TC04246

Appeal number: TC/2012/04014

VAT – partial exemption – CVCP Agreement between universities and HMRC – whether HMRC approved a new non-CVCP retrospective partial exemption special method ("PESM") from 1973 to 1994 – whether a combined business/non-business method was* ultra vires *– whether a PESM is valid if it is not fair and reasonable - whether non-inclusion of grant income in PESM means it was not fair and reasonable – further 1997 claim for residual VAT on overheads of academic departments – 1997 claim based on PESM but subject to three year cap –* Fleming *claim to recover further residual VAT for period from 1973 to 1994 – whether HMRC able to reopen earlier claims so as to include grant income – evidential issues – earlier years of* Fleming *claim dismissed for lack of evidence – adjournment of later years – directions given

FIRST-TIER TRIBUNAL
TAX CHAMBER

IMPERIAL COLLEGE OF SCIENCE, TECHNOLOGY & MEDICINE — **Appellant**

- and -

THE COMMISSIONERS FOR HER MAJESTY'S REVENUE & CUSTOMS — **Respondents**

TRIBUNAL: JUDGE ANNE REDSTON
MS REBECCA NEWNS

Sitting in public at the Royal Courts of Justice, Strand, London on 17-19 November 2014

Adam Rycroft of KPMG LLP, for the Appellant

Christian Zwart of Counsel, instructed by the General Counsel and Solicitor to HM Revenue and Customs, for the Respondents

DECISION

Introduction

1. The Imperial College of Science, Technology and Medicine ("the College") is a university based in London. On 31 March 2009, the College made a "*Fleming*" claim for repayment of £626,756.77 ("the Claim"), following the decision of *HMRC v Michael Fleming (t/a Bodycraft)* [2008] STC 324 ("*Fleming*"), which held that the three-year cap must be disapplied until an adequate prospective transitional period was in place.

2. The Claim is for the repayment of residual input tax incurred between 1 April 1973 and 31 July 1994 ("the relevant period") as a proportion of overhead costs incurred by the College's academic departments on the supply of commercial research, together with compound interest. On 9 February 2012, HM Revenue & Customs ("HMRC") refused the Claim.

3. The College submitted three previous claims in 1993, 1994 and 1995 ("the earlier claims"). When taken together, these were retrospective to the introduction of VAT in 1973. A fourth claim, made in 1997 ("the 1997 claim"), recovered residual VAT on a proportion of academic costs for the three year period from 1 August 1994 to 31 July 1997.

4. The College's case is that:

(1) the earlier claims were paid consequent upon HMRC allowing or approving a new partial exemption ("PE") special method, or "PESM";

(2) the 1997 claim was paid because HMRC recognised that certain overhead costs relating to the academic departments should have been included in the residual pot used for the PESM, but the 1997 claim was subject to the three year cap and

(3) the Claim simply extends the 1997 claim back to 1973, in reliance on *Fleming.*

5. HMRC say that no new PESM was allowed or approved consequent upon the earlier claims; that if some VAT is due to the College in relation to residual VAT on the academic departments' overhead costs, HMRC are able to reopen the earlier claims and this is likely to result in no sum being due to the College.

6. We decided all these issues in favour of the College. However, for the period from 1973-74 to 1980-81 we found that the Claim fails for want of evidence. For the period from 1981-82 to 1993-94 we adjourned the appeal and gave brief directions, which are set out at the end of this decision.

7. In so far as the Claim concerned compound interest, the parties agreed that it should be stayed behind the Respondents' appeal to the Court of Appeal from Henderson's J decision in *Littlewoods Retail v HMRC* [2014] STC 1761 and we so direct.

The evidence

8. The Claim is retrospective to 1973, now over forty years ago. Much of the dispute between the parties turned on what happened when the earlier claims were made, around twenty years ago. As one would expect, many documents have not survived.

9. Mr Mason and Mr Jamieson gave evidence for the College. Mr Mason is a chartered tax adviser who has been the College's tax manager since 2012; between 2007 and 2012 he was the College's tax compliance manager. He was not, therefore, able to give first hand oral evidence as to what happened when the earlier claims or the 1997 claim were made, although he discussed the Claim with others who have worked at the College for longer and he collated the supporting documentary evidence. He provided a witness statement explaining the Claim, gave evidence in chief, was cross-examined by Mr Zwart and answered questions from the Tribunal. We found him to be an honest witness.

10. Mr Jamieson is the HMRC Officer who agreed the repayments consequent upon the third of the earlier claims and the 1997 claim. Since March 2014 he has been employed by KPMG, who acted for the College in these proceedings. Mr Jamieson provided a witness statement, gave evidence in chief, was cross-examined by Mr Zwart and answered questions from the Tribunal. He gave honest and straightforward evidence, which included accepting that his memory of some of the events two decades previously was "hazy."

11. The documents provided were in four Bundles, and included:

(1) correspondence between the parties and correspondence between the parties and the Tribunal;

(2) the College's annual accounts from 1972-73 to 1993-94;

(3) certain other documents containing financial information for the relevant period;

(4) the Agreement between HMRC and the Committee of Vice-Chancellors and Principals of the United Kingdom ("the CVCP Guidelines"), versions dated 1987 and 1990. The purpose of the Agreement was stated to be to "interpret the law concerning VAT within the university context";

(5) an extract from HMRC's internal guidance dated 3/93; and

(6) the Framework for Higher Education Partial Exemption Special Methods, dated October 2007 and November 2013 ("the 2007 HE Framework" and "the 2013 HE Framework" respectively).

12. Neither party had a copy of the first version of the CVCP Guidelines, issued in 1973, but relied on the text set out in *University of Sussex v C&E Commrs* [1999] VTD 16221 ("*Sussex*") at [8] and [10] - [11]. Similarly, neither party had a copy of the "Grid" which they understood to have accompanied the first three versions of the CVCP Guidelines; they relied on the Grid included at [48] of *Wadham College and*

Merton College v HMRC [2007] VTD 20233 ("*Wadham*"). *Sussex* and *Wadham* are two of several first instance decisions which have considered the CVCP Guidelines.

The law and the CVCP Guidelines

13. During the twenty year period with which the Claim is concerned, the Directives, legislation and regulations have been amended several times. Relevant extracts are set out as Appendix 1 to this decision. The CVCP Guidelines were also amended and reissued four times; relevant extracts are at Appendix 2.

The Facts

14. On the basis of the evidence provided, we make the following findings of fact. Unless otherwise stated, the facts are agreed between the parties. We make further findings of fact later in our decision.

15. One of the issues in dispute is whether the VAT repayments made to the College were based on a new partial exemption *method* or whether HMRC simply agreed repayment *claims* following the submission of *calculations*. In this part of our decision we have tried to use neutral language when referring to the repayments. Whether or not they were consequential upon a retrospective PE method, and if so, whether that method was approved by HMRC, are considered at §§93-114 and at §§115-147 respectively.

16. The earlier claims were triggered by the decision of the VAT Tribunal in *University of Edinburgh v C&E Commrs* [1991] VTD 6569 ("*Edinburgh*"). For ease of reference we have included a summary of that judgment in this part of our decision.

The CVCP Guidelines and tunnelling

17. Universities and colleges make both taxable and exempt supplies, with the latter significantly exceeding the former. The first CVCP Guidelines were agreed shortly before the introduction of VAT in 1973. They provided for signatories to the Guidelines to claim back input tax using a method known as "tunnelling," as the 1973 version of the Guidelines explained at paragraph 11:

> "Customs and Excise have accordingly approved a special arrangement for universities whereby each taxable activity - i.e. those where an output tax liability will arise – can be dealt with separately or 'tunnelled'. Under this arrangement there will have to be separate accounting for each taxable activity, but it will be possible for input tax to be offset against output tax in relation to each such activity."

18. The Guidelines went on to say that "as an extension of this arrangement it has also been agreed that universities will not have to keep any detailed records, on either the output or input sides, in respect of their non-taxable activities."

19. Paragraph 14 of the Guidelines said that "in respect of each distinct taxable activity" schemes similar to those devised for commercial retailers for recovery of input tax…will have to be devised and agreed locally" and paragraph 15 that

"invoices - both received and rendered - relating to particular taxable activities will have to be retained for three years."

20. Paragraph 14 also said that "universities can elect, as appropriate, to forego the right to recover input tax" because the administrative work involved may be disproportionate to the benefits:

> "it should be remembered that input tax can only be recovered in the proportion to which the value of taxable outputs bear to the value of total outputs. In some instances – for example the sale of computer time at full commercial rates – this proportion may be very small."

21. The 1987 version of the Guidelines added at paragraph 42 that:

> "Where apportionment is made on a *pro rata* basis. it is normally necessary to make an annual adjustment of input tax deduction (based on annual figures for the activity). This will correct any seasonal variation in inputs and outputs which, if left unadjusted, could be unfair to the University or to the Exchequer."

22. In addition to these "tunnels" for distinct taxable activities, the Guidelines provided for three specific "formulaic tunnels" dealing with external catering, conferences, and bar sales: all areas where many universities had taxable outputs. In relation to the first two, the 1973 Guidelines said at paragraph 12:

> "…a formula approach has been agreed under which universities will not be required to keep any records of the amounts of tax actually paid in the cost of related inputs. On the basis of evidence collected from a sample of universities, Customs and Excise have agreed that each university shall be entitled to reclaim 20% of the output tax payable in respect of those two taxable supplies: this proportion will be regarded as representing related, deductible input tax."

23. For bars, there was a two-step approach: universities reclaimed the VAT on directly attributable inputs, such as purchase of alcohol and tobacco, and also claimed 5% of outputs.

24. These three formulaic tunnels remained unchanged in all material respects throughout the relevant period, as did the option of having specific "tunnels" for other activities. Until 1990 the guidelines were accompanied by a "Grid" or worksheet for calculating the recoverable input tax, and from this we find that "tunnels" might include launderettes and other shops; books and journals; admission charges and the self-supply of stationery.

The College, tunnelling and Edinburgh

25. When VAT was introduced in 1973, the College was a constituent college of the University of London, itself a signatory to all versions of the CVCP Guidelines. On 8 July 2007 the College separated from the University. On 1 September 2007, HMRC withdrew the Guidelines for all educational establishments.

26. During the years from 1973 to at least 1992, the College operated formulaic tunnels for bars and conferences; it did not operate any non-formulaic tunnels. Whether this was retrospectively amended at the time of the earlier claims is a key issue in dispute.

27. On 27 September 1991, the VAT Tribunal issued their decision in *Edinburgh*. Edinburgh University had used the CVCP Guidelines and recovered input tax directly attributable to its Computer Centre, but it had not sought to recover any residual input tax. HMRC submitted that this had been agreed between the parties at a meeting in 1978. The Tribunal found that there was no such agreement and said:

> "We hold that the mere fact that they did not [claim the residual input tax] was an error which they are now entitled to have put right. The mere fact that they did not claim, on the mistaken view that it was not worthwhile to do so, is in the Tribunal's view neither here nor there. It would be perfectly open to any taxpayer not to reclaim input tax if he did not choose to do so for any reason."

The first two of the earlier claims (1982-83 to 1991-92)

28. Following the decision in *Edinburgh*, on 25 March 1992, Coopers & Lybrand ("C&L") drafted a letter for the College to send to HMRC "to seek approval for Imperial College to recover a proportion of the VAT borne on central administration costs for the current year."

29. On 7 May 1992 a request for the recovery of the VAT on a proportion of those costs was submitted to HMRC, but no copy of that letter was in the Bundle. Mr Zwart said that "this letter is conspicuous by its absence and its absence is telling." However, Mr Martin gave unchallenged oral evidence that the College had "identified all documents relevant to the Claim" and he confirmed that "there is no other relevant document." We accept his evidence and find that there is no surviving copy of this letter, which was written some seventeen years before the Claim was made.

30. A C&L file note dated 15 December 1992 records that "Customs are delaying approval of the partial exemption method as they are not entirely happy about the exclusion of grants and donation from the partial exemption calculation."

31. On 12 January 1993, C&L wrote to Mrs Meadows of HMRC saying:

> "I am writing on behalf of my client, Imperial College, in connection with a request for approval to use a special method for partial exemption…I understand that the proposed method has been broadly agreed in principle and that you are in the process of establishing the view of HM C&E headquarters as regards point number 7 of the partial exemption approval application of 7 May 1992 i.e. exclusion of grants and donations from the calculation. I can confirm that approval from HM C&E has recently been obtained in relation to this point in respect of similar applications made by a number of higher education establishments."

32. On 25 May 1993, Ms Julie Moss of C&L met with Mrs Meadows and with Mr Hermitage of the College to discuss "the proposed reclaim of VAT incurred by Imperial College on overhead expenditure both for the past and for the future."

33. On 9 June 1993 Ms Moss called Mr Hermitage and told him that:

> "our recent meeting with Customs regarding the overhead VAT reclaim had gone very well. Customs approved the method and figures shown to them for FYE July 1992 in principle. The next step is to calculate the reclaim going back six years."

34. On 14 June 1993, C&L wrote to Mrs Meadows, referring to the meeting which had taken place on 25 May 1993 and to the "letter dated 7 May 1992…requesting formal approval of a standard turnover-based partial exemption method to be implemented by the College for the future."

35. On 21 July 1993, Ms Moss wrote to Mr Hermitage saying:

> "following our meeting on 25 May 1993, I am writing to confirm our understanding of the method to be adopted by the college to enable it to identify and capture VAT incurred on overhead expenditure with effect from 1 August 1993.
>
> <u>Overhead VAT accounting – Cost Centre Method</u>
>
> Certain overhead cost centres would be isolated in order that associated VAT on such expenditure can be determined. The main overhead cost centres in question are as follows:
>
> AD Administration
>
> CC Computer Centre
>
> NR General Maintenance
>
> PR General Maintenance."

