
The Personal Tax Planning Review

PRE-TRANSACTION RULINGS: A REVENUE CONSULTATIVE DOCUMENT

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Introduction

The Revenue has recently published (November 1995) a consultative document concerning the introduction of a formal scheme for obtaining pre-transaction rulings from the Revenue. It is envisaged that such rulings will broadly be of two kinds:

- "private" rulings — rulings on the tax treatment of a particular transaction before that transaction takes place; and
- "public" rulings — rulings on the Revenue's interpretation of the legislation, not tied to a specific set of facts.

It is envisaged that private rulings will be given in the following way:

Where a clearance is requested, details of a proposed transaction will be presented for consideration as to whether the relevant (normally anti-avoidance) legislation applies. After any necessary correspondence and/or an interview, the taxpayer will be informed of the Revenue view, and if the conclusion is that the legislation does not apply the Revenue will, in effect, be bound — provided the transaction is carried out in accordance with the application.

The objective behind this proposal is, the Revenue declares, to provide greater certainty of tax treatment to the taxpayer before he implements the transaction.

As a means of providing certainty, the proposed pre-transaction rulings regime should be welcomed.

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The writer, however, has reservations about any such proposal for two reasons. The first is that, in essence, the Revenue is usurping the law making authority of the legislature and is seeking to turn its interpretation of the law into the law.

The writer's second reservation is based on the capacity of the proposed scheme to provide the certainty of tax treatment which the Revenue claims it will provide.

Each reservation will be dealt with in turn.

Is the Revenue Usurping the Role of the Legislature?

The separation of the roles of the Legislature and the Executive is not one which is enshrined in any document such as a written constitution but, rather, is a division which has developed over time. It is generally understood that Parliament is the **only** law-making body in the UK. No other body has the authority to make the law — certainly not the administrators.

The administrators are meant to administer the law created by Parliament, and not create laws of their own. This basic tenet was evidenced by the precise way in which the laws were drafted so that there was minimal room for uncertainty. In this manner it was hoped that the administrator would not have any choice as to how he administered the law or what the law was.

In the tax area, however, the exigencies of modern business transactions have led to ever more complicated legislation. Further, there has been an increasing willingness on the part of judges to exercise their power to interpret statutes so as to create a tax law which they consider to be "fair". These factors have rendered the tax law uncertain.

It is obvious that the freedom to manoeuvre granted by such uncertainty has given the Revenue power effectively to legislate — either by concession which changes the law or by publishing their interpretations of the law which can, and quite often do, diverge from the general understanding.

In a sense, therefore, it is true to say that the Revenue has encroached upon the law-making authority of Parliament.

As a result, a taxpayer trying to plan his tax affairs not only has to take the Parliament-made law into account but must also take the Revenue view of the law into account.

The Revenue encroachment into the realm of law making is thrown into sharper focus in the context of pre-transaction rulings. In this context, it is even clearer who is deciding the law. The Revenue is, in essence, imposing its interpretation of the law as the definitive interpretation. Surely this activity is inconsistent with

the Revenue's position simply as administrator of the law? An administrator administers the law, he does not create it.

Note, however, paragraph 1.12 of the Consultative Document in which the Revenue asserts its ability to alter the law:

"The increasing complexity of tax legislation and commercial practice makes certainty of tax treatment that much more important, particularly when transactions of any size or complexity are being planned or contemplated. Taxpayers have traditionally coped with this by seeking the appropriate professional advice. But professional advice can only identify uncertainties in the law, not remove them. Rulings can provide that certainty."

There will undoubtedly be many people who will regard the writer's concern over the Revenue's self-appointed role as law-creator as exaggerated and pedantic. To these persons this blurring of responsibilities/activities is a small price to pay if, as a result, there is certainty of tax treatment.

It must, however, be noted that while the official law-creator, Parliament, is subject to public scrutiny, the same cannot be said of the Revenue. There are at present only two methods of controlling Revenue power — approaches to the Revenue Adjudicator and judicial review.

Neither of these is an adequate remedy. Judicial review is lengthy and expensive. Approaches to the Adjudicator are only appropriate where no legal issues arise. The Adjudicator's office refuses to act in any matter in which any legal issues arise.

The Consultative Document itself proposes a possible appeals procedure by the taxpayer. Whilst it is clear that such a procedure is desirable, the form it should take is not as clear. In order not to delay the commercial transaction in respect of which the ruling is being sought, the appeal procedure must provide a speedy determination after a thorough discussion of the issues.

The Revenue recognises the problems involved in deciding on an appeals procedure which will be both quick yet thorough. Paragraphs 2.24 and 2.25 of the Consultative Document state:

"... A right of appeal may not be of much practical benefit because the time involved in moving through the Commissioners and the Courts may well be too protracted to allow certainty to be obtained quickly enough for the prospective transactions. Furthermore, it seems undesirable to allow a taxpayer to test the law, through the court, on the basis of "hypothetical" facts.

2.25 As an alternative the taxpayer could have the right to "protest" ... the ruling, and have this heard by either a senior Revenue official, or the Special Commissioners, on an expedited basis. In the latter case, the Revenue could not be expected to give up the right to test the position in court, after the event, so only limited additional "certainty" would be achieved."

It is arguable that of the two possible appeals options, the latter may be the preferable one since it has the advantage of being quick. Its main drawback, however, is that it may not be finally determinative of the matter. As a result it is unclear whether any additional certainty will have been provided by the appeals procedure.

