



CO L O R A D O

**Department of
Regulatory Agencies**

**2015 Sunset Review:
The Issuance of Private Letter Rulings and
General Information Letters**

*Office of Policy, Research and Regulatory Reform
October 15, 2015*



COLORADO

Department of
Regulatory Agencies

Executive Director's Office

October 15, 2015

Members of the Colorado General Assembly
c/o the Office of Legislative Legal Services
State Capitol Building
Denver, Colorado 80203

Dear Members of the General Assembly:

The mission of the Department of Regulatory Agencies (DORA) is consumer protection. As a part of the Executive Director's Office within DORA, the Office of Policy, Research and Regulatory Reform seeks to fulfill its statutorily mandated responsibility to conduct sunset reviews with a focus on protecting the health, safety and welfare of all Coloradans.

Programs scheduled for sunset review receive a comprehensive analysis. The review includes a thorough dialogue with agency officials, representatives of the regulated profession and other stakeholders. Anyone can submit input on any upcoming sunrise or sunset review via DORA's website at: www.dora.colorado.gov/opr.

DORA has completed the evaluation of the Issuance of Private Letter Rulings (Rulings) and General Information Letters (Letters) by the Executive Director of the Department of Revenue (Executive Director). I am pleased to submit this written report, which will be the basis for my office's oral testimony before the 2016 legislative committee of reference. The report is submitted pursuant to section 24-34-104(8)(a), of the Colorado Revised Statutes (C.R.S.), which states in part:

The department of regulatory agencies shall conduct an analysis of the performance of each division, board or agency or each function scheduled for termination under this section...

The department of regulatory agencies shall submit a report and supporting materials to the office of legislative legal services no later than October 15 of the year preceding the date established for termination....

The report discusses the question of whether there is a need for the issuance of Rulings and Letters provided under Article 35 of Title 24, C.R.S. The report also discusses the effectiveness of the Executive Director and staff in carrying out the intent of the statutes and makes recommendations for statutory and administrative changes in the event this function of government is continued by the General Assembly.

Sincerely,

Joe Neguse
Executive Director





COLORADO

Department of Regulatory Agencies

2015 Sunset Review

The Issuance of Private Letter Rulings and General Information Letters

SUMMARY

What Are Private Letter Rulings and General Information Letters?

A Private Letter Ruling (Ruling) is a binding determination of tax liability related to a specific transaction. A General Information Letter (Letter) is a non-binding determination that addresses a general question from a taxpayer about a tax issue.

Why Are Rulings and Letters Necessary?

It is critical for a taxpayer to have certainty about tax questions. Otherwise, the taxpayer may only find out during an audit that the state interprets the law differently than the taxpayer.

Who Requests Rulings and Letters?

Most Ruling and Letter requests concern issues related to sales and use tax. However, a taxpayer may request a Ruling or Letter on any tax assessed by the state. Rulings and Letters provide taxpayers with a greater understanding of their tax liability in advance of making a transaction or filing taxes for a completed transaction.

How Are Rulings and Letters Issued?

The Executive Director of the Colorado Department of Revenue (Executive Director and Department, respectively) issues Rulings and Letters. In order to obtain a Ruling, a taxpayer must submit to the Office of Tax Policy Analysis (Office) a request along with specific information and documentation. Upon receiving a request for a Ruling, the Office estimates the amount of time it will take to perform an analysis of the tax issue and notifies the taxpayer of the fee. Then the Office performs an analysis and sends the taxpayer a draft of the Ruling. A taxpayer is only required to disclose its identity in order to move forward once a draft of the Ruling has been issued to the taxpayer.

In order to obtain a Letter, a taxpayer simply submits a request outlining the reason for the request. A taxpayer is not required to disclose its identity or pay a fee for a Letter.

What Does It Cost?

The issuance of Rulings is cash funded, but the Office, which has a much broader mandate, is financed by the General Fund. In fiscal year 13-14, the total expenditures for the Office were \$205,000, and there were 3.5 full-time equivalent employees in the Office. The total revenue collected for the issuance of Rulings was \$5,000.

What Activity Is There?

From fiscal year 09-10 to 13-14, the Executive Director issued a total of 47 Rulings and 79 Letters.

KEY RECOMMENDATIONS

Continue the issuance of Private Letter Rulings and General Information Letters for nine years, until 2025.

