View metadata, citation and similar papers at core.ac.uk

brought to you by CORE

provided by Case Western Reserve University School of Law

Case Western Reserve University
School of Law Scholarly Commons

Faculty Publications

1996

Model Codes and Tax Technical Assistance: Note on the Revised Edition of the Basic World Tax Code and Commentary

Richard K. Gordon
Case Western Reserve University School of Law, richard.gordon@case.edu

Follow this and additional works at: https://scholarlycommons.law.case.edu/faculty_publications

Part of the Taxation-Transnational Commons

Repository Citation

Gordon, Richard K., "Model Codes and Tax Technical Assistance: Note on the Revised Edition of the Basic World Tax Code and Commentary" (1996). *Faculty Publications*. 524.
https://scholarlycommons.law.case.edu/faculty_publications/524

This Article is brought to you for free and open access by Case Western Reserve University School of Law Scholarly Commons. It has been accepted for inclusion in Faculty Publications by an authorized administrator of Case Western Reserve University School of Law Scholarly Commons.

Tax Policy Forum

Model Codes and Tax Technical Assistance: Note on the Revised Edition of the Basic World Tax Code and Commentary

by Richard K. Gordon[1]

Richard K. Gordon is an advisor in the Legal Department of the International Monetary Fund.

There is a long tradition of specific, detailed tax reform study in individual developing countries, written for the most part in the 1950s, 1960s, and 1970s. Each study was unique to the specific country and economy involved, as was each recommendation for reform. Few development finance specialists are unfamiliar with the highly detailed nature of the Shoup mission's work in Japan, Venezuela, Brazil, and Liberia, the Kaldor reports on India and Sri Lanka, or the Musgrave reports on Bolivia and Colombia.[2] If one includes the significant amount of scholarly work undertaken by non-market-oriented economists, the amount of research and writing was enormous.[3]

Of course, reform is only successful if the expert recommendations are implemented, but (even considering only the predominantly market-oriented reform efforts), somewhat less than complete reform was actually achieved.[4] There was often little agreement between the market-friendly experts and the interventionists as to what general principles should be followed regarding income tax policy. Among those who were relatively market-oriented, there appeared to be no belief in a quick fix. Fiscal systems, including direct taxation, had to be finely tailored to the specific economy involved. Some of the earlier scholarly reform studies went into great detail concerning such topics as how in-

[1]Nothing in this note should be interpreted as representing the ideas of anyone or anything except, perhaps, Richard Gordon.

[2]The published reports of the various Shoup, Kaldor, and Musgrave missions are still classics, and can be read and reread to great benefit. *See, e.g.*, Carl S. Shoup, *Report on Japanese Taxation,* 4 vols. (1949); Carl S. Shoup, John F. Due, Lyle C. Fitch, Donald MacDougal, Oliver S. Oldman, and Stanley S. Surrey, *The Fiscal System of Venezuela: A Report* (1959); Carl S. Shoup, Douglas Dosser, Rudolph Penner, and William S. Vickery, *The Tax System of Liberia* (1970); Nicholas Kaldor, *Indian Tax Reform, Report of a Survey* (1957); Nicholas Kaldor, *Suggestions for a Comprehensive Reform of Direct Taxation in Ceylon* (1960); Richard A. Musgrave and Malcolm Gillis, *Fiscal Reform for Colombia* (1971); Richard A. Musgrave, *Fiscal Reform in Bolivia* (1981).

[3]Not all the work was performed by foreign experts. In some countries, such as India, most studies were undertaken by local scholars following Kaldor's 1957 report, while in most cases there was input from resident experts. *See, e.g., Government of India, Report of the Taxation Enquiry Committee,* 1953-4 (1960) (3 vols.); *Government of India, Direct Taxes Enquiry Committee, Final Report* (1972). These reports are still worth skimming, if not rereading.

