STATUTORY CLEARANCES

Pete Miller explains when and how to get clearances from HMRC for your clients’ proposed transactions

Tax legislation provides for clearances from HMRC in a number of situations. HMRC also operates an informal system of non-statutory clearances, available to all “business customers” and while we concentrate here on statutory clearances, much of the advice given would also apply to non-statutory clearances. There is useful advice on HMRC’s website at hmrc.gov.uk/cap

The most common statutory clearances are those for share exchanges (ss38, Taxation of Chargeable Gains Act 1992 (TCGA 1992)), schemes of reconstruction (ss39, 139C, TCGA 1992), share buy-backs (s104C, Corporation Tax Act 2010 (CTA 2010)), demergers (s1091, CTA 2010) and transactions in securities (s701, Income Tax Act 2007).

TIMING

HMRC must give a substantive response to clearance applications within 30 days of receipt. This deadline is taken extremely seriously and I have never known it not to be adhered to. In practical terms, this means that once you have sent a clearance application, it may take a month before HMRC replies. And if HMRC has material questions, the 30-day clock resets once you have answered those questions. In extreme cases, therefore, it may take two or three months to get a clearance.

In practice, the turnaround time will depend on how busy the clearance office is and how complex the application is. Recently, I have been getting clearances in less than a week, but this cannot be relied upon.

In practical terms, it is important to build clearance time into the transaction timetable and to manage clients’ expectations. In large corporate finance transactions there will often be a formal timetable for the various work streams so that the process can be controlled; that timetable should include the timing for tax clearances. If, as advisers, we are asked about tax at the last minute, which happens all too often, it may be impossible to get a clearance in time for the preferred completion date.

In smaller cases, there may not be a formal timetable, but the client often has a timescale in mind, such as the end of the accounting period or before they go on holiday. So it is still crucial to manage those expectations.

There is an interaction between timing and the level of detail required in the clearance application. Often the exact details of the transaction elements are not important in the context of the clearance sought. For example, share exchange clearances ask if HMRC is satisfied that the transactions are being carried out for commercial reasons and not to avoid tax. In most cases, details such as the exact terms of the shares or debentures issued in the exchange are not important in this context. So a clearance application can be made at an early stage, even if the exact terms have not been completely determined. Sometimes you might need to update HMRC with the final terms, but this is unusual.

URGENT APPLICATIONS

Sometimes it is unavoidable for a clearance to be sought at short notice. In these cases, HMRC will do its best to help, but you need to make clear that the letter is urgent. I recommend that the top of the first page of the letter be marked with “urgent, please” and the date by which you need your clearance. The urgency should then be explained early in the letter.

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The letter has to tell a story: What is this company? What does it do? How has it reached the current position? What needs to change? And why? You want the HMRC officer to be able to read the letter, understand what needs doing and confirm that the clearance should be given. Speaking from experience as an inspector, a confused or badly written letter is most likely to generate a request for clarification. Worse still, a badly written letter may suggest that clearance should be refused, perhaps through lack of a commercial reason. So clarity of storytelling is essential.

MATERIAL INFORMATION

Equally important is to provide all the material information. A clearance based on an application without all the material facts is not a valid clearance. If this comes to light, it usually happens after the transaction has been carried out, so that the tax consequences we have been trying to prevent will, instead, come home to roost.

My rule of thumb is that, if you are not sure whether a fact is material in a particular case, put it into the clearance application. That way, if it is material we find out before it is too late, and if it is not material, it does not matter.

WHAT HAPPENS AT HMRC?

The clearances for capital gains, demergers, transactions in securities and purchases of own shares are dealt with in a single office, a one-stop shop. The letters are logged in order of receipt and immediately given to an officer for
an initial sift. Many applications - probably the majority - are straightforward, so the officer can grant the clearance immediately.

Some cases need more consideration, so you will receive an acknowledgement of the application, with a reference and a date by when you should have a substantive answer. If you receive one of these, it does not mean that HMRC wants to refuse your application, merely that your case needs extra thinking time. In the vast majority of cases, clearance is eventually granted.

REFUSALS
What do you do if you receive a refusal? Some of the clearance facilities, such as those for reorganisations and reconstructions and demergers (but not the transactions in securities rules), contain a right to request a review of the correspondence by the First-tier Tribunal (which should be done within 30 days of HMRC’s decision). There is no hearing to attend, but make sure you set out your arguments clearly and logically in a letter, so the tribunal can consider your case more efficiently. If the tribunal grants clearance, this is binding on HMRC.

If you have a refusal from HMRC or the tribunal, you are still entitled to carry out the transactions. Obviously, this is a high-risk strategy, as HMRC is likely to challenge it and you will have to fight your case through the normal appeals process, so I would not normally recommend this route.

Before any of this, though, consider speaking to the clearance officer. HMRC must explain why it has refused clearance. Sometimes this is a simple misunderstanding, and a telephone conversation might clear things up. Or, the elements that concern HMRC may not be of commercial importance to your clients, so you can tweak the transactions so that HMRC can grant clearance. This more personal approach is also likely to be quicker than going to a tribunal.

MEANING OF CLEARANCES
It is important to understand what a clearance actually means, and its limitations. With demergers, for example, the transactions must satisfy the detailed conditions of ss1081-1085, CTA 2010, and clearance implies that HMRC accepts, on the information supplied, that those conditions are all satisfied.

In contrast, clearances for reconstructions only state that HMRC is satisfied, from the information supplied, that the transactions are for genuine commercial reasons and not to avoid corporation tax, capital gains tax or income tax. HMRC is not able to confirm that the transactions will amount to a scheme of reconstruction, so it is up to us, as advisers, to be satisfied that they do.

OR NOT BOTHER!
Finally, remember that you do not have to seek a pre-transaction clearance. The reliefs are generally mandatory, so long as the conditions are satisfied, and the facilities for a pre-transaction clearance are there to give taxpayers certainty. HMRC cannot demand that you apply for a clearance nor express suspicion when you have not. Indeed, there may be occasions when you choose not to apply for a clearance, due to time pressures or because you do not wish to disclose to HMRC any more detail than you have to by law. You are perfectly entitled to exercise your rights not to make an application in those cases.

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