

## Summary: Intervention & Options

Department /Agency:  
HMRC

Title:  
Improvements to the Non-Statutory Clearances Process

Stage: Implementation

Version: Final

Date: 21 July 2008

Related Publications: Review of Links with Large Business  
<http://www.hmrc.gov.uk/largecompanies/reviewlinks-large-bus.shtml>

**Available to view or download at:**

<http://www.hmrc.gov.uk/better-regulation/ia.htm>

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**What is the problem under consideration? Why is government intervention necessary?**

Business places particular importance on being able to obtain quicker and earlier certainty about the tax treatment of transactions. Proposal 2 of the Review of Links (RLLB) extends the existing non-statutory clearances service offered by HMRC in order to provide business with HMRC's view of the tax consequences of significant commercial transactions wherever there is genuine uncertainty. In addition proposal 3 provides for relevant guidance on the various clearances and rulings available to business in one single accessible location on HMRC's Internet site.

**What are the policy objectives and the intended effects?**

The objective is to provide UK and international business with easier, earlier and speedier certainty. HMRC will provide business with their view of the tax consequences of significant commercial issues wherever there is uncertainty, regardless of when the legislation was enacted (thus removing the four Finance Act restriction that direct tax clearance applications were subject to under Code of Practice 10). HMRC are also committed to responding to non-statutory clearance applications within 28 days as the norm. In addition we have published guidance on the various clearances and rulings.

**What policy options have been considered? Please justify any preferred option.**

One of the key issues raised was the provision of greater certainty of tax treatment. The review recommended a number of options for addressing this, all of which were supported by business, and all of which were accepted. This IA assesses the particular recommendation to improve the non-statutory clearance process, and measures the expected impact relative to the default option of keeping the status quo. The Review's other recommendations are complementary rather than alternatives, and as such are considered in separate impact assessments.

**When will the policy be reviewed to establish the actual costs and benefits and the achievement of the desired effects?** In the initial period both qualitative and quantitative research will be undertaken to test processes and guidance and assess customer satisfaction. The satisfaction survey will continue on an annual basis. HMRC is also keeping Management Information to ensure the 28 day deadline is met.

**Ministerial Sign-off** For final proposal/implementation stage Impact Assessments:

*I have read the Impact Assessment and I am satisfied that (a) it represents a fair and reasonable view of the expected costs, benefits and impact of the policy, and (b) the benefits justify the costs.*

Signed by the responsible Minister:

Jane Kennedy

..... Date: 21 July 2008

## Summary: Analysis & Evidence

<b>Policy Option:</b> Preferred	<b>Description:</b> Improve the non-statutory clearance process
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<b>COSTS</b>	<b>ANNUAL COSTS</b>	Description and scale of <b>key monetised costs</b> by 'main affected groups'  Businesses: cost of preparing applications, additional to routine compliance costs. HMRC: setting up centre of expertise to coordinate applications; processing staff resource; updating guidance; improvements to IT and data systems.
	<b>One-off</b> (Transition) <b>Yrs</b>	
	<b>£ 1.00 m (HMRC)</b> 1	
	<b>Average Annual Cost</b> (excluding one-off)	
<b>£ .15 - .30m (HMRC)</b>	<b>Total Cost (PV)</b>	<b>£ 1.15 - 1.30 m (HMRC)</b>
Other <b>key non-monetised costs</b> by 'main affected groups' None of significance. The total cost figure above is the one-off and recurring costs to HMRC. A full NPV calculation (which would normally be used to compare costs and benefits) would not be helpful in this case because the main benefits are difficult to quantify in monetary terms.		

<b>BENEFITS</b>	<b>ANNUAL BENEFITS</b>	Description and scale of <b>key monetised benefits</b> by 'main affected groups'  Businesses: The main quantifiable benefits (around £0.15m) are a reducing cost per application, and the potential for reduced inspection costs.  HMRC: see non-monetised section below.
	<b>One-off</b> <b>Yrs</b>	
	<b>£ nil</b>	
	<b>Average Annual Benefit</b> (excluding one-off)	
<b>£ 0.10 - 0.15 m</b>	<b>Total Benefit (PV)</b>	<b>£ Unquantifiable</b>
Other <b>key non-monetised benefits</b> by 'main affected groups' Businesses: The biggest benefit is increased certainty of tax treatment, which cannot be quantified precisely. This benefit does exceed the total cost, however, as shown by the increasing use of the (voluntary) clearances regime. HMRC: greater awareness of business needs & trends, improved expertise & efficiency.		

