



Neutral Citation Number: [2010] EWCA Civ 313

Case No: A3/2009/1281

IN THE HIGH COURT OF JUSTICE
COURT OF APPEAL (CIVIL DIVISION)
ON APPEAL FROM THE HIGH COURT CHANCERY DIVISION
VAT INTEREST CARS GROUP LITIGATION
THE HONOURABLE MR JUSTICE HENDERSON
LOWER COURT NO: HC07C00681/HC08C00662

Royal Courts of Justice
Strand, London, WC2A 2LL

Date: 25/03/2010

Before :

LORD JUSTICE MUMMERY
LORD JUSTICE EHERTON
and
LORD JUSTICE PATTEN

Between :

(1) F.J. CHALKE LIMITED **Appellants**
(2) A.C. BARNES (WOKINGHAM) LIMITED
- and -
THE COMMISSIONERS FOR HER MAJESTY'S REVENUE **Respondents**
& CUSTOMS

Mr Michael Conlon Q.C. and Mr David Scorey (instructed by McGrigors LLP) for the Appellant
Mr Jonathan Swift and Mr Peter Mantle and Mr Philip Woolfe (instructed by HMRC Solicitor's
Office) for the Respondents

Hearing dates : 13, 14, 15 January 2010

Approved Judgment

Lord Justice Etherton :

Introduction

1. This is an appeal from the judgment of Henderson J handed down on 8 May 2009. It is one of a steadily growing number of cases in which the courts of this jurisdiction are working out the legal and practical consequences of decisions of the Court of Justice of the European Communities (“the ECJ”) in which it has been found that domestic tax legislation has infringed or the United Kingdom has failed properly to implement Community law. The present case concerns payments of value added tax (“VAT”) exacted in breach of Community law from motor vehicle dealers. The Commissioners for HM Revenue and Customs or their predecessors, the Commissioners of Customs and Excise (together “the Commissioners”), have repaid the principal amount of the overpayments and simple interest. What is in issue in these proceedings is whether the claimants are entitled to compound interest, rather than just simple interest, on the overpayments, as a matter of principle and in the light of the lapse of time and the expenditure by the Commissioners of the overpaid amounts.
2. The claimants, FJ Chalke Limited (“Chalke”) and A.C. Barnes (Wokingham) Limited (“Barnes”), carried on business as motor vehicle dealers at the time of the relevant VAT overpayments. Those overpayments arose in respect of the Commissioners’ treatment of two matters. The first was so-called manufacturers’ bonuses, typically paid by a car manufacturer to a dealer who purchased a demonstrator vehicle, or paid to a dealer in the form of a rebate when certain volumes of sale were achieved. The second was onward sales of demonstrator vehicles, typically after their use by the dealer for between six months and a year for demonstration purposes and the provision to customers of test drives.
3. The proceedings are conducted under a Group Litigation Order (“GLO”) made in respect of what is called the VAT Interest Cars Group Litigation, known for short as the “VIC Group Litigation”. There are approximately 165 claimants subject to the VIC GLO. The maximum amount of a sub-group of 130 of the claims, if the claimants were to succeed on all points, has been calculated to be in the region of £136.5 million.
4. The background is set out comprehensively in the judgment of Henderson J which, like other judgments he has delivered in the line of cases to which I referred at the outset of this judgment, is marked by outstanding care and clarity of analysis and expression. In view of the fact that several of his findings are not challenged on this appeal, it is possible to state relatively briefly the factual and legal background to this appeal.

The VAT history

5. Henderson J summarised the relevant VAT history as follows.
 - “12. VAT was first introduced in the United Kingdom with effect from 1 April 1973 by the Finance Act 1972, in fulfilment of one of the conditions of the UK’s accession to the European Communities. In the most

basic terms, VAT is charged on the supply of goods and services by reference to the value of the supply. The tax is underpinned by the principle of fiscal neutrality, the object of which is to ensure that the burden of the tax is borne only by the final consumer. At all earlier stages in the chain of supply, a trader is in principle entitled to deduct from the output tax which he charges on his turnover (i.e. the supplies which he makes to his customers) the input tax which he has incurred on the purchase of his raw materials and other goods and services for the purposes of his business. In this way the burden of the tax is passed on up the chain to the ultimate consumer, and the amount of output tax due at each stage increases in line with the value which has been added to the supply.

13. One problem which a tax of this nature has to address is how to deal with supplies of goods which have, or may have, a mixed business and private use. Company cars supplied to employees are an obvious example. Less obviously, demonstrator cars purchased by a dealer may also in many cases be used by authorised members of staff for private purposes when they are not in use for demonstration purposes. For example, the car may be used as a runabout for shopping, or for collecting children from school, or for travel to and from an employee's home outside business hours.
14. In common with a number of other member states, the UK decided from the earliest days of VAT to tax the private use of business cars by the draconian expedient of blocking the deduction or recovery of input tax on the purchase of the car. In other words, as one of the Commissioners' witnesses, Mr David Easton, explains in paragraph 6 of his witness statement:

"If the business is blocked from recovering input tax on its purchase of the car, the car will effectively be subject to VAT in the hands of the business, as if it were a final consumer. The private use of that car, whilst it is in the possession of the business will then be subject to tax, without the need for a complicated or burdensome system of accounting for the private use of the vehicle by employees."
15. This solution had the effect of treating all demonstrator cars as if they had been purchased for exclusively private use, regardless of the extent (if at all) to which they were in fact so used. It is important to note, however, that the blocking of input tax in this way has

at all times been permitted under Community law, and this remains the position today. Article 11(4) of the Second Council Directive of 11 April 1967 relating to turnover taxes (67/228/ECC) ("the Second Directive") provided that:

"Certain goods and services may be excluded from the deduction system [*i.e. the system of deduction of input tax*], in particular those capable of being exclusively or partially used for the private needs of the taxable person or of his staff."

16. Article 17(6) of the Sixth Directive then provided as follows:

"Before a period of four years at the latest has elapsed from the date of entry into force of this Directive, the Council, acting unanimously on a proposal from the Commission, shall decide what expenditure shall not be eligible for a deduction of Value Added Tax. Value Added Tax shall in no circumstances be deductible on expenditure which is not strictly business expenditure, such as that on luxuries, amusements or entertainment.

Until the above rules come into force, Member States may retain all the exclusions provided for under their national laws when this Directive comes into force."

The four year transitional period envisaged by Article 17(6) elapsed without any rules having been introduced by the Council, and the question therefore arose whether it was open to the UK to maintain the prohibition on the recovery of input tax on the purchase of motor cars which had been provided for in a succession of statutory instruments. If so, further questions arose whether the prohibition could be maintained if the cars were in fact used exclusively for business purposes, or in various circumstances of mixed business and private use. On a reference for a preliminary ruling from the Court of Appeal, the ECJ answered these questions in favour of the Commissioners, holding that the expiry of the transitional period did not preclude member states from maintaining an input tax block on the purchase of motor cars, and that they could do so even where the cars "were essential tools in the business of the taxable person concerned": see Case C-305/97 *Royscot*

Leasing Limited and others v Customs and Excise Commissioners [2000] 1 WLR 1151, [1999] STC 998, especially at paragraphs 26 and 28 to 32 of the judgment of the court.

17. Despite the block on input tax for demonstrator cars, to a private purchaser output tax should still be charged, although only on the difference, or "margin", between the purchase price and the sale price. This system was generally known as "the margin scheme", and is described as follows by Mr Easton in paragraph 6 of his statement:

"However, in the case of a car dealer, selling a demonstrator, the car will normally be sold on relatively quickly in the course of business to a customer at (usually) a higher price than the dealer bought it for. Since the dealer has already borne VAT on the amount of the purchase price he had to pay, the Commissioners took the view that it would not be appropriate for the sale by the dealer to carry VAT on the full amount of the sale price. Rather, United Kingdom law required the dealer only to account for VAT on the "margin" between his purchase price and the sale price."

Before the decision of the ECJ in the *Italian Republic* case (see below), the block on input tax recovery on cars and the operation of the margin scheme were both contained in the Value Added Tax (Input Tax) Order 1992, SI 1992/3222.

18. According to Mr Easton, the policy view held by the Input Tax Branch of the Commissioners was that the combination of the block on input tax and the margin scheme represented "a pragmatic way of implementing the principle that VAT is a tax on the final consumption of goods", and was compatible with Article 13B of the Sixth Directive. Article 13 dealt with exemptions within the territory of a member state, and so far as material Article 13B provided as follows:

"Without prejudice to other Community provisions, Member States shall exempt the following under conditions which they shall lay down for the purpose of ensuring the correct and straightforward application of the exemption and of preventing any possible evasion, avoidance or abuse:

...