[4]Malcolm Gillis discusses the relative lack of success of many of the early reform missions in "Toward a Taxonomy for Tax Reform," in *Tax Reform in Developing Countries* 1-23 (Malcolm Gillis ed. 1989). *See also* the descriptions of the Venezuela, Brazil, and Liberia missions, as well as their relative lack of success in effecting actual change, in Carl S. Shoup, "Retrospective on Tax Missions to Venezuela (1959), Brazil (1964), and Liberia (1970)," in *Tax Reform in Developing Countries,* (Malcolm Gillis ed. 1989) at 252.

come taxes could effect specific resource allocation in a particular economy, or how unequal income distributions could be reduced. How microeconomic restructuring might effect macroeconomics, such as long-term growth, also was analyzed.[5]

Tax reform efforts prior to 1980 were a mere preamble to the rush that was to follow. The pace of reform began to accelerate after the debt crisis, when large numbers of developing countries were forced to seek major balance-of-payments assistance from multilateral lending institutions, such as the International Monetary Fund (IMF) and the World Bank. For example, fiscal reforms, including tax reforms, were frequently included as conditions for the disbursement of IMF upper credit tranches (and, incidentally, access to new IMF facilities). The collapse of Communism in Eastern Europe and the Soviet Union, and the nearly simultaneous collapse of their economies followed. The views of non-market-oriented economists became discredited. The adoption of adjustment programs in formerly closed economies, and of market economies in formerly centrally planned countries, resulted in a demand for an enormous number of significant changes in tax systems. Into the breach leapt a number of national aid agencies and international organizations, which provided experts to work with governments in designing reforms.[6]

Given the huge increase in demand for technical assistance, and the often pressing time constraints of many countries, it is not surprising that the individualized attention of a group of scholars such as the Shoup or Musgrave missions has not always been possible. However, it also has been increasingly accepted that such detail may no longer be necessary. Instead of a gaggle of scholars (often from the first world) undertaking massive studies of local economies, more often tax reform missions have become a combination of a single or relatively small number of long-term resident technical assistance advisors, followed up with short technical assistance missions by experts. The resident advisors are not necessarily senior scholars, but are frequently younger, and therefore somewhat less experienced.[7] In the 1990s, both resident advisors and tax reform missions have concentrated less on in-depth studies of the local economy, laws, and culture of a country, and more on the nuts and bolts of what taxes might raise sufficient revenue to meet government expenditure. In other words, experts have focused on how a basic set of taxes might be drafted, enacted, and implemented quickly and effectively, instead of conducting more detailed microeconomic work.[8] Quite often, expert tax reform proposals have been put in place in their entirety, frequently with surprising speed.[9]

Reform is successful only if the expert recommendations are implemented, but (even considering only the predominantly market-oriented reform efforts), somewhat less than complete reform was actually achieved.

The reasons for this relative change, or evolution, are probably a combination of the massive increase in demand for technical assistance, plus the often exceptionally pressing nature of fiscal reform.[10] Perhaps even more important has been an intellectual evolution in tax policy. Non-market-oriented economists have been discredited, and market-oriented development practitioners have reached considerable agreement not only on some basic principles of taxation, but also on the fact that those principles apply, by and large, to most situations. This agreement has been reached not only among scholars, but also among providers of international assistance, and among officials in

[5]While each report cited above delves specifically into these issues in the context of the country involved, it is an overstatement to say that they were unique to the specific set of circumstances. It is also true that many general principles of taxation were being hashed out in these scholarly compendia.

[6]*See* Richard K. Gordon, "Privatization and Legal Development," 13 *Boston University International Law Journal* 367, 367-8 (1995).

[7]As with everything written here, this broad generalization often is not applicable in specific cases.

[8]Once again, this statement is only a broad generalization, and much detailed scholarly work has been undertaken in certain instances. The material prepared for Colombian tax reform in the later 1980s is a good example. *See* Charles E. McLure Jr., Jack Mutti, Victor Thuronyi, and George Zodrow, *The Taxation of Income from Business and Capital in Colombia* (1990). In other cases, tax reform has taken place in the context of general fiscal reform, which itself has generated a considerable amount of scholarly study. The ongoing work carried out on behalf of the government of Indonesia by the Harvard Institute for International Development is another fine example.

[9]This often has been true in the former Soviet Union and in a number of African countries. However, an example to the contrary is the comprehensive Indonesian reform of the early 1980s, which continues even today, and which entailed both years of in-depth study followed by a relatively rapid, and nearly complete, adoption of reform proposals.

[10]In the definition of the term "pressing nature of reform" one would have to include structural adjustment programs whose financing depended, explicitly, on the adoption of tax reforms.

the target countries. Those involved in tax policy formulation now agree, with a fair degree of uniformity, that tax systems, instead of effecting resource allocation and income distribution in a particular economy, should instead aim at market neutrality. They have accepted that, with certain fairly explicit exceptions, rather than "encouraging" or "discouraging" certain types of behavior, the income tax system should collect revenue with a minimum of change in economic behavior. Scholars have accepted, to a large extent, that tax systems should not affect, as far as possible, the allocation of resources as determined by the market.