By issuing Rulings and Letters, the Executive Director provides taxpayers with clarity on their tax liability. Otherwise, a taxpayer may not collect the correct taxes at the point of sale and remit its own taxes correctly, and the taxpayer may only discover during an audit that the state interprets the law differently. However, the taxpayer would still owe the outstanding taxes and would also be required to pay additional penalties and interest. By reducing the uncertainty of tax consequences, these determinations are facilitating business transactions in the state. Therefore, the General Assembly should continue the issuance of Rulings and Letters for nine years, until 2025.

METHODOLOGY

As part of this review, staff at the Department of Regulatory Agencies interviewed Department staff, reviewed Department records, interviewed officials with state and national associations, interviewed stakeholders and officials from other states, reviewed Colorado statutes and rules, and reviewed the laws of other states.

MAJOR CONTACTS MADE DURING THIS REVIEW

Colorado Association of Commerce and Industry
Colorado Department of Revenue
Colorado Society of CPAs
Deloitte
Ernst and Young
Eide Bailley
Colorado Bar Association, Taxation Section
Arizona Department of Revenue
Kansas Department of Revenue
New Mexico Department of Revenue
Wyoming Department of Revenue

What is a Sunset Review?

A sunset review is a periodic assessment of state boards, programs, and functions to determine whether they should be continued by the legislature. Sunset reviews focus on creating the least restrictive form of regulation consistent with protecting the public. In formulating recommendations, sunset reviews consider the public's right to consistent, high quality professional or occupational services and the ability of businesses to exist and thrive in a competitive market, free from unnecessary regulation.

Sunset Reviews are prepared by:
Colorado Department of Regulatory Agencies
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Background

Introduction

Enacted in 1976, Colorado's sunset law was the first of its kind in the United States. A sunset provision repeals all or part of a law after a specific date, unless the legislature affirmatively acts to extend it. During the sunset review process, the Department of Regulatory Agencies (DORA) conducts a thorough evaluation of such programs based upon specific statutory criteria¹ and solicits diverse input from a broad spectrum of stakeholders including consumers, government agencies, public advocacy groups, and professional associations.

Sunset reviews are based on the following statutory criteria:

- Whether regulation by the agency is necessary to protect the public health, safety and welfare; whether the conditions which led to the initial regulation have changed; and whether other conditions have arisen which would warrant more, less or the same degree of regulation;
- If regulation is necessary, whether the existing statutes and regulations establish the least restrictive form of regulation consistent with the public interest, considering other available regulatory mechanisms and whether agency rules enhance the public interest and are within the scope of legislative intent;
- Whether the agency operates in the public interest and whether its operation is impeded or enhanced by existing statutes, rules, procedures and practices and any other circumstances, including budgetary, resource and personnel matters;
- Whether an analysis of agency operations indicates that the agency performs its statutory duties efficiently and effectively;
- Whether the composition of the agency's board or commission adequately represents the public interest and whether the agency encourages public participation in its decisions rather than participation only by the people it regulates;
- The economic impact of regulation and, if national economic information is not available, whether the agency stimulates or restricts competition;
- Whether complaint, investigation and disciplinary procedures adequately protect the public and whether final dispositions of complaints are in the public interest or self-serving to the profession;
- Whether the scope of practice of the regulated occupation contributes to the optimum utilization of personnel and whether entry requirements encourage affirmative action;

¹ Criteria may be found at § 24-34-104, C.R.S.

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- Whether the agency through its licensing or certification process imposes any disqualifications on applicants based on past criminal history and, if so, whether the disqualifications serve public safety or commercial or consumer protection interests. To assist in considering this factor, the analysis prepared pursuant to subparagraph (i) of paragraph (a) of subsection (8) of this section shall include data on the number of licenses or certifications that were denied, revoked, or suspended based on a disqualification and the basis for the disqualification; and
 - Whether administrative and statutory changes are necessary to improve agency operations to enhance the public interest.

Types of Regulation

Consistent, flexible, and fair regulatory oversight assures consumers, professionals and businesses an equitable playing field. All Coloradans share a long-term, common interest in a fair marketplace where consumers are protected. Regulation, if done appropriately, should protect consumers. If consumers are not better protected and competition is hindered, then regulation may not be the answer.

As regulatory programs relate to individual professionals, such programs typically entail the establishment of minimum standards for initial entry and continued participation in a given profession or occupation. This serves to protect the public from incompetent practitioners. Similarly, such programs provide a vehicle for limiting or removing from practice those practitioners deemed to have harmed the public.

From a practitioner perspective, regulation can lead to increased prestige and higher income. Accordingly, regulatory programs are often championed by those who will be the subject of regulation.

