

CHAPTER 2: RULINGS AND OTHER TAX OFFICE ADVICE

This Chapter outlines the main types of advice that the Tax Office provides to assist taxpayers and practitioners, comparing the advice with that provided by the national tax authorities in Canada, New Zealand, the UK and the US.

The Chapter reviews the key issues that have been identified in relation to the quality of Tax Office advice. It identifies several options for enhancing Tax Office advice, the most important being to make more of it legally binding, providing more protection for taxpayers who act in accordance with advice that applies to them.

Tax Office rulings and other advice are important for taxpayer certainty. Taxpayers who self assess in line with the Tax Office's interpretation of the law have confidence that they will not be liable to pay additional primary tax, interest or penalties. Taxpayers who do not follow Tax Office advice, or do not know the Tax Office position, run the risk that the Tax Office will amend their assessments and they will be liable to pay additional amounts.

The capacity of Tax Office advice to enhance taxpayer confidence depends on its quality (defined in Chapter 1 as its accessibility, timeliness, accuracy and reliability).

The quality of Tax Office advice is equally important for taxpayers who complete their own income tax returns and for the 75% of Australian taxpayers whose income tax returns are prepared on their behalf by tax agents. Practitioners play an important role in interpreting Tax Office advice, determining what Tax Office advice is relevant and whether more detailed advice is required. Practitioners need to have a clear understanding of the Tax Office's position on relevant issues in order to advise their clients effectively. Reforms that improve the capacity of practitioners to understand the views of the Tax Office can be expected to boost overall confidence in the system.

2.1 Types of Tax Office advice

The Tax Office provides taxpayers and practitioners with a comprehensive range of advice on how to apply the income tax law, through formal rulings as well as other products.

2.1.1 Formal rulings

There are currently three types of formal income tax rulings: public rulings, private binding rulings (PBRs) and oral rulings.¹ As noted in Chapter 1, public rulings and PBRs were introduced in 1992 in order to provide taxpayers with greater certainty. Oral rulings were introduced in 2000 as part of the New Tax System.

The advice contained in formal rulings is binding by law on the Tax Office. Rulings remain valid until they are either withdrawn or replaced and can only be withdrawn prospectively. This means that a taxpayer covered by a formal ruling is protected from retrospective amendment, even if the Tax Office subsequently changes its interpretation of the relevant provisions of the income tax law.² As the law currently stands, rulings may only deal with interpretation of those parts of the income tax laws under which a taxpayer's liability is worked out.

Public rulings

Public rulings provide general written guidance on matters relevant to a wide range of taxpayers. They state the Tax Office's view on how the income tax law applies to a particular type or class of arrangements.

Public rulings are provided at the discretion of the Tax Office and there are no statutory or administrative limits on the time taken for them to be issued. The Public Rulings Program is developed in consultation with the National Tax Liaison Group, which is chaired by the Tax Office, and draws its membership from Tax Office staff, practitioners and other external representatives. Rulings are prepared in conjunction with panels that contain representatives from the accounting and legal professions.

Recently, the Tax Office has introduced two sub-categories of public rulings that provide advice to groups of taxpayers.

- Product rulings were introduced in 1998 to rule publicly on the availability of tax benefits from particular investment products.

1. The legislative frameworks that underpin these three types of formal rulings are contained in Part IVAAA, Part IVAA and Part 5-5 of Schedule 1 of the *Taxation Administration Act 1953* (the TAA) respectively. The provisions of Part IVAAA and IVAA of the TAA also apply to the fringe benefits tax and fuel sales grants. A different legislative framework applies to the Goods and Services Tax (GST), the Luxury Car Tax (LCT) and the Wine Equalisation Tax (WET). This framework is contained in section 37 of the TAA.

2. In general, a public ruling or a PBR will continue to apply to a taxpayer in relation to an arrangement that has already commenced, even if it is withdrawn or replaced by the Tax Office. The only exception is when the relevant legislation is amended or repealed. If a ruling applying to an arrangement that has already commenced is replaced with another ruling, the ruling that is most advantageous to a taxpayer will be binding on the Tax Office.

