THE LAW SOCIETY
OF NEW SOUTH WALES

Our Ref: SW:LN:570044
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2 August 2011

Mr Gerry Antioch
General Manager
Tax System Division
The Treasury
Langton Crescent
PARKES ACT 2600

Email: privilege@treasury.gov.au

Dear Mr Antioch,

Privilege in relation to tax advice

The Business Law Committee of the Law Society of New South Wales ('Committee') has had the opportunity to review the Discussion Paper entitled 'Privilege in Relation to Tax Advice'.

The Committee endorses the submission of the Law Council of Australia, dated 29 July 2011, a copy of which is attached for your ease of reference.

Should you have any queries in relation to this correspondence, please do not hesitate to contact Ms Lana Nadj, Policy Lawyer, at lana.nadj@lawsociety.com.au or by telephone on (02) 9926 0375.

Yours sincerely,

Stuart Westgarth
President

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Law Council
OF AUSTRALIA

General Manager
Tax System Division
The Treasury
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PARKES ACT 2600
Email: privilege@treasury.gov.au

Dear Sir/Madam

RE: PRIVILEGE IN RELATION TO TAX ADVICE

I have pleasure in enclosing a submission in response to the Discussion Paper entitled "*Privilege in Relation to Tax Advice*".

The attached submission has been prepared by the Business Law Section of the Law Council of Australia.

Thank you for giving us the opportunity to comment.

Yours sincerely,

W Grant

Bill Grant
Secretary-General

29 July 2011

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Privilege in relation to tax advice

Commonwealth Treasury

29 July 2011

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Introduction

The Law Council of Australia notes the release on 15 April 2011, by the Assistant Treasurer and Minister for Financial Services and Superannuation the Hon Bill Shorten MP, of the Treasury discussion paper entitled "Privilege in relation to tax advice" (**Discussion Paper**)

As Treasury is aware, the Law Council is the peak national representative body of the Australian legal profession, representing approximately 50,000 Australian lawyers, through their representative bar associations and law societies (the "constituent bodies" of the Law Council).

This submission has been specifically endorsed by:

- The New South Wales Bar Association
- Law Institute of Victoria
- ACT Law Society
- Tasmanian Bar
- Law Society of WA
- Victorian Bar Inc
- The Law Society of New South Wales

As the Australian Law Reform Commission (**ALRC**) recognised in its 2007 report – "*Report No. 107: Privilege in Perspective: Client Legal Privilege and Federal Investigatory Bodies*" (**ALRC 107**) – client legal privilege is a fundamental common law right and "plays an important role in the administration of justice more broadly".[1] Equally, investigative activities of government bodies and agencies have an important role to play in the life of the Australian community and in the Australian system of administration of justice and the privilege that has been recognised and upheld is the result of balancing competing community interests in the context of the system of administration of justice.

In its submissions to the ALRC,[2] the Law Council noted its concerns about any attempt to abrogate, codify or modify client legal privilege. Nothing in the ALRC Report supported a need to do so. While ALRC 107 did recommend that professional privilege be extended to cover tax advice documents prepared by registered tax agents, that was not the primary focus of the inquiry the ALRC undertook and the Law Council proposed that this recommendation should not be taken up until it was the subject of a separate and more rigorous review that would consider:

1 ALRC 107, at pages 27-28.

2 See http://www.lawcouncil.asn.au/programs/national-policy/privilege.cfm.

1. the role advisers in other professions play in the system of administration of justice;

2. the duties they owe to that system and the regulatory systems under which their duties and roles are discharged;

3. introducing higher duties beyond duties to clients;

4. introducing regulatory regimes comparable to that which govern lawyers; and

5. clarifying the position of practising lawyers who are also tax agents.[3]

A lawyer's duty to the Court is a duty not often understood in its entirety. First, it is a paramount duty to be observed or performed even if a client gives instructions to the contrary.[4] Second the range of bodies to which it is owed is wide. In Victoria, for example, barristers owe this duty to bodies described as Courts, as well as judicial, statutory and disciplinary tribunals, statutory and Parliamentary investigations and enquiries, Royal Commissions, arbitrations and mediations. Solicitor's rules are not expressed in the same way but cover the same field. As an officer of the court a solicitor's professional duties extend to all legal work. Two Queensland cases (*LSC* v *Mullins* (barrister) and *LSC* v *Garrett* (instructing solicitor)) illustrate the duty not to mislead opponents in mediations.[5]

Without purporting to state exhaustively the requirements of this duty,[6] its performance prohibits, for example, misleading a Court, withholding documents contrary to a client's case, assisting in illegal and /or improper conduct, taking part in deception by a client of another party, involvement in abuses of process and requires the lawyer to provide assistance to the Court.

The importance of the role that lawyers play in the system of administration of justice and the uniqueness of that role cannot be over emphasised.

Chief Justice Keane relatively recently remarked on the role of lawyers and the interface with the courts to the effect that:

> *... the courts are an arm of government charged with the quelling of controversies ... the courts, in exercising the judicial power of the state, are not "providing legal services". The parties to litigation are not acting as consumers of legal services: they are being governed - whether they like it*

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3 Law Council, "Response to the Australian Law Reform Commission Report No. 107 – 'Privilege in Perspective: Client Legal Privilege and Federal Investigatory Bodies'", available at http://www.lawcouncil.asn.au/programs/national-policy/privilege.cfm.

4 *Giannarelli v Wraith* (1988) 165 CLR 543 at 556 and 572.

5 *Legal Services Commissioner v Mullins* [2006] LPT 012 and *Legal Services Commissioner v Garrett* [2009] LPT 012.

6 For more expansive discussion on the extent of the duty and how it is observed see Annesley *R Good Conduct Guide* 2006 The Victorian Bar Inc. and Warren CJ, *The duty owed to the Court – sometimes forgotten* Judicial Conference of Australia Colloquium, Melbourne 9 October 2009 at http://www.supremecourt.vic.gov.au/wps/wcm/connect/justlib/Supreme+Court/resources/2/a/2ad971804056e01ea35abbe505682c73/JCA+Colloquium+Keynote_final.pdf.

or not. ... [and] ... when lawyers act as officers of the court, they ... are participating in that aspect of government which establishes, in the most concrete way, the law of the land for the parties and for the rest of the community. ...[7]

And Warren CJ[8] remarked that:

.... the inherent objective of the lawyer's overriding duty to the court is to facilitate the administration of justice to the standards set by the legal profession. This often leads to conflict with the client's wishes, or with what the client thinks are his personal interests. ... The burden of being a lawyer lies in the lawyer's obligation to apply the rule of law and in the duty 'to assist the court in the doing of justice according to law' in a just, efficient, and timely manner.

and

The duty to the court seeks to preserve this particular relationship [the governmental aspect of the relationship observed by Keane CJ] between practitioner and courts ... .

