Advance rulings procedures

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Tax liability is so important that it ought to be possible to determine in advance what this liability will be. New Zealand currently has a form of advance rulings procedure but because those rulings are not binding taxpayers cannot with certainty rely upon them. In this paper John Prebble argues that a formal, binding advance ruling procedure for income tax questions should be instituted in New Zealand and discusses the operation and implementation of such a procedure.

I. INTRODUCTION

For most businesses taxation is significant. For some it is the single greatest expense. The attractiveness, even the viability, of some transactions and business operations depends on how they will be taxed. It is thus fortunate that generally speaking the incidence of taxation can be predicted accurately. By and large our tax system is reasonably certain in its effects. But in some cases there is no certainty. Doubts as to the tax effects of one's proposals can mean that to put them in train is to embark on a hazardous journey across a fiscal minefield, guided by maps that are misleading or non-existent.

In most jurisdictions these hazards can be mitigated in some measure. The taxpayer can put his proposals before the revenue authorities and request a ruling on their fiscal implications. However, this procedure is often deficient in one respect or another. For example, rulings can be granted in only limited types of cases; there may be discretion to decline to give a ruling; or rulings may not be binding, with the authorities reserving the right to change their mind.

In the last three or four decades, as tax systems have become steadily more complex and have demanded a growing share of the world's wealth, the shortcomings or complete absence of rulings procedures has attracted increasing comment and criticism. In 1980 the International Fiscal Association at its Paris conference surveyed twenty countries. Of these, only Canada, Portugal, Sweden, the United States of America, and Uruguay had comprehensive advance-rulings procedures in their taxation systems. Argentina, Belgium, Greece, and Hong Kong had no provision. In the United Kingdom rulings were available only in very limited circumstances. Australia, Austria, Colombia, Denmark, France, Germany, Israel, the Netherlands, Norway and Switzerland had provision for rulings varying from limited to relatively comprehensive.

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In some jurisdictions the taxpaying public simply puts up with a less than satisfactory situation. In others people try to find ways around the shortcomings of official procedures. In Belgium and France, for example, it is common for deputies to get some sort of rulings on behalf of their constituents by ministerial questions in Parliament, though the type of case where this procedure can produce a satisfactory result is limited.

From a New Zealand point of view probably the two most instructive models are found in Sweden and Canada. In both countries rulings procedures were instituted after proposals to that effect by commissions of enquiry appointed to report on the tax system. The Swedish procedure was instituted in 1951 and the Canadian in 1970.

II. REASONS FOR RULINGS PROCEDURES

It seems likely that a comprehensive and effective rulings procedure promotes respect for and compliance with fiscal laws. Certainly, an effective rulings procedure will generally promote good relations between the revenue authorities and the taxpayer. This is partly because the taxpayer will be glad to be able to find out the attitude of the revenue to his proposed transactions and partly because a rulings procedure can be used to promote uniformity in the application of tax legislation throughout any particular jurisdiction. Further, the availability of advance rulings should help to minimise controversy and litigation. Taxpayers who have the opportunity of discovering in advance the opinion of the authorities will be less likely to chance their arm and fight out the results later in court.

An advance rulings procedure can also be useful in the enforcement of tax laws. Revenue authorities always face some difficulty in keeping up with the latest practices in commercial and tax planning. Formal requests for rulings on proposed operations constitute one way for the authorities to keep up to date.

The quality of the relationship between taxpayers and the revenue authorities and other factors like those mentioned in the previous two paragraphs are almost impossible to measure but educated common sense suggests that an advance rulings procedure should promote most or all of these desirable features. Of countries with comprehensive advance rulings procedures, Canada, Sweden and the United States of America have been studied for the purposes of this paper. Such empirical evidence as there is from these jurisdictions supports the common sense conclusions advanced above.

III. TAX IN DISPUTE

In New Zealand there are three rather specific considerations that suggest that an advance rulings procedure would be desirable in this country. First, a change was announced in the 1984 budget as regards the procedure in respect of tax in dispute. Hitherto taxpayers have been able to defer the payment of disputed tax. From 1985 deferrals will not be permitted. Disputed tax must be paid, though any refunds allowed as a result of successful objections will carry interest. This change is no doubt reasonable. There are grounds to suspect that numbers of tax objections have been lodged to obtain a deferral of tax rather than because of any particular merit in the argument of the taxpayer. However, one result of the

change is that taxpayers and their professional advisers may be expected to become increasingly restive about delays in the disposal of objections to assessments, thus causing even more work for an already hard-pressed Inland Revenue Department. To the extent that an advance rulings procedure can prevent disputes from arising in the first place it should, in the long run, minimise disputes and litigation.