- Class rulings are a more recent innovation and are used to rule on the application of tax laws to a large number of persons in relation to a particular arrangement, such as an employee share scheme.

Product and class rulings are intended to eliminate the need for each participating taxpayer to obtain a separate PBR.

Private binding rulings

PBRs provide specific written advice to a particular taxpayer on how the Tax Office considers the law applies to that taxpayer. They only apply to a specified arrangement for a specified income year. They are not binding on the Tax Office in relation to other taxpayers.

PBRs are provided in response to requests for advice from taxpayers and practitioners.³ Most taxpayers may apply for a PBR at any time until four years after the last date for lodging a return for the income year to which the ruling relates.⁴ The Tax Office must provide a PBR unless the request falls into one of the exclusions listed in the relevant legislation. In these circumstances, the Tax Office can issue a PBR, but is not obliged to do so.⁵ Taxpayers are not charged a fee by the Tax Office for PBRs.

There is no statutory time limit for the Tax Office to make a PBR.⁶ The *Taxpayers' Charter* indicates that the Tax Office aims to provide PBRs within 28 days of receiving all necessary information from the applicant (or a longer period negotiated with the relevant taxpayer).

PBRs are published by the Tax Office on its website, in an edited form to protect the confidentiality of recipients. In practice, some taxpayers and practitioners use these to gain insights into how the Tax Office interprets particular provisions of the law, although the Tax Office would prefer them to use Australian Taxation Office Interpretative Decisions (ATOIDs, see 2.1.2) for this purpose.

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3. Section 14ZAG of the TAA allows practitioners to apply for a PBR on behalf of a taxpayer.
 4. Shorter Period of Review (SPOR) taxpayers have only two years to apply for a PBR.
 5. Section 14ZAN of the TAA lists the circumstances in which the Tax Office is not required to comply with an application for a PBR. These include: where a tax audit has commenced which will examine the matter covered by the application; where the matter is already subject to an objection against a self assessment; where the application is considered to be frivolous or vexatious; where the applicant has not provided the Tax Office with sufficient information; or where complying with the application would require an unreasonable amount of Tax Office resources.
 6. If no ruling has been issued within three months of the provision of the relevant information, an applicant may request a written notice from the Tax Office setting out the reasons for the delay.

Oral rulings

Oral rulings are used to provide specific advice on a limited range of simple income tax matters to taxpayers with simple tax affairs.⁷ In common with PBRs, the Tax Office is required to provide an oral ruling to a taxpayer unless the request falls into one of the specific exclusions contained in the legislation. An important difference between oral rulings and PBRs is that practitioners cannot generally apply for oral rulings on behalf of their clients.

Rulings data

In 2002-03, the Tax Office issued 7,631 PBRs, 46 public rulings (as well as 154 product and class rulings, excluding those dealing with superannuation) and nine oral rulings on income tax matters. Around 60% of PBRs were issued to individual non-business taxpayers and around 30% were issued to micro businesses. Less than 3% were issued to large businesses.⁸

The Tax Office estimates that only about 2% of PBR applications require a precedent to be established. The remainder are dealt with on the basis of existing Tax Office advice that is already available to taxpayers and practitioners. Only 3% of PBR applications are classified by the Tax Office as complex. Many PBR applications involve how the law might apply to particular fact patterns, rather than complex interpretive matters.⁹

2.1.2 Other types of Tax Office advice

Formal rulings are not the only way in which the Tax Office provides advice to taxpayers on the interpretation of the income tax law.

The Tax Office publishes a wide range of general written advice, a considerable amount of which is available on the Tax Office website. Possibly its most important publication for individuals is *TaxPack*. This is intended to provide taxpayers with the key information required to complete their annual income tax return. The information contained in *TaxPack* is supplemented by over 70 specialised publications that provide information on particular issues that are not relevant to the majority of taxpayers.

7. These concepts are defined in Part 5-5 of Schedule 1 of the TAA, which lists the matters on which an oral ruling may be sought. These include basic categories of assessable income, deductions and offsets.

8. 4,816 were issued to individual non-business taxpayers; 2,380 to micro businesses; 78 to small and medium businesses; 177 to large businesses and 180 to government and non-profit bodies.

