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## JMA Accounting: Judicial Diminution of Professional Privilege in Tax Investigations?

Rodney Fisher  
Rodney.Fisher@au.ey.com

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# JMA Accounting: Judicial Diminution of Professional Privilege in Tax Investigations?

## **Abstract**

JMA Accounting and Entrepreneur Services v Carmody suggested that there may be circumstances under which potentially privileged documents should be made available to executive officers, who could scan the documents to make a judgment on their privileged status. This article draws on the rationale underlying professional privilege, and the exceptions to the privilege, to examine the potential impacts that may follow when documents potentially subject to privilege are made available to the executive in the course of an ATO investigation using legislative access powers. The suggestion is made that the decision may amount to abrogation to the executive of a matter which should remain a judicial function.

# JMA ACCOUNTING: JUDICIAL DIMINUTION OF PROFESSIONAL PRIVILEGE IN TAX INVESTIGATIONS?

RODNEY FISHER

*JMA Accounting and Entrepreneur Services v Carmody* suggested that there may be circumstances under which potentially privileged documents should be made available to executive officers, who could scan the documents to make a judgment on their privileged status.

This article draws on the rationale underlying professional privilege, and the exceptions to the privilege, to examine the potential impacts that may follow when documents potentially subject to privilege are made available to the executive in the course of an ATO investigation using legislative access powers. The suggestion is made that the decision may amount to abrogation to the executive of a matter which should remain a judicial function.

## INTRODUCTION

One primary role for the Commissioner of Taxation is ensuring taxpayer compliance. In fulfilling this obligation the Commissioner is provided with legislative powers for access<sup>1</sup> and information gathering<sup>2</sup> in relation to taxpayer records. It is the availability of these legislative powers of access which underlie the audit and investigatory role of the ATO. Increasingly, the use of the ATO access powers has been met by a claim for legal professional privilege over documents sought, resulting in an increase in litigation as to availability of professional privilege as an answer to as the Commissioner's access powers.

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<sup>1</sup> Section 263 ITAA 1936 provides:

The Commissioner, or any officer authorised by him in that behalf, shall at all times have full and free access to all buildings, places, books, documents and other papers for the purposes of this Act, and for that purpose may make extracts from or copies of any such books, documents or papers.

<sup>2</sup> Section 264 ITAA 1936 provides:

The Commissioner may by notice in writing require any person, whether a taxpayer or not, ...

(a) to furnish him with such information as he may require; and

(b) to attend and give evidence before him ... concerning (the taxpayer's) or any other person's income or assessment, and may require him to produce all books, documents and other papers whatever in his custody or under his control relating thereto.

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While courts have generally shown a reluctance to curtail the availability of professional privilege, judicial comments in the Full Federal Court decision in *JMA Accounting and Entrepreneur Services v Carmody*<sup>3</sup> may appear to cast some doubt on the efficacy of professional privilege in protecting tax documents. The Court<sup>4</sup> found in this case that there were circumstances where taxpayer documents potentially subject to confidentiality under legal professional privilege should be made available to ATO officers who would scan the documents to determine whether professional privilege may apply.

The following discussion raises two broad matters of concern in relation to this finding by the court. The first issue concerns the grounds on which the court based this finding. Reference is made in the decision to the authority provided from the decision in *Allitt v Sullivan*.<sup>5</sup> It is suggested that the circumstances in the present case are sufficiently distinguishable from those in *Allitt v Sullivan* to suggest that there may be doubt as to the direct relevance of that case to the present circumstances.

The second matter addressed is that the outcome resulting from the decision must raise some serious concerns for taxpayers, as the judicial comments may be seen as abdicating to the executive the judicial role of adjudication on claims for professional privilege. There are two main aspects of concern in relation to this potential diminution of privilege as an answer to the Commissioner's access powers. The first concerns the role of the executive itself in determining confidentiality of taxpayer documents, when the executive is an interested party and would be the opposing party in any potential litigation. The second concern questions whether the conduct in providing potentially privileged material to the executive may constitute an express or implied waiver of the privilege which may otherwise have attached to the material.

By way of prelude to this discussion, the article initially outlines the rationale underlying legal professional privilege, and the circumstances under which the privilege would not be available, or may be foregone. From these principles, the paper examines the judicial comment in *JMA Accounting* in relation to whether it would be appropriate to apply the principles from *Allitt v Sullivan*. The paper will then discuss whether it is appropriate for the decision as to the availability of professional privilege to be delegated to the executive, and potential consequences which may flow from this.

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<sup>3</sup> (2004) 57 ATR 365.

<sup>4</sup> Joint judgment of Spender, Madgwick and Finkelstein JJ.

<sup>5</sup> [1988] VR 621.

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### COMMON LAW PROFESSIONAL PRIVILEGE

The common law doctrine of legal professional privilege protects from disclosure confidential communications between a client and legal adviser, where the dominant purpose of the communication is obtaining or giving legal advice or assistance.<sup>6</sup> Mason and Brennan JJ explained the rationale for the privilege as being the furtherance of the administration of justice through the fostering of trust and candour in the relationship between lawyer and client.<sup>7</sup> While the privilege may have a centuries long history,<sup>8</sup> this does not make it 'archaic, technical or outmoded',<sup>9</sup> but rather suggests it may be seen as 'an ancient doctrine which has assumed a life of its own'.<sup>10</sup>

What has come to be regarded as the classic statement of the rationale on which the privilege is based is explained in the judgment of Lord Brougham LC in *Greenough v Gaskell*:<sup>11</sup>

But it is out of regard to the interests of justice, which cannot be upholden, and to the administration of justice, which cannot go on, without the aid of men skilled in 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.

From these beginnings the rationale underlying professional privilege has expanded in scope as explained by Murphy J in the seminal case of *Baker v Campbell*:<sup>12</sup>

Its rationale is no longer the oath and honour of the lawyer as a gentleman ... It is now supported as a necessary corollary of fundamental constitutional or human rights<sup>13</sup> (with) a strong sense that any person charged or in peril of a charge has a fundamental human right to professional advice - which may not be effectively given if facts are withheld.<sup>14</sup>

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<sup>6</sup> *Attorney General for the Northern Territory v Maurice* (1986) 161 CLR 475 (Mason and Brennan JJ) 487 quoting *Reg v Bell; Ex parte Lees* (1980) 146 CLR 141, 144 (Gibbs J).