This change has occurred in both developed and developing countries. For example, income tax reform studies undertaken in the United States and New Zealand in the mid-1980s were enormously influential throughout the world. Those studies included overviews of basic, accepted economic principles concerning taxation, and then followed with specific proposals as to how to put those principles into effect. More recent studies have continued to follow this pattern.[11]

Of course, not every principle is agreed on among scholars and government officials. Disagreement still exists on a number of broad policy issues, for example, the savings disincentive of taxes on income from capital over taxes only on labor income (consumption taxes). There is also disagreement on many relatively technical points; for example, the method for taxing fringe benefits. However, in a surprising number of areas, principles of both direct and indirect taxation have been broadly accepted, making the process of tax reform far less contentious, and perhaps a bit easier.

One of the signs of the "new" tax reform movement in developing and transition countries has been a reduced emphasis on the specific analyses of development economists, and an increased emphasis on the crafting of legislation. Because many believe that economic principles and markets are quite similar worldwide, these rules may also have a greater transitivity, not only among different countries, but within a single country. Instead of having a series of tax provisions relating to "special" sectors or problems within a country, there has been a greater understanding that, at least with regard to principles, one size may more or less fit all.

The use of models can be highly beneficial in the creation of new laws. They can provide a checklist of issues that need to be to be addressed, as well as examples of how specific provisions might actually be drafted.

There is no doubt that the comparative use of provisions has a long history in the adoption of statutes in the developing world. Countries often adopted the laws of their colonial masters (or former masters) wholesale. Even absent such imitation, the drafting of new statutes has usually involved at least the examination of existing ones. One of the benefits of using existing tax codes to inform the creation of new ones is the ability to take into account the successes and mistakes of other jurisdictions. It makes sense to see what statutory provisions have been used elsewhere, whether they have worked or not, and the reasons for this. As greater uniformity as to tax principles has been reached, and as the private sector and the free market have taken an ever-increasing prominence, it has become easier to borrow from one jurisdiction to another. Such borrowing also seems to have acquired more acceptance among those involved in tax reform in developing countries.

The greater transitivity of world tax principles perceived by some has been partly responsible for the increased presence of "model" tax codes. A number of such evolving models are now used by experts in providing technical assistance. Some models are simply examples of tax reform statutes proposed or enacted in developing and transition countries. The first edition of Ward M. Hussey and Donald C. Lubick's *Basic World Tax Code and Commentary* (BWTC) is perhaps one of the most important of these models.[12] While I suspect that no model or sample code has yet been advanced as a universal solution for all needs, it is obvious that reference to them, be they actual legislation or more theoretical examples like the

[11]Good examples concerning company taxation are the OECD report, *Taxing Profits in a Global Economy* (1991); the European Commission Report of the Committee of Independent Experts on Company Taxation (Onno Rudding, Chairman: 1992); and the U.S. Treasury Department's report, *Integration of the Individual and Corporate Tax Systems: Taxing Business Income Once* (1992).

[12]The authors refer to the 1996 version as a "sample," as opposed to a model. BWTC, at 4. Presumably, they chose this word because they do not wish to imply that jurisdictions should think that this is the "only" model to which one should refer when drafting a law. See the discussion of this point *infra*. Unless otherwise noted, in this article the term "BWTC" refers to the revised, 1996 edition. *See* Ward M. Hussey and Donald C. Lubick, *Basic World Tax Code and Commentary: 1996 Edition*, sponsored by the Harvard University International Tax Program.

BWTC, has been an important element in the drafting of many new tax codes in transition and developing countries.

The use of models can be highly beneficial in the creation of new laws. They can provide checklists of issues that need to be addressed, as well as examples of how specific provisions actually might be drafted. In fact, existing drafts of legislative language, in the form of actual statutes or model laws, are absolutely essential tools in the technical assistance trade. On the other hand, excessive reliance on either existing statutes or model codes has a number of obvious flaws. Three of the most serious potential problems are the following:

- not all aspects of tax policy have been agreed on, even as a theoretical matter (different experts have different conclusions as to ideal types);
- even those policies that are generally accepted as a matter of theory may not be appropriate in a particular situation (every jurisdiction has its own unique economic, social, and political conditions); and
- the best legislative embodiment of even a single policy will differ depending on the particular situation (every jurisdiction is likely to have a unique legal and administrative style.)[13]

To make matters more difficult, virtually every existing law or model act makes technical errors; duplicating the model would duplicate those mistakes.