In more recent times with cost and timeliness of administration of justice having an elevated importance,[9] the role of the lawyer in the system of administration of justice and the duty to the Court in the wider sense includes a duty to assist in efficient Court processes.

Linked to the lawyer's duty to the Court are the lawyer's professional duties concerning conflicts of interest. A lawyer is required to "put at his client's disposal not only his skill but also his knowledge, so far as is relevant".[10] A lawyer also has an obligation to maintain the confidentiality of information provided by a client.[11] Importantly, as observed in *Rakusen* v *Ellis, Munday & Clarke*, "the degree of the confidential character of the relation ... is in the eyes of the law the very highest", and the court "can fix a standard for the behaviour of its own officers which is higher than it would be practicable to exact from persons in other types of confidential relations".[12] Further, the duty of confidentiality goes well beyond communications that are privileged.[13] It is evident that there may be conflict

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7 Address to the Judicial College of Australia in 2009 as quoted by Warren CJ in her paper *the duty owed to the Court: the overarching purpose of dispute resolution in Australia* given to the Bar Association of Queensland Annual Conference, Gold Coast on 6 March 2011.

8 In her paper *the duty owed to the Court: the overarching purpose of dispute resolution in Australia* given to the Bar Association of Queensland Annual Conference, Gold Coast on 6 March 2011.

9 One stimulus for the encouragement of this elevated importance being the decision in *AON Risk Services Australia Ltd* v *Australian National University* (2009) 239 CLR 175.

10 *Spector v Ageda* [1973] Ch 30, at 48 per Megarry J; G E Dal Pont, "Lawyers' Professional Responsibility" (4th Ed, Lawbook Co, 2010), at 107.

11 *Baker v Campbell* (1983) 153 CLR 52, at 65 per Gibbs J; Dal Pont at 231; see, for example, rules 1.1 and 3 of the *Professional Conduct and Practice Rules 2005* (Vic).

12 [1912] 1 Ch 831 per Fletcher Moulton LJ at 840; Dal Pont at 231.

between the obligation of confidentiality that a lawyer owes one client, and the obligation to impart all relevant knowledge to assist another client. In such a case, a lawyer has a conflict of interest and is obliged to cease to act for either party[14].

It is possibly the case that no other professional person stands in the same shoes and bears the same duties as a practicing lawyer who is said to have both

> *... a benefit and a burden. The benefit is obvious; the opportunity to pursue a career in the law as a member of the legal profession. The burden lies in the lawyer's obligation to apply the rule of law and in the duty 'to assist the court in the doing of justice according to law'. It is well-established that, as an officer of the court, a lawyer's paramount duty is to the court as part of the duty to the proper administration of justice. The oath or the affirmation that lawyers take means they have this additional level of responsibility and that they may not be driven by their client's wishes alone.* (Citations omitted)[15]

It is apparent that the Discussion Paper does not address these matters and it is apparent that they have not been considered in its gestation. Accordingly, the Law Council remains of the view that the proposed extension of privilege should not be taken up at this time. That said, the Law Council has some observations concerning the accountants' concession[16] to address various issues which arise in practice.

Below, we address the following matters:

Part 1: Rationale for privilege and concerns regarding any codification or modification;

Part 2: Issues with accountants' concession and possible solutions; and

Part 3: Responses to guiding questions.

The Law Council supports any initiative to enhance the ability of any member of the community to seek advice, not compromised by filtered communication for fear of disclosure, but only where the adviser participant in those communications is subject to the same checks and balances; and rules and regulations as the legal profession. This is critical to ensure the ongoing integrity of administration of the whole justice system, not just part of it.

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13 *Minter v Priest* [1930] AC 558 at 568 per Lord Buckmaster; Dal Pont at 233.

14 *Hilton v Barker Booth & Eastwood*, [2002] Lloyd's Rep PN 500; Dal Pont at 164-5; see, for example, rule 8.4 of the *Professional Conduct and Practice Rules 2005* (Vic).

15 Warren CJ, *The duty owed to the Court – sometimes forgotten* Judicial Conference of Australia Colloquium, Melbourne 9 October 2009 at http://www.supremecourt.vic.gov.au/wps/wcm/connect/justlib/Supreme+Court/resources/2/a/2ad971804056e01ea35abbe505682c73/JCA+Colloquium+Keynote_final.pdf.

16 As set out in the "Guidelines to accessing professional accounting advisors' papers" (**Guidelines**) in Chapter 7 of the Access and Information Gathering Manual of the Australian Taxation Office (**ATO**).

Currently, the legal system operates within a framework of checks and balances, where communications are protected, balanced against a higher duty owed to the judicial system and a comprehensive system of regulation of the adviser participating in that system. This creates an environment that promotes completely open, fearless and unfettered communication so as to procure fearless advice based on all possible facts , without being compromised by the possibility of disclosure. Any extension of the group of advisers whose communications are to be similarly protected ought be accompanied by the same checks and balances, higher duties to the justice system and regulation.

Please contact the Chairman of the Law Council of Australia, Business Law Section, Tax Committee, Teresa Dyson on teresa.dyson@blakedawson.com or 07 3259 7369 if you would like to discuss this submission further.

Part 1: Rationale for privilege and concerns regarding any codification or modification

1.1 Who is entitled to enforce the privilege

In ALRC 107, the Australian Law Reform Commission eschewed the term "legal professional privilege" (as it is referred to in the Discussion Paper) preferring "client legal privilege". This was to make clear that the privilege is an important common law immunity belonging to the client, not the lawyer. In *Baker v Campbell*[17], Murphy J stated that:

> *"The privilege is commonly described as legal professional privilege, which is unfortunate, because it suggests that the privilege is that of the members of the legal profession, which it is not. It is the client's privilege, so that it may be waived by the client, but not by the lawyer."*

This distinction is important to understanding the contemporary rationale and importance of the privilege. The privilege is not something that belongs to or inheres in a profession. Any proposition based on a premise that it does is misconceived.