**Key Assumptions/Sensitivities/Risks** The above figures are tentative and based on the best information available. HMRC is monitoring the process closely, through internal data collection and external customer surveys, to ensure continuous improvements, and to review the effects of reform where necessary. This reform will not directly affect the amount of tax collected.

Price Base Year 2008	Time Period Years 1	<b>Net Benefit Range (NPV)</b> <b>£ Not quantifiable</b>	<b>NET BENEFIT (NPV Best estimate)</b> <b>£ Significant(not quantifiable)</b>
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What is the geographic coverage of the policy/option?	United Kingdom
On what date will the policy be implemented?	1 April 2008
Which organisation(s) will enforce the policy?	HMRC
What is the total annual cost of enforcement for these organisations?	£ negligible
Does enforcement comply with Hampton principles?	Yes
Will implementation go beyond minimum EU requirements?	No
What is the value of the proposed offsetting measure per year?	£ N/A
What is the value of changes in greenhouse gas emissions?	£ N/A
Will the proposal have a significant impact on competition?	No
Annual cost (£-£) per organisation (excluding one-off)	Micro Nil      Small Nil      Medium Nil      Large Nil
Are any of these organisations exempt?	No      No      No      No

<b>Impact on Admin Burdens Baseline</b> (2005 Prices)		(Increase - Decrease)
Increase of    £ Negligible	Decrease of    £ Negligible	<b>Net Impact</b> £ Broadly neutral

Key:      Annual costs and benefits: Constant Prices      (Net) Present Value

## Evidence Base (for summary sheets)

### 1. The Issue

- 1.1 The Review of Links with Large Business, led by Sir David Varney, was commissioned by the Chancellor of the Exchequer to address business concerns about the nature of the relationship between large business and HM Revenue and Customs (HMRC). Government and business have a common goal of maintaining and enhancing the attractiveness of the UK as a place to do business in and to do business from. The relationship between large business and HMRC and the efficiency and effectiveness of the administration of the tax system are important in achieving this goal. The aim of this review was to fundamentally improve the nature of this relationship.
- 1.2 The Review of Links with Large Business targeted HMRC's largest business customers. The complexities of the tax affairs of these large complex businesses mean that they may have specific issues and needs. Nevertheless, HMRC believe that the principles underpinning the proposals arising from the Review of Links are equally applicable and relevant, albeit on a potentially different scale, to all of HMRC's business customers, be they large, medium or small and on this basis have extended many of the proposals, including the extended clearances service, to all our business customers.
- 1.3 The Review of Links with Large Business report, which can be found at <http://www.hmrc.gov.uk/large-business/review-report.pdf>, was published in November 2006 and identified four key outcomes that both business and HMRC wanted to see: -
  - greater certainty
  - an efficient risk based approach to dealing with tax matters
  - speedy resolution of issues; and
  - clarity through effective consultation and dialogue.
- 1.4 Key to both the outcomes of greater certainty and the speedy resolution of issues was the extension of the existing non-statutory clearances service offered by HMRC. HMRC already provide non-statutory clearances to our customers via Code of Practice 10 and VAT Notice 700/6. These outline both the process by which an individual or business can obtain a clearance, and the rules associated with applying for a clearance. Feedback received during the course of the Review of Links and in the subsequent consultation demonstrated that providing certainty on the tax consequences of a particular transaction is of paramount importance to business.
- 1.5 Certainty means getting a definitive answer as to HMRC's view of a particular circumstance, which is binding on HMRC and can therefore be relied upon by the customer. Being able to obtain certainty has the potential to make a real difference to the competitiveness of the UK in relation to tax administration.
- 1.6 Research undertaken during the Review of Links consultation showed that whilst Code of Practice 10 and VAT Notice 700/6 were generally regarded as an effective means of obtaining certainty in a number of scenarios there were some concerns. The key concerns raised were:
  - the fact that for direct tax the relevant legislation must fall within the last four Finance Acts for the issue to be considered; and
  - a perception that HMRC were not responding quickly enough to non-statutory clearance applications and the need for these to be dealt with as normal business practice.