In the wider context of the pre-transaction rulings, it is just as unclear whether these rulings will provide the promised greater certainty.

Greater Certainty?

An increased degree of certainty can only be provided by the Revenue to the taxpayer if both parties are bound by the pre-transaction ruling. If it is possible for either party to renege from the ruling then very little will have been gained by way of certainty. However, both parties can only be expected to be willing to be bound if there is a high level of disclosure by both sides as well as an appeals procedure.

In applying for the pre-transaction ruling, the Revenue requires a degree of disclosure similar to that for post-transaction rulings. Information required would probably include the following:

- the name and tax reference number of the taxpayer;
- full particulars of the transaction or event in question;
- a statement of issues to be considered;
- copies of all relevant documents, with the relevant passages identified;
- a statement that to the best of the taxpayer's knowledge and belief the facts as stated are correct and also the relevant facts have been disclosed;
- a statement of the specific points of difficulty giving rise to the rulings request;
- a statement of the ruling requested or suggested as appropriate by the applicant;

- particulars of any case law, statements of practice, extra-statutory concessions etc. considered to be relevant;
- particulars of any previous discussions or correspondence about the tax treatment of the transaction, or of any similar transaction, between the taxpayer and any Revenue office, and when the taxpayer or his advisers are aware of correspondence on the transaction between any other person and any Revenue office, particulars of that correspondence;
- a statement of the applicant's opinion of the tax consequences of the transaction, along with reasons to the extent that they were capable of being supplied;
- where the transaction is more complex, additional information or clarification may be required from the taxpayer.

And what will the Revenue provide in return, apart from a ruling? The answer is found at paragraph 2.7 of the Consultative Document:

"With available resources it is unlikely that extended correspondence or discussion on the Revenue's interpretation of the law adopted would be possible. For the same reason, it would not be possible for the Revenue to provide its own comprehensive and exhaustive analysis of the legal issues raised by the rulings application. Where a negative ruling was given, it might be possible to provide an indication as to why the Department's legal analysis differed (on the relevant issues) from that given in the rulings application."

In short, the taxpayer acquires the possibility — not even the certainty — of "an indication" of the reasons why a positive ruling is not given. This is not much, considering the extensive disclosure on the part of the taxpayer.

Even where a positive ruling is given, it is arguable that no great degree of certainty of tax treatment has been given. This is because, even after the transaction takes place, it is open to the Revenue to retract its "clearance" where it feels that the transaction has had tax avoidance results. If the taxpayer protests then it is open to the Revenue to claim that **all** the relevant facts or matters were not brought to the Revenue's attention.

This begs the question: what level of disclosure **before the transaction** would prevent the Revenue from claiming **after the transaction** that it was not made aware of all the relevant facts and matters?

In Annex 1 to the Consultative Document, the Revenue states:

"... you can rely on our advice if your application sets out **all the relevant facts** and draws attention to **all the issues (including questions of interpretation of the law)** relevant to the point upon which you are seeking advice. ... The term "relevant" should be interpreted broadly. It can be taken as including any transactions (proposed or actual) related to, or consequent upon, the transaction upon which advice is sought. If you are in any doubt about whether a particular item is relevant you can discuss it with us."

Therefore, "relevant" seems to mean **everything** pertaining to the particular transaction. In the context of Revenue clearances, the leading case law authorities do not render any clearer the level of disclosure which is required in order to get a binding clearance.

R v IRC exp MFK [1989] STC 873, contains the oft-quoted phrase of Bingham LJ at page 892 that "... it is necessary that the taxpayer should have put all his cards face upwards on the table". Further, phrases such as "full disclosure of all material facts known to [the taxpayer]" abound. No clear judicial attempt is made, however, to indicate what sort of facts would be "material", nor what the consequence would be if there **were** relevant facts but they were not known to the taxpayer.

Matrix Securities v IRC [1994] STC 272 goes further to extend the matters which are material and relevant and, therefore, need to be disclosed. From Lord Jauncey's speech, it appears that "full disclosure" means more than disclosing sufficient information to enable inferences to be drawn therefrom. He appears to say that the taxpayer has a duty to think of all the questions that a competent tax inspector would want answered and answer them (see page 290 at h). This appears to place a very heavy duty of disclosure on the taxpayer — and one which he will never be sure that he has discharged.

In the circumstances, it is the writer's view that it will be relatively easy for the Revenue to resile from any ruling given, on the ground that full disclosure was not made by the taxpayer.

That being the case, it is arguable that the proposed pre-transaction rulings will not provide the promised certainty of tax treatment. Consequently, their desirability, and indeed their usefulness, appear to be called into question.

Cynics would, however, say that the proposed scheme merely formalises the present state of affairs, i.e., that the Revenue's view of the law is relevant, perhaps more so than what the statute actually says and, therefore, it is best to find out the Revenue view before doing anything.

Conclusion

Whilst certainty of tax treatment is eminently desirable it is by no means certain that pre-transaction rulings will provide that certainty.

This is because it will be open to the Revenue, after the transaction, to resile from a positive ruling given, on the ground that the Revenue was not made aware of all the relevant facts and/or issues.

Further, it is arguable that certainty of tax treatment can only exist where both taxpayers and the Revenue understand the law to mean the same thing.

The law should ideally, therefore, be as clear and unambiguous as possible. The duty to do this should, and does, rest with the body designated to make the law — Parliament — not the Revenue.