IV. ANTI-AVOIDANCE LEGISLATION

Secondly, New Zealand has in section 99 of the Income Tax Act 1976 a comprehensive anti-avoidance provision. Where there are anti-avoidance provisions couched in general terms the arguments for an advance rulings procedure are particularly compelling. The reason is that generally-phrased anti-avoidance provisions are often so drafted that their literal words appear to catch transactions that are entirely innocent. For this reason the United Kingdom, which has no comprehensive advance rulings procedure, as a matter of practice provides special review procedures when it enacts general anti-avoidance provisions. An example may be found in section 88 of the Capital Gains Tax Act 1979. Section 88 relates to corporate mergers and reorganisations. As a general rule an exchange of shares to effect an amalgamation is not classed as a disposal for capital gains tax purposes. However, this general rule does not apply unless the "reconstruction or amalgamation in question is effected for bona fide commercial reasons and does not form part of a scheme or arrangement of which the main purpose . . . is avoidance of liability to capital gains tax or corporation tax" (section 87.)

Consequently, United Kingdom companies contemplating a merger will be concerned to know whether the revenue authorities will accept that their proposed actions are "for bona fiide commercial reasons" and not for the avoidance of taxation. Section 88 stipulates that companies in this position may obtain an advance ruling from the revenue authorities. Theer are several similar examples in other parts of the United Kingdom tax legislation.

Section 88 of the United Kingdom Capital Gains Tax Act applies only in respect of corporate reorganisations. In contrast, section 99 of the New Zealand Income Tax Act renders void for income tax purposes any arrangement that has the purpose or effect of tax avoidance. Literally, this provision might even apply if a taxpayer makes a gift to charity in circumstances where the donation will result in a rebate. There are many other cases which may, or may not, be vulnerable to section 99. This is a situation that cries out for a procedure whereby taxpayers can clear their proposals with the Inland Revenue Department in advance.

V. COMMISSIONER'S DISCRETIONS

Thirdly, it is a feature of the New Zealand Income Tax Act that many of its provisions are couched in terms not of clear rules but of discretions conferred upon the Commissioner of Inland Revenue. In "Objecting To Discretionary Determinations by the Commissioner of Inland Revenue", Patricia Reddy identified upwards of 400 separate discretions conferred by the Act upon the Commissioner.[1] Ms Reddy wrote in 1981. Doubtless the total is now a good deal higher.

1 11 V.U.W.L.R. 125.

An important example is found in section 108(1) of the Act. There, it is provided that where depreciation of a capital asset cannot be made good by repair "the Commissioner may, [subject to certain specific rules in the Act] allow such deduction as he thinks just". These few words underpin almost the whole of the depreciation schedules of the New Zealand tax system. Schedules of allowances that will be approved are published by the Commissioner and may be relied upon by the taxpayer. A formal procedure affording an opportunity to obtain advance rulings on depreciation questions for which the schedules do not adequately cater would have clear benefits. Likewise, binding rulings should be available in respect of other matters that are subject to administrative discretion.

VI. EXAMPLES OF CASES NEEDING RULINGS

Shortly stated, from the point of view of the taxpayer the chief merit of an advance rulings procedure is that he is able to resolve doubts about the fiscal implications of his proposed transactions. It is helpful to consider several examples of cases where taxpayers have a particular need to determine their potential liabilities before embarking on a proposed course of action.

First, take the taxpayer who proposes to sub-divide and sell a plot of land. Whether this person can be taxable on the profits from this transaction may depend on a number of factors. To take an example, it may be relevant whether he or she has engaged in a regular pattern of such transactions in the past. The taxpayer could go ahead and sell the land, risking an assessment and later argue the matter in court. But an advance ruling would permit him or her to know for certain whether the proposed sale will be assessed for tax. A second example is the case of a New Zealand employer who wants to tender for a contract in another country. If the tender is successful the employer will assign employees to the other country for periods of years, paying them from New Zealand. Are the salaries of these employees taxable in New Zealand? Must the employer account to the Inland Revenue Department for PAYE deductions? The answers to these questions will often have a crucial bearing on the competitiveness of the tender. It is their net remuneration that matters to the employees. Thus, if tax is not deductible the employer will be able to pay lower salaries and submit a more competitive price.

The third example comes from the field of conveyancing. Before the enactment of the Unit Titles Act 1972 it was difficult for people owning flats in blocks of apartments to get title to their own flat. One partial answer to the problem was to incorporate a company to own the apartment block and to issue shares to the dwellers. These shares were identified in such a way that ownership of particular shares entitled the shareholder to occupy a particular flat. This situation was less than satisfactory. Among other things shareholders found it difficult to sell their flats because the shares were often not regarded as good security for a loan. Nowadays the shareholders in many corporately-held apartment blocks want to liquidate the companies and issue to themselves unit titles to replace their shares. But because of certain rules regarding the taxation of companies it is possible that such a transaction would render the shareholders vulnerable to tax on the increase in value of their respective apartments between the date of acquisition of the apartments by the company and the date of liquidation. The position is not

certain but companies have been unwilling to take the risk of liquidation and the consequent imposition of taxation. Apart from anything else the tax would be chargeable in circumstances where the shareholder tax payers would have no money to pay it. This is the kind of problem that could well be resolved by an advance rulings.