- 1.7 In recognition of the lack of consistency within HMRC in relation to the 'time-based' rules on clearances we have removed the four Finance Act restriction that existed for direct tax issues under Code of Practice 10. Recognising that there could be high volumes of clearances received, and wanting to provide a good service for all of our customers, we ask that on legislation older than the last four Finance Acts the commercial significance to the business itself is demonstrated.
- 1.8 We have also committed to providing a speedy response to non-statutory clearance applications, namely responding to clearance applications within 28 days as the norm. In complex cases, where the input of a number of different experts in HMRC is required, we may exceed these time limits. In these cases we are committed to communicating more regularly with business in order that applicants are clear as to how their applications are being dealt with, and when a reply will be received.
- 1.9 In summary the purpose of the extended non-statutory clearances service is to provide certainty for businesses operating in the UK as a useful practical service where speed of response from HMRC can be reasonably assured. Code of Practice 10 and Notice 700/6 will remain in place for other HMRC customers, for example individuals and charities, who are not covered by the new clearances process.
- 1.10 HMRC aim to provide clearances
- within 28 days as the norm
  - on areas of material uncertainty arising within four Finance Acts of the introduction of any new legislation; and
  - on legislation older than last four Finance Acts where there is material uncertainty around the tax outcome of a real issue of commercial significance to the business itself, determined by reference to the scale of the business and the impact of the issue upon it.
- 1.11 In addition, in order to provide businesses who seek rulings and clearances from HMRC with greater clarity we have provided for relevant guidance to be located in one single accessible location on HMRC's internet site. This information can be found at <http://www.hmrc.gov.uk/cap/>

## **2. Policy Objectives and Intended Effects**

- 2.1 The objective of the extension of the existing non-statutory clearance service is to provide UK and international business with easier, earlier and speedier certainty. HMRC will now provide business with their view of the tax consequences of significant commercial issues wherever there is material uncertainty, regardless of when the legislation was enacted (thus removing the four Finance Act restriction that direct tax clearance applications were subject to under Code of Practice 10). HMRC are also committed to responding to clearance applications within 28 days as the norm as part of their commitment to provide speedy resolution.
- 2.2 The extension of the existing non-statutory clearances service will enable HMRC to provide business with their view of the tax consequences on issues of commercial significance. From 1 April 2008 all businesses seeking HMRC's view on significant issues, both pre and post transaction, will receive a binding HMRC view within 28 days as the norm.
- 2.3 In providing this extended non-statutory clearances service we have
- extended clearances across all taxes (thus removing the four Finance Act restriction that direct tax clearance applications were subject to under Code of Practice 10) in

order to provide increased certainty of the tax consequences of 'significant commercial issues'

- introduced a system of acknowledgements for non-statutory clearance applications
- published a checklist and detailed accompanying guidance notes to help customers complete a clearance application – the clear provision of this information not only assists the customer in completing their clearance application but also serves to improve the consistency of applications and provide greater transparency about the information required by HMRC to process a clearance application
- updated our existing guidance to provide an integrated, consistent and clear framework for business clearance applications across HMRC; and
- provided clear and transparent guidance on the meaning of 'binding'.

2.4 In addition we have provided, in one place on the HMRC website, details of the various rulings and clearances available to business. In doing this we will ensure that business has easy access to all the information required to understand the scope of the various clearances and rulings that can be applied for, the requirements and time-limits for each and a contact point for enquiries.

### 3. The Options

3.1 The Review of Links focused on prioritising the concerns of large business and developing, alongside large business, outcomes and proposals to address these concerns. One of the key outcomes identified as important for large business was the provision of greater certainty, to be addressed by a number of measures including the extension of the existing clearances system.

3.2 Whilst the Review of Links focuses primarily on large business HMRC recognises that the principles underpinning the proposals are equally applicable and relevant to small medium and large business and have extended the clearances service to all of our business customers.

3.3 The findings of the Review of Links and responses to the subsequent consultation clearly demonstrated that improvements to day to day working practices were required by both large business and HMRC. Successful delivery of the Review of Links proposals was seen as fundamental to improving the relationship between HMRC and business.

