



Australian Government  
Australian Taxation Office

AUSTRALIAN TAXATION OFFICE

# Traditional Rights and Freedoms—Encroachments by Commonwealth Laws

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Australian Law Reform Commission

6 October 2015

# 1 Introduction

1. The Australian Taxation Office (ATO) provided a confidential submission dated 1 April 2015 to the Australian Law Reform Commission's (ALRC) Freedoms Inquiry (the Inquiry) in response to the Issues Paper released on 10 December 2014 (the Original Submission).
2. In this further submission we are seeking to elaborate on certain aspects of our previous submission, in light of the discussion in the ALRC's *Interim Report* released on 3 August 2015 (the Report).
3. This further submission will focus on:
  - a. retrospective laws: transfer pricing and director penalty notices;
  - b. section 8Y of the *Taxation Administration Act 1953* (TAA); and
  - c. use and derivative use immunity in the context of criminal proceedings.

## 2 Retrospective Laws

4. Chapter 9 of the Report considers the retrospectivity of certain laws administered by the Commissioner of Taxation (Commissioner), including recent amendments to the transfer pricing rules and the director penalty regime.
5. To assist the Inquiry, the ATO provides the following additional information on the context in which the amendments were made, and their legal and practical effect.
6. However, whether a given legislative measure should apply retrospectively or not is ultimately a matter of policy for the Parliament to decide.

### Tax Laws Amendment (Cross-Border Transfer Pricing) Act (No. 1) 2012

7. The *Tax Laws Amendment (Cross-Border Transfer Pricing) Act (No. 1) 2012* inserted Subdivision 815-A into the *Income Tax Assessment Act 1997*. Subdivision 815-A ensures that the transfer pricing articles contained in Australia's tax treaties are able to be applied independently of the previously existing domestic transfer pricing provisions and that relevant Organisation for Economic Co-operation and Development (OECD) guidance material can be used when interpreting the rules.
8. The Act was enacted on 8 September 2012 but applies to income years starting on or after 1 July 2004.
9. As noted at paragraph 9.68 of the Report, the Explanatory Memorandum (EM) to the Tax Laws Amendment (Cross-Border Transfer Pricing) Bill (No. 1) 2012 (the Bill) set out why the then government thought it appropriate and necessary for these amendments to have retrospective application. The Treasury Submission to the Senate Economics Legislation Committee Inquiry on the Bill clarified and expanded on certain aspects of the EM.<sup>1</sup> The Senate Economics Legislation Committee considered concerns about the retrospective nature of the Bill in its report on the Bill but recommended (by majority) that the Senate pass the Bill.<sup>2</sup>
10. The potential negative impacts of retrospective legislation are mitigated to some degree in the circumstances of this legislation both through express legislative provisions and ATO administrative practices.
11. The legislation provides that administrative penalties in respect of any transfer pricing adjustment are only applied on a prospective basis. Broadly, for income years commencing prior to 1 July 2012 administrative penalties under Subdivision 284-C of the Schedule 1 to the TAA only arise to the extent that the transfer pricing adjustment could have been made under the previous legislation (former Division 13 of Part III of the *Income Tax Assessment Act 1936*).<sup>3</sup>

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<sup>1</sup> The Treasury, Submission to Senate Economics Legislation Committee, *Tax Laws Amendment (Cross-Border Transfer Pricing) Bill (No. 1) 2012*

<sup>2</sup> Senate Economics Legislation Committee 2012, *Tax Laws Amendment (Cross-Border Transfer Pricing) Bill (No. 1) 2012 [Provisions]*, at page 93. There was a dissenting minority report by Senators on the Senate Economics Legislation Committee recommending that the Bill not be passed, primarily because it operated retrospectively (see Senate Economics Legislation Committee 2012, *Tax Laws Amendment (Cross-Border Transfer Pricing) Bill (No. 1) 2012 [Provisions]*, at page 97).

<sup>3</sup> Section 815-10 of the *Income Tax (Transitional Provisions) Act 1997*

12. There has been no material change in the ATO's administrative approach following Subdivision 815-A's enactment. The ATO had long maintained that it could already use Australia's tax treaty articles to raise a transfer pricing adjustment applying the arm's length principle and, therefore, in practice does not see Subdivision 815-A as providing the Commissioner with any new or different administrative powers. Effectively, the ATO will continue to apply the relevant treaty article, including the same reasoning and analysis, in the manner it did before Subdivision 815-A was enacted.<sup>4</sup> This means that although the amendments had application prior to their commencement, the effect was not to retrospectively remove benefits to which taxpayers were certainly entitled or had previously enjoyed. Arguably the change in law increased certainty.
13. The ATO has stated publicly that there are no plans to change its compliance program on the basis of Subdivision 815-A. The ATO has maintained its current transfer pricing risk assessment and compliance activities.<sup>5</sup>