On the other hand, by erecting barriers to entry into a given profession or occupation, even when justified, regulation can serve to restrict the supply of practitioners. This not only limits consumer choice, but can also lead to an increase in the cost of services.

There are also several levels of regulation.

Licensure

Licensure is the most restrictive form of regulation, yet it provides the greatest level of public protection. Licensing programs typically involve the completion of a prescribed educational program (usually college level or higher) and the passage of an examination that is designed to measure a minimal level of competency. These types of programs usually entail title protection - only those individuals who are properly licensed may use a particular title(s) - and practice exclusivity - only those individuals who are properly licensed may engage in the particular practice. While these requirements can be viewed as barriers to entry, they also afford the highest level of consumer protection in that they ensure that only those who are deemed competent may practice and the public is alerted to those who may practice by the title(s) used.

Certification

Certification programs offer a level of consumer protection similar to licensing programs, but the barriers to entry are generally lower. The required educational program may be more vocational in nature, but the required examination should still measure a minimal level of competency. Additionally, certification programs typically involve a non-governmental entity that establishes the training requirements and owns and administers the examination. State certification is made conditional upon the individual practitioner obtaining and maintaining the relevant private credential. These types of programs also usually entail title protection and practice exclusivity.

While the aforementioned requirements can still be viewed as barriers to entry, they afford a level of consumer protection that is lower than a licensing program. They ensure that only those who are deemed competent may practice and the public is alerted to those who may practice by the title(s) used.

Registration

Registration programs can serve to protect the public with minimal barriers to entry. A typical registration program involves an individual satisfying certain prescribed requirements - typically non-practice related items, such as insurance or the use of a disclosure form - and the state, in turn, placing that individual on the pertinent registry. These types of programs can entail title protection and practice exclusivity. Since the barriers to entry in registration programs are relatively low, registration programs are generally best suited to those professions and occupations where the risk of public harm is relatively low, but nevertheless present. In short, registration programs serve to notify the state of which individuals are engaging in the relevant practice and to notify the public of those who may practice by the title(s) used.

Title Protection

Finally, title protection programs represent one of the lowest levels of regulation. Only those who satisfy certain prescribed requirements may use the relevant prescribed title(s). Practitioners need not register or otherwise notify the state that they are engaging in the relevant practice, and practice exclusivity does not attach. In other words, anyone may engage in the particular practice, but only those who satisfy the prescribed requirements may use the enumerated title(s). This serves to indirectly ensure a minimal level of competency - depending upon the prescribed preconditions for use of the protected title(s) - and the public is alerted to the qualifications of those who may use the particular title(s).

Licensing, certification and registration programs also typically involve some kind of mechanism for removing individuals from practice when such individuals engage in enumerated proscribed activities. This is generally not the case with title protection programs.

Regulation of Businesses

Regulatory programs involving businesses are typically in place to enhance public safety, as with a salon or pharmacy. These programs also help to ensure financial solvency and reliability of continued service for consumers, such as with a public utility, a bank or an insurance company.

Activities can involve auditing of certain capital, bookkeeping and other recordkeeping requirements, such as filing quarterly financial statements with the regulator. Other programs may require onsite examinations of financial records, safety features or service records.

Although these programs are intended to enhance public protection and reliability of service for consumers, costs of compliance are a factor. These administrative costs, if too burdensome, may be passed on to consumers.

Sunset Process

Regulatory programs scheduled for sunset review receive a comprehensive analysis. The review includes a thorough dialogue with agency officials, representatives of the regulated profession and other stakeholders. Anyone can submit input on any upcoming sunrise or sunset review via DORA's website at: www.dora.colorado.gov/opr.

The functions of the Executive Director of the Colorado Department of Revenue (Executive Director and Department, respectively) as enumerated in Section 103.5 of Article 35 of Title 24, Colorado Revised Statutes (C.R.S.), shall terminate on September 1, 2016, unless continued by the General Assembly. During the year prior to this date, it is the duty of DORA to conduct an analysis and evaluation of the issuance of Private Letter Rulings (Rulings) and General Information Letters (Letters) by the Executive Director pursuant to section 24-34-104, C.R.S.

The purpose of this review is to determine whether the currently prescribed program to issue Rulings and Letters should be continued and to evaluate the performance of the Executive Director and the staff. During this review, the Executive Director must demonstrate that issuing Rulings and Letters serves the public interest. DORA's findings and recommendations are submitted via this report to the Office of Legislative Legal Services.

