ATTA 2015 Abstract Submission

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Title: Scheme Penalties and Purpose – It's time for clarification

Abstract

Schedule 1 to the *Tax Administration Act 1953* (Cth) contains a number of mechanisms whereby penalties may apply to taxpayers and some other entities in relation to tax-related matters. The focus of this paper is the penalty system that operates in relation to arrangements designed to achieve tax benefits, specifically the administrative penalty under s 284-145 in relation to taxpayers and schemes (herein referred to as the taxpayer scheme penalty) and the civil penalty under s 290-50 in relation to the promotion of tax exploitation schemes, where the promoter rather than the taxpayer may be liable (the promoter scheme penalty). In the recent decision *Commissioner of Taxation v Ludekens* [2013] FCAFC 100, the Full Federal Court considered for the first time the application of the promoter scheme penalty but the decision not only leaves unanswered a number of questions in relation to the operation of that penalty but also highlights persisting uncertainties in relation to the taxpayer scheme penalty. This paper briefly considers the penalty framework for tax-related conduct and then focuses on one issue: the operation of the purpose test under the two scheme penalties.

Pursuant to the taxpayer administrative penalties in Division 284, which includes the scheme penalty, the Commissioner must make an assessment of the amount of any such penalty. Amongst other matters, the operation of s 284-145 requires that an entity entered into or carried out the scheme with the sole or dominant purpose of getting the scheme benefit. What has remained unclear since this provision came into effect in 2000 is whether this purpose test is an objective one or a subjective one, that is, does it look to the relevant entity's actual purpose in entering into the scheme? Although the general anti-avoidance provisions for income and other taxes employ similarly worded purpose tests, the scheme penalties can have application to schemes that have not necessarily triggered these general anti-avoidance rules. This issue has resurfaced after the *Ludekens* case because the promoter scheme penalty, which was explicitly designed to mirror the taxpayer scheme penalty, also includes a purpose test by way of the meaning given to the term 'tax exploitation scheme' in s 290-65 and the application of the penalty in the case did not require a finding that either Part IVA or the GST anti-avoidance rule operated. The Federal Court was not asked to consider the construction of the purpose test but the approach undertaken in the case suggests a presumption that the purpose test in this context is a subjective test. This paper explores the history behind these penalty provisions and judicial consideration of these issues in an effort to determine a preferred construction of both the taxpayer scheme penalty purpose test and the purpose test for the promoter scheme penalty. It is submitted that if these penalty provisions are to have their desired deterrent effect, taxpayers and promoters require increased certainty as to their application and the operation of the purpose tests may need to be clarified by legislative amendment.