PROSPECTS FOR A TAX ADVISORS’ PRIVILEGE IN AUSTRALIA

KEITH KENDALL

Keith Kendall is a Lecturer in the Faculty of Law and Management at La Trobe University.

I INTRODUCTION

As is the case generally in the common law world, communications between legal advisors and their clients in Australia are protected from compulsory disclosure under the doctrine of legal professional privilege. Specifically, such communications need to be for the dominant purpose of (a) the provision of legal advice, or (b) in relation to contemplated or current litigation. While it has been settled that legal professional privilege has been accepted as part of the substantive law in Australia, the content and application of the privilege is still a matter of debate, a state of affairs that at least one Federal Court judge has found surprising. Recent case law in Australia has seen the adoption of a dominant purpose test after almost a quarter of a century of applying a sole purpose test, considered whether the privilege is abrogated by taxation and trade practices legislation and addressed the question of whether the two heads of the privilege are in fact unified by a single rationale. This flurry of curial activity has also sparked a swathe of commentary analysing the role of legal professional privilege in the modern Australian legal setting.

The second head of the privilege, where the communication is made in the context of either contemplated or actual litigation, is usually invoked when a party to proceedings attempts to attach the privilege to communications involving third parties. To qualify for the privilege under this head, the communication needs to have been made for the purpose of intended use in that litigation.

2 The Daniels Corporation International Pty Ltd v Australian Competition and Consumer Commission (2002) 192 ALR 561, 564 (Gleeson CJ, Gaudron, Gummow and Hayne JJ). Note that in that same case, it is also described as being “an important common law immunity” (565), a description the Full Federal Court in Pratt Holdings Pty Ltd v Federal Commissioner of Taxation (2004) 207 ALR 217 used as evidence that the privilege goes beyond being “merely a rule of substantive law”; 207 ALR 217, 219 (Finn J).
3 Finn J, above n 2, 219.
4 Esso Australian Resources v Federal Commissioner of Taxation, above n 1 (overturning Grant v Downs (1976) 135 CLR 674).
5 JMA Accounting Pty Ltd v Carmody 2004 ATC 4916; Pratt Holdings Pty Ltd v Federal Commissioner of Taxation, above n 2 (s 263 Income Tax Assessment Act 1936 (Cth)); Federal Commissioner of Taxation v Coombes 99 ATC 4634 (s 264 Income Tax Assessment Act 1936 (Cth)).
6 The Daniels Corporation International Pty Ltd v Australian Competition and Consumer Commission, above n 2 (s 155 Trade Practices Act 1974 (Cth)).
7 Pratt Holdings Pty Ltd v Federal Commissioner of Taxation, above n 2.
9 Heydon, above n 1, [25235]. This position is usually traced back to the decision in Wheeler v Le Marchant (1881) Ch D 675 (CA).
the profession that third party communications (that is, non-employees or non-agents of the client) need to be directed to the legal advisor, rather than to the client. To insist that the legal advisor acts as the conduit for the privilege to attach, even if the communication was ultimately to be made to the client, was described as an “inevitable and obvious triumph of form over substance”.  

The facts of *Pratt Holdings* were that the taxpayer was restructuring and refinancing its corporate group. In doing so, an issue arose with respect to some accumulated losses within one of the entities in the group. The taxpayer sought advice from its legal advisor, who advised them to obtain a valuation of assets from a large accounting firm to assist in determining the losses. The taxpayer approached the accounting firm directly and received the valuations before passing them on to the legal advisors. During a later tax audit, the Commissioner sought access to the accounting firm’s documents (including working papers). The taxpayer asserted legal professional privilege over the documents held by the accounting firm. The Full Federal Court overturned the finding at first instance, holding that it is not necessary that the communication be commissioned by nor communicated directly to the legal advisor for privilege to attach. Essentially, the Full Federal Court allowed the taxpayer to claim privilege for the provision of legal advice, as no litigation was contemplated at the time the advice from the lawyers was sought.

While this decision may be viewed as expanding the ambit of the privilege in Australia, or at least allowing clients to be somewhat more pragmatic in their affairs, the involvement of a legal advisor is still a necessary requirement. Under the present state of the law, using the facts of *Pratt Holdings*, privilege would not attach to exactly the same communication if the taxpayer had approached the accounting firm for advice on the taxation treatment of the losses without ever involving their legal advisor. While *Pratt Holdings* may be seen as a victory of sorts for a substance over form approach, it is suggested that the chosen profession of the advisor consulted should have no bearing on the outcome of the question of whether privilege will attach to a given communication.

While the involvement of a qualified legal advisor is a feature of the common law privilege in all common law jurisdictions, the United States, since 1998, has extended a similar sort of privilege to tax advisors. In June 2005, legislation was passed by the New Zealand Parliament that introduced a similar extension into New Zealand law. This article will explore the scope for such an expansion to be incorporated into Australian law. This will be done through an examination of the underlying rationale for the common law privilege in Australia, the reasons why the privilege has been restricted to the legal profession, the experience of the United States since the introduction of the statutory privilege and the content of the New Zealand legislation.

II RATIONALE FOR THE PRIVILEGE

The original rationale for the privilege was based on the lawyer’s ethical duty to keep client confidences. This afforded a protection to the lawyer. By the late nineteenth century, the privilege was recognised as protecting the client. The popular formulation of the basis for the privilege is taken from the High Court decision in *Grant v Downs*:

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10 Finn J, above n 2, 219.
11 This was referred to as “advice privilege” in the judgment of the Federal Court (*Federal Commissioner of Taxation v Pratt Holdings Pty Ltd*) (2003) 195 ALR 717, 726.
12 While this may suggest the existence of a unified rationale, the court explicitly did not address this question directly, despite being put forward in argument by the taxpayer.
13 Internal Revenue Code s 7525.
15 *Pratt Holdings Pty Ltd v Federal Commissioner of Taxation*, above n 2, 235 (Stone J).
The rationale of this head of privilege, according to traditional doctrine, is that it promotes the public interest because it assists and enhances the administration of justice by facilitating the representation of clients by legal advisers, the law being a complex and complicated discipline. This it does by keeping secret their communications, thereby inducing the client to retain the solicitor and seek his advice, and encouraging the client to make a full and frank disclosure of the relevant circumstances to the solicitor. The existence of the privilege reflects, to the extent to which it is accorded, the paramountcy of this public interest over a more general public interest, that which requires that in the interests of a fair trial litigation should be conducted on the footing that all relevant documentary evidence is available.16

Similar statements of the purpose of legal professional privilege can be found in most common law jurisdictions.17

Subsequent statements have emphasised the importance of protecting the individual, particularly from intrusion into their private affairs by the state, and creating a climate in which their legal advisors may be fully abreast of the relevant facts in order to provide appropriate advice. For example, Dawson J in Baker v Campbell18 stated that:

[I]f a client cannot seek advice from his legal adviser confident that he is not acting to his disadvantage in doing so, then his lack of confidence is likely to be reflected in the instructions he gives, the advice he is given and ultimately in the legal process of which the advice forms a part.19

Further, Deane J stated in the same case:

That general principle represents some protection of the citizen – particularly the weak, the unintelligent and the ill-informed citizen – against the leviathan of the modern state. Without it there can be no assurance that those in need of independent legal advice to cope with the demands and intricacies of modern law will be able to obtain it without the risk of prejudice and damage by subsequent compulsory disclosure on the demand of any administrative officer with some general statutory authority to obtain information or seize documents.20

Concerns such as these have long been held in the common law, as evidenced by Jessel MR’s statement in Anderson v Bank of British Columbia21 over a century before Baker v Campbell. Further, Lord Brougham LC identified these issues and the concomitant public interest balancing act in Greenough v Gaskell:

It is not (as has sometimes been said) on account of any particular importance which the law attributes to the business of legal professors, or any particular disposition to afford them protection … But it is out of regard to the interests of justice, which cannot be uphelden, and to the administration of justice, which cannot go on without the aid of men skilled in

17 For example, Greenough v Gaskell (1833) 1 My & K 98, 103; 39 ER 618, 621 (United Kingdom); Fisher v United States 425 US 391, 403 (1976); Upjohn Co v United States 449 US 383, 391 (1983) (USA); Solosky v Canada (1979) 105 DLR (3d) 745, 755-757 (Canada); Commissioner of Inland Revenue v West-Walker [1954] NZLR 191, 219 (New Zealand).
19 Ibid, 130.
20 Ibid, 120.
21 Anderson v Bank of British Columbia (1876) 2 Ch D 644, 649.
jurisprudence, in the practice of the courts, and in those matters affecting rights and obligations which form the subject of all judicial proceedings. If the privilege did not exist at all, every one would be thrown upon his own legal resources. Deprived of all professional assistance, a man would not venture to consult any skilful person, or would only dare to tell his counsellor half his case.  