The 1996 edition of the BWTC is superior to the old version in two major respects: first, the authors have corrected a number of technical drafting flaws, and second, the introduction and commentary clarify that it is not intended to be used as a prepackaged statute to be enacted *in toto*. In fact, in the hands of economists and legal experts conversant in theories of taxation, comparative tax laws, and the practical aspects of drafting legislation, the BWTC can be a great help. These experts can use the BWTC, along with other models or "samples" and comparative legal materials to work with other experts familiar with the legal history of the jurisdiction, its economic and social structure, and its fiscal needs. Together, over time, and working as a group, these people can create a first-rate law, appropriate for the particular jurisdictions and largely free of technical glitches. I have little doubt that this is what Hussey and Lubick have intended; this has been the method by which Lubick, one of the most honorable and experienced tax experts it has ever been my good fortune to know, has directed the U.S. Treasury Department's tax technical assistance program. I also know that Hussey has been particularly catholic in his reference to comparative legal materials while performing technical assistance tasks in developing and transition countries.

It appears that the authors have dismissed the suggestion that a sample law should contain various alternative provisions.

However, my concerns lie primarily elsewhere. As I have described above, it is not always possible (in fact, it is somewhat unlikely, given time pressures and human resources constraints) for a diverse group of experts to work on the development of an appropriate tax law. This is why I worry about the publication of the BWTC as it now exists.[14] Perhaps it is less the exact content of the sample statutory provisions that worries me than the presentation.

A number of reviews of the preliminary edition complained that the presentation of a single draft law without alternative provisions "will only be of direct use to a country that agrees with every policy choice the authors have made."[15] In the preface to the 1996 edition, the authors, after first drawing attention to earlier criticism, state clearly that the purpose of their sample law is not, in fact, to provide a complete statute that should be enacted without change. Perhaps as an offer of proof, they go on to note (correctly) that as a practical matter it is unlikely for a sample law to be enacted without any changes.[16] While in the best of all possible worlds the BWTC could be used this way, I wonder whether this caveat might actually be a very tiny bit disingenuous. In fact, after disavowing the intent that the sample be used as a final draft for actual legislation, the authors go on to describe the BWTC as a "benchmark" for legislative reform endeavors.[17] Nor do they present any alternatives to the legislative provisions actually adopted as part of their "benchmark":

> [W]e were not, and are not, preparing a form book for tax

[13]*See* the discussion in Richard Vann, "Some Lessons from Hussey and Lubick," *Tax Notes Int'l,* July 26, 1993, p. 268.

[14]Although the BWTC continues to include a number of drafting errors, I will leave the correction of these to other commentators and to the authors themselves.

[15]Richard J. Vann, *supra* note 13, at 276. *See also* Richard K. Gordon, "Some Comments on the Basic World Tax Code and Commentary," *Tax Notes Int'l,* July 26, 1993, p. 279.

[16]BWTC at viii.

[17]*Id.*

legislation. Presenting a bewildering array of opinions impedes, and possibly precludes, the understanding by the user of an integrated whole. The number of changes in a unified draft that would result if one option were changed would be multiplied many times over if we attempted to show the effects of that changed option when coupled with each of the other options.[18]

First, this seems to mean that one really should not try to make any changes in the sample, and that in doing so the whole will cease to work, rather like a Rube Goldberg contraption. The only realistic alternative, at least as far as I can tell, is to adopt the sample law, now looking suspiciously like a model again, as a whole. Second, these sentences seem to suggest that one really cannot understand various legislative options concerning different policy matters except as part of an integrated whole. I cannot reconcile these two observations with another assertion by the authors: that with regard to tax legislation, and especially in reference to their sample code, "one size" does not fit all.[19]

Another possibility is simply that the authors believe that changes can be made to certain sections of their sample law, but that it would be too difficult to show exactly how these changes would be reflected in the rest of the sample. However, if this is their intent, they could write something like "a change in this section would have to be reflected and brought into agreement with other provisions in appropriate places throughout the rest of the sample law." This would make it clear that changes can be made in one part of the sample without causing the entire enterprise to fail, provided that due attention is paid.

It appears that the authors have dismissed the suggestion that a sample law should contain various alternative provisions. But if one were to accept the premise that a single unified law must be presented, the question arises, which provisions should be chosen, and how should they be drafted, to create this unified sample law? In effect, what should be the model for the "sample"? The authors were criticized in their preliminary edition because the draft statute they presented was too Anglo-Saxon, and more specifically, too American.[20]

It would be difficult (albeit not impossible) to import an Anglo-American-style model into a civil law legal tradition.