Methodology

As part of this review, DORA staff interviewed Department staff, reviewed Department records, interviewed officials with state and national associations, interviewed stakeholders and officials from other states, reviewed Colorado statutes and rules, and reviewed the laws of other states.

Profile of Private Letter Rulings and General Information Letters

State taxes are necessary in order to raise revenue to fund public services, such as building and maintaining highways and ensuring public safety. Each state has a taxing authority that audits and adjusts tax returns, and every state imposes penalties on taxpayers for failure to file tax returns or pay taxes when due. States also impose interest charges on late payments.

In Colorado, in order to determine how much tax is owed to the state, a taxpayer may refer to statutes, rules, tax forms and other publications issued by the Department. When a tax issue is not specifically addressed in law or in publications issued by the Department, a taxpayer may request a Ruling or a Letter.²

A Ruling is a binding determination of tax liability related to a specific transaction. A Letter, on the other hand, is a non-binding determination that addresses a general question about tax issues.³

Both Rulings and Letters provide taxpayers with a greater understanding of their tax liability in advance of entering into a transaction or filing taxes for a completed transaction. Rulings are often requested when taxpayers are negotiating a business transaction and they require guidance from the state on a particular issue. Rulings help taxpayers understand the risks associated with specific transactions.⁴ When a binding determination is not required, a taxpayer may instead opt for a Letter.⁵

In Colorado, taxpayers may request a Ruling or a Letter for any tax that is paid to the state.⁶

Forty-six states and the District of Columbia issue Rulings, and 33 states, including Colorado, make redacted versions of Rulings available to the public.

² Colorado Department of Revenue. *Letter Rulings*. Retrieved on December 5, 2014, from <https://www.colorado.gov/pacific/tax/letter-rulings>

³ Colorado Department of Revenue. *Letter Rulings*. Retrieved on December 5, 2014, from <https://www.colorado.gov/pacific/tax/letter-rulings>

⁴ Tax Analysts. *Transparency in State Taxation, Part 2: Legislative Process and Letter Rulings*. Retrieved on December 5, 2014, from

<http://www.taxanalysts.com/www/features.nsf/Articles/6C1EBF2539E2824285257A130057FEF5?OpenDocument>

⁵ Tax Analysts. *Transparency in State Taxation, Part 2: Legislative Process and Letter Rulings*. Retrieved on December 5, 2014, from

<http://www.taxanalysts.com/www/features.nsf/Articles/6C1EBF2539E2824285257A130057FEF5?OpenDocument>

⁶ Colorado Department of Revenue. *Letter Rulings*. Retrieved on December 5, 2014, from <https://www.colorado.gov/pacific/tax/letter-rulings>

Legal Framework

History of Regulation

In 2006, the General Assembly granted the Executive Director of the Colorado Department of Revenue (Executive Director and Department, respectively) the authority to issue binding opinions to taxpayers with questions regarding specific tax events. Before this time, the Executive Director could only issue non-binding opinions.

The issuance of binding opinions was cash funded, and in order to ensure transparency, House Bill 06-1312 established that binding and non-binding opinions issued by the Department would be public information, except that the name of the requesting taxpayer and any other identifying information would be redacted, and the request and supporting documentation would also remain confidential.

In 2011, the General Assembly continued the issuance of binding and non-binding opinions by the Executive Director following a sunset review.

Legal Summary

The Executive Director of the Department, or his or her designee, is charged with promulgating rules to establish the process to issue Private Letter Rulings (Rulings) and General Information Letters (Letters).⁷

A Ruling is a written determination issued by the Executive Director to a taxpayer regarding the tax consequences of a specific transaction that is made in response to a written request.⁸ A Letter is a non-binding statement issued by the Executive Director to a taxpayer in response to a written request.⁹

The Executive Director will issue Rulings and Letters on a broad range of subjects that involve an interpretation of tax law, the applicability of tax to a given set of facts, a taxpayer's tax status or procedural issues.¹⁰

To obtain a Letter, a taxpayer is required to mail a request that includes a reasonable description of the facts and identification of the issues. While citations to statutes and legal authority may be included, the Executive Director does not require them. The Executive Director does not charge a fee to issue a Letter.¹¹

A Ruling request is more comprehensive than a Letter request.¹²

⁷ § 24-35-103.5(2), C.R.S.

⁸ § 24-35-103.5(1)(b), C.R.S.

⁹ § 24-35-103.5(1)(a), C.R.S.

