Tax controversies – voluntary disclosures

THE STRATEGIC USE OF VOLUNTARY DISCLOSURES CAN MANAGE TAX RISKS.

Hear what I say, 'cause every word is true.

You know I wouldn't tell you no lies.

Your time's coming, is gonna be soon, boy.[1]

INTRODUCTION

A voluntary disclosure is a significant means of managing tax risk in accordance with a taxpayer's risk management protocol.

A voluntary disclosure before or during audit may reduce administrative penalties by 80% or 20% respectively. While some tax risks are susceptible to adopting a **reasonably arguable position** which will reduce or eliminate administrative penalties, advisers should consider voluntary disclosure to manage other tax administrative penalty and criminal prosecution risks.

Proposed amendments to the voluntary disclosure provisions will affect the operation of the administrative penalty provisions and indirectly the views of the Australian Taxation Office (**ATO**) expressed on voluntary disclosure and the taxpayer's tax risk management protocols.

The ATO's revised offshore voluntary disclosure initiative (**OVDI**) will end on 30 June 2010. A voluntary disclosure under the OVDI can reduce penalties to 10%, provide interest remissions and manage the risk of possible criminal prosecution arising from offshore income omission.

A combination of voluntary disclosure under the OVDI and the normal rules may be necessary to properly manage the international and domestic consequences of an OVDI disclosure.

Advisers should ensure that a voluntary disclosure does not inadvertently waive client legal privilege (**CLP**), prejudice client accounting privilege (**CAP**) or increase the risk of criminal prosecution.

This article discusses the voluntary disclosure provisions with particular emphasis on the OVDI and the risks of criminal prosecution.

VOLUNTARY DISCLOSURE

Introduction

The uniform administrative penalty provisions apply to statements made, returns lodged and schemes entered into from 1 July 2000.[2] The extent of the penalty imposed is determined by the behaviour of the taxpayer and the taxpayer's advisers.

Paul Sokolowski has provided a detailed analysis of the uniform administrative penalty regime (see page 520) so a detailed discussion is not provided in this article.[4]

A taxpayer that makes a voluntary disclosure in the approved form to the ATO may have administrative penalties reduced:[5]

- to nil where disclosure is made before an audit commences in respect of the income year and the tax shortfall was less than A$1,000;
- by 80% where disclosure is made before an audit commences in respect of the income year;
- by 80% where disclosure is made after an audit commences in respect of the income year and the ATO exercises its discretion to treat the disclosure as if it had been made before commencement of audit;[6] or
- by 20% where disclosure is made after an audit commences in respect of the income year and the disclosure saves the ATO significant time and resources.

Administrative penalties include penalties for false and misleading statements, taking a position that is not reasonably arguable, failure to lodge or provide documents or entering into a tax avoidance scheme. The ATO has a general discretion to further remit penalties.[7]

Voluntary disclosures are usually made:

- at the commencement of a review or audit where an issue is known to the taxpayer which is likely to be identified by the ATO and the taxpayer wants to access the 80% reduction;
- during a review or audit where the taxpayer identifies a risk issue which is likely to be identified by the ATO and the taxpayer wants to access the 20% reduction;
- prior to notification of a review or audit where the taxpayer is aware of a specific audit program and considers that the taxpayer is highly likely to be included in the specific audit program; or
- when a prudential audit identifies a tax risk area prior to notification of a review or audit and the taxpayer wants to make a voluntary disclosure to reduce penalties before commencing risk

management measures such as self-amending tax returns and objecting against the self-amended tax returns in preparation for any potential appeal.

A voluntary disclosure is, accordingly, a means to open up settlement negotiations or communications with the ATO to manage a tax risk which does not have the restrictions and appeal limitation of a private ruling application.

A voluntary disclosure does not necessarily initiate or escalate a review or audit, but does increase the risk of ATO scrutiny.

Whether and when to make a voluntary disclosure depends on the particular risk profile and risk management strategy adopted by the client.[8] In broad terms, the more likely the incident of the issue being detected the greater the utility of a voluntary disclosure.

ATO views

The ATO's view on voluntary disclosure is expressed in PSLA 2006/2[9] and MT 2008/3.[10] Relevantly, the following comments can be made:

- the definition of "audit" includes substantiation reviews and deduction verification enquiries;[11]
- the disclosure will not be **voluntary** and the discretion to treat a disclosure as made before commencement of audit will not be applied where the taxpayer was aware of the shortfall and would not have made a disclosure but for the receipt of the audit notification letter[12] or has had a previous tax audit in respect of the issues disclosed;[13]
- there will not be **disclosure** unless the ATO is told of information not otherwise known to the ATO;[14]
- in borderline cases the benefit of any doubt should generally be given to the taxpayer;[15]
- the discretion to treat a disclosure as made before commencement of audit should be exercised where it is fair and reasonable to do so and must not be exercised arbitrarily;
- the discretion to treat a disclosure as made before commencement of audit will usually be exercised where:[16]
  - the ATO inquiry is a risk review and not another form of audit;
  - the shortfall or scheme shortfall amount arises outside of the risks and issues covered by the audit;
  - disclosure is made before a date notified by the ATO for voluntary disclosure or the formal commencement date of the audit specified in the audit notification letter;[17] or
  - a company is undertaking a prudential audit at the time of the ATO notification of commencement of an audit and it could reasonably be concluded that the company was going to make a full disclosure irrespective of the audit;
- the 20% reduction requires the disclosure to objectively save the ATO a significant amount of time or resources in the tax audit;[18]
- the disclosure must be sufficient to permit the ATO to calculate and adjust the tax-related liability;[19]
- a voluntary disclosure does not preclude criminal prosecution;[20] and