## Director penalty notices

14. The ATO discussed the Director Penalty Regime in Division 269 of Schedule 1 to the TAA in its Original Submission, including how the provisions operate, their policy intent and the legislative and administrative limits and safeguards against their encroachment on rights and freedoms.
15. Broadly, the provisions oblige directors of a company to cause the company to comply with various pay as you go (PAYG) withholding tax and superannuation guarantee charge (SGC) obligations (withholding obligations). If a company does not pay, nor go into administration or liquidation, then the Commissioner can issue a Director Penalty Notice (DPN) to the director, which requires them to pay a penalty equal to the amount of the company's withholding obligations. Upon payment of the penalty, the director has a right of indemnity against the company.
16. As noted at paragraphs 9.78 to 9.79 of the Report, the Australian Institute of Company Directors expressed concerns that these provisions 'make new directors personally liable for the actions of the company' with respect to unpaid PAYG withholding and SGC amounts 'even when the person was not a director at the time of the company's breach'.<sup>6</sup>
17. However, it is the ATO's understanding that Division 269 does not hold new directors liable for breaches committed by the company at a time before the directors assumed their responsibilities. Instead, DPNs are issued to directors when the company is in *continuing* breach of its various withholding obligations, even if that breach *commenced* before the new directors started.
18. In circumstances where a DPN would be issued, the company would be in continuing breach of its various withholding obligations and directors, both new and existing, would be able to

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<sup>4</sup> Australian Taxation Office, *Tax Laws Amendment (Cross-Border Transfer Pricing) Act No. 1 (2012) 'Sub-Division 815-A' - Frequently asked questions*, [https://www.ato.gov.au/Business/International-tax-for-business/In-detail/Transfer-pricing/Tax-Laws-Amendment-\(Cross-Border-Transfer-Pricing\)-Act-No--1-\(2012\)--Sub-Division-815-A----Frequently-asked-questions/](https://www.ato.gov.au/Business/International-tax-for-business/In-detail/Transfer-pricing/Tax-Laws-Amendment-(Cross-Border-Transfer-Pricing)-Act-No--1-(2012)--Sub-Division-815-A----Frequently-asked-questions/) accessed on 29 September 2015.

<sup>5</sup> Australian Taxation Office, *Tax Laws Amendment (Cross-Border Transfer Pricing) Act No. 1 (2012) 'Sub-Division 815-A' - Frequently asked questions*, [https://www.ato.gov.au/Business/International-tax-for-business/In-detail/Transfer-pricing/Tax-Laws-Amendment-\(Cross-Border-Transfer-Pricing\)-Act-No--1-\(2012\)--Sub-Division-815-A----Frequently-asked-questions/](https://www.ato.gov.au/Business/International-tax-for-business/In-detail/Transfer-pricing/Tax-Laws-Amendment-(Cross-Border-Transfer-Pricing)-Act-No--1-(2012)--Sub-Division-815-A----Frequently-asked-questions/) accessed on 29 September 2015.

<sup>6</sup> Australian Institute of Company Directors, *Submission 42* [http://www.alrc.gov.au/sites/default/files/subs/42.\\_org\\_australian\\_institute\\_of\\_company\\_directors\\_.pdf](http://www.alrc.gov.au/sites/default/files/subs/42._org_australian_institute_of_company_directors_.pdf) accessed on 29 September 2015.

comply with the DPN by either having the company comply with its withholding obligations or appointing an administrator or liquidator for the company.

19. The *Tax Laws Amendment (2012 Measures No. 2) Act 2012* introduced more lenient treatment for new directors subject to DPNs. In particular, a new director is not liable to a director penalty for company debts until 30 days after they become a director. Previously, new directors could be liable for outstanding debts if they had failed to arrange for the company to take necessary action within 14 days of becoming a director. The increase in the grace period from 14 days to 30 days is because the director penalty regime will now apply to both PAYG withholding and SGC amounts, so new directors need more time to ensure their corporate affairs are in order before being liable for a personal penalty.<sup>7</sup>

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<sup>7</sup> Explanatory Memorandum to the Tax Laws Amendment (2012 Measures No. 2) Bill 2012 at paragraph 1.24.

## 3 Burden of Proof

20. At paragraphs 11.53 to 11.58 of the Report, the ALRC outlines how the burden of proof is reversed for the purposes of section 8Y of the TAA. The ATO provides the following information in relation to the matters discussed therein.
21. The ALRC noted how the 2009 Council of Australian Governments (COAG) pronouncement regarding personal liability for corporate fault was relevant to section 8Y at paragraph 11.56. The ALRC subsequently observed, at paragraph 11.58, that the Australian Institute of Company Directors takes the position that section 8Y 'has not been sufficiently justified pursuant to the COAG Principles'.
22. The ATO notes that the then government, in its legislative response to the COAG Principles, did not amend the provision.