<sup>7</sup> *Attorney General for the Northern Territory v Maurice* (1986) 161 CLR 475, 487.

<sup>8</sup> See, eg, Gibbs CJ in *Maurice* at 480.

<sup>9</sup> *Ibid* (Gibbs J) 480.

<sup>10</sup> *Maurice* (Mason and Brennan JJ) at 487.

<sup>11</sup> 1 My & K, 103; 39 E.R, 621 in *Baker v Campbell* (1983) 153 CLR 52, 77.

<sup>12</sup> *Baker v Campbell* (1983) 153 CLR 52.

<sup>13</sup> *Baker v Campbell*, (Murphy J) 85.

<sup>14</sup> *Baker v Campbell*, (Murphy J) 85 quoting *R v Ulljee* [1982] 1 NZLR 561, 569.

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In a similar vein, Deane J was prepared to find that the principle of professional privilege:

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.<sup>15</sup>

In applying the privilege a balance is sought between two competing public interests, being the public interest in the disclosure of all relevant communications, and a narrower public interest in preserving confidentiality between solicitor and client to assist the administration of justice.<sup>16</sup> The difficulty inherent in determining this balance was highlighted in *Eso Australian Resources v FCT*,<sup>17</sup> with the majority expressing the view that:

The obvious tension between this policy (privilege) and the desirability, in the interests of justice, of obtaining the fullest possible access to the facts relevant to the issues in a case lies at the heart of the problem of the scope of the privilege. Where the privilege applies, it inhibits or prevents access to potentially relevant information. ... For the law, in the interests of the administration of justice, to deny access to relevant information, involves a balancing of competing interests.<sup>18</sup>

The variance in judicial considerations confirms that the determination of this balance in particular cases has been 'controversial and unsettled'. Mason J (as he then was) in his dissent cautioned against a broad scope for the privilege, suggesting that:

it is by no means self-evident that the value of this public interest (candour by the client) is greater than the public interest in facilitating the availability of all relevant materials for production in litigious disputes.<sup>19</sup>

Despite the divergent views as to how the greater public interest is best served, professional privilege has retained primacy, as suggested by Lord Langdale MR:

The unrestricted communication between parties and their professional advisors, has been considered to be of such importance as to make it advisable to

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<sup>15</sup> *Baker v Campbell*, (Deane J) 120.

<sup>16</sup> *Clements Dunne & Bell* [2001] FCA 1858, [11] (North J).

<sup>17</sup> *Eso Australia Resources v FCT* (1999) 201 CLR 49.

<sup>18</sup> *Eso Australia Resources*, 64-5.

<sup>19</sup> *Baker v Campbell*, (Mason J) 74.

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protect it even by the concealment of matter without the discovery of which the truth of the case cannot be ascertained.<sup>20</sup>

This view has been followed in Australia, with Deane J confirming that the:

efficacy (of privilege) as a bulwark against tyranny and oppression depends upon the confidence of the community that it will in fact be enforced. That being so. It is not to be sacrificed even to promote the search for justice or truth in the individual case or matter.<sup>21</sup>

*Daniels Corporation International Pty Ltd v ACCC*<sup>22</sup> has affirmed the role of professional privilege as an answer to investigatory procedures of the executive, with the joint judgment of Gleeson CJ, Guadron, Gummow and Hayne JJ holding that:

in the absence of provision to the contrary, legal professional privilege may be availed of to resist the giving of information or the production of documents in accordance with investigatory procedures...<sup>23</sup>

The doctrine of professional privilege has become so firmly entrenched that abrogation of the privilege is seen as a role for the legislature,<sup>24</sup> and the privilege cannot be 'abolished by the flourish of the judicial pen.'<sup>25</sup> Further, any legislative abrogation must be by express words or necessary intendment, and:

(i) it is to be presumed that if the Parliament intended to authorise the impairment or destruction of that confidentiality by administrative action it would frame the relevant statutory mandate in express and unambiguous terms.<sup>26</sup>

Where legislation purports an implied abrogation of the privilege, the starting point for the courts has been:

a presumption that there is no intention to interfere with basic common law doctrines unless the words of the statute expressly or necessarily require that result. ... Legal professional privilege ... is clearly a doctrine which falls within the presumption.<sup>27</sup>

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<sup>20</sup> *Reece v Trye* (1846) 9 Beav 316, 319; 50 E.R. 365, 366 quoted in *Baker v Campbell*, 115.

<sup>21</sup> *Maurice*, (Deane J) 475.

<sup>22</sup> HCA 49 (7 November 2002).

<sup>23</sup> *Daniels v ACCC*, [10].

<sup>24</sup> The High Court decision in *Daniels v ACCC* has reaffirmed that the privilege can only be abrogated by clear and express statutory terms.

<sup>25</sup> *Baker v Campbell*, (Mason J) 26.

<sup>26</sup> *Baker v Campbell*, (Deane J) 116-7.

<sup>27</sup> *Baker v Campbell*, (Dawson J) 123.

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### Professional privilege in tax investigations

The taxation access powers have been given a wide interpretation by the courts, with French J in *FCT v Citibank Ltd*<sup>28</sup> finding that the powers in s263 are 'wide and not readily amenable to implied restrictions.'<sup>29</sup> His Honour elaborated on the meaning of the terms in the section:

The concept of 'full access' prima facie conveys that the availability of entry or examination extends to all parts of the relevant place or building and to the whole of the relevant ... documents and other papers. 'Free' conveys an absence of physical obstruction.<sup>30</sup>

Similarly, s 264 has been given a wide interpretation, with the Commissioner able to use the provision to conduct a 'fishing expedition', with there being no requirement for a dispute between the taxpayer and the Commissioner before the power is exercised.<sup>31</sup> The powers under both sections must only be exercised for the purpose of enabling the Commissioner to perform his functions under the Act.<sup>32</sup>

Despite the wide scope of the access powers, the courts have been prepared to find that the powers operate subject to legal professional privilege. In *Citibank*, Bowen CJ and Fisher J found that the power of the Commissioner to search and make copies of documents did not extend to documents to which privilege applied.<sup>33</sup> While there has been an absence of argument concerning the availability of professional privilege as an answer to a s 264 notice, in a joint decision in *FCT v Coombes*,<sup>34</sup> the Full Federal Court was prepared to state that s 264 was subject to legal professional privilege.<sup>35</sup>

When a request for access to documents is met by a claim for legal professional privilege, the claim may be either accepted or challenged by the investigatory body. If the claim is accepted, no access would be available to the documents subject to the claim for privilege.

