014-15/?page=3#Statistics>.

2 Some of the suggestions contained in this article are derived from Helen Anderson et al, *Phoenix Activity: Recommendations on Detection, Disruption and Enforcement* (Research Report, Centre for Corporate Law and Securities Regulation, The University of Melbourne, February 2017) ('*Phoenix Recommendations Report*').

3 Kelly O'Dwyer (Minister for Revenue and Financial Services), 'A Comprehensive Package of Reforms to Address Illegal Phoenixing' (Media Release, 12 September 2017).

in the Australian Government Treasury ('Treasury') *2017 Combatting Illegal Phoenixing* consultation paper[4] will be critiqued in this article.

In its simplest form, illegal phoenix activity involves the directors of one company deliberately closing it down and transferring its business to another company, either newly formed or already in existence. The aim is to avoid the business having to pay its debts, as they remain quarantined in, and unrecoverable from, the insolvent company. An employer operating their business as a sole trader, or through a partnership or trust, will be personally liable for these amounts even if the business cannot afford it, because 'the business' is not a separate legal entity. Some debts even survive the individual's bankruptcy.[5] On the other hand, a company, as a separate legal entity, can be liquidated or simply deregistered. The ATO's Commissioner of Taxation is a non-priority unsecured creditor in any liquidation, and is likely to suffer significant losses.[6] This creates a temptation for company controllers to accrue these corporate tax debts and then to allow the company to fail when the ATO tries to bring it to account.

Several recent scandals[7] involving illegal phoenix activity have heightened the need for action. At present, enforcement actions may be frustrated by a debt-laden company removing its genuine directors and appointing a 'man of straw' prior to a regulator taking action, with the new appointment backdated by a number of years. An example of this occurred in 2016, when the homeless client of an accounting firm was allegedly registered, without his knowledge or consent, as a director of a number of companies with outstanding ATO debts. He was then issued director penalty notices ('DPN') by the ATO, making him personally liable for the company's unremitted taxes. In some instances, the accounting firm had backdated the directorship up to five years.[8]

Where the company's assets are insufficient to meet the claims of revenue authorities as unsecured creditors, other measures need to be found. Actions against

---

4 Australian Government, Treasury, *Combatting Illegal Phoenixing*, September 2017.

5 *Bankruptcy Act 1966* (Cth) s 82. Penalties and fines, for example, are not provable (and are, thus, not extinguished) in bankruptcy, nor are various study support debts owed to the Government.

6 The 2016–17 collation of external administrator data shows that unpaid taxes occur in 85.5% of insolvencies (ie, in 14.5% of insolvencies, there are no unpaid taxes): Australian Securities and Investments Commission, *Report 558 Insolvency Statistics: External Administrators' Reports (July 2016 to June 2017)* (2017) 50 (table 39) ('*ASIC Report 558*'). ASIC provides no separate data on illegal phoenix activity so this figure relates to corporate insolvencies as a whole.

7 See the Plutus allegations discussed in Neil Chenoweth and David Marin-Guzman, 'ATO Tax Fraud: Behind a $191m Gen Y Crime Wave', *Australian Financial Review* (online), 3 July 2017 <http://www.afr.com/news/policy/tax/ato-tax-fraud-behind-a-191m-gen-y-crime-wave-20170630-gx1xjg>. See also the series of allegations against Philip Whiteman: Dan Oakes and Sam Clark, 'Staggering Number of Alleged Crimes in Massive Tax Scam', *ABC News* (online), 16 June 2017 <http://www.abc.net.au/news/2017-06-15/documents-lay-bare-staggering-number-of-alleged-crimes-in-scam/8620756>; Dan Oakes and Sam Clark, 'Melbourne Man Identified in Multi-Million Dollar Tax Evasion Investigation Still in Business', *ABC News* (online), 7 February 2017 <http://www.abc.net.au/news/2017-02-06/melbourne-man-linked-to-tax-avoidance-still-in-business/8244850>.

8 Dan Oakes and Sam Clark, 'Melbourne Man Linked to Alleged Tax Evasion Scheme Previously Accused of Ripping Off Investors' *ABC News* (online), 17 October 2016 <http://www.abc.net.au/news/2016-10-17/unwitting-clients-signed-up-as-directors-to-failing-businesses/7939622>; ABC, 'Unwitting Clients Signed up as Directors to Failing Businesses', *7.30 Report*, 17 October 2016 (Dan Oakes) <http://www.abc.net.au/7.30/unwitting-clients-signed-up-as-directors-to/7940908>.

third parties, including holding companies,[9] are limited, so if recovery is to be obtained, an alternative means can be actions against the company's directors, officers or advisors, either via primary liability or as an accessory to the company's liability for non-payment. However, enforcement actions alone are not enough; measures to prevent, disrupt and deter illegal phoenix activity are also needed to protect tax revenue.

There are no provisions in either company law or taxation law that expressly address illegal phoenix activity; what makes the phoenix activity illegal is a breach of some other provision that can be utilised against that behaviour. These mechanisms have not been entirely successful for reasons that this article will explain,[10] and this article proposes some ways in which these can be improved. In addition, because phoenix activity is essentially a process governed by corporate law — liquidating or abandoning one company and transferring the company's business to another company — this article suggests that some of the means of addressing tax losses caused by illegal phoenix activity can be found in corporate law, either as it presently exists or as it might be amended. This article also argues that improvements to the administrative arrangements involving the registration of companies and the appointment of their directors can have benefits for the ATO and state revenue authorities.

Part II provides the background to illegal phoenix activity and the ATO's ongoing concern about it. Part III looks at existing tax mechanisms available to tackle illegal phoenix activity and what might be done to improve them. These include administrative remedies like the imposition of a DPN, as well as possible criminal accessory liability under both the *Taxation Administration Act 1953* (Cth) ('*TAA*') and the *Crimes (Taxation Offences) Act 1980* (Cth) ('*CTOA*'). Suggestions for improvements, such as extending 'single touch payroll', are also considered here, and take into account the Treasury Laws Amendment (2018 Measures No 4) Bill 2018 ('TLA 2018 Super Measures Bill'), which, at the time of writing, was being considered by the Senate Economics Legislation Committee. Part IV sketches the range of existing corporate law actions available to creditors such as revenue authorities, before suggesting what might be done to expand them. However, in the interests of length and coherence, the article does not explore the possibilities of corporate third-party liability.[11] Part V concludes that improvements to existing tax and corporate legislation, as well as administrative reforms to processes controlled by the Australian Securities and Investments Commission ('ASIC') and the ATO,

---

9 See Jason Harris and Anil Hargovan, 'Corporate Groups: The Intersection between Corporate and Tax Law — *Commissioner of Taxation v BHP Billiton Finance Ltd*' (2010) 32(4) *Sydney Law Review* 723 and references cited therein. The Commissioner's appeal to the High Court to pierce the veil on intragroup financing arrangements was dismissed: *Commissioner of Taxation v BHP Billiton Ltd* (2011) 244 CLR 325. There is limited recovery for group payroll tax obligations under various state revenue laws. In addition, s 588V of the *Corporations Act 2001* (Cth) ('*Corporations Act*') imposes liability on a holding company for the insolvent trading of its subsidiary in specified circumstances. These will not be considered further in this article.

10 See further Colin Anderson, Jennifer Dickfos and Catherine Brown, 'The Australian Taxation Office — What Role Does it Play in Anti-Phoenix Activity?' (2016) 24(2) *Insolvency Law Journal* 127.

11 These include provisions adapted from chain-of-responsibility laws, security-of-payments laws, holding company liability, workplace health and safety law, 'person conducting a business or undertaking' and the *Fair Work Amendment (Protecting Vulnerable Workers) Act 2017* (Cth).

could significantly improve tax collections currently adversely affected by illegal phoenix activity.

II Background

It is not illegal for a company to fail owing unpaid debts. In the absence of wrongdoing of some kind,[12] the company's directors and officers should not be penalised when this happens. Detection and enforcement action against company directors and officers is difficult because it is the often well-disguised wrongdoing that attracts personal liability, not the externally visible evidence of corporate failure. As a result, where non-payment of tax is the directors' intention, it is much simpler for the company to properly incur the liability, then liquidate and transfer their business elsewhere, rather than devising a scheme to avoid incurring a tax liability that might stray into tax avoidance. These tax-related liabilities include the company's income tax, goods and services tax ('GST'), unremitted Pay-As-You-Go (Withholding) ('PAYG(W)') deductions, and unpaid superannuation ('super') obligations. This is the realm of illegal phoenix activity, where, as the ATO description states, 'a new company is created to continue the business of a company that has been deliberately liquidated to avoid paying its debts, including taxes, [unsecured] creditors and employee entitlements'.[13]

Clearly, this is not an option for a large company, which would suffer too much reputational damage if it were liquidated and replaced by a resurrected or 'phoenix' version of itself. However, it is certainly an option for a micro or small company, where one or more successor companies are used to maintain the business. Often the company's controlling individual and their contacts are the essence of the business. The liquidation of the actual proprietary limited company that owns the business and the creation of its replacement may go unnoticed by customers and suppliers, and even by employees in some cases. Illegal phoenix activity can also take place within corporate groups where the subsidiary of a large company is placed into liquidation. The group may be arranged in such a way that one company accrues tax liabilities (for example, a labour hire entity accruing PAYG(W) and super liabilities) and is then liquidated with its functions taken over by another company in the group. Again, this process can be repeated multiple times, deliberately to avoid payment of federal and state revenue obligations. In a similar way, supply chains can be used so that a small, dispensable company employs the workers and accrues the various liabilities, quarantining from liability the large company at the end of the

---

12 This is most likely to be a breach of directors' duties, discussed below in Part IVA(3).

13 ATO, *Illegal Phoenix Activity* (16 March 2018) <https://www.ato.gov.au/General/The-fight-against-tax-crime/Our-focus/Illegal-phoenix-activity/>. Each agency within the Inter-Agency Phoenix Forum has a slightly different definition, depending on which of their own areas are impinged upon. See ATO, *Inter-Agency Phoenix Forum* (25 September 2014) <https://www.ato.gov.au/General/The-fight-against-tax-crime/In-detail/Inter-Agency-Phoenix-Forum/Inter-Agency-Phoenix-Forum/>. Here, the ATO description is narrower: 'We define fraudulent phoenix activity as the evasion of tax and or superannuation guarantee liabilities through the deliberate, systematic and sometimes cyclic liquidation of related corporate trading entities.'

chain that benefits from their labour.[14] Another scenario involves a business being transferred to a new company with the old company simply abandoned by its management without being liquidated,[15] and eventually deregistered by ASIC.[16]

This is not to imply that the corporate form is the sole means of avoiding what is essentially a sole trader business from paying its tax obligations. Individuals operating outside of the corporate context can engage in personal asset protection strategies — putting assets into the name of a spouse or a family trust, for instance. However, the process may nonetheless leave the individual a bankrupt with all the stigma, practical difficulties and disruption to credit-worthiness that bankruptcy entails.[17] Much of this unpleasantness is avoided by those conducting their business through a company.

The ATO enjoys privileges as a creditor from its status as a regulator, such as enhanced access to information including investigative powers, criminal sanctions that deter non-compliance, and a range of specific mechanisms.[18] In each case, the ATO has the financial resources to use these powers that other unsecured creditors may not have. On the other hand, its suffers from some particular disadvantages, including a complex taxpaying population, an inability to refuse to deal with known recalcitrant taxpayers, a frequent lack of knowledge of what is owing and by whom,[19] its position as a deliberate target of illegal phoenix activity, and its requirement to act as a model litigant.[20]

---

14 See, eg, Tess Hardy and John Howe, 'Chain Reaction: A Strategic Approach to Addressing Employment Noncompliance in Complex Supply Chains' (2015) 57(4) *Journal of Industrial Relations* 563.

