LONDON TRIBUNAL CENTRE

B E T W E E N:

UNIVERSITY OF BRISTOL

Appellant

- and -

THE COMMISSIONERS OF CUSTOMS AND EXCISE

Respondents

Tribunal: Miss J C Gort (Chairman), Mr K C Manterfield FCA

Mr Andrew Young, of PricewaterhouseCoopers, for the Appellant

Mr Hugh M^{c}Kay, of Counsel, for the Respondents

Sitting in public in London on 23, 24 and 25 April 2001

Decision: 17 July 2001

DECISION

1. This is an appeal against a decision of the Commissioners in respect of an overclaim of residual input tax by the Appellant. Two assessments were issued, the first assessment relates to tax period 10/96 and is in the sum of £17,144 plus interest. It was notified to the Appellant by a fax dated 30 October 1999; there is a dispute between the parties as to whether the assessment was in fact made on 30 October 1999. The second assessment relates to tax periods 01/97 to 10/98 and was made by the Commissioners on 3 November 1999 in the sum of £50,962 plus interest. This assessment was notified to the Appellant by letter of 3 November 1999.

2. The disputed decision relates to the operation of a special partial exemption method which had been agreed between the parties. The Appellant claims that with the knowledge of Customs and Excise it was using consolidated accounts to calculate its VAT liability, the Respondents dispute that they were aware before 1995 that consolidated accounts were being used in the operation of the special partial exemption method, and claim that they would never have agreed to their use. The Appellant claims to have operated the method correctly, but in the event that it is held that it did not do so, then it is claimed by the Appellant that the first purported notice of assessment is time barred and neither notice of assessment is valid.

The background

3. The Appellant is a non-profit making body based in Bristol. It has been

registered for VAT since 1 April 1973.

4. The Appellant has many departments, some of which only make exempt supplies, but several make taxable supplies.

5. The Appellant has four subsidiary companies, Oval (717) Ltd, Bristol Earthquake and Engineering Laboratory Ltd, University of Bristol Services Ltd and Park Row Ltd. All these companies had VAT registration numbers at various times, Bristol Services Ltd being registered from 27.11.95 and Park Row Ltd being originally registered on 1.10.95, having deregistered on 1.5.97 and re-registered on 20.11.97.

6. In 1992 the Appellant became aware that, by not operating a full partial exemption method, it was overpaying value added tax. Discussions were therefore initiated between the Appellant and the Respondents in order to agree and implement a single, special partial exemption method ("the scheme"). Deloitte Haskins & Sells, who later merged to form Coopers & Lybrand, and who subsequently merged again to form PricewaterhouseCoopers, were employed by the Appellant to carry out negotiations. The chief negotiators were Lorraine James and Roger Broughton. Lorraine James subsequently left Coopers & Lybrand to work for the Commissioners. Various officers from the Respondents were involved in the meetings, and Derek Allen, the senior accountant of the Appellant was involved in all the meetings.

7. During the course of negotiations a spreadsheet was produced by the Appellant to reflect the application of the agreed method of calculation of the scheme. The University submitted returns on the basis of the spreadsheet but it was not until 8 November 1994 that the scheme itself was formally set down. The scheme was accepted by the Appellant by a fax dated 28 November 1994 and formally approved by the Respondents by a letter dated 30 November 1994.

8. The special method agreed between the Appellant and the Commissioners is set out in a letter of 8 November 1994 from Tony Harrison, who was a VAT assurance manager and surveyor at Customs and Excise, to Derek Allen at the University of Bristol with a copy to a Mr Ian Barrett of Touche Ross. (Mr Broughton was not at Coopers & Lybrand at this time, but rejoined them at the end of November 1994.) The letter where relevant states as follows:

> "The following arrangements have been approved for use with effect from 1 August 1994 for a minimum period of two years from the date of this letter.
>
> 1. Your tax year begins on 1 August and ends on 31 July. You are to calculate your deductible input tax with effect from 1 August 1994 on the following basis:
>
> (a) Each department will identify all the supplies, acquisitions and imports received which are wholly used, or to be used by each department in making taxable supplies. The input tax thereon is recoverable;
>
> (b) Each department will identify all the supplies, acquisitions and imports received which are wholly used, or to be used, by each department in making exempt supplies. The input tax thereon is not recoverable.
>
> (c) Each department will identify all the supplies, acquisitions and imports received which are wholly used, or to be used by each department in connection with any activity other than the making of taxable supplies.

> The input tax thereon is not recoverable.
>
> (d) To determine the recoverable amount for the departments shown at (e) below of any non-attributable input tax (other than those supplies excluded under paragraph 2 below) according to the following formula:
>
> Total value (excluding VAT) of taxable supplies x 100
>
> Total value (excluding VAT) of taxable and exempt supplies
>
> Equals percentage of remaining input tax which can be deducted.
>
> This percentage is to be calculated to two decimal points and is not to be rounded up or down. This will also apply when you carry out the annual adjustment (see 4 below).
>
> (e) It is agreed that the non-attributable input tax for the following departments only will be included in the formula at (d) above. Using your accounting codes the departments are:
>
> ACSD; AENG; BBUI; BELE; BMAEEC; BUAR; BURS; CARA; CENG; CENT; COMP; DEVO; EENG; FINC; HOUS; LIBR; MENG; PERS; REPR; SAFE; SECO; SECU; SITG; STAT; TELE."

9. The letter continues with various exclusions from the calculations and then sets out the method of carrying out the annual adjustment.

10. At paragraph 4 it is stated that the method is subject to review by Customs and Excise and may be withdrawn at any time, but also that if in the two year period following commencement of using the method if the circumstances of the business changed to the extent that the method no longer produces a fair and reasonable attribution of input tax to taxable supplies, then the Appellant may write to the office requesting a change of method. It was agreed between the parties that the aim of the special method was to produce a fair and reasonable attribution of input tax to taxable supplies.

The legislation

11. The power for the Commissioners to approve a special method is given by regulation 102 of the VAT Regulations 1995, which allows methods other than those that are set out in regulation 101.