In fact, client legal privilege is a right of the client; and an obligation of the lawyer, with critically linked liabilities and responsibilities (inseparable from the privilege itself).

1.2 Contemporary rationale for client legal privilege

The primary contemporary rationale for client legal privilege is to encourage full and frank disclosure between lawyers and clients, which assists the administration of justice:

The administration of justice is enhanced when communication between clients and legal practitioners can be completely candid, honest and fearless. The knowledge and assurance that communications are, at the option of the client rather than of the lawyer to be kept absolutely confidential facilitates openness and candour in the lawyer/client relationship. This is important, because we live in a complex society with at times complex laws and legal systems. It is in society's interest that people (including corporations) seek legal advice about their affairs and in seeking advice feel free to disclose all relevant facts and allow advice to be given in that setting rather than in a constrained setting where the efficacy of the advice may be compromised through a failure to communicate pertinent information. The complexity of modern laws is coupled with increasing reliance on self-regulation by the community, for example the self-assessment system of taxation, which elevates the need for advice and for that advice to be obtained and/or given in an efficacious setting.

Lawyers are an integral part of the system of administration of justice. They assist the community with its rights and obligations pursuant to the law. Lawyers undertake this task subject to the burdens of their professional obligations and duties as outlined in the Introduction. The conduct of lawyers is supervised by independent statutory regulators and their duties are ultimately supervised by the Court. Being a participant in communications that attract client legal privilege is an incidental aspect of the lawyer's role and the existence of the privilege both facilitates and compliments its fulfilment. Full and frank communication with a client underpins a lawyer's ability and/or duty to give appropriate advice, to encourage compliance with the law and settlement of disputes, to assist in procuring efficient process and to avoid abuse of process.

[17] (1983) 153 CLR 52, 85 (Murphy J).

The client legal privilege doctrines have developed and now operate in non-curial settings and prevail over administrative process of government bodies and agencies such as coercive information gathering powers found in various statutory settings including each Australian taxing system. Development of the doctrine has been underpinned by a philosophy of advancing the system of administration of justice. The client legal privilege doctrines we have today are the end result of a careful balancing of competing interests: first that of the community interest in furthering the system of justice by protecting confidential communications and second that of the community interest in having government authorities' investigative activities effectively undertaken, within the framework of the administration of justice.[18]

Part of that balance entails the involvement of legal practitioners and the part they play in the system of administration of justice. The higher duties and responsibilities are as outlined. These overarching duties are an important feature of the foundation for the doctrine. In *Prudential plc v Special Commissioner of Income Tax*,[19] the UK Court of Appeal referred (at [43]) to a tribunal decision which stated that privilege should only apply to advice given by:

> *"legal advisers such as solicitors and counsel, who are professionally qualified, who are members of professional bodies, who are subject to the rules and etiquette of their professions, and who owe a duty to the court."*

It is noted that many (though not all) tax advisers may satisfy the first 3 criteria outlined by the tribunal, but will never satisfy the last. The duty to the court is fundamental to the rationale for client legal privilege, because it serves to emphasise that the lawyer's duty is first and foremost to protect the administration of justice and to act as an officer of the Court. That duty is an important check and balance in the system. No other profession is subject to the same duties. As such, the same checks and balances do not exist for other professions. Some to whom the Discussion Paper contemplates the doctrine would be extended are not regulated by any independent body at all.

The regulatory role for the legal profession is carried out by independent statutory regulators in most jurisdictions and will soon be overseen by a national statutory body under the proposed national legal profession reforms. Whilst tax agents are subject to the jurisdiction of the Tax Practitioners Board, there is no over-arching higher duty to a system.

Extending client legal privilege to tax agents also presents difficulties with boundaries. Much of the taxation law turns on other law. For an amount to be deductible it needs to be a loss or outgoing incurred. For an outgoing to have been incurred where the expenditure has not been met requires an analysis as to whether a taxpayer has definitively committed to a liability – typically a matter of contract law. Similarly the attempted sale and lease back of goodwill failed in the case of *Just Jeans* v *Federal Commissioner of Taxation*[20] because as a matter of intellectual property law and/or property law it was not possible to alienate the goodwill of a business independently of the business. These are not topics in respect of which non-lawyers are permitted to advise. This appears to be one of the problems identified by the decision in *Sinclair and Commissioner of Taxation*.[21] Allowing the privilege to be extended to non-lawyers will

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[18] *Grant v Downs* (1976) 135 CLR 674; *Baker v Campbell* (1983) 153 CLR 52, *Attorney-General (NT) v Kearney* (1985) 158 CLR 500

[19] [2010] EWCA Civ 1094

[20] *Just Jeans Pty Ltd v Commissioner of Taxation* (Cth) (1986) 83 FLR 288, reversed in *Federal Commissioner of Taxation v Just Jeans Pty Ltd* (1987) 16 FCR 110.

[21] [2010] AATA 902

lead to greater instance of advisory activities beyond the scope permitted by relevant regulation of the provision of such advice.

Extending privilege, or a limited version of client legal privilege, to other professions simply on the basis that they are authorized to provide advice and administrative assistance in relation to a discrete legal framework is fraught with difficulty. In the *Prudential plc case*, referred to above, Lord Justice Lloyd described those concerns as follows:

> *It is of the essence of [legal privilege] that it should be clear and certain in its application, since it is not the subject of any ad hoc balancing exercise but is, to all intents and purposes, absolute. As applied to members of the legal professions, acting as such, it is sufficiently clear and certain. If it were to apply to members of other professions who give advice on points of law in the course of their professional activity, serious questions would arise as to its scope and application. To which accountants should it apply, given that "accountant" does not by itself denote membership of any particular professional body, or the obligation to comply with any, or any particular, professional obligations? To which other professional advisers would it apply? To what areas of the law would it apply as regards the advice of any adviser who is not a lawyer as such? These questions are serious and important, and would require a clear answer in order that the scope and application of the extended Legal professional privilege should be known and understood.*[22]

Competitive neutrality

The Law Council considers that calls for legal professional privilege to be applied to advice given by tax agents on the grounds of competitive neutrality are ill-considered.