36. The letter continues by setting out in more detail which sub-categories of cost centres should be included within each of those main cost centres. Under the heading "proposed method" Ms Moss then says:

> "VAT incurred on the appropriate invoices coded to the selected overhead cost centres will be identified, and the VAT element, multiplied by the applicable overhead recovery percentage, will be posted to a separate residual VAT control account…the applicable overhead recovery percentage will be based on the percentage applicable in the previous year. At the end of the year the actual percentage can be determined and an annual adjustment made in respect of VAT under or over claimed via the residual VAT control account.
>
> I would be grateful if you would confirm that your understanding of the 'new' VAT accounting procedures is correct and that we may advise Customs & Excise of these new procedures…"

37. On 5 August 1993, C&L wrote to Ms Meadows, saying:

> "please find enclosed retrospective recovery calculations for the years 1987 to 1992 inclusive. In general terms we followed the procedures as explained to you and Mr Hoad during our visit. You will notice, however, that there is a change in the format following 1989.
>
> Prior to 1989 certain activities were described as self-financing and were shown separately in the accounts. From 1990 onwards, these self-financing activities were included in the general income statement and were also included in the various general expenditure items. For clarity and to ensure that our summaries follow the same format as the accounts, we have shown them separately on the statements.
>
> The total retrospective recovery is £257,522…"

38. On 23 February 1994, C&L wrote to Mr Hermitage, saying:

> "please find enclosed the partial exemption calculations for the years 1983-1986. Customs & Excise (Christine Meadows) have agreed that the outstanding amount of £85,021 (see Appendix A) due to the College can be recovered on the College's current VAT return."

39. We find as a fact, on the basis of this correspondence, that repayments of VAT for the periods 1986-87 to 1991-92 and from 1982-83 to 1985-86 were agreed by HMRC before 23 February 1994. These are the first two of the "earlier claims."

The third of the earlier claims (from 1973-74 to 1981-82)

40. Ms Moss wrote again to Mr Hermitage on 4 January 1995, some ten months after the previous correspondence. The letter is headed "Retrospective partial exemption claim" and opens by saying that its purpose is "to set out various queries that have arisen as a result of calculating the retrospective input VAT recovery for the years 1982 to 1973." There follows a list of detailed questions about the source documents relevant to that claim.

41. On 28 February 1995, Ms Moss wrote to Mr Hermitage saying that "I have now completed the retrospective partial exemption calculations for the 1993-94 VAT claim." She set out a further list of queries, one of which concerns "expenditure analysis of overhead proportions" about which she said:

> "the various items of expenditure need to be reviewed to ensure that the percentages applied in the past, in respect of overhead/departmental review of costs, continue to be valid."

42. On 27 June 1995, Ms Moss met with Mr Hermitage. The file note of the meeting opens by saying "the meeting was held to finalise the retrospective PE claim for the years 1981-74 and to discuss any other issues outstanding." Under the heading "PE claims," the file note said:

> "1. All endowment, donation and subvention income for the years 1981 to 1974 falls outside the scope of VAT; this is consistent with the treatment of the same type of income for later years.

> 2. Both VATable and overhead percentages for all types of expenditure were discussed and agreed for both the 81-74 claim and the 93/94 claim…"

43. The note ends by saying that "Customs are planning to visit Imperial College within the next few weeks. It was agreed that I would finalise the PE claims for 74-81 and 94 to present to Customs at their forthcoming visit."

44. On 10 August 1995, Ms Moss sent Mr Hermitage "schedules of partial exemption calculations for VAT reclaims for the years 1974-1981" together with "a summary of the total VAT reclaim" which was for £89,873.33.

45. In the same letter, she informed Mr Hermitage that supplies of research services provided to the EC Commission and to EU transnational bodies "may be treated as taxable with effect from 1 January 1993" and so can be included in the numerator of the partial exemption fraction. She continued:

> "since a considerable proportion of the College's total research contracts relate to the EC Commission, the college's partial exemption recovery rate will improve dramatically."

46. At some point before 30 January 1995, Mr Jamieson, an officer of HMRC, had taken responsibility for the College. He had joined Customs & Excise in 1989 and was trained in VAT, but then spent two years as a personnel officer for the department. In 1994 he was assigned to a charity specialist unit and given a portfolio which included the College. In his witness statement he explained that "my real experience in VAT only commenced in any real sense in the course of 1994, with my obligations prior to that having been largely administrative."

47. On 13 September 1995, Ms Moss and Mr Hermitage met Mr Jamieson. At the end of her meeting note, Ms Moss records that the effect of including the EC research in the PE calculation for 1993-94 was to increase the overhead recovery rate from 6% to 16% and the quantum of overhead recovery by £100,000.

48. One of the two reasons for that meeting was "to submit the final tranche of the partial exemption retrospective claim." Ms Moss explained the principles of the reclaim to Mr Jamieson, and agreed to provide the statutory accounts on which it was based. Mr Jamieson said he would consider the claim. He also agreed that the College could use "the Accounts method" for the 1993-94 claim, and said he would consider whether it could also be used for the 1994-95 claim.

49. Mr Jamieson told the Tribunal that the phrase "Accounts method" was common terminology in the sector, and was not just a method used by the College; the name derived from the usage of the trader's annual accounts. This evidence was not disputed and we find Mr Jamieson's statements to be facts.

50. On 27 September 1995, Ms Moss sent Mr Jamieson "the final portion of the retrospective overhead VAT recovery claim covering the years 1982 to 1974." The covering letter said that she had used "the same general principles and procedures" as for the other two claims. Appendix 1 to the letter set out the retrospective claim by

year; taken together, the claim was for £297,106.32. Appendix 2 contains some "guidance notes" prepared for Mr Jamieson's benefit. These explain how capital acquisitions, equipment and furniture, library costs, computer centre costs, premises costs and catering costs have been apportioned.

51. On 1 December 1995, Mr Jamieson replied, saying that HMRC's "specialist education team" had "raised a few further points for my consideration before I could repay the money." One of these was headed "exclusion of grant income" and reads:

> "At present the method you have used for the college excludes the whole of the H[E]FCE [Higher Education Funding Council for England] grant. I would be grateful if you could provide an explanation as to why the whole amount is excluded from the calculation as it would appear very unlikely that the student's fees that are included reflect the true value of their education. There must be an element of this grant that covers education, and is therefore a consideration towards exempt activities. A breakdown of the way the grant is applied would be most useful."

52. In his oral evidence, Mr Jamieson said that there was at that time the "general emergence of an issue between colleges and HMRC about whether to take grant income into account"; that he had attended a meeting where an HMRC specialist Officer had explained the issue; that permission could not be given to move to the standard method unless the HEFCE teaching grant ("T-grant") was included in the denominator; and that "the commonly held view [in HMRC] was that it had [previously] not been included by universities." Mr Zwart did not challenge this evidence and we accept these statements as facts.

53. Our finding that universities had historically not treated the HEFCE grant as income in their PE calculations is supported by the CVCP Guidelines: the 1985 version says that the University Grants Commission grant (the earlier version of the HEFCE grant) was "outside the scope" of VAT.

54. In the same letter of 1 December 1995, under the heading "method used by Imperial College" Mr Jamieson said:

> "As you will be aware, the college has used the CVCP guidelines since their inception in 1973 to reclaim a portion of input tax incurred in relation to bars and halls of residence. The fact that these guidelines have been applied makes the college's method a special method for partial exemption purposes. The approval for the use of this method was given to all universities at the inception of the tax. This therefore means that the method you have applied to use, which is now the standard method, requires approval under Regulation 102 of the General Regulations.
>
> Unfortunately I cannot therefore give approval to the standard method, as I believe it does not produce a fair and reasonable apportionment of the non-attributable input tax."

55. On 4 January 1996 he wrote again, under the heading "Retrospective Reclaim 1974-1982, 1994, plus adjustments to Utility Costs and St Mary's supplies." These

two latter adjustments are not relevant to our decision. The first paragraph of his letter says:

> "I am sorry that I have taken so long to finalise the claim but there were a number of issues that it raised with regard to the partial exemption method used by the college. Happily these have all been satisfactorily resolved…points that arose are covered below"

56. The first of those points is under the heading "Partial exemption and Business/non-business method" and reads:

> "The VATA 1994 (and also the VATA 1983) prevents Customs & Excise from approving combined partial exemption and business/non-business methods. Any such methods already in use will be systematically withdrawn in the future. This is on the grounds that there are no legal vires to allow either the Commissioners to approve or businesses to adopt such combined methods. The regulations…make specific reference to 'input tax' which by definition excludes any non-business VAT.
>
> The claim submitted uses such a combined method. However, it is noted that approval has been sought by the college to use this method on several occasions, and although the previous Officer did not reply in writing, the fact that two repayments were made, gives, in effect, approval It is also recognised that the current method employed is slightly disadvantageous to the college comparative to using two separate methods, I therefore propose to accept the special method that has been used for calculations from Y/E 31/7/94 back to Y/E 31/7/74."

57. We find as a fact that by these paragraphs, Mr Jamieson of HMRC agreed to repay the third of the earlier claims, being that which covered the period from 1973-74 to 1981-82 as well as for 1992-93 and 1993-94 . We make further findings on the methodology of the earlier claims at §§82-85.

58. The next paragraph of the 4 January 1996 letter is headed "Adjustments to Reclaim" and states that the claim has been adjusted because:

> "the method used is a special method and there is no provision for rounding up of percentages when using special methods, this is only allowed when using the standard method. The majority of the adjustments relate to this error."

59. Attached to his letter is a page headed "Partial Exemption Reclaim Adjustments." This corrects two specific mistakes caused by using the wrong figure in error and, for ten of the years, changes the percentage used to eliminate the rounding up. For example:

Year	**Residual VAT**			**Totals**	**Difference**
1974	£75,361	Claimed at	8%	6028.9	
		Should be	7.67%	5780.18	£248

60. In the same letter, under the heading "Partial Exemption Special Method," Mr Jamieson says:

> "I will write under separate cover to give formal approval of the method that has been used by the college up to the 1994 reclaim. I have begun discussions with Graham Johnson [of C&L] regarding a future method in the light of the withdrawal of the combined method."

61. No copy of any formal approval letter was in the Bundle. Mr Zwart asked Mr Jamieson whether this part of his letter meant that he was "anticipating formal approval of a method and this is not such an approval." Mr Jamieson answered yes to that question. The Tribunal asked Mr Jamieson what he understood by "formal approval" and he said "send out a proper PESM approval letter." Mr Jamieson said he remembered sending out "one or two" such letters but could not remember whether one was ever sent to the College. Whether a letter setting out "formal approval" was sent out was disputed and we return to this later in the decision.

62. Mr Zwart also asked Mr Jamieson about the procedure for agreeing VAT repayments. Mr Jamieson said that the general approach was to carry out a visit and/or correspond with the trader, discuss the issue with colleagues and formulate the response, which would then be discussed with the surveyor, his immediate superior. However, as the surveyor's background was Customs rather than VAT, he would not have provided any technical challenge to a subordinates' decision to repay. Mr Jamieson had the authority "to agree methods other than the default [i.e., standard] method." However, the size of the repayments made to the College meant that they would have been "approved by someone more senior than [Mr Jamieson]."

The PELS guidance

63. Mr Jamieson worked out of Kensington VAT office along with another 400-500 Officers. There was only one copy of the VAT legislation in the building, which was kept in the assistant collector's office. Sometimes VAT Officers with specialist responsibilities provided specific text to be included in letters, but Mr Jamieson would not himself have referred directly to the words of the legislation; he would have used HMRC's internal guidance.

64. On 24 September 1993, HMRC issued internal guidance relating to partial exemption, labelled "PELS 3/93" ("the PELS guidance"). Mr Jamieson agreed under cross-examination that the PELS guidance was the sort of guidance to which he would have referred. The PELS guidance included the statement that methods other than the standard method and certain others specified in that guidance should not be "rounded up."

65. Under the heading "failure to recover non-attributable input tax" the PELS guidance said (emphasis in original):

> "In item 9 of PELS Newsletter 3/92 ["PELS 3/92] we indicated that the Commissioners were prepared to consider claims for input tax which had not been claimed in earlier tax years…We have recently received legal advice that the Commissioners cannot refuse to consider claims back to 1.4.73…Traders who enquire about retrospective claims should

> be advised accordingly….Changes to partial exemption methods to provide for future recovery of non-attributable input tax should only be approved from the start of the tax year in which the trader's proposals for a change of method were made. **We stress that no retrospective change of method is to be approved**."

66. Under cross-examination Mr Jamieson said that "the first time I saw this that I recall, was when Mr Rycroft showed it to me [before the hearing]." He went on to say that the guidance was issued in 1993, before he began working on VAT in 1994. Mr Zwart asked Mr Jamieson if this was an example of his "hazy memory" and Mr Jamieson agreed. He also accepted that his refusal to allow the College to use roundings for the reclaims was "consistent with" the PELS guidance.

67. Mr Zwart invited the Tribunal to find that Mr Jamieson had seen the PELS guidance before sending the letter of 4 January 1996, on the basis that he had relied on HMRC's guidance generally, had not rounded up the sums due (consistent with the PELS guidance) and that although Mr Jamieson was unable to remember the guidance, his memory was "hazy."

68. However, we find that such an inference goes beyond the facts. From the reference above to "item 9 of PELS Newsletter 3/92" we find that PELS 3/93 was also a newsletter and not permanent guidance. We were provided with no evidence as to how PELS 3/93 would have been stored and whether it was made available to Officers some two years after its publication. We were also not told whether later guidance modified PELS 3/93, just as the latter modified the instructions given in 3/92.

69. There is therefore no evidence that the PELS guidance was in force in January 2006 and there is no evidence that this guidance was seen by Mr Jamieson. We decline to find that it was in any way relevant to the decisions made on 4 January 1996.

1994-95 onwards

70. As set out at §57, on 4 January 1996 Mr Jamieson agreed to repay the third claim even though it used a combined method, but he refused to allow that basis to continue because HMRC understood there to be no *vires* for such a method: instead, traders should first split their residual VAT between business and non-business income, and then apportion the former using their PE method.

71. On 17 January 1997 Mr Jamieson wrote to the College saying "we need to agree a new method for the Y/E 1995-96. We can still use the existing method for y/e 1994-95." On 2 October 1997, he moved this forward a year, saying that "approval for the old method was withdrawn last year, ie for y/e 1996-97 as well as 1997-98." In cross-examination, Mr Jamieson agreed that he was becoming frustrated at the College's failure to respond.

