Relying on the HMRC Manuals

Most tax advisers, and many of their clients, will at one time or another have drawn comfort from - or even placed absolute reliance upon - a statement made or confirmation given by HMRC in one of its many published Guidance Manuals. Advisers might also have assumed, particularly in the case of a highly technical or arcane issue, that there was no particular need to explain to the client that reliance had been placed on something included in a Manual.

It is certainly true that the degree of reliance placed upon the Manuals is likely to have depended on the topic or area of tax in question. Having recently carried out what seems to have become an annual scrutiny of the pages in the Capital Gains Manual on the tax treatment of open offers of shares made pro rata to a company’s shareholders and, in particular, the question of whether such transactions are in practice going to be treated as reorganisations of share capital for capital gains purposes, it is tempting to conclude that there is very little in these pages which is expressed with anything like enough clarity for it to be possible for HMRC’s true position to be ascertained. The unsatisfactory result of this confusion is that most prospectuses for standard open offers continue to be despatched with the rather unhelpful disclosure that the issue of the new shares may or may not be treated as a reorganisation of share capital.

However, it now turns out that coping with confusion (or silence) in the Manuals may, for taxpayers and their advisers, be the easy part. To the extent that there are clear statements of HMRC practice in the Manuals, the more difficult question now seems to be whether HMRC is actually bound by its published position.

Decision of First-tier Tribunal in Hanover Company Services v HMRC [2010] UKFTT 256

The substantive point at issue in the Hanover case was whether the Company made separate supplies of standard-rated company formation services and zero-rated printed material or, alternatively, a single composite supply of standard-rated company formation services to which the supply of printed material was merely ancillary. The Company had in fact treated itself as making separate supplies, so that the supply of printed material could be zero-rated. This was on the basis that it understood that this was the practice adopted by the “industry leader”, Jordans; that it had explained its practice to an HMRC officer (during a visit) and had not been told by that officer that the practice was incorrect; and that it had subsequently sought advice from its accountants who, after consulting the relevant HMRC Manual (and other published guidance), had advised it that the practice was correct. The Manual in question stated specifically that the provision of printed material by a supplier of company formation services could be zero-rated provided that the prints were separately itemised on the invoice (just as Hanover had done).

Assessments for VAT were nevertheless raised on Hanover (some years later) on the basis that it had made a single supply of standard-rated company formation services. In disputing this, the Company’s principal argument was that it had a legitimate expectation that HMRC would apply the guidance published in the relevant Manual (the Supply and Consideration Manual) and that HMRC should therefore be “estopped” from making the assessments.
The Tribunal held, in essence, that the circumstances of the case did not provide Hanover with the legitimate expectation that it claimed. In the Tribunal's view, there had been no unfairness on HMRC's part amounting to an abuse of power. There seem to have been two main reasons for this conclusion. First, it was the Company's accountants - rather than Hanover itself - who had consulted the HMRC guidance, so that Hanover itself did not actually rely on any practice of HMRC; and, secondly, the effect of the so-called “health warning” at the beginning of the HMRC Manuals was that the representation in question (concerning the zero-rating of supplies of printed material) was not capable of giving rise to a legitimate expectation on the part of the taxpayer, because the representation “was not devoid of relevant qualification”.

The health warning
What the health warning actually says is that it “should not be assumed that the guidance is comprehensive nor that it will provide a definitive answer in every case”. It then goes on to state that the guidance in the Manuals is “based on the law as it stood at the date of publication. HMRC will publish amended or supplemental guidance if there is a change in the law or in the Department’s interpretation of it”.

It is very difficult to see why it is that any of the above should constitute a “relevant qualification” to the Manual representation in issue in the Hanover case. In other words, where a statement made in the Manuals is itself clear and unambiguous, and is not taken out of context, there seems no good reason why that statement should be regarded as being subject to a relevant qualification.

Legitimate expectation
The Tribunal’s focus on “relevant qualification” appears to be derived from a judicial statement in one of the earlier High Court decisions on the doctrine of legitimate expectation to the effect that the relevant HMRC ruling or statement relied upon should be “clear, unambiguous and devoid of relevant qualification”. Viewed in its proper context, this would seem to be a reference to a qualification embedded in, or at any rate related specifically to, the HMRC statement or representation itself. The “health warning” at the beginning of the Manuals really seems to be besides the point.

It is also noteworthy that the Tribunal’s finding that the Company did not itself consult the relevant Manual led it to conclude that there had been no reliance on any practice of HMRC, so that there could be no legitimate expectation on the Company’s part. The Tribunal does not appear to have considered whether HMRC’s previous conduct in relation to the VAT treatment of printed material in fact accorded with the approach adopted by Hanover and, if so, whether HMRC’s consistent past practice had itself induced a legitimate expectation on the part of Hanover.

As far as the Manuals themselves are concerned, it might also be asked why it is not legitimate for a taxpayer to expect HMRC to stand by their content (when it is clear and unambiguous), irrespective of whether the taxpayer - or anyone else - has actually scrutinised the relevant paragraphs.

Impact of the decision
Nevertheless, taking the decision at face value (and notwithstanding that it is only a decision of the First-tier Tribunal), it would appear that tax advisers need to adopt a rather different approach to the Manuals than has hitherto been the case. In the first place, it would seem prudent for advisers to explain the relevant technical issue to the client, send the client a copy of (at least) the relevant extract from the Manual and explain clearly how the Manual addresses the technical concern. Moreover, in doing so, the advisers should inform the client that, however clear HMRC’s representation might be, the client cannot place absolute reliance on it because it will always be open to HMRC to depart from its stated view or practice. In other words, the Manual becomes no more than an
indication of what HMRC’s position might be expected to be, so long as HMRC does not decide to adopt a different position (retrospectively, if it so wishes).

The first of those points (that it is not sufficient for a taxpayer to rely on its advisers’ consultation of the Manuals) seems somewhat harsh, particularly given the technicalities and general complexities involved in tax compliance. The introduction to the Manuals (the health warning) does say that the guidance is published for the information of taxpayers and their advisers; and when an adviser pays regard to the Manuals in the course of advising a particular client, it would seem perfectly reasonable for the taxpayer itself to be able to benefit from the guidance in question. The Tribunal’s view on this issue would seem to make it quite difficult for a relatively unsophisticated taxpayer ever to be able to rely on the Manuals. Moreover, their view would appear to create a distinction between the position of tax advisers on the one hand and tax agents on the other (see, for example, the rather different Tribunal decision in B&J Shopfitting Services v HMRC [2010] UKFTT 78), the underlying justification for which is far from obvious in terms of policy.

Way forward
The upshot of this litigation is clearly unsatisfactory. It is true that the decision is only one of the First-tier Tribunal and it can certainly be argued strongly that the Tribunal was wrong to conclude that the health warning at the beginning of the Manuals amounted to a “relevant qualification” and was therefore enough to deprive the taxpayer of a “legitimate expectation” that the particular statement in the Manual would be respected by HMRC. It might also be argued that the fact that the taxpayer did not itself consult the Manual should not, in itself, bar a claim based on legitimate expectation.

However, it is really for the courts to address these issues and it must be hoped that this case will be appealed by the taxpayer and that the Tribunal’s decision will be reversed in all material respects. It is certainly very hard to imagine that HMRC will be prepared to adjust the terms of the health warning or take any other steps with a view to allaying taxpayer concerns on these fundamental practical issues.

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