¹⁰ 1 CCR § 201-1-3(a), Taxpayer Service Division Rules.

¹¹ 1 CCR § 201-1-4, Taxpayer Service Division Rules.

¹² 1 CCR § 201-1-4, Taxpayer Service Division Rules.

In order to obtain a Ruling, a taxpayer must submit to the Department:¹³

- A statement requesting a Ruling;
- A complete and detailed statement of all the relevant facts;
- A discussion of the business reasons for the transaction;
- A discussion of all the relevant issues underlying the request for a transaction;
- Copies of all the relevant documents;
- A statement that the issue or a similar issue is not being considered by the Department or the Internal Revenue Service (IRS) in connection with an active examination, audit of the taxpayer or a related party; and
- A statement of whether a similar request has been made to the IRS or another taxing jurisdiction, including a copy of the request and the ruling, if issued.

The Executive Director is authorized to establish fees, by rule, to cover the direct and indirect costs of issuing Rulings.¹⁴

During the initial request for a Ruling, the taxpayer is not required to disclose the taxpayer's identity.¹⁵ However, for a formal Ruling to be issued, once the taxpayer receives a draft of the Ruling, the taxpayer must:

- Submit a request signed by the taxpayer, or authorized representative, using language specified in rule attesting that the facts and representations in the request are true, correct and complete;¹⁶
- Disclose the taxpayer's name, address, tax identification number, telephone numbers and email addresses;¹⁷ and
- Supplement the request with any other statements, facts, arguments and citations of facts not previously disclosed.¹⁸

The Executive Director may request additional information from the taxpayer before issuing a final Ruling.¹⁹

A taxpayer may withdraw a request any time prior to the issuance of the Ruling.²⁰

¹³ 1 CCR § 201-1-4, Taxpayer Service Division Rules.

¹⁴ § 24-35-103.5(6), C.R.S.

¹⁵ 1 CCR § 201-1-4(b)(x), Taxpayer Service Division Rules.

¹⁶ 1 CCR § 201-1-4(d), Taxpayer Service Division Rules.

¹⁷ 1 CCR § 201-1-4(b)(x), Taxpayer Service Division Rules.

¹⁸ 1 CCR § 201-1-4(c), Taxpayer Service Division Rules.

¹⁹ 1 CCR § 201-1-4(e), Taxpayer Service Division Rules.

²⁰ 1 CCR § 201-1-8, Taxpayer Service Division Rules.

The Executive Director must issue a Ruling within 90 days or decline to issue a Ruling within 30 days of receiving a written request.²¹

The Executive Director may decline a Ruling or Letter for the following reasons:²²

- An issue is closely related to an issue before the Department or the IRS in connection with an examination or audit of the taxpayer;
- An issue is pending appeal with the tax conferee, the Executive Director or the courts;
- A matter involves the tax consequence of any proposed federal, state or local legislation;
- A request is related to the application of a requirement of the tax law concerning "reasonable," "good cause," "good faith" or another similar standard;
- A request concerns whether a proposed transaction would subject the taxpayer to civil fraud or criminal penalty;
- An issue involves the application of a question of fact, such as valuation;
- The factual scenarios require documentation or facts so voluminous as to be onerous to resolve, such as questions of "business purpose" and "economic substance";
- An issue involves federal law or state constitutional law; or
- An issue is raised by a business, trade or industrial association, or another similar group that relates to the members' or constituency's tax status or liability.

The Executive Director may decline a Ruling or Letter request when the Department lacks the resources to prepare a response. In this case, the Department will issue a notice on its website.²³ The Executive Director may also decline to issue a Ruling or Letter if it determines that it would not be in the best interests of the state.²⁴

Neither a Ruling nor a Letter is binding on the taxpayer. However, a Ruling is binding on the Department, unless the Ruling is revoked or modified,²⁵ and a Ruling or Letter may be used as evidence relevant to the assessment of penalties and other issues of good faith.²⁶

A taxpayer does not have the right to appeal a Ruling or a Letter.²⁷

²¹ § 24-35-103.5(3), C.R.S.

²² 1 CCR § 201-1-3, Taxpayer Service Division Rules.

²³ 1 CCR § 201-1-3(c), Taxpayer Service Division Rules.

²⁴ 1 CCR § 201-1-3(d), Taxpayer Service Division Rules.

²⁵ 1 CCR § 201-1-10(a), Taxpayer Service Division Rules.

²⁶ 1 CCR § 201-1-12, Taxpayer Service Division Rules.