First, such an analysis seriously misconceives what the privilege is about. The privilege is not something enjoyed by lawyers: it is **a right and entitlement of clients that gives rise to** a corresponding ***obligation of lawyers.*** Thus, the extension of the doctrine to remove a competitive advantage is to misunderstand what the doctrine of legal professional privilege is about; in particular the role it plays in the judicial system and the role that lawyers play in upholding that system.

Second legal practitioners and other professionals do not practice under the same regimes. There are different regulatory arrangements, different professional and legal obligations. The legal profession has its features and other professions have theirs. Some are a benefit and some are a burden. A feature of work as a legal professional is the obligation owed to current and former clients in respect of conflicts of interest (see above). The accounting profession is not similarly subject to such a stringent obligation. The consolidation of the accounting profession over the last 15 years may not have occurred if it was subject to the same conflict of interest rules to which members of the legal profession are subject.

Third any competitive advantage for lawyers is not perceived in practice:

1 tax agents generally enjoy the advantage that their work primarily involves preparing and lodging tax returns for clients on an ongoing basis. This means that they are often the first to be consulted on tax issues by clients, which is a significant competitive advantage over lawyers that are not also tax agents;

[22] [2009] EWHC 2494, at [83]

2 in the middle-small market segment of the "taxpayer" community, the observations of the Law Council are that the regular SME professional advisory contact consists of accountants operating as the link between the legal profession and the end-client in the majority of cases. The accountant acts as a filter between the ultimate customer/client and the legal profession, so the accountant is in the position of competitive advantage; not the lawyer.

3 at the large market end of the sector any competitive advantage is less apparent than others. The number of partners and practitioners in large accounting firms providing tax advice, overwhelmingly exceeds the number of partners and practitioners in large law firms providing tax advice and the former firms have more frequent and systematic contact and exposure to the corporate marketplace, not enjoyed by the legal profession. It is a feature of the scope of work that the accounting profession performs that gives this systematic exposure;

4 the size and share of the tax-advisory economy enjoyed by accounting firms represents a significant majority of the amount spent for professional consulting work in a tax setting: indeed, the experience of our members is that taxpayers decide on the basis of expertise and efficiency. For instance, in relation to major projects (eg. public private partnerships), taxpayers have (and commonly exercise) choice whether to consult:

   a) a tax lawyer, on the basis that the tax lawyer can ensure that the tax and legal advice is appropriately integrated and reflects the legal documentation; or

   b) a tax accountant, on the basis that the tax accountant is better placed to review financial models and ensure consistency between the advice and the model.

Overseas experience

As indicated in the Discussion Paper, the two main jurisdictions to have introduced a form of privilege for tax advice are the United States and New Zealand. In the United States, this has been achieved by extending common law privilege to other tax advisers, subject to certain limitations. In New Zealand, this has been done by codifying a completely separate privilege. Both models raise issues as discussed in a recent article prepared by Keith Kendall,[23] although that analysis suggests that the New Zealand model is the preferable of the two.

It is apparent that both models start from the proposition that non-lawyer tax advisors should be placed on a level playing field – or something that approximates it – with lawyers.[24] What is lacking is a focus on clients, who are the intended beneficiaries of any privilege (rather than their advisers and any perceived competitive advantage), and the wider system for the administration of justice. Indeed, discussions with New Zealand lawyers suggest that one of the issues with the codified privilege there is that it is the tax adviser – rather than the client – who makes or waives the claim.

The analysis by Kendall indicates that considerable complexity arises from any attempt to codify a privilege or quasi privilege – in relation to issues such as waiver, use of privileged

[23] K Kendall, "Privilege and Taxation Advice: New Zealand's Nondisclosure Right Compared with the Tax Adviser's Privilege in the United States", (2011) 24 *NZULR* 337.

[24] Ibid, at 339.

material in state rather than federal courts, access to the information by non-tax regulatory authorities, etc giving rise to the need for Parliament's scarce resources to be applied to monitoring divergence between the codified and common law versions. An administrative privilege may, in fact, be more flexible and could still receive Parliamentary oversight if it were made by way of a disallowable instrument.

Moreover, as discussed in **Part 2** below, the main concern with the existing accountants' concession is the ability of the Commissioner to withdraw the concession on what is or may be perceived to be a "whim". However, fixing that does not require legislation. Redesign of the process of reviewing such decisions would be sufficient.

1.3 Conclusion

As indicated above, there are fundamental differences between the role of lawyers as part of the legal system and the role of tax agents in the tax system. These differences mean that there is no warrant for bringing lawyers who happen to give tax advice into a separate tax advice privilege. There are also real issues with extending privilege or something like it to tax agents, who do not share the obligations, training or judicial and regulatory oversight imposed on lawyers. While the Law Council does not suggest that these issues cannot be overcome, they do require more detailed review and analysis (as outlined in the Introduction) than is evident in the Discussion Paper.

Part 2: Issues with accountant's concession and possible solutions

As indicated in **Part 1**, the Law Council does not support the introduction of a "tax advice privilege" at this time. However, the Law Council recognises that there are features of the accountants' concession, or at least the ATO's interpretation of the concession, that impact on its application in practice and which ought to be examined in the context of this review.

In brief, the three key issues are:

- the limited scope of the concession, in that the ATO considers it only applies to written advice from a tax agent to his or her client, and does not extend to requests for such advice or the communication of the advice (eg. notes of a conference with the tax adviser);[25]
- the ability of the ATO to gain access to documents covered by the concession in "exceptional circumstances",[26] without external checks or balances, particularly where Part IVA of the *Income Tax Assessment Act 1936* is invoked; and
- uncertainty as to whether, and in what circumstances, the accountant's concession may be waived by a taxpayer.

