

# Company directors personally liable for GST



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Advising clients on the GST implications of a transaction or conveyance can be an area of risk for solicitors. Is the sale GST-free or subject to the GST Margin Scheme? Ticking a box doesn't make it so. If a client is wrongly advised, the company may find itself with an unexpected (and hefty) GST liability in addition to penalties and interest, and the solicitor may be held liable. Further, recent legislative reforms designed to tackle illegal phoenixing activity, mean that if a company fails to meet its GST obligations when they arise, the company's directors may be personally liable for the unpaid GST increasing the exposure of company directors.

## Snapshot

- Since 1 April 2020 directors have been personally liable for any unpaid GST and other unpaid taxes,
- When advising a company on the sale of a business or property it is prudent to inform the company of the potential liability of its directors and advise the directors to seek independent advice.
- If a client receives a Director Penalty Notice, consider and advise promptly.

The solicitor acting for ABC and its directors does not advise ABC or the directors that the property does not meet the requirements to be considered a supply of going concern.

ABC lodges a GST return for the quarter ending 30 June 2020 ('Initial Date') and does not report a liability in respect of the sale.

Subsequently, the ATO issues an assessment to ABC noting that the sale was not a supply of going concern and therefore ABC has a GST liability of \$250,000. This is due to be paid within 28 days of the assessment ('Due Date'). The company does not have the means to pay.

From the Initial Date, the directors have an obligation to ensure the company's debt is paid or, if that is not possible, to promptly appoint a voluntary administrator/ liquidator.

From the end of the Due Date, if the company has not paid (and an administrator/ liquidator has not been appointed), DPNs can be issued. The amount of the penalty is the unpaid tax liability of the company (i.e. \$250,000) and becomes personally recoverable from the director 21 days after the DPN is issued. If there are multiple directors, each has this exposure.

If GST returns have not been lodged, the Commissioner can issue a DPN based on an estimate of the unpaid tax.

The directors may seek to make a claim against the solicitor for their personal liability.

## FAQS

### What happens if the company pays the overdue debt?

If the company pays the overdue debt, the director penalties will be reduced by the same amount (TAA s 269-40).

### What happens if a director pays the penalty?

If a director pays the penalty, this will be applied towards the debt owed by the company (and should also in turn reduce the penalties for any other directors). The director has a statutory right of indemnity against the company (TAA s 269-45).

## What's changed?

The *Treasury Laws Amendment (Combating Illegal Phoenixing) Bill 2019* was passed by Parliament in February 2020. The legislation amends various provisions of the *Corporations Act 2001*, the *A New Tax System (Goods and Services Tax) Act 1999* and the *Taxation Administration Act 1953* ('TAA') and provides ASIC and liquidators with additional powers to combat phoenix activity.

From 1 April 2020, company directors are personally liable for any unpaid GST, Luxury Car Tax and Wine Equalisation Tax, in addition to the Pay As You Go Withholding and Superannuation Guarantee Contributions debts already captured under the current Director Penalty Notice ('DPN') regime (TAA Pt 4-15). Company directors are under an obligation to ensure that the companies they run pay the above tax debts or, if that is not possible, to promptly appoint a voluntary administrator/ liquidator to the company (TAA s 269-15).

## Case study

Assume ABC Pty Ltd sells a property. The contract for sale is marked as GST-free because the sale is a supply of going concern. However, the property does not meet the requirements to be sold as a supply of going concern. The property is sold for \$2.5M, ex GST, to XYZ Pty Ltd and contracts are exchanged on 1 May 2020 ('Sale').

## Are there any defences?

Yes. It may be a defence if the director was ill or, for some other good reason, can demonstrate they took no part in the management of the company at the relevant time.

A further defence may be that the company had a 'reasonably arguable position' ('RAP') and had taken reasonable care to comply with its tax obligations up to the time the DPN was issued. The best evidence of there being a RAP is a legal opinion confirming that such a position exists (TAA s 269-35).

## What is the impact on directors?

Personal liability means that individual directors face the possibility of bankruptcy and the loss of their personal assets, in the event of their company failing to meet its obligations.

Tax credits can be offset against a DPN liability, so that if a director is due for a tax refund, that money can be used to reduce or settle the DPN debt (TAA s 8AAZLG).

## Are new directors liable?

Yes. New directors can be held personally liable 30 days after their appointment where historical liabilities remain unpaid after the Due Date (TAA s 269-20(3)).

## Are former directors liable?

Yes. If a director resigns after the Initial Date, but prior to the Due Date, they remain liable for the penalty. A director retiring on 20 July 2020 would not avoid the \$250,000 penalty in the above example (TAA s 269-20(1)).

## What should solicitors do to mitigate the risk?

- Inform clients of the legislative change exposing company directors to personal liability for GST.
- Consider expressly limiting the retainer to set out that you are only advising the company and that the company's directors should obtain independent advice.
- If a client company and/or director seeks advice about whether GST is payable, in some cases, obtaining a GST private ruling from the ATO confirming that the transaction is GST-free will provide the certainty required about the status of the transaction.
- If a client director receives a DPN, you should consider and advise promptly. Given the strict time limits, failure by the director to take swift action may mean that a director is not entitled to remission of the penalty.

If you think you may be exposed to a claim arising from your role in the transaction, you should notifying Lawcover promptly. **LSJ**

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