Apparently taking this criticism to heart, the authors respond in the 1996 edition that:

> [n]or does our sometimes use of 'Americanisms'—ways of expressing concepts in terminology used in the United States—carry any implication that the U.S. term of art is the *mot juste* in any one case. We thought of using terminology borrowed from France, Germany, the U.K. *et al.*, but realized that it would be rare that any of our terms would be enacted in English.[21]

While I suppose that I understand the authors' point, I do not think they were addressing the intent of the criticisms leveled at their earlier draft law. First, any jurisdiction is likely to have considerable preexisting laws and an embedded legal culture. The body of law will be composed not only of a tax code, but other relevant statutes, and is likely to include case law as well. In former colonies, the legal culture, and frequently the laws and cases themselves, may have been largely imported from the previous colonial ruler.

One example from income taxation (perhaps the most obvious) is the general distinction between those countries that use largely accounting-based income tax systems for business enterprise,[22] and those that tend to use non-accounting-based systems.[23] In the former case, found mostly outside the Anglo-American/Commonwealth world, there often are separate income tax rules for legal persons and physical persons, while in the latter case, often a single system applies to all. There are, of course, many other examples of differences between these two types. Examples abound wherein the BWTC adopts an exclusively Anglo-American/Commonwealth style.

It would be difficult (albeit not impossible) to import an Anglo-American-style model into a civil

---

[18] *Id.* Also found at *id* at 4.

[19] *Id.* at viii.

[20] *See, e.g.*, Brian J. Arnold, "International Aspects of the Basic World Tax Code," *Tax Notes Int'l,* July 26, 1993, p. 260; Richard J. Vann, *supra* note 13, at 274.

[21] BWTC at 6.

[22] Many former French colonies follow the French style in their income tax laws. *See, e.g., Code General des Impots* 1981 (Cote d'Ivoire). While many Eastern European countries have enacted new income tax laws since the fall of the Berlin wall, these laws often include provisions based on the accounting model. For one relatively more similar to the German example, *see, e.g.,* The Income Taxes Act (No. 586/1922 Coll.) (Z. Posustova *et al.* trasn., Trade Links 1993) (Czech Republic).

[23] Former British colonies typically maintain the Anglo-American style, whether they have gone through a recent reform (e.g., Income Tax Order 1993 (Lesotho)), or not (e.g., Income Taxes Act, 1961 (India)).

law legal tradition. In fact, the Indonesian income tax is, more or less, an example of this.[24] However, the question automatically is raised: why would one want to do so? Take, for example, the different styles of treating depreciation. The rules of the French, German, and other civil law jurisdictions tend to rely relatively more on general, financial accounting principles that apply, broadly speaking, to all or nearly all depreciable assets, while others, particularly those of the Anglo-American/Commonwealth jurisdictions, tend to have specific (and sometimes not entirely congruent) rules for definable, different categories of property. Apart from special incentive provisions, depreciation systems can be divided into three groups:

(1) those that base deductions primarily on useful life;

(2) those that use somewhat broader rules of thumb, but are also based primarily on useful lives; and

(3) those that use rules that appear to be largely arbitrary.

Those systems that use (1) may also provide guidance, either mandatory or suggested, as to what the useful lives of a range of properties are. Those that use (1) and (2) often provide acceleration for properties that appear to decline in value more quickly than straight-line depreciation suggests.

The French and German rules, though not identical, provide some of the purest examples of system (1). They are based primarily on some kind of estimate of the useful life of the particular property in question, with special provisions for unexpected or exceptional decreases in value. In the French case, for example, the useful life of the property is determined by financial accounting principles, although a 20 percent variance is permitted.[25] However, because the French system is based on an attempt to duplicate real decreases in value of the asset, extra depreciation can be taken on any property to reflect special wear, changes in technology, or even the market for the good,[26] and the depreciation deductions that are taken for tax purposes also must be taken for financial reporting purposes.[27] The German rule also bases depreciation primarily on the useful life of the property, although most useful lives are not determined strictly by financial accounting principles, in that the Ministry of Finance has listed recommended rates by category (machinery, office equipment, office furniture), and then more specifically by individual type.[28]

The 'simplified' depreciation system found in the BWTC is not accounting-based, but 'group'-based.