Penalty Basis[3]	Penalty Amount			
		Adjusted Penalty %		
			Voluntary Disclosure	
Penalties relating to Statement	Base Penalty Amount	Culpable Behaviour + 20%^	During Audit - 20%	Before Audit - 80%
Intentional disregard of the law	75% shortfall	90%	60%	15%
Recklessness as to the operation of a law	50% shortfall	60%	40%	10%
Failure to take reasonable care to comply with tax law	25% shortfall	30%	20%	5%
Taking a position that is not reasonably arguable*#+	25% shortfall	30%	20%	5%
Failure to provide documents under s 284-75(3)	75% total tax	90%	60%	15%
Disregard private ruling pre 2004-05 income year	25% shortfall	30%	20%	5%
Penalties relating to Schemes				
Taking a position that is not reasonably arguable	50% shortfall	60%	40%	10%
Taking a position that is reasonably arguable	25% shortfall	30%	20%	5%
Transfer pricing or DTA position that is not reasonably arguable (no avoidance dominant purpose)	25% shortfall	30%	20%	5%
Transfer pricing or DTA position that is reasonably arguable (no avoidance dominant purpose)	10% shortfall	12%	8%	2%

^ Note: Hindering ATO, repeat offences and failure to disclose within reasonable time of becoming aware of shortfall

** Note: No penalty unless results from a change of more than A$10,000 or 1% of income tax payable*

 # Note: No penalty in relation to a trust unless results from a change of more than A$20,000 or 2% of trust net income

+ Note: No penalty in relation to a partnership unless results from a change of more than A$20,000 or 2% of partnership net income

- specific voluntary disclosure initiatives (such as the OVDI in respect of tax havens) may provide different penalty remission rates and criteria.[21]

Recently, case law has clarified the scope of the voluntary disclosure provision.

In *British American Tobacco Australia Services Ltd v FCT*[22] the Court held that to be a **voluntary** disclosure the taxpayer must volunteer information on the taxpayer's own initiative without prompting or apprehended pressure from the ATO and rejected the argument that a disclosure was voluntary unless the taxpayer was legally compelled to make the disclosure.

In *Lawrence v FCT*[23] the Court held that a compulsory examination under s 264 of the *Income Tax Assessment Act 1936* (Cth) (**ITAA36**) did not constitute notice of an audit for the purposes of voluntary disclosure.

In *Dixon v FCT*[24] the Court held that the ATO's detection of an input tax claim so no shortfall amount arose was not a ground for the exercise of the discretion not to impose penalty.

In *DG Empire v FCT*[25] the Tribunal held that the failure to offer the taxpayer an opportunity to make voluntary disclosure was a reason to exercise the discretion to reduce the penalty.

TLAB (Measure No 1) 2010 Amendments

Taxation Laws Amendments (2010 Measures No 1) Bill 2010 (Cth) (**TLAB (Measures No 1) 2010**) will amend the administrative penalty provisions from the date of Royal Assent to:[26]

- extend the penalty regime to impose penalty units for false and misleading statements that do not directly produce a tax shortfall amount;
- extend the penalty regime to impose penalties for false and misleading statements made to persons other than to the ATO exercising a power or performing a function under the taxation laws (such as pay-as-you-go statements made by employees to employers);
- extend the culpability increase and decrease of the base penalty amount in a similar manner to the new penalty unit regime where there is no tax shortfall; and
- enact the registered tax agent safe harbour where the tax agent takes

✓ Tip: Voluntary Disclosure

- A voluntary disclosure should be well drafted and supported by documents to reduce the chance of misunderstanding by the ATO and the unintended consequences arising from an inappropriate or unnecessary disclosure.
- The prudential review, risk assessment and risk management processes and disclosure management processes should be well considered and structured before disclosure so the taxpayer controls the voluntary disclosure rather than reacting to it.
- A history of correspondence between the ATO and the taxpayer and published ATO statements which may request a voluntary disclosure be made is necessary to determine if the 80% or 20% reduction will apply.
- Consider the scope of the audit to determine if the shortfall amount to be disclosed is within or outside the scope of the audit.
- In determining scope, consider the identity of the taxpayer, the type of tax under review, the particular provisions under review and the financial periods under review.
- The audit notification letter will generally specify a date by which a voluntary disclosure must be made to obtain the 80% remission so disclosures should be made by that date.
- A private ruling application constitutes a voluntary disclosure.
- Notification of an audit is limited to the named entity so associated entities not named can and should make a disclosure before audit commences.
- Where the 20% remission applies, identify the potential savings in time or resources for the ATO.
- Consider the audit notification letter and ensure it appropriately commences the audit or review engagement.
- Ensure the voluntary disclosure does not contain an implied waiver of CLP or CAP.
- Ensure the voluntary disclosure is properly authorised by the taxpayer and does not contain any inadvertent misstatements or material admissions.
- Ensure any disclosure of confidential information of third parties is authorised by the third party.
- Ensure any affected third parties are advised that a voluntary disclosure is made so they can manage the potential ATO enquiries that may flow from the disclosure.
- It is not necessary for the taxpayer to admit liability for the shortfall amount so any admission of facts or liability should be expressly excluded in the voluntary disclosure.
- Advisers should be careful when recommending that a voluntary disclosure not be made so as to avoid any professional misconduct or criminal allegations.

reasonable care under the *Tax Agents Services (Transitional Provisions and Consequential Amendments) Act 2009* (Cth) which commenced on 1 March 2010.

Where a false and misleading statement is made that does not produce a tax shortfall, an administrative penalty of 20 penalty units[27] (A$2,200) for lack of reasonable care, 40 penalty units (A$4,400) for recklessness and 60 penalty units (A$6,600) for intentional disregard will be imposed.

The remission of penalty provisions will apply to all types of administrative penalties, including the new penalty unit regime.

PSLA 2006/2 expresses the ATO's view in respect of false and misleading statement penalties and MT 2008/3 expresses the ATO's view in respect of voluntary disclosures. Each will require some amendments to reflect TLAB (Measures No 1) 2010.