A more common outcome may be for the privilege claim to be challenged, in which case it falls to the courts to adjudicate upon the claim for privilege. In these circumstances the common procedure would be for the documents subject to the privilege claim to be held by the courts, as a body independent from the executive

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<sup>28</sup> (1989) 20 ATR 292.

<sup>29</sup> *Citibank*, (French J) 313.

<sup>30</sup> *Ibid.*

<sup>31</sup> *McCormack v DCT* (2001) 48 ATR 608.

<sup>32</sup> *Deloitte Touch Tomatsu v DFCT* 98 ATC 5192, (Goldberg J) 5211-12.

<sup>33</sup> *Citibank*, 301.

<sup>34</sup> (1999) 42 ATR 356.

<sup>35</sup> *Coombes*, (Sundberg, Merkel & Kenny JJ) [10].



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under the doctrine of the separation of powers. The court would then sit in judgment upon the privilege claim, having regard to whether the tests to satisfy a claim for privilege had been met. If these tests were satisfied, access to the documents would be denied, while if the tests were not met, the claim for professional privilege would fail, and the documents would be available.

Central to this process is the role of the courts in determining whether documents sought by an investigating executive body, such as the ATO, would meet the tests to satisfy a claim for privilege. This is particularly so when the investigating body would itself be a party to any dispute or proceedings which may arise between the parties. Notions of justice and fairness require that a party to any dispute should not also be sitting in judgment to determine the outcome of the dispute. In such circumstances, even with the best of intentions, justice cannot be seen to be done.

### **Limitations on legal professional privilege**

As noted above, the operation of the doctrine requires a balancing between the competing public interests, with the consequence of this balancing being that the privilege cannot operate 'at large', but should be confined within strict limits.<sup>36</sup>

The major limitations which apply to confine the scope of the operation of professional privilege include the crime/fraud exception, and waiver.

### ***Illegal purpose***

Communications between a client and legal advisor which are intended to further any criminal or fraudulent<sup>37</sup> purpose cannot attract professional privilege. This principle has been stated clearly, with Gummow J describing that the 'privilege does not attach to a communication made as part of a criminal or unlawful proceeding or in furtherance of an illegal object.'<sup>38</sup> As explained by the Earl of Halsbury LC in *Bullivant v Attorney General (Vic)*:<sup>39</sup>

this limitation has been put, and justly put, that no court can be called upon to protect communications which are in themselves part of a criminal or unlawful proceeding.<sup>40</sup>

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<sup>36</sup> See, eg, *Grant v Downs* (1976) 135 CLR 674, 685 (Stephen, Mason & Murphy JJ).

<sup>37</sup> [F]raud in this connection is not limited to the tort of deceit and includes all forms of fraud and dishonesty ...'; *Attorney General (NT) v Kearney* (1985) 158 CLR 500 (Wilson J) quoting Goff J in *Crescent Farm (Sidcup) Sports Ltd v Sterling Offices Ltd* [1972] Ch 553, 564-5.

<sup>38</sup> *Commissioner for Australian Police v Propend Finance* (1997) 188 CLR 501, CLR 563-4 (Gummow J).

<sup>39</sup> [1901] AC 196.

<sup>40</sup> *Bullivant* quoted in *Clements, Dunne & Bell*, [30].

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The onus of establishing that an illegal or improper purpose attaches to a communication, thus denying the availability of privilege in relation to that communication, lies with the party resisting the claim. To deny privilege the party must show reasonable grounds for believing that the communication was made for an illegal or improper purpose, or a purpose contrary to the public interest.<sup>41</sup>

If communication is intended to further a criminal purpose, then professional privilege will be excluded whether it is the client or a third party who has the criminal intention. This will be the case even though the privilege would have been that of the client and not that of the third party.<sup>42</sup>

However, while it is clear that a communication with a legal advisor directed to evading the law by illegal conduct would not be privileged, 'if a client asked how he could do something which would not bring him within the scope of the Act, there would be evasion in another sense, but no illegality, and the communication would be privileged.'<sup>43</sup> Thus a distinction is drawn between communication involving illegality, which is against the interests of justice and the public interest and is thus outside the ambit of professional privilege, and communication which falls short of illegality, in relation to which privilege may still apply.

### *Waiver*

As with all common law privileges, professional privilege may be waived by the person otherwise entitled to rely on the privilege. With professional privilege designed to maintain confidentiality of the communication of a client with their legal advisor, it is the client who is entitled to the benefit of confidentiality, and the client who may relinquish that entitlement.<sup>44</sup> Waiver of professional privilege by the client may be express or implied, but difficulties may arise in identifying when there has been a waiver of privilege, as waiver 'is a vague term, used in many senses, and ... it often requires further definition according to the context.'<sup>45</sup>

### *Express waiver*

Express waiver is evidenced by a voluntary and intentional disclosure of the contents of an otherwise privileged communication, where the disclosure is made generally

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<sup>41</sup> *Propend Finance*, CLR 514 (Brennan J).

<sup>42</sup> *Clements, Dunne & Bell*, 697 (North J).

<sup>43</sup> *Bullivant*, 207 (Lord Lindley).

<sup>44</sup> See, eg, *Mann v Carnell* [1999] HCA 66 (21 December 1999) [28] (Gleeson CJ, Gaudron, Gummow and Callinan JJ).

<sup>45</sup> *Mann v Carnell* [1999] HCA 66 (21 December 1999), [28].

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and not for a limited or specific purpose. This will be the case even if the disclosure was not intended to have the consequence of constituting an express waiver.<sup>46</sup>

Where there has been a disclosure not meeting the requirements above for an express waiver, there may still be waiver imputed by the operation of law. Such an implied waiver may arise in circumstances where there has been a partial disclosure of the contents of a communication, or a disclosure which is made otherwise than as a voluntary and intentional disclosure.