15 *Corporations Act* s 601AB.

16 Note that under *Corporations Act* s 601AH(5), a deregistered company can be reinstated to pay debts, but some companies are abandoned because they lack sufficient assets to make the appointment of a liquidator financially viable. In such cases, it is unlikely that reinstatement will be a productive exercise.

17 See Australian Financial Security Authority, *What Are the Consequences of Bankruptcy?* (2016) <https://www.afsa.gov.au/insolvency/i-cant-pay-my-debts/what-are-consequences-bankruptcy>. An undischarged bankrupt is automatically disqualified from managing a company: *Corporations Act* s 206B(3).

18 These include departure prohibition orders under the *TAA* pt IVA; garnishee orders, where the Commissioner of Taxation can require that monies payable to, or held on behalf of, a person with a tax debt (eg by banks and other financial institutions) be paid to the ATO under *TAA* sch 1 s 260-5. See, eg, *Bruton Holdings Pty Ltd (in liq) v Federal Commissioner of Taxation* (2009) 239 CLR 346; *Federal Commissioner of Taxation v Park* (2012) 205 FCR 1. Also available are freezing orders (Mareva injunctions) under *Federal Court Rules 2011* (Cth) r 7.32; and *Pay As You Go Withholding Non-compliance Tax Act 2012* (Cth) s 3, which imposes tax per *TAA* sch 1 sub-div 18D on directors and their associates claiming PAYG(W) credits on amounts that were not remitted to the ATO. Other employees can claim these amounts notwithstanding non-remittance. The ATO's powers are detailed in ATO, *Practice Statement Law Administration: Enforcement Measures Used for the Collection and Recovery of Tax-Related Liabilities and Other Amounts*, PS LA 2011/18, 3 July 2014, annexure F <http://law.ato.gov.au/atolaw/view.htm?Docid=PSR/PS201118/NAT/ATO/00001>. See also Anderson, Dickfos and Brown, above n 10, and references cited therein; Sylvia Villios, 'Tax Collection, Recovery and Enforcement Issues for Insolvent Entities' (2016) 31(3) *Australian Tax Forum* 425.

19 See further David Morrison, 'Floundering around the Phoenix: Is it Possible to Use Court Proceedings Effectively?' (2015) 23(3) *Insolvency Law Journal* 143.

20 ATO, *Practice Statement Law Administration: Conduct of ATO Litigation and Engagement of ATO Dispute Resolution*, PS LA 2009/9, 19 December 2013. See also Australian Government, Attorney-General, *Legal Services Directions 2017* (Cth), app B.

The extent to which illegal phoenix activity impacts upon tax collection is not known, but estimates of the cost of lost tax revenue are high. In November 2009, Treasury released its *Action against Fraudulent Phoenix Activity: Proposals Paper*,[21] which estimated that to be $600 million — although the paper did not state the method of calculation of this figure. In 2012, PricewaterhouseCoopers estimated that illegal phoenix activity costs the Australian economy up to $3.19 billion per year.[22] A 2017 paper released by the Federal Government concluded that 'the incidence of illegal phoenix company activity, and the subsequent costs to the FEG [Fair Entitlements Guarantee] scheme, is increasing'.[23] Therefore, despite a lack of precision about the cost of illegal phoenix activity to tax revenues, it is clear from these estimates and the ATO's commitment to the Inter-Agency Phoenix Forum[24] and Phoenix Taskforce[25] that the losses are sufficiently concerning to look at ways to address the damage caused by illegal phoenix activity. The next part of this article will look at the existing tax mechanisms available and what might be done to improve them.

III Existing Tax Mechanisms and Ways to Improve Them

As noted above, the ATO has a number of ways in which it may recover unpaid taxes,[26] and these cover circumstances much broader than illegal phoenix activity. This discussion will concentrate on those most relevant to recovery from individuals involved in illegal phoenix activity and make suggestions for their reform. The provisions contained in the TLA 2018 Super Measures Bill will be considered only to the extent that they are pertinent to this discussion.

A *Director Penalty Notice Regime*

1 *Reform the DPN Regime to Address Illegal Phoenix Activity*

Employers, incorporated or not, are obliged to remit PAYG(W) to the ATO at periodic intervals, having withheld these taxation amounts from the pay-packets of their employees.[27] They are also obliged to remit super to their employees' nominated funds, failing which the employer becomes liable for the super guarantee charge.[28] In exchange for giving up priority creditor status for these and certain other

21 Australian Government, Treasury, *Action against Fraudulent Phoenix Activity: Proposals Paper*, 2009, 5 [2] ('*2009 Phoenix Proposals Paper*').
22 PricewaterhouseCoopers for the Fair Work Ombudsman, *Phoenix Activity: Sizing the Problem and Matching Solutions* (June 2012) 2.
23 Australian Government, Treasury and Department of Employment, *Reforms to Address the Corporate Misuse of the Fair Entitlements Guarantee Scheme: Consultation Paper* (May 2017) 5.
24 ATO, *Inter-Agency Phoenix Forum*, above n 13.
25 ATO, *Phoenix Taskforce* (4 May 2018) <https://www.ato.gov.au/General/The-fight-against-tax-crime/Our-focus/Illegal-phoenix-activity/Phoenix-Taskforce/?=redirected>.
26 See above n 18.
27 *TAA* sch 1 s 6-5(2).
28 *Superannuation Guarantee (Administration) Act 1992* (Cth) pt 3.

unpaid taxes,[29] the director penalty regime was introduced in 1993.[30] Currently, the *TAA* sets out the director's duty to 'cause the company to comply with its obligation' to remit the PAYG(W) and super.[31] Directors become liable for a penalty through the issuance of a DPN if they do not cause the company to make these payments or liquidate it or place it into voluntary administration ('VA') within 21 days.[32] The regime's conditions are stringent[33] and its defences are very narrowly articulated[34] and strictly construed.[35] Directors caught by the DPN regime cannot be granted relief for breach of duty.[36] However, they can completely avoid personal liability by placing the company into external administration within the time specified, no questions asked, no matter what their motivation in doing so.

From a policy perspective, the DPN regime appears to capture either the non-compliant company or its director. While in neither case is there an absolute obligation to pay, the regime is aimed at ensuring that accruing corporate PAYG(W) tax debts and super debts are dealt with promptly. This is an appropriate approach where the intention of the law is to remind directors not to let tax liabilities mount up through inadvertence.[37] It appears to assume that directors otherwise want to save

---

29 Insolvency (Tax Priorities) Legislation Amendment Bill 1993 (Second Reading): Commonwealth, *Parliamentary Debates*, House of Representatives, 27 May 1993, 1124–5 (George Gear, Assistant Treasurer). See further Helen Anderson, 'Directors' Liability for Unpaid Employee Entitlements: Suggestions for Reform Based on their Liabilities for Unremitted Taxes', (2008) 30(3) *Sydney Law Review* 470, 480–1.

30 The legislation introducing the DPN regime was the *Insolvency (Tax Priorities) Legislation Amendment Act 1993* (Cth), with the relevant provisions then located in div 8 (ss 222AFA–222AMB) and div 9 (ss 222ANA–222AQD) of pt VI of the *Income Tax Assessment Act 1936* (Cth). In 2010, the laws were moved to the *TAA* sch 1 div 269. Originally, the obligation only applied to unremitted PAYG(W); unremitted super was added in 2012: *Tax Laws Amendment (2012 Measures No 2) Act 2012* (Cth), sch 1 pt 3.

31 *TAA* sch 1 div 269-15. In addition to known amounts of unremitted taxes, estimates are also included: *TAA* sch 1 div 268. The TLA 2018 Super Measures Bill, sch 5 pt 2 has proposed amendments to tighten the estimates process. Directors will face 'lockdown' DPN liability where an estimate has been required because of a failure to lodge a super guarantee charge statement: TLA 2018 Super Measures Bill sch 5 pt 2 ss 9–11, which proposes to amend *TAA* sch 1, s 269-30.

32 *TAA* sch 1 s 269-20. Voluntary administration aims to save the company or its business to maximise the returns to creditors: *Corporations Act* s 435A.

33 Note also the strict procedural underpinnings of div 269. For example, notice is taken to be given when the Deputy Commissioner of Taxation posts it: *TAA* sch 1 s 269-25(4). As a result of this, the risk that the notice is lost in the post is on the director: *Roche v Deputy Commissioner of Taxation* [2015] WASCA 196 (24 September 2015).

34 For example, the director must prove that they took all reasonable steps to ensure compliance or to wind up the company, or that there were no reasonable steps that could be taken: *TAA* sch 1 s 269-35(2)(a). See *Deputy Commissioner of Taxation v Saunig* (2002) 55 NSWLR 722, 730–31 [28]; *Roche v Deputy Commissioner of Taxation* [2015] WASCA 196 (24 September 2015). See further Sylvia Villios, 'Director Penalty Notices — Promoting a Culture of Good Corporate Governance and of Successful Corporate Rescue Post Insolvency,' (2016) 25(1) *Revenue Law Journal* Article 2, 10–11.

35 It still applies to directors who have retired: *Deputy Commissioner of Taxation v Power* (2012) 273 FLR 35, 364 [51]. See further Matthew Broderick, 'Company Directors: Federal Taxation Liabilities and Obligations When Nearing Insolvency — Part 1' (2009) 38(1) *Australian Tax Review* 7, 12.

36 *TAA* sch 1 s 269-35(5) disallows courts from granting relief under s 1318 of the *Corporations Act* for a breach of the DPN provisions.

37 The stated aim of the DPN legislation was to 'ensure solvency problems are confronted earlier and the escalation of debts will be prevented': Second Reading Speech to the Insolvency (Tax Priorities) Legislation Amendment Bill 1993: Commonwealth, *Parliamentary Debates*, House of Representatives, 27 May 1993, 1125 (George Gear, Assistant Treasurer).

their companies. Yet it fails to deal with those who accrue liabilities and then intentionally liquidate their companies to avoid paying them. Incorporating a new company is well worth the effort when many thousands of dollars of company tax liabilities can be avoided. Given the present undemanding incorporation regime in Australia,[38] the only inconvenience for the director is a fee of $479.[39] As a strict liability provision, the DPN regime saves the court or the ATO having to establish fault. However, in doing so, it fails to achieve deterrence of misconduct or punishment of those who use the corporate form deliberately to avoid corporate taxation liabilities.

In many instances, amounts of unremitted PAYG(W) and super were neither paid nor reported, so in 2012, laws amended the DPN regime to create 'lockdown' DPNs.[40] If the amount owing is not reported, the director loses their right to use the external administration 'escape route' that is available for reported obligations under 'standard' DPNs. In other words, provided the ATO becomes aware of the amount owing from some means *other than* reporting by the employer and then sends the DPN, the directors must pay the company's PAYG(W) and super obligations and cannot avoid these by placing the company into external administration.[41]

Nonetheless, a scheme to accumulate (and report) tax and super debts via a series of companies that are then promptly liquidated escapes the DPN regime. The *2017 Combatting Illegal Phoenixing* consultation paper proposal that the ATO should be empowered to commence immediate recovery action against designated 'High Risk Phoenix Offenders' ('HRPOs')[42] following the issuance of a DPN is, therefore, likely to be only partly successful because it is still based on the ability to issue a DPN. The director of a company placed into liquidation or VA prior to the receipt of the DPN does not appear to be caught.