OFFSHORE VOLUNTARY DISCLOSURE INITIATIVE

Introduction

The ATO announced on 18 July 2007[28] increased tax haven audit activities together with the OVDI for undisclosed income and over-claimed deductions from offshore activities. The original initiative capped shortfall penalties at 5% for income tax disclosures.[29]

The ATO announced on 30 November 2009 revised offshore voluntary disclosure initiative terms which will end on 30 June 2010. The revised initiative:

- fully remits shortfall penalties where additional taxable income is A$20,000 or less for a tax year;
- remits shortfall penalties to 10% where additional taxable income exceeds A$20,000 for a tax year;
- fully remits general interest charge (**GIC**) for tax years up to and including the 2002 tax year;
- remits GIC to the base rate for the 2003 and 2004 tax years; and
- imposes shortfall interest charge (**SIC**) for the 2005 and subsequent tax years.

The revised initiative does not apply to a taxpayer if:

- the taxpayer is being audited (including under Project Wickenby) for tax issues directly or indirectly in connection with the omitted income or over-claimed deductions;
- that taxpayer has received an information request relating to the omitted income or over-claimed deductions;
- the omitted income arose from a breach of criminal law;
- the taxpayer was involved in marketing or encouraging others to enter into tax evasion schemes; or
- the taxpayer is under investigation by the ATO, Australian Federal Police (**AFP**) or Australian Crime Commission (**ACC**) in respect of taxation-related offences.

The revised initiative is at least superficially attractive because:

- an anonymous disclosure can be made initially to test the ATO's attitude; and
- the ATO will indicate whether the concessions apply and indicate whether criminal law investigations are likely to be initiated.

Australian residency

The OVDI presumes the taxpayer was a relevant Australian tax resident or a foreign resident with an Australian tax liability. Determining Australian tax residency is a vexed question of fact and law.[30]

Where there is uncertainty regarding Australian tax residency or uncertainty concerning if an exemption or Double Tax Agreement (**DTA**) applies, it may be appropriate to make an OVDI voluntary disclosure together with a private ruling application regarding whether Australian tax residency, the exemption or the DTA applies.

The desirability of making a private ruling application will require careful re-consideration from 1 January 2006 after *Tax Laws Amendment (Improvements to Self Assessment Act (No. 2) 2005* (Cth) (**TLA (ISA No.2) 2005**)) because the penalty for not complying with an unfavourable private ruling has been repealed for 2004-05 and subsequent years.[31]

Anonymous disclosure limitations

A no-named or named disclosure can be made. A no-named disclosure must be made through a registered tax agent, an accountant, a lawyer or another authorised person.

Superficially, an anonymous disclosure to test the ATO's attitude is attractive, but the effectiveness of anonymity is uncertain.

The ATO has coercive powers to access information and documents for income tax purposes.[32] The ATO has used these powers to obtain accountants' client lists[33] and lawyers' client lists.[34] Accordingly, the ATO may be entitled to seek and obtain at least the identity of the client that made an anonymous disclosure, so this change to permit anonymity may be illusionary.

The ATO's entitlement to other information and documents is subject to CAP and CLP.[35]

ATO access to accountant documents on tax compliance is administratively imposed only.[36] The ATO considers that the ATO has full access to **source documents**[37] and access to **restricted source documents**[38] and **non-source documents**[39] in exceptional circumstances.

The ATO considers "exceptional circumstances" include where:

- there is reasonable grounds to believe that fraud or evasion or criminal or other illegal activities have occurred;
- source documents have not been provided, have been destroyed or cannot be located or have not been provided under an offshore information request; or
- Part IVA ITAA36 applies.[40]

One-TEL v FCT[41] illustrates the scope and limitations on CAP.

The nature of the OVDI means that the ATO will often have a sufficient basis to allege exceptional circumstances and gain access to restricted source documents and non-source documents.

The CAP is superficially similar to CLP, but is more easily abrogated – more difficult to protect.

The scope of CLP is considered in *FCT v Pratt Holdings P/L*.[42] The scope of CLP is being tested by numerous cases arising out of Project Wickenby.

Instructions and documents provided to a lawyer for the purpose of obtaining legal advice are generally protected from disclosure by CLP. CLP may be lost where the documents were created for an improper purpose, such as evidenced by the application of Part IVA ITAA36.[43]

Broadly, obtaining advice from taxation lawyers in respect of offshore voluntary disclosure risks, procedures and documentation may provide greater protection under CLP than similar services provided by accountants would under CAP.

Excluded taxes

The OVDI is limited to income tax from offshore activities. Accordingly, disclosures about domestic income tax and other taxes are subject to the usual voluntary disclosure rules.

Where the offshore disclosure may have domestic tax consequences (such as deemed dividends or withholding tax obligations), a concurrent disclosure under the usual voluntary disclosure rules may also be made.

Full disclosure and scope of information

The ATO requires full disclosure of all foreign assets and foreign entities, not merely those entities directly or indirectly affected by the flow of funds, ownership or tax shortfall. The OVDI has information and intelligence-gathering aspects. Experience suggests that the ATO will reject a disclosure statement that fails to disclose irrelevant foreign assets or irrelevant foreign entities.

Particular difficulties arise for beneficiaries of discretionary trusts who may have no knowledge of foreign trust structures.

A disclosure is made on the approved form.[44] The approved form includes additional disclosure requirements not required under the usual voluntary disclosure rules such as:

- the purpose of establishing structures overseas;
- the reason the foreign income was omitted or the deduction over-claimed;
- the identification of false documentation; and
- the name and address of any advisers involved in the arrangements and the nature of the advice.

The OVDI may require disclosure of information and purposes that may be incriminating. The ATO coercive powers to access information and documents abrogate the privilege against self-incrimination[45] and spousal privilege[46] for taxation purposes. Those privileges are not generally abrogated for criminal law purposes.