McNicol asserts that the rationale presented applies only to the first head of the privilege. This is on the basis that the first head is justified on the basis that it engenders an environment in which the client is free to confide in their legal advisor without fear that such confidences will be compulsorily disclosed to the client’s prejudice. This has traditionally not enabled communications involving a third party to be covered by the privilege. For such third party communications to attract the privilege, the communication must have been made with litigation in mind. The communication may be between the legal advisor and the third party without any involvement of the client. Consequently, the state of mind of the client, specifically, whether the client felt comfortable making the relevant disclosure to the legal advisor, does not apply in these circumstances. However, while the Full Federal Court in _Pratt Holdings_ did not directly address the question of whether the two heads are based on a unified rationale, the finding that communications between a legal advisor and third party were privileged even in the absence of anticipated litigation goes some way to suggesting that a single rationale underlies both. This rationale would appear to be a public interest in the form of the promotion of the administration of justice through the services of trained professionals, namely lawyers. Such promotion necessarily would be based on candour and trust. Such a unified rationale was contemplated by McNicol.

Prior to examining the reasoning for restricting legal professional privilege to communications with qualified lawyers, it is relevant to consider the application of statute. Sections 118 and 119 of the _Evidence Act 1995_ (Cth) provide for a “client legal privilege” in federal proceedings that is substantially the same as the common law legal professional privilege. The major difference between the statutory privilege and the common law privilege prior to 1999 was that the _Evidence Act 1995_ used a dominant purpose test, whereas the common law privilege used a sole purpose test in identifying communications that attracted the privilege. The High Court in _Esso Australia Resources_ used the statutory dominant purpose test as evidence that legal values had moved on from those that applied when _Grant v Downs_ was decided and held that the common law test should be one that adopted the dominant purpose test, making it consistent with the statutory privilege.

However, the High Court stated in _Esso Australia Resources_ that the statutory privilege in the _Evidence Act 1995_ only applies to the adducing of evidence. The common law privilege extends beyond the adducing of evidence during trial, encompassing such matters as discovery and inspection of documents. In taxation matters, specifically s 263 and s 264 investigations, assertions of legal professional privilege are made in the context of access, rather than litigation.

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22 Above n 17.
24 This head was referred to as “litigation privilege” by the Federal Court in _Federal Commissioner of Taxation v Pratt Holdings Pty Ltd_, above n 11, 726.
25 Where applicable, this term is used throughout to refer collectively to barristers and solicitors.
26 McNicol, above n 23.
27 Section 120 provides a similar privilege to unrepresented parties.
28 _Esso Australian Resources Ltd v Federal Commissioner of Taxation_ (1999) 201 CLR 49.
29 Ibid, 55.
Consequently, the privilege given to litigants by the *Evidence Act 1995* is insufficient to prevent the Commissioner accessing sensitive documented communications.\(^\text{30}\)

### III RATIONALE FOR RESTRICTING THE PRIVILEGE

It should be noted explicitly that support for legal professional privilege is not universal. This stems from the delicate balancing act asked of the courts. Some very eminent jurists prefer the public interest of truth in litigation served by full disclosure in open court to the public interest of full and frank disclosure to trained legal advisors encouraged by the privilege. For example, to justify limiting the scope of legal professional privilege so that the other considerations of the public interest are not unduly affected, Mason J (as he then was) stated:

Notwithstanding strong judicial assertions of the value of the public interest said to be promoted by the privilege [referring to *Greenough v Gaskell* as an example], it is by no means self-evident that the value of this public interest is greater than the public interest in facilitating the availability of all relevant materials for production in litigious disputes.\(^\text{31}\)

Other comments have been directed at specific aspects of the privilege. For example, Pincus J in *Dingle v Commonwealth Development Bank of Australia*\(^\text{32}\) described the law relating to privileged third party communications as a “rather unattractive body of doctrine”.\(^\text{33}\)

Despite such reservations, though, it is quite clear from the present state of the case law that third party involvement does not necessarily abrogate any claim to legal professional privilege. However, the one thing that is quite clear is that an appropriately legally qualified professional must have some connection to the communication. Even in *Pratt Holdings*, where the Full Federal Court quite openly adopted a substance over form approach, the communication that was the subject of the dispute was made at the instigation of the lawyer. The accountant’s valuation would never have been made if it were not required for the purpose of supporting the lawyer’s subsequent advice.

There is currently no provision within the common law for communications between persons and their non-legally qualified professional advisors, such as accountants, surveyors or merchant bankers, to be protected by the privilege. The courts have previously rejected arguments for the extension of the privilege to other professional advisors that were based on client communications made in an environment of confidence.\(^\text{34}\)

Notwithstanding such judicial restraint, commentators have continued periodically to argue for extending the privilege to other professionals under certain circumstances. For instance, Baxt argues for the privilege to be extended to professional advisors under circumstances where the services they provide their clients is not materially different from the services provided by lawyers. Allowing privilege to attach to communications made with a legal advisor and not if the communication is made with some other form of professional advisor provides a comparative

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\(^\text{30}\) It should be further noted that, as the *Income Tax Assessment Act 1936* is a Federal Act, the consideration that the *Evidence Act 1995* is limited in its application to proceedings in federal and ACT courts is irrelevant.


\(^\text{33}\) Ibid, 243.

\(^\text{34}\) *Chantrey Martin & Co v Martin* [1953] QB 286; [1953] 2 All ER 691.
advantage to the legal profession. Similar concerns have been raised in New Zealand and the United States specifically in relation to tax matters.

Italia also argues for the extension of privilege with respect to tax advice to accountants not only on the basis of the similarity of services provided by the two professions, but also through reference to the encouragement of full and frank disclosure in communications.

It should be noted, though, that the courts are not oblivious to the notion that other professional relationships are based on a high degree of trust and confidence between the professional and their clients. In rejecting the extension of the privilege to other forms of relationship, Jessel MR stated in Wheeler v Le Marchant:

In the first place, the principle protecting confidential communications is of a very limited character. It does not protect all confidential communications which a man must necessarily make in order to obtain advice, even when needed for the protection of his life, or of his honour, or of his fortune. There are many communications which, though absolutely necessary because without them the ordinary business of life cannot be carried on, still are not privileged. The communications made to a medical man whose advice is sought by a patient with respect to the probable origin of the disease as to which he is consulted, and which must necessarily be made in order to enable the medical man to advise or to prescribe for the patient, are not protected. Communications made to a priest in the confessional on matters perhaps considered by the penitent to be more important even than his life or his fortune, are not protected. Communications made to a friend with respect to matters of the most delicate nature, on which advice is sought with respect to a man’s honour or reputation, are not protected. Therefore it must not be supposed that there is any principle which says that every confidential communication which it is necessary to make in order to carry on the ordinary business of life is protected. The protection is of a very limited character, and in this country is restricted to the obtaining the assistance of lawyers, as regards the conduct of litigation or the rights to property.

With respect to arguments for extending legal professional privilege to other types of confidential professional advice, the opening words of the quotation taken from Greenough v Gaskell reproduced earlier set out the common law justification for restricting the privilege to the legal profession. The law does not attempt to elevate the status of the legal profession nor give its members a comparative advantage over other professions by keeping their communications with their clients secret. The privilege is not designed to encourage citizens to seek the services of a lawyer in preference to some other equally capable professional. Nor is it designed to encourage full and frank disclosure per se. It is the administration of justice that is the raison d’être for the privilege. Stone and Wells go so far as to describe the privilege as existing not for protecting confidences, but for ensuring that confidences continue.