We expand on each of these matters below, together with suggestions for reform. For completeness, the Law Council does not share the view of some bodies that the "sole purpose" test embodied in the concession is inappropriate, when compared to the dominant purpose test that applies to legal professional privilege. The nature of tax advisory services provided by tax agents is such that the advice will mostly, if not always, be solely related to advising on tax. By contrast, as well as addressing non-tax legal issues (eg. obligations under the Corporations Act), legal advice may cover other incidental matters, such as board reporting, market disclosure, etc

2.1 Scope of the concession

As indicated above, the ATO appears to take a narrow view of the concession, limiting its scope to the physical manifestation of advice in a letter or other document provided by a tax agent to a taxpayer.

In the Law Council's view, this narrow interpretation is inappropriate as it is:

- inconsistent with the purpose of the concession, as set out in paragraph 1 of the Guidelines that "taxpayers should be able to consult with their professional accounting advisers on a confidential basis to enable full and frank discussion in respect of their rights and objections under taxation laws"; and
- out of step with developments in relation to client legal privilege which recognise that it is the "communication" that is protected, not its physical form.[27]

[25] See item 13 of the Minutes of the National Tax Liaison Group Meeting held in October 2010.

[26] See paragraph 2.2 of the Guidelines.

[27] As Kirby J observed in *Commissioner of Australian Federal Police v Propend Finance Pty Ltd* (1997) 188 CLR 501, 585:-

Further the limitation of the concession to the provision of advice, and not to requests for advice, is presumably based on the notion that requests will only include the factual information necessary for the tax agent to provide the relevant advice. However, as corporate tax teams have developed, they have established an in-house capability to consider the tax issues which their organisations confront. In circumstances where they include detailed analysis in a request for advice, in order to seek external and independent confirmation of their views, it is hard to see a justification for refusing to apply the concession to such communications.

In the Law Council's view, the scope of the concession ought to be extended to address these matters. This would remedy a number of the practical day to day concerns with the concession.

2.2 Exceptional circumstances

The Law Council considers that the ability to override the concession in "exceptional circumstances" is appropriate subject to two matters:

- The application of Part IVA should not, of itself, be regarded as an exceptional circumstance, unless the taxation advice is given to facilitate the commission of a crime, fraud or in pursuit of an illegal or improper object.
- There ought to be a procedure for resolving a dispute as to whether exceptional circumstances exist without having to resort to administrative law proceedings.

We elaborate on each of these matters below.

2.2.1 Part IVA

There is nothing exceptional about the ATO raising the potential application of Part IVA. The experience of our members is that the ATO will often, if not ordinarily, raise Part IVA as an alternative basis for assessment. However, recent case law suggests that the ATO often incorrectly seeks to apply Part IVA.[28]

Importantly, it is transactions to which Part IVA applies that are the very transactions which taxpayers should be encouraged to seek advice upon, and where a "full and frank discussion" is critical. Accordingly, to treat the application of Part IVA, of itself, as an exceptional circumstance allowing access to documents otherwise protected by the accountants' concession is counterintuitive and contrary to the purpose of the concession. Of course, if the advice is given to facilitate the commission of a crime, fraud or in pursuit of an illegal or improper object, then as with legal professional privilege,[29] the concession ought not apply.

"[it] is not the documents, as such, which attract the privilege, still less the information within them. It is the communication to and by the lawyer".

[28] See, for example, *FCT v News Australia Holdings Pty Ltd* [2010] FCAFC 78; *FCT v Ashwick (Qld) No 127 Pty Ltd* [2011] FCAFC 49 and *FCT v AXA Asia Pacific Holdings Ltd* [2010] FCAFC 134.

[29] *Baker v Campbell* (1983) 49 ALR 385, 409-410; *Clements, Dunne & Bell Pty Ltd v Commissioner of Australian Federal Police* (2001) 188 ALR 515.

2.2.2 *Procedure for resolving disputes*

There have been a number of cases where the waiver of the concession has been at issue.[30] As these are necessarily conducted as administrative law proceedings they fail to satisfactorily resolve taxpayer concerns that the ATO can simply waive the concession at its whim.

The Law Council suggests that these concerns could be readily addressed by providing for disputes as to exceptional circumstances to be built into the alternative dispute resolution mechanisms being developed to resolve claims under the accountants' concession.

2.3 Waiver of concession

The concept of waiver of client legal privilege is well developed and understood. What is less clear is whether principles of waiver have any application in the context of the accountant concession although the ATO appears to consider it does.[31]

The Law Council considers it important that it be made clear in those Guidelines when and how the concession may be waived by the acts of a taxpayer.

2.4 Conclusion

In summary, it is the view of the Law Council that the accountant's concession remains an appropriate mechanism to promote full and frank discussions between taxpayers and their tax agents subject to the following refinements:

- Extend the Guidelines to cover requests for advice from a tax agent and to the communication of the advice irrespective of its form.
- Remove the application of Part IVA as an "exceptional circumstance" allowing the ATO to access material otherwise protected by the concession, unless the taxation advice is given to facilitate the commission of a crime, fraud or civil offence or in pursuit of an illegal or improper object.
- Build in procedures for resolving disputes as to exceptional circumstances into the alternative dispute resolution procedures for resolving claims under the concession.
- Amend the Guidelines to provide greater clarity in relation to issues of waiver under the concession.

[30] See, for example, *Deloitte Touche Tohmatsu v FCT* [1998] FCA 1439, *OneTEL Ltd v FCT* [2000] FCA 270 and *Stewart v FCT* [2011] FCA 336.

[31] See paragraph 3.2 of the Guidelines where it is stated that the provision of a list of documents "in no way waives the restricted source and/or the non-source claim".

Part 3: Responses to guiding questions

Below, the Law Council addresses the specific issues that were raised at paragraph 95 of the Discussion Paper:

3.1(a) Are you experiencing any problems with the Tax Office's accountants' concession? If not, what specific problems do you believe exist?

Yes, see **Part 2** above. However, the Law Council considers that these problems can be overcome to ensure the accountants' concession operates appropriately.

3.1(b) Are claims of legal professional privilege or under the accountants' concession causing undue delay to, or frustrating, the functions of the Tax Office or other agencies?

The Law Council reiterates the view submitted to the ALRC[32] that it is not claims for client legal privilege that cause undue delay, but rather deficiencies in the process for resolving such claims efficiently and effectively. This was accepted by the ALRC at paragraphs 6.134 to 6.135 of ALRC 107. In this respect, there is no relevant difference in relation to claims under the accountants' concession.