Care is required when making disclosure under the OVDI to ensure incriminating statements are not made (or an OVDI is not made at all) where those disclosures may be used in any subsequent criminal proceedings.

The OVDI also requires the taxpayer to name the advisers that "helped or provided advice about establishing, maintaining or changing overseas assets, structures or related entities". The OVDI has a **whistleblower** aspect.

The ATO will receive information regarding the advice and promotion channels of tax arrangements so a tax adviser may be at risk from being fairly or unfairly disclosed for the promoter penalty regime,[47] for further investigation or as a criminal party or accomplice. The tax adviser will need to ensure that he or she is not in an ethical conflict with a client regarding the OVDI.

The adviser should ensure that the disclosure does not waive any CAP or CLP claim that ought to be sustained. Once CLP or CAP is waived it cannot be reinstated.[48] Disclosure will occur where the content of the privileged material is disclosed by the privilege holder (such as the taxpayer client disclosing the contents of legal advice or the ultimate conclusion of the advice without the reasoning process).[49] *FCT v Rio Tinto Ltd*[50] is the leading case on implied waiver.

An unauthorised waiver of any CAP or CLP by the adviser may expose the adviser to legal proceedings by the client.

Amendment period

The ATO will generally have four years from either the date the tax was payable under an original assessment or the date the notice of assessment was served on the relevant taxpayer to issue an amended assessment. Where Part IVA ITAA36 applies, the ATO has six years to issue the amended assessment. Where there has been fraud or evasion, the ATO has an unlimited period to issue an amended assessment.[51] Accordingly, in innocuous circumstances the ATO may be out of time to issue an amended assessment.

Where the taxpayer has paid less tax than ought to have been paid, there is an **avoidance of tax**.[52] **Fraud** is not necessarily the criminal law concept of fraud. **Evasion** requires more than an intentional avoidance, but something less than fraud.[53] The leading case on fraud and evasion is *Kajewski v FCT*.[54] PSLA 2008/6 expresses the ATO's view in respect of the scope of fraud and evasion.

The intentional omission of income without creditable explanation for the omission has been considered evasion.[55] Accordingly, in the circumstances under consideration by the OVDI, there is often an appreciable risk that the amendment period is unlimited.[56]

A disclosure under the OVDI can be made in respect of periods outside the four or six year amendment period together with submissions regarding the appropriate amendment period to preserve the OVDI concessions.

Reasonably arguable position

As an alternative to the OVDI, a taxpayer may manage the tax risks by adopting a written reasonably arguable position.

Where a taxpayer adopts an interpretation of a tax law that is **reasonably arguable** (which is subsequently found to be incorrect) the taxpayer may be obliged to pay any unpaid tax and interest on that tax, however, penalties should not be imposed on that unpaid tax.[57]

A position adopted is **reasonably arguable** if it would be concluded in the circumstances, having regard to relevant authorities, that what is argued for is about as likely to be correct as incorrect (or more likely to be correct than incorrect).[58] MT 2008/2 expresses the ATO's view in respect of the scope of reasonably arguable position.

If the taxpayer has taken a reasonably arguable position, there is arguably little benefit from making the disclosure, except that the fall back position will be a penalty capped at 10%. To secure the fall back position by making an offshore voluntary disclosure statement, the taxpayer will place the reasonably arguable position

under immediate scrutiny as it will be necessary to make a request for remission of penalty at the same time as lodging the approved form.

Additional remissions

Arguably, a lesser penalty may be possible in appropriate circumstances under the ATO's discretion to further remit penalties.[59]

There may also be appropriate circumstances for the ATO to exercise the ATO's discretion to further remit GIC or SIC.[60]

Payment

The usual enforcement rules will apply.[61] ATO acceptance of an instalment program is not a certainty. Accordingly, unless the taxpayer meets the ATO's administrative requirements, the taxpayer may also have to manage ATO enforcement action arising from the offshore voluntary disclosure statement.

> ✓ **Tip: Offshore Voluntary Disclosure Initiative**
>
> - Consider whether a tax lawyer should undertake the OVDI under CLP.
> - Consider obtaining criminal law risk management advice before making an OVDI.
> - Consider whether a reasonably arguable position should be adopted rather than an OVDI.
> - Ensure that all tax entities affected by the disclosure make separate disclosures.
> - Ensure the person making the disclosure for the entity is formally authorised to make the disclosure.
> - Consider making concurrent private ruling and disclosure under the usual voluntary disclosure regime for tax issues not covered by the OVDI.
> - Consider making a concurrent penalty or GIC or SIC remission application.
> - Consider making a concurrent instalment payment application.

PROSECUTION

Introduction

The decision to make an OVDI voluntary disclosure is important because it may affect:

- the decision of the ATO to refer the matter to the Commonwealth Director of Public Prosecutions (**CDPP**) for prosecution;
- the decision of the CDPP to proceed to prosecution;
- the recommendation to the court by the CDPP for a more lenient or non-custodian sentence;
- the granting of a reduction in sentence by a court for cooperation;[62] and
- the granting of an indemnity from prosecution by the CDPP for providing witness evidence.[63]

A detailed analysis is required to advise a taxpayer on the likelihood of prosecution arising from the OVDI.[64]

The highest risk of prosecution involves matters of fraud and dishonesty. *CPMS 2009* expresses the ATO's view in respect of the scope of fraud control and the prosecution process. Although not exhaustive, indicators of fraud include:

- deliberately hiding income;
- omissions of entire sources of income;
- unexplained failure to declare income;
- claiming fictitious deductions;
- backdated or post dated documents or false documents;
- distribution of income to fictitious partners or beneficiaries;
- the existence of non-arm's length transactions or arrangements;
- inclusion of an overseas loop in a domestic transaction;
- transactions not in the ordinary course of business or surrounded by secrecy; and
- deposits in secret bank accounts.

