AUSTRALIAN GOVERNMENT

TREASURY

**TACKLING THE BLACK ECONOMY: DESIGNING A MODERN AUSTRALIAN BUSINESS NUMBER SYSTEM**

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**INTRODUCTION**

I thank Treasury for the opportunity to comment on its ‘Tackling The Black Economy: Designing A Modern Australian Business Number System’ Consultation Paper. The Australian Research Council-funded project examining the regulation of illegal phoenix activity that I led has now concluded. Our aim was to devise ways in which this damaging behaviour can be most efficiently and effectively prevented and deterred, without harming legitimate business activities to the detriment of the economy. We produced three major reports: [Defining and Profiling Phoenix Activity](http://law.unimelb.edu.au/__data/assets/pdf_file/0003/1730703/Defining-and-Profiling-Phoenix-Activity_Melbourne-Law-School.pdf); [Quantifying Phoenix Activity: Cost, Incidence, Enforcement](http://law.unimelb.edu.au/__data/assets/pdf_file/0004/2255350/Anderson%2C-Quantifying-Phoenix-Activity_Oct-2015.pdf); and [Phoenix Activity: Recommendations on Detection, Disruption and Enforcement](http://law.unimelb.edu.au/__data/assets/pdf_file/0020/2274131/Phoenix-Activity-Recommendations-on-Detection-Disruption-and-Enforcement.pdf). The views expressed in this submission come partly from our Recommendations report and partly are my own.

The concept of phoenix activity broadly centres on the idea of a corporate failure and a second company, often newly incorporated, arising from the ashes of its failed predecessor where the second company’s controllers and business are essentially the same. Phoenix activity can be legal as well as illegal. Legal phoenix activity covers situations where the previous controllers start another similar business, using a new company when their earlier company fails, usually in order to rescue its business. Illegal phoenix activity involves similar activities, but the intention is to exploit the corporate form to the detriment of unsecured creditors, including employees and tax authorities. The illegality is generally as a result of a breach of directors’ duties in failing to act properly in respect of the failed company and its creditors.

While I agree with Treasury that changes to ABN rules on their own will not stop fraudulent behaviour, **I am strongly supportive of Treasury’s initiatives in reviewing ABNs, as I believe that they have a significant part to play in disrupting illegal activity.**

**RESPONSES TO CONSULTATION PAPER QUESTIONS**

My perspective is that of an academic researching fraudulent abuse of the corporate form. I am not an ABN holder nor am I considering ‘at the coalface’ issues of businesses dealing with ABN holders. For many years, I have been a major proponent of the Director Identification Number (DIN) in Australia, and I am delighted that the Consultation Paper makes the DIN a part of the ABN reforms under consideration.

I divide my comments into three related categories:

1. The level playing field factor

The easier it is to establish a business, the easier it is to create fraudulent arrangements where tax is avoided, employees underpaid and other liabilities shed. This is unfair and financially damaging to law-abiding competitors. Some level of qualification for incorporation and other business benefits such as an ABN is acceptable if it is a short term burden giving a long term benefit. I agree that an ABN is not a right, but rather a benefit to which conditions or obligations can be attached.

The consultation paper asks about periodic renewals of ABNs, with a fee charged for this service. I strongly urge Treasury, business and others to view such ‘paperwork’ requirements *not* as ‘red tape’ but rather as a valuable opportunity for the ATO to weed out wrongdoers. This can have significant benefits for legitimate businesses. In other words, it’s worth the money and the effort in renewing an ABN if cheats are no longer your competitors.

**Clearly, this imposes a significant corresponding obligation on regulators such as the ATO. More must be done to ensure that cheats are effectively dealt with.**

2. Adjusting ABN entitlement rules

I agree that denying an ABN to individuals to disrupt sham contracting is important. I make no comment on how the Australian Business Register (ABR), administering ABNs, can improve its processes to ensure that the ‘right’ people get their ABN promptly and the ‘wrong’ people are denied it.

My contribution here deals with a company’s entitlement to an ABN. There is no logic in automatically granting an ABN to a company but denying it to a person who does not satisfy the enterprise test. It is so simple and cheap to incorporate a company that the ‘automatic ABN for companies’ rule easily works around the denial of ABNs to individuals. Sham contracting of a ‘true employee’ can take place where the individual’s company contracts with the ‘employer’ company.

Quite apart from that, there is presently no restriction on the incorporation of companies, no matter how many previous failed companies a person may be associated with. If the person is not currently disqualified from managing a company, they are at liberty to incorporate and manage dozens of new companies at a time, and all of them are entitled to ABNs.

My view is that the ABR should be the gatekeeper here, particularly as the ATO is a major victim of deliberate insolvencies and illegal phoenix activity. Director penalty notices (DPNs) to recover unremitted PAYG(W), superannuation or GST are ineffective where directors can simply report the company’s obligations, then liquidate it within 21 days of receiving a DPN, start a new company, get a new ABN and carry on as before, accruing debts which will never be paid.

**Therefore, the ABR should have the right to deny, or grant conditionally upon payment of a bond or provision of security, an ABN to companies whose listed associates have a history of unpaid taxes by previous companies with which those people have also been associated.**

This is a different idea to imposing ABN-related conditions on companies with a past history of tax defaults or other non-compliance with government obligations. Remember, the defaulting company can quickly be disposed of, and its cleanskin successor will automatically get an ABN under the present rules.

3. Information flows

I am very pleased to see the commitment to the DIN and Modernising Business Registers project. Illegal behaviour flourishes in dark, uncoordinated spaces. Open flows of current, accurate information between regulators are vital to allow both prevention action – for example, disqualification of directors or denial of an ABN – as well as enforcement action if prevention and deterrence is not effective. The ABR should always check with ASIC that an associate applying for a company’s ABN is not disqualified from managing a company.

As I mentioned above, I support the renewal of ABNs to give the ATO and other regulators access to current information. I believe the renewal process will help address the concerns I have about the availability of shelf companies and fake directors. If a newly incorporated company is established by those with clean records, and those people are the company’s associates when it obtains an ABN, the ABN can then be used by other people who might attract ATO attention if they were the associates at the time of the ABN application. A similar problem occurs where dummy directors or unwitting directors are used to incorporate a company and apply for an ABN. In my view, a renewal process assists in bringing these sorts of situation to light.

The current associate information from ABN renewals should also be available to ASIC, so it can check that disqualified directors are not managing corporations.

**CONCLUSION**

I would be very pleased to discuss these ideas with Treasury.