12. Regulation 102 states:

> 102-(1) Subject to paragraph (2) below and regulation 103, the Commissioners may approve or direct the use by a taxable person of a method other than that specified in regulation 101, save that where the use of a method was allowed prior to August 1989.
>
> (2) Notwithstanding any provision of any method approved or directed to be used under this regulation which purports to have the contrary effect, in calculating the proportion of any input tax on goods or services used or to be used by the taxable person in making both taxable and exempt supplies which is to be treated as attributable to taxable supplies, the value of any supply within regulation 101(3) shall be excluded.
>
> (3) A taxable person using a method as approved or directed to be used by the Commissioners under paragraph (1) above shall continue to use that method unless the Commissioners approve or direct the

termination of its use.

(4) Any direction under paragraph (1) or (3) above shall take effect from the date upon which the Commissioners give such direction or from such later date as they may specify.

13. Section 73 of the VAT Act 1994 allows the Commissioners to assess the amount of VAT due where it appears to them that the returns are incomplete or incorrect. Section 73(6) sets out in part the relevant time limits as follows:

Section 73(6)

"An assessment under subsection (1), (2) or (3) above of an amount of VAT due for any prescribed accounting period must be made within the time limits provided for in section 77 and shall not be made after the later of the following-

(a) 2 years after the end of the prescribed accounting period; or

(b) one year after evidence of facts, sufficient in the opinion of the Commissioners to justify the making of the assessment, comes to their knowledge,

but (subject to that section) where further such evidence comes to the Commissioners' knowledge after the making of an assessment under subsection (1), (2) or (3) above, another assessment may be made under that subsection, in addition to any earlier assessment."

14. Section 77 provides:

(1) Subject to the following provisions of this section, an assessment under section 73, 75 or 76, shall not be made -

(a) more than three years after the end of the prescribed accounting period or importation or acquisition concerned ...

15. The Tribunal was referred to the following cases:

Investors Compensation Scheme Ltd v. West Bromwich Building Society [1998] 1 AER 98

Subhan, Uddin and Mustak v. Commissioners of Customs and Excise (2001) VAT Decision No.17110

University of Huddersfield v. Commissioners of Customs and Excise (2001) VAT Decision No. 17159

BP Supergas v. Greece [1995] STC 805

The facts

16. Mr Roger Broughton and Mr Derek Allen gave evidence on behalf of the Appellant. Mr Ian Jones, Mr Anthony Harrison, Mr John Davy and Ms Sally Blackford gave evidence on behalf of the Respondents. An agreed bundle consisting of four volumes was produced to the Tribunal.

17. Mr Roger Broughton is a qualified chartered accountant who had joined Coopers & Lybrand at the time the negotiations for the special methods were starting. Five to six people were involved in the task which took about three to four months. There were three main issues to be decided at that time:

1. The value of the input tax suffered by the University of Bristol in a chosen year. The University recorded all its expenditure gross and therefore a major sampling exercise had to be undertaken to determine the amount incurred for a chosen year. This involved sampling thousands of invoices.

2. In order to determine the numerator for the partial exemption calculation the value of the total taxable income needed to be determined for a chosen year. The University provided student education which was exempt from value added tax and it also undertook research and consultancy work which produced a taxable income. Some items related to both the exempt and taxable matters and as a first step the University had to determine what input tax it could recover relating directly to the taxable activities. The second step was to determine how much related to the exempt activities which could not be recovered and thirdly matters which related to both activities had to be determined so that input tax could be apportioned. These activities were mainly overheads.

3. The value of the combined total taxable income and the exempt income for a chosen year needed to be determined. This would become the denominator in the partial exemption calculation.

18. To determine the numerator Coopers & Lybrand took the VAT returns for one year which gave the declared output tax, and from this they could work out the net taxable sales. In order to determine the denominator it was decided that, because the University was such a large entity having 140 departments, it would be an enormous task to ascertain this. According to Mr Broughton it was then agreed with the Commissioners that the best source of this information would be the University's published accounts which were independently verified by outside auditors. The total income was taken from the University's consolidated accounts. This was considered by Coopers & Lybrand to be an attractive method, because the accounts were published it was simple for Customs and the University to cross-check and verify the partial exemption calculation. The Commissioners disputed that they were aware from the outset that consolidated accounts were to be used.

19. A sampling exercise was carried out on the financial year ended 31.7.92. A set of standard Lotus spreadsheets was developed to record the fndings of the sampling exercise and also to calculate the partial exemption recovery rate. Bristol University was the first to carry out such an exercise and therefore they were continually in touch with the Bristol VAT office. Sally Blackford and Tony Harrison were the two main contacts with Customs and Excise. Customs and Excise agreed that the University could tine this method to claim back tax over the previous five years.

20. The spreadsheet used to summarise the inputs recorded the year in question, and then divided that up into the income which had to be omitted entirely from the calculation (which was mainly the grant from the University Funding Council), the exempt income and the vatable income. The exempt income combined with the

vatable income gave the denominator for the calculation. Applying that figure to the numerator gave a percentage of 6.77. According to Mr Broughton, Sally Blackford of Customs and Excise was in regular contact with him about this method and it was reviewed by Tony Harrison at the final stage. Mr Harrison never indicated that Customs and Excise had not understood the method proposed. It was Mr Broughton's opinion that this was such a big matter for the University that the full co-operation and involvement of Customs and Excise was needed to complete the exercise. Six or seven other universities subsequently employed Coopers & Lybrand to carry out a similar exercise and Sally Blackford was used as a contact between those universities and their own local VAT officer.

21. In 1994 the Appellant was told that the method, which they had been operating since 1992, needed to be put into writing and therefore what was in the spreadsheets was reproduced in the letter of November 1994. The letter reflected the agreed special method, although whether or not it contained precisely all the matters agreed was a matter of dispute between the parties.

22. Customs and Excise had been provided with copies of all the University's published accounts between 1973 and 1992. In the subsequent years the published accounts were used to calculate the partial exemption and were always available to Customs and Excise. It was Mr Broughton's evidence that Customs and Excise had been specifically provided with copies of the report and accounts. They had been attached to the back of Mr Allen's working papers.

23. The 1994 accounts have an explanatory note at the front which, under a chapter headed "Basis of preparation" refer to the accounts of the Long Ashton Research Station, which is part of the University, but which is financed independently. Long Ashton provided separately audited financial statements to 31 March each year and the note says that the accounts of Long Ashton had been consolidated in accordance with FRS2 and continues: "The income and expenditure account also reflects transactions of the University's wholly-owned subsidiary companies Oval (717) Ltd and University of Bristol Services Ltd". FRS2 is the standard accounting method where there are subsidiary undertakings. The University accounts were consolidated according to the method set out in FRS2.