VII. THE CURRENT POSITION IN NEW ZEALAND

The New Zealand Income Tax Act contains the rules whereby tax is calculated. The Act imposes tax and therefore from a strictly jurisprudential point of view it is not possible for the Commissioner of Inland Revenue to give binding rulings on questions of tax liability. If the Commissioner gives a ruling and later decides that he was wrong he is obliged to make his assessments of the taxpayer according to the rules as he now understands them. If there is a dispute it is for the courts to decide the true effect of the law. The decision of the court cannot be governed by a ruling that may have been made earlier by the Commissioner. In effect that ruling is no more than an expression of opinion.

Despite his inability to give binding rulings the Commissioner has always been willing to express his view on proposals put to him by taxpayers or their advisers. The Commissioner is naturally reluctant to change his mind about such rulings, but this does happen from time to time.

The practice of the Commissioner was set out in his *Public Information Bulletin* No. 117, published in June 1982. Taxpayers may apply to their district offices for rulings on transactions that they propose to undertake. Generally speaking the ruling is made within the district office, acting under authority delegated from the Commissioner. Difficult cases are referred to regional offices or to the head office.

Salient features of the system include the following:

— The Inland Revenue Department does not consider itself obliged to issue rulings, though it endeavours to do so. One type of case where the Department may not give a ruling is where there is some doubt about the applicable law.

— There is no appeal from unfavourable rulings. The taxpayer may carry on regardless if he wishes and challenge the view of the department when a return has been furnished and an assessment issued.

— The department emphasises that its rulings are expressions of opinion and are not binding. Of course, the ruling may be revoked if it is subsequently discovered that the facts are not as stateed by the taxpayer. However, changes in the law or its interpretation will also cause the department to correct its ruling.

— Application for a ruling is by letter setting out the facts of the case together with drafts of relevant documents.

— The department will not give rulings on proposals which involve or could involve tax avoidance, hypothetical situations, a series of alternatives to the same transaction, or proposals where the names of the taxpayers are not disclosed.

There is a view among lawyers and accountants practising in the taxation field that the demand for rulings is decreasing. A somewhat unscientific survey was taken at a meeting of the New Zealand branch of the International Fiscal Association in Wellington on 13 December 1984. There were twenty taxation practitioners at that meeting. From all those twenty practitioners there had emanated only five applications for rulings in the whole of 1984. In the opinion of those present this was many fewer than would have been the case four or five years ago.

This decline in the use of the current rulings procedure is probably attributable to several factors. First, the expertise of New Zealand tax advisers has improved marketdly over the last five years or so. Consequently tax advisers are more willing to give their advice without reference to the Inland Revenue Department. Secondly, there may have been a misapprehension among less expert members of the professions that rulings were binding. If so, this impression was dispelled by the 1982 Public Information Bulletin. Thirdly, it is believed in some quarters that the Inland Revenue Department is these days more ready to reverse rulings that it has given than it was in the past. Accordingly a ruling is not as worthwhile as it was. A fourth reason is sometimes suggested. This is that tax planners are nowadays less willing to disclose their proposals to the Inland Revenue Department than they used to be. It is unlikely that this view is correct. Tax planners have always had to decide between disclosing their hand to the department in the hope of receiving a favourable ruling and keeping their plans confidential.

VIII. BINDING EFFECT OF RULINGS

In the view of sophisticated taxpayers and of tax practitioners probably the major shortcoming of the New Zealand advance rulings system is that rulings are not binding. Of course, it must be accepted that any rulings system must provide for revocation or modification if it is discovered that there was a material omission or misrepresentation in the application by the taxpayer. Further, if there is a retrospective statutory change it would seem fair that a taxpayer should not be able to rely on a ruling. Otherwise he would be in a significantly more favourable position than other taxpayers. Thus in Sweden, for example, where advance rulings are in other respects binding, there is an exception for retrospective legislation. However, contrary court decisions, much less reinterpretations by the revenue authorities, do not lead to the revocation of a ruling.

IX. CONTINUOUS COURSES OF ACTION

Rulings in respect of courses of action that are to be continued or repeated for some time raise more difficult questions than rulings on single transactions. Justice appears to require that modifications of rulings should not be retroactive. But is it fair to the general body of taxpayers for someone to take advantage of an erroneous ruling for a number of years? In the final analysis, the answer is probably yes. One may take up again one of the examples suggested earlier, the New Zealand employer who tenders for a foreign contract. If the contract is to last for, say, five years it would seem only reasonable that the taxpayer should be able to rely on a ruling in respect of the assessability of the remuneration of his staff throughout that period. Arguably, if a case is sufficiently serious to warrant the revocation of a ruling obtained after full and faithful disclosure by

the taxpayer then this should be done by retroactive legislation, or possibly by appropriate court proceedings but not by administrative action.

The problem of changes in the interpretation of the law can to some extent be mitigated by providing for time limits within rulings themselves. For example, a transaction may be ruled non-assessable if it is carried out within, say, twelve months. The tax implications of a certain course of action may be ruled upon, the ruling to be effective for, say, four years. The transactions and business operations of taxpayers are so various that there would be no merit in fixing specific time limits to be applicable for all rulings. But a practice of making rulings subject to appropriate limits decided on a case-by-case basis would have obvious advantages.