To overcome the deficiencies with the DPN as a mechanism against illegal phoenix activity, one would need to look at the actual behaviour of the directors and whether they had failed to act properly. A focus on behaviour would obviate the need for the generous external administration 'escape clause', yet would allow flexibility through the court's ability to grant relief for breach of duty if appropriate. This is certainly achievable. In the UK, officers of a company may be liable under a personal liability notice ('PLN') where the company has failed to remit employees' Pay As You Earn ('PAYE') deductions and national insurance contributions ('NIC').[43] Unlike the Australian DPN, the UK PLN can only be issued where 'the failure appears to the [Inland Revenue] to be attributable to fraud or neglect on the

[38] ASIC, *Steps to Register a Company* (10 May 2018) <http://asic.gov.au/for-business/starting-a-company/how-to-start-a-company/>.

[39] ASIC, *Forms: 201 Application for Registration as an Australian Company* (8 February 2018) <http://asic.gov.au/regulatory-resources/forms/forms-folder/201-application-for-registration-as-an-australian-company/>.

[40] *Tax Laws Amendment (2012 Measures No 2) Act 2012* (Cth) sch 1 pt 1 div 3, which amended *TAA* sch 1 s 269-30(2) table items 1 and 2. See further Helen Anderson, 'The Proposed Deterrence of Phoenix Activity: An Opportunity Lost?' (2012) 34(3) *Sydney Law Review* 411, 416–18.

[41] *TAA* sch 1 s 269-30 (2).

[42] *2017 Combatting Illegal Phoenixing*, above n 4, 30. For the two-step process to become an HRPO, see further 25–6.

[43] *Social Security Administration Act 1992* (UK) s 121C.

part of one or more individuals who, at the time of the fraud or neglect, were officers of the body corporate ("culpable officers")'.[44] The UK Government website states:

> It is important that HMRC acts to protect directors of genuinely failed businesses and those who are regarded to have taken all reasonable steps to prevent or minimise the company Income Tax PAYE and NIC liabilities from the scope of this legislation. Therefore before a Personal Liability Notice is authorised a thorough enquiry will always be undertaken by trained specialist officers to establish the specific facts and circumstances behind the company failure to pay. They will establish whether there is sufficient evidence for HMRC to prove 'on the balance of probabilities' that the failure to pay was attributable to fraudulent intent or negligent conduct. …
>
> A case may … be judged to involve more serious neglect where 'culpable officers' have been associated with previous liquidated companies or other companies that have demonstrated a failure to comply with the statutory requirements of the Income Tax PAYE and NIC legislations.[45]

The Australian Government should consider whether the DPN regime might be altered to follow the UK example. The present DPN misses the deliberate, calculating phoenixer who reports liabilities and then ensures a prompt liquidation. However, it captures the overwhelmed business person who has simply failed to remit company taxes as required or to appoint a liquidator. While this may result in fewer DPNs, the UK approach would provide a more effective weapon against illegal phoenix activity. It is also worth looking at the extension of the DPN regime to cover GST and state taxes such as payroll tax. These will now be considered.

2 *Expand the DPN Regime to the Goods and Services Tax*

One of the issues contained in the *2017 Combatting Illegal Phoenixing* consultation paper was that directors should be made liable for their company's GST liabilities through the director penalty regime.[46] This is a worthwhile suggestion and it was also a recommendation of Treasury's *2009 Phoenix Proposals Paper*.[47] One of the concerns is that GST is not payable until the sale of the finished item has taken place, but that input tax credits can be claimed prior to that time. This is a particular concern in the building and construction industry, where the ATO estimated that it had

---

[44] Ibid s 121C(1)(b).

[45] United Kingdom ('UK'), HM Revenue and Customs, *National Insurance Manual* (15 June 2017), NIM12206 Class 1: Personal Liability Notices: Considering Issue of a PLN <https://www.gov.uk/hmrc-internal-manuals/national-insurance-manual/nim12206>.

[46] *2017 Combatting Illegal Phoenixing*, above n 4, 19.

[47] *2009 Phoenix Proposals Paper*, above n 21, 14–15 [4.2.2]. This was also a recommendation of the Senate committee inquiry into insolvency in the building and construction industry: Senate Economics References Committee, Parliament of Australia, *'I Just Want to be Paid': Insolvency in the Australian Construction Industry* (2015) 119 [7.47] recommendation 19 ('*SERC Construction Insolvency Report*').

'written off $10.8 billion over the last 10 years'[48] in unrecovered GST from about 30 000 entities.[49]

However, the Australian Government Inspector-General of Taxation recommended against the inclusion of the GST in the DPN regime on the basis that:

> it would effectively elevate the … Government's standing against employees and other creditors. Such an outcome is contrary to the Government adoption of the recommendations of the 1988 Harmer Report which supported the removal of Commonwealth priority in relation to tax …[50]

Including the GST in the DPN does not elevate the Government's standing against employees and other creditors. Employees remain statutory priority creditors in a liquidation, with payment of their entitlements *from the company's assets* ranking behind secured creditors and the costs of the administration. The DPN regime imposes liability for unremitted PAYG(W) and super on the directors — an additional and separate source of payment. The most that adding GST to the DPN regime would do is to increase the amount payable by the director.[51] In the event that a larger DPN liability drove the director into personal bankruptcy, it could adversely affect employees. This is because although employee entitlements are priority payments under the company's liquidation, there is no such express statutory priority regime when PAYG(W) and super amounts are recovered from the bankruptcy of a company director under mechanisms such as a DPN.[52] While this could be addressed with specific amendments to the bankruptcy priorities, it would be a radical departure from the status quo.

3 *Expand the DPN Regime to Cover State Taxes*

States should consider the introduction of a DPN provision for state tax liabilities.[53] In New South Wales ('NSW'), Revenue NSW (formerly the Office of State Revenue) may issue a compliance notice, like a DPN, to a director in respect of unremitted payroll taxes.[54] As with a DPN, liability is avoided where the company is placed into VA or liquidation within 21 days.[55] Western Australia has somewhat different provisions, imposing joint and several liability for taxes where there has

48 See ATO, *Inter-Agency Phoenix Forum Minutes — 12 November 2013* (14 October 2015), item 7 <https://www.ato.gov.au/General/The-fight-against-tax-crime/In-detail/Inter-Agency-Phoenix-Forum/Inter-Agency-Phoenix-Forum-minutes---12-November-2013/>.

49 For an example of the Commissioner's ability to overcome a sham structure designed to defraud the Commissioner of GST revenue, see *Sunraysia Harvesting Contractors Pty Ltd (Trustee) v Commissioner of Taxation* (2017) 105 ATR 907.

50 Australian Government, Inspector-General of Taxation, *Debt Collection: A Report to the Assistant Treasurer* (July 2015) ('*IGT Debt Collection Report*') [4.52].

51 *Phoenix Recommendations Report*, above n 2, 73.

52 The priority payment regime of the *Bankruptcy Act 1966* (Cth) s 109(1)(e) and (g) refers to employees 'of the bankrupt'. Otherwise, debts rank equally and are paid proportionately if there is an insufficiency of assets: s 108. See further Anderson, Dickfos and Brown, above n 10, 135.

53 For example, at the end of the 2015–16 financial year, the Victorian State Revenue Office was owed $204 581 322 in unpaid taxes: State Revenue Office Victoria, *Analysis of Debt*, Annual Review 2015–16 <http://annualreview1516.sro.vic.gov.au/content/analysis-debt>.

54 *Taxation Administration Act 1996* (NSW) pt 7 div 2. The Australian Capital Territory and the Northern Territory have similar provisions: *Taxation Administration Act 1999* (ACT) s 56B; *Taxation Administration Act* (NT) s 61.

55 *Taxation Administration Act 1996* (NSW) s 47B(3).

been 'insolvent trading', subject to the usual scope to avoid liability with VA or liquidation within 21 days.[56] It is unclear why director penalties for unremitted company taxes have not been more widely adopted by other states. In evaluating the usefulness of DPN equivalents for state taxes, all states should look at introducing a 'lockdown' set of provisions and at whether some element of fault could be incorporated into the provisions, as discussed above.

The foregoing has considered a number of improvements that could be made to the DPN regime. However, by definition, only directors are included,[57] not other company officers and not any advisors as accessories.[58] Reaching beyond directors is considered in the next section.

B *Accessory Liability*

It is important to ensure that those who devise or implement schemes to deliberately exploit the separateness of companies to avoid obligations are deterred from doing so. This is so, whether these people are directors of small companies, and thus the indirect financial beneficiaries of the behaviour, or advisors who charge a fee. This section now considers the accessory liability provisions under tax law and their shortcomings.

1 *Options against Company Directors and Officers*

There are a number of criminal provisions available against accessories to tax avoidance schemes engaged in by corporate taxpayers. The one most appropriate to the current discussion is the *CTOA*, which was introduced following 'Bottom of the Harbour' tax evasion in the 1970s.[59] It imposes criminal sanctions where a person enters into an arrangement with the intention of securing that a company will be unable to pay income tax or a range of other taxes including the super guarantee charge.[60] The penalties are 10 years' imprisonment or 1000 penalty units or both. However, the Act's provisions do not appear to be used in the context of deliberate liquidations to avoid tax debts,[61] possibly because it is considered too difficult to

---

56 *Taxation Administration Act 2003* (WA) s 67.

57 *TAA* sch 1 s 269-15 imposes liability on 'directors (within the meaning of the *Corporations Act 2001*)' — ie, in accordance with s 9 of the *Corporations Act*, which only covers formally appointed, shadow and de facto directors.

58 Note, however, PAYG(W) non-compliance tax, above n 18.

59 See Peter Grabosky, *Wayward Governance: Illegality and its Control in the Public Sector* (Australian Studies in Law, Crime and Justice, Australian Institute of Criminology, 1989) ch 9.

60 *CTOA* ss 5, 17. See also Lidia Xynas, 'Tax Planning, Avoidance and Evasion in Australia 1970-2010: The Regulatory Responses and Taxpayer Compliance' (2011) 20(1) *Revenue Law Journal* Article 2.

61 The ATO has revealed that '[i]nvestigators executed six search warrants on the Gold Coast and in Victoria in respect to *Crimes (Taxation Offences) Act 1980* offences pertaining to super and alleged phoenix offences.': ATO, *Archived Serious Tax Crime Investigation Results* (22 Jan 2018) <https://www.ato.gov.au/general/the-fight-against-tax-crime/news-and-results/latest-serious-tax-crime-investigation-results/archived-serious-tax-crime-investigation-results/>. There is no other information available from the ATO on *CTOA* prosecutions. The Commonwealth Director of Public Prosecutions ('CDPP') prosecution statistics do not list the *CTOA* as a piece of legislation under

establish the required intent element to the criminal standard. Liquidation can have many apparent explanations.

The general anti-avoidance rule[62] does not assist, because it deals with the company obtaining a 'tax benefit',[63] avoiding a tax liability being incurred, not the non-payment of a liability properly incurred. Fraud provisions, such as conspiracy to defraud the Commonwealth,[64] are available, but require more than simply proof of the company's failure to remit taxes.[65] An alternative that the Government could consider is the reintroduction of the 'failure to remit' offence, which was removed in 2000.[66] Such an offence, coupled with s 8Y of the *TAA* (making directors liable for the tax offences of their company) and s 21B of the *Crimes Act 1914* (Cth) (allowing the court to order reparation), would effectively punish deliberate liquidation and redress the damage at the same time. It is an appealing idea because of its ability to deprive the wrongdoer of the benefit of their behaviour, and it could be used where the company is in liquidation, despite the existence of the parallel DPN regime.[67] However, like all criminal provisions, it suffers from the basic requirements of proving the criminal offence beyond reasonable doubt and in accordance with criminal rules of evidence, although as far as the accessory liability goes under s 8Y, the onus of proof is on the defendant to prove that he or she was not 'concerned in' or did not 'take part in' the management of the company.[68]

2 *Options against Advisors*

Given the complexity of tax laws, it makes sense from an enforcement perspective to target those who devise complicated ways to avoid tax, on the basis that many directors would lack the tax knowledge or ability to come up with these sorts of arrangements themselves. Treasury's *2009 Phoenix Proposals Paper* canvassed the option of revising the promoter penalty regime[69] to discourage those designing and advocating tax schemes to exploit the corporate form.[70] Extending penalties to advisors assisting phoenix operators, via an extension of the promoter penalty provisions, was one of the suggestions of the *2017 Combatting Illegal Phoenixing* consultation paper.[71]

In simple terms, the current promoter penalty regime contains a prohibition against those who promote 'tax exploitation schemes'.[72] The idea is to stop advisors

---

which prosecutions have been brought: CDPP, *Prosecution Statistics* <https://www.cdpp.gov.au/statistics/prosecution-statistics>.