### *Implied waiver*

The issue of implied waiver arose in the case of *Attorney-General for the Northern Territory v Maurice* where a claim book had been lodged and distributed and limited reference made to it, although it had never formally been tendered and accepted into evidence. Gibbs CJ, in looking to the principles underlying imputed waiver, had regard to Wigmore<sup>47</sup> which suggested regard should be had not only to the implied intention, but to an objective consideration of fairness and consistency. This principle suggested that where there was no intention to waive privilege, implied waiver could still be established from an objective consideration which may show that fairness required that privilege should cease.

His Honour saw the authorities as establishing that an implied waiver would depend on whether it would be unfair or misleading to allow a party to refer to or use material and still assert that the material was privileged.<sup>48</sup> The authorities referred to by Gibbs CJ suggested that privilege would not be waived by the 'mere reference' to the document in pleadings, as it would not be unfair or misleading for pleadings to refer to a document which is not part of the evidence. On this basis, there would be no implied waiver until material was adduced in evidence, and if the document was set out in full, the suggestion would be that the privilege was waived.<sup>49</sup>

Gibbs CJ took the view that while the question of whether material had been disclosed in evidence would be relevant, it would not be decisive. Rather he saw the focus as being on fairness, with the critical question being whether the disclosure or use made of the material was such as to render it unfair to continue to uphold the privilege.<sup>50</sup>

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<sup>46</sup> *FCT v Coombes* (1999) 42 ATR 356, 369.

<sup>47</sup> *Wigmore on Evidence* (3<sup>rd</sup> edit, 1940) vol 8.

<sup>48</sup> *Maurice* (Gibbs CJ) 481.

<sup>49</sup> *Maurice*, 481.

<sup>50</sup> *Maurice*, 483.

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The joint decision of Mason and Brennan JJ in *Maurice* also saw a critical role for fairness, suggesting that 'the implied waiver inquiry is at bottom focused on the fairness of imputing such a waiver.'<sup>51</sup> and that 'fairness will usually require that waiver as to one part of a protected communication should result in waiver as to the rest of the communication on that subject matter.'<sup>52</sup> However fairness was not an abstract concept, with fairness of maintaining privilege being a function of the conduct of the party claiming privilege, and whether this conduct made it unfair to maintain the privilege.<sup>53</sup>

In a similar vein, Deane J saw imputed or implied waiver as being based on notions on fairness, arising in circumstances where privileged material had been used in a way which made it unfair to continue to assert the privilege.<sup>54</sup> While recognising this as a difficult area of law, Dawson J was also prepared to find that implied waiver could be required by fairness, even though waiver was not intended.<sup>55</sup>

This notion of fairness continued as the focus in determining implied waiver, with Branson and Lehane JJ in *Telstra Corp Ltd v BT Australasia Ltd*<sup>56</sup> identifying fairness as a common principle underlying the different classes of waiver cases. Their Honours found that there would be waiver of professional privilege 'if by reason of some conduct of the party otherwise entitled to the privilege, it would be unfair to the other party, in a way which goes to the integrity of the legal process, for the privilege to be maintained.'<sup>57</sup> This finding accords with the emphasis being on the conduct of the party seeking to claim privilege, and whether maintaining privilege in the face of this conduct would be unfair.

While these cases had placed the focus for determining implied waiver on the issue of fairness and whether the conduct of a party made it unfair to continue to claim privilege, McHugh J in *Mann v Carnell* suggested that in using the fairness test, Gibbs CJ was not formulating a new principle of law, but rather was using fairness as a factual criterion in the circumstances to judge whether privilege had been waived.<sup>58</sup>

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<sup>51</sup> *Maurice*, 488 (Mason and Brennan JJ).

<sup>52</sup> *Ibid.*

<sup>53</sup> *Maurice* 487 (Mason and Brennan JJ).

<sup>54</sup> *Maurice*, 493.

<sup>55</sup> *Maurice*, 497.

<sup>56</sup> [1998] 901 FCA (24 July 1998).

<sup>57</sup> *Telstra* at 16 <[http://www.austlii.edu.au/au/cases/cth/federal\\_ct/1998/901.html](http://www.austlii.edu.au/au/cases/cth/federal_ct/1998/901.html)> accessed 16 March 2006.

<sup>58</sup> *Mann v Carnell*, [102] (McHugh J).

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At issue in *Mann v Carnell* was whether the disclosure of privileged material between members of the legislature would constitute waiver of the privilege otherwise attaching to the material.

The decision in *Mann v Carnell* placed greater emphasis on the other element which had been identified in *Wigmore*, being the element of consistency. The joint majority decision of the High Court noted that disputes as to waiver usually involved a decision as to whether particular conduct was inconsistent with the maintenance of confidentiality, and if so then waiver would be imputed by operation of law.<sup>59</sup> Conduct inconsistent with maintaining confidentiality would constitute an implied waiver of privilege regardless of the subjective intention of the party, or even if the party had not turned their mind to the question of waiver.<sup>60</sup>

The concept of 'fairness' was relegated to a secondary role of informing the decision as to consistency, rather than being the determining factor in its own right. As expressed by the Court:

What brings about the waiver is the inconsistency, which the courts, where necessary informed by considerations of fairness, perceive, between the conduct of the client and maintenance of the confidentiality; not some overriding principle of fairness operating at large.<sup>61</sup>

Depending on the circumstances, a consideration of fairness may be a relevant factor in determining whether there had been inconsistency,<sup>62</sup> but fairness alone was not the criterion on which the issue would turn.

In the same case, McHugh J suggested that the fairness test of waiver is not a test of general application,<sup>63</sup> as the fairness test of waiver is not supported by the rationales of legal professional privilege.<sup>64</sup>

While earlier cases had looked to whether a claim for privilege was fair in the face of the claimant's conduct, the test had now become whether conduct was consistent with maintaining a claim for privilege. Considerations of fairness would be part of this decision, but the change to a consistency of conduct test marked a change in focus and emphasis by the court.

A consistency test would initially appear to be a more objective test and readily determinable test. The inconsistency test places the focus on the activities of the

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<sup>59</sup> *Mann v Carnell*, [29].

<sup>60</sup> *Ibid.*

<sup>61</sup> *Ibid.*

<sup>62</sup> *Mann v Carnell*, [34].

<sup>63</sup> *Mann v Carnell*, [108].

<sup>64</sup> *Mann v Carnell*, [110].