X. BINDING EFFECT ON THE TAXPAYER

It is sometimes suggested that if advance rulings that are favourable to the taxpayer are to be binding on the revenue authorities then rulings that are unfavourable to him should be binding on the taxpayer. This suggestion comes from a misconception of the role of a rulings procedure. As far as is known, no jurisdiction that provides for advance rulings makes unfavourable rulings binding on the taxpayer. The justification for this approach differs depending upon whether rulings are given by the revenue authority itself or by an independent authority.

Where rulings are made by the revenue authorities, as is the case in most jurisdictions, one starts from the position that there are two persons: the taxpayer, who argues that his proposed transaction is not taxable (or taxable at a low rate); and the revenue authorities, who represent a conflicting interest, though not necessarily a conflicting point of view. If the revenue agrees with the taxpayer it is simply saying that its view of the law is the same as his. But the revenue authorities will be bound to this view because the taxpayer proposes to act upon it. On the other hand, if the revenue authorities disagree with the taxpayer they are doing no more that saying that their opinion is different from that of the taxpayer. It follows that the taxpayer should be permitted to carry out the proposed transaction if he or she wishes, and to object in court to the assessment of the revenue authorities in due course.

If the rulings authority is independent there is perhaps a stronger argument for saying that if the revenue authorities are bound so also should be the taxpayer. To allow the taxpayer to disregard the ruling of the rulings authority and to have a second argument before the tax court appears to give him two chances whereas the revenue authorities have only one chance in cases where the ruling is favourable to the taxpayer. But even here a useful analogy can be drawn with the legal doctrine of estoppel. Broadly speaking, this doctrine states that where someone changes his position on the basis of the representation of another he should be able to rely upon that representation. In cases involving advance rulings it is the taxpayer who changes his or her position, by going ahead with proposals that have been ruled upon. The position of the revenue authorities is not changed. Accordingly, it is not unfair that the revenue authorities should be bound by rulings adverse to their interests but that the taxpayer should be free to disregard them should he or she so decide.

XI. WHAT MAY BE RULED UPON

The rules of most rulings procedures provide that there are some types of cases in respect of which rulings will not be given. Certainly, there are some cases that reasonably should be excluded from a rulings process. In Sweden it is required that the matter in question should be of marked importance to the taxpayer. In practice this stipulation is applied leniently and few requests for rulings are denied for unimportance. However, it does seem reasonable that there should be at least some significance in the taxpayer's request. The primary purpose of such a rule should be to exclude vexatious or frivolous applications. Secondly, most jurisdictions that lay down detailed rules will not provide advance rulings in cases where the question of law involved is currently before the courts, either in respect of another taxpayer or in respect of the same taxpayer in relation to an earlier year. This seems a reasonable limitation, though one should bear in mind that one of the advantages of a rulings procedure is that it should be more rapid than typical judicial proceedings. It is not reasonable to hold up the transactions of the many while a particular case is waiting to be heard. One possible remedy would be to provide for expedited hearings of cases that are expected to have wide significance.

The essence of revenue rulings is that the rulings authority pronounces upon a set of facts presented by the taxpayer. Accordingly, the Canadian authorities indicate that rulings will not be granted where the issue is primarily a question of fact. This approach is unexceptionable. It would hardly be appropriate for rulings authorities to make determinations of fact on the basis of information supplied only by the taxpayer. The alternative, to add investigating duties to the role of rulings authorities, would be significantly to change their role.

A study of the provisions of advance rulings procedures of different jurisdictions reveals a miscellany of other cases that for one reason or another will not be entertained. Generally speaking there is less obvious merit in these limitations than in those mentioned above.

A. *"Hypothetical" cases*

Most revenue authorities, including those of New Zealand, state that they will not rule on what they call "hypothetical" cases. But what is meant by "hypothetical"? In one sense any proposed transaction is hypothetical in that it is a proposal rather than a fact. On the other hand, if by "hypothetical" one means "unlikely" it should not be difficult in most cases for the taxpayer's advisers so to draft his or her application that the proposal at least looks possible.

The word "hypothetical" has a pejorative air about it. One has the slight feeling that draftsmen of codes of advance rulings procedures say to themselves, "We can't have any hypothetical cases," as if this is an obvious truth, write it down, and go on to the next point. Be that as it may, in the end, one is forced to the conclusion that the exclusion of hypothetical cases probably has little significance, and probably does not do much harm.

B. *Cases not bona fide*

In Canada the revenue authorities will not rule on transactions that are not

clearly bona fide or that are designed primarily to reduce tax. Similarly, the New Zealand Inland Revenue Department declines to rule on proposals which involve or could involve tax avoidance. In New Zealand it is hard to see why there should be no rulings in such cases. If a scheme has the purpose or effect of avoiding taxation it is void for tax purposes by virtue of section 99 of the Income Tax Act. If this is the view of the Commissioner he should rule against the taxpayer, citing section 99 and giving reasons why the scheme is caught by that provision.