9. The Tax Office estimates that around 30% of all income tax PBR applications relate to the following matters: the status of compensation payments, the undeducted price of superannuation payments, eligible termination payments, primary production status, residency status, and deductibility of expenses. The Tax Office estimates that responding to these requests requires reference to 13 publicly available precedents or interpretative decisions.

Many of the Tax Office's main general advice products are tailored to particular taxpayer segments with special needs (such as immigrants, investors or indigenous Australians). The Tax Office also publishes a wide range of other advice in the forms of manuals, booklets, schedules, fact sheets, policy statements, press releases, ATOIDs, and taxpayer alerts.

- ATOIDs explain how the Tax Office has applied the law in relation to a particular matter. They are used primarily for internal purposes by Tax Office officials to promote consistency in decision making (including in the provision of advice to taxpayers and practitioners). They have precedential value in that the principles underlying a particular decision will often be followed in subsequent cases. However, these principles are not binding on the Tax Office and it is free to change its interpretation of relevant provisions and amend assessments accordingly. ATOIDs are published on the Tax Office's website pursuant to the *Freedom of Information Act 1982* (which generally requires Commonwealth agencies to publish or make available material relating to their internal decision-making processes).¹⁰
- Taxpayer alerts are intended to be an 'early warning' of significant new and emerging tax planning issues that the Tax Office has under risk assessment.

The Tax Office also provides a large amount of oral advice in response to enquiries from taxpayers and their advisers in person and by telephone. In 2002-03, the Tax Office received more than 6 million telephone calls, evenly divided between its personal tax information line and business call centres, and over 1 million visits to its assistance centres. About a third of the telephone calls sought advice about the tax law. During the same period, over 3 million calls were made to the Tax Office's agent telephone inquiry service, and it received more than 600,000 general telephone inquiries.¹¹

Status of other Tax Office advice

Advice provided through these other mechanisms is not legally binding on the Tax Office. In theory this means that it could be altered or withdrawn at any time. However, some of this advice is treated as administratively binding. The Tax Office's policy is to only depart from administratively binding advice where there is a material change to the relevant law, where a court or tribunal adopts a different interpretation to that previously followed by the Tax Office, or where the existing interpretation is no longer

10. Australian Taxation Office 2001, *Practice Statement PS LA 2001/8*, Australian Taxation Office, Canberra.

11. The data refers to all taxpayer inquiries and is not confined to inquiries relating to income tax matters.

considered appropriate (for example, because it has created unforeseen consequences for the revenue).¹²

Taxpayers who have relied on non-legally binding advice to complete their returns may be liable to pay additional primary tax and interest (but no shortfall penalties) as a result of a change in the Tax Office's interpretation.¹³ Where advice is neither legally nor administratively binding, the Tax Office does not generally¹⁴ provide an assurance that it will 'stand by' it. For example, the *Consolidation Reference Manual*, an important source of advice for many business taxpayers, is not legally binding and has no formal status. However, advice contained in *TaxPack* and the publications it refers to are covered by the *Commissioner's Guarantee*. This states that:

- If a taxpayer relies on advice in *TaxPack* (or one of the related publications) and makes an honest mistake, the Tax Office will not charge a penalty, but may charge interest.
- If the taxpayer's mistake has been made because the Tax Office advice is misleading, it will not charge either penalties or interest.

In either case, the taxpayer will have to pay any shortfall in their primary tax liability.

2.2 International comparisons

In Canada, New Zealand, the UK and the US, the national tax authorities also provide a wide range of general and specific income tax advice to taxpayers. In particular, each authority provides taxpayers with general advice in the form of public rulings and most also provide specific tax advice to particular taxpayers and practitioners.

Despite these broad similarities, there are some differences.

Australia and New Zealand provide legally binding advice (as well as administratively binding and non-binding advice). By contrast, the Canadian, UK and US tax authorities do not provide legally binding advice. Another difference is the extent to which it is

12. The circumstances in which the Tax Office may depart from administratively binding advice are set out in paragraph 73 of Australian Taxation Office 2001, *Practice Statement PS LA 2001/4*, Australian Taxation Office, Canberra.

13. Subsection 284-215 (1) of the TAA provides that penalties do not apply where a taxpayer has a shortfall as a result of following Tax Office advice.