In advising a taxpayer, an adviser must consider whether activities could constitute fraud or another criminal offence or refer the matter to specialist lawyers.[65]

The ATO has published criminal prosecution statistics (see Table on page 525).[66]

Introduction to criminal law

A particular criminal act or omission may be punishable under the State criminal law or the Federal criminal law (or both). Where the State law and the Federal law are equivalent, the Federal law will prevail.[67]

The State courts, procedures and sentencing apply to Federal criminal prosecutions, unless the Federal law expressly or by implication makes provision contrary to the State law.[68] The court can make reparation orders to disgorge proceeds of crime.[69]

Part III of the *Taxation Administration Act 1953* (Cth) (**TAA 1953**) imposes a number of taxation offences, including the making of false or misleading statements[70] and falsifying or concealing the identity of another.[71] The ATO may elect to treat these offences as civil **prescribed taxation offences** rather than as criminal offences. The civil standard of on the balance of probabilities applies. Such offences are summary in nature and sentences are limited to fines.

More serious indictable offences are under the State criminal law or Federal criminal law. Possibly relevant offences include (Commonwealth offences[72] are identified in italics and Victorian offences are provided for illustration purposes):

- obtaining a financial advantage by deception,[73] fraudulently inducing person to invest money,[74] conspiracy to defraud,[75] *obtaining a financial advantage of Commonwealth property by deception,*[76] *obtaining a gain of Commonwealth property by dishonesty,*[77] *obtaining a financial advantage of Commonwealth property*[78] and *conspiracy to defraud the Commonwealth;*[79]
- false accounting,[80] falsification of documents,[81] suppression of documents,[82] destruction of evidence,[83] *fabricating evidence,*[84] *destroying evidence,*[85] *making false statements in application,*[86] *false or misleading information or documents,*[87] *forgery,*[88] *using forged documents*[89] and *falsification of documents;*[90]
- secret commissions;[91] or

- money laundering,[92] and *money laundering of at least A$1,000,000*[93] *or smaller amounts.*

If prosecution occurs based on the same act or omission for which a taxpayer was liable for an administrative penalty, then the administrative penalty must be abandoned.[94]

ATO referral to prosecution

In summary, the ATO's policies for prosecution action include:[95]

- Administrative penalties will be imposed and prosecution action reserved for the most serious offenders.
- Prosecution action is directed at those taxpayers whose behaviour is least compliant in terms of the Compliance Model.
- Case selection concentrates on offences in the following categories:
  - those that are particularly serious, blatant or involve persistent offenders;
  - those for which there are no other effective means of securing compliance or no other sanctions; or
  - those which are representative of significant/prevalent non-compliance practices and which, if prosecuted on a timely basis, may carry effects wider than those of the particular case.
- Prosecution should not be pursued unless in the public interest after considering:
  - the degree of seriousness of the offence and whether it is of a **technical** nature only;
  - any mitigating or aggravating factors;
  - the youth, age, intelligence, physical health, mental health or special infirmity of the taxpayer;
  - the period that has elapsed since the alleged offence;
  - the degree of culpability of the taxpayer in connection with the offence;
  - the availability and efficacy of any alternatives to prosecution;
  - the prevalence of the offence and the need for deterrence, both for the offender and generally; and
  - the necessity to maintain public confidence in the tax system.
- Prosecution will normally only be considered where it is clear that:
  - the entity or their agent is clearly aware of their obligations and would have sufficient knowledge to meet those obligations;
  - the entity has made no attempt to come to an acceptable arrangement for lodgement with the ATO;
  - the entity has a poor history of compliance with taxation laws having regard to an entity's entire payment, lodgment, withholding and correspondence compliance history; or
  - circumstances such that failure to comply by the entity represents a significant risk to tax administration.

See diagram on page 526.

CDPP and OPP

The *Prosecution Policy of the Commonwealth* and the Victorian *Prosecutorial Guidelines* contain the factors for evaluating whether prosecution should occur. Fox[96] summarises the guidelines as follows:

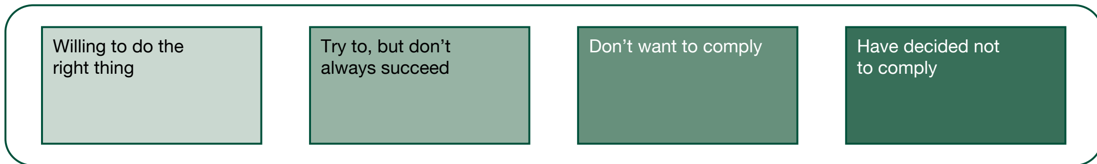
1. Whether there is sufficient admissible, substantial and reliable evidence of a crime known to the law to create a reasonable prospects of securing a conviction. This factor depends not only on an evaluation of the weight and sufficiency of available evidence, but (in the case of indictable offences) also upon whether or not a reasonable jury, properly instructed, would be likely to convict in all the circumstances.
2. Whether the public interest requires a prosecution to be pursued. Evaluation of the public interest factor requires account to be taken of such matters as:
   (a) the seriousness or triviality of the alleged offence;
   (b) the existence of mitigating or aggravating factors;
   (c) the offender's background;
   (d) the youthfulness, mental health or infirmity of the alleged offender;
   (e) the staleness of the alleged offence;
   (f) the alleged degree of culpability of the offender;
   (g) the obsolescence or obscurity of the law under which the charge has been laid;
   (h) whether the prosecution itself would tend to bring the law into disrepute;
   (i) the availability of alternate forms of disposition, eg civil commitment under mental health or related legislation, formal cautioning of young offenders, or other special arrangements for persons under special disability;
   (j) the prevalence of the alleged offence;

