

Would You Like to be a Director? What are the Risks?

There is a lot that goes hand in hand with becoming a director of a company. Acting in the best interest of the company and the fiduciary duties in the Corporations Act 2001 are cornerstones of acting as a Director. But what happens when things go wrong? How much personal liability can be attributed to the director. What happens to the personal assets owned by a director?

The first important point to note is that this Newsletter is merely general advice. If you need specific advice applicable to your circumstances, please contact our office as we immediately engage experts in this field on your behalf.

The following is a summary on the various ways a director may be held personally liable for the debts of the company:

A. Director Guarantees

As the name suggests, a Director Guarantee is one where an individual signs a document promising to pay a company debt if the company cannot pay that debt. Written into many loan documents, it puts the individual on notice that the lender can reach around the company and attack the director personally if the company defaults. This then means the assets owned by the director are at risk of being taken.

Interestingly, we have seen situations where directors have resigned from their positions BUT the lender has kept the guarantee in place. The only way to protect yourself in this scenario is to make sure the loan is completely refinanced with new individual guarantees put in place.

B. Creditor Guarantees

You open up an account with a supplier and sign the form without reading it properly. The form outlines many terms and conditions and the one you didn't see was a guarantee that if the company did not pay, you would cover the debt. We have asked clients "How many Creditor Guarantees have you signed over the years?". Very few directors keep a track of this information but as you can see it is crucial in asset protection.

C. Insolvent Trading

We could fill 20 pages of a newsletter on this topic alone. It's complex but the general idea is that if you as a director know or ought to know that your company cannot pay its bills as and when they fall due, then the director can be held personally liable for the debts raised from that point on. Our recent experience with a Sydney liquidator was less than satisfactory and it was clear they were merely trying to scare the director, our client, into paying the liquidator money that he was not legally obliged to pay.

D. The Australian Taxation Office (ATO)

Then there is the ATO, a whole section on its own. Making directors personally liable for the debts of the company began back in August 1993. Before then, the ATO was ranked high in the pecking order to recover money as a creditor in a wind up. However, many companies were hopelessly insolvent and the ATO often missed out on recovering any unpaid Pay As You Go Withholding (PAYG W the tax withheld on employee's wages). So in August 1993, they gave up their high ranking for the right to go after the director(s) personally. This decision completely changed the landscape around asset protection, as directors moved to protect their private assets.

Since then more and more types of payments have been added to the list where directors may be personally liable. These are summarised as follows:

Type of Payment	Effective Date
PAYG W from above	August 1993
Superannuation Guarantee (SGC)	01 April 2012
Goods and Services Tax (GST)	01 April 2020
Luxury Car Tax (LCT)	01 April 2020
Wine Equalisation Tax (WET)	01 April 2020

The only types of payments not on that list is a company's income tax liability, a company's PAYG Instalment (PAYG I), the General Interest Charge (GIC) and the Shortfall Interest Charge (SIC).

E. NSW State Government

Even the State Government moved to securing actions against directors with:

Type of Payment	Effective Date
Failure to have Workers Comp Policy	~1995
NSW Payroll Tax	01 January 2004

F. How Does a Director Avoid Personal Liability

There are a few rules in this regard.

1. The 30 Days Rule - Firstly a newly appointed director to a company is given 30 days to assess the company's finances and its ability to pay its bills on time. As a new director, you will not be personally liable for amounts owing by the company to the ATO before your appointment, if within the 30 days you cause the company to:

- a. Pay the outstanding amounts, or
- b. Appoint an Administrator, or
- c. Appoint a Small Business Restructure Practitioner, or
- d. Place the company into liquidation.

If you do not do any of the actions plans above, you will be personally liable for the unpaid amounts owing by the company to the ATO before your appointment! Hence why the decision to become a director of a company is a very important one. We can see a rise in the amount of Due Diligence being carried out an individual, before they take up the role as a Director.

2. Lockdown v Non-lockdown Amounts – Broadly speaking a director can avoid personal liability if, the amounts owing to the ATO were **reported** to the ATO in the required timeframes **and** the directors carried out one of the items in the Action Plan at F1 above.

The reporting dates are three months for PAYG W/GST/LCT and WET and 28 days for SGC. Directors cannot avoid personal liability if the PAYG W/GST/LCT/WET/SGC were not reported within the required timeframes, ie the liability is locked down.

Hence why it has become crucial to make sure you meet your reporting deadlines, is lodge your Business Activity Statements (BAS's) and Instalment Activity Statements (IAS's) on time.

Also, placing a company into Liquidation may not necessarily avoid personal liability if the time frames have not been met.

G. What do you do if you Receive a Director Penalty Notice (DPN)

The ATO call them Director Penalty Notices (DPN's) and they are currently issuing a staggering 120 per day!!

If you receive a DPN, the first thing you do is contact our office. We will then identify which reporting period(s) the DPN refers to.

We will also check if any amount has been paid against the debt and if the amount owing to the ATO were reported with the allowed timeframes.

Also, be aware that the ATO sends the DPN to the address as per the details in the Company Statement held by the Australian Securities and Investments Commission (ASIC).

Case after case has been won by the ATO, if the address is factually incorrect, but that it what is on an ASIC search.

H. A Final Word On Trusts

All of the references above are in respect of a company. The same applies to a Trust if the Trust has a Corporate Trustee. Remember that a Trust is not a separate legal entity and only exists because the Trustee makes all of the day to day decisions for the Trust.

So if a Trust has unpaid obligations to the ATO, they may still be traced back to the Director(s) of the Trustee company.

I. Glossary

We've used a lot of acronyms, here is a summary:

ASIC	Australian Securities and Investments Commission
ATO	Australian Taxation Office
BAS's	Business Activity Statements
DPN's	Director Penalty Notices
GIC	General Interest Charge
GST	Goods and Services Tax
IAS's	Instalment Activity Statements
JFK	John F Kennedy
LCT	Luxury Car Tax
PAYG I	Pay As You Go Instalment
PAYG W	Pay As You Go Withholding
SIC	Shortfall Interest Charge
SGC	Superannuation Guarantee

J. Conclusion

Acting as a Director of a company comes with many responsibilities and obligations. Again, I reference the terrific quote from former US President John F Kennedy who said during his State of the Union Address on 11 January 1962 “The time to repair the roof is when the sun is shining”.

Don't wait until it's too late to act. More information on Director Penalties can be found here - <https://www.ato.gov.au/Business/Engaging-a-worker/In-detail/Director-penalty-regime/> and as always, if you have any questions, please contact our office.

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