The British rules are a fairly good example of system (3) above, i.e., those that use rules that appear to be largely arbitrary. British depreciation rules are not based on useful lives, or on any other apparent estimation of actual decline in value. With only two rates available for all depreciable physical assets, it can be guaranteed that allowances do not approximate reality.[29] The U.S. statute is closer to (2): it puts most physical property into one of nine categories based on the property's useful life; three categories are based on rules of thumb, without any direct reference to useful lives: residential rental property, nonresidential real property, and railroad grading or tunnel bores.[30] Of course, reference to useful lives is indi-

[24] *See generally* Income Tax Law (Law 7 of 1983) (English translation, Ministry of Finance, Republic of Indonesia 1993) (Indonesia) (hereinafter "IND ITC").

[25] *Code Général des Impots* (France) [hereinafter "FRA CGI"] article 39-1-2o; *Direction général des Impots,* Précis de Fiscalité 1994 Par. 1083. Straight-line depreciation is then generally required for the property, including all nonphysical property, unless declining balance is specifically allowed. *See Direction général des Impots,* Précis de Fiscalit 1994 Par. 1083; FRA CGI Ann. II, article 24. Declining balance depreciation is allowed, although not required, for certain physical property, with the degree of declining balance depending on useful lives: 1.5 for useful lives of three to four years, 2.0 for five to six years, and 2.5 for six years or more. FRA CGI article 39A; FRA CGI Ann. II, article 22; FRA CGI Ann. II, article 24-2.

[26] Although reasonable proof would have to be provided. *Direction général des Impots,* Précis de Fiscalité 1994 Par. 1083.

[27] *Id.*, at Par. 1083.

[28] *Einkommensteuergesetz* 1990 BGBI I S. 1989 (Germany) [hereinafter "DEU EStG"] section 7. The tables, with useful lives and rates, are found in Afa-Tabellen, vom. 15 August 1957, in *Fassung der ersten bis driezehnten Ergdnzung.*

[29] Costs for industrial buildings, hotels, and dredging are all depreciated at 4 percent per year. Capital Allowances Act, 1986 (United Kingdom) [hereinafter "GBR CAA"] sections 3, 7, and 134. Costs for machinery and plant, motor vehicles, mining, patents, and copyrights are all depreciated at 25 percent per year. GBR CAA sections 24, 34, 67, 69, 70, 71, 72, 98, 105; Income and Corporation Tax Act 1988 (United Kingdom) [hereinafter "GBR ICTA"] section 520. However, a number of Commonwealth countries do not follow this model exactly. For example, the Australian statute is in some ways quite similar to the U.K. one, while it departs radically from it in others. Although the Australian law does not specify that a useful life must be determinable, depreciation for the costs of physical property is based on the effective life of the unit. Depreciation is allowed only for costs of "plant or articles" and a "unit of industrial property," which includes "rights" such as patents, copyrights, or designs. *See* Income Tax Assessment Act 1936 (Australia) sections 54(1), 124K(1), 124L. Depreciation is based on the "effective" life of the property, with six different spans of effective lives from fewer than three years to 30 or more. *Id.* sections 55(1)-(5), 124M(1).

[30] U.S. Internal Revenue Code of 1986, as amended [hereinafter "US IRC"] section 168(c)(1), (e)(1). Note that this system is similar to that found in Australia. *See supra* note 28.

rect, in that property with similar useful lives was chosen for each class, and the allowable depreciation deduction based on estimates of those useful lives.

The "simplified" depreciation system found in the BWTC is not accounting-based, but "group"-based, and leans closer in many ways to the U.K. system than to the U.S. example.[31] In fact, the BWTC system provides only three groups: buildings, depreciated at 5 percent; automobiles, office furniture, computers, and the like, at 25 percent; and all other tangible property, at 15 percent.[32] The "catchall category," similar in some ways to the U.K. law, is not based on useful lives, estimates of actual decline in value, or anything else.[33] A steel furnace, which might last 20 years, will be depreciated at the same rate as a computer-operated lathe, which might last a fraction of that time.

While in the real world cars or computers might actually lose value as rapidly as 25 percent per year, by definition there are likely to be assets that lose value considerably less rapidly than 15 percent per year; also, there may well be assets that lose value more rapidly.[34] Whenever there is great mismeasurement of depreciation of an asset for tax purposes, and the amounts invested in such assets are significant, the effect on tax revenues (and investment incentives) can be substantial.[35]

A real-world example may be found in the experience of a particular emerging economy.[36] The jurisdiction in question had not been a British colony; in fact, it had a civil law system with a strong French base. Nevertheless, as part of a reform of the income tax, foreign tax advisors had recommended a cross between a U.K.- and U.S.-style depreciation system, with a small number of depreciation rates based on the asset's inclusion in a category. In this particular economy, cement, steel, and mineral processing were prominent. These sectors employ long-lived assets, and under the category system had been entitled to what empirically appears to be have been massively accelerated allowances, while other assets in the same category may have had depreciation allowances that rather understated actual declines in value. As a result, the effective tax rate on income from the heavy, capital-intensive assets had been low, and an incentive had been created to invest in those assets. A recent tax reform switched from the limited-category system to an account-based one, not entirely dissimilar from the German system.