Reporting period	Investigations	Prosecutions finalised	Convictions	Custodial sentences	Finalised serious evasion and fraud audits	Tax liability raised ($m)
2009-10*	20	15	15	14	191	69.2
2008-09	183	58	54	40	756	351.5
2007-08	178	77	77	46	314	330.7
2006-07	269	108	106	64	241	94.6
2005-06	367	107	102	57	363	121.4
2004-05	336	164	158	102	400	162.1
2003-04	685	172	166	81	441	137.9

** Part year*

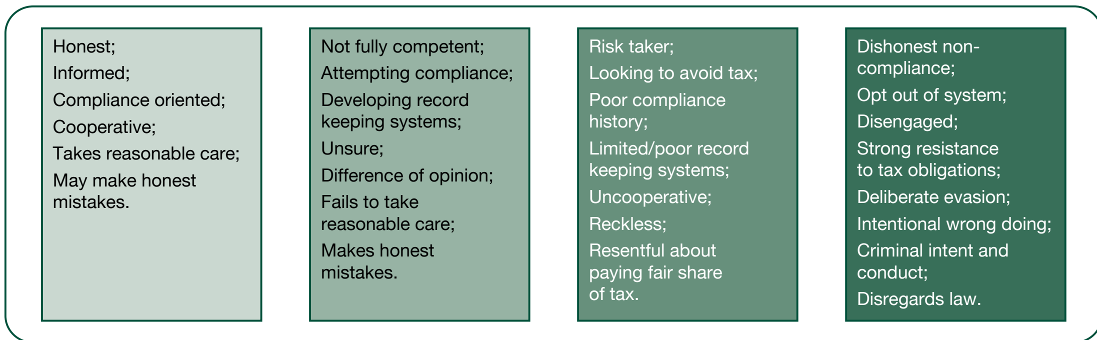
TAXATION OFFICE COMPLIANCE CONTINUUM CMPS 2009

Attitude to Compliance*

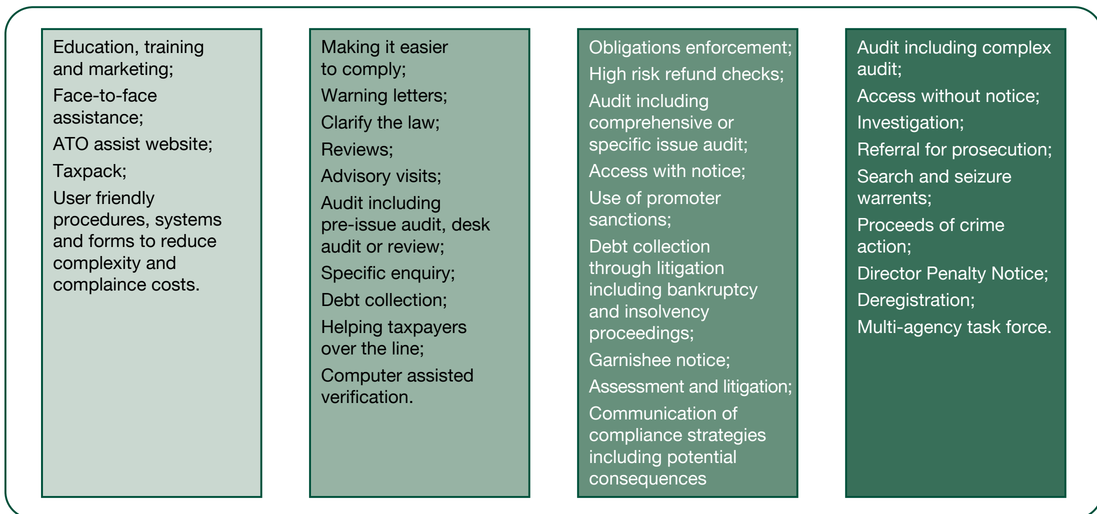


Compliance Strategy*

Taxpayer Behaviour/Motivation**



Tax Office Treatment/Response**



Risk

* Taken from the Compliance model. ** These lists are indicative only and not exhaustive.

(k) whether the consequences of conviction would be harsh or oppressive;

(l) the degree of apparent public concern;

(m) the effect on compensation, reparation and forfeiture if a prosecution is undertaken;

(n) the victim's attitude;

(o) the likely length and expense of the trial;

(p) the degree of cooperation provided by the accused in relation to the prosecution of others;

(q) the likely sentencing outcome;

(r) whether the offence is only triable by indictment; and

(s) the necessity of maintaining public confidence in the courts.

The decision to prosecute concerns the balancing of several factors outside the characteristics of the taxpayer. Accordingly, there are limitations on the ability to accurately predict whether the CDPP will prosecute.

Only the CDPP can grant an indemnity from prosecution. The indemnity is from use of self incriminating evidence[97] or from prosecution.[98] The CDPP has indicated he will give favourable consideration to granting immunity for an offshore voluntary disclosure.[99] How these statements reconcile with the more restrictive statements in *Prosecution Policy of the Commonwealth* is unclear.[100]

TAX ADVISER'S LIABILITIES

Promoter penalties

The promoter penalty regime applies to proscribed conduct on or after 6 April 2006 so there may be some exposure for advisers for activities after that date.[101]

PSLA 2008/7 and PSLA 2008/8 express the ATO's view in respect of the scope of the promoter penalty regime.

The PSLAs distinguish between promotion and provision of independent and objective tax planning advice. To assist advisers to identify circumstances when they may be at risk from the promoter penalty regime, the PSLAs make the following relevant statements:

- the mere provision of positive and supportive advice about an arrangement or structuring of an arrangement is not the promotion of a tax exploitation scheme;
- receipt of success or contingency fees, hourly billing in excess of time actually spent, mark-ups on normal fee rates generally or for skill care and attention or commissions will likely exclude the mere provision of advice exemption;
- the higher the degree of involvement in the activities the more likely the adviser will be a promoter (such as doing presentations to the deviser's clients explaining the advice);
- the higher the degree of involvement in the management of the deviser or marketing the more likely the adviser will be a promoter;
- the more robust the advice and review and quality assurance procedures the less likely an adviser will be a promoter; or
- well drafted scoping, qualification and disclaimer provisions in advice may reduce the risk that an adviser will be a promoter.