(c) supplies ... of goods on the acquisition or production of which, by virtue of Article 17(6), value added tax did not become deductible;"

19. This view was, however, shown to be untenable by the decision of the ECJ on 25 June 1997 in Case C-45/95 *EC Commission v Italian Republic* [1997] STC 1062 ("*Italian Republic*"). In that case the Commission brought infraction proceedings against Italy under Article 169 of the EC Treaty, alleging that Italy had failed to fulfil its obligations under Article 13B of the Sixth Directive. In upholding the Commission's complaint, the ECJ held (para 16) that the final part of Article 13B(c) requires member states to exempt the supply of goods in respect of which, by virtue of Article 17(6), VAT did not become deductible when they were previously acquired or produced by the taxable person, and (para 19) that Article 13B(c) does not allow member states to treat a transaction which is to be exempted as one which falls wholly outside the scope of VAT. It clearly follows from this reasoning that the United Kingdom should at all material times have treated sales of demonstrator cars as exempt supplies in respect of which no output tax could be charged, and that the margin scheme was therefore unlawful. The implications of the decision were soon realised, and on 10 October 1997 the Commissioners published Business Brief 23/97 in which they explained that, while consideration was given to what changes to UK legislation might be necessary, businesses could choose either to continue to use the margin scheme or to rely upon the ECJ judgment and treat the sale of input tax blocked cars as being exempt. The business brief went on to say that the Commissioners would accept claims for refunds of tax that had been overpaid as a result of the UK applying a margin scheme as opposed to an exemption, but that such refunds would be subject to the three year cap which was by then in force.
20. Mr Easton goes on to explain how consideration was then given to the question of how best to tax the private use of demonstrator cars and (more generally) the private use of vehicles by employees. Following consultation with motor industry trade bodies, proposals for new legislation relating to the VAT treatment of cars were published in April 1999, and new regulations were then introduced with effect from 1 March 2000, by the Value Added Tax (Supplies of Goods where Input Tax

cannot be recovered) Order 1999, SI 1999 No. 2833. The general effect of these regulations was to remove the input tax block and to require private use to be accounted for by means of a notional self-supply. The margin scheme was abolished with effect from the same date.

21. I now turn to the treatment of manufacturers' bonuses. Before the judgment of the ECJ in the *Elida Gibbs* case (see below), the Commissioners took the view that, as a matter of law, bonuses paid by car manufacturers to dealers on demonstrator vehicles, or to dealers or other customers on bulk orders, were to be treated as payments for a supply of services by the dealer or customer to the manufacturer. The normal practice seems to have been that the dealer would invoice the manufacturer for a supply of services including VAT, or alternatively the manufacturer would raise a self-bill invoice for the supply of services including VAT. Either way, the manufacturer would be entitled to deduct input tax on the supposed supply of services, but the dealer would of course have to account to the Commissioners for the output tax. With the benefit of hindsight, it can be seen that there were at least two difficulties with this treatment. First, the nature of the supposed services supplied by the dealer to the manufacturer in return for the bonus was elusive, and in many cases appears to have been an artificial construct invented to account for the fact that money was passing between two persons in a business relationship. Secondly, if it was right to regard the bonus as a discount from the price of the supply by the manufacturer, the principle of fiscal neutrality would appear to require that the taxable consideration for the original supply should be reduced by the amount of the discount.
22. On a preliminary reference by the VAT and Duties Tribunal in London, the ECJ held in Case C-317/94 *Elida Gibbs Limited v Customs and Excise Commissioners* [1997] QB 499, [1996] STC 1387 ("*Elida Gibbs*"), that retrospective discounts given by a manufacturer of toiletries under two coupon schemes (the first of which offered consumers a price reduction at the point of sale on the production of money-off coupons circulated in magazines or newspapers, and the second of which allowed the consumer to obtain a cash refund from the company by returning cash-back coupons which were printed on the label of the products) were indeed to be treated as reducing the taxable price at which the manufacturer had sold the

goods in the first place. The reasoning of the ECJ appears sufficiently from the following paragraphs in the judgment:

"28. In circumstances such as those in the main proceedings, the manufacturer, who has refunded the value of the money-off coupon to the retailer or the value of the cash-back coupon to the final consumer, receives, on completion of the transaction, a sum corresponding to the sale price paid by the wholesalers or retailers for his goods, less the value of those coupons. It would not therefore be in conformity with the [*Sixth Directive*] for the taxable amount used to calculate the VAT chargeable to the manufacturer, as a taxable person, to exceed the sum finally received by him. Were that the case, the principle of neutrality of VAT vis-à-vis taxable persons, of whom the manufacturer is one, would not be complied with.

29. Consequently, the taxable amount attributable to the manufacturer as a taxable person must be the amount corresponding to the price at which he sold the goods to the wholesalers or retailers, less the value of those coupons.

30. That interpretation is borne out by article 11C(1) of the Sixth Directive which, in order to ensure the neutrality of the taxable person's position, provides that, in the case of cancellation, refusal or total or partial non-payment, or where the price is reduced after the supply takes place, the taxable amount is to be reduced accordingly under conditions to be determined by the member states."

23. ...

24. The implications of *Elida Gibbs* in the context of bonuses given by car manufacturers understandably took some time to consider, but on 21 July 1997 the Commissioners issued business brief 16/97 accepting that such bonuses should normally be treated as discounts by the manufacturers which reduced the value of their supplies. Businesses which believed that they had as a result overpaid VAT in the past three years were invited to contact their local VAT business advice centre.

25. The result of the decisions of the ECJ in *Italian Republic* and *Elida Gibbs* was that dealerships with demonstrator cars were likely to have overpaid VAT both (a) in respect of manufacturers' bonus payments which they had received, whether for the purchase of demonstrator cars or the achievement of specified sales volumes, and (b) in respect of the onward sale of demonstrator cars, when the margin scheme operated. It is not disputed by the Commissioners that the overpaid VAT was unlawfully levied, at any rate with effect from 1 January 1978, and that the claimants were entitled to have it repaid in full once the unlawfulness under Community law of the three year cap had been established in *Marks & Spencer I*.”
6. The domestic legislation relating to overpaid VAT was consolidated in section 80 of the Value Added Tax Act 1994 (“VATA 1994”). At all material times, until amended in 1997 as mentioned below, it provided as follows.

"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.

(2) The Commissioners shall only be liable to repay an amount under this section on a claim being made for the purpose.

(3) It shall be a defence, in relation to a claim under this section, that repayment of an amount would unjustly enrich the claimant.

(4) No amount may be claimed under this section after the expiry of 6 years from the date on which it was paid, except where subsection (5) below applies.

(5) Where an amount has been paid to the Commissioners by reason of a mistake, a claim for the repayment of the amount under this section may be made at any time before the expiry of 6 years from the date on which the claimant discovered the mistake or could with reasonable diligence have discovered it.

(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.

(7) Except as provided by this section, the Commissioners shall not be liable to repay an amount paid to them by way of VAT by virtue of the fact that it was not VAT due to them."

7. Legislative provision concerning interest on overpayments of VAT was consolidated in section 78 of VATA 1994, which so far as relevant is as follows:

"78. Interest in certain cases of official error

(1) Where, due to an error on the part of the Commissioners, a person has –

(a) accounted to them for an amount by way of output tax which was not output tax due from him and which they are in consequence liable to repay to him, or

(b) failed to claim credit under section 25 for an amount for which he was entitled so to claim credit and which they are in consequence liable to pay to him, or

(c) (otherwise than in a case falling within paragraph (a) or (b) above) paid to them by way of VAT an amount that was not VAT due and which they are in consequence liable to repay to him, or

(d) suffered delay in receiving payment of an amount due to him from them in connection with VAT,

then, if and to the extent that they would not be liable to do so apart from this section, they shall pay interest to him on that amount for the applicable period, but subject to the following provisions of this section.

...

(3) Interest under this section shall be payable at such rates as may from time to time be prescribed by order made by the Treasury; ...

...

(10) The Commissioners shall only be liable to pay interest under this section on a claim made in writing for that purpose.

(11) No claim shall be made under this section after the expiry of 6 years from the date on which the claimant discovered the error or could with reasonable diligence have discovered it.

... "

8. Rates of interest were set by statutory instrument for VAT back to 1 April 1973, ranging from a low of 8% at the beginning to a high of 15% in the calendar year 1980 and during the period from 1 December 1981 to 28 February 1982.