C. *Completed transactions*

In some jurisdictions, notably Canada, it is not possible to obtain a ruling in respect of completed transactions. In others, including the United States of America, one can obtain rulings on completed transactions but they are not binding on the revenue. The rationale is that the transaction was not entered into in reliance upon the ruling and it is thus not unfair for the ruling to be modified. This reasoning ignores the fact that a taxpayer may have relied upon such a ruling in entering other transactions. For example, a taxpayer receiving a ruling agreeing that he has suffered a deductible loss may decide in the same year to sell some land in circumstances such that the sale produces assessable income, income that he can set off against the loss. Were it not for the favourable ruling the taxpayer might decide to defer the sale of the land for a year or two until it can be sold without tax consequences. In such circumstances it appears unfair that the ruling should be able to be modified.

D. *Applications containing alternatives*

Most ruling authorities, again including those in New Zealand, will not entertain applications in respect of cases involving several alternatives. One has a similar reaction to this restriction to one's reaction to the exclusion of so-called "hypothetical" cases. The expression "series of alternatives" by itself tends to create an unfavourable impression. One might conclude without much thought, "Of course the taxpayer should not be allowed to burden a rulings authority with a series of alternatives". But this opinion does not stand up to close analylsis. There are numerous cases where it is not at all unreasonable for a taxpayer to submit alternatives in his or her application. Take another of the examples mentioned earlier in this paper: the case of the shareholders who by virtue of their shareholding are entitled to occupy flats in a block owned by their company. If one wants to liquidate such a company there are several ways to do it. For example, the flats could be sold to the occupiers and the price paid out to them as dividends on winding up. Alternatively, the flats could be distributed in specie to the occupiers in return for the cancellation of their shares. There are alternatives within these two broad strategies. It may be that one alternative produces a taxable result but another is non-taxable. The taxpayer should be permitted to place the different alternatives before the ruling authority.

E. *Revenue or capital*

In Canada, the authorities will not rule on the question of whether a particular receipt or expense is revenue or capital. The reason appears to be that ultimately these matters are usually questions of fact. It is relatively difficult for the authority to become apprised of all the relevant facts. The New Zealand Inland

Revenue Department appears not to make a similar reservation in such rulings at it does give. It is suggested that the New Zealand position is to be preferred. One must bear in mind that the onus is on the taxpayer to put all the relevant facts correctly before the authorities. If it later turns out that the application was misleading the ruling may be revoked and the taxpayer has only himself to blame. In practice, the New Zealand Inland Revenue Department appears to be reasonably experienced in ruling on questions of capital and income. For example, in the period up to 31 August 1981 the DIC Ltd. a public company, incurred expenditure of $2,869,750 in strengthening its Wellington department store to comply with local bylaws. The earthquake resistance of the building was markedly improved by the installation of a skeleton of massive steel girders. The Commissioner of Inland Revenue allowed the total sum as a deduction on revenue account, as noted in the 1981 annual report of the company.

F. *Taxpayer's name not disclosed; rulings for trade associations*

Most jurisdictions will not allow advance rulings where the name of the taxpayer is not disclosed. There is perhaps some justice in this rule in general principle. If one of the justifications of a rulings procedure is that the intelligence-gathering of the revenue authorities is enhanced it may be an unreasonable advantage for a taxpayer to be able to obtain a ruling without saying who he is. On the other hand, there seems no reason in principle why trade associations and trade unions should not be able to obtain rulings on behalf of their members. In practice this does occur. For example, New Zealand trade unions often get rulings from the Department of Inland Revenue that, say, expenditure on clothing or equipment will be allowed as a deduction up to a certain level, though these rulings are apparently not regarded as being made pursuant to the procedure laid down in the 1982 circular.

Sweden stipulates that only the taxpayer himself may apply for a ruling. The effect of this rule is avoided by trade associations supporting the application of individual members in order to create a precedent. There seems no particular reason to prevent trade associations, trade unions, and similar organisations from obtaining rulings that will be applicable to their individual members.

The New Zealand Society of Accountants regularly obtains rulings for groups or categories of clients in respect of such matters as depreciation allowances and rules relating to the recognition of income. There is no reason to abandon the present informal dialogue between the Society and the Inland Revenue Department. But at the same time there may be advantages in allowing the Society, or similar applicants, to obtain formal rulings should they so wish.

G. *Opinions on commercial practices*

In Canada the authorities may decline to give a ruling which requires an opinion as to generally accepted accounting or commercial practices. The reason for this limitation is not clear. Ultimately, tax liability is a question of law. An accounting or commercial practice may be helpful in settling the law. But there seems no reason for revenue authorities to hesitate to state their view as to whether accounting or commercial practices are in accordance with the law, either generally or in the context of an advance ruling for which there has been a formal application.