14. The Australian Taxation Office 2003, *Practice Statement PS LA 2003/3*, Australian Taxation Office, Canberra indicates that it will be administratively bound by publicly issued rulings that are not formal public rulings within the meaning of Part IVA of the TAA.

possible to appeal against private rulings. This is possible in Australia, but not in either New Zealand or Canada. The UK and the US both allow limited appeals against certain rulings (although it is not possible to appeal against a refusal by the UK Inland Revenue to issue a ruling). Canada, New Zealand and the US all charge fees for private advice. This is provided free of charge in Australia. The UK charges for some types of private advice, but not others.

Australia is the only jurisdiction that imposes a penalty where a taxpayer has an income tax shortfall as a result of a failure to follow a PBR. Furthermore, only Australia has a formal system of binding oral rulings (albeit one that has been little used since its introduction in 2000). Finally, among the five tax authorities, Australia's Tax Office has arguably the most extensive processes for involving practitioners and other representatives in the selection and preparation of public rulings.

2.3 Previous reviews of the rulings system

Australia's formal tax ruling system has been subject to a number of reviews since its introduction in 1992. These reviews have examined the policy objectives underlying the system as well as its administration by the Tax Office.

- In 1993, the Joint Committee of Public Accounts reviewed the ruling system as part of a wider inquiry into tax administration.¹⁵ It also examined some of the Tax Office's other advice products, most notably *TaxPack*.
- In 1998, the Government's plan for the introduction of A New Tax System proposed a number of reforms to the income tax rulings system.¹⁶
- In 1999, the Review of Business Taxation (the Ralph Review) considered the ruling system as part of its examination of Australia's business tax framework.¹⁷

15. Commonwealth of Australia Joint Committee of Public Accounts 1993, *An Assessment of Tax, Report 326*, 1993, Commonwealth of Australia, Canberra.

16. Commonwealth of Australia 1998, *Tax Reform: not a new tax, a new tax system*, August 1998, Commonwealth of Australia, Canberra.

17. Commonwealth of Australia 1999, *Review of Business Taxation: A tax system redesigned*, July 1999, Commonwealth of Australia, Canberra.

- In 2000, the Tax Office commissioned Mr Tom Sherman AO to review the Tax Office's systems and procedures for producing PBRs.¹⁸
- In 2001, the Australian National Audit Office (ANAO) completed a performance audit on the Tax Office's administration of taxation rulings.¹⁹

While not constituting a formal review, in 2003, the Inspector-General of Taxation reported on practitioners' concerns with aspects of the Tax Office's administration of the formal rulings system.²⁰

These reviews all expressed general support for the rulings system, but identified shortcomings with particular aspects of its operation.

There have been few significant amendments to the legislative framework for rulings, but the Tax Office has changed the way it administers the system. These changes have included the introduction of new classes of public rulings, new procedures intended to produce greater consistency in PBRs and publication of PBRs and ATOIDs on the Tax Office's website.

While there have been reviews of the formal rulings system, other advice products have generally only been subject to internal review by the Tax Office (although many are developed in conjunction with community bodies). The Tax Office's recent *Listening to the Community* project has gathered extensive qualitative data concerning the perceptions of a range of taxpayers and tax agents towards Tax Office advice products. It found that taxpayers want quick, accurate and accessible advice that the Tax Office stands behind.²¹

2.4 Tax Office advice – issues and possible reforms

The Review seeks feedback on how Tax Office advice might be improved in order to enhance taxpayer confidence, while maintaining the overall integrity of the income tax system. To facilitate this feedback, this section lists, without necessarily endorsing, some

18. Sherman, T 2000, Report of an internal review of the systems and procedures relating to private binding rulings and advance opinions in the Australian Taxation Office, Commonwealth of Australia, Canberra.

19. The Auditor-General (Australian National Audit Office) 2002, *The Australian Taxation Office's administration of taxation rulings*, Audit Report Number 3 of 2001/02, Commonwealth of Australia, Canberra.

20. Inspector-General of Taxation 2003, *Issues Paper Number 3: Self-Assessment*: <<http://www.igt.gov.au/content/submissions.asp?NavID=7>>.