24. There was a meeting on the 12 December 1995 between John Davy of Customs and Excise, Derek Allen, who is the senior accountant at the finance office of the University of Bristol, and Roger Broughton. Roger Broughton made notes of the meeting and a copy of those notes dates 19 December 1995 states:

> "DA (Derek Allen) had calculated the recovery percentage using the same method that had been agreed by Customs in previous years. At the end of the visit JD (John Davy) raised no queries."

The note continues to the effect that Derek Allen showed John Davy the working papers for the calculation for the annual adjustment. Those working papers showed details of the VAT returns for the year ending 1993/94 and then set out an analysis of the annual accounts for the year to 31 July 1994 to establish the taxable activity percentage. The consolidated accounts of the University were said to be attached to these working papers.

25. By the time of this meeting the University had adopted the practice of carrying out an annual adjustment using the recovery percentage from the previous year for the current year and these figures were then adjusted for the actual figures which were known at the year end. The University year ends in July and therefore the October value added tax returns were calculated according to the annual adjustment.

26. At the meeting in December John Davy had wanted to go through the recovery rates for July 1995 year end using the agreed method. He reviewed the calculation of the annual adjustment which at that time showed an additional payment to the University of £50,000 and, having checked the calculations and the annual adjustment, he was happy to allow the recovery. He specifically checked the input tax percentage. At that time there had been a change from the VAT legislation which made more of the University income taxable and some departments which had previously not been included had to be included and this was done with Customs and Excise agreement. The draft accounts for the year ended 31 July 1995 which were shown to John Davy at that meeting are headed "Consolidated Income and Expenditure Accounts for the year ended 31 July 1995". Similarly attached to the working papers was the balance sheet which is headed "Consolidated Balance Sheet as at 31 July 1995".

27. It was accepted by Mr Broughton that the standard method for calculating partial exemption in the absence of a specially agreed method was as set out in regulation 101 which requires that all taxable supplies be put into a numerator and all taxable and exempt supplies go into the denominator.

28. The University income and expenditure account for the year ended 31 July 1994 does not specifically refer to the account being consolidated, other than in the explanatory notes (see above). In Mr Broughton's opinion the word "reflects" in those notes meant "includes" and on reading them he would deem the accounts to be consolidated.

29. Derek Allen was specifically charged with preparing the University's value added tax returns and with undertaking the partial exemption calculation. He had been involved in negotiations with Customs and Excise throughout most of the relevant period other than for a short period from November 1994 when he had returned to New Zealand. Mr Allen confirmed to the Tribunal that the calculations for the annual adjustment would routinely be provided to Customs and Excise supported by a copy of the University's published accounts. Neither John Davy nor any other officer of Customs and Excise ever asked for unconsolidated accounts. It was not until July of 1998 that he was informed by Customs and Excise that by using consolidated accounts they were distorting the figures.

30. Sally Blackford was the officer of Customs and Excise responsible for Bristol University for the period July 1992 to March 1994. She had been involved in the early discussions both about making a retrospective claim to input tax and the special exemption method which was to be used for future recovery. It was her evidence that the agreement with Lorraine James, who at the time was with Coopers & Lybrand, was that all taxable supplies should be used for the formula, and if it had been known that consolidated accounts were being used then this would have been queried by her.

31. Miss Blackford did not recall whether she had seen the consolidated accounts or not, however she had looked at the income in depth and she had examined a document called form 3 which it is a legal requirement for university to complete. Form 3 required the university to set out specific details of income and expenditure in a particular manner.

32. Mr Harrison had previously accompanied Sally Blackford from time to time to the University. The first of these visits had taken place on 5 October 1993 when he met Mr Allen and a representative of Coopers & Lybrand.

33. At a visit to the university on 2 November the basis for the special method was agreed. Mr Allen's spreadsheet was used and it was agreed that Mr Harrison would send a letter to Mr Allen setting out the proposed special method. Mr Harrison was unable to recall any discussion of the use of consolidated accounts in arriving at the denominator. Mr Harrison said he would never have agreed to the use of consolidated accounts because a fraction that uses different basis for its numerator and denominator was not going to give a proper figure for input tax recovery. Thus if the top number was arrived at by looking at all taxable supplies, including those made between subsidiaries and the University, and a lower figure was arrived at by looking at all taxable and exempt supplies except those made between subsidiaries and the University, it would not tell anything about the proportion that taxable supply made tip of all supplies. It did not provide an input tax recovery percentage accurate to two decimal places. Mr Harrison informed the Tribunal that the only accounts he would accept as being consolidated were ones which were clearly headed "consolidated".

34. In Mr Harrison's opinion the letter of 8 November 1994 contained everything that was needed to describe the method and omitted nothing. He agreed that at the time of examining the spreadsheets he had seen extracts from Form 3. His powers were only to agree a special method with a taxpayer, he was not able to direct the use of one. It would not be possible to get a fair and reasonable result if the items above the line in the equation used were not reflected below the line.

35. John Davy was the officer of Customs and Excise responsible for Bristol University for the period April 1995 to March 1996. He was present at the meeting on 12 December 1995 when he examined the method used for calculating the partial exemption for the year ended 31 July 1995. In a witness statement dated l April 2001 he stated in respect of the annual adjustment: "… I saw that the denominator of the fraction was made up of taxable income and that this taxable income was extracted from the VAT returns submitted covering the year to 31 July 1995. The value of the denominator came from the annual accounts. I queried the fact that the values for the top and bottom of the fraction were from different sources but were assured that this wag what had been agreed between the University and Bristol VAT office." He continued that he believed that he had seen neither consolidated nor ordinary annual accounts, and he repeated this in his evidence to the Tribunal. Like Mr Harrison, he told the Tribunal that he understood that the letter of November 1994 covered the agreement in its entirety and if a matter were not in the letter, then it had not been agreed.

36. However under cross-examination Mr Davy accepted that grant income was to be excluded from the denominator, and that this was not specifically stated in the letter setting out the special method. There was however some grant income which

was included in the denominator and this was known as a "bolt-on". It referred to grant income for specific educational work, and some of this was included in the denominator and some was not. According to Mr Davy all parties at the time had understood how the grant income was to be treated. It was not classed as exempt income, but was outside the scope of value added tax. He did not know why it had been agreed that "bolt-ons" were to be included in the denominator.