H. *Interpretation of new legislation*

Another category of case in which Canadian authorities will not act is where the requested ruling would require an interpretation of new legislation on which Revenue Canada has not yet adopted an official position or where the department is currently in the process of reviewing its position on existing legislation. In fact neither this reason (nor, indeed, the reason mentioned in the previous paragraph) is frequently a cause for Revenue Canada to decline to give a ruling that has been requested. By and large one would hope that the need to interpret new legislation or to review existing legislation should not prevent the issuance of rulings, though a certain delay might not be unreasonable in these circumstances.

XII. WHO SHOULD MAKE RULINGS?

In New Zealand the current non-binding rulings procedure is administered on a district basis. While the evidence is largely anecdotal, this system does appear to suffer from certain shortcomings. Most tax practitioners have stories of differing rulings on similar sets of facts from different district offices, or even from the same office but from different personnel. It is surely significant that the three jurisdictions with the most developed rulings systems, Canada, Sweden, and the United States of America, all centralised their procedures many years ago. Apart from promoting uniformity centralisation helps to create a body of knowledge and experience that enables rulings to be given speedily and accurately. As far as the writer is aware all commentators and tax practitioners who have given thought to the matter favour a centralised rulings procedure for New Zealand.

A more difficult question is whether the ruling authority should be an office within the Department of Inland Revenue or an independent or semi-independent organisation. In most countries rulings are handled within the tax department.

XIII. SWEDISH SYSTEM

Sweden provides an interesting exception. In that country the functional decentralisation that is a leading feature of all public administration in Sweden is also a characteristic of the tax administration. County administrative boards act independently within the limits laid down by tax laws and government instructions. There are about 3,000 assessment boards, each as a rule handling between 1,500 and 3,000 taxpayers. The chairman of each board is appointed by the county administration. Other members are elected by municipal assemblies in the district concerned. Thus a considerable measure of political control of the tax administration is delegated to a local level.

There is also the Riksskatteverket (RSV), the national tax board. Broadly speaking, the function of the RSV is to promote the uniform application of all taxes throughout the country. It is an advisory and co-ordinating authority but has no directive power over the provincial and local tax authorities.

An important function of the RSV is to make rulings on the application of individual taxpayers. This function is delegated to the RSV's committee for legal matters. Rulings of this committee are binding on local assessment committees when the taxpayer files his return. Thus in Sweden rulings are administered independently of the revenue administration and at a reasonably high level.

An appeal lies from a decision of the RSV direct to the Supreme Administrative Court of Sweden, which is Sweden's highest judicial authority in taxation matters. A direct appeal to such a superior court might appear strange to New Zealand readers. However, it should be borne in mind that there are no questions of fact involved and that the rulings authority, the RSV, is itself a body of considerable eminence.

The Swedish system has definite attractions. The object of having an independent rulings authority is to promote public confidence. One would expect there to be a similar effect in New Zealand. The Swedish provision for appeals is also attractive. Indeed, the grounds for providing for appeals are probably even stronger in jurisdictions like New Zealand where rulings are administered within a department of state. One problem with appeals to judicial courts is the question of delay. This difficulty is overcome in Sweden by giving rulings appeals priority. They are dealt with by the Supreme Administrative Court within six or eight months, which compares with a delay of some years for appeals in ordinary tax cases.

XIV. PROCEDURE FOR NEW ZEALAND

It may be that if New Zealand is to establish a binding rulings procedure it would be appropriate to adopt the better features of both the Canadian and the Swedish systems. New Zealand does not have any official body like the Swedish RSV. A strong case for a New Zealand national tax advisory board could be made out, though that is beyond the scope of this paper. If there were such a board the giving of advance rulings could usefully be one of its functions. In the absence of a national board it would seem appropriate that rulings should be dealt with by a unit within the head office of the Inland Revenue Department, possibly a unit within the legal section of that office.

One would expect that most cases could be dealt with by letters between the taxpayer or his advisers and the rulings unit, the taxpayer's district being invited to give its views on the application and possibly also on a draft of the proposed ruling.

XV. CONFERENCES BETWEEN TAXPAYER AND RULINGS AUTHORITY

Some cases would merit an interview or conference between the taxpayer and the staff dealing with the case. In some jurisdictions a taxpayer asking for a ruling may request one conference as of right and may be granted other conferences in the discretion of the authorities. In New Zealand it would probably not be necessary to lay down rules about numbers of conferences. Rather, one could see how the procedure operated for a year or two. If it seemed that taxpayers were imposing unduly upon the time of the staff of the rulings unit some rules could be laid down. It is thought unlikely that such rules would prove necessary.

XVI. APPEALS

An appeal should lie from decisions adverse to the interests of the taxpayer. It would seem appropriate that the appeal should be to the Taxation Review Authority or direct to the High Court. The current criteria for direct appeals to

the High Court in respect of objections to assessments appear to be reasonably appropriate also in the advance rulings context. Pursuant to section 33(4) of the Income Tax Act 1976 an objection may be referred directly to the High Court if both the Commissioner and the objector consent or if the court grants leave on the application of either party on the ground that "by reason of the amount of tax in dispute between the parties or of the general or public importance of the matter or of its extraordinary difficulty or for any other reason it is desirable that the objection be heard and determined by the High Court instead of by a Taxation Review Authority".