3.1(c) Does the rationale for legal professional privilege also apply to tax advice communications with an accountant?

As outlined earlier in this submission, the compliance rationale may apply to tax advice communications. However, as noted in **Part 1**, the primary reason for client legal privilege is to promote and protect the administration of justice, which does not apply to advice by tax agents. Tax agents do not owe a duty to the Court or to protect the administration of justice.

3.1(d) Do you think that the current arrangements should be changed by amending the law to provide a privilege for tax law advice given by tax agents?

The Law Council considers that, subject to the changes proposed in **Part 2** of this submission, the accountants' concession is sufficient. Further, if privilege were to be extended to tax agents, this should only be contemplated after conducting a more comprehensive review of the differences in the roles and obligations of tax agents as compared to lawyers.

3.1(e) Would it be preferable to develop the principles and procedures in conjunction with the Attorney-General's Department on a Commonwealth-wide basis, or does the nature of tax advice suggest that it should be developed separately?

The Law Council assumes this question relates to whether the proposed tax advice privilege should be developed as a broader policy in relation to all legal frameworks governing the provision of advice, extending advice privilege to other professions and industry advisers.

As previously noted, the Law Council considers that tax advice privilege should not be formalised and can see no basis for extending privilege to any other industry or

[32] See paragraph 27 of the submission dated 1 November 2007 to the ALRC in response to its discussion paper, available at http://www.lawcouncil.asn.au/programs/national-policy/privilege.cfm.

profession. The Law Council's arguments with respect to the lack of any basis for extending the privilege apply with equal or greater force to other forms of advice.

3.1(f) Are the Tax Practitioners Board requirements equivalent to those imposed on lawyers, as officers of the court? Are any differences relevant in this context?

As outlined earlier in this submission, as officers of the Court legal practitioners are required to protect the administration of justice and promote compliance with the law. Legal practitioners are also subject to a strict regulatory framework and code of conduct.

The Australian Solicitors Conduct Rules, which will harmonise existing standards in each jurisdiction, provide as follows:

Rule 3.1 A solicitor's duty to the court and the administration of justice is paramount and prevails to the extent of inconsistency with any other duty.

Rule 5.1 A solicitor must not engage in conduct, in the course of practice or otherwise, which demonstrates that the solicitor is not a fit and proper person to practice law, or which is likely to a material degree to:

- be prejudicial to, or diminish the public confidence in, the administration of justice; or
- bring the profession into disrepute.

There is no equivalent to these broad principles under the Tax Agents Services Act 2009 (Cth). In this sense, the bar set by the tax agent regime is not at a sufficiently high level. This is compounded by the provisions that grandfathered registration for those who did not meet the required standards under the new rules but were nevertheless included on the basis that they were registered under the pre-existing scheme.

3.1(g) Would the professional confidential relationship privilege provisions of the model Uniform Evidence Bill, combined with the accountants' concession, provide adequate protection for tax advice provided by non-lawyers?

Potentially. However, the Law Council considers that the primary concern in relation to the tax advice concession is the capacity of the Commissioner to revoke the concession whenever it is deemed appropriate.

This concern could be addressed, to a significant extent, by narrowing the scope of the Commissioner's power to revoke the concession and by providing formal guidance on the circumstances in which the power to revoke the concession might be enlivened. Procedures could also be established for the Commissioner to resolve any concerns about whether a claim has been appropriately made.

3.2(a) What procedures should there be to ensure client information is protected, while also ensuring that the proper investigative functions of the Tax Office are not unduly delayed or frustrated? For instance, what penalties should apply for spurious claims? Should the protection extend beyond investigations to protect privileged information in court proceedings?

The first part of the question presupposes that there is a conflict or tension between the protection afforded by a privilege and the *"proper investigative functions of the Tax Office"*. In the case of client legal privilege there is no conflict because, as a fundamental common law right, that privilege must, by definition, be preferred over any investigative

inconvenience, real or perceived. On the other hand, in the case of a putative tax advice privilege (of any sort) a real tension can be seen to emerge. As submitted in **Part 1**, the client legal privilege cannot be equated with a tax advice privilege. It is the prospect of that tension that, as submitted in **Part 1**, raises the need for caution in considering the introduction of a statutory tax advice privilege. The Law Council observes that in those countries that have introduced some form of statutory privilege for tax advice, it has been found necessary to impose limits on the extent of that protection.[33]

As to procedures required to deal with the inevitable conflict arising on the introduction of any tax advice privilege, a useful starting point would be to consider the approach taken by the ATO in Chapter 6 of its Access and Information Gathering Manual. In that regard, the procedures could be based on the following principles:

- Wherever possible, claims for the privilege should be determined under a consultative approach.
- If a claim cannot be determined quickly, the relevant material should be secured (or given to a disinterested party for safekeeping) pending the determination of the claim, with the ATO having no access until the claim is determined.
- Claims that remain unresolved by negotiation, should be resolved, wherever possible, by ADR processes, including review by an independent person (such as counsel) or by mediation.

As to possible "penalties" for claims proven to have been made without justification, they already exist in the uniform penalty regime in Division 284 of Schedule 1 to the *Taxation Administration Act* 1953. Under s 284-75(1), a person is liable to a penalty if they make a false or misleading statement to the Commissioner (eg. a claim for privilege that is falsely asserted). Further, s 284-220(1)(a) provides for a 20% increase in a "base penalty amount" if a person prevents or obstructs the Commissioner in finding out about a tax shortfall or the false or misleading nature of a statement. Alternatively, consideration might be given to an approach similar to that taken in s 264A of the *Income Tax Assessment Act* 1936. Under that approach, a claimant could be denied the right (subject to exceptions) to tender in proceedings material that was subject to unjustifiable claims proven to have been made.

3.2(b) What model would best serve the policy objectives, taking into account international experience? For instance, should Australia codify a privilege for tax law advice provided by tax agents (as in the New Zealand model) or should it simply extend the application of legal professional privilege to tax law advice provided by tax agents (as in the United States model)?

In the submission of the Law Council, neither model is necessary to serve the policy objectives. Rather, as observed in **Part 2**, some modification of the accountants' concession could be made to address the issues which have arisen with the concession in practice.