37. Following Mr Davy's evidence, Mr Harrison was recalled. He remained of the opinion that the letter hilly set out all relevant matters. Insofar as the grant income was concerned it was his opinion that item 1(a) of the letter referred to as taxable supplies, so it was required to be identified under that. Further or alternatively, it was included in subparagraph (c) which covered everything else. He considered that grant income was a supply, and as a source of income should be included.

38. Ian Jones is the officer of Customs and Excise currently responsible for the University of Bristol and has been so since August 1997. In July 1998 he had carried out a routine visit to the University. The purpose of the visit was to review the partial exemption calculations. He requested copies of the University's accounts and was given copies of the published accounts, which are the consolidated ones. From the University's 1996/97 accounts he noticed that Note 36 stated that the subsidiary companies' undertakings had been consolidated in the University's accounts and this appeared to him to be the first time this statement had been made, and the subsidiaries listed in the financial statements. From this he deduced that the supplies by the University to the subsidiaries would not be included in the accounts and therefore those supplies would not be included in the value of taxable and exempt supplies which made up the denominator for the partial exemption method. The taxable supplies made by the University to the subsidiaries would, however, be included in the numerator.

39. On 17 August 1998 Mr Jones wrote to the Appellant asking for confirmation that the supplies by the University to the subsidiary companies would not be included in the declared income in the accounts. He received no reply to that letter and sent reminders subsequently in September and October. Again he received no reply and so he wrote on 5 November 1998 advising the Appellant that he considered the total income figure used by the University for partial exemption purposes was incorrect and requested details of the supplies by the University to the subsidiary companies for the years 1995/96, 1996/97 and 1997/98.

40. By a letter dated 28 November 1998 the Appellant wrote saying that it was accepted that the use of consolidated accounts caused a problem when recording the true level of income, and it was also accepted that the matter should be corrected with effect from 1 August 1998. The Appellant wrote as follows:

> "The partial exemption method the University operates is a special method agreed with your department on 30 November, 1994. The spreadsheet which sets out the calculation of the recovery percentage was also agreed with your department at the same time. When devising the method both the University and Customs appreciated the complexity of the business and therefore the method agreed was one which was easy to operate for the University and easy to check for Customs. As a result compromises were made on both sides to devise a method that was fair and reasonable.
>
> Accordingly, although we fully accept that the mathematical errors in

> calculating the recovery percentage should be corrected, retrospective changes to the basis of the calculation cannot be made.
>
> This point is highlighted by the issue you raised regarding the use of consolidated accounts. The method agreed was that the University would take its total income figure (after agreed adjustments) on the published consolidated accounts as denominator of its partial exemption method. As you point out this potentially leads to some difficulties regarding income, which may be netted off on consolidation. However, the special method operated was the agreed method.
>
> In summary we feel retrospective changes to an agreed special method cannot be made. We appreciate that the queries you raised regarding the consolidated accounts and self-supplies of printing need to be addressed for the future (i.e. from 1 August 1998). However, the method used for the past, was agreed as being fair and reasonable by both parties."

41. It was Mr Jones' opinion that he was not seeking retrospectively to amend an agreed method, but was seeking assurance that the agreed method had been correctly applied.

42. In his evidence, Mr Jones accepted that it was common practice for universities to utilise the accounts to arrive at the total income figure for partial exemption purposes, however he did not consider that this overrode the need to make any adjustments to ensure an accurate reflection of the true value of the figure. He considered it fair and reasonable to expect the value of taxable supplies included in the denominator to be the same as that used for the numerator, and that the value of any exempt supplies should also include exempt supplies to the subsidiaries.

43. Further correspondence ensued by the details of the transactions with the subsidiaries were not supplied to the Commissioners. There was a meeting between 25 to 29 January 1999 in which Mr Jones was provided by the University with the schedules and copy invoices detailing supplies to the University of Bristol Services Ltd for May and August 1996, Mr Jones did not have the details. He therefore based the University's supplies on the input tax recovery in the returns submitted by the University of Bristol Services Ltd. Mr Jones again wrote to the University and asked for a breakdown of the University's charges to the subsidiaries. This was not provided. Again further correspondence ensued. This culminated in the meeting of 29 October 1999 at which no agreement was reached but at which Mr Jones confirmed that he would review the correspondence between Coopers & Lybrand and Customs prior to the agreement of 30 November 1994 before commenting further. He would then issue a final ruling with regard to this matter.

44. The 29 October 1999 was a Friday. The three-year period for issuing an assessment in respect of the year 1996 ended on 31 October 1999. Mr Jones recalled this fact late on Friday and therefore went into the office on Saturday 30 October in order to make an assessment. He completed an Excel spreadsheet on his computer on which he calculated the amount of tax due. He also wrote a letter to the Appellant. However, when he came to printing off the spreadsheet and the letter he found that there was a network printer fault. He therefore sent a handwritten fax to the University advising them that he was issuing an assessment for £17,144 plus interest in relation to 1995/96 annual adjustment and the October 1996 accounting period. He completed a Form 641 in which he recorded details of the trader and the amount of

the assessment and signed and dated it. On Monday 1 November he posted a copy of the letter that he had typed on the Saturday and of the Schedules. The assessment itself was issued on 3 November. On that date Mr Jones also wrote to the University advising them that he was issuing an assessment for £50,962 plus interest for the periods 01/97 to 07/98 together with the 1997/98 annual adjustment in period 10/98. That assessment was issued on 8 November 1999.

45. The Appellant subsequently requested a reconsideration of the assessments.

46. It was Mr Jones' opinion that no assessment could have been made until detailed information as to the supplies to the subsidiaries had been obtained. He accepted that he had not taken steps to find out when the Commissioners were first aware of the use of consolidated accounts. He had discussed the case with Lorraine James but she did not tell him that consolidated accounts had been used. Tony Harrison had had no recollection of consolidated accounts being mentioned.