21. Australian Taxation Office 2003, *Making it easier to comply: the easier, cheaper and more personalised program*, Australian Taxation Office, Canberra, p.5.

of the main issues relating to Tax Office advice that have been identified by previous reviews and in commentary by academics and practitioners.

2.4.1 Accessibility

Accessibility is an important characteristic of high quality advice. The Tax Office should provide sufficient advice for taxpayers to meet their obligations and this advice ought to be easily obtained and understood by those to whom it is directed.

Several issues have been identified in relation to the accessibility of Tax Office advice.

Taxpayers and practitioners derive considerable benefit from the general advice that is provided by the Tax Office. The existence of a comprehensive range of general advice assists taxpayers and practitioners to apply the law correctly without the need to request specific advice from the Tax Office. However, some practitioners have expressed concerns about their capacity to cope with the volume of general advice that the Tax Office produces and to determine which advice might be relevant in particular circumstances. Some practitioners have expressed concerns about the difficulty of locating ATOIDs and other relevant information on the Tax Office website.

In recognition of the importance of this issue, the Tax Office has recently redeveloped its website to improve its accessibility. It has also introduced improvements such as a mechanism to allow frequent users to suggest further refinements.

Concerns have also been expressed that it can be hard for taxpayers and practitioners to obtain PBRs on particular topics. The Tax Office is said to have adopted informal policies of refusing to provide PBRs in areas which have been designated 'off-limits'.

A particular concern in this regard relates to PBRs covering the possible application of Part IVA.²² Some practitioners have expressed concern that the Tax Office is reluctant to issue rulings on whether or not Part IVA will apply to a particular arrangement. It has also been argued that the Tax Office has inappropriately sought to invoke Part IVA in relation to arrangements that are covered by a PBR (where the PBR does not deal with

22. Part IVA of the *Income Tax Assessment Act 1936* contains what are known as the general anti-avoidance provisions. These provisions enable the Tax Office to disallow taxation benefits obtained from schemes whose dominant purpose is to enable a taxpayer to obtain a tax benefit. The question of whether the dominant purpose of a particular scheme is to confer a tax benefit is determined with regard to the matters listed in paragraph 177D(b) in Part IVA.

the potential application of Part IVA). These concerns were noted by the Inspector-General of Taxation in his recent issues paper on self assessment.²³

Concerns about the willingness of the Tax Office to issue PBRs on certain topics have tended to be raised by large business taxpayers and their representatives (rather than individual or small business taxpayers). It is difficult to empirically assess the validity of these concerns. The Tax Office has stated that there are certain limited circumstances in which it may not be appropriate for it to issue PBRs, although in 2002-03 it only refused to rule in relation to three applications from large business taxpayers. In relation to the possible application of Part IVA, it has stated that it will issue PBRs where it can do so on the basis of the information that has been supplied to it.

Another issue is the capacity of taxpayers and their advisers to understand Tax Office advice. Some concerns have been expressed about the clarity of Tax Office advice (especially for ordinary taxpayers). Taxpayers could benefit if Tax Office advice could be expressed in straightforward language. However, the Tax Office must strike a difficult balance between the need to provide advice that is succinct and the need to ensure that its advice is accurate in all circumstances. Moreover, some taxpayers and practitioners may prefer a lengthier explanation of principles in order to gain a better understanding of how the Tax Office might approach similar cases.

2.4.2 Timeliness

To be useful, advice needs to be provided in time to meet the needs of taxpayers. This is most important where a decision to enter into a prospective transaction is dependent on the Tax Office's view of its taxation consequences.

The time required to provide advice often depends on the complexity of the matter in relation to which advice is sought. It is also likely to depend on the time taken for the Tax Office to be provided with the information needed to formulate the advice – an issue that is often beyond the Tax Office's control.

In previous reviews, some large business taxpayers and their advisers have criticised the time taken by the Tax Office to produce PBRs covering prospective transactions. Similar criticisms have been levelled at the time taken to finalise some public rulings (although the time taken also reflects the lengthy consultation processes that currently apply to them). Finally, there appears to be some criticism from some taxpayers and practitioners about the time taken by the Tax Office to respond to telephone and over the counter requests for information about the operation of the income tax law.