39 Above n 9, 681-682.
40 Greenough v Gaskell v Gaskell (1833) 1 My & K 98, 103; 39 ER 618, 621.
As the administration of justice is the basis for the privilege, arguments based upon the notion that the delineation between the work of lawyers and that of other professionals is no longer as clear cut as it may once have been fail to address the central issue. While the original basis for the privilege was the maintenance of client confidences, the law now values the indirect role the privilege plays in upholding the integrity of the legal system as a whole. The maintenance of confidences is only a secondary consideration. The privilege is based upon the notion that a legal system, especially an adversarial system such as that operating within common law jurisdictions, is heavily dependent on the practising members of the legal profession. For these members to be able to operate effectively, it is necessary for them to be aware of all aspects of their client’s circumstances. The absence of the privilege to ensure that these specific types of communication are kept confidential is considered to be detrimental to the trust relationship at the heart of the lawyer-client relationship. If clients are aware that their confidences may be broken through compulsory disclosure at a later point in time, the concern is that such clients will only provide favourable information to their legal representatives, impeding the effective administration of the legal system. Such considerations led McNicol to regard as dangerous, analogies between the lawyer-client relationship and other professional relationships, where those analogies are based in large part on the maintenance of confidences as justification for the extension of the privilege. McNicol submitted that Dixon J’s reasoning that an inflexible rule had been “established that no obligation of honour, no duties of non-disclosure arising from the nature of a pursuit or calling, could stand in the way of the imperative necessity of revealing the truth in the witness box” was to be preferred.

Such reasoning becomes weaker, however, when non-lawyers begin to play a role in the administration of justice (through participation in the legal system). For present purposes, it is acknowledged that a close similarity in the substance of the professional services supplied by lawyers vis-à-vis non-lawyers is not a basis in and of itself for extending privilege to non-lawyer relationships. However, once that “close similarity” is transformed into an identity, the restriction of the privilege becomes much more difficult to justify.

Under the Australian *Income Tax Assessment Act 1936*, s 251L(1) states:

Subject to this section, a person who is not a registered tax agent must not knowingly or recklessly demand or receive any fee for:

(a) preparing or lodging on behalf of a taxpayer a return, notice, statement, application or other document about the taxpayer’s liabilities under a taxation law; or

(b) giving advice about a taxation law on behalf of a taxpayer; or

(c) preparing or lodging on behalf of a taxpayer an objection … against an assessment, determination, notice or decision under a taxation law; or

(d) applying for a review of, or instituting an appeal against, a decision on such an objection; or

(e) on behalf of a taxpayer, dealing with the Commissioner or a person who is exercising powers or performing functions under a taxation law.

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43 McNicol, above n 23, 5.
44 Ibid, 4.
45 *McGuinness v Attorney-General (Vic.)* (1940) 63 CLR 73, 102-103.
Subsection 251L(8) provides an exception from the registration requirement for barristers and solicitors acting in the course of their profession.

As a result of s 251L, it is not necessary to be a member of the legal profession to provide advice on a taxation law (or other services commonly associated with the legal profession). While many tax agents will be members of either the legal or accounting professions, this is not a requirement either. Qualification for registration as a tax agent in Australia is determined primarily by the amount of experience obtained in applying tax laws (principally in the form of the preparation of income tax returns) and level of relevant education obtained (which determines the amount of work experience required before being qualified to apply for registration).

As it is not a prerequisite to be a member of the legal profession to provide advice to clients on matters involving the interpretation of tax legislation, as it is in most other areas of legal practice, extending legal professional privilege only to members of the legal profession and not other persons qualified to advise on taxation law, even where the advice would be identical, is anomalous. In being able to provide tax advice, tax agents that are not members of the legal profession play just as much of a role in the administration of justice as do lawyers. Any arguments in favour of legal professional privilege protecting communications with lawyers on tax related matters apply equally strongly to tax agents generally.

In recognition of the confidential nature of many communications that taxpayers have with their accounting advisors (who, more often than not, would be their sole source of taxation advice), the Australian Taxation Office (ATO) has produced some guidelines for its officers to follow when seeking access to accountant’s documentation. The guidelines in relation to access to accounting advisors’ papers are incorporated into Chapter 7 of the ATO’s more general Access and Information Gathering Manual under the heading of “Guidelines to Accessing Professional Accounting Advisors’ Papers” (“the Guidelines”). These Guidelines are essentially an internal document designed to guide the activities of the ATO’s officers, but they are available to the general public as part of the ATO’s requirement for transparency in its operations. Chapter 7 was compiled in consultation with the major professional accounting and taxation organisations in Australia.

The Guidelines make the distinction between three types of documents, being source documents, restricted source documents and non-source documents. Source documents are those documents that are “prepared in connection with the conception, implementation and formal recording of a transaction or arrangement and which explain the setting, context and purpose of the transaction or arrangement”. The ATO considers such documents as being freely available for inspection as part of the appropriate exercise of its access powers. Restricted source documents are those documents that fit the description of source documents but are prepared for the sole purpose of advising the client on taxation matters that call for a degree of candour. The ATO will only seek access to such documents in exceptional circumstances. Non-source documents are documents that do not relate to a transaction or arrangement entered into by the taxpayer. For example, advice relating to the application of the law to a transaction suggested to the client but not ultimately entered into would be a non-source document. These are treated in the same fashion as restricted source documents.

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46 The term “taxation law” is defined in s 995-1(1) of the Income Tax Assessment Act 1997 as any “Act [or related regulations] of which the Commissioner has the general administration”. As well as the two Income Tax Acts, this includes fringe benefits tax legislation and the goods and services tax legislation.

47 Reg 156 Income Tax Regulations 1936.

48 In particular, the Australian Society of Certified Practising Accountants, the Institute of Chartered Accountants in Australia, the National Institute of Accountants and the Taxation Institute of Australia.

49 Australian Taxation Office, Guidelines to Accessing Professional Accounting Advisors’ Papers para 2.1 (as updated to 17 December 2004).
The Guidelines essentially act as an administrative restriction on the ATO to the effect of extending a privilege akin to legal professional privilege to the relevant documents (specifically, restricted source and non-source documents). For example, the restriction may be waived in circumstances similar to the waiver of legal professional privilege (such as through voluntary disclosure to an independent third party on a non-confidential basis).\(^\text{50}\)

However, while this administrative restriction is an admirable recognition by the ATO of the realities of business and accounting practice, it does not have the backing of either statute or common law behind it. Consequently, the Guidelines do not provide additional legal rights to taxpayers, although they do create a legitimate expectation that, in the exercise of the Commissioner’s access and investigatory powers, ATO officers will adhere to their terms.\(^\text{51}\) This means that the ATO can still access restricted source and non-source documents in certain circumstances. For example, the Guidelines only protect the relevant documents if they were prepared for the sole purpose of advising on taxation matters. Legal professional privilege uses a dominant purpose test. Further, the Guidelines set out that if the Commissioner is unable to obtain sufficient factual information (which is not specifically defined) from other sources, this lack of information can form the basis of circumstances in which the ATO will seek access to restricted source and, possibly, non-source documents.\(^\text{52}\) As such, it can be appreciated that the administrative restriction set out by the Guidelines falls far short of the protection afforded by legal professional privilege to professional communications.

An interesting alternate perspective on the relationship between the Guidelines and common law legal professional privilege is put by Morfuni.\(^\text{53}\) As noted, the Guidelines create a legitimate expectation for accountants. Morfuni claims that, as a result, accountants now enjoy a greater protection than lawyers. This is on the basis that the creation of a legitimate expectation makes the issue of a s 264 (and also, presumably, a s 263) notice by the Commissioner to be a reviewable decision, as the Commissioner has conceded that access to certain documents will only be made in exceptional circumstances. Lawyers have no right of review of the issuing of such notices. The availability of administrative review rights, for accountants, appears to confer additional avenues of redress for accountants.