²⁷ 1 CCR § 201-1-11, Taxpayer Service Division Rules.

A Ruling must be either revoked or modified in any of the following cases:²⁸

- The Ruling is determined to be in error by the Department,
- Legislation or rules are adopted that contradict the tax determination in the Ruling, or
- The Colorado Court of Appeals or the Colorado Supreme Court issues a contrary decision.

Rulings and Letters do not constitute a tax policy change in relation to section 20(4)(a) of Article X of the Constitution of the State of Colorado.²⁹

The Department will, at its own discretion, make Rulings and Letters available to the public.³⁰ A taxpayer may file objections to a redacted version of a Ruling or Letter prior to its publication. However, the Department retains the authority to make the final determination regarding the public version of the Ruling or Letter.³¹

²⁸ 1 CCR § 201-1-10(c), Taxpayer Service Division Rules.

²⁹ § 24-35-103.5(4), C.R.S.

³⁰ 1 CCR § 201-1-14(b), Taxpayer Service Division Rules.

³¹ 1 CCR § 201-1-13(d), Taxpayer Service Division Rules.

Program Description and Administration

The Executive Director of the Department of Revenue (Executive Director and Department, respectively), or his or her designee, is charged with issuing Private Letter Rulings (Rulings) and General Information Letters (Letters).

The Office of Tax Policy and Analysis (Office) in the Division of Taxation (Division) is responsible for receiving Ruling and Letter requests and conducting the analysis for the Executive Director. In addition to issuing Rulings and Letters, the Office reviews and writes all tax regulations for the Division, provides general tax guidance to the public, and reviews legislation. The Office also provides guidance and responds to questions from legislators, legislative staff and employees within the Division.

Table 1 illustrates the total expenditures for the Office, the total revenue collected for Rulings, and the full-time equivalent (FTE) employees in the Office. No revenue is collected for Letters.

Table 1
Agency Fiscal Information

Fiscal Year	Total Expenditures*	Rulings Revenue	Office FTE
09-10	\$122,158	\$6,000	2.0
10-11	\$122,158	\$7,000	2.3
11-12	\$156,682	\$4,500	2.7
12-13	\$185,052	\$8,500	3.0
13-14	\$205,000	\$5,000	3.5

*The Total Expenditures column reflects the total expenditures for the Office, including but not limited to Rulings and Letters.

The Office does not track the hours or the FTE dedicated to issuing Rulings and Letters. The amount of time necessary to issue a Ruling or a Letter varies depending on the complexity of the tax issues involved, so it is difficult to determine the workload dedicated to Rulings and Letters for each fiscal year.

The issuance of Rulings is cash funded, but the Office, which has a much broader mandate, is financed by the General Fund.

In fiscal year 11-12, the revenue was significantly lower than in the previous two years. In part, this may be due to staffing changes. Also, the revenue from Rulings fluctuates depending on the amount of time staff estimates it will require to complete Rulings, and a Ruling may not necessarily be issued during the same fiscal year that payment is received.

Table 2 shows the fee structure for Rulings.

**Table 2
Fee Tiers**

Tier	Fees	Hours
First	\$500	Any
Second	\$1,000	20
Third	\$2,500	50
Fourth	\$5,000	100
Fifth	\$7,000	140
Sixth	\$10,000	200

The base fee of \$500 is charged on all Rulings. In order to determine the fee tier, the Office evaluates the request and estimates the amount of time necessary to complete the Ruling. Then it multiplies the number of hours by \$50. Once the fee tier is set, the Office will not alter the fee tier unless it uncovers material facts that require additional analysis.

Over five fiscal years, the Office charged \$500 for nearly all Rulings. It charged the second tier fee of \$1,000 for only a few Rulings and did not charge above the second tier during any of the years reported.

Ruling and Letter Activity

In order to obtain a Ruling, a taxpayer must submit a request along with specific information and documentation required by the Executive Director. Upon receiving a request for a Ruling and payment of the base fee, the Office estimates the amount of time it will take to perform an analysis of the tax issue and notifies the taxpayer of the fee tier. Then the Office performs an analysis and sends the taxpayer a draft of the Ruling.

A taxpayer is only required to disclose its identity in order to move forward once a draft of the Ruling has been issued to the taxpayer.

In order to obtain a Letter, a taxpayer simply submits a request outlining the reason for the request. A taxpayer is not required to disclose its identity for a Letter.