The civil penalty is the greater of twice the consideration received or receivable in respect of the scheme or $550,000 for an individual and A$2,750,000 for a company.[102]

Adviser's liabilities

An adviser may have a criminal law exposure where the adviser has personally committed or attempted to commit an offence or is a party or an accomplice to the promoter's criminal offence or client's criminal offence.[103] Relevantly, being an accessory,[104] concealing the offence of another,[105] abetting,[106] conspiring,[107] inciting,[108] or attempting[109] an offence may constitute an offence.

A person who attempts, incites or conspires to commit an offence commits a discrete offence of attempting, inciting or conspiring to commit that offence. In contrast, an accomplice is taken to commit the same offence as the principal criminal. The area of parties and accomplices is very complex.[110]

CONCLUSION

The increasing incidence of review and audit activities means there is great value in making voluntary disclosure to manage tax risks.

The OVDI is of undoubted benefit for those taxpayers that have undeclared offshore income in innocuous circumstances. However, for taxpayers that have been involved in tax haven products or promoted offshore structures and products, there is an appreciable risk that the OVDI will not apply and, in some circumstances, an appreciable risk that criminal prosecution action may be instigated.

While the voluntary disclosure and OVDI appear simple, a proper analysis of the taxation administration and criminal prosecution aspects of the disclosure are extremely complex and require careful consideration.

In providing disclosure advice in respect of offshore arrangements that have an element of criminality, the adviser should take care to ensure that the adviser does not inadvertently commit a criminal offence such as concealing an offence, falsification of accounts or documents or suppressing documents.

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Reference notes

1. *Derek and the Dominos, "Tell the Truth", Layla and Other Assorted Love Songs (Polydor Records, 1970).*
2. *Part 4-25 Taxation Administration Act 1953 (Cth) (TAA 1953).*
3. *Table adapted from the CCH Australia Ltd Australian Federal Tax Reporter at ¶978-005.*
4. *P Sokolowski, The Administrative Penalty Regime – A Swinging Reminder or Just Swinging, Taxation Institute of Australia (National), 5 March 2010.*
5. *Section 284-225 TAA 1953; MT 2008/3: Shortfall penalties: voluntary disclosure (formerly TR 94/6).*
6. *Section 284-225(5) TAA 1953.*
7. *Section 298-20 TAA 1953; PSLA 2006/2 at [150]; MT 2008/3 at [27].*
8. *Failure to disclose a shortfall once known to the taxpayer may constitute tax avoidance or a crime.*
9. *PSLA 2006/2: Administration of shortfall penalty for false or misleading statements.*
10. *MT 2008/3: Shortfall penalties: voluntary disclosure.*
11. *PSLA 2006/2 at [121].*
12. *PSLA 2006/2 at [129]; MT 2008/3 at [63].*
13. *MT 2008/3 at [28].*
14. *MT 2008/3 at [71].*
15. *MT 2008/3 at [245].*
16. *MT 2008/3 at [43] & [44].*

17 PSLA 2006/2 at [128].

18 MT 2008/3 at [86].

19 MT 2008/3 at [90].

20 MT 2008/3 at [7].

21 M D'Acenzo, "Tax office announces offshore voluntary disclosure initiative", Media Release 2007/34, 18 July 2007.

22 British American Tobacco Australia Services Ltd v FCT [2009] FCA 1550 at [107].

23 Lawrence v FCT (2008) 70 ATR 376 at [111].

24 Dixon v FCT (2008) 69 ATR 627 at [23].

25 DG Empire v FCT (2007) 66 ATR 925 at [70].

26 There are also other amendments to the penalty regime which are not discussed in this article.

27 A penalty unit is $110, s 4AA Crimes Act 1914 (Cth) (CA1914).

28 M D'Acenzo, "Tax office announces offshore voluntary disclosure initiative", Media Release 2007/34, 18 July 2007.

29 See R Jorgensen, "Offshore Voluntary Disclosure Initiative & Prosecution", Taxation Institute of Australia (Victoria), 27 September 2007 for a discussion of the former OVDI.

30 A detailed discussion of Australian tax residency is beyond the scope of this article.

31 Professor S Graw, "Living with ROSA – implications of the self-assessment changes for tax practitioners", Taxation Institute of Australia 21st National Convention, 7 April 2006.

32 Section 263 Income Tax Assessment Act 1936 (Cth) (ITAA36) (access to premises and documents) and s 264 ITAA36 (provision of information and documents).

33 Deloitte Touche Tohmatsu v FCT (1998) 40 ATR 435.

34 FCT v Coombes (No 2) (1989) 40 ATR 403.

35 Detailed consideration of CAP and CLP is beyond the scope of this article.

36 Guidelines to Accessing Professional Accounting Advisors' Papers.

37 All documents prepared in connection with the conception, implementation and formal recording of a transaction, traditional accounting records and the permanent file for statutory audits.

38 All advices prepared by external professional accountants for the sole purpose of advising a client on taxation and prepared in connection with the conception and implementation of a transaction (front end advice at the time of conception or implementation).

39 All advices (other than restricted source documents) created post transaction including documents in the current audit file, prudential tax advice and due diligence advices.