47. Mr Jones was challenged by Mr Young to the effect that he had not in fact made the assessment on the 30 October, but had merely gone into the office, had written the fax and sent it out but he had done the necessary work on the Monday 1, November, rendering the assessment out of time. This was denied by Mr Jones. According to Mr Jones he had reviewed the correspondence, he had made the calculations and he had put the letter onto the computer and had also handwritten the fax at the time when he was in the office on the Saturday morning. It was subsequently submitted by Mr Young, although not put to Mr Jones, that it would not have been possible for him to have done all these things given that he went into the office at about 13.45 on the Saturday and the fax is timed at 14.12, giving him only 27 minutes to complete all the various tasks.

48. The Appellant's representatives had asked for the Commissioners to supply evidence from their IT officer to confirm that the network was down on that Saturday. The Commissioners declined, saying that the officer himself could be cross-examined about the matter.

49. The Tribunal finds it surprising that the officer was able to review the correspondence, type a letter, complete a 641, complete spreadsheets on Excel on which he had to work out calculations, and to discover that the Printer was not working in the time available. However, in the absence of expert or other evidence we are prepared to accept the officer's word as to the functions which he carried out.

The Respondents' case

50. Mr M^{c}Kay submitted that the first question to be decided by the Tribunal was whether the special partial exemption method agreed between the parties allowed for the use of consolidated accounts in fixing the denominator, but not the numerator, of the fraction. Secondly, the Tribunal had to construe the terms of the contract, and to decide whether it was possible to construe the fraction in such a way that "total value" had a special meaning. The third issue for determination was the question of whether or not the assessments had been made within the appropriate time limits.

51. Both regulations 101 and 102 were directed to find the fairest and most accurate method of attributing input tax to taxable supplies made by a partly exempt

trade to allow for the trader's recovery of input tax. In the present case the relevant then is paragraph 1(d) of the scheme. It was submitted that the terms of this agreement are unambiguous. The only proper meaning to attach to "total" is the natural meaning of the word, and it was not to be understood in any other sense, still less a sense that has a different means of calculating the top and bottom parts of the fraction.

52. The purpose of the method was to seek the proper proportion of input tax, and to achieve that end a fraction multiplied by a 100 is used to give a percentage. That percentage represents the "proportion" of input tax that qualifies for credit.

53. It was submitted that it was not rational to compute the figures for the top line differently from the method of computing those for the bottom line. This would defy the rational basis underlying the legislation which is aimed at ascertaining the "proportion" of input tax that qualifies for credit, as well as defying the basic arithmetical notions behind the concept of fractions. In Mr M^{c}Kay's submission, by using consolidated accounts the Appellant was not just comparing oranges and apples, it was more akin to comparing oranges with Tuesday afternoons.

54. It was the Commissioners' case that because the proposition advanced by the Appellant was so startling, if it were the correct one, one would expect to find a clear and unambiguous reference to it in the agreement. In the agreement there is a reference to the particular treatment of supplies of property, which is a departure from the typical case, but there is no mention of a treatment allowing for the fraction to have the numerator and denominator computed on different bases.

55. For there to be an agreement there must be a meeting of minds, and for such a departure from the accepted method as set out in regulation 101, there would have to have been proper discussions. It was clear from the evidence that the matter of consolidated accounts was not discussed at all. The burden was on the Appellant to draw the Commissioners' attention to the point, VAT being a self-assessed tax. The Appellant here had special knowledge and should have made the Commissioners aware of the situation.

56. Mr M^{c}Kay pointed to the evidence of the Appellant's witnesses, who are both accountants. In particular Mr Allen had not had any real understanding of consolidated accounts, and Mr Broughton had thought that the word "reflects", which is found in the note to the 1994 account, meant "includes". It was not obvious on the face of it at the time of the agreement that the accounts were consolidated, it was only in the third set of accounts dated 1995 that the heading "consolidated" appeared. It was not possible for there to have been a term in the agreement that consolidated accounts were used because there was no suggestion made about this by either side, and there was no meeting of minds.

57. The spreadsheets referred merely to "annual accounts", with no reference to those accounts being consolidated. The contents of the spreadsheets themselves had to be determined by reference to the special method. The Tribunal must examine what is the meaning of "total". For this purpose the Tribunal was referred to the case of *Investors Compensation Scheme Ltd*, which involved the mis-selling of home income plans. It concerned the interpretation of a contractual document, although it was not a VAT case. The headnote of that case reads that it was held that:

> "The matrix of fact against which a contractual document was to be construed included anything which would have affected the way in which the language of the document would have been understood by a reasonable man. Although the court would as a matter of common sense normally apply the presumption that words were to be given their natural and ordinary meaning, if it was clear from the background that the parties, for whatever reason, had used the wrong words or syntax or that something must have gone wrong with the language used, the court was not obliged to attribute to the parties an intention which they plainly could not have had ..."

58. In the present case nobody had alluded to the consolidated accounts, therefore they could not be considered to be part of the background knowledge. There were no clues from the background that the fraction should not bear its ordinary and natural meaning. If one expressed the fraction as A over A + B it was clear that the "A's" must match. Furthermore as the special method was meant to produce a result which was accurate to one hundredth of a percentage point, this did not allow for the Appellant's construction.

59. With regard to the time limits, the Appellant's argument that "notify" and "assess" were conjunctive had been repeatedly discredited. They were two separate acts which could not take place simultaneously. The time limits applied to the assessment, and not to notification of it.

60. With regard to the Appellant's argument that the Commissioners had judicial notice of the document FRS2, that notice was not referred to in judicial terms. In the present case the assessment had to be made to best judgment, and had to be an assessment of an amount. For that to be done there must be sufficient evidence of the facts which governed the amount. Whilst the Commissioners may have known of the consolidated accounts, until they had sufficient material knowledge of the transactions within the University departments they were unable to assess the amount. Mr Jones had asked for details which had not been forthcoming, it was not until he got sufficient information to justify the assessment that it could be made. He did not obtain this information in the summer of 1998 but not until different times in January, February and March 1999.

61. The Tribunal was referred to the case of *Suban, Uddin & Mustak*, where the *Royal Bank of Scotland Group Plc v. Customs and Excise Commissioners* (1999) VAT Decision No.16418, was considered. In that case the Tribunal stated inter alia as follows:

> "It is suggested that the decision of the Edinburgh tribunal in *The Royal Bank of Scotland* case is authority for a contrary view. With regret, we find ourselves unable to follow that decision, which appears to us to be contrary to the weight of authority. We do, however, find ourselves in entire agreement with the last two sentences on page 9 of that decision. We would go further; we find it not just manifestly unsatisfactory but monstrously offensive that the Commissioners can write to a trader on 24 May telling him, in effect, that he has been assessed on 18 January - a date of which he has no knowledge whatever - and that he is liable to pay interest with effect from that date - interest which he may have wished to avoid by making a payment on the assessment, However, we cannot use our natural repugnance as an aid to the interpretation of the statute.