9. Both section 80 and section 78 of VATA 1994 were amended by the Finance Act 1997 so as to replace the six year limitation periods set out above with a three year cap. A new subsection (4) was inserted in section 80 in the following terms:

"(4) The Commissioners shall not be liable, on a claim made under this section, to repay any amount paid to them more than three years before the making of the claim."

In section 78, subsection (11) was replaced with the following:

"(11) A claim under this section shall not be made more than three years after the end of the applicable period to which it relates."

10. Various other relatively minor amendments were made to the two sections in 1996 and 1997, but for present purposes nothing turns on them
11. On 11 July 2002 the ECJ held in Case C-62/00 *Marks & Spencer v Customs and Excise Commissioners* [2002] ECR I-6325, [2003] QB 866 ("*Marks & Spencer*") that the three year cap was unlawful.

Factual history of the claims

12. On 26 July 1999 Chalke submitted a claim to the Commissioners for overpayment of VAT in relation to the sale of demonstrator vehicles during the period of three years from 1 May 1996 to 30 April 1999. The amount of the claim was £12,974.30. This was a "capped" claim because the three year cap was still in force.
13. On 9 August 1999 the Commissioners paid Chalke's capped claim relating to the demonstrator vehicles in full, and on 16 September 1999 they paid simple interest on that sum of £694.20.
14. On 27 September 1999 Chalke submitted a capped claim for the same three year period relating to manufacturers' bonus payments in the amount of £18,685.98. That claim was paid in full on 12 October 1999. Simple interest of £1,487.39 was paid on that sum on 20 October 1999.
15. Following the ECJ's judgment in *Marks & Spencer* and the issue by the Commissioners of Business Brief 22/2 introducing a retrospective transitional regime in response to that judgment, Chalke and Barnes submitted uncapped claims in relation to both manufacturers' bonus payments and the sale of demonstrator cars going back to 1973. Chalke submitted its uncapped claim on 13 June 2003. Barnes submitted a similar claim on 28 June 2003.
16. On 12 May 2004 the Commissioners duly paid Barnes £101,866.03 in relation to its uncapped claim, and on 25 July 2004 they paid simple interest on that sum amounting to £121,691.38. The Commissioners paid Chalke the principal sum of £146,526 on 16 August 2004 and simple interest of £127,545.93 on 24 August 2004. At that point, Chalke and Barnes had been repaid all of the tax which they had overpaid, going back to 1973, together with simple interest pursuant to section 78 of VATA 1994.

17. The Court of Appeal handed down its judgment in *Sempre Metals Ltd v IRC* [2005] EWCA Civ 389, [2006] QB 37 (“*Sempre*”) on 12 April 2005, upholding the decision of Park J ([2004] EWHC 2387 (Ch), [2004] STC 1178) that Community law required the national court to provide a remedy by way of compound interest for the premature payment of corporation tax (in the form of Advance Corporation Tax (“ACT”)) exacted in breach of Community law. The first hearings in *Sempre* in the House of Lords were on 1 and 2 November 2006. On 18 July 2007 judgment was given by the House of Lords dismissing the appeal. They decided unanimously that an English Court has jurisdiction to award compound interest where a claimant seeks restitution for money paid under a mistake. On the facts of that case, the majority decided that compound interest should be paid by reference to the rates of interest and other terms applicable to borrowing by the Government in the market during the relevant period.
18. Chalke issued its claim form in the Chancery Division on 16 March 2007. On 7 March 2008 Chalke served amended particulars of claim, and Barnes issued its claim form and particulars of claim. They were settled by the same team of counsel, and are in substantially similar terms. They claim that Community law requires the principal sums to be repaid with interest at a commercial rate and on a compound basis by virtue of the Community law principles of effectiveness and equivalence; and that the payment of interest at a rate lower than the commercial rate and on a simple basis was in breach of their directly effective Community law rights. Their claims were advanced both as a restitutionary claim (“the restitutionary claim”), and as a claim for in damages for breach of Community law (“the damages claim”).
19. Henderson J summarised as follows the pleaded basis for the two claims. He did so by reference to Chalke’s amended particulars, but on the basis that the pleaded particulars for Barnes were in substantially similar terms.
 - “42. The restitutionary claim proceeds by the following stages. First, by enacting and maintaining legislation which imposed VAT on manufacturers’ bonus payments and which did not exempt from VAT the onward sales of demonstrator cars on the purchase of which input tax recovery had been blocked, the UK acted in breach of the directly effective Community law rights of Chalke, as articulated by the ECJ in *Elida Gibbs* and *Italian Republic*.
 43. Secondly, it is alleged that Chalke laboured under three mistaken beliefs:
 - (a) the belief that it was liable to account for the principal sums as output tax, which continued until the judgments of the ECJ in *Elida Gibbs* and *Italian Republic*;
 - (b) the mistaken belief, which continued until Chalke made the uncapped claim, that its claim for the principal sums was limited by the retrospective three-year limitation period; and

(c) the mistaken belief, which continued until the making of the current claim, that its claim for a remedy was limited to the return of the principal sums with simple interest only.

It will be convenient to refer to these three alleged mistakes, although they are not definitions employed by Chalke in the particulars of claim, as "the liability mistake", "the time limit mistake" and "the simple interest mistake" respectively.

44. Thirdly, as from the date of the overpayments Chalke has been deprived of the use of the principal sums, and the Commissioners have had the benefit and use of the principal sums, and have thereby been unjustly enriched.
45. Fourthly, the Commissioners have repaid the principal sums together with simple interest thereon, but they continue to be unjustly enriched to the extent that they have failed to account for the full benefits obtained by them from the use of the principal sums.
46. Restitution is then claimed of the benefits obtained by the Commissioners in the form of compound interest at a rate calculated by reference to the average cost of Government borrowing during the relevant periods going back to 1973, or alternatively to the introduction of the Sixth Directive in 1978. Calculations of the interest so claimed are set out in an annexe to the particulars, using a rate of 1% above the Bank of England's base rate and compounding the interest with daily, or alternatively quarterly, rests. The maximum value of the claim down to the end of January 2008, with daily rests and after deducting the simple interest already paid, is £229,513.46. With quarterly rests, the amount claimed is some £9,000 less, namely £220,533.27. If interest is payable only from January 1978 onwards, the corresponding figures are £197,829.70 and £190,189.77.
47. Paragraph 30 then anticipates the Commissioners' limitation defence by advancing two contentions. First, by virtue of section 32(1)(c) of the Limitation Act 1980, the six year limitation period began to run when Chalke discovered its simple interest mistake. This mistake could not have been discovered with reasonable diligence until the House of Lords had given judgment in *Sempra*. Secondly, in respect of the interest due on the uncapped claim, the payment of the principal amount of that claim on 16 August 2004 (or

alternatively the issue of business brief 22/02 on 5 August 2002) is to be treated as an acknowledgment for the purposes of section 29(5) of the Limitation Act 1980, with the consequence that the six year limitation period began to run afresh on those dates.

48. The damages claim alleges the following breaches of Community law by the Commissioners:

(a) the enactment and maintenance in force of the offending VAT legislation relating to manufacturers' bonus payments and the sale of demonstrator cars;

(b) the enactment and maintenance in force of the three year cap, with no transitional period in respect of rights which had accrued prior to 18 July 1996;

(c) the failure to pay compound interest on the overpaid VAT, in breach of the principles of effectiveness and/or equivalence; and

(d) the enactment and maintenance in force of the statutory bar to the payment of compound interest in section 78(3) of VATA 1994.

49. It is then pleaded that the three *Factortame* conditions for liability in damages by a member state are satisfied, and that Chalke has thereby suffered loss and damage in the form of "the loss of the value of money over time" (paragraph 35). A computation of the compound interest claimed is set out in a second annexe, which is in materially identical terms to the first annexe save that the rate of interest claimed is now 3% above base rate, no doubt intended to reflect the commercial borrowing rates which would have been available to Chalke had it borrowed money to replace the overpaid amounts of VAT. The maximum amount of the claim on this basis, going back to 1973 and compounding with daily rests, is £483,898.57. With quarterly rests, the corresponding figure is £462,477.19.

50. Finally, the same limitation points are made as in respect of the restitution claim (paragraph 36)."

20. The Commissioners admitted, in their defences, that from 1 January 1978 until the publication of the relevant business briefs in 1997 the Commissioners' treatment of manufacturers' bonus payments was contrary to Article 11 of the Sixth Directive, as interpreted by the ECJ in *Elida Gibbs*; and that their treatment of demonstrator cars was contrary to Article 13B(c) of the Sixth Directive, as interpreted by the ECJ in

Italian Republic; and that the relevant provisions of Article 11 and Article 13 conferred directly effective rights on Chalke and Barnes. Subject to those admissions, the Commissioners denied the claims for compound interest on a variety of grounds.