23. Inspector-General of Taxation 2003, *Issues Paper Number 3: Self-Assessment*: <<http://www.igt.gov.au/content/submissions.asp?NavID=7>>.

Concerns about the time taken by the Tax Office to finalise public rulings and to respond to requests for legally binding advice were noted in the Inspector-General of Taxation's recent issues paper on self assessment.²⁴ That paper also noted that the Tax Office has proposed a package of administrative measures to improve the timeliness of PBRs.²⁵

Table 2.1: Data on timeliness of Tax Office advice – 2002-03

	Performance benchmark	Performance (%)
General correspondence	84% completed in 28 days	88
General telephone inquiries	80% answered in 2 minutes (peak 5 minutes)	89
General visit inquiries	85% attended in 10 minutes (peak 15 minutes)	92
PBRs	75% completed in 28 days or a longer period negotiated with the applicant	77(a)
Objections against PBRs	85% completed in 28 days	72
Public rulings (b)	n/a	n/a

Source: Tax Office data. The data covers all taxes (not just advice relating to income tax).

- (a) The Tax Office has indicated that 37% of all PBR applications from individuals were finalised within 28 days, but only 8% of PBR applications from large business taxpayers were finalised in that period.
- (b) In 2000, the Tax Office finalised 69 Taxation Rulings and Taxation Determinations. 18 of these were finalised in 100 days or less; 8 were finalised in 101 to 200 days; 18 were finalised in 201-300 days; 17 were finalised in 401 to 500 days; and 8 had taken more than 501 days to finalise (cited in ANAO Audit Report No 3, 2001, p.57).

While there is no statutory time limit on the provision of PBRs, taxpayers have a right to obtain reasons for the delay if no PBR has been provided within three months after all necessary information has been provided.

It would be possible to impose a statutory time limit within which certain types of advice must be provided by the Tax Office. However, it would be necessary to consider the following issues:

- How long should the Tax Office be given to respond to complex requests from taxpayers?
- What would happen if no advice has been provided by the end of the period?

One suggestion on this second issue is that the taxpayer should receive a default positive ruling. Alternatively, the taxpayer could receive a default negative ruling (and could then appeal against it). Both these options are problematic. The former may create incentives

24. Inspector-General of Taxation 2003, *Issues Paper Number 3: Self-Assessment*: <<http://www.igt.gov.au/content/submissions.asp?NavID=7>> pp.4-5, 9-11.

25. Inspector-General of Taxation 2003, *Issues Paper Number 3: Self-Assessment*: <<http://www.igt.gov.au/content/submissions.asp?NavID=7>> p.10.

for taxpayers to withhold information from the Tax Office (especially if the time period is not reset when new information was requested) or overload the Tax Office with requests for advice. The latter may not assist those taxpayers who prefer to wait longer for a substantive ruling. It may also simply shift any 'timeliness' problems from the rulings process to the appeal process.

An alternative to the introduction of a statutory time limit may be for the Tax Office to establish more demanding internal performance standards.

The resource implications of any proposals for the Tax Office to provide advice more quickly need to be considered, as well as their possible impact on the accuracy of advice. Reducing the time taken to produce public rulings might impact on the extensive consultation processes in place to facilitate input from practitioner representatives.

2.4.3 Accuracy

Taxpayers and practitioners are entitled to expect the advice they receive from the Tax Office to be accurate. However, the meaning of this concept depends on the nature of the issue to which the advice relates.

If the advice relates to a provision of the law that is not contentious, it can simply mean that the advice is the same as would be given to any other person who asked the same question. Concerns have been raised about the consistency of Tax Office advice.²⁶

Where advice relates to a provision that can be interpreted in different ways with different tax consequences, the concept of accuracy is more closely related to objectivity. It has been argued by some taxpayers and practitioners that, rather than being objective, there is a systematic 'pro-revenue' bias in Tax Office advice on complex and contentious issues.