It might have been particularly helpful for the authors to have noted, perhaps in their introduction, the existence of other 'sample' codes that are based on different styles and that make different policy choices.

As noted, there is an obvious advantage in matching tax depreciation to real decreases in value. The accounting-type rules at least set this as a principal goal. However, there are a number of objections to these systems: they are too complicated, they give the taxpayer too much of an opportunity to understate lives, or to take unjustified additional depreciation. In fact, the principal, if not the only justification in the BWTC for using its three-category system is simplicity. However, the BWTC appears to make rather dramatic assumptions about the jurisdictions for which the "sample" provision is appropriate. Even if one were designing a system for an Anglo-American/Commonwealth jurisdiction, one need not limit the rule to only three categories of depreciable assets. More specifically, having most machinery and equipment fall into a single category seems, at least to this author, as going rather too far in the vast number of developing and transitional economies. I find it hard to believe that huge multinational companies, with audited accounts by the big six accounting firms, could not comply with more accurate depreciation systems. My guess is that in many developing and emerging economies much smaller enterprise also can handle a more complicated system, tied closer to estimates of useful lives. The level of administrative development in the jurisdiction, coupled with the size and nature of the business enterprise, would determine how complicated a system might be appropriate for what types of business enterprise. How that system is designed for purposes of actually drafting legislation, as one based on the Anglo-American

---

[31]BWTC, sec. 34.

[32]*Id.*

[33]"(3) Category 3. — All other tangible property." BWTC sec. 34(d)(3).

[34]*See generally* Charles R. Hulten and Frank C. Wykoff, "The Measurement of Economic Depreciation," in *Depreciation, Inflation, and the Taxation of Income from Capital* 81, 81-125 (Charles R. Hulten ed. 1981).

[35]Therefore, one might even suggest that the BWTC system of depreciation will result in a "tilting of the playing field . . . result[ing] in the long run misallocation of labor and capital resources and in a less prosperous and stable economy." BWTC, at 7-8.

[36]For purposes of confidentiality, I will withhold the name of the jurisdiction.

system of categories or on the account-based systems often found in civil law jurisdictions, would depend on the legal traditions of the particular country. The BWTC would have benefited from a discussion of both of these issues.

The depreciation example also raises the question of terms and definitions, and how they are defined in statutes and case law. This is not simply a matter of translation, but of meaning. For example, the BWTC limits depreciation to property "used in the business of a kind which is likely to lose value because of wear and tear and obsolescence."[37] This reminds me of the U.S. statute, which begins with the general rule allowing a deduction for a "reasonable allowance for the exhaustion, wear and tear (including a reasonable allowance for obsolescence)" of business or income-producing property.[38] On the other hand, the French accounting-type rule makes no reference to physical wear and tear or to obsolescence. Instead, the rule limits depreciation to property, both physical and nonphysical, with reasonably ascertainable useful lives.[39] If the useful life is not known beforehand, but "extraordinary depreciation" occurs, a deductible "provision" similar in effect to depreciation, is allowed.[40] Therefore, in countries that have a French legal tradition, it is likely that there will be case law describing property that has useful lives, but not what property "is likely to lose value due to wear and tear and obsolescence," regardless of what French words are used by the translator. The U.K. statute has no general rule restricting the depreciation of property either to wear and tear or obsolescence, nor, for that matter, to property with determinable useful lives. Instead, individual statutory rules fix deductions for certain types of property.[41] Again, the term would be a new one.

A highly competent lawyer or group of lawyers (such as Hussey and Lubick) would never be fooled into adopting their own sample wholesale in an inappropriate setting. I am worried, however, about what might happen when others refer to their sample. I think that this problem, if such a problem does in fact exist, can be fixed rather easily. First, the authors of the BWTC can make it even clearer in the introduction and commentary that their sample law is based on an Anglo-Saxon/Commonwealth model, and might perhaps be of greater use in Commonwealth countries than elsewhere. To state or imply, as the authors do, that the sample law is Anglo-Saxon only in that it uses English is really to hide the ball.