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claimant in terms of identifiable conduct, and it would be expected that this may be more readily apparent and identifiable than a balancing of fairness, which essentially is looking to the potential alternative outcomes rather than the activities undertaken.

In *Bennett v Aust Customs Service*,<sup>65</sup> Tamberlin J noted that a determination as to whether conduct or circumstances suggest an imputed waiver involves questions of fact and degree.<sup>66</sup> All of the judges<sup>67</sup> were prepared to find in this case that disclosure and use of the conclusion of advice would be inconsistent with maintaining privilege over the advice, and accordingly there had been an imputed waiver of privilege in relation to the advice.

The second part of this paper outlines the judicial comments in *JMA Accounting* which would appear to confer on the executive the power to determine the issue of privilege in certain circumstances. The discussion draws on the foregoing analysis in considering the impact of the judgment on claims for privilege, and whether a potential outcome may be an implied waiver of privilege in relation to communications which may otherwise have been subject to privilege.

### JUDICIAL COMMENT IN *JMA ACCOUNTING*

The case of *JMA Accounting Pty Ltd and Entrepreneur Services Pty Ltd v Carmody*<sup>68</sup> arose from an ATO 'raid' on two offices of JMA Accounting seeking access to documents and records pursuant to a s 263 notice. Of the several issues arising from the ATO actions in this case<sup>69</sup> this paper is concerned only with the claim for legal professional privilege, and the finding of the court in relation to these claims and the manner in which they should have been dealt with.

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<sup>65</sup> [2004] FCAFC 237.

<sup>66</sup> *Bennett*, [12].

<sup>67</sup> Tamberlin, Emmett and Gyles JJ.

<sup>68</sup> [2004] FCA 896; [2004] FCAFC 274.

<sup>69</sup> This case involved a 'seize and control' operation by the ATO. While outside the scope of this paper, there were a number of disturbing elements in the ATO actions whereby employees were denied access to records and so could not perform their tasks, and were locked out of their building. Apart from such action not being contemplated in the Taxpayers Charter, it may be seen as surprising, if not somewhat concerning, that the ATO could form the view that the powers for 'full and free' access to buildings and documents allowed exclusive access and denial to others; let alone that the access powers permitted a potential breach of other laws. The court took a dim view of the ATO actions, with the Full Federal Court noting (at 367) that 'Whatever the outer limits of the power conferred by s 263 may be, the section did not permit the taskforce to take control of JMA's offices and deny its staff access to the computer records.' Further (at 367), 'The respondents are indeed fortunate that they did not face claims in trespass or abuse of power'.

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In the course of the ATO raids, officers took and copied documents to which a claim of legal professional privilege may have attached. Two copies were made, with one being given to JMA and the other to the Australian Government Solicitor, with an undertaking that the information would not be accessed for 14 days to allow for the making of claims for professional privilege in relation to these documents.

At first instance in the Federal Court, Dowsett J concluded that in the circumstances 'it would have been appropriate to examine virtually all of the documents found in the offices, at least in a cursory way, and *subject to any claim to legal professional privilege*.'<sup>70</sup> His Honour thus affirmed that the access powers in s 263, as wide as they may be, remain subject to the limitation of professional privilege, and that documents which are subject to a claim for professional privilege would be excluded from examination by ATO officers.

On appeal, the Full Federal Court<sup>71</sup> held that the 'power of search and seizure'<sup>72</sup> is very wide but not unlimited, and that s 263 does not oust professional privilege and authorise the Commissioner to read or copy documents which are subject to legal professional privilege.<sup>73</sup> However, as noted by their Honours, a serious deficiency in the provision is that there is no procedure to establish whether a document is privileged, and cases have held that if privileged material is read, the privilege may be lost.<sup>74</sup> Where a claim for legal professional privilege is made in relation to a communication, then the resolution of that claim must be a matter for the judiciary.

To overcome this serious deficiency of a lack of legislative procedure for determining a privilege claim, the Court explained that the courts have devised a mechanism to ensure that privilege is not abrogated by executive action without the consent of the claimant to the privilege. Effectively, courts have required that the executive officers allow an adequate, or practical and realistic opportunity, to claim privilege, and if this was not provided then the right of access would be invalidated.<sup>75</sup>

Their Honours explained that this condition was based on the underlying purpose for professional privilege, which was to keep secret the communication between a

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<sup>70</sup> 56 ATR 327, 343 (emphasis added).

<sup>71</sup> Spender, Madgwick, and Finkelstein JJ.

<sup>72</sup> The FFC description of the s 263 power as a power of 'search and seizure' may appear difficult to reconcile with the wording of the section itself, which provides for full and free access to buildings and documents, and requires the occupier to provide reasonable facilities and assistance. Neither s 263 nor s 264 refers to either 'search' or 'seizure'.

<sup>73</sup> *JMA Accounting v Carmody* (2004) 57 ATR 365, 368.

<sup>74</sup> *JMA Accounting*, 368.

<sup>75</sup> *JMA Accounting*, 368-9.

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lawyer and client, and 'where the communication is written, it is to prevent the document containing the communication from being read'.<sup>76</sup>

Having carefully explained that the role of resolving a claim for privilege lay exclusively with the courts, and that the purpose of professional privilege was to prevent privileged documents being read by the executive, their Honours then rather surprisingly concluded that:

there will be circumstances in which it will be proper for the officer exercising the s 263 power to look at a privileged document, including a document for which privilege is claimed, for the purpose of determining whether it might be covered by the privilege. The document should not be looked at closely; merely enough to enable the officer to decide whether the document may be copied ... The circumstances in which an officer will be entitled to undertake a bona fide examination of a document for this limited purpose will include cases where no one is present to claim the privilege and when there is a blanket claim for privilege and it is reasonably apparent that the claim is not sustainable.<sup>77</sup>

The suggested authority for making this finding was provided as being the reference by Brooking J in *Allitt v Sullivan* to a 'lawful violation' of privilege.

The concerns with this finding of the court are addressed in relation to two issues. The first concern relates to whether the judicial comments of Brooking J are applicable in the case of *JMA Accounting*, or whether the circumstances of the cases may be distinguished to the extent that the judicial comments may not apply. The second concern relates to the question of the executive, as a party to any potential litigation, acting in judgement on a professional privilege issue.