40 One-TEL v FCT (2000) 44 ATR 52; PSLA 2004/14 access to board documents.

41 One-TEL v FCT (2000) 44 ATR 52.

42 FCT v Pratt Holdings P/L (2005) 60 ATR 466; Pratt Holdings P/L v FCT (2004) 56 ATR 128.

43 Clements, Dinne & Bell P/L v AFP (2001) 188 ALR 515.

44 NAT 71149-12.2009.

45 FCT v De Vonk (1995) 31 ATR 48.

46 Stoddart v ACC [2009] FCA 1108.

47 Division 290, Schedule 1, TAA 1953.

48 Ampolex Ltd v Perpetual Trustee Co (Canberra) Ltd (1996) 137 ALJR 28 at 32.

49 Goldberg v Ng (1996) 185 CLR 83 at 95-96; Ampolex Ltd v Perpetual Trustee Co (Canberra) Ltd (1996) 137 ALJR 28 at 32.

50 FCT v Rio Tinto Ltd (2006) 63 ATR 79.

51 Section 170 ITAA36

52 Westgarth [1950] 81 CLR 396 at 414.

53 Simms v Register of Probate (1900) AC 332 at 334.

54 Kajewski v FCT (2003) 52 ATR 455 at [111], [113] & [114].

55 Chemical Manufacturing Co v CT(NSW) (1949) 79 CLR 296.

56 A detailed discussion of fraud and evasion is beyond the scope of this article.

57 Section 284-75(2) Sch. 1 TAA 1953.

58 Section 284-15 Sch. 1 TAA 1953

59 Section 298-20 TAA 1953; PSLA 2006/2

60 PSLA 2006/8 at [88]; PSLA 2008/13: ATO Receivables Policy, Chapter 93.

61 PSLA 2008/13: ATO Receivables Policy, Chapter 10.

62 Section 21E CA 1914.

63 Section 9(6) and (6A)-(6F) Director of Public Prosecutions Act 1983 (DPPA 1983).

64 WB Zichy-Woinarski QC, "Giving Criminal Law Advice to the Tax Client", (2001) 30 AT Rev 206.

65 A detailed discussion of the ATO and CDPP prosecution policies is beyond the scope of this article.

66 www.ato.gov.au/corporate/content.asp?doc=/content/00134154.htm (reviewed 1 March 2010).

67 Miller v Miller (1978) 141 CLR 269.

68 Sections 68 and 79 Judiciary Act 1903 (Cth) (JA 1903).

69 Section 116 Proceeds of Crimes Act 2002 (Cth) (PCA 2002).

70 Sections 8K, 8N and 8P TAA 1953.

71 Section 8U TAA 1953.

72 For a detailed explanation refer to Commonwealth Attorney-General's Department, The Commonwealth Criminal Code – A Guide for Practitioners, March 2002.

73 Section 82 Crimes Act 1958 (Vic) (CA 1958) "A person who by any deception dishonestly obtains for himself or another any financial advantage is guilty of an indictable offence" (max 10 years).

74 Section 191 CA 1958 (max 15 years).

75 Common law offence with statutory penalty s 320 CA 1958 (max 15 years).

76 Section 134.2 Criminal Code 1995 (Cth) (CC 1995) (max 10 years).

77 Section 135.1 CC 1995 (max five years).

78 Section 134.5 CC 1995 (max one year).

79 Section 135.4 CC 1995 (max 10 years).

80 Section 83 CA 1958 (max 10 years).

81 Section 83A CA 1958 (max 10 years).

82 Section 86 CA 1958 (max 10 years).

83 Section 254 CA 1958 (max five years).

84 Section 36 CA 1914 (max five years).

85 Section 39 CA 1914 (max five years).

86 Section 136.1 CC 1995 (max one year).

87 Sections 137.1 and 137.2 CC 1995 (max one year).

88 Section 144.1 CC 1995 (max 10 year).

89 Section 145.1 CC 1995 (max 10 years).

90 Section 145.4 CC 1995 (max seven years).

91 Section 176 CA 1958 (max 10 years).

92 Section 194 CA 1958 (max 20 years).

93 Section 400.3. CC 1995 (max 25 years).

94 Section 8ZE TAA 1953.

95 CPMS 2009, The Prosecution Policy of the Commonwealth 1990 (2nd ed), Commonwealth Fraud Control Guidelines 2002, Australian Government Investigation Standards 2003, Heads of Commonwealth Operational Law Enforcement Agencies (HOCOLEA) principles for case selection, prosecution and enforcement, Memorandum of Understanding with CDPP, Various Memoranda of Understanding or Service Level Agreements with key agencies including Australian Federal Police, Australian Crime Commission, Australian Customs Services and Australian Securities and Investments Commission.

96 R Fox, Victorian Criminal Procedure State and Federal Law, Monash Law Book Co-operative Ltd 2005 at 2.3.3.1.

97 Section 9(6) DPPA 1983.

98 Section 9(6D) DPPA 1983.

99 www.ato.gov.au/corporate/content.asp?doc=/content/87095.htm (reviewed 1 March 2010).

100 See paras 5.4 to 5.6 Prosecution Policy of the Commonwealth.

101 Division 290, Schedule 1 TAA 1953.

102 5000 penalty units for individuals and 25,000 penalty units for a company s 290-50 Sch. 1 TAA 1953 and each penalty units is $110 – s 4AA CA 1914.

103 A detailed discussion of the extensions of criminal responsibility to a party or accomplice is beyond the scope of this article.

104 Section 325 CA 1958; s 6 CA 1914.

105 Section 326 CA 1958.

106 Section 323 CA 1958; s 11.2 CC 1995.

107 Section 321 CA 1958; s 11.5 CC 1995.

108 Section 321G CA 1958; s 11.4 CC 1995.

109 Section 321M CA 1958; s 11.1 CC 1995.

110 VA Morfuni SC, "The Civil Liability of Tax Advisors". (2005) 34 AT Rev 131; VA Morfuni SC, "Criminal Law Risks for the Tax Adviser" (2002) 31 AT Rev 4.