A highly competent lawyer or group of lawyers would never be fooled into adopting their own sample wholesale in an inappropriate setting.

Second, the authors could state briefly what models, if any, they used to draft particular sections of their sample law. I do not mean that they must provide elaborate references to similar existing statutory language, although that would be very helpful as well. But it would be of great assistance if they could add simple commentary about where even the idea for a particular provision came from. This would, at the very least, put people from obviously different legal traditions on guard against the "sample" provision in question.

Third, the authors could, wherever possible, suggest, if only briefly, alternative policies and drafting possibilities. The authors state in the 1996 edition that:

> [a] number of commentators on the Preliminary Edition suggested that we should have drafted alternatives to almost every choice we have made in our sample (n.b. not 'model') code. We are unconvinced. To have prepared and described all the alternatives would have been an endless work. The delay would have precluded emergence of a timely and useful guide to decisionmaking. That holds true of this edition as well.[42]

While I readily agree with the authors that drafting alternative provisions would take so much more time and effort that a delay would be inevitable, a second, intermediate, alternative exists. They at least could have described, even if briefly and in an informal way, the types of alternatives found in other laws or other legal traditions, allowing the reader to go and ferret out examples of those alternatives. I wonder if this would have taken much additional time and effort.

---

[37] BWTC section 34(a).

[38] U.S. IRC section 167(a).

[39] The French statutory provision does not expressly state this. *See* FRA CGI article 39-1-2o. However, decisions of the Council of State make clear that no property can be depreciated unless its useful life can be determined when acquired. *See* Decision of the Conseil d'Etat of February 24, 1936, *Recueil des décisions du Conseil d'Etat* [Lebon] 236.

[40] FRA CGI Ann. III, article 38 *sexies*.

[41] *Supra* note 29.

[42] BWTC at 4.

The authors, in researching their sample code, as well as in the extensive technical assistance they have provided throughout the developing and transitional world, have already become well aware of the basic alternatives. Once again, by failing to make even the briefest annotations in this regard, the authors appear, however unintentionally, as if they are hiding the ball. It might have been particularly helpful for the authors to have noted, perhaps in their introduction, the existence of other "sample" codes that are based on different styles, and that make different policy choices.[43]

Finally, I would suggest that the next edition make it clear that, while the preparation of the BWTC was sponsored by Harvard University, the sample code itself is not in any way endorsed by the university or the Harvard Law School. I think a general disclaimer also might note prudently that no member of the Harvard Law School faculty participated in its production. The cachet of that rather famous university, and especially of its law school (of which I am an alumnus, both as a student and a member of the faculty), should probably not be used to advance the sample's acceptance. This may seem like a rather picky point. I have no doubt that it was not the intention of the authors to create any false impressions; yet, while I was in a developing country, my host exclaimed that (and I paraphrase here) the "Harvard model law (i.e., the BWTC) must be superior because the Harvard Law School has such a superior tax faculty."

Both comparative tax scholars and those brave souls who engage in technical assistance should welcome this latest edition of the BWTC, which can serve as an important component in the study of comparative taxation. It is my hope that continuing research, and especially cooperation among experts, results in more country-specific work in tax reform. As part of this process, it is also my hope that more annotated works on comparative taxation that draw from different legal traditions appear in print. Perhaps the next version of the BWTC could advance this goal even further than has the 1996 edition. ✦

---

[43]The Legal Department at the IMF, under the editorship of Victor Thuronyi, is in the process of completing a two-volume study entitled *Tax Law Design and Drafting*. These books, the first volume of which should be available this summer and the second in the fall, include considerable comparative discussion of tax laws, as well as references to those laws.

TWO

for the price of ONE!

Now Exempt Organization Tax Review brings you MORE news, MORE quickly ...but costs NO MORE

If you work with exempt organizations, EOTR offers a unique source of the specialized information you need. IRS rulings...court opinions... regulations...even Treasury Department correspondence—all carefully read and assessed to bring you every development affecting EO taxation law.

Keep in touch with the news AS IT HAPPENS

Exempt organization practitioners have always trusted EOTR for reliable and informative coverage of the field. Now the new EOTR Weekly adds timely news reporting at no extra cost—giving you even better value. This quick-read news digest keeps you in touch with the important decisions that affect you and your clients.

To order, call our Customer Service Department at 800-955-2444.
Outside the U.S. or in the Washington, D.C., area, call 703-533-4600.

292-96