### **Authority from *Allitt v Sullivan***

The case of *Allitt v Sullivan* concerned the validity of a search warrant issued pursuant to s 465 of the *Victorian Crimes Act*. At issue was whether the failure of the search warrant to specifically state that it did not apply to documents subject to professional privilege provided sufficient grounds to invalidate the warrant. Murphy J noted the significance of the issue given the not uncommon use of the relevant section to attempt to obtain incriminating material which would support inferences that the client suspected had engaged in criminal activities, when such material had been deposited with legal advisers.<sup>78</sup>

The difference in circumstances between *Allitt* and *JMA Accounting* is by itself sufficient to distinguish the cases. The search in *Allitt* was based on a search warrant,

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<sup>76</sup> *JMA Accounting*, 369-70.

<sup>77</sup> *JMA Accounting*, 370.

<sup>78</sup> *Allitt v Sullivan*, 4.



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and concerned a criminal investigation. By contrast, the Commissioner's actions in *JMA Accounting* constituted administrative activities, and the statutory access powers under which the Commissioner operated, albeit broad, fall far short of the powers provided by a search warrant.

The access powers are provided to allow the Commissioner to ensure compliance by taxpayers operating under a self assessment regime, and the use of the access powers carries no implication that the taxpayer subject to review has committed any breach of the taxation provisions. There is nothing to suggest the use of the powers is directed to obtaining incriminating evidence, as would be the case with a search warrant. The difference in power is evident from the requirements for the use of the power, where the statutory access power is provided to the Commissioner and any official delegate, while the power provided by a search warrant must be specifically sought and obtained on each occasion.

In the joint judgment in *JMA Accounting*, their Honours refer to the statutory access powers available to the executive in terms of being 'the power of search and seizure',<sup>79</sup> which, with respect, must be seen as an overstatement of the power available to the Commissioner. While the power under a search warrant may provide the power of search and seizure, the statutory access power available to the Commissioner allows full and free access to documents, and it is suggested that this power falls far short of a power of search and seizure.

In *JMA Accounting*, their Honours suggest that there would be circumstances under which an executive officer could look at a potentially privileged document 'for the purpose of determining whether it might be covered by the privilege.'<sup>80</sup> Their Honours base this proposition on the reference by Brooking J in *Allitt* to a 'lawful violation' of the privilege. However it may again be suggested, with respect, that this proposition does not necessarily reflect the judicial comments of Brooking J.

The 'lawful violation' of the privilege to which Brooking J referred related to an identification of the document for the purposes of determining whether the document was covered by the search warrant. Such identification could only occur in the absence of identification by the party having possession. A document, once identified as being subject to the warrant, could be seized and taken before a justice.

If a document were subject to a claim for professional privilege, there was no suggestion that the officer executing the warrant could look at the document to determine whether privilege would apply. Rather, the officer was charged with taking the document before a justice who would determine the privilege question,

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<sup>79</sup> *JMA Accounting*, 368.

<sup>80</sup> *JMA Accounting*, 370.

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and if finding the document subject to privilege, the document would be returned to the person from whom it was seized.<sup>81</sup> The document could be taken to a justice, since the mere delivery of a privileged document to a third party would not offend against the policy of the law.

It would appear that even in allowing for identification of a document Brooking J had reservations, in that there was a danger that the 'mere inspection of documents for the purpose of identification will trespass upon the relationship of solicitor and client' and that there was also a practical danger that the officer executing the warrant would act wrongfully by looking at the document other than for the sole purpose of identification.<sup>82</sup> However his Honour was prepared to accept that police would act lawfully in the execution of a warrant.

### *Role of executive in professional privilege*

The judicial comments in JMA Accounting allowing for ATO officers to adjudicate on the privileged status of a communication may have the appearance of abdicating the judicial function of determining a claim for privilege to the executive, and allowing the ATO officers, who are a party to the proceedings, to also act in a simultaneous role of 'independent umpire', which at the very least would appear to create a potential conflict of interest. One issue arising from this approach, and discussed below, is whether it would be appropriate for ATO officers to sit in 'judgment' on the determination of a claim for professional privilege, and whether there are circumstances which may warrant such an outcome. A further issue, also discussed later, is whether allowing an ATO officer to read a document, no matter how quickly it may be scanned, may amount to a waiver of professional privilege, even if the document is read at the direction or behest of a court.

### *Determining privilege*

As noted earlier, legal professional privilege operates in the interests of justice and the greater public interest, acting to protect individual freedoms against the leviathan state by encouraging individuals to consult legal advisors. The judiciary have considered professional privilege to be of such significance, and entrenched to such an extent, that it should not be 'abolished by the flourish of the judicial pen',<sup>83</sup> but rather may only be abrogated by express legislative words. As noted by Deane J:

[i]t is to be presumed that if the Parliament intended to authorize the impairment or destruction of that confidentiality by administrative action it

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<sup>81</sup> *Allitt v Sullivan*, 55-6.

<sup>82</sup> *Allitt v Sullivan*, 60.

<sup>83</sup> *O'Reilly v Commr of State Bank of Victoria* (1982-3) 153 CLR 1, 26 (Mason J).

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would frame the relevant statutory mandate in express and unambiguous terms.<sup>84</sup>

As noted above, the determination of a claim for professional privilege in relation to a communication has always been a matter for the judiciary. The reason for the requirement for adjudication by the judiciary is that a claim for privilege involves a legal dispute, and is not an administrative issue which can be determined at an executive level. As noted by Brennan CJ in *Propend*:

In determining the claim for privilege, the court is not reviewing judicially an executive action but is determining a distinct controversy between the person who seeks to inspect the seized document and the person who seeks to maintain its immunity from inspection on the ground of legal professional privilege. To determine that controversy, the court must act upon admissible evidence ....<sup>85</sup>

Given the significance attaching to privilege, and the requirement for an independent determination of any claim for privilege, it may appear surprising on a number of levels that the Full Federal Court in *JMA Accounting* would be prepared to not only condone but to endorse ATO officers to be charged with the responsibility of resolving a privilege claim.

At the base level, the ATO is an interested party in the determination of a privilege claim, being one of the parties to the dispute, which as recognised by Brennan CJ, is a real legal dispute, the resolution of which is dependent on the evidence admitted. It may appear anomalous that a party to a dispute would be charged with the responsibility of determining the outcome of that dispute, regardless of the circumstances surrounding the particular claim for privilege.

