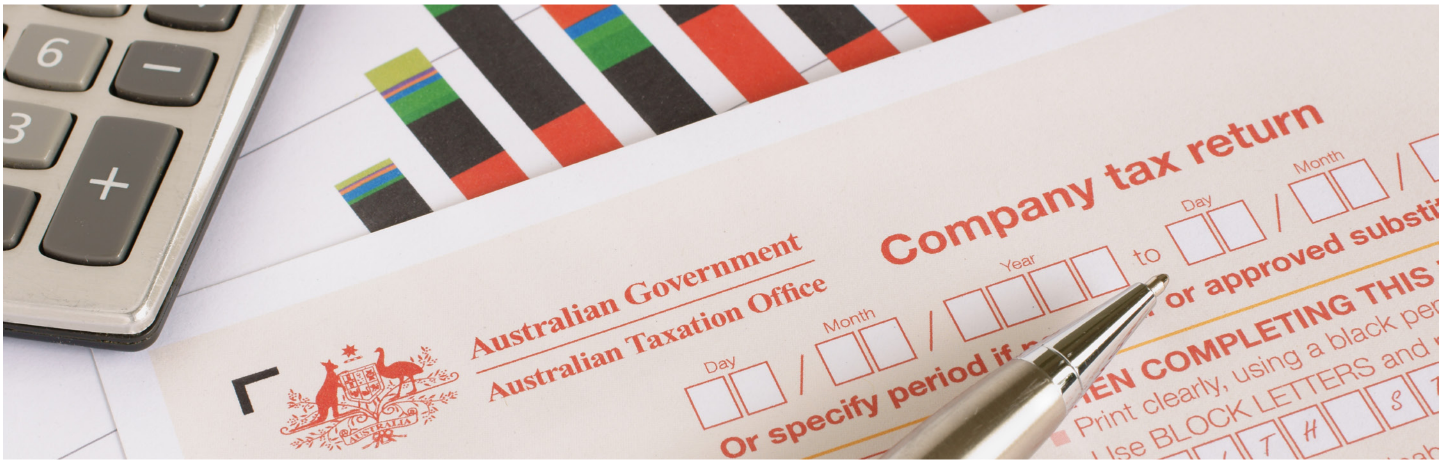
INDUSTRY INSIGHTS

By Peter Krejci

What's normal to the spider is chaos to the fly…



The Federal Government's mid-year budget update in December 2016 included an announcement that will have certain SME business owners (and their advisors) concerned and thinking carefully about using the ATO as an unofficial overdraft to cover their corporate tax obligations.

In this article, we discuss the ATO's changes and the implications for small and medium-sized enterprises (SMEs).

Reigning in SME debt

To help reign in escalating corporate debt, the Federal Government has given the ATO the powers to report delinquent debtors to credit rating agencies (such as Dunn & Bradstreet) unless they have "effectively engaged with the ATO to manage their debts".

Escalating tax debts of around $20 billion are putting considerable pressure on the Government's budget revenue. By improving SME compliance with their tax payment obligations, the Government hopes to relieve some of this pressure. Historically, tax law secrecy provisions prevented the release of such information to credit rating agencies (CRAs). This now appears to have been abandoned to help drive debtor collections.

What does this mean for delinquent SME debtors?

Once aware of a debtor's tax issue, banks and other credit suppliers, may take steps to restrict the debtor's access to credit. They may also pursue recovery of outstanding accounts. This can quickly cripple a business. The Government is banking on the threat of reporting to credit rating agencies to improve the collection of SME debts. We believe this strategy will probably work.

The ATO's latest annual report disclosed total collectable debt of around $20 billion. SMEs accounted for $12.5 billion of this debt. This accumulation of debt is the result of a previous ATO policy which allowed an SME to owe more than $345,000 in back taxes before any legal action was taken.

Whilst there are no available statistics, it is likely that many of these corporates went into some form of external administration. The question being asked by the business community is: why is the Government not taking firmer action to limit ATO losses?

In response, under the new measures announced by the Government, the ATO will be pursuing debts as low as $10,000 and reporting those debtors to credit rating agencies.