It is difficult to establish the validity of the concern relating to objectivity, because of the difficulty in measuring it. The Tax Office has indicated that where there are two viable interpretations of a provision that are consistent with its underlying policy objectives, it will adopt the more practical approach, or the approach that minimises compliance costs. Tax Office statistics suggest that more than two thirds of the PBRs issued are either

26. Inspector-General of Taxation 2003, *Issues Paper Number 5: ATO/Client Interface Systems*: <<http://www.igt.gov.au/content/submissions.asp?NavID=7>>, p.16.

wholly or partially favourable to the applicant.²⁷ However, some practitioners argue that this is to be expected given the penalty for not following a PBR.²⁸

One way to address concerns about the objectivity of Tax Office advice might be for a suitable independent body to undertake a systematic evaluation of advice, especially that in PBRs.

2.4.4 Reliability

The reliability of Tax Office advice is fundamental to taxpayer confidence. Reliability depends on the extent to which the Tax Office's advice is binding on it or, if not binding, will be followed nevertheless.

As previously noted, the Tax Office must stand behind advice that is legally binding.²⁹

Where its advice is not legally binding, the Tax Office is able to withdraw it or adopt a new position. However, in practice the Tax Office will only depart from its advice relatively infrequently and only with what it believes to be good cause.

The reliability of Tax Office advice might be improved by making more advice legally binding. The main benefit of making more advice legally binding is that the Tax Office would only be able to withdraw or amend it prospectively. As a consequence, taxpayers who follow Tax Office advice would be protected from any requirement to pay additional primary tax or interest (rather than just being protected in relation to penalties). Making more general advice legally binding on the Tax Office would also bring this aspect of the income tax rulings system more closely into line with the effect of the ruling system that currently applies to the GST, WET and LCT (and that previously applied to wholesale sales tax). Under these systems, almost all published Tax Office advice is binding for the purposes of determining whether the Tax Office can recover underpaid tax or overpaid refunds.

Adopting this approach could constitute a significant extension of the existing formal income tax rulings system. Under the present system, the Tax Office only provides legally binding income tax advice in the form of public rulings, PBRs and oral rulings. PBRs and

27. In 2002-03, the Tax Office issued 7,631 PBRs. 4,150 were wholly favourable to the applicant, 1,246 were partially favourable and 2,235 were unfavourable. It also finalised 3,674 applications without issuing rulings (usually because the application was withdrawn, deemed invalid or because the Tax Office refused to rule).

28. A taxpayer who disregards a PBR is liable to a penalty if their failure to follow the ruling results in a shortfall. Many practitioners argue that they only request rulings when they are confident that the ruling will be favourable. Penalties are examined in greater detail in Chapter 4.

29. Provided advice was not obtained under false pretences and, where it covers a prospective transaction, the transaction is implemented as foreshadowed at the time the advice was sought.

oral rulings provide specific advice to particular taxpayers in relation to arrangements where the Tax Office has all the material facts.³⁰ Public rulings relate to defined arrangements and are subject to a lengthy process of refinement and consultation before they are released. These procedures do not currently apply to the same extent to many of the other advice products currently provided by the Tax Office. If more Tax Office advice was binding, it might become more limited, cautious and conditional and therefore more complex and less timely.

Providing more legally binding advice would reduce the capacity of the Tax Office to amend assessments where taxpayers have paid too little tax on the basis of incorrect Tax Office advice. This may have significant revenue consequences, or the tax foregone might effectively be borne by taxpayers as a whole. However, these concerns do not apply if the advice is correct.

For Tax Office advice to be reliable, it is also necessary for taxpayers and practitioners to be confident about when it applies. This is particularly important for advice intended to have potential application to a wide range of taxpayers. If more of the Tax Office's general advice were made legally binding, it would still be necessary for taxpayers and practitioners to determine when it applies. The benefit of making more of its general advice legally binding would depend on the way in which this advice is framed, as well as the skill of taxpayers and practitioners in applying it in particular cases.³¹ A comprehensive binding regime might result in higher dispute levels between taxpayers and the Tax Office over whether particular arrangements are covered by general advice, although this has not been the experience with the indirect tax ruling system.

2.5 Rights of appeal against private binding rulings

In Australia, taxpayers have the right to object against a PBR with which they disagree. In 2002-03, the Tax Office received a total of 156 objections in relation to PBRs. If taxpayers are dissatisfied with the Tax Office's response, they may appeal to either the Administrative Appeals Tribunal (AAT) or the Federal Court.