Such arguments, however, do not take into account that, while at least two Federal Court decisions have found that the Guidelines do create a legitimate expectation with the resultant review rights, the legitimate expectation is only that the Guidelines will be given sufficient weight by the ATO officer in determining whether exceptional circumstances exist to access the relevant documents. In *Deloitte*, Goldberg J held that it was not for the court, but the ATO officer to determine whether the appropriate weight had been given to the terms of the Guidelines.\(^\text{54}\) As such, so long as the ATO officer can demonstrate that regard was had for the Guidelines, it is difficult to conceive of circumstances in which an accountant will be successful in using the Guidelines as a vehicle to deny the ATO access to documents. As the Commissioner’s access powers are subject to legal professional privilege, documents held by lawyers enjoy the greater protection as, once it is found legal professional privilege applies to the communication, access is denied regardless of the circumstances.

\(^{50}\) Ibid, para 4.
\(^{51}\) *Deloitte Touche Tohmatsu v Federal Commissioner of Taxation* 98 ATC 5192; *One.Tel Ltd v Federal Commissioner of Taxation* 2000 ATC 4229.
\(^{52}\) Australian Taxation Office, above n 49, para 6.
\(^{53}\) Morfuni, above n 8.
\(^{54}\) *Deloitte Touche Tohmatsu v Federal Commissioner of Taxation*, 98 ATC 5192, 5208.
At the other end of the spectrum, suggestions have also been made to abolish legal professional privilege in respect of matters involving the genuine exercise of the relevant revenue authority’s investigatory powers. For example, in New Zealand, the Winebox Inquiry\textsuperscript{55} and a majority of the Law Commission in 2000 (in relation to matters not involving litigation)\textsuperscript{56} recommended that legal professional privilege be abolished in relation to tax matters. Such calls are often on the basis that taxation is a special case as the “existence of a solid tax base is essential to the efficient functioning of a developed state”.\textsuperscript{57} Preventing the revenue authorities from accessing taxpayer’s communications (usually documents) hinders the efficient execution of their statutory powers and responsibilities. Further, some concerns have been raised that a number of claims to legal professional privilege are dubious,\textsuperscript{58} thereby exacerbating the problems associated with reconciling a long established common law right with the more pragmatic task of ensuring appropriate compliance with taxation laws.

Kayle sets forth a number of additional arguments for legal professional privilege to not apply in taxation matters at all.\textsuperscript{59} Kayle distinguishes taxation law from other areas of law, such as environmental and trade practices law, on the basis that tax law does not mandate or prohibit specific conduct, with a few trivial exceptions such as the filing of returns. Rather, tax law sets out the consequences of transactions under the law. As tax advice will be slanted more towards tax minimisation, rather than compliance with the law (as is the case in other areas of the law), justifications for the privilege on the basis that it promotes compliance with the law through the efficient administration of justice are substantially weakened. Further, tax law is more general and far reaching than almost any other area of law, as it affects virtually every individual and business in the economy. Consequently, there is the potential for many more claims of privilege than in other areas of the law. Kayle also argues that tax law is closer to accounting than the law per se, as “the ultimate objective [of tax law] is to correctly tally a taxpayer’s income tax liability, just the issue that has caused the courts to struggle for some time”.\textsuperscript{60} Finally, in a self-assessment tax environment, which exists in both Australia and the United States, voluntary compliance is essential for the efficient operation of the system. To ensure that laws are complied with, assertions of legal professional privilege are likely to be particularly onerous for the revenue authorities, as it protects the most crucial information and is the hardest for the authorities to obtain.

While such concerns carry a great deal of weight, privileged communication with lawyers is now generally regarded as a fundamental common law right, at least in Australia.\textsuperscript{61} It is difficult to conceive of the Australian Government removing the precedence legal professional privilege has over the Commissioner of Taxation’s statutory investigatory powers, given the length of time the relevant provisions\textsuperscript{62} have featured in the legislation and been interpreted as being subject to legal professional privilege. In addition, such arguments, insofar as they look to the inability of the revenue authorities to access information, do not take into account the prospect that the only reason the communication was ever made was due to the fact that the communication would be protected by the privilege. As Saltzburg states:

\textsuperscript{57} Ibid, [11].  
\textsuperscript{58} Committee of Experts on Tax Compliance, Tax Compliance: Report to the Treasurer and Minister of Revenue by a Committee of Experts on Tax Compliance, (1998) [9.36]-[9.63].  
\textsuperscript{60} Ibid, 551.  
\textsuperscript{61} For example, Commissioner of Australian Federal Police v Propend Finance Pty Ltd (1997) 188 CLR 501.  
\textsuperscript{62} Sections 263 and 264 of the Income Tax Assessment Act 1936.
In dealing with privilege claims the courts should focus on the ex ante issue: To what extent will the privilege promote the creation of information that might otherwise not exist? If the court focuses only on the ex post question – i.e., after information already has been created, what are the respective harms in a particular case of disclosure and nondisclosure – the court ignores the crucial aspect of privileges, which is the promotion of information-sharing and experimentation in the future, when others will think about whether to assist in the creation of information.63

IV THE US EXPERIENCE – SECTION 7525

Until 1998, like most common law jurisdictions, the United States did not have a recognised privilege for communications with accountants.64 Additionally, it had been held that lawyers performing activities that have been considered “accounting work”, such as the preparation of tax returns, did not enjoy legal professional privilege65 in relation to that work.66 This amounts to there being no “tax preparer’s privilege”, let alone no accountant’s privilege.67 Further, communications made that would be disclosed in a tax return had been held to waive any privilege that attached.68 However, it has been long established that accounting work will be covered by legal professional privilege if the accountant is acting under the direction of a lawyer,69 although the requirements set out for protection have been interpreted strictly over the years.70

A further form of privilege in the United States is referred to as the “work product doctrine”, a doctrine that is much more recent in its development, stemming from a 1947 decision.71 This doctrine protects communications made in relation to actual or anticipated litigation72 and also protects non-legal documentation, such as an accountant’s communications, so long as those materials were prepared for the purpose of a lawyer providing legal advice.73 This is distinct from the privilege already described and is both wider and narrower than legal professional privilege74 and bears somewhat of a resemblance to the second head of the privilege relating to litigation in Australia.75 The work product doctrine is also incorporated into Federal law through Rule 26(3)(b) of the Federal Rules of Civil Procedure, requiring that, when requesting documentation prepared by counsel, opposing parties need to demonstrate a “substantial need” and that “undue hardship” would

65 In the United States, legal professional privilege is usually referred to as “attorney-client privilege”.
68 United States v Lawless 709 F2d 485 (7th Cir, 1983).
69 United States v Kovel 209 F2d 918 (2nd Cir, 1961).
73 United States v Clark 847 F2d 1467, 1471 (10th Cir, 1988).
74 Gruetzmacher, above n 70, 989.
be experienced in attempting to acquire substantially the same information through other means. Even where these tests are met, many communications made by lawyers will remain protected.\textsuperscript{76}

As described by Petroni,\textsuperscript{77} this inequality in the protection of communications in taxation matters came to a head in the 1990s, with the aggressive expansion of the larger accounting firms in the areas of taxation advice. This led to a “turf war” between the accounting and legal professions, in part played out in the courtroom.\textsuperscript{78} The political climate was such that, eventually, in consultation with the American Institute of Certified Public Accountants (AICPA), when the United States Congress passed the \textit{Internal Revenue Service Restructuring and Reform Act of 1998}\textsuperscript{79} it incorporated IRC s 7525 into the Internal Revenue Code. IRC s 7525 reads as follows:

\textit{Confidentiality privileges relating to taxpayer communications}

(a) Uniform application to taxpayer communications with federally authorized practitioners

(1) General rule

With respect to tax advice, the same common law protections of confidentiality which apply to a communication between a taxpayer and an attorney shall also apply to a communication between a taxpayer and any federally authorized tax practitioner to the extent the communication would be considered a privileged communication if it were between a taxpayer and an attorney.