> Since the statute does not give any indication of when an assessment is taken to have been made, we must go on the natural meaning of the word; Mr Forsyth made his assessment when he came to his decision, just as this tribunal made its decision when its members agreed on what that decision was to be, even though this then had to be followed by drafting, dictation, typing, checking, re-typing, signing and release. The Form 641 and the notebook provide ample evidence for Mr Forsyth having made his decision."

62. In the present case the assessment was made on the Saturday when the officer completed the 641, the fact that the fax was not received until Monday was irrelevant. The fax was merely evidence of the time when the assessment was made.

63. The Tribunal was also referred to the case of the *University of Huddersfield* in which another tribunal held that the assessment was made when the officer had determined the amount to be assessed, had recorded the amount and his decision to assess on the Form PAT 641 and that form had been dated.

64. Mr M^{c}Kay further submitted that the question of whether there was any maladministration caused by there being a delay between the making and the notification of the assessment was a matter for the administrative court and not for the tribunal.

65. With regard to the Appellant's argument that limitation was a necessary feature of the principle of legal certainty, it was submitted that legal certainty only required Member States not to leave time open-ended. Section 73 and 77 of the VAT Act contained time limits, and it was critical to the issue of time that a reclaim by the Commissioners may not be made after three years.

66. With regard to the matter of sound administration, any suggestion of maladministration was again a matter for the administrative court and not for the tribunal.

The Appellant's case

67. It was the Appellant's case that the Appellant had correctly operated the special partial exemption method and therefore the decision to assess was wrong as a matter of law. It was a subsidiary argument that, if the Appellant had not operated the special partial exemption method correctly, (a) the first purported notice of assessment was in any event time barred and (b) neither notice of assessment was valid.

68. There was no dispute about the legislative background to partial exemption, nor was there dispute that the parties had agreed a special partial exemption method by 30 November 1994. Neither party was submitting that the method used was not, or ought not, to be valid. It was therefore not for the tribunal to consider whether the method secured a fair and reasonable means of attribution. The single question, which was a question of fact, was whether the method was operated correctly by the Appellant.

69. It was an important factor in the case that consolidated accounts had always been used by the Appellant. This was important for two reasons: firstly because it

affected when the various time points came into operation, and secondly there had in fact been a misunderstanding by the Commissioners originally as to when they were first used.

70. It had been the Commissioners' case that the 1994 letter set out all aspects of the agreement. However it was clear from the evidence of Mr Davey about the position of grant income that the letter was not completely clear on its face and one had to look outside the letter.

71. There had been a method in place prior to the disputed agreement letter. Consolidated accounts were in use at that time. Given that it was conceded by the Commissioners that Customs and Excise knew at the time of Mr Davey's visit in 1995 that consolidated accounts were being used, why weren't steps taken to draw it to the attention of the Appellant at this time and to stop it? It was clear from Mr Jones' evidence, in which he had said that knowledge of the use of consolidated accounts was irrelevant, that he was misdirecting himself. It was quite obvious from the way the consolidated accounts were constructed that if certain transactions were ignored, that was relevant to partial exemption. It however did not matter whether consolidated accounts were used or not if the method to be used was agreed. As a matter of fact, at the time of the date of the letter the agreement had been operating on the basis of consolidated accounts. There had been a great deal of discussion and documents had been seen. It was not possible to say that the letter represented the full agreement because there were frequent changes to VAT liability and the agreement was a living animal. Changes did occur. Parties do not always take account of all the terms of an agreement, there are always implied terms. There always existed the possibility that one party had misunderstood some aspect of the agreement. The Appellant believed that an agreement had been reached. If he was wrong about that, then once the Respondents became aware that consolidated accounts had been used they ought to have pointed out to the Appellant that this was not their interpretation of the agreement and to have stopped their use. The agreement had in effect been confirmed by the conduct of the Respondents.

72. If the Appellant were wrong about this, then there was in existence a de facto method. The agreed method in the letter had been varied by the Commissioners' acceptance of the use of consolidated accounts once they became aware of their use.

73. Mr Young posed the question: If there was any uncertainty as to the terms of the agreement, and if the agreement was construed narrowly, then what was the position about grant income? It would have to be excluded, which was not in fact the case. It was not accepted by the Appellant that it was in clause (c) of the agreement. A sensible arrangement was arrived at whereby it was taken into consideration. The fact that grant income was taken into account, even though that was odd, showed that one had to look beyond the letter.

74. With regard to the issue of timing, the assessment having been made under section 73(2) of the VAT Act 1994, it was not clear that the notion of best judgment was imported. In making the assessment the officer failed to take into consideration the knowledge the Commissioners already had that consolidated accounts were being used. A large number of officers had been involved over the years, and collectively these officers had a great deal of knowledge in particular they had knowledge of the FR825 and any one particular officer's ignorance or misunderstanding about a

particular item was irrelevant to the knowledge of the Commissioners. The time points started in 1995 when the Commissioners were first aware of the use of consolidated accounts.

75. With regard to the making of the assessment, it was not accepted that Mr Jones could have been able to carry out all the activities which he claimed to have in the 27 minutes which it appears from the evidence that he took. There was a lack of evidence to demonstrate that the assessment was in fact made on 30 October.

76. With regard to whether the making and notifying of an assessment should be conjunctive, in neither of the two cases relied on by the Respondents had the community law position been considered. Value added tax is a community tax, and a teleological approach to construction is required in order to comply with article 22(8) of the Sixth Directive. This gives a broad discretion to a member country with regard to the collection of tax. Whilst the article is not of direct effect, and there is to be a wide margin of appreciation, because the United Kingdom was creating domestic legislation under article 22 it must conform to the general principles of community law. The principle of legal certainty requires limitation. Domestic statutes should be construed in conformity with community law. When construing section 73, the words "may assess" may either be construed as two separate actions, as the tribunal had construed them in the case of *Subhan, Uddin and Mustak*, or they may be construed conjunctively so that the making of the assessment and the notifying of it coincide in the sense that the notification should be within the time limits which apply to the making of the assessment. It is only by so doing that the principle of legal certainty is satisfied.