The question arises as to whether there should be a further right of appeal to the Court of Appeal. Given that the papers and arguments in the case would have had to have been prepared for the High Court it should not be unduly time-consuming for an appeal to be taken further, to the Court of Appeal, particularly if priority could be given in rulings cases as is done in Sweden. There should be no appeal to the Privy Council. The delays would be such as to make that exercise rather pointless within the context of an advance rulings procedure, one of the main reasons for which is to obtain speedy answers to difficult questions.

XVII. RELIANCE BY THIRD PARTIES

The question of whether and to what extent one taxpayer should be able to rely on a ruling obtained by another raises a number of difficult issues, but above all there is the question of uniformity. Fairness, in the sense of the uniform application of the tax rules to taxpayers in similar circumstances, is an important objective of any tax system. In the present context this objective is probably decisive. It would appear unreasonable that one taxpayer should be treated more generously than another simply because the first happened to have obtained a favourable advance ruling about his tax liability.

If it is accepted that taxpayers in general should be able to rely on rulings given to individuals certain consequences follow. First, one must be particularly concerned as to the quality of the rulings process. If mistakes are made that affect the affairs of one taxpayer it is bad enough. But if a body of taxpayers is able to take advantage of a ruling mistake the loss to the revenue authorities could be very significant. This consideration boils down in the end to a matter of expense. Simply, a rulings office must be staffed by people of high qualifications and expertise.

XVIII. REVOCATION: EFFECT ON THIRD PARTIES

Secondly, there is the question of revocation or modification of rulings. If the rulings authority decides that a ruling should be changed it seems reasonable that taxpayers who have not yet taken advantage of the ruling should not be able to do so in the future. But what of taxpayers apart from the original applicant who have put in train transactions or business systems that rely for their viability on the original ruling? If those transactions or systems are terminated by the time the revocation or modification is announced there is no problem. But a taxpayer may have arranged his affairs in the expectation of being able to rely on a ruling for several years. Should that taxpayer be able to continue to rely on the ruling even after it is modified? In principle, the answer should be yes. In

practice this principle could lead to an unacceptable loss of revenue. One solution may be to provide that if a taxpayer wishes to rely upon a ruling granted to someone else he or she must give notice to that effect to the Inland Revenue Department. Such a procedure should not be particularly onerous for either the taxpayer or the Department. Indeed, there are already within the Income Tax Act a number of provisions requiring notice if the taxpayer wishes to take advantage of them. These include several of the provisions relating to the sale of livestock and also section 129(4), pursuant to which a taxpayer may by notice to the Commissioner of Inland Revenue elect to spread into future years deemed income from a claw-back of development expenditure or interest on the sale of land held for less than 10 years. A notice requirement of this nature would enable the effect of a ruling to be monitored in order to gauge its effect on the collection of revenue. If necessary the authorities could review the position to determine whether the ruling was correct. If not it could be modified or remedial legislation could be proposed.

XIX. PUBLICATION OF RULINGS

If taxpayers in general are to take advantage of rulings given to individuals a system of publication is necessary. In any event pursuant to the Official Information Act rulings would have to be made public subject to the deletion of details that would identify the taxpayer concerned or his or her commercial secrets.

Rulings would be in a similar position to judgments of the Taxation Review Authority. Currently such judgments are supplied to publishers without the deletion of identifying material. Publishers' editors purge the judgments as necessary before they are printed and circulated. A similar system could work effectively with advance rulings.

An alternative is for rulings to be edited, published, and sold by the Inland Revenue Department. Theoretically such sales could cover the costs of the work involved. In practice there might be difficulties. For instance, the Inland Revenue Department, like other departments of State, is not accustomed to publishing material for sale. Secondly, the publication of a series of rulings would probably be able to be done more efficiently within a firm already engaged in a similar business.

Overseas experience suggests that many rulings are of little or no general importance but are highly specific to the applicant. In many jurisdictions the practice is not to publish such rulings. The question therefore arises as to whether a decision not to publish should be made by the Inland Revenue Department or by private publishers. It is suggested that the publishers should make the decision. Admittedly, they would almost certainly err on the side of publication rather than non-publication. However, so long as this practice did not involve the revenue administration in any expense no great harm would be done. In fact, to leave the decision to publish up to private enterprise should reduce costs for the revenue authorities by eliminating the need to make a judgment as to the publishability of each ruling.

Rulings that had not been published would remain open to inspection under the Official Information Act. One would not anticipate many applications to see such rulings. They would need to be edited within the department before being made available to members of the public.

XX. FEES FOR RULINGS

In both Sweden and Canada taxpayers are charged fees for rulings that they request. There are no fees in the United States: rulings are provided as a service to the public. Currently New Zealand does not charge fees for its non-binding rulings.