3.4 The business sector fully endorsed the proposals set out in the Review of Links report, stating that *'when taken together, the proposals represented a significant package which will make a real difference in taking forward the relationship between business and HMRC. The proposals, when delivered and with the support and engagement of HM Treasury, will contribute to the competitiveness of the UK and will foster and encourage an environment in which business can flourish'*.

3.5 The Review of Links clearly set out that HMRC would provide business with greater certainty by the *'swift provision, as normal business practice, of HMRC's view of the tax consequences of genuine significant commercial issues whenever there is uncertainty. By no later than Budget 2008 businesses who seek HMRC's view on the tax treatment of transactions, either pre-transaction or post-transaction but pre-filing, will receive a binding view within 28 days of the request as the norm on the basis they make full and transparent disclosure of the supporting facts and commercial intent'*.

3.6 In light of the support of business for the proposals contained within the Review of Links, and recognising the importance of building on our relationship with business to maintain and enhance the attractiveness of the UK as a place to do business in and to do business from and in order to increase the efficiency and effectiveness of the

administration of the tax system, we have implemented the proposal on extending the existing clearances service as laid out in the Review of Links document.

3.7 The review considered a range of options for improving links with large business, and for improving certainty in particular. Compared with those other proposals, the clearance reforms were seen as complementary, rather than as an alternative. As such, those other proposals are considered separately in their own impact assessments, and the main benchmark for evaluating the clearance proposals is the default option of maintaining the status quo. This approach is consistent with the importance attached by business to the provision of greater certainty through a range of complementary reforms.

#### **4. Costs and Benefits / Impacts**

4.1 Clearances are designed to reduce uncertainty, and hence to reduce the risk associated with business decisions where the tax treatment is unclear. Businesses and HMRC incur an upfront cost in making and processing the clearance application, but benefit in the longer term.

4.2 The reform will have two main effects, both of which have been welcomed by business.

- It will increase the range of circumstances in which businesses can seek an HMRC ruling, by extending non-statutory clearances across all taxes beyond the current four Finance Act limit.
- It will make the clearance process more efficient, more customer-focused and more transparent.

4.3 This means that both the number of clearance applications, and the level of benefits arising from them, should rise. The cost of making applications may rise in total, but should fall on a “per case” basis. In essence, the reform will improve the benefit to cost ratio for any business seeking a clearance ruling, and give such rulings in a wider range of circumstances.

#### **COSTS**

##### *Costs to business*

4.4 The non-statutory clearance application process is voluntary. No business will incur costs unless they choose to (i.e. if they expect the benefits to outweigh the costs on average).

4.5 For those that do make applications, the main cost is the resource spent on preparing the clearance application itself. However, HMRC expect this cost to fall slightly on a “per case” basis because of the improvements to guidance and transparency. This likely cost reduction is assessed in the benefits section below.

4.6 The total cost to the business community of making applications depends primarily on the number of applications made. The extension beyond the current four Finance Act limit may increase the number of applications, although such an increase may partly be a temporary effect in the first year or two. The reforms to the application process (making it clearer and easier) may also boost demand.

4.7 Initial research in 2005 suggested that HMRC already handled an estimated 12,000 COP10 non-statutory clearance applications each year. We have continued to base our analysis on this figure. Early indications for April 2008 have shown a much lower level of applications, but this may be partly explained by seasonal factors, together with the fact that the reformed system is new. HMRC are monitoring developments daily. It is difficult to estimate any increase in demand arising from these reforms, but the early indications are as follows.

- In the June 2007 consultation, around half of those offering an opinion said they expected an increase. The other half either expected no change or were unable to

say. One representative body suggested there might be an extra 50 applications per year from the investment industry alone. Collectively, the consultation implied an increase of the order of 1,000 extra applications per year in total, although this is extremely tentative and includes any temporary effect. Some industry experts have suggested that any permanent increase in application numbers may be below 500 per year.

- The reforms were piloted in the first quarter of 2008. Around 1 application in 8 was additional to the existing COP10 procedure, in the sense of falling outside the four Finance Act limit.

