

Claiming refunds for old VAT errors

A Guest Article by Alan Pearce
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There's still time to make the VAT man pay up!

Most businesses will be aware that VAT overpaid or under-claimed more than three years ago will not be refunded by Her Majesty's Revenue and Customs (HMRC). The law introducing this time restriction was implemented in December 1996 for output VAT over-paid on sales, and in May 1997 for input VAT under-claimed on purchases and expenditure.

However, following almost 12 years of litigation challenging the imposition of the three-year cap, a window of opportunity has now arisen.

Frantic afternoon

HMRC (then HMC&E) introduced the three-year cap without any notice period on 4 December 2006. That was a memorable afternoon, when the then Paymaster General announced that VAT repayment claims for errors made by taxpayers were to be capped from 6pm that evening.

There ensued a frantic few hours during which faxes were sent to HMRC by businesses and their advisors in an attempt to beat the 6pm deadline. Naturally, only a relatively small number of claims actually made it in time, leaving many – even those that were in the process of being negotiated with HMRC – no longer eligible under the new law.

Rights infringed

However, as a result of HMRC's all-too-swift action, the House of Lords has finally decided that this was contrary to taxpayers' rights and that the three-year restriction, albeit legal in its own right, should not have been implemented without first allowing a suitable transitional period.

New laws, introduced in the 2008 Finance Act, make claims for output VAT errors relating to periods before December 1996 and for input VAT errors before May 1997 eligible for refunds once again. In order to rectify the failure to legislate correctly, a transitional period has now been introduced where all such claims must be submitted before 31 March 2009.

Ironically, this means that any claims arising now that are more than three years but less than 12 years old remain blocked, while those over 12 years old and potential go as far back as 1973 (more than 33 years ago) are, albeit temporarily, eligible for a refund.

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Review your claims

Businesses should review whether, since 1996, they have had claims rejected or partially restricted by HMRC under the three-year capping rules, or, in fact, whether at the time they did not submit a claim believing it to be caught by the capping provisions. Some of the more common types of claim being submitted as a result of this change include:

- VAT incurred by builders on certain landscaping costs of a development site
- VAT on advisory services relating to mergers and acquisitions involving a share issue
- VAT on business mileage where employees are paid a fixed mileage rate
- VAT overpaid by cultural bodies such as museums and zoos between 1990 and 1996
- VAT overpaid by opticians for partly exempt services
- VAT on deposits paid to hotels that are forfeited as compensation for "no shows".

The list is endless and can involve a simple one-off error that was not discovered until after the introduction of the capping provision, or an ongoing incorrect accounting or liability issue that extends back to the introduction of VAT in 1973.

Problem of proof

The practical difficulty will be one of identification. How many businesses will remember a rejected claim or an instance that could have given rise to a claim that occurred more than 12 years ago? Are the same accounting personnel, professional advisors or even business owners still in situ today? Even if knowledge of an overpayment or an under-claim of VAT is identified, will the accounting records or alternative evidence be available to satisfy HMRC of your eligibility to successfully lodge a claim?

Consequently, obtaining proof of a claim and then quantifying it to the standard acceptable to HMRC can often be a lengthy and at times tortuous process.

With such difficulties, there are bound to be many refunds that will go unclaimed come 31 March 2009. Having lost the legal battle, HMRC will still be the ultimate winner in terms of the overall tax to be refunded!

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Cap to increase

There is a final and ironic twist to this long-running saga. After a 12-year legal battle, in which it fought tooth and nail to defend its introduction of the three year cap, HMRC has announced that the cap is to increase to four years! This is part of the harmonisation with the directive due to take effect in 2009/10.

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If you would like more information on any of the points covered in this Guest Article, please contact **TCii** on **020 7099 2621**.