62 *Income Tax Assessment Act 1936* (Cth) s 177D(1).

63 Ibid s 177C.

64 *Criminal Code Act 1995* (Cth) sch 1 ('*Criminal Code*') s 135.4(3).

65 See, eg, *R v Iannelli* (2003) 56 NSWLR 247. Fraud was established in *R v Walters* [2002] NSWCCA 291 (25 July 2002), a case involving 10 successor companies defaulting on $7.3 million of group tax liabilities.

66 *2009 Phoenix Proposals Paper*, above n 21, 16–18 [4.2.5].

67 *Gould v Federal Commissioner of Taxation* (1998) 147 FLR 173.

68 *TAA* s 8Y(3). For a discussion of the reverse onus, see, eg, *Buist v Federal Commissioner of Taxation; Ex parte Buist* (1988) 90 FLR 72, 74–5.

69 *TAA* sch 1 div 290.

70 *2009 Phoenix Proposals Paper*, above n 21, 9 [3.1.2], 15 [4.2.3].

71 *2017 Combatting Illegal Phoenixing*, above n 4, 17.

72 *TAA* sch 1 div 290.

actively marketing and encouraging[73] companies, among others, to structure their arrangements in schemes that exploit tax laws in order to reduce the amount of a tax-related liability.[74] Again, these schemes reduce or eliminate the company's liability to pay tax — the incurring of the tax debt. However, as with the general anti-avoidance rule,[75] these provisions are not effective where tax debts are avoided through liquidation, because the company's tax liability is unaffected. The company has simply failed to pay what it properly owes. Moreover, the provisions do not extend to those who simply advise about the scheme.[76] Treasury's 2009 suggestion was that the provision, which presently imposes a civil penalty on these advisors, could be adapted to address phoenix activity.[77] However, if the provision were to be adapted to cover the deliberate liquidation scenario, there is a risk that a narrowly drawn liability provision would be too difficult to establish as 'tax exploitation scheme'[78] or else overextend to take in legitimate liquidations if more moderate language were adopted. Advisors who tell their clients that they should liquidate companies facing insolvency should not be penalised.[79]

Advisors, however, might be caught under the *CTOA*. Liability is imposed under s 6(1) for being an accessory to an arrangement or transaction,[80] 'knowing or believing' that the arrangement is being entered into by the other person with the intention of securing the prohibited avoidance of payment of tax debts.[81] The *CTOA* also speaks about 'future income tax'.[82] Yet there do not appear to be cases against advisors brought under this provision[83] and it is telling that neither Treasury's *2009 Phoenix Proposals Paper* nor its *2017 Combatting Illegal Phoenixing* consultation paper mention the *CTOA* provisions in seeking to address advisor liability. Section 5 of the *CTOA* requires the main perpetrator to have the intention of securing that the company will be unable to pay the income tax. However, under s 6 the accessory does not need that purpose, only the knowledge or belief that the other person has it. This makes the *CTOA* accessory provisions much more suitable for use against advisors who are knowingly involved in illegal phoenix activity for the purpose of not paying tax.

The foregoing discussion has highlighted some under-utilised tax provisions that can be used to bring enforcement actions and how some of them could be enhanced. The next section examines some procedural improvements that could be made to significantly reduce the ATO's later reliance on enforcement actions.

---

73 Promoter is defined in *TAA* sch 1 s 290-60.

74 According to *TAA* sch 1 s 290-65(1), a tax exploitation scheme occurs when it was entered into for 'the sole or dominant purpose of that entity or another entity getting a scheme benefit from the scheme' and 'it is not reasonably arguable that the scheme benefit is available at law'.

75 See above n 62 and accompanying text.

76 *TAA* sch 1 s 290-60(2).

77 Ibid s 290-50(3).

78 Ibid s 290-65. See also above n 74 and accompanying text.

79 *Phoenix Recommendations Report*, above n 2, 128.

80 The usual accessory liability words are used: 'directly or indirectly, aids, abets, counsels or procures another person … or is, in any way, by act or omission, directly or indirectly concerned in, or party to, the entry by another person … into an arrangement or transaction': *CTOA* s 6(1).

81 Ibid s 5.

82 Ibid s 5(2)(a).

83 See above n 61 and accompanying text.

C *Other Suggestions*

1 *Single Touch Payroll*

The Government's 'single touch payroll' ('STP') regime could reduce the incentive to engage in illegal phoenix activity by taking away much of its benefit. Initially, STP was mooted as a mechanism whereby employers would pay both their employees and related PAYG(W) remittances and super contributions at the same time. However, the Government amended the STP proposal and it now only covers the reporting of tax and super obligations.[84]

This alteration was in response to concerns from business about the cash flow implications[85] of having to pay the taxes at an earlier time than is presently the case. While wages are generally paid fortnightly, PAYG(W) and super are usually only remitted monthly or quarterly depending on the size of the business and the terms of the super fund trust deed. The objection raised shows the extent to which businesses rely on employee-related sums — 'their money' until it is legally payable — to finance their businesses, and the Government's response shows its reluctance to interfere with this practice. The legitimate cash flow concerns of small business have recently been acknowledged by the Australian Small Business and Family Enterprise Ombudsman.[86]

At present, the STP reporting obligation is only compulsory for employers with 20 or more employees. However, the TLA 2018 Super Measures Bill proposes to make it compulsory for all employers.[87] This is sensible given that micro and small businesses employing less than 20 employees make up 97.4% of Australian businesses.[88] However, the onus remains on the ATO to detect non-payment and then send the DPN. In 2012, automatic DPNs were mooted, but rejected.[89] In the event that the expansion of the STP as proposed by the TLA 2018 Super Measures Bill is passed into law, the ATO will need to ensure adequate resourcing to deal with

---

84 *Phoenix Recommendations Report*, above n 2, 77.

85 Michael Masterman, 'CAANZ Latest to Criticise ATO's Single Touch Payroll', *Accountants Daily* (online), 17 March 2015 <http://www.accountantsdaily.com.au/latest-news/17-news/8069-caanz-latest-to-criticise-ato-s-single-touch-payroll>, quoting Michael Croker, head of tax at Chartered Accountants Australia and New Zealand ('CAANZ'):

> Nobody disputes that PAYG tax and super is an employee entitlement and must be paid, the sooner the better. But this is an area where a desirable policy objective needs to take into account the fact that many [small- and medium-sized enterprises] struggle with cash flow. It takes more than 50 days on average for small business accounts to be paid and many are in a weak negotiation position with key clients.

See also Michael Croker, Submission to ATO, *Single Touch Payroll Discussion Paper* (12 March 2015) 10–13.

86 See Australian Small Business and Family Enterprise Ombudsman, *Payment Times and Practices Inquiry* (April 2017) <http://asbfeo.gov.au/inquiries/payment-times-and-practices>.

87 TLA 2018 Super Measures Bill, sch 3.

88 Australian Small Business and Family Enterprise Ombudsman, *Small Business Counts: Small Business in the Australian Economy* (2016), 8 [2.1.1] table 1.

89 Tax Laws Amendment (2011 Measures No 8) Bill 2011 (Cth) sch 3; Kai Swoboda and Xenia Stathopoulos (Department of Parliamentary Services), *Tax Laws Amendment (2011 Measures No 8) Bill 2011 [and] Pay As You Go Withholding Non-compliance Tax Bill 2011* (Bills Digest No 78 of 2011–12, 21 November 2011) 11.

the volume of DPNs that will be required. The ATO's submission to the Senate Economics References Committee inquiry into super guarantee non-compliance in 2017 noted that '[s]ome 97 per cent of reports of unpaid super made to the ATO were against small business employers and this same group accounted for around 98 per cent of the liability raised by the ATO.'[90]

Even so, STP as a reporting-only mechanism undermines the effectiveness of 'lockdown' DPNs, which can only be used against those who fail to report their tax liability, via STP or otherwise. As noted above, once the directors of a company that has reported its liabilities, but failed to pay them, receive their 'standard' DPNs, they have 21 days to shed this liability by placing the company into external administration. In other words, if liabilities are reported, the ATO has more information, but fewer means of recovery. If liabilities are not reported, the ATO has less information and more means of recovery. This dilemma could be overcome by reverting to the original conception of STP; namely, simultaneous reporting and payment.

2 *Security Bonds*

The ability of the Commissioner of Taxation to obtain security from a taxpayer was reformed in 2010.[91] A bond may be sought for any existing or future tax liability, including PAYG(W) and the super guarantee charge,[92] if the Commissioner considers that the taxpayer intends to carry on an enterprise for a limited time only, or if it is otherwise appropriate.[93] Various types of security are provided for, including payments of money and other securities.[94] Failure to pay the security, following receipt of a written notice from the Commissioner,[95] is an offence punishable by a fine.[96] However, the punishment is relatively modest at 100 penalty units for an individual (currently $21 000) and 500 penalty units for a company (currently $105 000). The TLA 2018 Super Measures Bill proposes increasing these penalties to include imprisonment for failure to comply with a security deposit payment order, issued by the Federal Court of Australia on the application of the Commissioner.[97]

The difficulty with any penalty levied on companies in the phoenix context is that the very act of phoenixing — closing one company down and opening another

---

90 Quoted in Senate Economics References Committee, Parliament of Australia, *Superbad — Wage Theft and Non-compliance with the Superannuation Guarantee* (May 2017) [5.90].

91 *TAA* sch 1 sub-div 255-D, inserted by *Tax Laws Amendment (Transfer of Provisions) Act 2010* (Cth) ('*Tax Laws Amendment (Transfer of Provisions) Act*') sch 1 s 9. Prior to this amendment, s 213 of the *Income Tax Assessment Act 1936* (Cth) allowed the Commissioner to ask for a security bond or deposit for income tax liabilities. Subdivision 255-D expanded on this existing power in a number of important respects: see Morag Donaldson (Department of Parliamentary Services), *Tax Laws Amendment (Transfer of Provisions) Bill 2010* (Bills Digest No 153 of 2009–10, 26 May 2010) 6–8. See further Matthew Broderick, 'Legislative Change to Director Penalty Notices and Security for Tax Payments' (2011) 40(1) *Australian Tax Review* 60, 63–4.

92 *TAA* sch 1 s 250-100(2).