The decision in any legal dispute must rest on an independent judgment, and it can hardly be accepted that an interested and involved party, even with the best will in the world, could be expected to discharge the responsibility for real, let alone perceived, independence. It would be expected that there may be a strong temptation for executive staff to be more prone to find against the existence of privilege, especially given that the access power would often be exercised in circumstances where the ATO may be seeking to 'build a case' against the taxpayer. The ATO officers would be cognisant of the fact that any privileged document may act to weaken the case against the taxpayer, creating a pressure to deny any claim for privilege.

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<sup>84</sup> *Baker v Campbell* (1983) 153 CLR 52, 116-7.

<sup>85</sup> *Propend Finance*, 513-4.

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Even if a later challenge to the ATO decision was upheld, the question arises as to the integrity of the document, and whether the privileged status may have been impugned or compromised, as discussed later.

A further reason for the requirement for judicial resolution of privilege claims devolves from the doctrine of the separation of powers, whereby the functions of the legislature, executive and judiciary provide the checks and balances required in a democratic system. As noted in the earlier comments from Deane J, privilege acts to protect the individual against the leviathan state, and the absence of privilege would expose individuals to prejudice and damage from compulsory disclosure to administrative officers.

With the Australian reality of a merged legislature/executive, the independence of the judiciary becomes even more critical. Allowing for the executive to both pursue actions under an access notice against a taxpayer, and sit in judgment on whether a communication was subject to professional privilege, would deny the taxpayer the protection intended to be afforded by the separation of powers, and expose them to the damage and prejudice warned of by Deane J.

A further concern must arise from the ability of ATO officers to adequately discharge the responsibility of resolving a professional privilege dispute. This concern must exist on a number of levels. As the privilege dispute is a real legal dispute, there must be concern as to whether the training and experience of ATO officers would elevate their judgment to the level of the judiciary, who currently resolve such matters. It would generally be expected that the execution of an access notice would not involve staff at the highest levels of the executive, and with the privilege issue being determined on the premises, the expectation would be that the decisions would be made by less senior staff who would have a lesser degree of knowledge and experience.

An additional concern would be that when the ATO had quickly but not closely read a document, the privilege vesting in the information in the document may have been compromised in that that communication was now known to the ATO. This may be the case, even if the privilege claim was upheld. It may be unrealistic to expect an ATO officer to 'segregate' any information gleaned from a quick read of a document from other information which may already be known, and forget this new information when it was such as to become an integrated part of existing knowledge. Again, even with the best will in the world, individuals cannot be expected to remember the source of particular parts of a combined knowledge, and selectively forget certain components because they had a privileged source.

It is suggested that it is for all of the above reasons that the adjudication as to the privileged status of a communication has been a task reserved for an independent

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judiciary, and it would be suggested that for these reasons there is a strong case for the judiciary remaining as the sole arbiter of this matter. The abdication by the judiciary to the executive of decisions as to privilege attaching to a document must be seen as potentially compromising the independence of the judgment, the quality of the decision made, any legal proceedings which may arise from the decision as to privilege, or any legal disputes arising where the evidence involves documents subject to an executive privilege decision.

### *Potential for implied waiver?*

Their Honours in the joint decision would appear to implicitly recognise that there may be a danger in assigning the privilege decision to the executive, when they explain that 'documents ... would not be closely read, although they might be glanced at to determine their relevance. This way the privilege would not be lost.'<sup>86</sup> However there is no explanation as to what degree of a 'glance' is permitted to ascertain the relevance, and at what point a glance to determine relevance becomes a 'close read' of contents. On this basis it may be difficult to see just how the privilege is maintained when the privilege may have been compromised.

The issue explored in this context is whether the 'glancing' at an otherwise privileged document by ATO officers, even if the glancing is done with the sanction and imprimatur of the court, may be sufficient to constitute an express or implied waiver of the privilege otherwise attaching to the document. While it may be argued that a distinction may be drawn between glancing at a document to determine the nature of the document (eg, a bank statement) and viewing the contents of the document, the distinction may not be clear in all cases, making the argument difficult to support in marginal cases.

As noted above, an express waiver is evidenced by a voluntary and intentional disclosure of the contents of an otherwise privileged communication, where the disclosure is made generally and not for a limited or specific purpose. Where a document has been disclosed at the behest of the court for perusal by ATO officers, the disclosure may be intentional but could not be described as voluntary. The disclosure would only be made on the basis that the court had decreed such a disclosure for the limited purpose of the ATO officers determining whether in their view the document would attract professional privilege.

On this basis it may be that the perusal of documents by ATO officers, when the documents had only been made available for this limited purpose because of the court requirement, would not be sufficient to constitute an express waiver of

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<sup>86</sup> *JMA Accounting*, 371.

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privilege in relation to these documents. This would be the case where it had been made clear that a claim of privilege remained extant in relation to the documents, and the documents were only being made available, because of the court requirement, for the limited purpose of ATO perusal to determine their status. In any case the ATO determination of the privilege status of a document cannot be final, as the determination of privilege is a matter which must finally rest with the judiciary.

However, a non-voluntary disclosure of otherwise privileged material, regardless of the intention of the party, raises the issue of whether there has been an implied waiver of the privilege which may have otherwise attached to the document. An implied waiver would be established if the tests for implied waiver, as discussed earlier, had been satisfied.

A somewhat analogous situation had arisen in *Maurice*, where a Claim Book had been lodged in compliance with a Practice Direction, the broad question then arising as to whether this amounted to an implied waiver of supporting documentation. In their joint judgment, Mason and Brennan JJ identified the difficulty in finding an implied waiver when material had been made available in compliance with a legal requirement, explaining that:

it would be unfair to impute to the respondents a waiver of the privilege attaching to source materials merely because the respondents, in complying with Practice Directions without clear procedures to follow, provided information tracing the basis of their claim.<sup>87</sup>

In a similar vein, Deane J considered that:

there are, however, no considerations of fairness which require that compliance by a party with a procedural requirement that he prepare and make available a document setting forth the case which he proposes to make before a court or quasi-judicial tribunal should be treated as a waiver of his right to claim legal professional privilege in respect of all the material upon which he has relied in the preparation of that document.<sup>88</sup>

His Honour went so far as to suggest that:

it would be an affront to ordinary notions of fairness to hold that the effect of his compliance with that procedural requirement was that he has waived his legal professional privilege in relation to such material.<sup>89</sup>

These judgments suggest that unfairness of the outcome would mean that compliance with a legal requirement would not be sufficient of itself to constitute an

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<sup>87</sup> *Maurice*, 489.

