NEW ANTI-PHOENIXING LEGISLATION

The Federal Government has recently passed new legislation further strengthening its ability to combat illegal phoenix activity and those who engage in it.

Illegal phoenix activity has been described by the Australian Securities & Investments Commission as being where a new company is created to continue the business of an existing company that has been deliberately liquidated to avoid paying outstanding debts, including taxes, creditors and employee entitlements. [1] This often involves directors transferring the assets of an existing company to a new company without paying true or market value, leaving debts with the old company, after which, when the old company is placed in liquidation, there are no assets for the liquidator to sell to pay creditors.

A July 2018 report by PricewaterhouseCoopers, prepared for the Phoenix Taskforce, estimated the annual direct cost to businesses, employees and government as a result of potential illegal phoenix activity to be between $2.85 billion and $5.13 billion in 2015-16.[2]

In the 2018-19 Budget, the Government announced a package of reforms to the corporations and tax laws to combat illegal phoenix activity. The proposed reforms included a range of measures to both deter and disrupt illegal phoenixing and more harshly punish those who engage in and facilitate this activity.

As a result of those proposed reforms, the *Treasury Laws Amendment (Combating Illegal Phoenixing) Act 2020 (Cth)* (the "**Act**") recently received Royal Assent on 17 February 2020.

The Act has introduced four measures to combat illegal phoenix activity; namely:

1. New phoenixing offences and other rules about property transfers to defeat creditors;
2. Improving the accountability of resigning directors;
3. Making company directors personally liable for the company's GST liabilities; and

[1] https://asic.gov.au/for-business/small-business/closing-a-small-business/illegal-phoenix-activity/#:~:text=Illegal%20phoenix%20activity-,Illegal%20phoenix%20activity,taxes%2C%20creditors%20and%20employee%20entitlements.

[2] *Explanatory Memorandum, Treasury Laws Amendment (Combating Illegal Phoenixing) Bill 2019*, paragraph 1.4.

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4. Allowing the ATO to retain tax funds in certain circumstances.

Each will be briefly discussed below.

Creditor-defeating dispositions

Schedule 1 of the Act titled "*Phoenixing offences and other rules about property transfers to defeat creditors*" enacts new provisions to combat creditor-defeating dispositions of company property, to penalise those who engage in or facilitate such dispositions, and to allow liquidators and ASIC to recover such property.[3]

The Act provides that a creditor-defeating disposition in this context is a disposition of company property for less than its market value (or the best price reasonably obtainable) that has the effect of preventing, hindering or significantly delaying the property becoming available to meet the demands of the company's creditors in winding-up.[4]

The concept of a disposition is broad and can include the creation by the company of a right or other interest in property in favour of another person.[5] In the situation where a company disposes of property to one person and that person pays some or all of the consideration to a third party, the company is taken to have made a disposition of the property actually transferred, as well as a disposition of the consideration paid to the third party.[6]

It is also necessary to establish the company received consideration that was less than the market value of the property disposed of and less than the best price reasonably obtainable for the disposition.[7] In this context, market value is said to mean the price that would be paid in a hypothetical transaction between a knowledgeable and willing, but not anxious, seller to a knowledgeable and willing, but not anxious, buyer, who transact at arm's length.[8]

A transaction will be voidable if it is a creditor-defeating disposition made by a company at a time when the company is insolvent, or if, because of the disposition, the company immediately becomes insolvent or enters external administration within the following 12 months.[9]

New amendments contained in in Schedule 1 to the Act make it an offence for a company officer or a facilitator such as a pre-insolvency adviser to cause a company to make a creditor-defeating disposition.[10]

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[3] Ibid, paragraph 2.2.
[4] Ibid, paragraph 2.12; *Treasury Laws Amendment (Combating Illegal Phoenixing) Act 2020 (Cth)* Schedule 1, section 1 and 18; Corporations Act 2001 subsection 588FDB(1) and section 9.
[5] *Treasury Laws Amendment (Combating Illegal Phoenixing) Act 2020 (Cth)* Schedule 1, section 18(2); *Explanatory Memorandum, Treasury Laws Amendment (Combating Illegal Phoenixing) Bill 2019*, paragraph 2.13.
[6] *Treasury Laws Amendment (Combating Illegal Phoenixing) Act 2020 (Cth)* Schedule 1, section 18(3); *Explanatory Memorandum, Treasury Laws Amendment (Combating Illegal Phoenixing) Bill 2019*, paragraph 2.13.
[7] *Treasury Laws Amendment (Combating Illegal Phoenixing) Act 2020 (Cth)* Schedule 1, section 18(1); *Explanatory Memorandum, Treasury Laws Amendment (Combating Illegal Phoenixing) Bill 2019*, paragraph 2.16.
[8] *Explanatory Memorandum, Treasury Laws Amendment (Combating Illegal Phoenixing) Bill 2019*, paragraph 2.18.
[9] *Treasury Laws Amendment (Combating Illegal Phoenixing) Act 2020 (Cth)* Schedule 1, section 19 and 20; *Corporations Act 2001* section 588FE(1)(c), (6B)(a) and (b).
[10] Ibid section 588GAA.