93 Ibid sch 1 s 255-100(1).

94 Ibid sch 1 s 255-100(2).

95 Ibid sch 1 s 255-105.

96 Ibid sch 1 s 255-110.

97 TLA 2018 Super Measures Bill sch 5 pt 3 s 15.

— has the happy side-effect (for the company's directors) of avoiding payment by the company of the penalty, the security bond and the taxes that the ATO was trying to protect in the first place. This situation is unchanged by the proposed provisions of the TLA 2018 Super Measures Bill where the entity has a defence against criminal liability where it is not capable of complying with the order, for reasons such as insolvency.[98]

Prior to the company closing down, it continues to trade, accruing tax debts right up until the time the ATO's security bond penalty action goes to court. This might suggest that the law should be reformed to require the company to cease trading immediately upon failure to pay the security bond. However, this could adversely affect the company's employees, customers and suppliers. Another response could be to tighten the security bond mechanism so that there is a meaningful penalty imposed on the directors and managers of companies who cause the company's failure and non-payment of the security bond and penalty, and who then liquidate the company. However, this has the potential to catch those 'innocent' individuals in charge of a financially troubled company that lacks the ability to pay the security bond or the penalty. The proper action for such people *is* to liquidate the company promptly. They face personal liability for insolvent trading otherwise.[99] Liquidating the company cannot, therefore, also be the trigger for a personal punishment.

The *2017 Combatting Illegal Phoenixing* consultation paper sought feedback on including security bonds in the existing garnishee power.[100] That is certainly an option worth considering. Another approach here would be not to target the failing company, but rather to target the creation of a new company. Because the ATO is such a significant creditor affected by illegal phoenix activity, consideration should be given to allowing the ATO to grant an Australian Business Number ('ABN')[101] conditionally by requiring payment of a bond or the provision of security over an asset owned by the director. The ATO's ABN refusal powers are considered further in the next section.

3 *Refusal of an ABN*

One problem for the ATO is it currently lacks the power to deny an ABN to a company, as it may to an individual where they do not believe the individual is carrying on an enterprise.[102] Even if the ATO has grave suspicions about the individuals controlling a company, it must still grant that company an ABN, and this is so whether those individuals are running one or 100 companies. This deficiency must be addressed if the ATO is to have meaningful tools against serial phoenix operators. In addition, the 'fit and proper person' test for the issue of an ABN, raised

98 Explanatory Memorandum, TLA 2018 Super Measures Bill, [5.58]–[5.59].

99 *Corporations Act* s 588G(2). Criminal penalties are also available for offences under s 588G(3).

100 *2017 Combatting Illegal Phoenixing*, above n 4, 20.

101 The importance of ABNs is explained at Australian Government, Business, *Register for an Australian Business Number (ABN)* (15 March 2018) <https://www.business.gov.au/info/plan-and-start/start-your-business/business-and-company-registration/register-for-an-australian-business-number-abn>.

102 See Australian Business Register, *ABN Entitlement* (17 April 2018) <https://abr.gov.au/For-Business,-Super-funds---Charities/Applying-for-an-ABN/ABN-entitlement/>.

for consideration in Treasury's *Black Economy Taskforce* consultation paper,[103] is worth investigating. To implement these measures, it is essential to have access to reliable information from ASIC to establish a person's good faith. Suggestions to improve the quality of the information held by ASIC are outlined below in Part IV.

4 *Credit Agencies to Make Information Public*

Where directors of companies are seeking financing to run their businesses, potential lenders, via the services of a credit reporting agency, would benefit from seeing information about prior tax defaults by companies with which those people have previously been associated. If credit reporting agencies could include this sort of information in their advice to prospective lenders and trade creditors, illegal phoenix activity could be more easily detected. While the ATO can use external debt collection agencies to pursue unpaid taxes,[104] it has not been able to register tax defaults with credit reporting agencies, as a bank or trade creditor might.

In January 2018, the Australian Government released draft provisions of a legislative instrument to allow for limited disclosure of tax-debt information.[105] The measure would initially apply only to businesses with ABNs and tax debt of more than $10 000 that is at least 90 days overdue, where the business has not engaged with the ATO regarding the debt, appealed the liability nor objected to the release of the information.[106] However, as currently drafted, the ATO may only release tax-debt information for the purpose of allowing credit bureaus to assess the credit worthiness of the defaulting entity.[107] This limitation has the capacity to encourage illegal phoenix activity, because the entity's liquidation will deprive the ATO of the power to release that tax-debt information. A re-drafting of the provision to allow the ATO to reveal information for the purpose of assessing the credit worthiness of that entity and any present and future entities controlled by the defaulting entity's directors and officers would be very useful in deterring illegal phoenix activity.

5 *Director Disqualification Initiated by the ATO*

The only penalty that results from a DPN is the payment of the company's tax — effectively quarantining a director divested of personal assets from the effect of the DPN. To deter more effectively the improper conduct that leads to the DPN being issued, consideration should be given to exacting a separate punishment upon the director personally.[108] This could be done by allowing the ATO to seek a court order for their disqualification.[109] Currently, the ATO can refer the director to ASIC to

---

[103] Australian Government, Treasury, *Black Economy Taskforce Consultation Paper* (August 2017) [4].

[104] Note the discussion of this issue in the *IGT Debt Collection Report*, above n 50, ch 5.

[105] Exposure Draft, Treasury Laws Amendment (Tax Transparency) Bill 2018: Transparency of Taxation Debts.

[106] Ibid s 355-72; Exposure Draft, Tax Debt Information Disclosure Declaration 2018, s 7.

[107] Exposure Draft, Treasury Laws Amendment (Tax Transparency) Bill 2018 s 355-72(1)(d).

[108] The punitive nature of disqualifications was acknowledged in *Murdaca v ASIC* (2009) 178 FCR 119, 143–4 [101]; *Visnic v ASIC* (2007) 231 CLR 381, 385 [11], 388 [26]; *Rich v ASIC* (2004) 220 CLR 129, 151–5 [47]–[50].

[109] The Australian Consumer and Competition Commission ('ACCC') has the power to seek disqualification of directors: *Competition and Consumer Act 2010* (Cth) s 86E. See further Tom Middleton, 'Banning, Disqualification and Licensing Powers: ACCC, Australian Prudential

bring a disqualification action, discussed below,[110] but a useful message, and more reliable outcome,[111] could be obtained by bringing this matter 'in-house'.[112] Disqualification would also remove the director from managing other companies that might default on their tax obligations. Sensibly, the definition of 'director' in the DPN laws picks up the *Corporations Act* definition, which covers properly appointed directors as well as those acting as directors or 'calling the shots'.[113] This means that an elderly relative, for example, could be appointed director of the company, but that the person who truly runs the company will still be caught, presuming that the ATO is able to detect who that person is.

The grounds upon which disqualification is sought could be based on the ATO's the DPN itself. Division 269 imposes a duty on directors to ensure that the company meets various taxation obligations or promptly enters liquidation or VA. A new subsection could be inserted into s 269-20 empowering the ATO to seek a disqualification order against a director in the event that they breach this duty. To ensure that only directors involved in improper behaviour were caught by the provision, an additional requirement could be that the court believed that it was just and equitable to disqualify the director.

6 *Other Suggestions from Treasury to the Minister for Revenue*

The *2017 Combatting Illegal Phoenixing* consultation paper mooted a number of other ideas to tackle illegal phoenix activity, which raise some concerns.

(a) *A Specific Phoenix Offence*

The Minister suggested a specific phoenix offence 'to better enable regulators to take decisive action against those who engage in this illegal activity'.[114] There are two ways to accomplish this: by proscribing 'phoenix activity' as defined; or by

---

Regulation Authority ('APRA'), ASIC and the ATO — Regulatory Overlap, Penalty Privilege and Law Reform' (2015) 33(8) *Company and Securities Law Journal* 555, 556.

110 See below Part IVA(1).

111 Detailed statistics about ATO referrals to ASIC regarding possible disqualification are unavailable. However, ASIC has revealed that in 2013–14, in its disqualification program 'with a particular focus on phoenix activity', it disqualified 60 company directors: ASIC, Submission No 32 to Senate Economics References Committee, *Inquiry into Corporate Tax Avoidance and Minimisation*, February 2015, 19 [103]. In contrast, while remembering that not all DPNs are issued in circumstances involving illegal phoenix activity, the *IGT Debt Collection Report* noted that in 2013–14, there were 1572 DPNs issued where the company became insolvent following the issue of the DPN: above n 50, [4.43], table 4.2.

112 In fact, external administrators often refer tax-related breaches by directors straight to the ATO. Between 1 July 2016 and 30 June 2017, there were 105 such referrals: ASIC Report 558, above n 6, 35–6 (table 29).

113 *Corporations Act* s 9 includes in the definition of director those who act as directors (de facto directors) and those in accordance with whose instructions or wishes the board is accustomed to act (shadow directors).

114 O'Dwyer, above n 3. See also the earlier attempt of the Australian Labor Party: the Fair Work Amendment (Protecting Australian Workers) Bill 2016. The Bill was introduced into the Senate on 15 March 2016, but lapsed with the proroguing of Parliament before the July 2016 Federal Election. The difficulties with the Bill's attempt to proscribe illegal phoenix activity were considered in Helen Anderson, 'Corporate Insolvency: Labor's Policy to Deal with Phoenix Activity Affecting Employees' (2016) 34(4) *Company and Securities Law Journal* 316.

proscribing specific actions directly. Either way is unlikely to be successful. The first would require the phoenix definition to be able to differentiate legitimate and improper behaviour.[115] A broad proscription based on describing the circumstances of the sham 'business rescue' may pick up legitimate VAs,[116] which allow time for an administrator to try to save the company.[117] Where the rescue is unsuccessful, but a company controlled by the failed company's directors buys its assets, the directors might find themselves liable under a provision that penalises this sort of behaviour.

A limited definition, on the other hand, is an easily negotiated roadmap to avoidance. For example, one research paper defined phoenix activities as:

> […] those where an incorporated entity either:
>
> 1. fails and is unable to pay its debts and/or;
> 2. acts in a manner which intentionally denies unsecured creditors equal access to the entity's assets in order to meet unpaid debts; and
> 3. within 12 months another business commences which may use some or all of the assets of the former business, and is controlled by parties related to either the management or directors of the previous entity.[118]

Apart from the difficulty of proving this intention, the use of the word 'commences' is problematic. In some instances of phoenix activity, the company to which the business activities of the failed company are transferred is already in existence at the time of the demise of the first. It could also be done within a corporate group where one company owns the assets, and contracts for their use by the operating or labour hire company, which incurs the tax and other debts. The assetless operating or labour hire company is then liquidated, and the process is repeated. In some phoenixing, no assets are transferred at all, because the business is a service provider.

Any phoenix liability provision that attempts to penalise directors acting improperly around the time of liquidation will also fail to address phoenix activity through the abandonment of a company that remains dormant until it is eventually deregistered by ASIC. Unless a creditor seeks to have the company wound up, no liquidation will take place and the company is eventually removed from the register of companies by ASIC where its controllers have failed to pay annual fees and return paperwork.[119] Abandonment without liquidation is likely to happen in very small companies where the creditors are unwilling to spend money on a liquidator to chase possibly non-existent corporate assets. Because assestless companies may hide illegal phoenix activity,[120] it is likely that the businesses of abandoned companies are often phoenixed. These companies are discussed further below.[121]

---

115 See Helen Anderson et al, 'Illegal Phoenix Activity: Is a "Phoenix Prohibition" the Solution?' (2017) 35(3) *Company and Securities Law Journal* 184.

116 *Corporations Act* pt 5.3A.

117 Ibid s 435A.

118 Australian Securities Commission, *Project One: Phoenix Activities and Insolvent Trading — Public Version* (Research Paper 95/01, 13 May 1996) 39.

119 *Corporations Act* s 601AB(1), (1A) respectively.

120 This is one of the reasons for the Assetless Administration Fund: ASIC, *Regulatory Guide 109: Assetless Administration Fund: Funding Criteria and Guidelines* (November 2012) [109.6]–[109.7].