(2) Limitations

Paragraph (1) may only be asserted in –

(A) any noncriminal tax matter before the Internal Revenue Service; and

(B) any noncriminal tax proceeding in Federal court brought by or against the United States.

(3) Definitions

For the purposes of this subsection –

(A) Federally authorized tax practitioner

The term “federally authorized tax practitioner” means any individual who is authorized under Federal law to practice before the Internal Revenue Service if such practice is subject to regulation under section 330 of Title 31, United States Code.

(B) Tax advice

\textsuperscript{76} Kayle, above, n 59, 513.
\textsuperscript{77} A Petroni, “Unpacking the Accountant-Client Privilege Under IRC Section 7525” (1999) 18 \textit{Virginia Tax Review} 843.
\textsuperscript{78} Ibid, describing lawsuits against large accounting firms Arthur Andersen and Deloitte & Touche. See also G Billhartz, “Can’t We All Just Get Along? Competing for Client Confidences: The Integration of the Accounting and Legal Professions” (1998) 17 \textit{Saint Louis University Public Law Review} 427.
\textsuperscript{79} Pub L No 105-206, 112 Stat 750.
The term “tax advice” means advice given by an individual with respect to a matter which is within the scope of the individual’s authority to practice described in subparagraph (A).

(b) Section not to apply to communications regarding corporate tax shelters

The privilege under subsection (a) shall not apply to any written communication between a federally authorized tax practitioner and a director, shareholder, officer, or employee, agent, or representative of a corporation in connection with the promotion of the direct or indirect participation of such corporation in any tax shelter.

Almost as soon as IRC s 7525 was inserted into the Internal Revenue Code, commentators began expressing concerns as to the ambiguities relating to its content and scope. For instance, the non-criminal requirement is problematic, as the Internal Revenue Service (IRS) has discretion over which matters are treated as civil and which are criminal. Questions also arise when proceedings are converted from civil into criminal once started.

Also, as IRC s 7525 only applies to Federal matters, it does not protect communications from compulsory disclosure in state proceedings. Such disclosure may constitute a waiver of the privilege. Such waiver may come about also as a result of proceedings pursued by another government agency. IRC s 7525 only protects disclosure to the IRS. It does not extend to inquiries made by regulators such as the Securities and Exchange Commission or the Federal Trade Commission. Compulsory disclosure to such another government regulator may result in waiver of the privilege.

The definition of “tax advice” is also seen as problematic, due to its lack of clarity. IRC s 7525 refers only to professionals that may represent taxpayers before the IRS and the privilege only protects matters falling within the advisor’s “authority to practice”. However, what constitute the appropriate responsibilities of such professionals is not set out anywhere. Such concerns continue to persist, although it is suggested that IRC s 7525 will protect communications only if they would have been protected by legal professional privilege if made to a lawyer.

Other concerns involve the limitation regarding advice relating to corporate tax shelters. As tax shelters are transactions that are predominantly, if not specifically, designed to minimise tax, it is difficult to see where taxpayers would be more likely to wish to assert the privilege. This has the potential to severely limit a substantial amount of the business of the intended beneficiaries of the privilege, as well as raising certain procedural issues.

These concerns continue to be expressed by various commentators, despite several interceding years in which these matters could have been resolved, by legislative amendment if not judicial decision. For example, Gillet raises many of the concerns listed above, as does Gruetzmacher.

References:

80 See, for example, Petroni, above n 77, 857.
83 Ibid, 595.
84 Kayle, above n 59, 514.
85 LeBlanc, above n 82, 596.
86 P Gillet, “The Federal Tax Practitioner-Client Privilege (IRC Section 7525): A Shield to Cloak Confidential Communication or a Dagger for Both the Practitioner and the Client?” (2001) 70 University of Missouri at Kansas City Law Review 129.
Additional concerns have been raised more recently, such as the appropriateness of the procedural model adopted by the 1998 reforms in relation to the remainder of the Internal Revenue Code and the application in the context of professionals practising as both accountants and lawyers. Further, questions have been raised of the likely success the accounting profession will have in court in asserting the section 7525 privilege, given the reduced public respect for the accounting profession as a result of recent scandals and the types of transactions they are seeking to protect. Such efforts may result in a reduction of the scope of the privilege as a consequence of the poor timing of the assertions. Whether IRC section 7525 also provides protection along the lines of the work product doctrine has also been called into question.

While persisting uncertainty relating to new legislation is nothing new (Australians need look no further than Part IVA of the Income Tax Assessment Act 1936 for an example closer to home), the continued existence of these concerns indicates that the introduction of IRC section 7525 may not be the solution that was intended by Congress. This is unfortunate, given the calls and lobbying for a tax-advisor’s privilege prior to 1998, especially by the AICPA.

Petroni sets out that the objectives of the legislation were primarily to remove the “unfair penalty” imposed on taxpayers who have their tax affairs handled by a professional other than a lawyer, to curb some of the aggressive auditing practices exercised by the IRS and not advantaging taxpayers who were sufficiently well informed to run their affairs through a lawyer prior to approaching an accountant (or some other advisor) in order to access the privilege. If such objectives were to be achieved, one would expect certain changes to have taken place in accounting practice within the United States. In a survey of 1,072 practitioners and educators, Bauman and Fowler found that there was some evidence that some practitioners had taken steps to educate clients and indicate on correspondence communications that would be potentially covered by the privilege. However, overall, the evidence gathered from the survey indicated that no major changes had been made to office practices or procedures as a result of the new privilege, nor was the privilege being asserted on a regular basis. Further, the majority of respondents did not believe that their practices would experience increased growth due to the removal of the perceived competitive advantage previously enjoyed by lawyers. In fact, other evidence would suggest that accountants continue to refer clients to lawyers when matters involving the application of privilege could potentially arise. For example, the following was taken off a publicly available website in November 2004:

But the biggest and most difficult restriction [on the availability of the section 7525 privilege] is the one in the tax code that specifically excludes the use of this privilege with respect to any “criminal tax matter (sic) or proceeding”. Thus, if a taxpayer contacts me as a CPA and discloses that he or she has failed to file some tax returns or to pay some taxes that were due, that communication is not subject to the new accountant-client privilege.

…

87 Gruetzmacher, above n 70, 981.
89 Brooks, above n 37.
91 Gruetzmacher, above n 70, 993.
92 Petroni, above n 77, 845.
The greatest risk occurs if I should be retained to assist with the preparation of some delinquent tax returns and the information provided to me by the client causes me to recommend that the client seek counsel from a tax defense lawyer. Any information the client had previously given to me would not be protected and I could be required by law to disclose any discussions with that client.

It hasn’t happened; it’s not likely to happen but it could happen.

Therefore if a prospective client contacts me for assistance with the preparation of delinquent returns, I strongly suggest that the only inquiry should be for a referral to some lawyers who are specialists in criminal defense law.94

This evidence, while limited, suggests that the tax advisor privilege in the Internal Revenue Code may not have had the desired effect of tax practices in the United States that was originally intended. While the ambit of IRC § 7525 has not been fully tested in the courts to date, the evidence available does indicate that accountants have not altered their practices in the manner that may have been envisaged by the framers of the legislation.

V THE NEW ZEALAND LEGISLATION

On 15 June 2005, the Taxation (Base Maintenance and Miscellaneous Provisions) Act 2005 was passed by the New Zealand Parliament.95 Amongst other measures, it contains a new statutory privilege for professionals, such as chartered accountants, that will apply to “tax advice documents” in a similar fashion to common law legal professional privilege.96 The main operative provision is s 20B of the Tax Administration Act 1994 (NZ), which states:

No requirement to disclose tax advice document

(1) A person (called in this section … an information holder) who is required under 1 or more of sections 16 to 19 to disclose information in relation to a person is not required to disclose a document that is a tax advice document for that person.

(2) A document is eligible to be a tax advice document for a person if the document—

(a) is created by—

(i) the person for the main purpose of instructing a tax advisor to act for the person by giving to the person advice about the operation and effect of tax laws;

(ii) by a tax advisor for the main purpose of giving to the person advice about the operation and effect of tax laws; and

(b) for purposes that do not include a purpose of committing, or promoting or assisting the committing of, an illegal or wrongful act.