Having said that, a model that comes closest to the accountants' concession, as modified along the line discussed in **Part 2**, would seem to be a model worthy of further consideration. For the reasons discussed in **Part 1**, the client legal privilege should not, as a matter of principle, be extended to communications with non-lawyers. We note that a

[33] See Kendall, above note 13.

recent comparison of the New Zealand and United States models suggests that the former is preferable.[34]

3.2(c) Should a codified privilege apply equally to communications with lawyers as well as with tax agents, replacing the common law legal professional privilege for tax matters?

No, for the reasons discussed in **Part 1**.

The primary concern of the Law Council is that any statutory regime not weaken or water down the fundamental common law right of client legal privilege. There is no warrant for treating legal advice in relation to tax matters in some different manner to other legal advice, and there was nothing in ALRC 107 that suggested any need to do so.

Where a lawyer is advising on tax, the legal advice will be provided in a broader context, encompassing compliance not just with tax obligations but also with obligations under other legislative frameworks and the common law. This militates against any codification of tax advice privilege to cover both the legal profession and tax agents. In short, for lawyers, there would be insurmountable difficulties in trying to establish where tax advice ends and broader legal advice begins.

We interpret the proposal for a codified privilege to mean that a separate regime would be established that provides immunity from disclosure of tax advice (and certain associated communications and documents) provided by legal practitioners and tax agents to taxpayers (referred to below as "tax advice privilege"). The scope and manner of the suggested regime is not clear to us. We refer to our comments elsewhere in this submission concerning the Law Council's views in relation to the appropriate scope of protection from production of tax advice provided by tax agents.
There are three fundamental considerations that must be taken into account in considering any such proposal.

First, and most importantly, does it promote compliant behaviour amongst taxpayers? In this context, the issue is whether such a reform is likely to facilitate taxpayers obtaining clear, concise, comprehensive and correct advice from appropriately qualified professionals at minimum expense?

Second, and linked to the first, will it promote the more efficient administration of the taxation regime by the ATO?

Third, will it introduce an unwarranted systemic bias in the marketplace for the provision of tax advice?

Turning to the first question, the inferences to be drawn from the suggestion that there be two regimes include that: (a) tax advice privilege will not apply in all the circumstances in which client legal privilege applies and (b) tax advice privilege will not be treated as a fundamental common law right and therefore may be abrogated in circumstances where client legal privilege would not.

Irrespective of whether there be one regimes or two affording immunity from disclosure of certain information communicated or recorded in the course of providing legal services, prudent legal practitioners will continue to conduct their affairs in a manner calculated to afford immunity from disclosure of communications/documents made or prepared in the course of providing legal advice to clients.

[34] Ibid.

The risk that tax advice privilege may not apply where client legal privilege would otherwise apply, and that the disclosure of the former may result in a waiver of the latter, will be a disincentive to legal practitioners to provide integrated legal and tax advice. That separation will necessarily make the communication of tax advice in a straightforward and easily understood manner more difficult. By way of explanation, legal advice in relation to tax law flows from the application of the tax legislation to the proper characterisation at law of the taxpayer's affairs. It follows that it is extremely difficult to separate legal advice in relation to tax and non-tax issues and may result in confusion and uncertainty. This is where the basic distinction between the nature of tax advice provided by legal practitioners and accountants is important. Legal practitioners almost invariably examine and advise upon the proper characterisation at law of the taxpayers' affairs (eg interpreting contracts etc), and how the tax legislation applies to those circumstances. Accounting advisers commonly assume a particular state of affairs (without advising on whether or not that is correct at law) and based on those assumptions advise the client on the application of the tax legislation.

Separating non-tax advice from tax advice will:

(a) not promote the provision of clear and concise advice;
(b) likely result in increased costs to taxpayers of obtaining that advice; and
(c) consequently will not promote compliant behaviour amongst taxpayers.

It follows from the conclusions in relation to the first consideration that the answer to the second consideration must be that it will not promote the more efficient administration of the taxation regime. The principal reason for this is that there will be more non-compliant taxpayers, whether because they have been dissuaded from seeking appropriate legal advice concerning their affairs and the tax consequences that flow by the cost of doing so, or because they have not properly understood the advice provided because of the bifurcated manner in which separated types of privilege encourage legal practitioners to provide, and clients to receive, legal (tax and non-tax) advice.

As to the third consideration the additional administrative difficulties of complying with two privileges, and disaggregating tax and non-tax legal advice, may also create distortions in the market as small legal firms and barristers may not be able to pass on to their clients the cost of dealing with those difficulties. If it becomes desirable because of the differences in the separated privileges - to have different people providing tax and non-tax legal advice then that will have a serious deleterious impact on the ability of small service providers to complete. There is no policy justification for introducing such a bias.

3.2(d) Should a codified privilege extend only to registered tax agents (and their nominees or employees) or should it also cover the advice provided by Business Activity Statement (BAS) agents, and by the employees and nominees of tax agents and BAS agents?

If there is to be a codified privilege, then as discussed in **Part 1**, this should only be contemplated after conducting a more comprehensive review of the differences in the roles and obligations of tax agents and BAS agents as compared to lawyers should be accompanied by a broad replication of the obligations, duties and regulation currently applied to lawyers to ensure the privilege is appropriately framed. That said, it seems more likely that BAS agents would be focused on tax compliance such as preparation of periodic tax returns rather than providing tax advisory services.

3.2(e) Should a codified privilege apply to other financial advisers who provide tax advice, economists advising in respect of transfer pricing, or accountants providing asset and liability valuations in thin capitalisation cases?

If a codified tax advice privilege is established for tax agents simply on the basis of the need for full and frank disclosure, then it is hard to see why the same rationale would not apply to other industries that offer professional or administrative advice, or receive information from their clients for the purpose of assisting them in their affairs.

Indeed, it is noted that extending privilege, or a limited version of client legal privilege, to other professions simply on the basis that they are authorised to provide advice and administrative assistance in relation to a discrete legal framework is fraught with difficulty.

However, as noted above, if privilege is to be extended to other advisers, this should only be contemplated after conducting a more comprehensive review of the differences between the roles and obligations of such advisers and those of lawyers.

3.2(f) Should a codified privilege apply to in-house accountants?