121 See below Part IVB(3).

The second way of creating a specific phoenix offence is to target the company's specific actions, and this was the method suggested by the *2017 Combatting Illegal Phoenixing* consultation paper. It proposed that a new provision be inserted into the *Corporations Act* 'to specifically prohibit the transfer of property from Company A to Company B if the main purpose of the transfer was to prevent, hinder or delay the process of that property becoming available for division among the first company's creditors'.[122] Feedback was also sought on what additional remedies might be useful,[123] including whether certain existing provisions should be designated as 'phoenix offences' for the purpose of a more severe regime for HRPOs.[124]

Clearly, the proposed phoenix offence only captures phoenixing involving the transfer of property, with the deficiencies already noted. As the 2017 consultation paper acknowledges,[125] illegal phoenix activity is already a breach of directors' duties,[126] examined further below, and these duties capture all improper phoenix behaviour, involving asset transfers or not. Section 588FE(5) of the *Corporations Act* already allows a liquidator to claw back asset transfers where 'the company became a party to the transaction for the purpose, or for purposes including the purpose, of defeating, delaying, or interfering with, the rights of any or all of its creditors on a winding up of the company'.[127] This has two advantages over the proposed provision: it does not require the creditor-defeating purpose to be the main purpose; and it allows the liquidator to look back at transactions in the previous 10 years. The only stipulation relevant here is that it must also be 'an insolvent transaction'.[128] Therefore, asset transfers made deliberately within the 10 years prior to a company's insolvency to render the company unable to pay its creditors are already subject to considerable recovery powers in the hands of liquidators.

In addition, uncommercial asset transfers are already actionable as one of a number of voidable transactions[129] and as a form of insolvent trading.[130] Both the directors' duties and insolvent trading provisions have a number of advantages over the proposed offence. These provisions are civil penalty breaches. On the application of ASIC, the court may order disqualification or penalties payable to the Government. The court may also make compensation orders against directors. With respect to the final order, action can be taken by both the liquidator, in the name of the company, and by ASIC. In the event of particularly egregious behaviour, ASIC

---

122 *2017 Combatting Illegal Phoenixing*, above n 4, 8–9.
123 Ibid 11.
124 Ibid 23.
125 Ibid 8.
126 *Corporations Act* ss 180–83.
127 This provision and its antecedents were discussed recently in *Ashala Model Agency Pty Ltd (in liq) v Featherstone* [2017] 2 Qd R 1; *Featherstone v Ashala Model Agency Pty Ltd (in liq)* [2017] QCA 260 (3 November 2017).
128 Section 588FC defines an insolvent transaction as one that is entered into when the company is insolvent or one where the company becomes insolvent wholly or partly because of entering into the transaction.
129 *Corporations Act* pt 5.7B div 2. Uncommercial transactions, as defined by s 588FB, may be set aside on the application of a liquidator under s 588FE(3).
130 This is the combined effect of *Corporations Act* ss 588FB and 588G(1A).

also has the option of bringing criminal action with respect to both directors' duties and insolvent trading breaches.[131]

A further concern over the proposed phoenix offence is that it is based on proving an intention — 'the main purpose' — to a criminal standard, even with the transfer's relationship to the imminent insolvency being 'reasonably … inferred from all the circumstances'.[132] The proposed provision is reminiscent of s 596AB of the *Corporations Act*, the criminal provision relating to entering into transactions with the intention of preventing or significantly reducing the recovery of employee entitlements. This section has never been used.

(b) *High Risk Phoenix Operator ('HRPO') Regime*

To ensure that the most stringent provisions are only applicable to those at highest risk of illegal phoenix activity, the *2017 Combatting Illegal Phoenixing* consultation paper suggested a separate suite of measures only applicable to those deemed HRPOs.[133] However, the proposed mechanism for such a designation appears quite cumbersome, requiring the identification of a 'Higher Risk Entity' as a prerequisite to the Commissioner declaring a person to be an HRPO.[134] Because adverse consequences follow, a person affected would be entitled to apply to the Administrative Appeals Tribunal for a review of the decision. The proposed consequences are a 'cab rank' liquidator appointment,[135] the removal of the 21-day 'grace period' after a DPN is issued, and the ability of the ATO to retain certain refunds.[136]

It is questionable whether the benefits of the proposed HRPO procedure will outweigh the administrative burden. In particular, the DPN proposal is problematic. It will impose liability on HRPO directors for any reported, but unpaid, PAYG(W), super and GST. The issue of the DPN then becomes a formality, rather than allowing the director time to get the company's affairs into order by seeking liquidation. If the liabilities were both unreported and unpaid, the 21-day period is lost anyway as a 'lockdown' DPN. The stated rationale is that the new regime takes away the 21 days that the HRPO would use to shift their personal assets,[137] but it is suggested that more thought needs to be given to the behavioural profile here.

The somewhat naive HRPO caught by the proposal both reports liabilities and keeps personal assets until sent a DPN. However, a more likely profile is a determined HRPO that makes themself DPN-proof by ensuring that they have little, if anything, in their own name throughout their time as a director. They probably do not report liabilities, so that the ATO does not know what is owing. In any event, they do not fear a lockdown DPN, since the only penalty is payment of the company's taxes — from money they do not have. This makes a further DPN-related

131 Ibid ss 184, 588G(3) respectively.
132 *2017 Combatting Illegal Phoenixing*, above n 4, 9.
133 Ibid part two.
134 Ibid 24.
135 See below Part IIIC(6)(c).
136 *2017 Combatting Illegal Phoenixing*, above n 4, 30–31.
137 Ibid 30.

punishment, such as an ATO-initiated disqualification,[138] a more effective measure than the proposed removal of the 21-day grace period.

(c) *Liquidator Interventions*

Another suggestion in the *2017 Combatting Illegal Phoenixing* consultation paper was that there would be 'cab rank' system for appointing liquidators[139] for those companies controlled by HRPOs.[140] The 'cab rank' proposal follows a similar recommendation by the Productivity Commission in 2015 in relation to small, streamlined liquidations.[141] The worthy intention is to ensure that 'friendly' liquidators, chosen by the company's fraudulent directors, are not appointed so that they can collude with them to deny creditors a proper return. However, the idea is nonetheless problematic. Given that many phoenix liquidations involve few or no assets — that being the very point of the phoenixing — those liquidators 'on the cab rank' need assurance that they will be paid. The *Corporations Act* makes it clear that liquidators are not obliged to do work for which they will not be paid, apart from their statutory reporting obligations.[142]

In the event that the Government adopts a 'cab rank' system, guaranteed funding will need to be provided. The 2017 consultation paper suggested that the panels could be funded 'via a component of the industry levy on corporations'.[143] There is no industry levy on corporations, only an industry levy on 'regulated entities' including liquidators.[144] This levy is claimed to have 'significant benefits including … improving equity, as only those entities that are regulated by ASIC and create need for regulation will bear its costs, rather than ordinary Australian taxpayers'.[145] If the 2017 consultation paper is referring to this levy, it would be substantially unfair to liquidators, requiring them to contribute as an administrative expense of their business to a levy that pays for them, or some other liquidator, to conduct an assigned liquidation.

It would also be unfair if liquidators assigned from the cab rank were forced to rely upon the present Assetless Administration Fund, depending as it does upon a liquidator investigating and making a case for funding, which may be refused.[146] A much better source of funding would be from a small increase on the cost of incorporation or the lodgement of a company's documents to ASIC annually.

An alternative to liquidators on a cab rank panel mooted by the *2017 Combatting Illegal Phoenixing* consultation paper is the creation of a government

---

138 See above n 111 and accompanying text.
139 *2017 Combatting Illegal Phoenixing*, above n 4, 28.
140 See above Part IIIC(6)(b).
141 Productivity Commission, *Business Set-up, Transfer and Closure*, Report No 75 (2015) 408–9 recommendation 15.1: 'Liquidators for [streamlined liquidations] would be drawn from a panel of providers selected by tender to ASIC. Panel membership would be for a period of up to five years, with ASIC able to conduct tenders at regular intervals to ensure that demand can be met.'
142 *Corporations Act* s 545.
143 *2017 Combatting Illegal Phoenixing*, above n 4, 28.
144 *ASIC Supervisory Cost Recovery Levy Act 2017* (Cth).
145 See Kelly O'Dwyer (Minister for Revenue and Financial Services), 'ASIC Industry Funding Model Passed into Law' (Media Release, 15 June 2017).
146 ASIC, *Regulatory Guide 109*, above n 120 [109.5]–[109.8].

liquidator to deal with small- and medium-sized enterprise liquidations. This idea is worth investigating further. A government-funded liquidator can achieve economies of scale and access government-held information more easily. In addition, it would solve the funding dilemma, which should be by way of allocation from consolidated revenue. There are considerable benefits that could be achieved. A more efficient system for conducting liquidations of small- and medium-sized enterprises could provide better detection, enforcement and, therefore, deterrence of illegal phoenix activity. This could result in the collection of more tax revenue, improved payment of super, less reliance on the Fair Entitlements Guarantee and a fairer, more competitive market bringing economic benefits across society.

This Part has examined a variety of improvements or new initiatives that could assist the ATO to deter and disrupt illegal phoenix activity, or to recover from wrongdoers if it occurs. The next Part serves as a reminder that ASIC, as the corporate regulator, and the *Corporations Act*, as the principal governing statute, can also play a significant role in the recovery of tax debts and the punishment of corporate misbehaviour.

IV Existing Corporate Law Mechanisms and Ways to Improve Them

A *Actions Available under the* Corporations Act

Depending on the provision involved, there is scope under the *Corporations Act* for ASIC, the company's liquidator or the ATO directly to seek a range of remedies or to implement preventative measures. The liquidator may be funded by the ATO, which is a well-resourced and motivated creditor, to pursue company controllers and others to recover unremitted taxes and other debts. Some of these provisions will now be considered.

1 *Disqualification*

ASIC may seek an order from a court to disqualify a director or may do so administratively itself. In both cases, the grounds include being involved in two or more failed companies in the past seven years, with the court disqualification limited to 20 years and ASIC disqualification to five years.[147] The former depends upon the company's management being 'wholly or partly responsible for the corporation failing'[148] and the latter upon ASIC receiving an adverse liquidator's report. In both cases, the disqualification must be justified. In addition, ASIC may seek a court order for a director's disqualification for breach of a civil penalty provision.[149] These include breaches of directors' duties and insolvent trading, both of which are noted below.

[147] *Corporations Act* ss 206D, 206F respectively.
[148] Ibid s 206D(1)(b)(i).
[149] Ibid s 206C. Note also *Australian Securities Commission v Forem-Freeway Enterprises Pty Ltd*, where the director engaged in phoenix-like behaviour and was disqualified for 12 years under s 1317EA(3)(a) of the *Corporations Act*: (1999) 30 ACSR 339, 351.

An example of an ASIC disqualification involving tax debts is *Re Grossman*.[150] The Administrative Appeals Tribunal affirmed ASIC's exercise of its administrative power to disqualify Mr Grossman from managing corporations for five years. He had been a director of three failed companies within a seven-year period, and each had failed to pay their taxation liabilities. Another successful collaboration between ASIC and the ATO in 2017 is the disqualification of Steven Soong, which involved three companies failing to remit over $1.2 million in taxation liabilities.[151]

The advantage of ASIC's disqualification powers is that there is no need to prove any illegality nor the non-remittance of specific debts, as would be the case with the ATO disqualification power recommended above in Part IIIC(5) of this article. However, what is needed for ASIC-initiated disqualification to be effective in relation to tax defaults is an efficient system of referrals and responsive action by ASIC.[152]

2 *Winding Up, Recovering Voidable Transactions and Insolvent Trading*

The ATO can seek the winding up of a company where illegal phoenix activity is suspected based on the past history of the enterprise. For example, in *Deputy Commissioner of Taxation v Casualife Furniture International Pty Ltd*,[153] the Court ordered the winding up under s 462(1)(k) of the two solvent companies in the group, the latest in a string of companies run by the Guss family. The order was made on the basis that it was just and equitable to do so. The pattern of behaviour of incurring tax and other debts, transferring assets to a new company and then liquidating the debt-laden company, had been occurring for 20 years.[154]

The ATO can also seek the winding up of a company already in VA[155] where, for example, the votes of the some creditors in support of a deed of company administration are tainted by payments from the fraudulent director.[156] However, as noted above, one of the defining features of illegal phoenix activity is the readiness of company controllers to place their company into liquidation, after stripping its assets or overloading it with tax debts, so the ATO's ability to wind-up these companies will not assist it to recover taxes in many cases.