4.8 On balance, HMRC's view is that the reform will enable businesses to seek clearance rulings in a wider range of circumstances than before, and some are clearly choosing to do so. The resultant rise in applications is uncertain and will be monitored.

4.9 The cost of making a clearance application is very variable. It is also difficult to separate the specific costs associated with the application from the analytical costs that a business would incur anyway as part of tax and/or normal business planning. Where a business has most of the information to hand business has indicated that the marginal (additional) cost of making an application can be quite small.

4.10 Based on research into the administrative burden on business in 2005, the June 2007 consultation, the recent pilot exercise and anecdotal evidence, HMRC estimates that a straightforward application, completed by in-house company staff with minimal consultancy support, might cost around £200 over and above existing business costs. More complex applications might require several days to prepare, and cost a lot more, particularly if prepared by third party accountants or advisors. The reality is that the cost of an application depends on the particular circumstances, the degree to which the work has already been done, and the nature of the tax area where clearance is being sought. The one common factor is that all applications are voluntary and are unlikely to be made unless the applicant believes the potential benefits outweigh the costs.

4.11 It is not yet known whether applications made outside the four Finance Act limit are likely to be more or less costly to prepare than normal. HMRC will continue to monitor feedback from businesses on this aspect, and work to minimise any additional cost through improved guidance and support. At an assumed marginal cost of £200, the additional 500-1,000 applications would cost around £100k-£200k in total.

#### *Costs to HMRC*

4.12 HMRC will incur a number of one-off costs at the outset: administrative set-up costs, staff training and IT systems. There will also be costs involved in updating guidance. The reforms were piloted from January to March 2008, and most of the set-up costs have already been incurred. Most of these costs have been fairly low and absorbed within normal running costs. The exception is the one-off staff cost associated specifically with setting up new processes. This is estimated, roughly, to be around £1 million to HMRC.

4.13 On a recurring basis, HMRC will need to process applications, consider whether or not to accept them, analyse the proposals and issue clearances. Supporting activities, such as management information systems, will be required as well.

4.14 The net change in recurring costs will follow the same principles as the costs to business. In other words, the number of applications may rise, but the cost of dealing with each case should fall. Improvements to guidance may help businesses supply the right information first time, for example. The net effect on HMRC costs will depend on the balance between these various factors.

4.15 Information collected during the pilot exercise in early 2008 suggested that it takes around 1.5 hours for HMRC to receive, consider and reply to a clearance application. The time is very variable (and significantly more for complex cases) but this is an indicative average. We would expect the cost to fall slightly as the new rules and

systems bed in, and familiarity increases. The total resource cost of processing the additional 500-1000 applications is around £50k - £100k per year.

### *Other costs*

4.16 The guidance provided for the extended non-statutory clearances service and on other clearances and rulings offered by HMRC will need to be kept up to date to remain effective. HMRC expects to absorb the associated costs within the above figures. Overall, combining business and HMRC effects, the total recurring cost is likely to be between £150k - £300k.

## **BENEFITS**

### *Administrative efficiency benefits for business*

4.17 HMRC are streamlining the application process with particular emphasis on consistency and transparency. The benefits include

- improved communications between HMRC and business during the period that HMRC are considering the clearance application. HMRC will aim to ensure that, wherever possible, applications are dealt with within 28 days of receipt. Where this is not possible (because of the complexity of a particular clearance application) HMRC will work with the customer to provide a response as soon as practical
- updated and integrated guidance on HMRC's clearance service. This will mean that businesses can be certain of the service that HMRC provides across all taxes and duties. It will also enhance customer awareness of information requirements and so improve the consistency of the clearance service. In particular, HMRC will publish a checklist with detailed guidance notes to help applicants
- publishing guidance and advice on the HMRC website. This was proposed in Sir David Varney's Review of Links review, and will enhance transparency
- making clear what the scope of clearances is, so that businesses know when, and to what extent, they can rely on HMRC's view
- publishing details of the various rulings and clearances available to business in one place on the HMRC website.

4.18 Overall, the reforms will improve working relationships between HMRC and business, reduce the cost of making clearance applications and enhance their value.