Most New Zealand commentators and tax practitioners appear to take the view that fees should be charged for rulings, and that these fees should fully reimburse the Inland Revenue Department for its costs. One problem is that if rulings are published and are relied upon by other taxpayers it may be thought unfair that the person who obtained the ruling should bear the whole cost. However, it should be borne in mind that this is effectively what happens with tax litigation. Test cases are frequently fought out by individual taxpayers at considerable expense, to the ultimate benefit of the taxpaying public in general. The cost of obtaining a ruling would be unlikely ever to approach the costs of even relatively simple tax litigation.

It is appreciated that the proposals in this paper for the establishment of a formal, binding rulings procedure would add to the burdens already imposed on the Inland Revenue Department. The department is currently under some pressure. Over the last twelve months or so there has been a 26 percent turnover of staff and the department is now in the process of increasing its staff in order to administer the proposed goods and services tax that is due to come into effect in 1986. In these circumstances it seems entirely reasonable that taxpayers obtaining advance rulings should meet the full cost. Further, from a political and practical point of view one might anticipate more immediate progress in the establishment of an advance rulings procedure if there could be an assurance that it would not increase the administrative costs of the revenue system.

XXI. THE ESTABLISHMENT OF A RULINGS SYSTEM

If it is accepted that a procedure for giving binding advance ruling should be grafted onto the New Zealand tax system the question arises as to how this should be done. There are two alternatives: legislation and administrative action. The Canadian rulings system was instituted by administrative action. In response to recommendations by the 1966 Royal Commission on Taxation Revenue Canada determined unilaterally to put in place a rulings system. Rules of practice and procedure were drawn up and distributed to the taxpaying public and their advisers by departmental circular.

XXII. CANADIAN SYSTEM

The legal basis of the announcement by Revenue Canada was not strong. Strictly speaking the Canadian law as to advance rulings is the same as New Zealand law. That is, the liability of a taxpayer is set by legislation. The function of revenue officials is simply to quantify that liability. Consequently, officials

cannot be bound by their prior expressions of opinion whether or not those expressions are stated to be rulings. Be that as it may, as a matter of practice if the revenue chooses not to reverse its prior rulings they will simply stand. Accordingly, the authority of the Canadian system is based on an announcement by Revenue Canada that rulings once given will not be reversed, save in cases of certain specified exceptions. These include retrospective legislative changes and a discovery that the taxpayer had misrepresented or suppressed relevant facts in obtaining his ruling. The public acceptance in Canada of a system based on rulings that are unenforceable in the last analysis may well have been influenced by the fact that a similar system already existed and worked reasonably well in the United States of America. The shaky theoretical basis of the Canadian system does not appear to have caused significant problems.

XXIII. LEGISLATION

It would be possible for the New Zealand Department of Inland Revenue to adopt the same approach as Revenue Canada. The Commissioner of Inland Revenue could simply announce that henceforth he will be bound by advance rulings obtained pursuant to a procedure that he would specify. Such a development would be better than nothing. However, the better course would be for a binding rulings procedure to be established by legislation. New Zealand has a more strongly established history of judicial statements of the principle that the Commissioner of Inland Revenue cannot bind himseelf for the future than was the case in Canada. Further, there is the Commissioner's reiteration of this principle in his Public Information Bulletin published as recently as 1982. Consequently, it is likely that an advance rulings system established simply by administrative action would not immediately command the same respect in New Zealand as in Canada. Secondly, and more importantly, there are serious questions of constitutional principle involved. It is undesirable for departments of state to be seen to be acting contrary to the law even though they may do so for the benefit of members of the public. It is far better for the law to be changed by legislation. The institution of a binding advance rulings procedure would be a significant constitutional change for New Zealand's tax system. Such a change should be made by Parliament.

Another significant advantage of legislative rather than administrative action is that administrative action could not confer a right of appeal to the Taxation Review Authority or to the High Court. Appeal rights would enhance the acceptability and quality of a rulings procedure. It would be regrettable were a procedure to be established without such rights. Further, if it were decided that rulings should be made in the first instance by an independent authority and not by the Inland Revenue Department legislation would be necessary to establish that authority. The appropriate form of the necessary legislation would probably be an additional part inserted into one of the taxation acts. It is suggested that the Inland Revenue Department Act 1974 would be more appropriate than the Income Tax Act 1976. There are two reasons. First, the 1974 Act is more concerned with administration of the tax system while the 1976 Act lays down the rules about tax liability. Secondly, the Inland Revenue Department Act applies to the administration of the collection of all taxes within the jurisdiction of the

Inland Revenue Department, and not just income tax. The arguments in favour of an advance rulings procedure apply also to liability for estate duty, gift duty, and goods and services tax. One would anticipate fewer applications in respect of these other taxes, though in the first few years of the goods and services tax there would well be significant numbers of applications for rulings due to the lack of reported cases in the area that can assist in the interpretation of the new laws. Indeed, the introduction in 1986 of the goods and services tax furnishes is by itself another reason for the institution of a binding rulings procedure. If an advance rulings procedure is instituted for income tax the same procedure should be extended to the other taxes administered by the Inland Revenue Department. Consequently, the Inland Revenue Department Act 1974 is the appropriate place for the necessary legislation.

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