What's normal to the spider is chaos to the fly…

Chaos (and concern)

Early feedback from accountants, who are at the coalface of SME compliance, is that the new measures are unfair for business. They believe it is unlikely the ATO will consider the cyclical nature of many SMEs who will, from time to time, delay payment to the ATO before the business cycle changes in the SME's favour. They're worried the measure has the potential to bring a business to its knees should trade suppliers stop providing credit to an otherwise sound business after becoming aware of a default being recorded with a CRA.

Also, a failure to meet statutory obligations will likely constitute a breach of covenant under most bank facilities.

Ordinarily, when seasonal factors are at play, such a breach may never come to the attention of a company's bank. A report to a CRA by the ATO will now mean that a bank will have reason to review a company's performance and reassess their risk profile. This could include instructing an investigating accountant to review the business. The bank may increase penalty interest rates or indeed, request that the company refinance with another bank. This would likely be problematic for the SME. A 'default record' with a CRA will mean the refinancing of a debt facility, if at all possible, will likely be with a 2nd or 3rd tier lender that charges significantly higher interest rates.

Key Takeaway

The ATO's new measures are designed to increase compliance and force SME business owners to meet their statutory obligations.

The ATO has indicated that these measures will initially apply to those debtors who have not actively engaged with the ATO in managing their debts, where their debts are at least $10,000 in value and more than 90 days overdue.

The best insurance for an SME owner experiencing cyclical cash shortfalls or is undercapitalised, is to get in contact with the ATO immediately. Discussing their circumstances and the timing of their outstanding payment(s) should provide comfort to the ATO. Should circumstances change and the business is unable to pay its ATO debt (which may lead to insolvency), at least then the business owner can seek advice about restructuring its affairs either informally or formally. This is better than the ATO 'pulling the rug out from under' a SME by reporting them as delinquent to a CRA.

I believe the ATO will be successful in achieving the Government's goal of reigning in escalating debt and may limit the losses incurred by those non-viable businesses.

However, the key to success for this public policy will be the finesse demonstrated by the ATO to avoid unfairly harming viable SME businesses.

Whilst the ATO seeks to weave its web and catch delinquent SMEs, it's not hard to see how chaos can ensue if the measure is mismanaged, forcing viable SMEs into external administration unnecessarily.

BRI Ferrier

What's normal to the spider is chaos to the fly…

Need advice

BRI Ferrier provides a range of services for distressed and non-distressed property and construction groups, combining extensive experience and knowledge to deliver tailored solutions in a cost effective manner.

If you would like to discuss this matter and how it might affect you or your business please Peter Krejci, who would be happy to discuss this further.

Author

Peter Krejci
Principal
BRI Ferrier, Sydney

T: +61 2 8263 2300
E: pkrejci@brifnsw.com.au

About BRI Ferrier

BRI Ferrier is a unique affiliation of expert business recovery, insolvency, forensic accounting and advisory firms. We provide practical, innovative services that help financially distressed businesses to recover or at least minimise the negative impacts of insolvency.

With over 160 staff and eleven practices in Australia, New Zealand, Hong Kong and the United Kingdom, we work with clients of all types – from individuals, sole traders and small businesses to public corporations and government entities.

We also work with financiers, solicitors, accountants and creditors to address the needs of all stakeholders when businesses face financial challenges.

BRI Ferrier's team has the expertise and resources to meet any client challenge. By combining our skills and enthusiasm, we achieve the best possible outcomes in all cases where a business experiences financial distress.

How BRI Ferrier can help

BRI Ferrier can assess your current situation and advise on a path forward to minimise further risk.

Early intervention is often the key for a successful restructure of your business. If you or your client is experiencing financial challenges then don't delay, contact us today.

For positive solutions to financial difficulties please contact us.
The initial consultation to your client is free, strictly confidential and without obligation.

Sydney
T: 02 8263 2300
info@brifnsw.com.au

Melbourne
T: 03 9622 1800
info@brifvic.com.au

Adelaide
T: 08 8233 9900
info@brifsa.com.au

Perth
T: 08 6316 2600
info@brifwa.com.au

Brisbane
T: 07 3220 0994
info@brifsq.com.au

Cairns
T: 07 4037 7000
info@brifnq.com.au

Townsville
T: 07 4755 3300
info@brifnq.com.au

Mackay
T: 07 4953 7900
info@brifnq.com.au