The Executive Director must issue a Ruling within 90 days of receiving a completed request. No statutory deadline has been established for issuing Letters. However, it is the policy of the Executive Director to issue a Letter within 120 days of receiving a request.

Table 3 provides the number of Rulings and Letters issued by the Executive Director over the five fiscal years indicated.

Table 3
Number of Rulings and Letters Issued

Fiscal Year	Rulings	Letters	Total
09-10	4	7	11
10-11	11	15	26
11-12	11	8	19
12-13	9	22	31
13-14	12	27	39

The number of Rulings and Letters the Executive Director issues varies from year to year depending on the economic activity in the state and changes to tax law. Most Rulings and Letters concern tax issues related to sales and use tax. Otherwise, they generally question whether a company is subject to income tax in the state.

The Executive Director may decline a Ruling or a Letter request for several reasons, such as the Department lacks the resources to issue a Ruling or the Executive Director determines issuing a Ruling would not be in the best interests of the state. However, the Executive Director attempts to fulfill all Ruling and Letter requests, if possible.

Table 4 provides the number of Rulings and Letters declined by the Executive Director over a five-year period.

Table 4
Number of Rulings and Letters Declined

Fiscal Year	Rulings	Letters	Total
09-10	2	49	51
10-11	0	17	17
11-12	0	5	5
12-13	1	4	5
13-14	0	4	4

The number of Rulings and Letters declined varies considerably over the five-year period, but these numbers seem to have stabilized between fiscal year 11-12 and fiscal year 13-14. In fiscal year 09-10, the Office was not sufficiently staffed to fulfill all of the requests.

The Executive Director may modify a Ruling if a taxpayer requests a modification after the Ruling has been issued and the Executive Director agrees to the modification. The Executive Director only modifies Letters when they are found to be inaccurate.

Table 5 provides the number of Rulings and Letters that were modified by the Executive Director after they were issued.

Table 5
Number of Rulings and Letters Modified

Fiscal Year	Rulings	Letters	Total
09-10	0	1	1
10-11	0	1	1
11-12	0	0	0
12-13	0	1	1
13-14	3	5	8

While the Executive Director occasionally modifies a Letter, it is unusual for the Executive Director to modify a Ruling. However, in fiscal year 13-14, the Executive Director modified three Rulings and five Letters following changes in law and a court ruling.

If a taxpayer does not agree with a Ruling for any reason, it may withdraw the request prior to the Executive Director issuing it.

Table 6 shows the number of Rulings and Letters that were withdrawn by the taxpayer prior to the Executive Director issuing them.

Table 6
Number of Ruling and Letter Requests Withdrawn

Fiscal Year	Rulings	Letters	Total
09-10	1	1	2
10-11	4	0	4
11-12	2	0	2
12-13	3	0	3
13-14	0	0	0

It is not unusual for a taxpayer to withdraw a Ruling request, but taxpayers rarely withdraw Letter requests. This may be due to the fact that taxpayers must disclose their identity for Rulings, and Rulings may be used by the Department as evidence relevant to the assessment of penalties and other issues of good faith.

Collateral Consequences – Criminal Convictions

Section 24-34-104(9)(b)(VIII.5), Colorado Revised Statutes, requires the Department of Regulatory Agencies to determine whether the agency under review, through its licensing processes, imposes any disqualifications on applicants or licensees based on past criminal history, and if so, whether the disqualifications serve public safety or commercial or consumer protection interests.

This provision is not relevant to the issuance of Letters or Rulings.

Analysis and Recommendations

Recommendation 1 – Continue the issuance of Private Letter Rulings and General Information Letters for nine years, until 2025.

The Executive Director of the Colorado Department of Revenue (Executive Director and Department, respectively) issues Private Letter Rulings (Rulings) and General Information Letters (Letters) as authorized in section 24-35-103.5, Colorado Revised Statutes, (Act).

A Ruling is a binding determination of tax liability related to a specific transaction. A Letter is a non-binding determination that addresses a general question from a taxpayer about a tax issue.³²

In a sunset review, the Department of Regulatory Agencies must determine whether a program or function of government is necessary to protect the public health, safety and welfare.

Sometimes, there is no way of interpreting the statutes and regulations without guidance from the state. It is critical for a taxpayer to have certainty about tax questions. Otherwise, the taxpayer may only find out during an audit that the state interprets the law differently than the taxpayer.

