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Legislative Comment

Finance Act 2014 notes: section 299: removal of limitation period restriction for EU cases

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Legislation: Finance Act 2014 (c.26) s.299
Finance Act 2007 (c.11) s.107
Finance Act 2004 (c.12) s.320
Cases: Deutsche Morgan Grenfell Group Plc v Inland Revenue Commissioners [2003] EWHC 1779 (Ch); [2003] 4 All E.R. 645 (Ch D)
Test Claimants in the FII Group Litigation v Revenue and Customs Commissioners [2012] UKSC 19; [2012] 2 A.C. 337 (SC)

There is quite a lot of historical background to this change. The best starting point is probably July 18, 2003 when Park J issued his judgment at first instance in *Deutsche Morgan Grenfell Group plc v HMRC* (the *DMG* case).[1] That case was the first confirmation that a claim for repayment of tax wrongly paid under a mistake of law could be made by the taxpayer under the extended limitation period in section 32(1)(c) of the Limitation Act 1980. That paragraph provides that, in the case of an action based upon a mistake, the limitation period does not begin to run until the mistake is discovered. Where tax has been levied contrary to EU law, the mistake is not generally discovered until the Court of Justice of the European Union (CJEU) gives a ruling that confirms that the tax is unlawful. This gave rise to a much extended limitation period for claims for repayment of tax based upon judgments of the CJEU.

The UK Government's response to Park J's judgment was to announce on September 8, 2003 that retrospective legislation would be introduced preventing the application of the extended time limit to claims for repayment of any taxes under the management of the Commissioners of Inland Revenue. That provision was eventually enacted as section 320 of the Finance Act 2004 (FA 2004), and took effect generally from September 8, 2003. Thus, claims brought after that date were no longer eligible for the extended time limit. The change applied with effect from that earlier date; there was no lead-in time during which claims might be brought in accordance with the prior law (a factor that we will come back to).[2]

The *DMG* case went on appeal eventually to the House of Lords which confirmed the availability of the extended time limit on October 25, 2006. Shortly thereafter, on December 6, 2006, the UK Government announced the introduction of further retrospective legislation. That legislation was eventually enacted as section 107 of the Finance Act 2007 (FA 2007), and it provided that the exclusion of the extended limitation period would apply not just to actions brought after September 8, 2003, but to any action brought before that date as well (with the exception, in effect, of the *DMG* case itself). The effect of section 107 FA 2007 was, therefore retrospectively to take away the right of action for claims that had already been brought under the extended time limit.

At the time that section 107 FA 2007 was enacted, the Finance Act Notes in this Review raised—with tremendous prescience—the issue whether the section was compatible with EU law. Monica Chowdry, writing the Finance Act Note, raised the issue of whether the retrospective shortening of the time limit was contrary to the principle of effectiveness under EU law.[3]

The compatibility of both section 107 FA 2007 and section 320 FA 2004 with EU law was at issue in *Test Claimants in the Franked Investment Income Group Litigation v HMRC* (the *FII (Supreme Court)* case).[4] The Supreme Court held unanimously (seven members sitting in the hearing) that section 107 FA 2007 was incompatible with EU law as it curtailed existing claims to repayment of tax retrospectively. The Law Lords were divided, however, on whether section 320 FA 2004 was incompatible, and referred the issue to the CJEU. In *Test Claimant in the Franked Investment Income Group Litigation v Commissioners of Inland Revenue* (the *FII (3) Judgment*)[5] the CJEU held that section 320 FA 2004 was contrary to the European principles of effectiveness and legal certainty/protection of legitimate expectations in so far as it curtailed the extended limitation period retroactively and without notice. Thus, the Supreme Court found that section 107 FA 2007 was incompatible with the EU law (thus confirming Monica Bhandari's view in this Review[6]), and the CJEU confirmed that section 320 FA 2004 was also incompatible.

One comes finally, therefore, to section 299 of the current Finance Act (FA 2014), which inserts a new subsection into section 107 FA 2007 which provides as follows:

(5A)"Subsection (1) also does not have effect in relation to an action, or so much of an action as relates to a cause of action, if the consequences of a mistake of law to which the action, or cause of action, relates is the charging of tax contrary to EU Law." [7]

Thus, the exclusion of the extended time limit is itself subject to the exception that it will not apply where the claim for repayment of tax wrongfully collected is based upon the imposition of the tax being contrary to EU Law.[8] In those cases, therefore, the extended time limit will apply and the limitation period will only begin to run from the time that the mistake is discovered.