72. On 27 November 1997, Mrs Hughes of HMRC (who had taken over responsibility for the College from Mr Jamieson) wrote to C&L as follows:

> "having perused previous correspondence between Andy Jamieson and Imperial College on the partial exemption method, I note that Andy withdrew approval for the non-business income to be included in the denominator, in his letter dated 4 January 1996. Formal approval of the method that had been used by the College was granted only for the Y/E74-Y/E94 claims, and discussions had begun with Graham Johnson [of C&L] regarding a future method in the light of the withdrawal of the combined method."

73. On 29 December 1997, Mrs Hughes wrote to confirm that she had "processed the repayment for the year end adjustments for 1995 and 1996" and went on to say that:

> "because Andy Jamieson did not withdraw Imperial College's partial exemption method until January 1996, the method of apportionment in use at that time has been accepted for the annual adjustments up to, and including, July 1996…As ruled in Andy Jamieson's letter of January 1996, the single pot method cannot be accepted from that date."

74. On 19 March 1998, HMRC agreed to "accept the repayment for the year 1996-97 based on the same partial exemption method as accepted for the previous periods" and recorded the College's agreement that from from 1997-98 a new method" would be introduced, which did not include "the business/non-business calculation within the partial exemption method."

75. Despite this correspondence, the College continued to use the same basis and no new method was agreed. The parties continued to correspond on the combined method, and on whether the T-grant should be included in the denominator of the fraction.

76. On 1 July 1998, C&L combined with Price Waterhouse to form PwC. A letter of 27 July 1998 from PwC to the College refers to HMRC having responded to "the BUFDG Submission in relation to the VAT treatment of grant income." We understand BUFDG to be an acronym for the British Universities Finance Directors Group. PwC say that HMRC "believe that the inclusion of the grant income in the denominator of partial exemption calculations can only produce the right, or fair and reasonable, result in terms of residual VAT recovery…"

77. On 21 July 1999, a letter from PwC to HMRC, under the heading "effective date of the method" says:

> "we understand that the effective date for the change in method for the College is 1 August 1997. We would be grateful if you would confirm that this is the effective date to be applied to universities generally as the College is aware that their colleagues in the sector have been granted an extension of time, such that they are implementing new methods commencing August 1999…this would leave Imperial College severely disadvantaged in comparison to other institutions…"

78. On 5 June 2000, HMRC wrote to PwC saying that:

> "your proposal to include the teaching element of the HEFCE grant in the denominator is accepted. It is accepted that if policy concerning grants differs materially from the agreement reached, the position is open to review…"

79. Mr Rycroft's skeleton argument stated that the College changed its methodology to include the T-grant with effect from 1 August 1999. This was not disputed and we accept it as a fact.

80. By letter dated 15 September 2005, Mr Hendry of HMRC wrote to the College saying:

> "As you are aware, the Commissioners have been seeking agreement with the University on a new PESM since we wrote to the university on this topic on 1 December 1995. There has been continuing discussion and correspondence, with both the university and its advisers, since that date without a resolution."

81. It was not until October 2007, when the 2007 HE Framework was introduced, that the College obtained approval to use a PESM based on that Framework. We find as a fact that, until then the College continued to use a combined method.

The methodology of the earlier claims

82. No copies of the earlier claims have survived. However, a letter from the College to C&L dated 6 May 1997 sets out "the draft partial exemption computations for 1994-95 and 1995-96." We know from Mr Jamieson's letters that the approach in those years was the same as that used in the earlier years' claims.

83. The 1994-95 and 1995-96 computations used this formula:

$$\frac{\text{taxable income}}{\text{total income (business and non-business)}} \times \text{residual VAT}$$

84. The detail of the computations show that taxable income was calculated by taking the College's output VAT, grossing it up and adjusting for zero-rated outputs. The total income was taken from the statutory accounts. We know from C&L's letter of 21 July 1993 that certain identified cost centres provided the residual VAT, and that there was no splitting out of non-business VAT from these cost centres before the computation was submitted (because it was a "combined method"). A later letter from C&L dated 23 November 1999 refers to the College making recoveries of residual VAT using a "global method" under the same formula.

85. We find as a fact that the earlier claims calculated recoverable VAT using the formula and methodology described in the previous two paragraphs.

The 1997 claim

86. On 2 July 1997, C&L wrote to Mr Jamieson saying:

> "Imperial College generates significant research of all types. Changes to the VAT legislation on 1 January 1993 and 1 August 1994

> impacting on research has meant that the College has generated significant taxable income in recent years.
>
> In the year 1995/96, its taxable research income including EU and non-EU contractual services total approximately £20m. To date, it has recovered input VAT directly relating to such research where possible and a percentage of central administration costs. However, it has not recovered any overhead VAT incurred by the academic departments.
>
> Therefore, we propose to carry out an exercise for the year 95/96 to identify this overhead VAT. As this overhead VAT will not relate solely to supplies of taxable research but also to exempt teaching and research activities, we propose to treat this VAT as residual. Such VAT will therefore be apportioned using the residual recovery rate for the appropriate year. The years we wish to consider for the exercise are 94/95, 95/96 and 96/97 which fall within the three years allowed for the retrospective recovery of unclaimed tax."

87. On 2 October 1997, Mr Jamieson replied, saying:

> "I write to confirm that Customs & Excise will accept a claim for overhead VAT incurred in academic departments which has not previously been recovered. It is recognised that there is an element recoverable due to the fact that these departments make both taxable (research supplies) and exempt supplies. The claim will of course be subject to any necessary restrictions under the 3 year capping rules."

88. At some subsequent date, the 1997 claim was paid.

Summary of the payments and repayments

89. In summary, payments or repayments were agreed from 1973-1974 through to 1996-1997 as follows:

(1) 1973-74 to 1981-82: the third claim - agreed by Mr Jamieson, see §57.

(2) 1982-83 to 1985-86: the second claim - agreed by Mrs Meadows, see §38 and confirmed by Mr Jamieson, see §57.

(3) 1986-87 to 1991-92: the first claim – as (2) above.

(4) 1992-93 and 1993-94: agreed by Mr Jamieson, see §57.

(5) 1994-95: agreed by Mr Jamieson, see §71; plus the 1997 claim so far as it related to 1994-95, see §87.

(6) 1995-96: eventually agreed, see §73; plus the 1997 claim so far as it related to 1995-96, see §87.

(7) 1996-97: agreed §74; plus the 1997 claim so far as it related to 1996-97, see §87.

The Claim

90. On 31 March 2009, KPMG submitted the Claim on behalf of the College. It was made on the basis that the 1997 claim had been capped, preventing the recovery of residual VAT relating to the College's academic departments for the period from

1973-74 to 1993-94. In other words, the Claim was for the periods listed at (1) to (4) set out in the previous paragraph.

The issues in outline

91. The issues between the parties can be summarised as follows:

(1) The College submits that HMRC agreed a new PESM, replacing the CVCP method, both *de facto*, by paying the first two of the earlier claims, and explicitly by Mr Jamieson's letter of 4 January 1996. HMRC say that the College continued to operate within the CVCP Guidelines.

(2) HMRC say that if they are wrong in this, the new PESM was not approved by HMRC; the College disagrees.

(3) The College submits that the 1997 claim simply added other academic cost centres into the residual pot used for the global PESM calculation, that Mr Jamieson had accepted that these costs were rightly included in that pot, but that the claim was subject to the three year cap. HMRC say that as there was no PESM, any *Fleming* claim can only be made on the basis that there was a "gap" in the CVCP Guidelines as applied by the College. Because of the discretion inherent in those Guidelines, if the Claim is pursued, HMRC can also recalculate the College's earlier claims in the light of its current views and knowledge: in particular, the T-grant would now be included in the denominator of the fraction. As a result, it is likely that the College has been overpaid, not underpaid.

(4) Finally, if the College succeeds on the first two issues, HMRC submit that the evidence provided to support the Claim is inadequate and the Claim should be refused.

92. We have structured our analysis by asking the following questions:

(1) Was there a retrospective non-CVCP PE method for the period 1973-74 to 1993-94, and if so, was it a special method or the standard method?

(2) If there was a new non-CVCP PESM, was it approved by HMRC?

(3) If approval was given, was that approval *ultra vires* because it used a combined method and/or because the T-grant was not included?

(4) If the answer to question 1 is "no", did the retrospective change to the College's operation of the CVCP Guidelines mean that there was a CVCP-based PESM?

(5) If the 1997 claim was paid under a PESM, is HMRC bound by its terms to repay the Claim, subject to the evidential burden being satisfied?

(6) If so, is the evidential burden satisfied?

Question 1: new retrospective non-CVCP PE method for 1973-74 to 1993-94?

Mr Rycroft's submissions on behalf of the College

93. Mr Rycroft said that the correspondence between the College and HMRC repeatedly referred to a "retrospective partial exemption claim," see for example the

letters of 23 February 1994, 4 January 1995 and 10 August 1995, as well as the meeting notes of 13 September 1995.

94. He submitted that "the only reasonable meaning" of the term "partial exemption" in that correspondence is "to a method applying under Regulation 101 or 102 of the VAT Regulations 1995." Those regulations provide for standard and special PE methods, see Appendix 1 to this decision.

Mr Zwart's submissions on behalf of HMRC

95. Mr Zwart said that no new PE method had been agreed and the retrospective claims had been dealt with as adjustments under the CVCP Guidelines The 1987 version of those Guidelines says, at para 42, that:

> "Where apportionment is made on a *pro rata* basis, it is normally necessary to make an annual adjustment of input tax deduction (based on annual figures for the activity). This will correct any seasonal variation in inputs and outputs which, if left unadjusted, could be unfair to the University or to the Exchequer."

96. The calculations submitted by the College to HMRC simply established "the fraction used to work out the amount reclaimable for the tunnels." It was not a new PE method but "an application of the Guidelines."

97. He said that the references in the correspondence to "the calculations" supported his case. For example, in the key letter of 4 January 1996, Mr Jamieson said "I therefore propose to accept the special method that has been used *for the calculations.*" Moreover, the attachment to that letter is headed "Partial Exemption Reclaim *Adjustments.*"

98. In Mr Zwart's submission, Mr Jamieson had agreed "a claim" but not a new PESM, and "subsequent correspondence from the Respondents is entirely consistent with the absence of approval on 4 January 1996." He referred in particular to the letter of 15 September 2005 from Mr Hendry of HMRC, which said "the Commissioners have been seeking agreement with the University on a new PESM since we wrote to the university on this topic on 1 December 1995" and that therefore no new PESM was agreed on 4 January 1996.

Whether a retrospective PESM was operated

99. We agree with Mr Rycroft that the correspondence consistently refers to the claims being based on a "method" other than that which had been in place previously. On 12 January 1993, C&L asked HMRC for "approval to *use a special method* for partial exemption" and on 9 June 1993 the C&L file note says "Customs approved the *method* and figures shown to them for FYE July 1992 in principle." On 21 July 1993 C&L refer to "the *method* to be adopted by the college." On 1 December 1995, Mr Jamieson, referring to the first two claims, says "at present *the method* you have used for the college…" In his letter of 4 January 1996, under the heading "Partial exemption and Business/non-business *method*," Mr Jamieson says "the claim submitted uses such a combined *method*" and goes on to say that "*the method used is*

a special method and there is no provision for rounding up of percentages when using *special methods*."

100. In contrast, there is no mention anywhere in the correspondence to "filling in a gap in the CVCP Guidelines," or to creating a new tunnel or to any paragraph of the CVCP Guidelines. There is no reference to those Guidelines at all, other than in Mr Jamieson's letter of 1 December 1995, which predates the key letter of 4 January 1996.

101. While it is true that the CVCP method allows for "adjustments," we disagree with Mr Zwart that the attachment to Mr Jamieson's letter, headed "Partial Exemption Reclaim *Adjustments*" refers to the Guidelines. It is clear from the text of Mr Jamieson's letter, and from the attachment itself, that the adjustments referred to are (a) two specific errors and (b) the reversal of rounding in the calculation because the method is a special method not a standard method, see §59.

102. Moreover, as para 42 of the Guidelines makes clear, the purpose of the annual adjustments in the CVCP method is to "correct *any seasonal variation* in inputs and outputs." The earlier claims are not correcting seasonal variations but recovering hitherto unclaimed residual input tax.

103. If, as Mr Zwart submits, the earlier claims were simply annual adjustments within the CVCP Guidelines, then they would have to fit the framework provided by those Guidelines. That is not the case because:

(1) the repayments are not limited to residual input tax relating to bars and conferences, the only two of the formulaic tunnels used by the College. This can be seen from the fact that:

(a) the residual input tax repaid under the first two of the earlier claims arose on general administration, computer centre and general maintenance costs;

(b) the third claim repaid residual tax incurred on capital acquisitions, equipment and furniture, library, the computer centre, premises and catering costs; and

(c) the 1997 claim was for residual input tax on overheads of the academic departments in relation to commercial research.

(2) apart from the formulaic tunnels, other tunnels require "separate accounting for each taxable activity" (see para 11 of the 1973 Guidelines and para 42 of the 1987 Guidelines). In contrast, the repayments made to the College were not based on "separate accounting " but on a "global method" calculated using taxable income/total income; and

(3) that method is referred to as "the Accounts method," not the CVCP method. We have found as facts that the Accounts method was not just a method used by the College, and that name derived from the usage of the trader's annual accounts, see §49.

104. We do not accept the inference Mr Zwart draws from the 15 September 2005 letter from Mr Hendry, namely that the reference to "1 December 1995" in the sentence "the Commissioners have been seeking agreement with the University on a new PESM since we wrote to the university on this topic on 1 December 1995" means that no new PESM was retrospectively agreed after that date.

105. That is for two reasons. First, that letter was ten years after the events in question, and was written by Mr Hendry, who had no first hand knowledge of the events in question. Second, while it is true that the issue of a new PESM was raised in the letter of December 1995, that letter was not the final position. On 4 January 1996 Mr Jamieson saying (emphasis added) "there were a number of issues that it raised with regard to the partial exemption method used by the college. *Happily these have all been satisfactorily resolved*."