The hearing before Henderson J and his decision

21. The following issues were addressed in the hearing before Henderson J, and were decided by him as follows.
- i) The Commissioners submitted that the right to repayment of wrongly paid VAT in section 80 of VATA 1994 was intended by Parliament to be both exhaustive and exclusive of other possible remedies. The claimants did not dispute that contention insofar as it related to the recovery of VAT itself, but did not accept that their claims for compound interest at common law were ousted by the statutory scheme. The Judge rejected the claimants' qualification. He held that, as a matter of domestic law, the statutory scheme for the recovery of overpaid VAT in section 80 of VATA 1994 is an exhaustive one, and that interest may only be recovered on a repayment of overpaid VAT by the Commissioners if it is awarded by the VAT and Duties Tribunal pursuant to its statutory power to do so or pursuant to section 78 of VATA 1994.
 - ii) The claimants submitted that the Community law principles of effectiveness and equivalence require overpaid VAT, exacted in breach of Community law, to be repaid with compound interest. The Judge agreed that the Community law principle of effectiveness overrides the otherwise exhaustive and exclusive statutory scheme for the payment of interest on overpaid VAT, where the overpayment arose from breach of directly effective provisions of Community law. He held that, subject to the Commissioners' other defences, the claimants were entitled to compound interest on the tax they overpaid, at any rate from 1 January 1978 when the Sixth Directive came into effect, since only in that way could effect be given to the underlying principle that the United Kingdom should not be permitted to profit from the overpaid tax. He decided that the requirement that compound interest should be paid is a requirement of Community law, but the manner in which it should be worked out is a matter for national law. He held that it should therefore be calculated on the basis laid down by the majority of the House of Lords in *Sempra*, namely by reference to the rates of interest and other terms applicable to government borrowing in the market.
 - iii) Henderson J held, however, that the restitutionary claims advanced by the claimants for recovery of such interest as money paid under a mistake were time-barred. He considered that the claims were properly to be regarded, for this purpose, as simply one element which remained unsatisfied of the restitutionary claims of Barnes and Chalke arising from the overpayments. The claims fell outside the basic limitation period applicable to restitutionary claims, which was agreed to be (by analogy) the six year period under section 5 of the Limitation Act 1980 ("the 1980 Act") for actions founded on simple contract. The approximate date of the last overpayment of VAT by Barnes was September 1996, and the approximate date of the last overpayment by Chalke was April 1999. Chalke did not issue its High Court claim form until

16 March 2007, nearly 8 years after its last payment. Barnes issued its claim form on 7 March 2008, some 11 and a half years after its last payment. The claimants relied upon the extension to the basic limitation period where the action is for “relief from the consequences of a mistake” within section 32(1)(c) of the 1980 Act, which provides that the limitation period does not begin to run until the claimant has discovered the mistake or could with reasonable diligence have discovered it. The Judge found, on the facts, that Chalke was aware of both the *Italian Republic* and the *Elida Gibbs* liability mistakes by the end of June 1997 at the latest. He held that, accordingly, as a matter of English domestic law, the extended period under section 32(1)(c) of the 1980 Act for the commencement of Chalke’s restitutionary claim expired no later than the end of June 2003. Furthermore, the ordinary six year limitation period for recovery of its most recent overpayments (April 1999) also expired by around April 2005. In the case of Barnes, the Judge found that it was aware of each of the liability mistakes by June 1997, and accordingly the extended period under section 32(1)(c) also expired in its case no later than the end of June 2003. The ordinary six year period for recovery of its most recent overpayments (September 1996) expired by September 2002.

- iv) Henderson J rejected the case of Barnes and Chalke that the payment of their uncapped claims in 2004 amounted to an acknowledgment for the purposes of section 29(5) of the 1980 Act with the consequence that the six year limitation period was to be treated as having accrued on the dates of those payments. The Judge’s decision followed from his analysis that the payment by the Commissioners of each uncapped claim was a payment in respect of the claimants’ right to repayment under section 80 of VATA 1994, and could not be treated as a payment made in respect of, or which recognised or acknowledged, the non-statutory common law right to compound interest derived from Community law. The alternative pleaded case that the issue by the Commissioners of Business Brief 22/02 on 5 August 2002 amounted to an acknowledgment within section 29(5) was not pressed in oral argument before the Judge, and he therefore said nothing about it.
- v) It was then contended on behalf of Barnes and Chalke that the combined effect of the introduction of the three year cap and the principle of Community law that, at least for some purposes, a member state cannot rely on its own wrong was to suspend the running of time under section 32(1)(c) of the 1980 Act from the date of the introduction of the cap at least until the ECJ gave its judgment in *Marks & Spencer* on 11 July 2002. A further argument, on the basis of the same principle, was mounted on the provisions of section 121(1) of the Finance Act 2008 (“FA 2008”). That sub-section, which by virtue of subsection (4) was treated as having come into force on 19 March 2008, provided that the 3 year cap in section 80(4) of VATA 1994 did not apply to a payment in respect of an accounting period ending before 4 December 1996 if a claim was made before 1 April 2009. It was submitted for Chalke and Barnes that the breach of Community law occasioned by the three year cap remained unremedied in domestic law until the enactment of FA 2008 section 121(1), and, accordingly, it was not open to the United Kingdom prior to that enactment to rely on domestic limitation defences to claims for VAT overpaid before 4 December 1996 . Henderson J rejected those arguments on the

ground that the compound interest claims which the claimants are now advancing have nothing whatever to do with the cap, and are not made under section 80 of VATA 1994, and could have been started at any time, whether or not the cap was in place. The Judge also noted that the unlawfulness of the cap under Community law in relation to accrued claims was established by the judgment of the ECJ in *Marks & Spencer* on 11 July 2002, which still left approximately one year of the extended limitation period within which the claimants could have started proceedings: the decision in *Italian Republic* having been decided on 25 July 1997, and Business Brief 16/97 dealing with the implications of *Elida Gibbs* having been issued by the Commissioners on 21 July 1997.

- vi) Henderson J then addressed a change of position defence if he was wrong in his conclusion that the restitutionary claims were time-barred. He held that change of position is unavailable as a defence to a claim for the recovery of VAT based on an individually enforceable Community law right, that is a *San Giorgio* claim (after the principle explained by the ECJ in case C-199/82 *Amministrazione delle Finanze dello Stato v San Giorgio Spa* [1983] ECR 3595 (“*San Giorgio*”). He concluded that, since the claimants’ compound interest claims come within the scope of the *San Giorgio* principle and no wider domestic restitutionary claims are advanced, the Commissioners are unable to rely on a change of position defence to the present claims.
- vii) Henderson J rejected the claimants’ alternative damages claim, partly for reasons of limitation and causation, but also because the breaches of Community law which caused the claimants’ loss were not sufficiently serious to found liability.
- viii) Finally, the Henderson J considered the question whether the claimants can maintain any claim in relation to the period before the Sixth Directive came into force on 1 January 1978. The claimants rely on Article 2 of the First Directive of 11 April 1969. The Judge did not have to resolve that point because he had already decided that the claimants’ pre-1978 claims, in common with their later claims, were time-barred. He considered that the question whether the provisions of Article 2 have direct effect is not clear, and so, had it been necessary to decide the matter, he would have referred it to the ECJ for a preliminary ruling.
- ix) The end result, accordingly, was that the Judge dismissed the claims of both Chalke and Barnes.

Grounds of appeal and Respondents’ notice

- 22. The claimants have appealed, with the permission of the Judge, the Judge’s findings which I have described above in sub-paragraphs 21(iii) (expiry of the extended limitation period in section 32(1)(c) of the 1980 Act before the proceedings were commenced), 21(iv) (no acknowledgement or part payment within section 29(5) of the 1980 Act), and 21(v) (no suspension of the limitation period by virtue of the application of the principle of Community law that a member state cannot rely on its own wrong).