(3) A document is a tax advice document for a person if—

95 Minister of Finance, New Zealand, Major Tax Bill Passes, Media Statement (16 June 2005).
96 Minister of Finance, New Zealand, Statutory Privilege for Legal Advice Extended, Media Statement, (14 September 2004).
(a) the document is eligible under subsection (2) to be a tax advice document for the
person; and

(b) the person makes a claim, under section 20D, that the document is a tax advice
document; and

(c) the person satisfies the requirements of sections 20E and 20F for the document.

(4) A **tax advisor** is a natural person who–

(a) is part of an approved advisor group; and

(b) has a significant function of giving advice on the operation and effect of tax laws; and

(c) is subject to the code of conduct and disciplinary processes referred to in subsection
[(5)](a)(ii) and (iii).

(5) An **approved advisor group** is a group that–

(a) Includes natural persons–

(i) who have a significant function of giving advice on the operation and effect of tax
law; and

(ii) are subject to a professional code of conduct in the giving the advice; and

(iii) are subject to a disciplinary process that enforces compliance with the code of
conduct; and

(b) is approved by the Commissioner for the purposes of this definition.

The explanatory note to the Bill indicates that the objective behind the new privilege, like IRC s
7525, is to level the playing field for non-legal tax practitioners with lawyers by providing “a
degree of consistency with the current privilege enjoyed by a lawyer’s client, who may refuse to
disclose to Inland Revenue confidential communications with the lawyer”.97 The new privilege is
not intended to impact on the existing common law legal professional privilege.98

A quick reading of s 20B reveals a number of similarities with IRC s 7525. Firstly, the privilege is
aimed generally at tax advisors, not specifically at accountants (although the accounting profession
is usually the example given of the class of professionals that is likely to make use of the
privilege99). Both provisions are aimed at the provision of tax advice and both are subject to similar
limitations as for the common law legal professional privilege. Further, both provisions require
that, as a prerequisite for an assertion of privilege to be successful, the tax advisor must be
recognised as such by the relevant revenue authority.

As would be expected, there are a number of points of difference between these provisions. Most
appear to be attempts by the framers of the New Zealand legislation to mitigate (if not avoid) some
of the problems identified with the United States legislation. For example, s 20B does not appear to
be explicitly limited to documents sought by the Inland Revenue Department (IRD). The language

98 Ibid.
99 Minister of Finance, above n 95.
of the legislation does not indicate that it is intended to be restricted only to taxation matters, nor is there any equivalent to IRC s 7525(a)(2)(A), which explicitly limits the application of IRC s 7525 to non-criminal matters before the IRS. All that appears to be required under the New Zealand legislation is that the document in question is categorised as a “tax advice document” (within the meaning of s 20B(3)). Once this has been established, the treatment of the document is set out in s 20D, with items within the document that may still be required for disclosure set out in s 20F.

While s 20D(4) indicates that a claim that the document is a tax advice document must be made if the IRD requires disclosure of the relevant information under one of a number of other provisions of the Tax Administration Act 1994 (NZ) (ss 16, 16B, 17, 17A, 18 and 19), the language used does not appear to limit the application of s 20B to the exercise of the Commissioner’s powers under only those provisions. Consequently, there does not appear to be the opportunity for involuntary waiver of the privilege through compulsory disclosure to another government agency, as there does appear to be under IRC s 7525.

Another difficulty with the United States legislation that appears to have been dealt with in the New Zealand legislation is the definition of “tax advice”. IRC s 7525(a)(3)(B) defines tax advice as being advice given by a federally authorised tax practitioner with respect to a matter within their authority to practice. As indicated earlier, there is some degree of uncertainty as to what is encompassed within a practitioner’s “authority to practice”. The New Zealand legislation does not explicitly set out a definition for “tax advice”, however, it does set out in s 20B(2) the requirements for a document to be a tax advice document (and, therefore, eligible for protection from compulsory disclosure). Specifically, to qualify as a tax advice document, either the client or the tax advisor must have created the document for the main purpose of formulating advice on the operation and effect of tax laws. Any other ancillary purpose, whether or not within the usual scope of the tax advisor’s profession, does not appear sufficient for the document to qualify for the privilege.

Another point of difference is the absence in the New Zealand legislation of an explicit restriction to civil proceedings. While there is an exclusion in s 20B(2)(b) for advice that includes a purpose of committing an illegal act, this is distinct from a proceeding for a criminal offence. This may be explained, in part, by differences in structure between the New Zealand income tax system and that in the United States. The majority of offences under New Zealand income tax law are civil offences, whereas criminal offences are much more numerous under the United States. Consequently, concerns regarding potential breaches of ancillary powers (such as the power to pursue a matter as either a criminal or civil offence) by the relevant revenue authority are much less relevant in New Zealand than in the United States. However, it is would appear that, even in a criminal proceeding, the tax advice document would still be protected by the privilege so long as the advice did not have as a purpose the promotion or assisting of the commission of any illegal act.

Related to this area is the absence of a limitation in the New Zealand legislation excluding advice regarding tax minimisation schemes (tax shelters in the United States) from the scope of the privilege. Indeed, this limitation in the United States legislation was included only at the last minute just prior to its passage through Congress.100 This, however, does raise an ambiguity in the New Zealand legislation. As identified above, s 20B excludes advice that has a purpose of the commission of an illegal act. While this exclusion is necessary, and is consistent with exclusions from the scope of common law legal professional privilege, it is not immediately clear where illegality begins and ends in this context, an issue shared with the common law privilege. In particular, would advice regarding the interpretation of New Zealand tax laws, especially an interpretation that is contrary to Parliament’s clear intention, be considered to be illegal if it were later rejected in court once challenged by the Commissioner? Would the illegality question be any

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100 Petroni, above n 77, 862.
clearer if the advice was covered by any anti-avoidance provisions within the New Zealand tax statutes? Australia provides an illustration for the foundation of such concerns, as Subdivision 284-C of the *Taxation Administration Act 1953* explicitly allows for the increase of penalties to be applied to taxpayers found to have wrongfully reduced their tax liability through the use of a tax minimisation scheme.\(^{101}\)

Another point of divergence between s 20B and IRC s 7525 is the role of common law legal professional privilege. The United States legislation explicitly uses the common law rule as the basis for the statutory privilege, whereas there is no mention of legal professional privilege in the New Zealand legislation. It is apparent that s 20B is closely modelled on the common law privilege, for example, the exclusion of advice designed to promote illegal activities and the requirement to disclose certain factual information (referred to as “tax contextual information” and required to be disclosed under s 20F). Similar requirements are made under the common law privilege. However, certain requirements under the new statutory privilege depart from its common law counterpart. For instance, there is a prescribed procedure under s 20D for the assertion of the privilege, which has no equivalent under the common law. For example, s 20D(3) requires the following disclosures when an assertion for privilege is made over a document created by a tax advisor:

(a) a brief description of the form and contents of the document; and

(b) the name of the tax advisor who created the document; and

(c) the approved advisor group to which the tax advisor belonged when creating the document; and

(d) the areas of law about which the tax advisor was intending to give advice when creating the document; and

(e) the date on which the document was created.

While the use of the common law doctrine in the United States legislation has not presented any problems with the application of the statutory privilege to date,\(^{102}\) the New Zealand approach to establish a procedure separate and independent from the common law may be explained as an attempt to maintain parliamentary control over the process. Developments in the common law privilege will not have an effect on the New Zealand statutory privilege, whereas such developments will impact on the application of the United States provision. Section 20B is unlikely to be an attempt by the New Zealand Parliament to influence the development of the common law privilege as the Explanatory Note indicates that it is not Parliament’s intention to affect the common law privilege.\(^{103}\)

While the benefit of separating the statutory privilege from the common law privilege, as indicated, would be to retain greater parliamentary control over the privilege’s development, this may also prove to be a burden. As identified earlier, one of the standard arguments for the establishment of a tax advisors’ privilege is to “level the playing field” with legal practitioners. If this is at least one of

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\(^{101}\) Note that these Australian provisions also apply to tax legislation other than income tax legislation, such as the goods and services tax and fringe benefits tax statutes.