106. More generally, we also do not agree with Mr Zwart that subsequent correspondence is "entirely consistent" with no new method having been agreed. On 27 November 1997, Mrs Hughes, having read the correspondence, says "*formal approval of the method that had been used* by the College was granted only for the Y/E74-Y/E94 claims" and "as ruled in Andy Jamieson's letter of January 1996, *the single pot method* cannot be accepted from that date." On 29 December 1997 Mrs Hughes said "Andy Jamieson did not withdraw Imperial College's *partial exemption method* until January 1996…" On 19 March 2008, HMRC agreed to "accept the repayment for the year 1996-97 *based on the same partial exemption method* as accepted for the previous periods."

107. Furthermore, we have already found as a fact that until October 2007 the College continued to use the method used for the earlier claims and the 1997 claim, see §75 and §81. The CVCP method was withdrawn by HMRC in September 1997. Mr Jamieson wrote to the College in October 1997, reiterating that "approval for the old method was withdrawn *last year*, ie for y/e 1996-97 as well as 1997-98." If, as Mr Zwart submitted, the earlier claims were made under the CVCP Guidelines rather than being consequential on a new PESM, then it is surprising that Mr Jamieson made no reference to the withdrawal of the Guidelines in the previous month, given that, as he said, he was becoming frustrated at the College's failure to respond. Moreover, HMRC's later letters are consistent with this: they do not mention the withdrawal of the CVCP Guidelines but talk about the withdrawal of "the single pot method" and of "the combined method,"

108. Finally, we also do not accept that the references in the correspondence to "the calculations" bear the weight Mr Zwart seeks to place on them. In particular, he stressed the word "calculations" in Mr Jamieson's statement that "I therefore propose to accept the special method that has been used for the calculations." The natural emphasis is on the first part of this sentence, not the second.

109. It is clear from all of the above that the method used for the claims was wholly different to the CVCP method.

Whether it was a standard method

110. Neither party sought to argue that the College was operating the "standard" partial exemption method, i.e., as provided for by Reg 101(2)(d) of the VAT Regulations 1995 and Reg 30(2)(d) of the VAT (General) Regulations 1992, both of which provide as follows:

> "there shall be attributed to taxable supplies such proportion of the input tax on such of those goods or services as are used or to be used by him in making both taxable and exempt supplies as bears the same ratio to the total of such input tax as the value of taxable supplies made by him bears to the value of all supplies made by him in the period."

111. We agree: the denominator of the fraction was derived from the accounts, and so was an approximation for "the value of all supplies made by him in the period." Furthermore, because the College used a combined method, the residual pot did not consist only of "input tax" but of all VAT charged to the particular cost centres which were included in the PE calculation.

112. Although Mr Jamieson originally appeared to consider the proposed retrospective PE method to be a standard method, see §54, on 4 January 1996 he explicitly stated that "the method used is a special method and there is no provision for rounding up of percentages when using special methods, this is only allowed when using the standard method."

113. This is of course correct: Reg 102(4) of the 1995 Regs stated[1] that "the ratio calculated for the purpose of paragraph (2)(d) above shall be expressed as a percentage and, if that percentage is not a whole number, it shall be rounded up to the next whole number." There is no such automatic rounding for special methods. Mr Jamieson therefore changed his mind on this, as well as on the other matters already considered, between December 1995 and January 1996.

Answer to Question 1

114. We find that a non-CVCP PESM was retrospectively implemented for the period from 1973-74 to 1993-94.

Question 2: was the PESM approved by HMRC?

Mr Rycroft's submissions

115. Mr Rycroft said that the earlier claims were paid by HMRC, and:

> "as HMRC have obligations for care and management of VAT and should only pay sums against a claim which they consider to be properly due in law. The sums claimed are only due under the terms of UK Law if there was a valid PESM in place providing entitlement to recover by reference to the Accounts Method. HMRC must therefore, as a prior act to repaying the three claims, have approved the PESM for the particular period."

[1] The regulation was subsequently amended by SI 2005/762, but that has no relevance to this decision.

116. He also said that Mr Jamieson's letter of 4 January 1996 confirms that payment of the first two claims gave *de facto* approval: Mr Jamieson said "although the previous Officer did not reply in writing, the fact that two repayments were made, gives, in effect, approval." That letter not only endorsed that earlier approval but confirmed it in writing, before going on "to accept the special method that has been used for calculations from Y/E 31/7/94 back to Y/E 31/7/74."

117. Mr Rycroft relied on *S&U Stores v C&E Commrs* [1985] STC 506 ("*S&U Stores*") at page 511, where Farquharson J considered the correspondence between the parties in that case and said:

> "One comes back again to the letter in light of these regulations. The way in which I pose the question is: whether anybody, having received that letter, could have supposed that the commissioners were allowing the Stanlor percentage method [the PESM at issue in that case] to continue; or were the terms in which the letter was written so clear that whatever alternative arrangement may have emerged, none the less that one was put an end to…When, therefore, on 2 May 1980, the commissioners write to say that that method of apportioning the value added tax 'is not acceptable to the department', I cannot find in my own judgment that anybody could possibly have concluded that this was other than a direction that it had to stop."

118. Mr Rycroft said that the correspondence between Mr Jamieson and the College should similarly "be construed by reference to the person receiving it and as to what they ought reasonably to have concluded from it." We observe that he appears to be inviting the Tribunal to apply a combined subjective and objective approach.

119. Mr Rycroft also relied on *Wellington Private Hospital Ltd v C&E Commrs* (LON/92/2203) ("*Wellington Hospital*") and on *BMW Finance GB Limited v C&E Commrs* [1995] (VTD 13131) ("*BMW*"). In the latter case the tribunal decided that the pre-existing PESM was "tacitly approved," because HMRC had "accepted without objection the returns made on the basis of the new method." Mr Rycroft submitted that a stronger inference could be drawn in the College's case, because it had made a claim and not simply submitted returns. A claim, he said, is subject to specific review, whereas a return is "only subject to whatever assurance procedures HMRC should decide to apply."

Mr Zwart's submissions

120. Mr Zwart said that if, contrary to his main submission, there was a new non-CVCP PESM, it had not been approved by HMRC. He referred to Mr Jamieson's letter of 1 December 1995, which said that a new combined method was "impermissible under VATA 1983 and 1994, and the VAT General Regulations 1985, Regulations 30 to 37E inclusive because 'input tax' by definition excludes any non-business VAT." He submitted that this showed that a new PESM including a combined method had not been approved, because Mr Jamieson knew it was in breach of the VAT regulations.

121. Furthermore, the same letter showed that Mr Jamieson also knew HMRC's specialist team was concerned about the exclusion of T-grant: he told C&L that there "must be an element of this grant that covers education, and is therefore a consideration towards exempt activities." Yet the T-grant was excluded from the denominator of the PESM.

122. Mr Zwart invited the Tribunal to find that no "formal approval" had been given, after Mr Jamieson's 4 January 1996 letter, because "that document would no doubt have been provided by [the College] in this claim and [Mr Jamieson] also required approval from [his] surveyor line manager."

123. He also sought to rely on Mr Jamieson's reference in the same letter to discussions about a "future method," saying that this showed that there had been no agreement, because otherwise why would he still be requiring agreement to a new method?

Approve or allow?

124. Before considering those submissions, we first set out the relevant legal provisions. During the twenty year period covered by the Claim, four sets of VAT regulations were promulgated. The first two stated that HMRC may "allow or direct" the use of a PE method other than that specifically provided for in the legislation, see Reg 24(2) of the VAT (General) Regulations 1972 and Reg 30(5) of the VAT (General) (Amendment) (No. 2) Regulations 1987.

125. In 1992 the wording changed: Reg 31(1) of the VAT (General) (Amendment) Regulations 1992 provided that (emphasis added) "the Commissioners may *approve* or direct the use by a taxable person of a method other than that specified in regulation 30 above [i.e., the standard PE method]." Reg 102(1) of the VAT Regulations 1995 uses the same wording.

126. Although we had submissions on both "allow" and "approve," it is clear from the correspondence that the PESM was not agreed before 1993, see the C&L file note dated 9 June 1993. The regulations in force therefore required that the new PESM be "approved" rather than "allowed" by HMRC.

127. Mr Zwart submitted that "approve" was a higher threshold than "allow," relying on the definitions in the Shorter Oxford English Dictionary. We agree. "Allow" is there defined to mean "accept as true or valid, acknowledge, admit, grant, concede." In contrast, "approve" means "to confirm authoritatively, to sanction" or to "pronounce or consider to be good or satisfactory."

128. Both *BMW* and *Wellington Hospital* considered whether a PESM had been "allowed" and we found that neither provided reliable guidance as to whether a PESM had been "approved." Although not cited to us, this tribunal in *DFS Furniture v HMRC* [2009] UKFTT 204 (TC) ("*DFS*") (Judge Hellier and Mr Robinson) came to a similar conclusion, saying at [189]:

> "'Approve' to our minds has different connotations from 'allow'. 'Approve' suggests some demonstration of consent, whereas 'allow' encompasses simply letting something happen."

129. That tribunal went on to say that the test as to whether or not a PESM has been approved is objective:

> "[195]…the regulations cannot have been intended to require an investigation into the actual knowledge and state of mind of HMRC before a taxpayer could be confident that approval had been given. So construed the regulations would be unworkable and impractical: no one would be able to rely even on a plain letter from HMRC saying 'we approve' without extensive further investigation. In our view the test must be an objective one: the question must be whether HMRC have acted so as to convey their approbation of the method. But these issues are, in the sense we indicate below, indirectly relevant to that objective determination.
>
> [196] In our judgment approval is given by HMRC to a method used or to be used by the taxpayer for calculating recoverable input tax if HMRC conduct themselves in such a way that their conduct would convey to a reasonable man in the circumstances of the taxpayer (a) that HMRC knew what method was being used or proposed, (b) that they had considered it, (c) that they had agreed to it, and (d) that their conduct constituted the communication of those elements.
>
> [197] As a result what HMRC actually knew, and what the taxpayer actually understood are irrelevant."

130. We respectfully agree. We also considered the decision in *S&U Stores,* which dealt with an earlier version of the regulations, although in the context of this objective/subjective question nothing turns on that. Our reading of *S&U Stores* is that Farquharson J also decided that the test was objective – see the references to "anybody" in the text:

> "The way in which I pose the question is: whether anybody, having received that letter, could have supposed that the commissioners were allowing the Stanlor percentage method to continue; or were the terms in which the letter was written so clear…I cannot find in my own judgment that anybody could possibly have concluded that this was other than a direction that it had to stop."

131. Both Farquharson J in *S&U Stores* and the tribunal in *DFS* therefore found that the test was objective, and we concur. We do not accept the dual approach which we understood Mr Rycroft to be proposing.

132. We also agree with the tribunal in *DFS* that to have "approved" the new PESM, HMRC must have demonstrated its acceptance. We consider at §140 below, whether or not that occurred in this case.

133. The tribunal in *DFS* concluded this part of their judgment by saying:

> [198] …If what HMRC apparently approved is so odd, so contrary to the spirit of attribution based on use that 'there must have been some mistake', then it could not be said approval had been given because it would be clear that the objectively obvious mistake meant they had not truly approved."

134. We considered whether the College's approved PESM was "so odd…that 'there must have been some mistake.'" It seemed to us that there were two potentially relevant issues. First, Mr Jamieson approved the PESM despite stating that the combined method was *ultra vires* HMRC's powers. If this was the position, the approval would have been invalid. Although we do not think this is the sort of "objectively obvious mistake" the tribunal in DFS were considering, the effect would nevertheless be the same – the PESM would not have been "truly approved." We therefore consider at §148 whether agreement to the combined method was *ultra vires* UK law, and at §157 whether it was *ultra vires* EU law.

135. Second, the PESM did not include the T-grant in the denominator and Mr Zwart submits that the failure to include that grant means that the method was not "fair and reasonable." At §166 we discuss whether a PESM which is not "fair and reasonable" is void, before considering at §172 whether the non-inclusion of the T-grant in the denominator was not "fair and reasonable."

136. We did not identify any other possibly "objectively obvious mistakes" in the approval given for the College's PESM and none was put to us.

Method of giving permission

137. Before discussing these issues, another regulation requires consideration. Although neither party referred it in their submissions, and we only identified it after the hearing, Reg 67 of the VAT (General) Regulations 1985 and Reg 4 of the VAT (General) Regulations 1995 say:

> "Requirement, direction, demand or permission
>
> Any requirement, direction, demand or permission by the Commissioners, under or for the purposes of these Regulations, may be made or given by a notice in writing, or otherwise."

138. That regulation remains in force, although Reg 4 of the VAT (Amendment) Regulations (SI 2005/762) amended Reg 102 (that relating to the approval of special methods) with effect from 1 April 2005 as follows:

> "Any approval given or direction made under this regulation shall only have effect if it is in writing in the form of a document which identifies itself as being such an approval or direction."

139. We therefore find that, at all relevant times, there was no requirement for approval of a PESM to be given in writing, and in particular, no requirement that it be "in the form of a document which identifies itself as being such an approval or direction."

Was approval given?

140. Applying the objective approach discussed above, we find that the reasonable person, receiving Mr Jamieson's letter of 4 January 1996, which said "I therefore propose to accept the special method that has been used for calculations from Y/E 31/7/94 back to Y/E 31/7/74" would have been in no doubt that the PESM had been approved for the period from 1973-74 to 1993-94. He would also have understood that Mr Jamieson expressly confirmed the *de facto* approval given by his predecessor when he said that "although the previous Officer did not reply in writing, the fact that two repayments were made, gives, in effect, approval."

141. We also do not accept the inference Mr Zwart invited us to draw, that formal approval was not given because no copy of a formal approval letter has been provided with the Bundle. As we have already said, the events in question were around two decades ago and it is unsurprising that the documentary chain was incomplete. Instead, we rely on a letter sent to the College by Mr Jamieson's successor, Mrs Hughes, on 27 November 1997, i.e., within two years of Mr Jamieson's 4 January 1996 letter. She said (emphasis added):

> "having perused previous correspondence between Andy Jamieson and Imperial College…Formal approval of the method that had been used by the College was granted only for the Y/E74-Y/E94 claims…"

142. We find as a fact, in reliance on this evidence, that formal approval was given by Mr Jamieson some time after the 4 January 1996 letter. This is also consistent with his oral evidence that he did send out one or two such formal approvals.