23. The Commissioners have filed a Respondents' notice, in which they seek to uphold Henderson J's judgment on the following further grounds. First, the Judge should have concluded that section 29 of the 1980 Act has no application to the claimants' claims because they are not claims to recover "any debt or other liquidated pecuniary claim" within section 29(5) of the 1980 Act. Secondly, the Judge's conclusion described in paragraph 21(ii) above was wrong. He should have decided that the claimants have no entitlement under Community law to recover an amount exceeding the overpayments together with simple interest pursuant to section 78 of VATA 1994. Thirdly, the amount of any restitutionary claim in respect of the use value of money overpaid should be limited to the period for which the Government actually enjoyed the benefit of the use of that money, namely for approximately one year following the receipt of each overpayment. Fourthly, Article 2 of the First Council Directive did not confer any directly effective right on the claimants, and so they had no entitlement, as a matter of Community law, to repayment of sums overpaid before 1 January 1978 or interest on them.

The interveners

24. Permission was given for two sets of interveners to make written submissions on the appeal. Those two sets of interveners are themselves appellants in pending appeals from a test case in the Upper Tribunal. They too have paid VAT levied in breach of Community law and contend, like the claimants, that there is a Community law right to compound interest as an integral part of the right to repayment of the overpaid VAT. Unlike the claimants, however, they contend that VATA 1994 can and should be interpreted in accordance with the principle in Case C-106/89 *Marleasing SA v La Comercial International de Alimentation SA* [1990] ECR I-4135 ("*Marleasing*") to give effect to that right. Henderson J was not invited to, and did not, consider that question. Nor does it arise on this appeal. This appeal, like Henderson J's judgment, proceeds on the assumption that VATA 1994 cannot be so interpreted, without the need to form any view as to the merits of the interveners' contentions on that issue or the merits of their appeals. The permission granted to the interveners to intervene was limited to the actual issues in this appeal, and excluded issues arising only in their own appeals. In the event, it was not necessary to hear oral submissions on behalf of the interveners on any of the substantive matters raised in the grounds of appeal or the Respondents' notice.

Community law and compound interest

25. Logically, the first issue to address on the appeal is the challenge in the Respondents' notice to Henderson J's conclusion that, as a matter of Community law, the claimants are entitled in principle to compound interest on their overpayments of VAT, rather than the simple interest recoverable and already paid to them under section 78 of VATA 1994. The claimants assert that the Community law principles of effectiveness and equivalence require the tax to be repaid with compound interest.
26. The starting point of the claimants' case on this issue is the well established principle of Community law that individuals are entitled to a refund of taxes and duties levied in breach of Community law. This is the *San Giorgio* principle, which was first clearly stated as follows in paragraph 12 of the judgment of the ECJ in *San Giorgio*:

"In that connection it must be pointed out in the first place that entitlement to the repayment of charges levied by a Member State contrary to the rules of Community law is a consequence of, and adjunct to, the rights conferred on individuals by the Community provisions prohibiting charges having an effect equivalent to customs duties or, as the case may be, the discriminatory application of internal taxes. Whilst it is true that repayment may be sought only within the framework of the conditions as to both substance and form, laid down by the various national laws applicable thereto, the fact nevertheless remains, as the Court has consistently held, that those conditions may not be less favourable than those relating to similar claims regarding national charges and they may not be so framed as to render virtually impossible the exercise of rights conferred by Community law."

27. As the Judge observed, the conditions referred to at the end of that quotation are the Community law principles of equivalence and effectiveness respectively.
28. *San Giorgio* itself said nothing about the payment of interest on unlawful charges repaid by a member state. The claimants contend that the right to interest is established by a further principle of Community law that those with *San Giorgio* claims are entitled to be compensated for the loss of the use of the amounts unlawfully levied or rather they are entitled to payment for the advantage gained by the tax authorities for the value of the use of the money prior to repayment. For that principle, they rely in particular on the judgment of the ECJ in joined cases C-397/98 and 410/98 *Metallgesellschaft Limited v IRC, Hoechst AG v IRC*, [2001] ECR I-1727, [2001] Ch 620 (which the Judge called "*Hoechst*" but which I shall call "*Metallgesellschaft*" as the ECJ usually describes it and as did counsel before us) and the opinion of the Advocate General and the judgment of the ECJ in case C-446/04 *Test Claimants in the FII Group Litigation v IRC* [2006] ECR I-11753, [2007] STC 326 ("*FII*").
29. *Metallgesellschaft* concerned the failure of United Kingdom legislation, in breach of Community freedom of establishment in Article 52 of the EC Treaty, to allow a group income election to be made by a United Kingdom resident company, paying a dividend to its non-resident parent company in another member state, in circumstances where such an election could have been made on payment of a dividend to a United Kingdom resident parent. The consequence was that ACT, which is regarded by the ECJ simply as an advance payment of mainstream corporation tax ("MCT"), was paid earlier than would otherwise have been the case. The ACT was later set off against MCT, but the absence of the ability to make a group income election meant that the tax was levied too early. The ECJ held that the taxpayers had a *San Giorgio* restitutionary claim to interest on the ACT between the date of its payment and the date on which MCT became payable. The following important passages in the judgment of the ECJ were quoted by the Judge in his judgment:

"83. It is important to bear in mind in this regard that what is contrary to Community law, in the disputes in the main proceedings, is not the levying of a tax in the United Kingdom

on the payment of dividends by a subsidiary to its parent company but the fact that subsidiaries, resident in the United Kingdom, of parent companies having their seat in another Member State were required to pay that tax in advance whereas resident subsidiaries of resident parent companies were able to avoid that requirement."

[The Court then referred to the *San Giorgio* principle, and continued:]

"85. In the absence of Community rules on the restitution of national charges that have been improperly levied, it is for the domestic legal system of each Member State to designate the courts and tribunals having jurisdiction and to lay down the detailed procedural rules governing actions for safeguarding rights which individuals derive from Community law, provided, first, that such rules are not less favourable than those governing similar domestic actions (principle of equivalence) and, secondly, that they do not render practically impossible or excessively difficult the exercise of rights conferred by Community law (principle of effectiveness): [authority was then cited].

86. It is likewise for national law to settle all ancillary questions relating to the reimbursement of charges improperly levied, such as the payment of interest, including the rate of interest and the date from which it must be calculated: [reference was made to Case 26/74 *Société Roquette Frères v EC Commission* [1976] ECR 677 ("*Roquette Frères*") paras 11 and 12 and to Case 130/79 *Express Dairy Foods Limited v Intervention Board for Agricultural Produce* [1980] ECR 1887 ("*Express Dairy Foods*") paras 16 and 17].

87. In the main proceedings, however, the claim for payment of interest covering the cost of loss of the use of the sums paid by way of advance corporation tax is not ancillary, but is the very objective sought by the claimants' actions in the main proceedings. In such circumstances, where the breach of Community law arises, not from the payment of the tax itself but from its being levied prematurely, the award of interest represents the "reimbursement" of that which was improperly paid and would appear to be essential in restoring the equal treatment guaranteed by Article 52 of the Treaty.

88. The national court has said that it is in dispute whether English law provides for restitution in respect of damages arising from loss of the use of sums of money where no principal sum is due. It must be stressed that in an action for restitution the principal sum due is none other than the amount of interest which would have been generated by the sum, use of which was lost as a result of the premature levy of the tax.

89. Consequently, Article 52 of the Treaty enables a subsidiary resident in the United Kingdom and/or its parent company having its seat in another Member State to obtain interest accrued on the advance corporation tax paid by the subsidiary during the period between the payment of advance corporation tax and the date on which mainstream corporation tax became payable, and that sum may be claimed by way of restitution."

30. *FII* concerned a number of complex disputes concerning United Kingdom corporation tax under Case V of Schedule D and ACT, which were referred to the ECJ for preliminary rulings. Those disputes are described in paragraph 94 of Henderson J's judgment. For present purposes, it is sufficient to say that the claims included both overpayments of tax and premature payments of tax, which the ECJ found to be in breach of Community law. The Advocate General commented on *Metallgesellschaft*, and then said as follows at paragraph 132 of his opinion:

"132. In the present case, it seems to me that, with one exception, the claims described in the national court's sixth question should be considered equivalent to claims for recovery of sums unduly paid, that is to say, claims for recovery of charges unlawfully levied within the meaning of the Court's case law, which the UK is in principle obliged to repay. The underlying principle should be that the UK should not profit and companies (or groups of companies) which have been required to pay the unlawful charge must not suffer loss as a result of the imposition of the charge. As such, in order that the remedy provided to the test claimants should be effective in obtaining reimbursement for reparation of the financial loss which they had sustained and from which the authorities of the member state concerned had benefited, this relief should in my view extend to all direct consequences of the unlawful levying of tax. This includes to my mind: (1) repayment of unlawfully levied corporation tax ...; (2) the restoration of any relief applied against such unlawfully levied corporation tax ...; (3) the restoration of reliefs foregone in order to set off unlawfully levied corporation tax ...; (4) loss of use of money in so far as corporation tax was, due to the breach of Community law, paid earlier than it would otherwise have been In each case, it would be for the national court to satisfy itself that the relief claimed was a direct consequence of the unlawful levy charged."