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The object of the new offences is to target asset stripping behaviour designed to avoid a company paying creditors' entitlements.[11]

Improving the accountability of resigning directors

Schedule 2 to the Act is aimed at ensuring that directors are held accountable for misconduct by preventing directors from improperly backdating resignations or ceasing to be a director when this would leave the company with no directors. The purpose of this is to reduce the incidence of illegal phoenix activity and its effect on employees, creditors and government revenue.[12]

Schedule 2 to the Act has instructed the following new laws:

- If the resignation of a director is reported to ASIC more than 28 days after the purported resignation, the resignation takes effect from the day it is reported to ASIC.[13] A company or a director may apply to ASIC or the Court to give effect to the resignation notwithstanding the delay in reporting the change to ASIC.[14]
- A director may not resign from a company if doing so would leave the company without a director (unless the company is being wound up).[15]
- A director may not be removed by a resolution of members of a proprietary company if doing so would leave the company without a director (unless the company is being wound up).[16]

GST Estimates and director penalties

Schedule 3 to the Act allows the Commissioner to collect estimates of anticipated GST liabilities and make company directors personally liable for their company's GST liabilities in certain circumstances.

The pre-existing director penalty regime [17] made directors of a company personally liable for specified taxation liabilities of the company in certain circumstances of non-payment by the company. Under section 269-10, the director penalty regime applied to a company's liabilities to pay to the Commissioner: PAYG withholding amounts; superannuation guarantee charges; and estimates of PAYG withholding liabilities and superannuation guarantee charges.[18] Directors were subject to a penalty if their obligation is unfulfilled by the due date, and new directors that are appointed after the due date, become subject to the penalty if the obligation remains unsatisfied for a further 30 days (section 269-20).[19]

The new legislation now expands upon the pre-existing director penalty regime to enable the Commissioner to collect estimates of anticipated GST liabilities, including LCT and WET liabilities. The Commissioner can also recover director penalties from company directors to collect outstanding GST liabilities, including LCT and WET liabilities, and estimates of those liabilities.

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[11] *Explanatory Memorandum, Treasury Laws Amendment (Combating Illegal Phoenixing) Bill 2019*, paragraph 2.65
[12] Ibid, paragraph 3.1.
[13] *Treasury Laws Amendment (Combating Illegal Phoenixing) Act 2020 (Cth)* Schedule 2, Section 2; Corporations Act 2001 section 203AA(1).
[14] Ibid, section 203AA(2).
[15] Ibid, section 203AB (At page 41).
[16] Ibid, section 203CA.
[17] *Taxation Administration Act 1953*, Schedule 1, Division 269.
[18] *Explanatory Memorandum, Treasury Laws Amendment (Combating Illegal Phoenixing) Bill 2019*, paragraph 4.9.
[19] Ibid, paragraph 4.12

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Retention of tax refunds

Schedule 4 to the Act amends the *Taxation Administration Act 1953* to authorise the Commissioner to retain tax refunds where a taxpayer has failed to lodge a return or provide other information to the Commissioner that may affect the amount the Commissioner refunds.[20] The purpose of this is to ensure that taxpayers satisfy their tax obligations and pay outstanding amounts of tax before being entitled to a tax refund.

Conclusion

The above amendments are part of the ongoing package of reforms to the corporations and tax laws to combat illegal phoenix activity introduced in the 2018-19 Budget.

The new rules about property transfers to defeat creditors and the new restrictions placed upon resigning directors in particular are likely to assist liquidators in respect of investigating the affairs of companies placed in liquidation and the recovery of voidable transactions.

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[20] *Treasury Laws Amendment (Combating Illegal Phoenixing) Act 2020 (Cth)* Schedule 4, section 1.

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