143. In any event, even if no such formal approval letter had been sent out, the College would have succeeded in this part of its argument. Mr Jamieson's letter provided written approval for the new PESM at a time when the VAT regulations did not even require approval be given in writing, let alone oblige HMRC to provide a formal "document which identifies itself as being such an approval," such as is now the position.

144. Mr Zwart seeks to rely on the letter of 1 December 1995, which concluded by saying that the CVCP method subsisted and that approval was refused for the proposed new method (which Mr Jamieson then thought was the standard method). As we have already found at §113 and §140, that letter was not the final position. It is clear from the letter of 4 January 1996 that the earlier difficulties, being the combined method and the T-grant, were no longer in issue in relation to the claim, which, as we have already found, depended on the retrospective PESM.

145. However, the combined method remained in issue going forwards. From the letter of 4 January 1996, together with subsequent correspondence from HMRC (letters of 17 January 1997, 2 October 1997, 27 November 1997 and 29 December 1997) we find as a further fact that Mr Jamieson's letter of 4 January 1996 gave approval only for the period 1973-74 to 1993-94.

146. Mr Jamieson later approved the same PESM for 1994-95, see the letter of 17 January 1997; approval was given for 1995-96 by HMRC's letter of 19 March 1998, although these and subsequent years are not in issue in this appeal.

147. Our answer to Question 2 is therefore that approval was given by HMRC for a new non-CVCP PESM for the period 1973-74 to 1993-94.

Question 3: was that approval* ultra vires*?

The combined method under UK law

148. Mr Jamieson had told C&L on 4 January 1996 that "there are no legal vires to allow either the Commissioners to approve or businesses to adopt such combined methods."

149. Mr Rycroft submitted that the combined method gave the same answer as the two-step procedure provided for by the regulations, and was therefore not *ultra vires.* He cited a letter from PwC to HMRC dated 23 November 1999 which set out comparative calculations which come to identical answers. However, we were not convinced. It seems to us that whether the combined method gives the same result as a two-step procedure must depend on the particular facts. Even in the College's case, Mr Jamieson's letter of 4 January 1996 said:

> "It is also recognised that the current method employed is slightly disadvantageous to the college comparative to using two separate methods."

150. We infer from the phrase "it is…recognised" that Mr Jamieson is responding to a submission made by C&L, and therefore that at the time the PESM was approved, neither C&L nor Mr Jamieson thought that the combined method gave the same result as that provided for by the regulations.

151. We have already seen, at §126, that HMRC had the power to "approve or direct the use by a taxable person of a method other than [the standard method]," see Reg 102 of the VAT Regulations 1995. The same power existed at the time of the *de facto* approvals given by Mr Jamieson's predecessors, see Reg 30 of 1985 VAT General Regulations 1985, as amended by the 1987 regulations. HMRC also had a general discretion for the "care and management" of VAT, see VATA 1994, Sch 11 para 1 and VATA 1983, Sch 7 para 1.

152. In *The Labour Party v C&E Commrs* VTD 17034 ("*The Labour Party*") the tribunal (under the chairmanship of Dr AN Brice) considered whether HMRC had the *vires* to make a single composite agreement, see [54] of that decision. The tribunal said at [57]:

> "On the words of the legislation alone we would conclude that Customs and Excise had power to allow or direct the use of a special method in any way that they saw fit. There is nothing in the legislation to prevent Customs and Excise from combining the allowing or directing of a special method with the exercise of any other power, including the agreement of a method of apportioning input tax between business and non-business supplies."

153. Although the regulation in force at the time referred to "allow" rather than "approve," in the context of this issue nothing turns on that. The tribunal in *The Labour Party* then considered *GUS v C&E Commrs (No 2)* [1995] STC 279 and *R v C&E Commrs, ex parte Kay* [1996] STC 1500. At [59] they continued, in reliance on those authorities:

> "there is nothing to prevent one agreement being both an agreement for a special method and also an agreement under the general powers of care and management to deal with the apportionment between business and non-business supplies."

154. We respectfully concur, and find that the approval of a combined method was not *ultra vires* UK law, taking into account both the VAT regulations and HMRC's general care and management powers. It also follows that it was not objectively unreasonable.

155. Since we agree with the tribunal in *DFS* that the test is objective, Mr Jamieson's own opinion about the legality of the PESM is not in point, see *DFS* at [197]*:* "what HMRC actually knew, and what the taxpayer actually understood are irrelevant."

156. As we have seen, Mr Jamieson's letter and *The Labour Party* judgment are only concerned with the UK regulations. We have also considered whether the use of a combined method is *ultra vires* the Directive.

The combined method and EU law

157. Article 11(2) of the Second Directive provides (emphasis added) that VAT on "goods and services used in *non-taxable or exempt* transactions shall not be deductible" but that:

> "As regards goods and services which are used both in transactions giving entitlement to deduction and in transactions which do not give entitlement to deduction, deduction shall only be allowed for that part of the value added tax which is proportional to the amount relating to the transactions giving entitlement to deduction (*pro rata* rule)."

158. The Second Directive therefore did not restrict the denominator of the *pro-rata* calculation to taxable and exempt supplies, but also included "transactions which do not give entitlement to deduction," which included not only exempt transactions but also "non-taxable" transactions.

159. Annex A forms an integral part of the Directive; paragraph 22, like Article 11(2), refers to "all transactions":

> "The *pro rata* figure shall, in general, be determined in respect of all transactions carried out by the taxable person (general *pro rata* figure). However a taxable person may, exceptionally, obtain administrative permission to determine special *pro rata* figures for certain sectors of his activities."

160. The Sixth Directive took the same approach: Article 19(1) says that the denominator of the PE fraction is:

> "…the total amount, exclusive of value added tax, of turnover per year attributable to transactions included in the numerator and to transactions in respect of which value added tax is not deductible."

161. UK legislation was narrower: FA 1972, s 3(3)(b) allows a person to deduct the part of the "input tax" which is attributable to taxable supplies, and s3(1) defines "input tax" as the VAT charged on goods or services "for the purpose of a business." By 1983 the requirement to separate the VAT incurred on business and non-business transactions was explicit: VATA 1983 s 14(4) says:

> "Where goods or services supplied to a taxable person...are used or to be used partly for the purposes of a business carried on or to be carried on by him and partly for other purposes, tax on supplies...shall be apportioned so that only so much as is referable to his business purposes is counted as his input tax "shall be apportioned so that only so much as is referable to his business purposes is counted as his input tax."

162. This provision was carried forwards into VATA 1994, s 24(5) and remains in force.

163. Because the requirement for a prior business/non-business apportionment derives from UK law and not the Directives, the use of HMRC's discretionary powers to permit a combined method cannot be *ultra vires* EU law.

164. That our analysis is correct is indicated by the 2010 amendment to Reg 102 of the 1995 Regulations, which introduced new Reg 102ZA. This allows a partially exempt trader to have a combined method. Indeed, HMRC's existing practice is to refuse to approve *separate* methods for partially exempt businesses. The current version of Notice 706, "Partial Exemption" at paragraph 7.6 says:

> ***Will HMRC approve separate BNB and partial exemption methods?***
>
> "Not if you are partly exempt. In these circumstances, where approval of a method for BNB calculations is sought, it must also cover partial exemption calculations (excluding [private use] apportionments…). This is to save the cost of seeking approval of two separate methods and also helps to make sure a fair recovery of VAT overall as the calculations can be considered in their entirety."

165. This is repeated at page 6 of the 2013 HE Framework. Page 7 says:

> "Although any current B/NB agreements remain valid, HMRC will not approve separate B/NB and partial exemption methods after 1 January 2011. HMRC advises HEIs [Higher Education Institutions] to seek approval for a combined method when they next routinely update their existing B/NB agreement."

The requirement that a PESM be "fair and reasonable"

166. We next consider whether the non-inclusion of the T-grant in the denominator of the fraction makes a PESM *ultra vires,* in the context of the statutory requirement

that a PESM must be "fair and reasonable": see FA 1972 s 3(4); VATA 1983 s 15(3) and VATA 1994, s 26(5).

167. In *Kwik-Fit v HMRC* [1998] STC 159 ("*Kwik-Fit*"), the Extra Division of the Inner House of the Court of Session held that a PE method which was not "fair and reasonable" was invalid. However, in *DFS* the tribunal came to a different conclusion, although *Kwik-Fit* was not cited to them. At [193] it said that "we do not accept that the use of the power given by the regulations in a manner which results in an unfair method is void" and gave four reasons for deciding that once a PE method had been approved, it could not be invalid. In particular, the tribunal rejected the submission made by Mr Thomas, for HMRC, at [190(1)], that:

> "it is ultra vires the powers conferred on the Commissioners to give approval to a method which does not reasonably or fairly attribute input tax on the basis of use. And accordingly that any purported approval given of a method which is unfair or unreasonable is void."

168. Although we agreed with that tribunal's analysis of whether a PESM has been approved (see §§129-132 above), we respectfully disagree with their reasons for deciding that, once approved, an unfair and/or unreasonable PESM cannot be void.

169. We set out their reasons in italics, together with our own analysis:

(1) *Reg 102(3) allows HMRC to terminate an approved method, and this "suggests that it is not necessarily intended that an approved unfair method is void."* However, the *vires* for that regulation are found in VATA 1994 s 26(5), which provides that "the Commissioners shall make regulations for securing a fair and reasonable attribution of input tax to taxable supplies." If an approved PESM is not "fair and reasonable" it does not come within Reg 102(3) at all.

(2) *In 2003, Regs 102A and 102C were included in the VAT Regulations 1995. These provide that if a person is using an approved or directed PESM, which "does not fairly and reasonably represent the extent to which goods or services are used by him or are to be used by him in making taxable supplies," HMRC and the trader can serve a notice on the other setting out the required adjustment. This provision "at least hints that it is possible that an unfair method may have been approved or directed as well as that a method may have become unfair.* A method must be fair and reasonable in order to be approved; these regulations allow HMRC to terminate a method which subsequently becomes unfair or unreasonable. There is no necessary inference from these regulations that a method is valid simply on the basis that it was approved, despite never having been fair and reasonable.

(3) *The trader has a right of appeal against the imposition of an unfair method or the failure to approve a fair method, and "that suggests that the proper remedy for the taxpayer against an unfair method is to appeal."* This is the mechanism for legal challenge, so that a trader does not have to resort to judicial review, but it does not carry the necessary implication that unfair methods are valid.

(4) *In* St Helen's School Northwood v HMRC *[2007] STC 633 ["St Helen's"*] *Warren J said at [27] that "if the tribunal thinks that both the existing method and the proposed method are unfair or unreasonable, it could not allow the appeal even if it considers that the proposed special method is less unfair and unreasonable that the existing method." Therefore Warren J "seems at least to be assuming that an unfair method imposed by the Commissioners is not void."* The cited sentence is under the heading "jurisdiction" and we read it as illustrating the limits of the tribunal's powers: it confirms that we cannot intervene to prescribe a new PESM. Warren J does not in fact decide whether the appellant's proposed special method is not *a* fair and reasonable method, see [80] of *St Helen's.*

170. The decision in *Kwik-fit* is brief: the Court simply decided that the directed method was ambiguous and therefore unfair, and so invalid. We too find that a PESM which is not "fair and reasonable" is *ultra vires* the statutory provisions under which the regulations are made.

171. That is, of course, a high threshold. Neither HMRC nor the trader can retrospectively resile from a PESM on the grounds that a different method would be more fair, or more reasonable. Given the extent of HMRC's discretion to approve a PESM under the VAT regulations and its general care and management powers, cases where an approved PESM is *ultra vires* will be rare. However, they are nevertheless possible.

Was approval of a PESM which excluded the HEFC grant, ultra vires*?*

172. We next consider whether or not the exclusion of the T-grant from the PESM meant that it was not fair and reasonable, so as to make it *ultra vires.*

173. Under the CVCP guidelines, all non-formulaic tunnels required "input tax to be offset against output tax in relation to each such activity." We agree with the Tribunal in *Wadham* at [104] that "the CVCP guidelines and the Grid provided the basis for a university or college to adopt a special method… [which included] the recovery of properly attributable residual input tax." Thus, the PESMs used by universities had to address the issue of what to do with the T-grant.

174. In reliance on the CVCP Guidelines and Mr Jamieson's oral evidence, we have already found as a fact at §§52-53 that universities historically did not include the T-grant in the denominator as consideration for an exempt supply of education, but instead treated it as "outside the scope" of VAT.

175. At §76 we found that between 1998 and 2000 the university sector and HMRC were negotiating on changing this approach, and at §77 that the HMRC had corresponded with PwC, resulting in a change to the PESM from 1 July 1999. As already set out at §78, on 5 June 2000, HMRC wrote to PwC saying that:

> "your proposal to include the teaching element of the HEFCE grant in the denominator is accepted. It is accepted that if policy concerning grants differs materially from the agreement reached, the position is open to review…"

176. We therefore find as a fact that in or around 1999-2000, HMRC changed their policy in relation to the treatment of the T-grant for the university sector. This is also consistent with *Sussex,* heard in April and May 1999 at exactly the same time as these issues were being discussed between HMRC and PwC. The tribunal in *Sussex* found that the T-grant should not be included in PESMs based either on the CVCP method or in the PE fraction used for the standard method. At [38] they said:

> "We do not need either to dwell long on the issue concerning the effect of grant income. It is quite clear to us that neither in the standard method nor in the special method with the CVCP guidelines as its framework or setting does grant income as a true subsidy have any place in the partial exemption calculation.

177. Before a tribunal sitting today could came to a different decision from that tribunal, and find that the PESM was void because it did not include the T-grant, it would need to address the somewhat complex case law on grants and subsidies, in the context of facts now between 15 and 40 years old, and which occurred during a period when the provision of funding for university education was very different to that now prevailing. The submissions made to us did not address these questions.

178. Furthermore, any such submission would need to take as its starting point that the attribution of residual input tax "in a more or less rough and ready, proxy fashion" is intrinsic to the nature of the task, as McCombe J put it in *Vision Express v HMRC* [2010] STC 242. In *Wadham* the tribunal said at [102] that any method "other than an impractical one which analyses each input's use is going to have rough edges."