\(^{102}\) Although there have been some concerns expressed as to the correct procedure to assert the privilege conferred by IRC s 7525 in the United States; Gillet, above n 86, 143.

the objectives of the legislation, as it is in New Zealand,\textsuperscript{104} then such equivalency would be best achieved by applying exactly the same rules, as is the case in the United States (although this is undermined by the additional restrictions included in IRC s 7525). By providing for a separate privilege, the potential exists for either legal practitioners to enjoy a broader privilege than tax advisors generally, or vice versa. So long as the legal profession is approved by the Commissioner as an approved advisor group, the latter scenario is not likely to eventuate. However, it is difficult to reconcile the introduction of a completely separate statutory privilege with the objective of creating a consistent set of conditions for all tax professionals.

VI PROSPECTS FOR A TAX ADVISORS’ PRIVILEGE IN AUSTRALIA\textsuperscript{105}

In identifying relationships that are suitable for protection by a privilege, commentators often refer to the writings of Wigmore.\textsuperscript{106} Four criteria are set out as prerequisites for protection to be afforded by a privilege with respect to a particular form of relationship:

(1) The communications must originate in a confidence that they will not be disclosed.

(2) This element of confidentiality must be essential to the full and satisfactory maintenance of the relation between the parties.

(3) The relation must be one which in the opinion of the community ought to be sedulously fostered.

(4) The injury that would inure to the relation by the disclosure of the communications must be greater than the benefit thereby gained for the correct disposal of litigation.\textsuperscript{107}

With respect to communications between accountants and clients, it is the fourth criterion that tends to be the centre of debate.\textsuperscript{108} There is little question that communications are made in confidence, at least from the perspective of the client and that there would be a substantial incentive to withhold information if it were likely that much of that information would be disclosed to third parties, especially in taxation matters. The high degree of public shock at recent corporate scandals brought about by accounting irregularities, such as with Enron in the United States and HIH Insurance in Australia, serves as evidence of the high level of trust placed in the accounting profession by the community.

As is evident from the discussion of the case law earlier that rejected the extension of privilege to other professional relationships, the courts have come down on the side that the public interest served in having access to a greater amount of information in the resolution of disputes, including professional communications with non-lawyers, outweighs the public interest in upholding non-legal confidences. However, in the area of tax law, the distinction between legal and other professionals is very blurred, if it exists at all. As already noted, Australian legislation does not

\textsuperscript{104} Explanatory Note, Taxation (Base Maintenance and Miscellaneous Provisions) Bill (NZ), 10.

\textsuperscript{105} It should be noted that a judicial discretion is conferred on courts in New South Wales by s 126B of the Evidence Act 1995 (NSW) to exclude communications made in confidence to a non-legal professional; see Heydon, above n 1, para 25340.


\textsuperscript{108} Molony, above n 106, 260-261.
require an advisor to be admitted to legal practice to be able to provide advice on taxation laws. Consequently, calls for an extension of privilege to tax practitioners generally are much more justified than in the context of, for example, accountants performing non-tax work (such as audits).

It is apparent, though, that any extension of legal professional privilege, if one is to eventuate, will need to be made through the legislature rather than the courts. In doing so, the Australian Parliament has a number of options that it may pursue if it were to change the status quo.

The first possibility is to abolish legal professional privilege completely with respect to taxation matters. As noted earlier, there are some strong arguments in favour of such a position, including the recognition that taxation law is much more pervasive throughout society than most laws, with the result that assertions of any privilege preventing access to relevant information represent a greater hindrance to the revenue authorities than regulators in other areas of the law. Related to this is the notion that taxes are the foundation upon which developed economies function, as they are the chief source of revenue through which the government is able to implement its economic (and often social) policies. Any avenue that prevents the revenue authority from ascertaining all relevant facts over a given matter may therefore be regarded as an impediment to the efficient and effective implementation and enforcement of government policy.

However, it is submitted that this option would be contrary to the position that legal professional privilege has come to hold in Australian law. The statement by McHugh J in Propend Finance that legal professional privilege is now regarded as a fundamental common law right, rather than merely a rule of evidence, is typical of the judicial view. Consequently, there is negligible chance that Parliament will pass a statute abrogating legal professional privilege in taxation matters. In any event, the language used for such a provision to be effective would have to be very clear and unambiguous, as set out by Mason CJ, Brennan, Gaudron and McHugh JJ in Coco v R, requiring clear and unambiguous language to be used by Parliament when abrogating a fundamental common law right. The clarity required is demonstrated by the interpretation given to the Commissioner’s access powers in ss 263 and 264 of the Income Tax Assessment Act 1936 in recent decisions. Despite the very wide powers conferred on the Commissioner and the sweeping language used, the courts have found that these provisions do not abrogate legal professional privilege and, therefore, must be interpreted subject to the privilege. The fact that there has been no suggestion by Parliament in the light of these decisions for the provisions to be redrafted so as to remove the privilege as an impediment to the Commissioner’s access is testimony to Parliament’s reluctance to dilute the protection provided by the privilege.

The other option would be to follow the lead of the United States and New Zealand and introduce a statutory privilege to non-lawyer tax professionals. Such a privilege could draw upon the common law privilege directly, as is the case in the United States, or establish an independent statutory rule, as in New Zealand.

If Parliament were to extend the privilege, it should cover all tax practitioners. The chief argument presented by proponents of extension is of “levelling the playing field” with lawyers. It would be nonsensical to create a privilege for accountants practising tax, but not cover other tax agents. In Australia, as described earlier, it is not necessary to be formally admitted to either the legal or accounting professions to be qualified as a tax agent. Consequently, any statutory privilege should cover tax agents in general.

110 (1994) 179 CLR 427, 436. See also Baker v Campbell, (1983) 153 CLR 52, 117 (Deane J) and 123 (Dawson J) discussing legal professional privilege.
Secondly, it is submitted that the basic United States approach is to be preferred to that of New Zealand. The primary function of any statutory privilege should be to allow clients of all tax practitioners the same protection of their communications as that currently enjoyed by the clients of legal practitioners. Essentially, this means ensuring that if a communication would be protected if made to a lawyer, then it should also be protected if made to a non-lawyer tax agent. This is in line with the advocate’s argument of achieving parity between the professions. It is submitted that the most effective method of ensuring this result is to explicitly rely on the common law rule, as is done by IRC s 7525 in the United States. The alternative, which would be more akin to the New Zealand approach, is to attempt to replicate the effect of the common law privilege through the language adopted in statute. This would be a difficult task to begin with, as the rules of statutory interpretation may be applied in a manner unexpected by Parliament, creating differences between the common law privilege and the statutory rule. Even if parity were achieved initially, developments in the common law privilege would create a situation where the two rules are no longer equivalent (unless there was an immediate amendment of the statutory privilege to replicate the development). To maintain equivalency would necessitate regular reviews of the statute to accommodate common law developments.

It may be argued that creating an independent statutory rule allows Parliament to retain greater control over the privilege. However, this undermines the primary argument of achieving equal treatment of communications between tax agents. The only means by which parity could be guaranteed with an independent statutory rule is to ensure that the statutory rule is broader than the common law privilege. While such a position is feasible, there has been little suggestion that the common law privilege is insufficient in its coverage of which communications that it protects. Further, given the strong arguments presented earlier calling for a reduced application of legal professional privilege in taxation matters, especially the impediments that it represents to the revenue authorities, it is difficult to envisage the Australian Parliament introducing a privilege that protects an even broader range of communications than that covered by the common law privilege at the moment for lawyers.

However, while it has been submitted that the approach adopted by the United States at first instance is to be preferred, IRC s 7525 has been undermined by the additional restrictions introduced. In particular, the corporate tax shelter limitation represents a significant departure from the common law privilege. Such advice, from a lawyer, is likely to be privileged, yet the same advice from an accountant would not. While Congress may not be enamoured with the prospect of denying access to the IRS to communications relating to such tax minimisation arrangements, treating like communications differently depending on the professional affiliation of the advisor significantly detracts from the stated objective of creating parity between the professions.