<sup>88</sup> *Maurice*, 493.

<sup>89</sup> *Ibid.*

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implied waiver of professional privilege. However the fairness test for implied waiver as applied in *Maurice* has since given way to an expanded consistency test in *Mann v Carnell*, whereby fairness became one of the factors in considering consistency rather than the decisive criterion itself. This raises the question as to whether disclosure of otherwise privileged information to ATO officers is inconsistent with the maintenance of privilege.

In *Mann v Carnell*, the majority judgment had regard to the English Court of Appeal decisions in *British Coal Corporation v Dennis Rye (No 2)*<sup>90</sup> and *Goldman v Hesper*,<sup>91</sup> which found that ‘disclosure to a third party for a limited and specific purpose did not lead to a loss of the privilege as against a person opposed in litigation.’<sup>92</sup> While this may appear to provide some comfort in that documents made available to the ATO for a limited purpose may retain any professional privilege attaching to them, there is a significant difference in that the ATO can hardly be seen as a third party, and in any litigation which may arise the ATO would be the opposing party. Any comfort provided from this finding would not appear to reach as far as preserving privilege when documents were made available to the opposing party in the form of the ATO, even when only provided for a ‘glance’ and for a limited purpose.

In applying the inconsistent conduct test, the majority explained that:

Disclosure by a client of confidential legal advice received by the client, which may be for the purpose of explaining or justifying the client’s actions, *or for some other purpose*, will waive privilege if such disclosure is inconsistent with the confidentiality which the privilege serves to protect.<sup>93</sup>

As noted above, their Honours added that considerations of fairness may be relevant in determining such consistency.

This would suggest that, regardless of the purpose for which the otherwise privileged material is made available, actions inconsistent with preserving the privilege would imply a waiver of the privilege. There could be little doubt that disclosure of otherwise privileged material to the ATO, which is an interested party and a potential opposed litigant, would be seen as inconsistent with maintaining the privilege in the material. The emphasised phrase above would suggest that the purpose for making the material available would be irrelevant as the wording leaves open the purposes for which material may be made available. This would appear to be contrary to *Maurice*, where the Court had found that it would be unfair to find implied waiver of privilege where the disclosure was in compliance with a legal

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<sup>90</sup> [1988] 3 All ER 816; considered in *Mann v Carnell*, [32].

<sup>91</sup> [1988] All ER 97; considered in *Mann v Carnell*, [32].

<sup>92</sup> *Mann v Carnell*, [32].

<sup>93</sup> *Mann v Carnell*, [34] (emphasis added).

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requirement. It may be that fairness, as a factor to consider in consistency, may argue for maintenance of privilege, but it would appear that compliance with a legal requirement would not alone prevent the finding that privilege had been impliedly waived.

If inconsistency is found between conduct and maintaining confidentiality, and on its face making material available to the ATO may appear to qualify as inconsistent with maintaining confidentiality of the material, then the law may find an imputed waiver. This test is an objective test, and there may be an imputed waiver found regardless of whether it reflected the subjective intention of the party who has lost the privilege.<sup>94</sup>

The implied waiver test as enunciated in *Mann v Carnell* may thus appear to raise real concerns that, by following a court requirement and making otherwise potentially privileged material available to officers of the executive, the taxpayer would be found to have acted inconsistently with maintaining confidentiality, and thus have impliedly waived their professional privilege in the material.

This would be so regardless of the reason for making the material available, as the judgement appears to suggest that the purpose for the inconsistent conduct is not relevant, the determining factor being the inconsistency with maintaining confidentiality. If this is the case, then a waiver of privilege could potentially be implied, even though disclosure was at the behest of the court. As noted in *Maurice*, this would appear a particularly unfair outcome, but while fairness is a factor for consideration, it would not be determinative of the issue.

### CONCLUDING REMARKS

Legal professional privilege has a long and established tradition in common law, the rationale underlying the privilege being to serve the interests of justice, and in this way to serve the greater public interest. While there is a continuing tension between the confidentiality provided by professional privilege and the requirement for full disclosure, the maintenance of privilege has been seen as essential to protect the rights of individuals in the power imbalance that exists with the state.

This article has been concerned to examine whether the status of privilege in tax investigations has potentially been adversely impacted following the judicial comments in *JMA Accounting* that there are circumstances where potentially privileged material should be made available to ATO officers who would determine the issue of privilege. It is suggested that there must be some doubt as to whether the authority of *Allitt v Sullivan* on which the comments rely is an appropriate authority,

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<sup>94</sup> *Mann v Carnell*, [29].



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or whether the cases are sufficiently distinguished as to suggest different principles should apply.

If it is the case that responsibility would fall on ATO officers to determine whether professional privilege vested in the material, it is suggested that this may be seen as an anomalous outcome in that the judiciary may appear to be abdicating to the executive the judicial role in adjudicating on claims of professional privilege. If the judicial comments are seen as an abrogation of the judicial role in determining privilege, this must cause concern as to the continued ability for professional privilege to fulfill the role envisaged by Deane J in providing 'some protection of the citizen - particularly the weak, the unintelligent and the ill-informed citizen - against the leviathan of the modern state.'<sup>95</sup>

An additional concern is that by making available to ATO officers material to which professional privilege may have otherwise attached, taxpayers may be seen to have impliedly waived their right to the privilege, as the conduct would be inconsistent with maintaining professional privilege. If this is the case then this may appear to be a particularly harsh result, given that the only reason such material would be made available to the ATO for perusal would be as a result of the requirement from the court that the executive was capable and competent to determine the question of professional privilege.

### Postscript:

After this paper had been submitted the Australian Law Reform Commission (ALRC) was commissioned to consider the investigatory functions of Commonwealth bodies which have coercive information gathering powers, one such body being the Australian Taxation Office. In particular the ALRC is to consider the modification or clarification of legal professional privilege in relation to these investigatory powers. The ALRC is due to release the final report in December 2007.

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<sup>95</sup> *Baker v Campbell*, 120 (Deane J).