179. Taking all this into account, and in the absence of either detailed argument or contemporaneous facts about the relevant background, we have decided that there is no basis on which we could find Mr Jamieson's decision to allow a PESM without including the T-grant to have been *ultra vires.*

Conclusion

180. We therefore find that HMRC approved the PESM for the periods relevant to the Claim and that such approval was *intra vires*.

Question 4: If the answer to Question 1 is "no," did the retrospective change to the College's operation of the CVCP Guidelines mean that there was a CVCP-based PESM?

181. In view of our findings on Questions 1 and 2, this Question falls away. The CVCP was abandoned and replaced by a new retrospective non-CVCP PESM.

Question 5: is HMRC bound by the PESM to repay the Claim, subject to the evidential burden being satisfied?

Mr Rycroft's submissions

182. Mr Rycroft said the College was entitled to make the Claim because it previously failed to claim sums to which it was entitled under the PESM, and

this failure to claim was a mistake of law, namely that the three year cap which was applied to the 1997 claim had been legal.

183. Mr Rycroft also submitted that, even if the College's failure to include the T-grant in the denominator would now be regarded as unfair and/or unreasonable, that is irrelevant to the matter the Tribunal has to decide. The Claim is on the basis of the PESM which existed in the relevant period, not on the basis of a PESM which might be approved today.

Mr Zwart's submissions

184. Mr Zwart submitted that there was no "mistake" by the College, so as to entitle it to any repayments under VATA s 80. Rather, it had chosen for many years to use the CVCP Guidelines of which it was a "beneficiary," in particular because it was effectively dispensed from the obligation to keep the books and records required of registered traders.

185. Mr Zwart went on to say that it was clear that the T-grant should have been included in the denominator, and that "a fair and reasonable basis requires, in some way, Imperial to take account of the grant income."

186. He therefore submitted that the Claim should be considered together with the earlier claims, which should be recalculated to take into account the T-grant. It was likely that this would trigger an over-repayment, which should be offset against any new sum shown to be due as a result of a failure to include the overheads of academic departments in the residual pot. Mr Zwart relied on *C&E Commrs v National Westminster Bank plc* [2003] STC 1072 ("*National Westminster*") where Jacob J said:

> "[64] Just because a tax gatherer makes a blunder which favours some taxpayers by way of a windfall does not mean that he should perpetuate the blunder in favour of others. A number of wrongs do not necessarily make a right. The interests of the general community are involved—taxpayers collectively have an interest that tax properly due should be collected, and that there should not be repayments to people who are not entitled to them…
>
> [66] It appears to me to be entirely within the ambit of objective justification to say that mistakes need not be perpetuated and to take into account the fact that what is involved here is both complex law and a necessarily large administrative system."

Discussion

187. The Claim was made under VATA s 80(1), which reads:

> "Where a person has (whether before or after the commencement of this Act) paid an amount to the Commissioners by way of VAT which was not VAT due to them, they shall be liable to repay the amount to him."

188. The Claim is for the period 1974 to 1994. We have already decided that the PESM which applied to 1984-93 was *de facto* approved by Mr Jamieson's predecessor(s), and confirmed in writing by Mr Jamieson, who also approved the

PESM from 1974-83 and for 1994. We have also found that the PESM was not *ultra vires* or otherwise objectively unreasonable.

189. The methodology of the PESM depended on the allocation of residual VAT relating to taxable outputs. On 2 October 1997, Mr Jamieson confirmed that HMRC would allow a further claim for the overheads of academic departments previously omitted from the residual pot, because it "recognised that there is an element recoverable due to the fact that these departments make both taxable (research supplies) and exempt supplies." Mr Jamieson's letter went on to say that "the claim will of course be subject to any necessary restrictions under the 3 year capping rules."

190. In each of the years 1973-74 to 1993-94 an approved PESM was in place. If, under that PESM, some of the residual input VAT properly attributable to the taxable outputs was not claimed, then this is "an amount [paid] to the Commissioners by way of VAT which was not due to them." HMRC are therefore liable to repay that VAT.

191. We do not agree with Mr Zwart's submission that the College did not make a mistake of law. His submission is founded on an argument that we have already rejected, namely that the College continued to operate within the CVCP Guidelines. Rather, it is evident from Mr Jamieson's letter of 2 October 1997, cited above, that both HMRC and the College believed that the three year cap prevented further recovery, and that is the error of law under which the College's *Fleming* claim is made.

192. We also do not accept Mr Zwart's submission that *National Westminster* is relevant. In that case HMRC had successfully argued (the burden being on them) that the taxpayer would be unjustly enriched if a VAT repayment was made The taxpayer had submitted that it should be repaid VAT so as to put it in the same position as competitors who had succeeded in their claims. At [55] Jacob J says (emphasis in original):

> "Section 80 applies where the taxpayer has paid VAT 'which was not VAT due'. The essence of the unfair treatment case is not that the VAT was not due. It is that *even though it was due*, it should be repaid because trade rivals were unjustifiably repaid. That, as a matter of construction, is outwith s 80..."

193. Thus, in *National Westminster* both parties accepted that the VAT was due; the appellant had no statutory right to be repaid. Its case rested on the argument that it should nevertheless receive a repayment as a matter of fairness, because HMRC had failed to apply the defence of unjust enrichment so as to prevent repayments being made to the appellant's competitors. There is no parallel with the College's case, which is that VATA s 80 gives it a statutory right to repayment.

194. This is the context of the passages cited by Mr Zwart – "*just because a tax gatherer makes a blunder which favours some taxpayers by way of a windfall does not mean that he should perpetuate the blunder in favour of others*" and "*mistakes need not be perpetuated.*" The "blunder" and the "mistakes" referred to was HMRC's failure properly to apply the law to others.

195. *National Westminster* does not provide any authority for HMRC to revisit a PESM which was "fair and reasonable" when it was approved around two decades ago, even if its terms would have been different were it to be considered now. Such a reading would be irreconcilable with Reg 102 and 102A of the VAT Regulations 1995, which allow HMRC to direct the termination of an approved PESM, and specifically provide that this takes effect from "prescribed accounting periods commencing on or after the date of the notice or such later date as may be specified in the notice."

196. Mr Zwart has not put forward any other argument to support his position that the PESM can now be revisited.

197. Our answer to Question 5 is that HMRC are bound by the PESM to repay the Claim, subject to the evidential burden being satisfied. The only remaining matter is whether the College can satisfy that burden.

Question 6: is the evidential burden satisfied?

198. We first set out the parties' submissions about the approach required in dealing with such elderly claims, before considering the evidence put forward to support the Claim.

Mr Rycroft's submissions

199. Mr Rycroft did not explicitly dispute that the burden of proof lay with the College. However, he sought to rely on *Marks & Spencer v HMRC* [1999] STC 205 ("*Marks & Spencer*"), where Moses J said at page 241, in relation to the difficulties faced by a trader who has passed on the wrongly charged VAT to its customers but was seeking to claim that it had nevertheless suffered damage:

> "…the tribunal of fact must bear in mind that in making that assertion the trader may, at least until the three-year cap was introduced, be forced into the position of providing material relevant to a time when it did not suspect and had no reason to suspect that it might be overpaying tax and, thus, have any need to prepare a claim for repayment. Any difficulty that a trader has in providing such material either because of lapse of time or because of the complexity of determining whether, in fact, the passing on of a charge affected profits or sales and caused damage should be viewed sympathetically. Lacunae in the evidence should not be considered to the detriment of the trader. It was, after all, the taxing authority which caused the problem in the first place. Thus, it seems to me, if, after considering all the evidence, there is uncertainty or absence of detail, that should not be held against the trader."

200. Mr Rycroft invited the Tribunal to take the same approach, so that gaps in the evidence should not be "held against" the College, as it was HMRC who had capped the 1997 claim, and had the Claim been submitted then, it would have been easier to obtain the evidence.

Mr Zwart's submissions

201. Mr Zwart said that the burden was on the College to produce the evidence necessary to support the Claim. He cited *The Claimants Listed in the Group Register of the Loss Relief GLO v HMRC* [2013] EWHC 205, where Henderson J said at [52], in relation the concerns of the claimants about providing the evidence to show that the "no possibilities" test at issue in those proceedings had been satisfied:

> "…it is the claimants who have chosen to bring their claims, involving very large sums of money, and the evidential burden lies on them to demonstrate that the no possibilities test is satisfied. The Revenue cannot reasonably be blamed for making searching enquiries when so much is at stake…The process may well be inconvenient, time-consuming and expensive for the claimants; but (subject to what I say below about the way forward) it is in my view a burden which they have brought upon themselves, and about which they cannot legitimately complain."

202. He also relied on *WMG Acquisition Co UK Ltd v HMRC* [2013] UKFTT 215 (Judge Demack), a recent case lost by the taxpayer because it failed to satisfy the tribunal that it had the evidence to support *Fleming* claims relating to travel and subsistence. At [29], Judge Demack said:

> "The burden of proving that the two companies have not recovered the input tax on employee's travel and subsistence expenses falls on the taxpayer in appeals such as the present one. And whilst only the civil standard proof is involved, the tribunal cannot be expected to make decisions simply on the basis that a claim covers a period long ago for which a taxpayer cannot be expected to hold any records, so that its claims should be accepted without question and without evidence. It is simply not good enough for the two companies to say to the Commissioners, 'You accepted our claims for input tax recovery for the period 1999 to 2002 on the basis of our records for that period. We say that we made no input tax recovery for earlier periods for which we hold no records whatsoever, but for which we say we operated in exactly the same way and made no input tax recovery claims. You must accept our claims and repay the input tax concerned.'"

Discussion

203. We are uneasy about Mr Rycroft's reliance on *Marks & Spencer*. The paragraph cited is in the context of an unjust enrichment claim, where the burden was on HMRC. Later on the same page, Moses J said:

> "…the tribunal ought not to place reliance upon any failure to produce detailed facts and figures when that failure will normally be the fault of the taxing authority which levied a charge to which it was not entitled. A tribunal should only conclude that the defence of unjust enrichment is made out where the evidence satisfies it that a repayment will cause unjust enrichment."

204. The College's position is different: as Mr Zwart says, the burden of proving the Claim rests with the College. HMRC should, of course, be reasonable in terms of the evidence which it will accept: it is as true for the College as it was for M&S that the

three year cap was not its fault, and gathering evidence would have been more straightforward in 1997 than it was when the Claim was made, some twelve years later. But we respectfully agree with both Henderson J and Judge Demack that there must be sufficient evidence to support the Claim.

205. The parties asked us to determine the issues which we formulated as Questions 1-6, see §92. If appropriate, we were asked to adjourn the appeal to give the parties the opportunity to progress matters of quantum outside the Tribunal.

206. We decided that the position was beyond doubt for the period 1973-74 to 1980-81. The basis of the Claim is that the college's academic staff were making taxable supplies of commercial research to external third party customers. For the period from 1973-74 to 1980-81, the only evidence for the Claim is the statutory accounts. These do not identify any income as arising from "work for outside bodies" or "WOBs"; the first such income is in the accounts for the year ended 31 July 1983, which contained a comparative figure for 1982. The Claim for the period 1973-74 to 1980-81 is instead based on extrapolation from later years, based on the assumption that academic staff were carrying out paid work for non-university clients; that the income from that work accrued to the university and is reflected in the "other income" category of the statutory accounts; and that the academic departments incurred unallocated residual VAT which relates in part to those taxable outputs. Other than the statutory accounts, there is no supporting documentary evidence, such as research papers provided for such third party customers, invoices, letters, financial analysis or other details. Mr Mason very fairly said that "the current systems and retained records don't allow me to get any detail before 1982." There is also no oral evidence from anyone who was present at the time.

207. We find that for the period 1973-74 to 1980-81 the evidence is insufficient to support the Claim, and we dismiss that part of the College's appeal.

208. For the period from 1981-82 to 1993-94 there was more evidence, but the focus of both party's submissions during the hearing was on the legal issues in dispute rather than on providing the Tribunal with a clear exposition of the detail supporting the part of the Claim relating to each year.

209. As a result, we remain uncertain about a number of evidential matters: the cost centres used for the Claim and those used for the 1997 claim; the interaction with IC Consultants Limited, a company set up in 1990 to provide third party research; how the income and costs arising in St Mary's Hospital medical school (which merged with the College in 1988) were taken into account; and how the VAT recovery percentages used were calculated. Although we were assisted by Mr Zwart's cross-examination of Mr Martin, it is in the nature of such exercises that they do not provide a complete picture. For example, it would have been helpful to be provided, for each year, with a cross-referenced document showing the amount of the claim for that year, the source of the evidence and the inferences being made.

210. The uncertainties are such that a further hearing would be required to decide whether sufficient evidence exists to support the Claim for the years 1981-82 to 1993-

94. Given that the parties suggested that they be given the opportunity to try and agree issues of quantum outside the tribunal, we decided to adjourn the appeal in relation to those years and issue the following directions:

(1) Within three calendar months of a final decision on the matters decided in this judgment, the parties are to inform the Tribunal as to whether they have come to an agreement on the remaining part of the Claim, being the years 1982 to 1994.

(2) If the remaining part of the Claim has not been settled by that date, the Tribunal will give further directions for the conduct of the hearing of this appeal, which is to be before the same panel.

Overall decision and appeal rights

211. We have decided Questions 1-5 set out at §92, in the College's favour. In relation to Question 6, we dismissed the part of the Claim relating to the period from 1973-74 to 1980-81 for lack of evidential support. The part of the Claim which relates to the period from 1981-82 to 1993-94 is adjourned as set out above.

212. This document contains full findings of fact and reasons for the Tribunal's decision on the issues in this appeal. Any party dissatisfied with this decision has a right to apply for permission to appeal against it pursuant to Rule 39 of the Tribunal Procedure (First-tier Tribunal) (Tax Chamber) Rules 2009. The application must be received by this Tribunal not later than 56 days after this decision is sent to that party. The parties are referred to "Guidance to accompany a Decision from the First-tier Tribunal (Tax Chamber)" which accompanies and forms part of this decision notice.