Consequently, any efforts made by the Australian Parliament to introduce a tax advisor privilege should be explicitly based on the common law rule. An explicit feature of any such privilege should be that a communication, if it would be privileged if made by or to a lawyer, should also be privileged if made by or to another form of tax agent. Such an approach would mitigate many of the difficulties experienced with the United States legislation and the potential problems of the New Zealand legislation.

The question of what constitutes tax advice, or some similar question, may be answered with reference to established common law concepts. If the advice were to come from a lawyer, then it should also be privileged if comes from another tax agent. Questions such as whether information disclosed to an advisor that is intended to be utilised in the preparation of a tax return should be privileged may be resolved by the courts, as it is currently for common law legal professional privilege. Factual information would not be privileged, as this is not privileged with respect to
lawyers.\textsuperscript{111} There would be no need to specify limitations, such as advice for illegal purposes, as this is not covered by the common law privilege either.\textsuperscript{112}

There may be some residual questions over whether specific types of communications are covered by common law legal professional privilege and, hence, whether they would be covered by a statutory privilege in the form put forward here. However, this is not an argument against establishing the rule based on the common law privilege. Firstly, if there is doubt as to whether a lawyer’s communications are protected, then this would also be the case for other forms of tax agent, and vice versa. Parity is still achieved. Secondly, there is likely to be some uncertainty in the application of any new rule. The advantage of basing the statutory privilege on the common law rule is that practitioners may attempt to anticipate a court’s interpretation of the new rule based on several centuries of established doctrine. Any uncertainties emanating from an independent rule will be much more difficult to resolve in the absence of judicial interpretation. Consequently, any criticism of a statutory rule in this form is more of a criticism levelled at the common law system generally, rather than the statute specifically. Common law practitioners are well accustomed to providing advice in such grey areas and, therefore, arguments of this nature do not hold much weight.

Any such privilege should apply to extra-litigation matters. In particular, this would ensure that exercises of the ATO’s access and investigatory powers, as well as discovery proceedings, would be covered. Otherwise, this would merely represent an extension of the limited client legal professional in the Commonwealth \textit{Evidence Act} to other professionals.

An overriding concern, though, is whether any benefit is achieved by the introduction of such a privilege. The only jurisdiction to have an established rule, the United States, has had the rule in place for just over six years. As a result, there is little conclusive evidence either way of the effects of the statutory privilege. However, the results of the Baumann and Fowler survey\textsuperscript{113} appear to indicate that the privilege has not brought about the benefits that had originally been anticipated by Congress and the AICPA.

While it may be argued that these results represent a cautious approach being adopted by the accounting profession based on the inherent uncertainty that comes with any novel legislation, the additional limitations included in IRC s 7525 that do not apply to the common law privilege are also highly likely to have contributed to current practices. The limitations, particularly that relating to corporate tax shelters and restricting the application to non-criminal proceedings, appear to target the very areas where the benefits would be expected to accrue. Therefore, the result that the privilege has not had much of an impact on accounting practices in the United States should not come as a surprise. This evidence reaffirms the contention put forward earlier that any statutory rule to be introduced in Australia should simply apply the common law rules to tax agents generally, without modification.

Finally, in determining whether such an extension is appropriate for Australia, it is worth noting that another reason cited for the adoption of the tax advisors’ privilege in the United States was concern over aggressive audit techniques used by the IRS to identify areas of non-compliance.\textsuperscript{114} The Commissioner of Taxation in Australia has announced initiatives to ensure compliance with taxation laws that cross over borders, including sharing information and experience with revenue

\textsuperscript{111} For example, \textit{Sharp v Federal Commissioner of Taxation} 88 ATC 4165.

\textsuperscript{112} \textit{R v Cox and Railton} (1884) 14 QBD 153; \textit{Varawa v Howard Smith & Co} (1910) 10 CLR 382.

\textsuperscript{113} Baumann and Fowler, above n 93.

\textsuperscript{114} Petroni, above n 77, 845.
authorities in other jurisdictions, including the IRS.\textsuperscript{115} As a result, it is not hard to anticipate an environment in the future where aggressive audit techniques adopted by the IRS in the United States are also adopted by the ATO in Australia. If such concerns were sufficient to extend privilege to tax advisors generally in the United States, then the arguments for introducing a similar statutory rule in Australia gather further weight.

\section*{VII Conclusion}

This article has assessed the prospects of extending a privilege based on the present common law legal professional privilege to tax practitioners in Australia by analysing the foundations and rationales for the common law rule and then looking to the attempts to implement such an extension in two other common law jurisdictions, specifically the United States and New Zealand. In particular, the United States has had a statutory privilege in place for over six years. This has provided ample opportunity for criticism and analysis by commentators, highlighting the strengths and problems with the legislation. Unfortunately, the timeframe involved is too short to enable the collection of much empirical evidence indicating the effect the new legislation has had in practice, nor have the courts had much opportunity to interpret the statute in the context of actual disputes. It should be noted, though, that early evidence suggests that the provision has not resulted in much change in the practices of accountants with respect to their tax advice.

It may be argued that the United States legislation has undermined the original objectives driving the introduction of the legislation, in particular, creating parity between tax advisors with legal qualifications and practitioners with another professional affiliation. The final version that was passed by Congress incorporated a number of restrictions, which do not apply under the common law privilege. Consequently, legal professionals are still able to protect their client communications in a number of circumstances where other professionals are unable to do so. Such circumstances are likely to arise quite frequently for tax advisors in larger practices, causing these restrictions to have a significant impact on the potential benefits originally offered to the professions.

The New Zealand Parliament has recently passed legislation of its own incorporating a similar provision in its own tax legislation. In its drafting, a number of the problems identified with the United States legislation have been avoided. However, the New Zealand legislation establishes a privilege completely separate from its common law counterpart, creating a number of potential issues itself.

In Australia, the arguments for establishing a general tax advisors’ privilege are just as forceful as they are in the United States and New Zealand. These arguments include treating the same advice in the same fashion, regardless of the professional affiliation of the advisor and the confidential nature inherent in communications relating to clients’ tax affairs. Such arguments have traditionally been rebutted by noting that the underlying rationale of common law legal professional privilege is not the maintenance of confidences per se, but rather the efficient administration of justice through the facilitation of the legal system, of which confidentiality is an essential part. However, such arguments lose weight in the context of taxation, as it is not necessary for a tax practitioner to be qualified as a lawyer to be able to provide advice on taxation laws in Australia in the same manner as tax lawyers.

If the Australian Parliament were to introduce a statutory tax practitioner privilege, this should be explicitly based on the common law legal professional privilege. This will ensure parity between

\textsuperscript{115} See, for example, M Carmody, Address to the Australian Institute of Company Directors Victoria Division, Melbourne, 28 May 2004.
the professions able to offer taxation advice, achieving the main goal of such legislation. Additional restrictions should be avoided, so as not to undermine this objective.

However, caution should be exercised prior to the introduction of such a privilege in Australia. The evidence from the United States is somewhat equivocal, with the peculiar features of the legislation likely to have caused the lack of impact on practice suggested by initial research. Consequently, the arguments in favour of introducing a new statutory privilege cannot be rebutted from these findings. While it is too early for any empirical evidence to have come from New Zealand, the differences between the New Zealand legislation and the model proposed here may provide grounds for concern as to the applicability of any such data to Australian conditions. As such, the evidence provided by these other jurisdictions may be of limited value in Australia, except to the extent that it may provide guidance as to the effects of a departure from the common law benchmark. Therefore, an assessment of the policy issues at hand prior to a position being adopted is required. It is submitted that the policy arguments in favour of treating like communications in the same manner should be considered paramount, not for any reason of lawyers otherwise holding a competitive advantage over other tax professionals, but in order to facilitate the appropriate administration of the legal system with respect to taxation. This will have the ultimate benefit of allowing the taxation profession to be more transparent and accessible from a client’s perspective.