It is not possible for a taxpayer to directly seek review of any other type of Tax Office advice. However, a taxpayer who is dissatisfied with a public ruling or an oral ruling can

30. In this sense, taxpayers who are covered by these types of rulings are in a similar position to that which applied before the introduction of self assessment, whereby the Tax Office could not alter an assessment if a 'full and true disclosure' of the facts had been made.

31. This issue is less significant in relation to specific advice (such as that provided to taxpayers in the form of a PBR). Because the Tax Office must have all relevant facts in relation to an arrangement before a PBR can be issued, taxpayers can have a high degree of confidence that the advice will apply to them.

appeal by obtaining a PBR and then objecting to it, or assessing themselves on the basis of the advice and then objecting to the assessment.³²

Direct appeal rights for PBRs are linked to the penalty that applies to shortfalls where the taxpayer disregards a PBR. Taxpayers who have shortfalls after failing to follow either public or oral rulings are not liable to penalties merely for that reason.

Previous reviews have identified the inability of the AAT or Federal Court to consider additional facts relating to an arrangement not set out in the relevant ruling. This has meant that matters have had to be referred back to the Tax Office, increasing the duration and cost of the review process for dissatisfied taxpayers.³³

2.6 Funding rulings and other advice

Tax Office advice is currently funded from consolidated revenue as part of its annual budget allocation. It is provided free of charge to taxpayers and practitioners (although significant costs may be incurred in obtaining certain types of advice, for example, in preparing an application for a PBR on a complex issue).

If it is considered that the Tax Office should provide more advice to taxpayers and practitioners, or that it should provide advice within a shorter time frame, it is necessary to consider how these improvements should be funded.

Another issue is whether there are any mechanisms that could be used by the Tax Office to provide taxpayers and practitioners with specific advice at lower cost than under the current PBR system. One suggestion is to make greater use of legally binding oral advice than is possible under the current system. Another idea that has been raised is for practitioners to be licensed to provide taxpayers with limited types of specific advice on behalf of the Tax Office. This advice could be submitted to the Tax Office at the time that a taxpayer lodges their return and become binding on the Tax Office if it were not explicitly disallowed within a particular period. This would be a major step, requiring lengthy consultation, the establishment of a licensing regime, monitoring procedures, and possibly also penalties.

32. Part IVC of the TAA contains standardised objection, review and appeal provisions that apply to a wide range of taxation decisions. These provisions apply to decisions about PBRs as well as decisions relating to assessments.

33. Commonwealth of Australia 1999, *Review of Business Taxation: A tax system redesigned*, Commonwealth of Australia, Canberra, p.142.

2.7 Questions for consultation

- 2.A Is Tax Office advice sufficiently accessible?
- 2.B Should Tax Office advice indicate whether Part IVA applies to a particular arrangement as a matter of course, or only on request?
- 2.C Do taxpayers and their advisers currently encounter delays in obtaining Tax Office advice? If so, what strategies might allow the Tax Office to provide advice on a more timely basis?
- 2.D Are there significant problems with the accuracy of Tax Office advice? If so, how should they be addressed?
- 2.E Is there evidence of pro-revenue bias in Tax Office advice? What measures would improve confidence in the objectivity of Tax Office advice? Would an independent evaluation assist?
- 2.F How should Tax Office advice be framed to assist taxpayers – by explaining contending views of the law, or by setting out how the Tax Office intends to apply it? Does this impact on the way that advice is expressed?
- 2.G How might the Tax Office clarify the circumstances in which general advice can be relied upon?
- 2.H Is there value in making more Tax Office advice legally binding? What additional safeguards would be required?
- 2.I Should taxpayers be penalised merely for not following PBRs when self assessing their income tax liabilities?
- 2.J If no penalty applied, would direct appeals against PBRs still be required?
- 2.K If appeals are retained, how could the process be improved?
- 2.L Should the Tax Office be permitted to charge for certain advice?
- 2.M How could the Tax Office use more cost effective channels for the delivery of binding advice to taxpayers or through practitioners?