31. The claimants submit, and the Judge accepted, that the Advocate General was there laying down the underlying principle as being that "the United Kingdom should not profit and companies (or groups of companies) which have been required to pay the unlawful charge must not suffer loss as a result of the imposition of the charge", and that he linked that to the requirement of effectiveness by saying that the relief should extend "to all direct consequences of the unlawful levying of tax". The claimants also claim, and the Judge accepted, that the ECJ followed the same reasoning as the Advocate General and adopted the same broad principle. This is said to appear from

paragraphs 197 to 207 and 220 of the ECJ's judgment, and, in particular, the following paragraphs.

"204. In addition, the Court held in para 96 of its judgment in [*Metallgesellschaft*], that, where a resident company or its parent have suffered a financial loss from which the authorities of a member state have benefited as the result of a payment of advance corporation tax, levied on the resident company in respect of dividends paid to its non-resident parent but which would not have been levied on a resident company which had paid dividends to a parent company which was also resident in that member state, the Treaty provisions on freedom of movement require that resident subsidiaries and their non-resident parent companies should have an effective legal remedy in order to obtain reimbursement or reparation of the loss which they have sustained.

205. It follows from that case law that, where a member state has levied charges in breach of the rules of Community law, individuals are entitled to reimbursement not only of the tax unduly levied but also of the amounts paid to that state or retained by it which relate directly to that tax. As the Court held in paras 87 and 88 of [*Metallgesellschaft*], that also includes losses constituted by the unavailability of sums of money as a result of a tax being levied prematurely.

206. In so far as the rules of national law governing the availability of tax relief have prevented a tax, such as ACT, levied in breach of Community law, from being recovered by a taxpayer who has accounted for it, the latter is entitled to repayment of that tax."

32. Henderson J referred to Case C-524/04 *Test Claimants in the Thin Cap Group Litigation v IRC* [2007] STC 906 ("*Thin Cap*") as supporting the reliance he placed on *FII*. *Thin Cap* concerned the compatibility with Community law of the United Kingdom rules on thin capitalisation, and raised questions on remedies similar to those raised in *FII*. The Judge observed that the Grand Chamber of the ECJ gave its judgment on 13 March 2007, some three months after *FII*, and that the *juge rapporteur* (Lenaerts) and the Advocate General (Geelhoed) were the same as in *FII*. The Judge considered that both the Advocate General and the ECJ followed the same general approach as in *FII*, and that he could find no indication that they sought either to modify or to develop that approach. He concluded, therefore, that *Thin Cap* confirmed that *FII* represents the current, and carefully considered, jurisprudence of the ECJ on these topics.
33. The claimants submit, and the Judge agreed, that the claim to compound interest on the overpayments of VAT was supported by the judgments of Park J, the Court of Appeal and the House of Lords in *Sempre*, in which the ECJ's judgment in *Metallgesellschaft* was implemented as a matter of domestic law. The analysis of those judgments in *Sempre* by the Judge is to be found at paragraphs 109 to 116 of his judgment. It is not necessary to quote them or to examine them in detail here. It is

sufficient to say that he observed that it was clearly the view of Park J and the Court of Appeal in *Sempra* that compound interest in respect of prematurely paid ACT was a requirement of Community law; that the House of Lords decided unanimously that an English court has jurisdiction to award compound interest where a claimant seeks restitution of money paid under a mistake; and that the House of Lords decided by a majority that the claimant's claim for restitution in respect of prematurely paid ACT, ultimately set off against MCT, ought to be measured by an award of compound interest at conventional rates calculated by reference to the rates of interest applicable to borrowing by the Government in the market during the relevant period.

34. The conclusions of Henderson J on the issue, which reflect the submissions of the claimants and on which they rely upon on this appeal, are clearly and concisely stated in paragraphs 108 and 255(2) of his judgment as follows.

“108. Certain important consequences seem to me to follow from this analysis. In the first place, if an effective remedy requires that the member state should not profit from the unlawful charge, the claimant should in principle be entitled not only to repayment of the tax itself but also to interest. Otherwise the claimant would effectively be compelled to make an interest free loan to the member state for the period between the wrongful exaction of the tax and its repayment. Secondly, no sensible distinction can be drawn in relation to interest between cases where tax is levied prematurely (as in *Hoechst*) and cases where the tax itself has to be repaid. In each case, the claimant should receive by way of "interest" a sum which represents the loss of use of the money, or (perhaps more accurately) the benefit of the use of the money to the member state, over the relevant period. If anything, common sense suggests that this right should be stronger in cases where the tax itself has to be repaid than in cases where the tax was merely levied prematurely. Thirdly, the measure of such loss of use or benefit, in the context of a restitutionary claim brought in an English court, should normally be compound, not simple, interest, as the majority of the House of Lords (upholding Park J and the Court of Appeal) recognised and held in *Sempra*: it is only by an award of compound interest that the commercial value of the use of the money over the time when it was retained can be properly reflected. Fourthly, such an award of interest can no longer be regarded as merely ancillary to the repayment of the tax, within the principle of *Roquette Frères* and *Express Dairy Foods* (restated in *Hoechst* at paragraph 86 of the judgment of the Court), because it must now be seen as an integral part of the *San Giorgio* claim for the repayment of the tax and reimbursement of all directly related benefits retained by the member state.”

“ 255 (2) ... the Community law principle of effectiveness overrides the domestic statutory scheme where (as in the present cases) the overpayment of VAT was caused by breach

of directly effective provisions of Community law. In those circumstances the *San Giorgio* principle, as it is now to be understood in the light of the judgments of the ECJ in *FII* and *Thin Cap*, requires that compound interest should be paid.”

35. Before turning to the Commissioners’ case on this issue, it is necessary to highlight one important aspect of the Judge’s analysis with which the claimants do not agree, and which is reflected in paragraph 108 of his judgment quoted above. Henderson J was of the view that the opinion of the Advocate General and, more particularly, the judgment of the ECJ in *FII* marked a significant advance in the jurisprudence of the ECJ on the issue of interest in the context of the *San Giorgio* principle. His view was that until *FII* there was a consistent line of ECJ authority that *San Giorgio* claims are for the repayment of the unlawful charges and that it is for the national law to settle all ancillary questions such as the payment of interest and the date from which it must be calculated. In that connection, he referred to *Roquette Frères* (paragraphs 11 and 12 of the ECJ’s judgment), and *Express Dairy Foods* (paragraphs 16 and 17 of the ECJ’s judgment). On the Judge’s reasoning, *Metallgesellschaft* was not out of step with that line of authority since the ECJ’s judgment in that case proceeded on the basis that the “interest” claimed was not, on a true analysis, ancillary to the payment of unlawfully levied tax, but was itself the principal sum claimed by way of reparation for the United Kingdom’s breach of Community law, that principal sum to be measured by reference to loss of use of the prematurely paid tax. Indeed, he commented (paragraph 90) that paragraph 86 of the ECJ’s judgment in *Metallgesellschaft* restated “the well-established” principle derived from *Roquette Freres* and *Express Dairy Foods* that payment of interest is an ancillary matter for national law to determine. As I have said, the Judge considered that *FII* marked the critical change in Community law. The Judge’s view of the occurrence and nature of that change in *FII* appears clearly from paragraphs 105 and 107 of his judgment.

“105. In my judgment the reasoning of the ECJ [in *FII*] in paragraphs 201 to 207 was in all essential respects the same as that of the Advocate General, and they differed from him only on the question whether a claim for reliefs which had been waived (whatever the precise significance of that rather enigmatic phrase may be) could be classified under Community law as a reimbursement claim. Subject to that relatively minor point of disagreement, it seems to me that the Court agreed with the Advocate General in identifying an underlying principle, first adumbrated in paragraph 96 of its judgment in *Hoechst*, and in linking it with the principle of effectiveness (see the reference to “an effective legal remedy” at the end of paragraph 204). The general principle, as stated in paragraph 205, is that individuals are entitled to reimbursement “not only of the tax unduly levied but also of the amounts paid to that state or retained by it which relate directly to that tax”. This may be compared with the Advocate General’s view (in paragraph 132 of his opinion) that an effective remedy should “extend to all direct consequences of the unlawful levying of tax”. The final sentence of paragraph 205 indicates that the Court, like the Advocate General, viewed the remedy fashioned

by the Court in *Hoechst* as coming within the scope of the general principle thus identified.”