77. The Tribunal was referred to the case of *BP Supergas v. Greece* where it is said at paragraph 58:

> "… Subject to the requirement of ensuring the effectiveness of community law, it is for the Member States, in the absence of harmonised rules, to decide upon the appropriate balance between the requirements of legal certainty and sound administration and the need to ensure the correct application of the tax in a particular tax year." (From the opinion of the Advocate General F G Jacobs.)

78. It was submitted that if the Commissioners were right in their construction, it would be possible for an assessment to be withheld for twenty years, and it is not sufficient to say that an Appellant could apply for judicial review in such circumstances. The principle of sound administration required that assessments be notified within the limitation period. The limitation itself was a necessary feature of the principle of legal certainty. In construing section 77 the three-year limitation should be read as requiring notification to the taxpayer within three years. If the Respondents were correct in their interpretation, then by parity of reasoning, they may also be left unaware of "claims made" pursuant to section 80 of the VAT Act, without being limited by the time limits prescribed in section 80(4).

79. Were the Tribunal to decide that the Appellant's submission on the above matter were correct, then the Commissioners would not be disadvantaged for the future because they had already recognised the difficulty caused to the trader and had put out a business brief "Statement of Practice for Tax Assessments" (Business Brief

5101, 13 March 2001). Whilst it was accepted that it was a startling proposition that there can be community law rights where there is no direct effect, this was nonetheless a proper approach. There were at present no authorities directly on the point.

80. Mr Young took the point that the notices, of assessment were technically defective in that the officer had used output tax forms when he was dealing with input tax, not the notice specially designed to deal with input tax. Whilst the statute did not prescribe the form of the notice, the Appellant should be able to rely on the notice to be what it says it is. The officer had not directed his mind to the proper form. The document was invalid and therefore was unenforceable.

Reasons for decision

81. The Tribunal considers that the first question it has to decide is whether there was in existence from November 1994 a method for calculating partial exemption to VAT which was agreed between the parties.

82. If so what were the particulars of that method? Are the terms of the letter of November 1994 to be construed so narrowly as to exclude any variation?

83. We must further decide if the knowledge which, quite late in the day, the Respondents admitted to having in 1995 that the accounts used by the Appellant were in fact consolidated, has a bearing on the above matter?

84. It was not disputed by the Respondents that accounts were attached to the working papers which they saw prior to November 1994. It is, however, disputed by them that it was evident that these were consolidated accounts. It is the case that they were not headed "consolidated accounts", however both Mr Harrison and Ms Blackford were aware that there was a difference between consolidated accounts and ordinary accounts. The Tribunal would expect officers of Customs and Excise dealing with a technical matter such as was in involved in the present case to have been alive to the possibility that consolidated accounts were in fact being used.

85. The Tribunal accepts Mr Broughton's evidence that it was agreed with the Commissioners that the best source of information would be the University's published accounts which were independently verified by outside auditors. The Tribunal also accepts his evidence that because the matter was of such importance to the University, the full co-operation and involvement of Customs & Excise was needed and obtained. The Tribunal notes that on 25 October 1994 an officer named Mr A Thomas of Customs and Excise visited the University and in his visit report he states at paragraph 3 as follows: "Examined accounts y.e. 31.7.93." Mr Thomas was not called to give evidence before the Tribunal and it was only in the course of the hearing that his visit report was produced.

86. It was not disputed by the Respondents that the University's accounts were being used to determine the denominator. It is in effect argued on their behalf that they could not have been aware that consolidated accounts were being used because the use of consolidated accounts would not produce a proper and fair result. It does not seem to the Tribunal that it is appropriate for the Commissioners to argue on this basis. It is not now disputed by the Commissioners that the accounts which were

produced were in fact consolidated accounts. Quite a few officers of Customs and Excise at one time or another saw these accounts. Even in 1995 when the accounts were headed "Consolidated" accounts the Commissioners did not become alive to the point which they now seek to argue that use of consolidated accounts produces an unfair and unnatural result. Whilst the Tribunal does not dispute that by the use of the consolidated accounts the University did achieve an advantage, and that it might, be thought to be unusual to allow them to use the consolidated accounts, nonetheless, given the difficulty to which Mr Broughton alluded about the size of the task confronting both parties, it was reasonable that a readily assessable and verifiable source such as the published accounts should have been used. It would have been a very simple matter for the Commissioners to have clarified the matter with the Appellants. It was Miss Blackford's evidence that in 1993 she had started to look at the Appellant's income and debts and she had at that time examined form 3. Nonetheless she claimed not to know what accounts were used by the Appellant, and that if she had known that they were consolidated accounts she would have queried the matter. This begs the question of whether, since she did not know which accounts were being used, whether she ought to have made sure that she was aware which accounts were being used. The Tribunal considers that in the circumstances it was up to the Commissioners to resolve any ambiguity. There was of course no such ambiguity in the mind of the Appellant.

87. The Tribunal finds that the Commissioners either knew or ought to have known that the Appellant was using consolidated accounts to derive the total income figure to be used in the partial exemption calculation. The Tribunal does not find that in the circumstances it is necessary for it to consider the question raised on behalf of the Respondents as to whether it was possible to construe the fraction contained in the letter of November 1994 in such a way that "total value" has a special meaning. The Tribunal finds that the method agreed between the parties was that in order to calculate the total income the Appellant should use the published accounts of the University which were consolidated accounts. The fact that the Respondents were either unaware of or ignored, this fact is not such as to render the agreement null and void on the basis that the parties were never ad idem. There was an agreement, and it was operated by both parties for several years. Whilst it was not the agreement that the Respondents now wish they had made, does not mean that it was not an agreement which it was not possible for them to make. It is open to the Commissioners to amend the special method for the future.