### Application of section 8Y in practice

23. In practice, compliance action will generally be commenced against a company first, rather than its officers in relation to any offence committed by that company. This approach resolves the majority of cases.
24. Alternatively, the Commissioner may initiate prosecution under section 8Y in circumstances where it is considered that action against a company is unlikely to achieve the desired compliance result.
25. The types of cases selected for section 8Y target particularly egregious behaviour. Of the 19 cases in which the ATO applied section 8Y in 2013, the majority of cases involved the ATO first prosecuting a company for tax offences. These companies failed to stop the offensive behaviour, and in those circumstances the ATO took action under section 8Y to stop the ongoing tax offences.
26. Such prosecutions would not be initiated without first approaching a company in contravention of its obligations to promote voluntary compliance with the tax law.

## 4 Privilege Against Self-incrimination

27. The ALRC called for further submissions regarding the privilege against self-incrimination, and in particular where use and derivative use of self-incriminating information does not exist.<sup>8</sup> The ATO provides the following information regarding the use and derivative use of information obtained by the ATO via powers of compulsion (access and information gathering powers) in criminal proceedings.
28. The following submission complements Chapter 4 of the Original Submission on the Commissioner's access and information gathering powers.

### Access and Information Gathering Powers

29. As stated in the Original Submission, the Commissioner's access and information gathering powers are vital to the ATO's compliance operations and are necessary to ensure that the Commissioner can access and establish relevant facts and evidence quickly. This is particularly important in circumstances where taxpayers have self-assessed their liabilities and where the Commissioner has limited time to establish the true facts.
30. It is the ATO's position that, consistent with the ALRC's observations,<sup>9</sup> the Commissioner's powers are not subject to claims of privilege against self-incrimination.
31. The Federal Court in *Stergis & Ors v. Federal Commissioner of Taxation & Anor* (1989) 89 ATC 44 and *Deputy Commissioner of Taxation v. de Vonk* (1995) 61 FCR 564 has acknowledged that the legislative policy behind these powers would be frustrated if the privilege against self-incrimination were allowed to operate to limit them.
32. The Tax Institute's submission to the ALRC's issues paper<sup>10</sup> acknowledged that it was at times essential for the ATO to be able to access information quickly.
33. Further to paragraphs 76 to 83 of the Original Submission, the ATO notes that these powers have been subject to a number of reviews. To elaborate briefly on two such reviews, the ATO provides the following information:
- a. **The Senate Standing Committee for the Scrutiny of Bills, Fourth Report of 2000: Entry and Search Provisions in Commonwealth Legislation:** in 2003 the then Government responded to the Committee's report, whereby it acknowledged that in a system where taxpayers self-assess their liabilities, and are required to keep adequate records, to support their assessments, the Commissioner's powers were essential to the effective administration of tax laws. Accordingly, the then Government rejected the recommendation to review and amend the powers.
  - b. **The Senate Standing Committee for the Scrutiny of Bills, Twelfth Report of 2006: Entry, Search and Seizure Provisions in Commonwealth Legislation:** in its report the Committee directly addressed the then Government's response to its previous report (above). The Committee noted that the then Government did not intend to alter the Commissioner's powers.

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<sup>8</sup> See paragraphs 12.102 to 106 of the Report.

<sup>9</sup> See paragraph 12.60 of the Report.

<sup>10</sup> Australian Law Reform Commission, Traditional Rights and Freedoms—Encroachments by Commonwealth Laws (IP 46) dated 10 December 2014.

## Use and derivative use immunity

34. The ATO agrees with the ALRC's observation<sup>11</sup> that the Commissioner's powers are unrestricted by either use or derivative use immunity (as defined at paragraph 12.36 of the Report).<sup>12</sup>
35. This has long been the position in taxation legislation.<sup>13</sup>
36. The Tax Institute's submission to the Inquiry raised concerns about the use of information gathered under the Commissioner's access and information gathering powers in subsequent criminal proceedings.<sup>14</sup> In addressing this concern, the ATO takes the Tax Institute's reference to derivative use to include use immunity. This submission seeks to inform the ALRC about other administrative, legislative and judicial limits and safeguards on the use and derivative use of information gathered under these powers, and in this regard expands upon Chapter 4 of the Original Submission.
37. The ATO's use of information is restricted to some extent by:
- a. the ATO's policies and procedures;
  - b. the taxpayer confidentiality provisions; and
  - c. judicial oversight regarding the admissibility of evidence.