---

150 [2011] AATA 6 (12 January 2011).

151 See ASIC, 'Former Director Disqualified from Managing Companies' (Media Release, 17-309MR, 12 September 2017) <http://asic.gov.au/about-asic/media-centre/find-a-media-release/2017-releases/17-309mr-former-director-disqualified-from-managing-companies/>.

152 For a discussion about the number of referrals currently made, see above n 111 and accompanying text.

153 (2004) 9 VR 549.

154 For a detailed discussion of *Deputy Commissioner of Taxation (Cth) v Casualife Furniture International Pty Ltd* (2004) 9 VR 549, see Anne Matthew, 'The Conundrum of Phoenix Activity: Is Further Reform Necessary?' (2015) 23(3) *Insolvency Law Journal* 116, 127–8.

155 *Corporations Act* s 447A(2).

156 *Deputy Commissioner of Taxation v Woodings* (1995) 13 WAR 189.

Part 5.7B of the *Corporations Act* empowers the liquidator to recover voidable transactions[157] in a variety of situations, subject to defences.[158] These were noted above in the context of the suggested new phoenix offence to target asset transfers. In addition, at the suit of the liquidator, the court can also order equitable compensation for breach of directors' fiduciary duty in the phoenix context.[159]

3 *Breaches of Directors' Duties*

In addition to fiduciary duties and common law duties, the *Corporations Act* imposes a range of duties upon directors and officers, and, in some cases, even on employees.[160] Those duties are: the duty of care and diligence;[161] the duties to exercise powers and discharge duties in good faith in the best interests of the corporation and for a proper purpose;[162] the duties to not use position or information improperly to gain an advantage for oneself or someone else, or to cause detriment to the company;[163] and the duty to prevent insolvent trading by the company.[164] For example, the misuse of position to make a personal gain or to benefit another entity at the time of insolvency in phoenix circumstances is clearly within the scope of s 182 of the *Corporations Act*. ASIC can also bring both civil penalty[165] and criminal action[166] against the company's directors in relation to an uncommercial transaction as a form of insolvent trading.[167] Accessories[168] may also be liable, both for the improper purposes and the two misuse of position breaches,[169] as well as criminal breaches.[170]

However, since civil penalties were introduced for breaches of directors' duties in 1993, there has only been one civil penalty application brought by ASIC for breach of directors' duties in the context of phoenix activity.[171] To put this in perspective, in 2016–17 alone, external administrators reported to ASIC that they suspected 340 criminal breaches of the directors' duties[172] and 1160 civil breaches

157 The court may order, inter alia, payment of an amount of money or the transfer of property: *Corporations Act* ss 588FF(1)(a), (b) respectively.
158 Ibid s 588FG.
159 *HWY Rent Pty Ltd v HWY Rentals (in liq) (No 2)* [2014] FCA 449 (8 May 2014) [6].
160 *Corporations Act* ss 182–3.
161 Ibid s 180.
162 Ibid s 181.
163 Ibid ss 182–3.
164 Ibid s 588G(2).
165 Ibid s 1317J.
166 Ibid s 588G(3).
167 Ibid s 588G(1A) deems the uncommercial transaction to be the incurring of a debt for the purpose of the insolvent trading action.
168 Ibid s 79.
169 Ibid ss 181(2), 182(2), 183(2).
170 *Criminal Code* pt 2.4.
171 *ASIC v Somerville* (2009) 77 NSWLR 110; *ASIC v Somerville (No 2)* [2009] NSWSC 998 (24 September 2009). See further Helen Anderson and Linda Haller, 'Phoenix Activity and the Liability of the Advisor' (2014) 34(3) *Sydney Law Review* 471, 483–6.
172 ASIC Report 558, above n 6, 37 (table 30). This figure includes 117 suspected criminal breaches of the directors' duty to prevent insolvent trading: *Corporations Act* s 588G(3). See also above n 171.

of the s 182 duty.[173] While the wrongdoing reported by external administrators covers circumstances beyond phoenix activity, and these are only suspected rather than proven breaches, these figures suggest that ASIC is not bringing actions for breach of directors' duties in the phoenix context. This concern is now addressed.

4 *Widen Enforcement of* Corporations Act *Provisions*

Effective enforcement not only requires appropriate tools to bring actions; they also need to be in the hands of a funded, motivated party.[174] Given the ATO's exposure to the adverse consequences of illegal phoenix activity, it might seem that new laws should be placed in the *TAA*. However, another approach is to allow the ATO to bring actions under the *Corporations Act*. This could be done by broadening the parties who have a right to seek a remedy for a civil penalty breach under Part 9.4B. Such an expansion is not without precedent: under pt 9.4B s 1317GA(2)(c), the client of a financial services licensee may apply to the court for the refund of a fee claimed by the licensee in breach of s 962P, a civil penalty provision. Allowing a regulator such as the ATO to bring civil remedy actions, such as an action for insolvent trading (as discussed above), would send a powerful message of deterrence, aligning money, motivation and legal means.

Just as the ATO practices considered in Part III of this article could be enhanced, so can those of ASIC. Those ASIC practices with the capacity to deter and disrupt illegal phoenix activity, or enhance recovery of tax revenue, are now examined.

B *Enhanced Prevention and Disruption Measures*

1 *Implement Director Identification Number*

The Government announced that its Illegal Phoenixing Package 'reforms will include the introduction of a Director Identification Number (DIN)' that 'will interface with other government agencies and databases to allow regulators to map the relationships between individuals and entities and individuals and other people'.[175] This reform[176] — the issue of a unique identification number after proof of identity has been provided — has been widely supported.[177] It is an important step

---

173 ASIC Report 558, above n 6, 38 (table 31). In addition, external administrators reported that they suspected 3818 breaches of s 180, 2087 breaches of s 181, 338 breaches of s 183, and 4878 breaches of ss 588G(1)–(2): at 38 (table 31).

174 Anderson, Dickfos and Brown, above n 10, 137–8.

175 O'Dwyer, above n 3.

176 Note that this idea has been around for some years: Helen Anderson, 'An Ounce of Prevention: Practical Ways to Hinder Phoenix Activity' (2013) 25(3) *Australian Insolvency Journal* 16.

177 Productivity Commission, above n 141, 429 recommendation 15.6. Note that the Productivity Commission also endorsed the DIN in its report, *Workplace Relations Framework*, Report No 76 (2015) vol 1, 48; vol 2, 915, 938. A DIN was also supported by the Senate Economics References Committee's inquiry into insolvency in the construction industry: *SERC Construction Insolvency Report*, above n 47, 188 [12.38] recommendation 36 (DIN), 188 [12.39] recommendation 37 (proof of identity). Recommendation 38 called for the *Australian Securities and Investments Commission Act 2001* (Cth) to be amended to require ASIC to verify company information: 188 [12.40].

towards overcoming the difficulties in detecting illegal phoenix activity and bringing enforcement action against it. At present, the registration of an Australian company simply requires the name, address, and date and place of birth of each proposed officeholder.[178] ASIC's current form[179] does not ask for the prior corporate history of its proposed directors, and no supporting evidence about the identity of the proposed directors is required. Nor does ASIC independently verify the information provided to it. Those repeatedly engaging in illegal phoenix activity might try to conceal their later directorships under the guise of a fictitious character, or their own name misspelt or a false date of birth.[180]

In order to implement the proposal, directors of existing companies should be required to quote their DIN at the time of companies' annual reviews or annual returns, and therefore it should only take one annual cycle for ASIC's systems to obtain director identity information for both new and existing companies. Where an existing trading company is purchased, the DIN would be required to be stated on the 'notification of change to directors' form.[181]

A DIN should also be searchable by the public via ASIC's online registers and should reveal present and past directorships. Requiring directors to use their DINs in their dealings with creditors, as the ABN is currently used, would enable creditors to conduct their own self-protection inquiries prior to dealing with companies. This transparency should act as a serious deterrent to directors hoping to conceal their illegal phoenix activity through the formation of a new company. It could alert the ATO to potential wrongdoing where an elderly person with no assessable income (ATO-held information) is the director of numerous companies (ASIC-held information). The wider sharing of information between these agencies is discussed further below.[182]

2 *Review the Incorporation Process and the Legitimacy of Shelf Companies*

The incorporation process can be useful in detecting the creation of companies being set up to engage in illegal phoenix activity. The DIN, used as part of this, would provide significantly more information to ASIC than the present paper form does. An online application system, completed by the applicant, is the most efficient. In the UK, for example, the Secretary of State has been required to provide a streamlined incorporations process that can be completed online on a single occasion.[183] Directors with existing and previous directorships would cite their DIN and the online form would pre-populate with those details. First-timer directors would have little to complete after giving their DIN.

178 *Corporations Act* s 117(2).
179 ASIC, *Form 201: Application for Registration as an Australian Company* (8 February 2018); *Corporations Act* s 117(4).
180 See *SERC Construction Insolvency Report*, above n 47, 187 [12.31].
181 ASIC, *Form 490: Notification of Change to Directors of a Registered Body* (9 May 2018); *Corporations Act* s 601CV(1)(c).
182 Below Part IVC(1).
183 *Small Business, Enterprise and Employment Act 2015* (UK) s 15

The aim here is to equip ASIC with information about this person, allowing the regulator to take appropriate action, which may include placing them on a watch. An equally important aim is to alert the would-be director to the fact that ASIC has this information at its fingertips. They, and their previous corporate histories, are not invisible. Directors would be required to supply any missing information, and if this is false, they may be prosecuted.[184] All of this director and incorporation information would add to the intelligence that ASIC could share with other government agencies.

At present, to register a company, prospective directors must either complete Form 201 and mail it to ASIC with appropriate payment, or must transact through a business service provider who uses software to deal directly with ASIC.[185] This may involve the purchase of an aged 'shelf' company that the business service provider has already registered. In the past, when incorporation involved weeks of delay while forms were being processed, it made sense to be able to acquire an existing company immediately. However, those days have passed, as a company can now be created online within an hour. While the use of shelf companies remains popular with professionals setting up business structures on behalf of clients, it is not unreasonable to require prospective directors to complete the online incorporation form themselves, given the heavy reliance that the Government, through MyGov and other online portals, places on electronic interactions between businesses and their controllers.

The legitimacy of shelf companies is also questionable and this is something the Government should review.[186] In particular, aged shelf companies may make it more difficult for regulators to use data analytics to identify companies that are or may be engaged in illegal phoenix activity. If a short incorporation age is used as one of the parameters for searching regulator databases for 'at risk' companies, aged shelf companies may not be captured by the search. The use of shelf companies of varying ages may create the impression that each company that fails is an established, independent company that has failed due to unforeseen circumstances, rather than part of a deliberate pattern of fraudulent behaviour.

3 *Limit Backdating of Directorships and Abandoned Companies*

At present, the change of directorship form is free to lodge within one month, with a $78 fee for up to one month late, and a $323 fee for more than one month late. These are costs worth incurring to avoid a DPN or liability as a director under the *Corporations Act*.

