

The Three-Year Cap on Claims for Input VAT

Fleming (trading as Bodycraft) v HMRC

Background

The Court of Appeal has given its decision in an important case regarding the 3 year capping provisions on VAT reclaims. The appellant (Flemming) was a dealer in specialist cars. He had purchased 13 cars during the course of 1989 and 1990 for business use. In November 1993, Mr Fleming submitted a voluntary disclosure in respect of input tax on ten of the cars and this claim was paid on April 1994. On 23 October 2000 Mr Fleming made a claim for repayment of the input tax paid on the remaining three cars. Customs (now HM Revenue & Customs – HMRC) refused the claim for the input tax on the basis that the claim was made after 1 May 1997 and related to VAT incurred more than three years earlier and was therefore time barred under Regulation 29(1A) of the VAT Regulations 1995. Mr Fleming complained that his rights had been curtailed with no transitional period.

The judgment

The CoA found that the real issues of this case were whether EU VAT law would recognise or imply (or both) a national transitional period (that is, one not specifically set out in legislation) and, if so, by reference to what event that period should be fixed.

The CoA held that a transitional period could not be read into regulation 29(1A). Regulation 29(1A) was incompatible with the principle of effectiveness and fell foul of the ECJ decision in Marks & Spencer which stated at paragraph 38 that ‘transitional arrangements allowing an adequate period after the enactment of legislation for lodging claims for repayment’ were required. The regulation should therefore be disapplied.

Ward LJ also ruled that a transitional period could not be read into Regulation 29(1A) on the basis that one can not construe something out of nothing. He further ruled that Regulation 29(1A) should be disapplied as it failed the Marks & Spencer test.

Why is this important?

This is a major defeat for HMRC's capping provisions. Generally the English courts and VAT Tribunal have supported HMRC in capping cases, and only the Scottish Tribunal has to date raised a voice in protest. The judgment is extremely interesting, with a unanimous rejection of HMRC's case but for different reasons. One judge (Arden LJ) tried to read a transitional period into Regulation 29 - she seemed to suggest that this would start on 11 July 2002 (the date the ECJ decided Marks & Spencer) and end six months later. This was a leap too far for the other two judges, who could not stretch the provisions that far and who concluded that as there was no transitional period in the Regulation, the Regulation 29(1A) cap was disapplied. On the face of it that might

suggest that there is now no cap for late input tax claims at all, until HMRC change the law and make it compliant with EU principles!

In the author's view, however, this argument is unsustainable as the Marks & Spencer case confirms that Member States have the power to introduce a cap and may retrospectively shorten the time to make a claim provided that pre-existing rights are protected by an adequate transitional period. That is to say, it is the protection of existing rights that EU law requires. Curtailing future rights that only arise after the time limit comes in is not a problem.

What now?

The decision in Fleming confirms that any input tax claim where the right to claim arose before 1 May 1997 should not be capped. If Arden LJ is right this VAT should have been claimed by 11 January 2003 in order to benefit from this. However, if the majority decision is right, this VAT can be claimed now. The date the error was discovered should not affect this. The same principles should also apply to output tax overpaid by repayment traders as such claims are also covered by the secondary capping legislation. On the basis of the majority reasoning, since no legislative transitional provision was introduced for the s80 VATA 1994 primary cap either, it is also arguable that the time limits in s80(4) are ineffective for all claims for overpaid output tax by payment traders prior to 4 December 1996.

Action point

Clearly we do not know how HMRC will react to this defeat and whether they will pursue leave to appeal. However this is an opportune time to revisit old claims. The arguments are complex (as can be seen by the fact that the three judges, although reaching the same end conclusion, did not all take the same route to get there) and we recommend that anyone affected by this decision contacts 4 Eyes Ltd to help to maximise their chances of releasing a blocked claim.