## ATO policies and procedures

38. The ATO's policies and procedures regarding information gathering are outlined in the document ***Our approach to information gathering***.<sup>15</sup> The Original Submission includes a significant analysis of our approach, which includes safeguards such as the ATO's stated policy not to use notice powers to gather evidence for the purposes of prosecution, the administrative concessions regarding accountant and corporate board advice, and claims of legal professional privilege.<sup>16</sup> The ATO notes that these policies and procedures are subject to periodic internal review and have previously been subject to multiple external reviews.<sup>17</sup>
39. For the purposes of criminal proceedings, where potential tax crimes are identified by ATO officers in the course of their duties, the matter must be escalated to specialist investigative officers that deal with tax crime and the related information gathering and use requirements.<sup>18</sup>

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<sup>11</sup> See paragraph 12.62 of the Report.

<sup>12</sup> "Use immunity means that the statement given or record produced cannot be used in subsequent criminal or civil penalty proceedings against the person, except in proceedings in relation to the falsity of the evidence itself. Derivative use immunity means that evidence obtained as a result of the person having made a statement, or provided a document, cannot be used in subsequent proceedings." (footnotes excluded)

<sup>13</sup> The situation is slightly different in sections 130B and 287 of the *Superannuation (Industry) Supervision Act 1993*. Please refer to the Original Submission at paragraph 46.

<sup>14</sup> See paragraphs 12.63 to 12.66 of the Report.

<sup>15</sup> Australian Taxation Office, *Our approach to information gathering*, <http://www.ato.gov.au/infogathering> accessed on 15 September 2015.

<sup>16</sup> For more information see paragraphs 58 through 82 of the Original Submission.

<sup>17</sup> A list of these external reviews is included at paragraph 76 of the Original Submission.

<sup>18</sup> See ATO Chief Executive Instruction 2014/05/09 'Tax Crime and External Fraud'.



Any investigation must follow ***Our approach to information gathering***, and evidence analysed in accordance with the *Prosecution Policy Of The Commonwealth*.<sup>19</sup>

## Taxpayer confidentiality provisions

40. As outlined in the Original Submission, tax officers are subject to strict taxpayer confidentiality provisions where penalties for non-compliance include imprisonment. The ATO provides the following information to elaborate on the Original Submission on these strict provisions governing the disclosure of protected information (including that gathered under access and information powers).
41. Division 355 of Schedule 1 to the TAA provides a number of exceptions to these provisions in limited circumstances. Of relevance for present purposes are two exceptions: where the disclosure is made in the performance of a taxation officer's duties, and where the disclosure is made to a law enforcement agency.
42. Permitted disclosures in the performance of duties would include disclosing information to any court, entity or tribunal for the purpose of the making or proposed or possible making of an order under the *Proceeds of Crime Act 2002* or for the purpose of criminal, civil or administrative proceedings; however, the order or proceedings must relate to a taxation law.<sup>20</sup>
43. In the case of permitted disclosures to authorised law enforcement agency officers, these are limited to matters relating to serious offences (attracting a sentence of imprisonment of more than 12 months) and offences under proceeds of crime legislation.<sup>21</sup> In these cases, any such disclosure must be agreed to by either the Commissioner, a Second Commissioner, a Senior Executive Service (SES) employee, or if the disclosure is to be made by another taxation officer, it must be approved by an SES employee that does not directly supervise the disclosing officer.
44. The ability to use information in this way ensures that the ATO can contribute to serious and organised crime taskforces and improve regulatory co-operation on matters of public interest.
45. In 2013-14 the ATO made over 1,600 disclosures relating to serious offences and proceeds of crime offences.<sup>22</sup> Of these disclosures, less than 10% were initiated by the ATO. These processes are important to ensuring that the Australian Federal Police and the Commonwealth Director of Public Prosecutions are able to investigate and prosecute such crimes.

## Judicial oversight

46. The ATO notes the ALRC's remarks regarding the judicial limits on the admissibility of derivative evidence at paragraph 12.26 of the Report.

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<sup>19</sup> Commonwealth Director of Public Prosecutions 2014, *Prosecution Policy Of The Commonwealth*, <http://www.cdpp.gov.au/publications/prosecution-policy-of-the-commonwealth/> accessed on 16 September 2015.

<sup>20</sup> Section 355-50 of Schedule 1 to the *Taxation Administration Act 1953*.

<sup>21</sup> Section 355-70 of Schedule 1 to the *Taxation Administration Act 1953* outlines further disclosures, including to prescribed taskforces, national security, and commissions of inquiry.

<sup>22</sup> The ATO Annual Report 2013-14, <http://annualreport.ato.gov.au/04-appendixes/appendix-11-information-provided-law-enforcement-agencies> accessed on 7 September 2015.