### *Greater certainty of tax treatment*

4.19 HMRC aims to provide businesses with a view on the tax consequences of significant commercial issues wherever there is uncertainty. This is the biggest benefit of the non-statutory clearance regime, and hence of the extension beyond four Finance Acts. Clearances provide

- a clearer framework for making business decisions; and
- a substantially reduced risk of incurring unexpected tax charges.

4.20 In the absence of a clearance application, a business may be able to reduce the level of uncertainty to an extent (for example by seeking consultancy advice) but the ability to seek a clearance from HMRC specifically may (i) be cheaper, and (ii) reduce uncertainty to a greater degree.

4.21 The benefits of certainty are significant, but are likely to vary substantially from case to case. They are also intangible and difficult to quantify precisely. Nevertheless, the ability to make more informed decisions can have a direct effect on commercial profitability. Some businesses have stated during consultation that they attach very large values



(potentially £millions) to this benefit. Even where a clearance application is rejected, that rejection can itself help a business make more robust decisions.

Hypothetical example to illustrate the value of certainty

4.22 Although it is not possible to quantify the benefits of certainty precisely, the following example is illustrative. It is based on the statistical concept of expectation (essentially a summation of all possible outcomes, weighted by their respective probabilities). Although somewhat hypothetical, this approach is recommended within government for use in cost/benefit impact assessment analysis of this kind. It is also likely to be used for many different kinds of private sector business decisions.

4.23 Suppose that a business is considering restructuring to save money, but that there is a possibility that tax considerations would outweigh the savings and give a net cost.

Do not seek clearance		Seek clearance	
Spend £0.5m on restructuring		Spend £0.05m on application	
70% chance Make savings Gain £1m	30% chance Tax liability Lose £1m	70% chance OK to proceed Spend £0.5m Gain £1m	30% chance Do not proceed
Expected value of decision: $-0.5 + (0.7 \times 1) - (0.3 \times 1) = -0.1$		Expected value of decision: $-0.05 + 0.7 \times (1 - 0.5) + 0 = +0.3$	

4.24 Without the clearance, the uncertainty over tax treatment would discourage restructuring, because the costs would outweigh the benefits. The clearance clarifies the likely outcomes early and allows a better decision to be made. The value of the clearance could be measured by taking the difference in expected values (£0.4m in this fictional example).

4.25 In the real world, the impact would depend on individual circumstances and it would be difficult to assign precise values. A business may be able to reduce uncertainty to some extent through other means (c.f. 4.20 above). Nevertheless, consultation has confirmed that clearance rulings are highly desirable from a business perspective. HMRC believe that in most cases, the benefits of certainty would significantly outweigh the costs of making applications. It is not, however, possible to quote a precise figure.

*Reduction in the cost to business of making an application*

4.26 Improvements to guidance should make it easier for businesses to prepare applications, submit the necessary information correctly first time, and avoid follow-up queries. We do not have a robust estimate of the time saved (it would vary from zero in some cases, to many hours in others) but ongoing monitoring will ensure that the guidance is effective and helpful. For costing purposes we have assumed an average 5% reduction in costs (i.e. a small saving but a worthwhile one) but with a caveat that such a figure is tentative.

*Reduced costs associated with audits & inspections*

4.27 It is not possible at this stage to estimate the likely size or prevalence of any reduction in audit costs, but HMRC will keep the situation under review as part of wider reforms of the audit and inspection regime.

4.28 Finally, early dialogue of clearance issues will almost certainly improve mutual understanding between HMRC and its customers. That will have knock-on benefits, such as a reduced chance of problems not being tackled, or of penalties being applied.

*Benefits for HMRC*

4.29 To a large extent, HMRC will benefit from improvements to the application process in a similar way to businesses. The benefits include

- efficiency benefits arising from centralisation, improved guidance and training
- enhanced awareness of trends, particular in terms of which technical issues are generating most requests for clearances
- continuing improvements in HMRC's relationship with large business, and in awareness of the issues of concern to those businesses
- an enhanced ability to maintain and update guidance in line with recent and anticipated trends; and
- a centralised repository of clearance-related information and management information, enabling a better service to be provided.

4.30 These benefits are qualitative in nature, and have not been quantified accordingly. HMRC will continue to monitor developments to ensure that all benefits (whether quantifiable or not) are maximised.