A few comments might be made on this provision.

First, the Supreme Court held that section 107 FA 2007 was incompatible with European law on May 23, 2012. Why has it taken over two years for the Government to respond to that? It is not as if there was any consultation necessary. It cannot take two years to draft precisely 51 words of additional legislation.

Secondly, given that the CJEU decided on December 12, 2013 that section 320 FA 2004 was equally incompatible, why is legislation not included in FA 2014 to remedy that incompatibility?

Thirdly, and perhaps most significant, does section 299 FA 2014 remedy the mischief? The problem with section 107 FA 2007 was that it removed the extended limitation period for all claims to recover tax wrongly imposed where those claims were brought prior to September 8, 2003. It did not matter on what basis the taxation was found to be unlawful. Section 107 FA 2007 was struck down because it conflicted with the principles of legal certainty and the protection of legitimate expectations. Not only did it conflict with EU law, it also conflicted with provisions of the European Convention on Human Rights (ECHR). That would be equally applicable whether the claim for repayment of tax was based on incompatibility with EU law, or upon some other defect in the original imposition of the tax.

As a matter of practice, it may be that the only claims that were likely to be made for repayment of tax on the basis of a mistake, and that had already been lodged prior to September 8, 2003, were based upon EU law. Suppose, however, that a taxpayer had brought an action before that date claiming repayment of tax on some other grounds—incompatibility with the ECHR, or with a tax treaty, or that the tax was wrongly imposed for some other reason—then there was an equal legitimate expectation that the action should proceed. Section 299 FA 2014 only restores the extended limitation period where the action for recovery of tax is based on a contravention of EU law. To truly remedy the position, section 107 FA 2007 should have been removed in its entirety. Section 299 FA 2014 is symptomatic of the Government's tendency to do as little as possible to comply with EU law just to the point where no one—taxpayer or Commission—might complain. That is a shabby approach from a Government that is supposed to be governing in accordance with both the letter of the law and its spirit.

Fourthly, and the final comment: as emphasised above, the Finance Act Notes published in this Review in 2007 already made it clear that the provisions of section 107 FA 2007 were of doubtful legality. If the Government had read this Review, they could have saved themselves and a lot of taxpayers a great deal of bother and quite a bit of expense wasted on fruitless litigation.

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1.*Deutsche Morgan Grenfell Group plc v HMRC [2003] EWHC 1779 (Ch); [2003] STC 1017*.

2.The history of the enactment of FA 2004 s.320 and FA 2007 s.107 is summarised in the judgment of Lord Walker in the Supreme Court in *Test Claimants in the Franked Investment Income Group Litigation v HMRC [2012] UKSC 19; [2012] STC 1362* at [103]–[110].

3.See M. Chowdry, "Limitation period in old actions for mistake of law relating to direct tax—section107" [2007] BTR 577. Monica Chowdry (now Monica Bhandari), was not the only one to query the validity of s.107 FA 2007. The writer of this note also prepared an Opinion under the instructions of the Law Society (which was supplied to members of the Finance Bill Committee in 2007 and is referred to in *Hansard, Standing Committee (2006–07), 14th Sitting, cols 508–512 (June 7, 2007)*) confirming that the legislation infringed EU law and the European Convention on Human Rights.

4.*Test Claimants in the Franked Investment Income Group Litigation v HMRC*, above fn.2, *[2012] STC 1362*.

5.*Test Claimant in the Franked Investment Income Group Litigation v Commissioners of Inland Revenue (C-362/12) [2014] STC 638 (European Court of Justice); [2014] 2 CMLR.33*.

6.Bhandari nee Chowdry, above fn.3.

7.FA 2014 s.299(1).

8.The Finance Bill defined "contrary to EU Law" as being contrary to the fundamental freedoms. During the passage of FA 2014 this definition was removed, presumably to make it clear that a claim on the basis that the tax was contrary to any element of the EU law would suffice.