ANNE REDSTON
TRIBUNAL JUDGE

RELEASE DATE: 22 January 2015

APPENDIX 1
DIRECTIVES, LEGISLATION AND REGULATIONS

EU DIRECTIVES

The Second Directive 67/228/EEC

Article 11

1. Where goods and services are used for the purposes of his undertaking, the taxable person shall be authorised to deduct from the tax for which he is liable

(a) the value added tax invoiced to him in respect of goods supplied to him or in respect of services rendered to him…

2. Value added tax on goods and services used in non-taxable or exempt transactions shall not be deductible…

As regards goods and services which are used both in transactions giving entitlement to deduction and in transactions which do not give entitlement to deduction, deduction shall only be allowed for that part of the value added tax which is proportional to the amount relating to the transactions giving entitlement to deduction (*pro rata* rule)."

Article 20

The Annexes shall form an integral part of this Directive

Annex A

22. Regarding Article 11, second paragraph

The pro rata figure shall, in general, be determined in respect of all transactions carried out by the taxable person (general *pro rata* figure). However a taxable person may, exceptionally, obtain administrative permission to determine special *pro rata* figures for certain sectors of his activities.

The Sixth Directive (77/388/EEC) dated 17 May 1977

Article 17: origin and scope of the right to deduct

2. In so far as the goods and services are used for his taxable transactions the taxable person shall be entitled to deduct from the tax which he is liable to pay:

(a) value added tax due or paid in respect of goods or services supplied or to be supplied to him by another taxable person…

5. As regards goods and services to be used by a taxable person both for transactions covered by paragraphs 2 and 3, in respect of which value added tax is deductible, only such proportion of the VAT shall be deductible as is attributable to the former transactions.

This proportion shall be determined in accordance with Article 19.

However, Member States may:

(a) authorize the taxable person to determine a proportion for each sector of his business, provided that separate accounts are kept for each sector.

(b) compel the taxable person to determine a proportion for each sector of his business and to keep separate accounts for each sector,

(c) authorize or compel a taxable person to make the deduction on the basis of the use of all of the part of the goods and services

(d) authorize or compel the taxable person to make the deduction in accordance with the rule laid down in the first subparagraph, in respect of all goods and services used for all transactions referred to therein;

(e) provide that where the value added tax which is not deductible by the taxable person is insignificant it shall be treated as nil.

Article 19: Calculation of the deductible proportion

1. The proportion deductible under the first subparagraph of Article 17(5) shall be made up of a fraction having:

- as numerator, the total amount, exclusive of value added tax, of turnover per year attributable to transactions in respect of which value added tax is deductible under Article 17 (2) and (3),

- as denominator, the total amount, exclusive of value added tax, of turnover per year attributable to transactions included in the numerator and to transactions in respect of which value added tax is not deductible...

The proportion shall be determined on an annual basis, fixed as a percentage and rounded up to a figure not exceeding the next unit.

2. …

3. The provisional proportion for a year shall be that calculated on the basis of the preceding year's transactions. In the absence of any such transactions to refer to, or where they were insignificant in amount, the deductible proportion shall be estimated provisionally, under supervision of the tax authorities, by the taxable person from his own forecasts. However, Member States may retain their current rules.

Deductions made on the basis of such provisional proportion shall be adjusted when the final proportion is fixed during the next year.

UK LEGISLATION

Finance Act 1972

Section 1: Value Added Tax

(1) A tax, to be known as value added tax, shall be charged

(2) the tax shall be under the care and management of the Commissioners.

Section 3: Deduction of input tax

(1) The following tax (in this Part of this Act referred to as “input tax”), that is to say

(a) tax on the supply to a taxable person of any goods or services for the purpose of a business carried on or to be carried on by him; and

(b) tax paid or payable by a taxable person on the importation of any goods used or to be used for the purpose of a business carried on or to be carried on by him;

may, at the end of any prescribed accounting period, be deducted by him, so far as not previously deducted and to the extent and subject to the exceptions provided for by or under this section, from the tax chargeable on supplies by him (in this section referred to as " output tax ")…

(3) …the input tax that may be deducted by a taxable person shall be:

(a) the whole of that tax if all his supplies of goods or services are taxable supplies; and

(b) such part of that tax as, in accordance with regulations made under this section, is attributable to taxable supplies, if some but not all of his supplies are taxable supplies…

(4) The Commissioners shall make regulations for securing a fair and reasonable attribution of input tax to taxable supplies…

and may make different provision for different circumstances and, in particular (but without prejudice to the generality of this provision) for different descriptions of goods or services; and may contain such incidental and supplementary provisions as appear to the Commissioners necessary or expedient.

Finance Act 1977

Schedule 6: Value Added Tax: Part 1: Substantive amendments of FA 1972

1. For section 2 to 6 of the 1972 Act (scope of tax, deduction of input tax, taxable persons, supply and self-supply) the following sections shall be substituted…

Section 3: Credit for input tax against output tax

(3) Subject to subsection (4), "input tax", in relation to a taxable person, means the following tax, that is to say-

(a) tax on the supply to him of any goods or services; and

(b) tax paid or payable by him on the importation of any goods,

being (in either case) goods or services used or to be used for the purpose of any business carried on or to be carried on by him; and "output tax" means tax on supplies which he makes.

(4) Where goods or services supplied to a taxable person, or goods imported by him, are used or to be used partly for the purposes of a business carried on or to be carried on by him and partly for other purposes, tax on supplies and importations is apportioned so that only so much as is referable to his business purposes is counted as his input tax.

Section 4: input tax allowable under section 3

(1) The amount of input tax for which a taxable person is entitled to credit at the end of any period shall be determined as follows

(a) if his business is such that all his supplies are taxable supplies, there is allowable the whole of the input tax for the period (that is, input tax on supplies and importations in the period) ;

(b) if it is such that some but not all of his supplies are taxable supplies, there is allowable such proportion of the input tax for the period as, in accordance with regulations, is attributable to taxable supplies;…

(3) The Commissioners shall make regulations for securing a fair and reasonable attribution of input tax to taxable supplies, and any such regulations may provide for-

(a) determining a proportion of supplies in any prescribed accounting period which is to be taken as consisting of taxable supplies and provisionally attributing the input tax for that period in accordance with the proportion so determined…

(4) Regulations under subsection (3) may make different provision for different circumstances and, in particular (but without prejudice to the generality of that subsection) for different descriptions of goods or services; and may contain such incidental and supplementary provisions as appear to the Commissioners necessary or expedient.

Value Added Taxes Act 1983 (a consolidating act)

Section 14: credit for input tax against output tax

(2) Subject to the provisions of this section, he is entitled at the end of each such period to credit for so much of his input tax as is allowable under section 15 below, and then to deduct that amount from any output tax that is due from him.

(3) Subject to subsection (4) below, "input tax", in relation to a taxable person, means the following tax, that is to say-

(a) tax on the supply to him of any goods or services…

being (in either case) goods or services used or to be used for the purpose of any business carried on or to be carried on by him ; and "output tax" means tax on supplies which he makes.

(4) Where goods or services supplied to a taxable person...are used or to be used partly for the purposes of a business carried on or to be carried on by him and partly for other purposes, tax on supplies...shall be apportioned so that only so much as is referable to his business purposes is counted as his input tax.

Section 15: Input tax allowable under section 14

(1) The amount of input tax for which a taxable person is entitled to credit at the end of any period shall be determined as follows:

(a) if his business is such that all his supplies are taxable supplies, there is allowable the whole of the input tax for the period (that is input tax on supplies and importations in the period);

(b) if it is such that some but not all of his supplies are taxable supplies, there is allowable such proportion of the input tax for the period as, in accordance with regulations, is attributable to taxable supplies;…

(3) The Commissioners shall make regulations for securing a fair and reasonable attribution of input tax to taxable supplies, and any such regulations may provide for:

(a) determining a proportion of supplies in any prescribed accounting period which is to be taken as consisting of taxable supplies and provisionally attributing the input tax for that period in accordance with the proportion so determined;

(b) …

(4) Regulations under subsection (3) above may make different provision for different circumstances and, in particular (but without prejudice to the generality of that subsection) for different descriptions of goods or services; and may contain such incidental and supplementary provisions as appear to the Commissioners necessary or expedient.

Schedule 7: Administration, collection and enforcement

1(1) The tax shall be under the care and management of the Commissioners.

Value Added Taxes Act 1994 (a consolidating act effective from 5 July 1994)

Section 24: Input tax and output tax

(1) Subject to the following provisions of this section, "input tax", in relation to a taxable person, means the following tax, that is to say—

(a) VAT on the supply to him of any goods or services..

being (in each case) goods or services used or to be used for the purpose of any business carried on or to be carried on by him

(2)-(4) …

(5) Where goods or services supplied to a taxable person…are used or to be used partly for the purposes of a business carried on or to be carried on by him and partly for other purposes, VAT on supplies…shall be apportioned so that only so much as is referable to his business purposes is counted as his input tax….

Section 25: Payment by reference to accounting periods and credit for input tax against output tax

(1) …

(2) Subject to the provisions of this section, [the taxable person] is entitled at the end of each prescribed accounting period to credit for so much of his input tax as is allowable under section 26, and then to deduct that amount from any output tax that is due from him…

Section 26: Input tax allowable under section 25

(1) The amount of input tax for which a taxable person is entitled to credit at the end of any period shall be so much of the input tax for the period (that is input tax on supplies, acquisitions and importations in the period) as is allowable by or under regulations as being attributable to supplies within subsection (2) below.

(2) The supplies within this subsection are the following supplies made or to be made by the taxable person in the course or furtherance of his business—

(a) taxable supplies…

(3) The Commissioners shall make regulations for securing a fair and reasonable attribution of input tax to supplies within subsection (2) above, and any such regulations may provide for—

(a) determining a proportion by reference to which input tax for any prescribed accounting period is to be provisionally attributed to those supplies…

(4) Regulations under subsection (3) above may make different provision for different circumstances and, in particular (but without prejudice to the generality of that subsection) for different descriptions of goods or services; and may contain such incidental and supplementary provisions as appear to the Commissioners necessary or expedient.

Section 80: Recovery of overpaid VAT

(1) Where a person has (whether before or after the commencement of this Act) paid an amount to the Commissioners by way of VAT which was not VAT due to them, they shall be liable to repay the amount to him…

(6) A claim under this section shall be made in such form and manner and shall be supported by such documentary evidence as the Commissioners prescribe by regulations; and regulations under this subsection may make different provision for different cases.

Schedule 11: Administration, collection and enforcement

1. General

(1) The tax shall be under the care and management of the Commissioners.

REGULATIONS

The Value Added Tax (General) Regulations (1972/1147) and The Value Added Tax (General) Regulations (1980/1536)

Regulation 24

(1) Subject to paragraph (2) of this Regulation, the proportion of input tax to be attributed to taxable supplies by any taxable person who makes exempt supplies shall be determined in any prescribed accounting period by either of the following methods:

Method 1

Subject to Regulation 25 [which dealt with certain exclusions] he may deduct such part of his input tax as bears the same ratio to his total input tax as the value of taxable supplies by him bears to the value of all supplies made by him.

Method 2 [not relevant to this decision]

(2) The Commissioners may allow or direct the use of a method other than the one specified in paragraph (1) of this Regulation.

The Value Added Tax (General) Regulations 1985 (1985/886)

30 Attribution of input tax by a person making exempt supplies

(1) Subject to paragraph (2) of this regulation, the amount of input tax to be provisionally attributed to taxable supplies by any taxable person who makes exempt supplies shall be determined in any prescribed accounting period by the following method, that is to say:

Subject to regulation 32 he may deduct such part of his input tax as bears the same ratio to his total input tax as the value of taxable supplies by him bears to the value of all supplies by him.

(2) The Commissioners may allow or direct the use of a method other than that specified in paragraph (1) of this regulation.

67. Requirement, direction, demand or permission

Any requirement, direction, demand or permission by the Commissioners, under or for the purposes of these Regulations, may be made or given by a notice in writing, or otherwise.

The Value Added Tax (General) (Amendment) (No. 2) Regulations 1987 (1987/510)

30(1) Subject to paragraphs (2), (3), (4) and (5) of this regulation, the amount of input tax to be provisionally attributed to taxable supplies by a taxable person shall be determined…by the following method:

(a) …

(b) the input tax on such importations and supplies as are wholly used or to be used by him in making taxable supplies may be deducted;

(c) the input tax on such importations and supplies as are wholly used or to be used in making exempt supplies or if any activity other than the making of taxable supplies may not be deducted;

(d) the deductible proportion of any remaining input tax shall be provisionally calculated as follows:

(i) importations by and supplies to the taxable person in the period which are partly used or to be used by him in making taxable supplies shall be identified;

(ii) the extent to which the above importations and supplies are used or to be used by him in making taxable supplies shall be ascertained, and expressed as a proportion of the whole use made or to be made by him of such importations and supplies;

(iii) there may be deducted such proportion of the remaining input tax as corresponds with the proportion ascertained above.

(2) The Commissioners may in the case of a taxable person who incurs exempt input tax [i.e. input tax wholly or partly attributable to an exempt supply] allow that paragraph (1)(d) of this regulation shall not apply, in which case the deductible proportion of any remaining input tax may be provisionally calculated as follows:

Subject to paragraph (3) of this regulation, there may be deducted such proportion of any remaining input tax as bears the same ratio to the total remaining input tax of the taxable person as the value of taxable supplies by him bears to the value of all supplies by him.

(3) …

(4) Where the Commissioners consider it necessary in order to secure a fair and reasonable attribution of input tax to taxable supplies, they may in the case of any taxable person or class of such persons, direct the manner in which the extent of use of importations and supplies is to be ascertained under paragraph (1)(d) of this regulation.

(5) The Commissioners may allow the use of a method other than that specified in this regulation."

The Value Added Tax (General) (Amendment) Regulations 1992 (SI 1992/645)

30. Attribution of input tax to taxable supplies

(1) Subject to regulation 31 below, the amount of input tax which a taxable person shall be entitled to deduct provisionally shall be that amount which is attributable to taxable supplies in accordance with this regulation.