## 5. Administrative Burden.

5.1 Within the overall compliance cost to business, HMRC track one component in particular. The "administrative burden on business" is defined very specifically as the time and cost on compliant businesses of retaining information and/or sending it to the Department and/or a third party. As such, it includes (e.g.) the burden of completing forms and returns, and of complying with audits and inspections. All government Departments have targets to reduce administrative burdens and HMRC impact assessments provide an itemised figure accordingly. This does not mean that other types of burden are ignored: it means simply that HMRC are taking additional steps to address business concerns that the administrative burden, as defined, is minimised.

5.2 In the case of clearances, the cost of making an application is included within the definition of admin burden. So too is any cost incurred during audits and inspections. Therefore, the impacts on admin burden are

- an increase, because the number of applications is expected to rise
- a reduction, because the cost per application is expected to fall; and
- a further reduction, because the cost of audits and inspections may fall.

5.3 Based on the earlier analysis of costs and benefits, and an additional assumption that around 10% of firms will see a reduction in inspection costs of £100, the net effect on admin burden is estimated as follows.

- Between 500 & 1,000 additional applications at £200 each = +£100k to +£200k
- An assumed 5% reduction in the cost of the 12,000 existing applications = -£120k
- An assumed reduction in audit costs of £100 for 10% of new applicants = -£7.5k

5.4 These effects cancel each other out, giving a net change of around £22.5k across industry as a whole. This is effectively negligible and the impact on admin burden is classed as broadly neutral accordingly. The figure itself is tentative: the precise outcome will depend on the extent to which businesses find the new application process easier to use, the extent to which they use consultants or accountants to help them, the take up of the clearances regime itself and a number of other factors.

5.5 Some firms may experience a small rise in their own burden, particularly if they make a large number of additional applications as a result of these reforms. This reinforces the importance of making the application process as efficient and effective as possible. The reform achieves that by reducing the cost per application, and HMRC remain committed to maximising the benefit to cost ratio of clearance applications.

5.6 The key message is that while the administrative burden is likely to remain largely unchanged overall, the unquantifiable benefit of certainty is significant and likely to

outweigh any costs on average. Additionally, the voluntary nature of clearance applications means that businesses are able to decide whether the benefits of each individual clearance application are likely to outweigh the cost.

### **Exchequer effects**

- 5.7 The clearance process is designed to clarify the tax treatment of business situations. It does not in itself change that treatment: it simply explains what the treatment is likely to be, so that businesses can make informed decisions.
- 5.8 As such, HMRC do not expect this reform to have a direct effect on the total amount of tax raised.

## **6. Implementation Plan**

- 6.1 Prior to full implementation of the extended non-statutory clearance service on 1 April 2008 we ran a pilot scheme for a section of our business customers - business customers in the Retail sector whose tax affairs are handled by the Large Business Service (LBS) and business customers, across all sectors, whose tax affairs are handled by offices within the North West & Midlands group of Local Compliance.
- 6.2 The pilot commenced on 2 January 2008 running until 31 March 2008. The pilot provided HMRC with an opportunity to test its processes in advance of full implementation. We were pleased to report that during the course of the pilot we replied to over 90% of applications within 28 days exceeding our target of responding to more than 75% of applications within 28 days.
- 6.3 Full implementation commenced on 1 April 2008. The relevant announcements and guidance can be found at <http://www.hmrc.gov.uk/news/extend-clearances.htm>, <http://www.hmrc.gov.uk/briefs/vat/brief2008.htm> and <http://www.hmrc.gov.uk/cap/links-dec07.htm>
- 6.4 We are keeping the extended clearances service under constant review.

## **7. Impact Tests.**

### *Small firms impact*

- 7.1 The clearance service is available to all commercial customers and there is only an impact if customers choose to make an application. The impact on small businesses is no different in theory than on any other applicant. In practice, the larger the business the more likely they are to encounter complex tax issues where a clearance ruling might be valuable. Because of this, the benefits of certainty may accrue more to larger firms. This however is primarily because small businesses are likely to have simpler affairs (and hence more certainty) to begin with.
- 7.2 The cost of making a clearance application depends on various factors, but in particular on whether accountants are employed to assist with the application. Small firms may be slightly more likely to employ advisors to help them (through not having in-house resource) but are much less likely to make an application in the first place.