In short, no.

One of the unsettled areas of the law of client legal privilege is its application to in-house lawyers. At paragraph 6.4.4 and 6.4.5 of the ATO's Access and Information Gathering Manual, there is a summary of the position, which (correctly in the Law Council's view) states as follows:

> "*... In Waterford*[35] *it was held that there must be a lawyer/client relationship, and the lawyer's position must have an independent character despite the fact of employment.*
>
> ...
>
> *These requirements of independence and capacity also apply to salaried corporate lawyers. The Tax Office considers that there is uncertainty as to the state of the law on claims for LPP involving in-house lawyer.*[36] *Several lower courts have decided cases on the basis of issues such as independence, capacity and the need for a current practising certificate. However there is some inconsistency between the judgments. Until the High Court authoritatively determines the matter otherwise, the Tax Office acknowledges that legal professional privilege applies to communications to and from salaried lawyers employed by the client provided that the dominant purpose test applies and whether the lawyer:*
>
> - *can demonstrate appropriate independence from the employer client*
> - *was acting in the capacity of a lawyer at the time that the communication was made, and*
> - *has been admitted to practice as a lawyer."* (paragraph number omitted, footnotes in the original)

As difficult as the position might be in relation to in-house lawyers, a key factor which goes to the matter of independence is that legal practitioners provide advice in the context of an overarching duty to the Court. Tax agents, as noted in **Part 1**, have no such duty and it is

[35] *Waterford v Commonwealth* (1987) 163 CLR 54.

[36] See *Southern Equities Corp Ltd v Arthur Andersen & Co* (No 6) [2001] SASC 398 (Unreported).

difficult to see, in the case of tax agents, how appropriate independence could be established. It would be even more difficult to find appropriate independence in in-house accountants who are not tax agents, thus not subject to even the limited statutory supervision under the *Tax Agents Services Act* 2009.

However, as noted above, if privilege were to be extended to in-house accountants, this should only be contemplated after conducting a more comprehensive review of the differences between the roles and obligations of such accountants and those of lawyers.

3.2(g) To which communications or documents should a tax advice privilege apply? For instance, should it extend to the same material that is covered by legal professional privilege, or should it only cover the advice parts of documents as the ALRC has recommended?

The scope of the privilege should be consistent with the comments in **Part 2** as to the scope of the accountants' concession.

3.2(h) What exclusions or exceptions should apply? For instance, should the common law exclusions be imported, or is a wider or narrower set of exceptions appropriate?

The scope of the privilege should be consistent with the comments in **Part 2** as to the scope of the accountants' concession.

3.2(i) Should a tax advice privilege apply only for the coercive information gathering powers of the Tax Office, or also to other bodies such as the Australian Crime Commission?

This question raises many difficult issues, which reinforce the Law Council's view that it cannot support the introduction of a statutory tax advice privilege, at least not without more detailed review and analysis (as outlined in the Introduction) than is evident in the Discussion Paper.

The short point that can be made is that the Australian Crime Commission investigates a wide range of criminal activity. It does not only investigate tax crimes, it covers everything from money laundering to drug related organised crime. The rationale for introducing a statutory tax advice privilege dissipates when it is sought to apply it outside the context of advice on tax laws.

If it should only apply to access attempts by the Tax Office:

- *How should the law deal with cases where another agency holds the information the Tax Office seeks access to?*
- *How would this affect the ability of other law enforcement agencies to access information from the Tax Office?*

Again, this question raises many difficult issues, which reinforce the Law Council's view that it cannot support the introduction of a statutory tax advice privilege, at least not without more detailed review and analysis (as outlined in the Introduction) than is evident in the Discussion Paper.

The short point is that statutory tax advice privilege should operate in a different way to how the client legal privilege operates in those circumstances. This is consistent with overseas experience where a codified privilege has been established.[37]

3.2(j) What would be the appropriate instrument for enactment of a tax advice privilege? For instance, should the provisions be contained in the Taxation Administration Act 1953?

If the rationale for a statutory tax advice privilege is to put tax advice on par with legal advice (a proposition the Law Council does not, in any case, accept), then it would not seem appropriate to enact the privilege in legislation administered by the Commissioner. It would, in the view of the Law Council, make some sense to enact the tax advice privilege in the *Tax Agents Services Act* 2009.

3.2(k) Should any changes to current arrangements be brought into effect as soon as possible, or should they be delayed until the Government is ready to implement a general arrangement for resolving claims of privilege along the lines recommended by the ALRC?

As indicated at paragraph 50 of the Law Council's response to the ALRC report,[38] the Law Council is supportive of introducing an independent review mechanism into the processes for resolving disputes as to client legal privilege (and the accountants' concession). This is consistent with the move towards alternative dispute resolution processes in relation to tax matters generally. That said, the Law Council sees no reason why the reforms to the accountants' concession proposed in **Part 2** above could not be introduced in the meanwhile.

[37] See Kendall, above note 13.

[38] See response dated 28 March 2008 available at http://www.lawcouncil.asn.au/programs/national-policy/privilege.cfm.

Attachment A: Profile of the Law Council of Australia

The Law Council of Australia is the peak national representative body of the Australian legal profession. The Law Council was established in 1933. It is the federal organisation representing approximately 50,000 Australian lawyers, through their representative bar associations and law societies (the "constituent bodies" of the Law Council).

The constituent bodies of the Law Council are, in alphabetical order:

- Australian Capital Territory Bar Association
- Bar Association of Queensland Inc
- Law Institute of Victoria
- Law Society of New South Wales
- Law Society of South Australia
- Law Society of Tasmania
- Law Society of the Australian Capital Territory
- Law Society of the Northern Territory
- Law Society of Western Australia
- New South Wales Bar Association
- Northern Territory Bar Association
- Queensland Law Society
- South Australian Bar Association
- Tasmanian Bar Association
- The Victorian Bar Inc
- Western Australian Bar Association
- LLFG Limited (a corporation with large law firm members)

The Law Council speaks for the Australian legal profession on the legal aspects of national and international issues, on federal law and on the operation of federal courts and tribunals. It works for the improvement of the law and of the administration of justice.

The Law Council is the most inclusive, on both geographical and professional bases, of all Australian legal professional organisations.