“107. I have dealt at considerable length with *FII*, even at the risk of traversing again much ground which I have already covered in *FII* Chancery at paragraphs 220 to 235 and 240, because it does in my judgment represent a significant advance on *Hoechst* in the jurisprudence of the Court. The identification of an underlying general principle, the linking of it to the principle of effectiveness, and the subsuming within the general principle of the loss of use claim in *Hoechst*, are important new milestones (or perhaps I should say kilometre posts) on a journey that is still far from completed. They are sufficient, however, to make it clear, to my mind, that the *San Giorgio* principle must now be regarded as entitling a claimant who has paid tax levied in breach of Community law not only to repayment of the tax itself, but also to reimbursement of all directly related benefits retained by the member state as a consequence of the unlawful charge. It is only in this way that the claimant can obtain an effective remedy for its loss, and effect can be given to the underlying principle that the member state should not profit from the imposition of the unlawful charge.”

36. Mr Michael Conlon Q.C, for the claimants, submitted that the Judge incorrectly characterised the line of authority on interest prior to *FII*. In broad terms, he submitted that the word “ancillary” in cases such as *Roquette Frères* and *Express Dairy Foods* was not being used to mean something secondary or subordinate. Rather, having regard to the particular facts and context of those cases, the ECJ intended “ancillary” to bear the sense of something that goes hand-in-hand with and is an integral part of, for example, the right to recover overpaid tax. In Case C-271/91 *Marshall v Southampton and South West Hampshire Area Health Authority (Teaching) (No 2)* [1993] ECR1-4367, [1994] QB 126 (“*Marshall*”) the ECJ held that interest was an essential component of compensation which Community law required to be paid in the event of discriminatory dismissal from employment. Mr Conlon also cited in support of the claimants’ submissions on this aspect the following statement of Advocate General Trabucchi in *Roquette Frères* (itself quoted by Advocate General Fennelly in *Metallgesellschaft*):

“... the payment of the interest on a capital sum unduly paid is strictly dependent upon the right to repayment of the principal itself... An application for interest is subject to the same criteria as those laid down by the case-law of the Court in respect of the claim for repayment of the capital on which the interest is based. An application for interest must, therefore, be made in accordance with the same procedure as that applicable to recovery of the capital sum.”

37. That difference of approach between the claimants and the Judge on the ECJ’s jurisprudence prior to *FII* on the characterisation of “interest” as ancillary, and a matter for the domestic courts, is a helpful springboard for consideration of the

Commissioners' criticism of the Judge's conclusion on the issue of compound interest. The kernel of the criticism is that the Judge, having correctly analysed and described that jurisprudence, was wrong to interpret the ECJ's judgment in *FII* as he did and as the important milestone he thought it was.

38. In powerful submissions Mr Jonathan Swift, for the Commissioners, referred to a number of ECJ cases, in addition to *Roquette Frères* and *Express Dairy Foods*, as authority for the proposition that the *San Giorgio* principle extends only to repayment of charges levied in breach of Community law, and that it is for the national authorities to settle all ancillary questions relating to such reimbursement, including the payment of interest, by applying their own domestic rules regarding the rate of interest and the date from which interest must be calculated or indeed whether interest is recoverable at all. They included Joined Cases C-279/96, C-280/96 and C-281/96 *Ansaldo Energia Spa v Amministrazione delle Finanze dello Stato* [1998] ECR I-5025 (paras 27-30), Case C-197/03 *Commission v Italian Republic* (para 43), *Metallgesellschaft* (para 86), and Case C-66/95 *R v Secretary of State for Social Security, ex parte Sutton* [1997] ECR I-2163 [1997] ICR 961 (para 25). Mr Swift pointed out that the interest in dispute in *Marshall* was simple, and not compound, interest. The Commissioners also rely on the judgment of Lawrence Collins LJ in *Revenue and Customs Commissioners v RSPCA, Revenue and Customs Commissioners v ToTel Ltd* [2007] EWHC 422 (Ch), [2008] STC 885. Mr Swift submitted that what is apparent from the cases is that, in applying the Community law principle of effectiveness, the ECJ has always had regard to the nature of the breach, and that what is required is that the remedy matches the breach. That is, he said, the basis for the difference between the Community law requirements as to interest in the case of overpayment of tax, on the one hand, and in the case of premature levying and payment of tax, on the other hand.
39. The Commissioners submit that neither the opinion of the Advocate General nor the judgment of the ECJ in *FII* contain any new principles governing the award of interest. They criticise the Judge for placing far too much weight on two sentences in paragraph 132 of the opinion of the Advocate General and on one sentence of the ECJ in paragraph 205 of its judgment. They say that the Judge was, in any event, wrong to consider that the reasoning of the ECJ was in all essential respects the same as that of the Advocate General. They say that the ECJ was adopting a narrower test in paragraph 205 of its judgment than the Advocate General in paragraph 132 of his opinion. Indeed, that was the view of this Court in *Test Claimants in The Franked Investment Group Litigation v IRC* [2010] EWCA Civ 103 ("*FII CA*"). They point out that *FII* concerned a number of specific questions addressed to the Court, none of which concerned the issue of interest in general, and the rate of interest in particular, in respect of *San Giorgio* claims. They contend that, in paragraph 205 of its judgment in *FII*, the ECJ identified the *Metallgesellschaft* principle specifically as one relating to the premature levying of tax, and that is consistent with the categorisation of heads of relief in paragraph 132 of the opinion of the Advocate General, and was the approach of the Advocate General and the ECJ in *Metallgesellschaft* itself. Mr Swift observed that, if the Judge was correct, it was curious that the Advocate General in *Metallgesellschaft* did not include interest as a head of relief in category (1) in paragraph 132 of his opinion ("repayment of unlawfully levied corporation tax"). He submitted that there is nothing in the opinion of the Advocate General or in the judgment of the Court in *FII* which expressly demonstrates or announces a new

approach to interest in cases of overpaid tax. Mr Swift submitted that no support for the claimants' contention and the Judge's conclusion can be derived from the ECJ's judgment in *Thin Cap*, the material paragraphs of which (especially paragraph 112) merely repeat what was said by the ECJ in *FII*. He further submitted that the argument of the claimants and the decision of the Judge on this issue conflict with the established principle of Community law that a member state need not reimburse a taxpayer where this would result in the taxpayer's unjust enrichment, for example where a trader has passed on the burden of the charge to some other person: Case C-147/01 *Weber's Wine Work v Abgabenberufungskommission Wien* [2003] ECR I-11365 (Advocate General's opinion paras 45-46, ECJ's judgment para 94).

40. This issue is one of great importance carrying enormous financial consequences, not only for the United Kingdom but all member states. It is relevant to other cases pending or anticipated in the High Court and the Court of Appeal. I do not consider that the answer to the issue is clear. There is considerable cogency in the argument of the Commissioners and the analysis of the Judge that, at least until *FII*, the settled jurisprudence of the ECJ in relation to *San Giorgio* claims was that, save in the *Metallgesellschaft* case of premature levying of tax, interest was an ancillary matter to be dealt with in accordance with national law, including whether there was a right to any interest at all and, if so, the rate and the time for which it was to be paid. It is also striking, as the Commissioners have forcefully submitted, that there is no clear statement by the ECJ, whether in *FII* or any subsequent case, that the former settled jurisprudence has been changed by the formulation of the *San Giorgio* principle in paragraph 205 of the ECJ's judgment in *FII*, and that, in cases of overpayment as much as cases of premature payment, the *San Giorgio* principle requires the recipient to pay compensation for the time value of the wrongful retention of tax when it was not lawfully due. On the other hand, it is clear, as the Judge found and as the claimants contend, that the formulation of the *San Giorgio* principle in paragraph 205 of *FII* is, on one interpretation, broad enough to encompass the claimants' claims to payment for the time value of the overpayments of VAT while retained by the Commissioners. It is also difficult to see any logical basis for distinguishing in this respect between the premature levying and payment of tax and the overpayment of tax. In both cases, only compound interest will normally give a full and effective remedy. As Mr Conlon observed, it is possible to conceive examples in which VAT is exacted prematurely in breach of Community law, and it is difficult to see any principled reason for treating such cases differently from overpayments of VAT.
41. In view of those doubts and difficulties and the importance and financial implications of the issue, it seems plainly desirable that there should be a reference to the ECJ for a preliminary ruling on the issue. The Judge himself (in paragraph 125) considered whether to refer the question to the ECJ for a further preliminary ruling. One of the reasons why he declined to do so was that it was open to the Commissioners to appeal his decision, in which case the question of a further reference could be more appropriately considered by this Court. In the light of the decision of Henderson J that the restitutionary claims of the claimants for compound interest are time barred and my conclusion (below) that he was right in that decision, it is not possible for the reference to be made in these proceedings since a reference is not necessary to enable judgment to be given: see Article 267 of the Consolidated Treaty on the Functioning of the European Union (formerly Article 234 of the EC Treaty), and paragraphs 11 and 14 of the ECJ's Information Note on references from national courts for a

preliminary ruling (OJ 2009/C 297/01). Other than to state that there should be a reference to the ECJ for a preliminary ruling when a proper opportunity arises, it is not necessary, and I do not consider it appropriate, to express any further view about the merits of this part of the appeal.