### *Competition effects*

- 7.3 We do not anticipate any significant impacts on competition arising from these reforms. The benefit of increased certainty will enable businesses to make more informed, and hence better, planning decisions. This may help those businesses become more competitive than they would otherwise have been.

- 7.4 There may be some indirect effects on third party advisors. If a business applies for a clearance then they may or may not choose to employ consultants or accountants to assist them. Equally, if they do not apply for a clearance they may choose to employ advisors to help them reduce uncertainty in other ways. We do not believe these reforms will distort the market in any significant way, but there may be a slight shift away from advisors providing advice on certainty and towards those advisors helping make clearance applications. This is particularly likely in situations outside the four Finance Act limit, where clearances were previously not available.

#### *Other impact tests*

- 7.5 All the other tests in the annex have been considered, but are not materially affected by this reform.

## **8. Caveats and Risks.**

### *Caveats & risks associated with the reform itself*

#### When a business can rely on a clearance

- 8.1 Our starting point is that business should be able to rely on any advice we provide. All the relevant facts must be included in the application and the customer must draw attention to all relevant issues (for example, by providing information on related transactions where relevant)
- 8.2 There may be a very small number of cases where we provide an advance agreement that is incorrect in law. Where this happens, we will be bound by the advice we have given if the business reasonably relied on it and there could be financial detriment. In those cases it is possible that to apply the statute would be so unfair that it could amount to an abuse of our powers. Where we have given an incorrect agreement, our primary duty is to collect the correct amount of tax as required by the law and therefore there will be some, very rare, circumstances when we would not be bound by the advice we have given.

#### Tax Planning

- 8.3 The enhanced clearances policy is firmly based on the understanding that decisions will not be sought or given in respect of arrangements which could be considered as tax planning. HMRC have made it clear in the guidance and Consultation Document that, while clearances and rulings will be available for a wider range of transactions than is currently the case, they will not become involved in any tax planning activities.
- 8.4 This approach is consistent with existing Code of Practice 10, which states that HMRC 'will not help with tax planning, or advise on transactions designed to avoid or reduce the tax charge which might otherwise be expected to arise'.

### *Caveats & risks associated with the analysis*

- 8.5 The impacts of this reform are difficult to assess for several reasons.
- The costs and benefits are driven by the individual circumstances of each application, and are extremely variable.
  - The level of clearance applications is uncertain and may change as a result of factors unrelated to these reforms.

- The extension to the scope of the clearance regime interacts with the improvements to the efficiency of that regime, and it is difficult to assess each impact independently.
- The main benefit of reform, increased certainty, cannot be readily quantified.

8.6 The effect of this is that the analysis includes a number of assumptions and uncertainties, as described in section 4 above. Although quantified as far as possible, the assessment of costs and benefits remains tentative. The conclusion that the benefits outweigh the costs is robust, however, and is fully supported by the outcome of earlier consultation with affected businesses.

## **9. Monitoring and Evaluation.**

9.1 The extended clearances service will be subject to research conducted by an external research organisation on order to ascertain customer satisfaction and to provide feedback on the processes employed.

9.2 The extended clearances service will, in line with standard Government practice, be subject to formal post-implementation review once the reforms have bedded in and suitable data become available. This is likely to be within 1-3 years of implementation. The dedicated customer satisfaction surveys will be carried out during 2008 and 2009. These surveys may become incorporated into wider customer surveys from 2010, as the processes become embedded into 'business as usual' activity.

## Specific Impact Tests: Checklist

Use the table below to demonstrate how broadly you have considered the potential impacts of your policy options.

**Ensure that the results of any tests that impact on the cost-benefit analysis are contained within the main evidence base; other results may be annexed.**

Type of testing undertaken	<i>Results in Evidence Base?</i>	<i>Results annexed?</i>
Competition Assessment	Yes	No
Small Firms Impact Test	Yes	No
Legal Aid	Yes	No
Sustainable Development	Yes	No
Carbon Assessment	Yes	No
Other Environment	Yes	No
Health Impact Assessment	Yes	No
Race Equality	Yes	No
Disability Equality	Yes	No
Gender Equality	Yes	No
Human Rights	Yes	No
Rural Proofing	Yes	No