Most Ruling and Letter requests concern issues related to sales tax. With sales tax, when a taxpayer interprets the law differently from the state, the taxpayer almost certainly will not collect the correct taxes at the point of sale, but the tax is still due. When an audit uncovers a taxpayer who did not pay the state what it is owed, then the taxpayer must pay the outstanding taxes in addition to penalties and interest.

The state creates the tax law, and it enforces it. If the laws are unclear, it is only reasonable for the state to provide the guidance necessary so that taxpayers understand how much tax to collect and pay.

Rulings and Letters, along with other forms of guidance, are important because they provide taxpayers with clarity on tax law, and the Department should continue to provide them.

Moreover, Rulings and Letters have the potential to drive economic activity. By reducing the uncertainty of tax consequences, these determinations are facilitating business transactions in the state.

³² Colorado Department of Revenue. *Letter Rulings*. Retrieved on December 5, 2014, from <https://www.colorado.gov/pacific/tax/letter-rulings>

Few issues were identified during the sunset review, so a nine-year continuation is reasonable.

Therefore, General Assembly should continue the issuance of Rulings and Letters for nine years, until 2025.

Administrative Recommendation 1 – The Executive Director should establish a flat fee for all Rulings.

The Act requires the Executive Director to establish by rule reasonable fees to issue Rulings.

In rule, the Executive Director has established a tiered fee schedule in which there are six tiers ranging from \$500 to \$10,000.

In order to determine the fee tier, staff in the Office of Tax Policy Analysis (Office) in the Division of Taxation evaluates the request and estimates the amount of time necessary to complete the Ruling, and then it multiplies the number of hours by \$50. For example, if the Office estimates a Ruling may take 20 hours to complete, the fee will fall in the second tier, which is set at \$1,000.

Sunset criteria question whether the agency's operation is impeded by existing statutes, rules, procedures, practices and any other circumstances, including budgetary, resource and personnel matters.

Over the five fiscal years analyzed for this sunset review, the Office charged the base fee of \$500 for nearly all Rulings, and it did not charge above the second tier during any of the years reported.

Considering this, the tiered system of fees seems unnecessarily complicated.

There is also evidence that the Office may be underestimating the amount of time necessary to complete a Ruling and, consequently, undercharging. The problem with undercharging for Rulings is that the issuance of binding determinations is intended to be cash funded. The Office is otherwise funded by the General Fund, so when the Office does not adequately charge for Rulings, all taxpayers essentially subsidize the issuance of Rulings through the General Fund.

There are several options to address this issue.

One option would be for the General Assembly to repeal the requirement to charge for Rulings. It would be reasonable to pay for the cost of issuing Rulings through the General Fund, since binding determinations provide value to the public beyond the individual taxpayer who requests one. However, stakeholders value the ability to obtain binding determinations, and they recognize that establishing a cash-funded program safeguards their continued issuance.

Another option would be for the Executive Director to eliminate the tiered system and simply allow the Office to estimate the amount of time it will take to complete a Ruling and multiply the time by an hourly rate. The problem with this solution is that it is difficult for the Office to determine in advance how much time a single Ruling may take. The Office has struggled with this since it began issuing Rulings, nine years ago. While this solution is simpler than the tiered system, it does not resolve the problem of undercharging for Rulings.

Finally, the Executive Director could establish a single fixed fee. Rather than assess the cost of a Ruling for each separate request, the Office could assess the historical costs over a period of time and estimate future costs. It would then be able to establish a reasonable fee that could be charged for each Ruling request, regardless of the time spent to issue an individual Ruling.

On average, the Office received requests for about twelve Rulings a year over the most recent three fiscal years. If the Office tracked the time spent on each Ruling, then it would be able to adjust the fee when setting the annual budget. While the amount of time required may differ depending on individual Rulings, the Office should be able to estimate future activity and develop a fee sufficient to cover the annual costs.

The consensus among stakeholders is that the \$500 to \$1,000 fee that the Office has historically charged is fair for a binding determination on a complex area of tax law. Taxpayers that seek binding determinations are generally considering sizeable transactions, and the fee is minor in comparison. Moreover, there is always a concern that the Office could charge as much as \$10,000 for a Ruling. Establishing a single fee would eliminate this uncertainty.

In fact, other states, such as Alabama, North Carolina and Tennessee, that charge a fee for Rulings have established a flat fee.

Additionally, setting a single fixed fee would be more efficient since it would decrease the amount of time staff spends on estimating the cost for each individual Ruling. It would also increase the likelihood that the Office is adequately funded.

For these reasons, the Executive Director should establish a flat fee for all Rulings.