---

[184] *Corporations Act* s 1308(2), sch 3 item 335.

[185] See ASIC, above n 39.

[186] See Australian Resident Director and Corporate Services, *Australian Pre-Registered Company* (2018) <https://www.ardcs.com.au/corporate-services/australian-shelf-company/>. This site states that the advantages of buying a pre-registered company, instead of a newly incorporated company, include increased business partner confidence, access to restricted services, improved credit options, being favourable for immigration purposes, and contract tendering eligibility. Each appears to be built on a deception that the business is already established. The site states that:

> Older shelf companies give confidence to potential business partners or clients who feel more comfortable dealing with an established company. ARD Corporate Services shelf companies are able to be provided to you with additional services such as existing ABN (Australian Business Number), TFN (Tax File Number) and in some cases, an already opened bank account.

The *2017 Combatting Illegal Phoenixing* consultation paper suggested that there be a rebuttable presumption against resignations lodged more than 28 days late, such that a director would still be liable for misconduct until the time of lodgement.[187] However, rather than a rebuttable presumption, the Government should consider whether the director should simply be liable for all misconduct predating the lodging of the change of directorship form, rather than the date of the purported resignation on the form itself. This would be a significant motivator towards ensuring that the form is lodged. It would not amount to an onerous compliance burden, particularly if the notification could be lodged online instantaneously by the director using their DIN.

If the director is liable for all of their pre-lodgement conduct, the measure requires no independent enforcement either administratively or via court action. The director is simply liable for whatever substantive breach is involved, and it is incumbent on ASIC or the liquidator to bring appropriate enforcement and recovery action. A sole director should ensure that if their involvement with the company is at an end and no other person is willing to be its director, the company should be placed into liquidation.

Disallowing the resignation of a sole director until another was appointed, as a way of avoiding liability for misconduct, was the 2017 consultation paper's suggestion to deal with abandoned companies.[188] However, this suggestion misses the point. Abandoning a company to conceal misconduct would constitute a breach of directors' duty to act with care, for example, because a reasonable director, acting with care and diligence, would not do so.[189] The director abandoning the company cannot escape liability by resigning as part of that abandonment.

Nonetheless, two significant issues here are volume and enforcement. Although ASIC does not publish statistics on the number of companies deregistered after being abandoned, there appears to be about 37 600 companies deregistered by ASIC each year for failure to return forms and pay fees.[190] This is nearly five times the number of companies liquidated. The intent of the Government's suggestion is that by deeming the resignation to be ineffective, the director remains accountable as a director. However, this measure does nothing towards ensuring that the affairs of those abandoned, deregistered companies are investigated or that action will be brought against those directors.

Making it an administrative offence to abandon a company might be a better option, but, again, there is the issue of enforcement. As part of the deregistration process, ASIC can send a penalty notice to the last known address of the last registered director or directors. Whether the penalty is paid is another matter entirely. A much more effective deterrent could be a 'black mark' against the person, via their DIN, such that they cannot become the director of any further company without

---

187 *2017 Combatting Illegal Phoenixing*, above n 4, 13.

188 Ibid 13.

189 *Corporations Act* s 180(1). Note that as a company approaches insolvency, the interests of creditors become the interests of the company for the purpose of a breach of duty under s 181: *Kinsela v Russell Kinsela Pty Ltd (in liq)* (1986) 4 NSWLR 722.

190 Email from Adrian Brown (Senior Executive Leader, Insolvency Practitioners, ASIC) to the author, 18 March 2016 (copy on file with the author).

some specified consequences attaching. As a practical matter, it should be noted here that being a good citizen and voluntarily winding up a company involves extensive paperwork, liquidator costs and the payment to ASIC of a fee.[191] Abandoning the company means ASIC removes the company with no costs and no repercussions. It is, therefore, perhaps not surprising that so many companies are abandoned.

C *Enhanced Information Sharing*

1 *Improve Information Sharing between ASIC and the ATO*

The *2017 Combatting Illegal Phoenixing* consultation paper recommended the creation of a single phone phoenix hotline.[192] This is an excellent initiative for the gathering of information.[193] However, what is most important is that information, once gathered, is shared between regulators. In 2017, the Federal Parliament amended the *Australian Securities and Investments Commission Act 2001* (Cth) to allow ASIC to share confidential or protected information with the Commissioner of Taxation.[194] The amendment was in line with a recommendation of the 2015 Senate Economic References Committee *Construction Insolvency Report*, that 'consideration be given to amending confidentiality requirements in statutory frameworks of agencies participating in the Phoenix Taskforce to permit dissemination of relevant information to the ATO'.[195] The ATO's latest annual report indicates that under Phoenix Taskforce provisions, ASIC made eight requests to the ATO for information, and the ATO initiated 16 disclosures of information to ASIC.[196] This seems a modest amount, given the estimates about the size of the phoenix problem noted above.[197]

However, it is also vital that *non*-confidential information is shared more systematically. A great deal of information about companies and their controllers is gathered by ASIC and is either available from its website without charge or may be purchased. The ATO would benefit enormously from freer and more timely flows of this information.[198] Some specific examples are now considered.

---

[191] See ASIC, *Winding Up a Solvent Company* (15 October 2014) <http://asic.gov.au/for-business/closing-your-company/deregistration/winding-up-a-solvent-company/>. Only companies with assets of less than $1000 may deregister voluntarily, but this also involves paperwork and the payment of a small fee: ASIC, *Closing Your Company* (15 October 2014) <http://asic.gov.au/for-business/closing-your-company/>.

[192] *2017 Combatting Illegal Phoenixing*, above n 4, 7.

[193] See further Helen Anderson, 'Sunlight as the Disinfectant for Phoenix Activity' (2016) 34(4) *Company and Securities Law Journal* 257.

[194] *Treasury Laws Amendment (2017 Measures No 1) Act 2017* (Cth) sch 2, which inserted s 127(2A)(g) into the *Australian Securities and Investments Commission Act 2001* (Cth).

[195] *SERC Construction Insolvency Report*, above n 47, 82 [5.84] recommendation 12.

[196] ATO, *Annual Report 2016–17*, 233.

[197] See above n 21 and accompanying text.

[198] See further Anderson, Dickfos and Brown, above n 10, 137, questioning the ATO's role in phoenix enforcement.

2 *ATO Should Seek ASIC Information about 'Associates' before Issuing ABNs*

ABNs are issued by the Australian Business Register, whose custodian is the ATO. An application by those seeking an ABN for their company requires 'associate details', including the name, date of birth, position held and tax file number of all Australian resident directors.[199] At present, the ATO does consult with ASIC regarding ABN applications, but only to check the validity of the Australian Company Number. It does not check whether any associates of the company are disqualified directors or what other companies those associates own or control. This is an oversight that should be addressed.

3 *ASIC Should Advise ATO about Unpaid Super*

In addition to complaints from employees,[200] super non-compliance is detected and reported to the ATO through third-party referrals. The ATO submission to the Senate Economics References Committee inquiry into the non-payment of the superannuation guarantee noted that in 2015–16, the Fair Work Ombudsman made 2405 referrals, with 73 from super funds, 651 community referrals, 70 internal ATO referrals and 57 from 'other' sources.[201] There was no figure given for referrals from ASIC.

This is not because ASIC is unaware of unpaid super. External administrator reports to ASIC at the conclusion of an insolvency appointment include broad band estimates of unremitted super in each administration.[202] In 2016–17, ASIC's collation of these reports showed that there was unpaid super in 3155, or 40.6% of reports.[203] There were 18 external administrator reports where over $1 000 000 of super was lost; 164 reports of unpaid super between $250 001 and $1 000 000; and 412 between $100 001 and $250 000.[204] These figures alone represent that at the very least, there was over $100 million of unpaid super. They do not take into account the 2561 companies where there was between $1 and $100 000 owing. This is not de-identified statistical information: liquidators, receivers or administrators have looked into the affairs of these companies enough to know that these amounts have not been remitted for their employees, and ASIC knows the names of these companies.

The Senate Economic References Committee recommended that the ATO and ASIC review data sharing so that information on insolvency cases are referred

---

199 Australian Business Register, *Associates' Details* (13 April 2018) <https://abr.gov.au/For-Business,-Super-funds---Charities/Applying-for-an-ABN/What-you-need-for-your-ABN-application/Associates-details/>.

200 These are known as employee notifications.

201 ATO, Submission No 6 to Senate Economics References Committee, *Inquiry into the Impact of the Non-Payment of the Superannuation Guarantee*, 23 January 2017, 10. Similar numbers of referrals were made in 2014–15: 2103, 33, 431, 50 and 50 respectively.

202 This reporting is done in compliance with ASIC, *Regulatory Guide 16: External Administrators: Reporting and Lodging* (July 2008). See further above n 6 and accompanying text.

203 ASIC Report 558, above n 6, 46 (table 37).

204 Ibid.

by ASIC to the ATO.[205] It is not clear why such communication is not already taking place given the legislative power to share this information exists.[206] It might be too late for the ATO to issue a 'standard' DPN where the amount of the liability has been reported, but not paid to the ATO. However, the ATO still has the capacity to issue a 'lockdown' with respect to *unreported* withholding and super liabilities, which are *not* avoided by external administration. Therefore ASIC, unaware of whether a super liability has or has not been reported to the ATO, should report *all* unpaid super information from external administration reporting to the ATO to allow 'lockdown' DPNs to be issued where appropriate and to augment the ATO's risk profile data collection. The external administrator information may or may not relate to illegal phoenix activity, but that is irrelevant: a lockdown DPN does not require any such illegality.

V Conclusion

This article has sought to canvas some practical ways to improve the recovery of taxation revenue, currently lost to the Australian Government as a result of illegal phoenix activity. The difficulty with recovering tax debts where the corporate taxpayer is insolvent is that company failure — with a consequent loss to unsecured creditors — is a legitimate and, indeed, inevitable outcome of allowing businesses to operate as companies. Attacking the improper behaviour of the company's controllers, where the company, rather than those individuals, is the taxpayer, largely confounds the ATO.

Some of the deficiencies in taxation law and its administration were addressed here. These included suggestions for improvements to the DPN regime, the leading tool against illegal phoenix activity. The ATO was also encouraged to make use of the existing 'bottom of the harbour'-inspired *CTOA* provisions that appear highly useful against the wrongdoing of both directors and advisors. This article has also suggested administrative improvements, including: the expansion of the single touch payroll initiative; the ATO being empowered to seek director disqualification; and the ATO being permitted to deny an ABN or issue it conditionally upon payment of a security deposit where serial phoenix operators were involved. The DIN, if introduced as promised, should make these improvements even more effective.

Significantly, this article has recommended that corporate laws, existing or improved, be utilised against tax losses. This is logical given that the source of the ATO's difficulties largely stems from the corporate law principle that a company is a legal entity separate from its directors and shareholders who have no obligation for the company's debts. Many corporate law provisions are presently adequate to punish all of the improper behaviour that constitutes illegal phoenix activity, as well as to recover assets improperly transferred. However, the continued existence of illegal phoenix activity and the comparative rarity with which ASIC brings actions means that changes are required. These include: allowing the ATO to bring civil penalty actions; improving information exchanges between ASIC and the ATO in

205 Senate Economic References Committee, above n 90, 20 [7.26] (recommendation 26).
206 ASIC, *Regulatory Guide 16*, above n 202, [16.18].

relevant areas; improving incorporation processes; attaching consequences to the abandonment of companies; and limiting the backdating of directorships. Some of these suggestions or related ideas are contained in Treasury's *2017 Combatting Illegal Phoenixing* consultation paper. It is to be hoped that the momentum generated by Treasury's paper continues and that legislative and administrative changes follow.