(2) In respect of each prescribed accounting period:

(a) goods imported by and goods or services supplied to the taxable person in the period shall be identified;

(b) there shall be attributed to taxable supplies the whole of the input tax on such of those goods or services as are used or to be used by him exclusively in making taxable supplies;

(c) no part of the input tax on such of those goods or services as are used or to be used by him exclusively in making exempt supplies, or in carrying on any activity other than the making of taxable supplies, shall be attributed to taxable supplies;

(d) there shall be attributed to taxable supplies such proportion of the input tax on such of those goods or services as are used or to be used by him in making both taxable and exempt supplies as bears the same ratio to the total of such input tax as the value of taxable supplies made by him bears to the value of all supplies made by him in the period.

(4) The ratio calculated for the purpose of paragraph (2)(d) above shall be expressed as a percentage and, if that percentage is not a whole number, it shall be rounded up to the next whole number.

31. Use of other methods

(1) The Commissioners may approve or direct the use by a taxable person of a method other than that specified in regulation 30 above, save that where the use of a method was allowed prior to 1st August 1989 there shall not be included in the calculation (if the method in question would otherwise allow it)—

(a) the value of any supply which, under or by virtue of any provision of the Act, the taxable person makes to himself; and

(b) the input tax on such a supply.

(2) A taxable person using a method as approved or directed by the Commissioners under paragraph (1) above shall continue to use that method unless the Commissioners approve or direct the termination of its use.

(3) Any direction under paragraph (1) or (2) above shall take effect from the date upon which the Commissioners give such direction or from such later date as they may specify.

The Value Added Tax Regulations 1995 (1995/2518)

4. Requirement, direction, demand or permission

Any requirement, direction, demand or permission by the Commissioners, under or for the purposes of these Regulations, may be made or given by a notice in writing, or otherwise.

34. ***Correction of errors****…*

35.

1. Where a taxable person has made an error—

(a) in accounting for VAT, or

(b) in any return made by him,

Then…he shall correct it in such manner and within such time as the Commissioners may require.

37. Claims for recovery of overpaid VAT

Any claim under section 80 of the Act shall be made in writing to the Commissioners and shall, by reference to such documentary evidence as is in the possession of the claimant, state the amount of the claim and the method by which that amount was calculated.

101. Attribution of input tax to taxable supplies

(1) Subject to regulation 102, the amount of input tax which a taxable person shall be entitled to deduct provisionally shall be that amount which is attributable to taxable supplies in accordance with this regulation.

(2) In respect of each prescribed accounting period:

(a) goods imported or acquired by and, subject to paragraph (5) below, goods or services supplied to, the taxable person in the period shall be identified,

(b) there shall be attributed to taxable supplies the whole of the input tax on such of those goods or services as are used or to be used by him exclusively in making taxable supplies,

(c) no part of the input tax on such of those goods or services as are used or to be used by him exclusively in making exempt supplies, or in carrying on any activity other than the making of taxable supplies, shall be attributed to taxable supplies, and

(d) there shall be attributed to taxable supplies such proportion of the input tax on such of those goods or services as are used or to be used by him in making both taxable and exempt supplies as bears the same ratio to the total of such input tax as the value of taxable supplies made by him bears to the value of all supplies made by him in the period…

(4) The ratio calculated for the purpose of paragraph (2)(d) above shall be expressed as a percentage and, if that percentage is not a whole number, it shall be rounded up to the next whole number.

102. Use of other methods

(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…

(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.

Value Added Tax (Amendment) (No 6) Regulations 2003 (SI 2003/3220)

21. After regulation 102, insert

102A. (1) Where a taxable person—

(a) is for the time being using a method approved or directed under regulation 102, and

(b) that method does not fairly and reasonably represent the extent to which goods or services are used by him or are to be used by him in making taxable supplies,

the Commissioners may serve on him a notice to that effect, setting out their reasons in support of that notification and stating the effect of the notice.

(2) The effect of a notice served under this regulation is that regulation 102B shall apply to the person served with the notice in relation to—

(a) prescribed accounting periods commencing on or after the date of the notice or such later date as may be specified in the notice, and

(b) longer periods to the extent of that part of the longer period falling on or after the date of the notice or such later date as may be specified in the notice.

102B…

102C

(1) Subject to regulation 102A, where a taxable person—

(a) is for the time being using a method approved or directed under regulation 102, and

(b) that method does not fairly and reasonably represent the extent to which goods or services are used by him or are to be used by him in making taxable supplies,

the taxable person may serve on the Commissioners a notice to that effect, setting out his reasons in support of that notification.

(2) Where the Commissioners approve a notice served under this regulation, the effect is that regulation 102B shall apply to the person serving the notice in relation to—

(a) prescribed accounting periods commencing on or after the date of the notice or such later date as may be specified in the notice, and

(b) longer periods to the extent of that part of the longer period falling on or after the date of the notice or such later date as may be specified in the notice.".

Value Added Tax (Amendment) Regulations 2005 (SI 2005/762)

2. The Value Added Tax Regulations 1995(**2**) are amended as follows

3. (1) In regulation 101(4), for "to the next whole number" substitute "as specified in paragraph (5) below".

(2) After regulation 101(4) add—

"(5) The percentage shall be rounded up—

(a) where in any prescribed accounting period or longer period which is applied the amount of input tax which is available for attribution under paragraph 2(d) above prior to any such attribution being made does not amount to more than £400,000 per month on average, to the next whole number, and

(b) in any other case, to two decimal places.".

4. After regulation 102(4) add—

"(5) Any approval given or direction made under this regulation shall only have effect if it is in writing in the form of a document which identifies itself as being such an approval or direction."

The Value Added Tax (Amendment) (No. 4) Regulations 2010 (SI 2010/3022)

6. After regulation 102 (use of other methods), insert

102ZA

(1) A taxable person who is required to make an apportionment under section 24(5) of the Act in relation to goods or services which are used or are to be used partly for business purposes and partly for other purposes may effect that apportionment using a method provided for in regulation 102(1).

(2) Where the taxable person referred to in paragraph (1) is not a fully taxable person, the method used shall be the only method used to calculate that person's deductible input tax.

(3) …

(4) Where a person effects the apportionment referred to in paragraph (1) using a method provided for in regulation 102(1)--

(a) regulations 102(1A) to (17) and 102A to 102C shall apply;

(b) regulations 105A, 106 and 106ZA shall not apply; and

(c) for the purposes of defining a longer period and determining an adjustment of attribution under regulation 107, "exempt input tax" shall include non-business VAT.

(5) …

APPENDIX 2

THE CVCP GUIDELINES

The first CVCP Guidelines were agreed in March 1973, and so far as relevant to this decision, provided as follows:

> "11. Universities will be entitled to recover input tax, or a proportion of it, included in the cost of goods and services used wholly or in part to make taxable supplies. A description of the normal arrangements for the recovery of input tax by partially exempt organisations is contained in Section 1 of Customs and Excise Notice No. 706. The concept in this Notice is one in which a partly exempt organisation apportions its input tax between taxable and exempt outputs and then deducts only that part of the input tax which relates to taxable outputs. This would not be effective in university circumstances since the value of a university's exempt outputs (the whole of its teaching and research effort) is much the greater part of the value of its total outputs. Customs and Excise have accordingly approved a special arrangement for universities whereby each taxable activity - i.e. those where an output tax liability will arise - can be dealt with separately or 'tunnelled'. Under this arrangement there will have to be separate accounting for each taxable activity, but it will be possible for input tax to be offset against output tax in relation to each such activity. As an extension of this arrangement it has also been agreed that universities will not have to keep any detailed records, on either the output or input sides, in respect of their non-taxable activities.
>
> 12. In relation to the making of some of the taxable supplies - such as the letting of accommodation to an outside, non-educational body for a conference organised by that body - it will be apparent that goods and services will be used which are also required for the purpose of making exempt supplies. The two areas in which this factor is of special relevance are those at (iv) and (v) in paragraph 7 which, in shorthand form, may be described as the supply of outside conference/holiday facilities and the supply of non-exempt catering. Here a formula approach has been agreed under which universities will not be required to keep any records of the amounts of tax actually paid in the cost of related inputs. On the basis of evidence collected from a sample of universities, Customs and Excise have agreed that each university shall be entitled to reclaim 20% of the output tax payable in respect of those two taxable supplies: this proportion will be regarded as representing related, deductible input tax. The Group has welcomed this as a major contribution towards eliminating time-consuming, detailed accounting work which would otherwise have been necessary: its expectation is that the saving in administrative costs which will result will more than compensate any university which might believe that it could substantiate a case for recovering greater amounts of input tax than will be recoverable under this formula. The alternative to acceptance of the formula, which any university is entitled to explore and opt for, is full and rigorous accounting for all input tax included in the cost of goods and services used to make these particular taxable supplies and the

presentation to Customs and Excise of a detailed breakdown of the apportionment of that input tax between taxable and exempt outputs.

13. There is one other instance in which it has been possible to agree the use of the formula approach. This relates to bars. Universities will wish to keep separate account of all input tax included in the cost of liquor and tobacco purchases since this will all be recoverable to the extent that sales of these items will be wholly taxable. It has been recognised however, that there will be other expenditure on goods and services relating to bars, apart from the drink and tobacco purchases, where input tax will be payable - for example on glasses, cleaning materials and items of equipment - and ought to be recoverable. Customs and Excise have accordingly agreed that each university shall be entitled to reclaim 5% of the total output tax payable in respect of bars as representing related deductible input tax on these items.

14. In relation to all other areas where an output tax liability will arise, schemes similar to those devised for commercial retailers for recovery of input tax - of which examples are given on pages 6 and 7 of Notice No. 706 - will have to be devised and agreed locally in respect of each distinct taxable activity. In this connection it should be remembered that input tax can only be recovered in the proportion to which the value of taxable outputs bear to the value of total outputs. In some instances - for example the sale of computer time at full commercial rates - this proportion may be very small. In circumstances where the amount of tax potentially recoverable is likely to be exceeded by the cost of keeping the necessary records to support a claim, universities can elect, as appropriate, to forego the right to recover input tax and thereby avoid the additional administrative work which would otherwise be involved.

Accounting Procedures

15. The administration necessary to account for VAT will have to include:

(i) The provision of separate accounting for each taxable activity. Where input tax is to be recovered other than on the formula bases described in paragraphs 12 and 13, invoices - both received and rendered - relating to particular taxable activities will have to be retained for three years. Where the formula approach is to be used, it will not be necessary to keep input invoices. For non-exempt catering, a record of the total value of sales through all taxable dining outlets (such as that provided by cash registers) will be adequate on the output side."

The guidelines were accompanied by a Grid or worksheet for calculating the recoverable input tax from the formulaic and non-formulaic. This is set out at [48] of *Wadham* and is not reproduced here, as the College did not use any non-formulaic tunnels.

The Guidelines were amended in March 1977. Section C "Interpretation" said:

"1. Input VAT

It will be realised that where new areas have been brought into liability to VAT by the revised Guidance it is possible, under the principle of 'tunnelling', to claim back input VAT on supplies wholly attributable to the outputs chargeable. Where the outputs consist of both chargeable (which includes zero-rated) and exempt supplies (as, for example, where exempt supplies to students are made in addition to chargeable supplies) only a proportion of inputs can be reclaimed on the following formula.

$$\text{Input VAT} \times \frac{\text{Chargeable Supplies}}{\text{Chargeable Supplies + Exempt Supplies}}$$

Recalculation of the input reclaim on an annual basis is also required and any adjustment of input made in the return to the end of July in each year.

In order to avoid the complication of this reclaim there are two possible alternatives:

a. VAT may be charged on all outputs so that the whole input may be reclaimed;

b. A formula may be negotiated with the local VAT office on the basis of reclaim of a fixed percentage of the output VAT.

In 1985 further changes were agreed, and these were incorporated in the 1987 version of the guidelines, which included the following paragraph about grant income:

"*6. Transactions which are outside the scope of the tax*

Grants and donations which are given freely and do not confer any unique benefit to the recipient are not consideration for a supply and are therefore outside the scope of the tax. An example of such an outside the scope payment is a UGC [University Grants Commission] grant, but for others you should be careful in that some bodies use the term 'grant' in a general way and some 'grants' are the consideration for a supply. If you are in any doubt, please consult your local VAT office."

Part IV of the 1987 Guidelines was headed "VAT on purchases and recovery of input tax, and included the following paragraphs:

"*42. Recovery of Input tax (tunnelling)*

Universities are entitled to recover input tax, or a proportion of it included in the cost of goods and services used wholly or in part to make taxable supplies. Because of the value of a university's exempt outputs is much the greater part of the value of its total outputs, and it would recover little input tax under a pro-rata method, Customs and Excise approved special arrangements for universities whereby each taxable activity can been dealt with separately or 'tunnelled'. Under these arrangement there has to be separate accounting for each taxable activity. but it would be possible for input tax to be offset against output tax in relation to each activity except when a university disposes of capital goods…As an extension of this arrangement. it was also

agreed that universities would not have to keep any detail record on either the output or input sides in respect of their wholly exempt activities. In respect of activities where both taxable and exempt outputs arise, apportionment of input tax will be necessary. Where apportionment is made on a pro rata basis. it is normally necessary to make an annual adjustment of input tax deduction (based on annual figures for the activity). This will correct any seasonal variation in inputs and outputs which, if left unadjusted, could be unfair to the University or to the Exchequer.

In some instances – for example the sale of computer time at commercial rates – the amount of input tax recoverable may be very small. Where the amount is likely to be exceeded by the cost of keeping the necessary records, universities can, if they wish, refrain from claiming it and thereby avoid additional administrative work.

43. Recovery of Input tax on taxable accommodation, catering and bar sales.

Customs have agreed to a formula approach for recovery of input tax for three areas of taxable supplies where goods and services are used which are also required for exempt uses. For taxable supplies of accommodation and catering, you may recover as input tax 20 percent of the output tax. In respect of bars, input tax is payable on purchase of liquor, soft drinks and tobacco, and this will be fully recoverable to the extent that sales of these items will be liable to output tax. Each university will also be entitled to reclaim 5% of the total output tax charged in respect of bars as representing related deductible output tax on items such as glasses, cleaning materials and items of equipment. With this approach it will not be necessary to keep records of purchases other than for liquor etc. Any alternative approach must be agreed with your local VAT office and will normally be required to apply for at least two years."

The Guidelines changed again in 1990 but in the context of this decision, no substantive amendments were made, other than that the Grid was not attached. They were withdrawn in 1997.