88. With regard to the matter of construing the specific terms of the agreement, the Tribunal does not accept the narrow construction argued for by the Respondents. It was apparent from the evidence of Mr Davey that grant income was in an anomolous position and was not specifically accounted for in the November letter. The fact that some of the grant income was included in the denominator and some was not shows that the parties were operating the agreement in a flexible manner. The Tribunal does not accept Mr Harrison's evidence as to grant income being included either in item 1(a) of the letter or in sub-paragraph (c). In saying that he considered grant income was a supply, and as a source of income should be included, he omitted to consider whether grant income was in fact a taxable supply, which is the relevant question. The way that the parties treated grant income shows that a degree of flexibility existed in interpreting the terms of the November letter.

89. With regard to the *Investors* case, Mr M^{c}Kay had submitted that as nobody had alluded to consolidated accounts, their use was not part of the relevant background knowledge; the Tribunal finds that the relevant background knowledge is that a university's published accounts are consolidated accounts. It was in the Commissioners' ignorance of this fact that the understanding lay. The Tribunal does not find that this is an excusable ignorance, given that it is a requirement that the Universities' accounts are consolidated, and that FRS 2, which sets out the method to be used in presenting the accounts, is specifically referred to in the notes to the 1994 accounts.

90. If the Tribunal is wrong in holding that there was an agreement between the parties in and prior to November j994, then the Tribunal considers that the fact that in 1995 the Commissioners were aware that consolidated accounts were being used, because the accounts were by then headed "consolidated", is not something that the Commissioners can ignore. The Commissioners did not at that time take up the matter with the Appellant and point out to them what they now say, namely that they had not understood that consolidated accounts were being used and that this was not how they had intended that the special method should be operated. This was not done. That step was not taken by the Commissioners until Mr Jones raised the matter in his letter of 17 August 1998. It was Mr Jones' evidence that the first reference to consolidated accounts appears in the University's 1996/97 accounts. This is not in fact the case. Mr M^{c}Kay relied on Mr Allen's evidence that no one had thought about consolidated accounts as demonstrating that there was no agreement that they should be used. Mr Allen's evidence was in fact that nobody had thought about the effect of consolidated accounts upon the special method which was agreed. It was submitted by Mr M^{c}Kay that there was no meeting of minds on this matter. If this were the case, then the effect would be that there was no agreement at all, but this was clearly not the case; given the fact that a method was operated between the parties over several years.

91. It was also submitted by Mr M^{c}Kay that it was for the taxpayer to draw the Commissioners' attention to the point that consolidated accounts were used, given that VAT is a self-assessed tax, and that the taxpayer had special knowledge of the circumstances. The Tribunal does not accept this argument. There was very close co-operation between the taxpayer and Customs & Excise when the agreement was made. It would have been a simple matter for the Commissioners, all of whose officers claimed to know the difference between ordinary and consolidated accounts, to make the simple enquiry at the beginning as to the type of accounts being used, even if they did not know that a University's published accounts had to be consolidated.

92. Mr M^{c}Kay did not address the Tribunal on the effect that the Commissioners being aware in 1995 that the accounts were consolidated has on the time limits. Whilst the Commissioners were not in a position to make the assessment which they did make without having the further details requested by Mr Jones of the supplies by the University to subsidiary companies for 1995/96, 1996/97 and 1997/98, this begs the question of whether the Commissioners ought to have set in train such enquiries once they had specific knowledge that consolidated accounts were being used.

93. The Tribunal finds that the Commissioners, through Mr Davey, by 12

December 1995 were or ought to have been aware of the fact that the value for the top and the bottom of the fraction were from different sources. In his witness statement Mr Davey states as follows:

> "I concentrated my efforts on ... and the annual adjustment made at the end of the July 1995 quarter. As to this annual adjustment I saw that the nominator of the fraction was made up of taxable income and that this taxable income was extracted from the VAT returns submitted covering the year to 31 July 1995. The value of the denominator came from the annual accounts. I queried the fact that the values for the top and bottom of the fraction were from different sources but was assured that this was what had been agreed between the University and the Bristol VAT office. I do not recall who said this to me but I accepted it as an actual statement. I believe that I neither saw consolidated nor ordinary annual accounts."

94. It is therefore clear from Mr Davey's statement that the Commissioners were fully aware of a possible anomaly and the working of the special method at this time but failed to pursue it. In the Tribunal's opinion the Commissioners ought to have made further enquiries at this time and we therefore find that the time limits for the making of an assessment run from 12 December 1995. With regard to whether or not Mr Davey knew consolidated accounts were being used, Mr M^{c}Kay in the course of the hearing made an admission that the Commissioners were aware by this time that consolidated accounts were being used.

95. Although the fact that the Tribunal has decided in the Appellant's favour with regard to whether or not the agreed special method was that consolidated accounts should be used as the basis for the total income, it is necessary for us also to decide the matter of whether the assessments were out of time on the basis that they were made mop than one year after evidence of the facts sufficient in the opinion of the Commissioners to justify the making of the assessment came to their knowledge. Whilst to make the assessments which were made the Commissioners needed information about the transactions between the University and its subsidiaries, the fact that back in 1995 they knew of the anomaly, but did nothing about it until Mr Jones set his enquiries in train in 1998, does not in the opinion of the Tribunal allow the Commissioners to rely on the Appellant's failure to respond in a timely fashion to Mr Jones' queries of late 1998. We therefore find that the Commissioners failure to take steps in 1995 to clarify the way in which the Appellant was operating the scheme bars them from relying on the Appellant's later delay in replying to their enquiries to bring them within the relevant time limits.

96. The Tribunal considers that it is settled law that the making of the assessment and the notifying of the assessment are not to be construed conjunctively. The Tribunal follows the decision in the case of *Subhan, Uddin and Mustak* where the matter was considered.

97. With regard to Mr Young's submission that Article 22(8) of the Sixth Directive applies indirectly, whilst the Tribunal is very sympathetic to this argument, we were referred to no authority on the point, and indeed Mr Young conceded that there was no such authority, and it is not for this Tribunal to depart from the present situation which, is, in the light of current cases, that time limits are a matter for national courts.

98. The final argument advanced by Mr Young was that both assessments were invalid because the form of the notices used was that for output tax and not for input tax claims. Mr Young submitted that that fact rendered the notices technically defective. However, the Act does not prescribe the form in which the notice should be issued, the Appellants have not been misled by the notices and in the circumstances the Tribunal does not find that the technical defect is such as to render the notices invalid.

99. For the above reasons this appeal is allowed and it is directed that the Appellant should have reasonable costs of and relating to the hearing.