The nature of the “mistake” within Limitation Act 1980 s32(1)(c)

42. As I have said, it is common ground between the parties that the ordinary limitation period for restitutionary claims for the recovery of money is the 6 year period prescribed by section 5 of the 1980 Act. The claimants rely on the longer limitation period in section 32(1)(c) of the 1980 Act. That subsection provides so far as relevant as follows:

“(1) Subject to subsection (3) and (4A) below, where in the case of any action for which a period of limitation is prescribed by this Act, ...

...

(c) the action is for relief from the consequences of a mistake;
the period of limitation shall not begin to run until the plaintiff has discovered the ... mistake ... or could with reasonable diligence have discovered it.”

43. The claimants contend that Henderson J wrongly interpreted and applied section 32(1)(c) as being engaged only where the mistake, that is the mistake from the consequences of which relief is sought, is an essential ingredient of the claimants’ cause of action. That was what the Judge called the claimants’ “liability mistake” (namely, the mistake as to the original overpayment of VAT), by contrast with what he called their “time limit mistake” and their “simple interest mistake” (see paragraph 19 above), neither of which he considered were relevant to section 32(1)(c). The claimants contend that he was wrong to take that approach, and that both claimants’ time limit mistake and their simple interest mistake are relevant mistakes for the purposes of section 32(1)(c).
44. We discouraged oral submissions on this aspect of the appeal since the precise point was in issue in *FII CA*, and a judgment of the Court of Appeal in that case was expected shortly. That judgment has now been handed down and is binding on us. In it the Court of Appeal has held, consistently with Henderson J’s approach in the present case, that a mistake is only relevant for the purposes of section 32(1)(c) if it is an essential element of the cause of action. Accordingly, this ground of appeal fails.

Limitation Act 1980 s.29(5): acknowledgment and part payment.

45. The claimants submit that the Judge wrongly rejected their case that the 6 year limitation period was extended by virtue of acknowledgment or part payment within section 29(5) of the 1980 Act. Barnes claims that the payment to it of £101,866.03 by the Commissioners on 12 May 2004 was part payment of its claim within section 29(5) of the 1980 Act, and that an e-mail from the Commissioners dated 26 July 2004 giving notice of intention to pay interest under the statutory scheme was an acknowledgment of its claim within that sub-section, with the consequence that the 6 year limitation period only began to run from one or other of those dates. Chalke claims that the payment to it of £146,526 on 16 August 2004 was a part payment within the sub-section, with the consequence that the 6 year limitation period only

began to run against it from that date. If those contentions are correct, both sets of proceedings were commenced within the limitation period.

46. Section 29(5) is as follows:

(5) Subject to subsection (6) below, where any right of action has accrued to recover-

(a) any debt or other liquidated pecuniary claim; or

(b) any claim to the personal estate of a deceased person or to any share or interest in any such estate;

and the person liable or accountable for the claim acknowledges the claim or makes any payment in respect of it the right shall be treated as having accrued on and not before the date of the acknowledgment or payment.

47. Henderson J rejected the claimants' submission on this issue on the ground that the payments relied upon were in respect of each claimant's right to repayment under section 80 of VATA 1980, and not in respect of, or by way or recognition or acknowledgment of, the non-statutory common law restitutionary right to compound interest which the claimants seek to establish in the present proceedings (paragraph 153).

48. Mr Conlon submitted that the Judge was in error in confusing the "right of action" in section 29(5) with the "claim". He contended that what is material for the purposes of section 29(5) is acknowledgment or part payment of "the claim", and not the cause of action. He submitted that the relevant "claim" in the present proceedings is the composite claim under Community law to repayment of tax and reimbursement of all directly related benefits retained by the member state, and that the Judge himself recognised the composite nature of that claim in paragraph 108 of his judgment. He contended that the statutory scheme in sections 78 and 80 of VATA 1994 were merely the domestic means for enforcement of that composite *San Giorgio* claim. He further submitted that Henderson J was wrong to rely upon the judgment of Kerr LJ in *Surrendra Overseas Limited v Government of Sri Lanka* [1977] 1 WLR 565 in support of the Judge's analysis and conclusion, since that case was distinguishable.

49. I can deal with this ground of the appeal very briefly. It cannot succeed in the light of section 29(7), to which Henderson J was not referred. That subsection is as follows:

"(7) Subject to subsection (6) above, a current period of limitation may be repeatedly extended under this section by further acknowledgments or payments, but a right of action, once barred by this Act, shall not be revived by any subsequent acknowledgment or payment."

50. Henderson J found that Chalke and Barnes were aware of the "liability mistake" by July 1997. Accordingly, unless disapplied as a result of Community law, the extended limitation period under section 32(1)(c) expired before the part payments and acknowledgment relied upon by the claimants for the purposes of section 29(5). For the reasons given below, Community law did not have the effect of disapplying

the limitation period in section 32(1)(c). The effect of section 29(7) of the 1980 Act, therefore, is that section 29(5) has no application to the claims in these proceedings.

51. For completeness, I would add that, in any event, I agree with the Judge that the part payments and acknowledgment relied upon by the claimants were not in respect of their “claims” in these proceedings. They were plainly made and given in respect of the claimants’ statutory entitlement under the provisions of VATA 1994, and not in respect of the common law restitutionary claims which the claimants seek to enforce in these proceedings. For the domestic law purposes of the 1980 Act, those different claims are not merely based on different causes of action. The claims themselves are quite separate and distinct.
52. The Commissioners contended before the Judge that the claimants’ restitutionary cause of action is not a right of action to recover a “debt or liquidated pecuniary claim” within the meaning of section 29(5)(a) of the 1980 Act. Although it was not necessary for the Judge to do so in the light of his other conclusion on the application of section 29(5), he considered the point and expressed the view that the present claims for compound interest do fall within the scope of section 29(5)(a). Mr Swift argued the point again on this appeal, but it is not necessary, and I do not consider it desirable, to decide it. The answer to the point is not straightforward, as the Judge himself recognised in paragraph 157 of his judgment. It would be better to decide it in a case where it is necessary to do so.

Suspension or modification of the time periods in the Limitation Act 1980.

53. The consequence of the above analysis of the operation of the 1980 Act is that, under national law, the claimants’ claim to compound interest is barred by lapse of time. The claimants submit that, in those circumstances, the Community law principle of effectiveness requires that the national 6 year limitation period (from discovery of the liability mistake for the purpose of s.32(1)(c) of the 1980 Act) did not start to run against the claimants until they could, with reasonable diligence, have known of their Community law right to compound interest. They submit, in the alternative, that the 6 year time limit was suspended during periods where, in breach of their directly effective Community law rights, the claimants were prevented from obtaining a remedy. In the course of his oral submissions, Mr Conlon appeared to advance a further alternative, namely that, by virtue of the Community law principle of effectiveness, the claimants had a reasonable time to institute proceedings after they could with reasonable diligence have discovered their Community law right to compound interest. The claimants submit that, on any of those alternatives, the proceedings were instituted by them within a permissible period since the three year cap was only found to be unlawful by the ECJ in *Marks & Spencer* in 2002 and, they contend, it was only the Court of Appeal’s decision in *Sempre* in April 2005 which disclosed the right or the possibility of a right in domestic law to recover compound interest on the overpayments of VAT, the capital of which had been repaid in 2004.
54. The claimants’ argument in more detail proceeds along the following lines. They acknowledge that it is compatible with Community law for member states to impose time limits for enforcement of *San Giorgio* claims. Such limits must not, however, as is common ground between the parties, render virtually impossible or excessively difficult the exercise of such rights. Those principles appear clearly from, for example, paragraphs 34 and 36 of the ECJ’s judgment in *Marks & Spencer*:

“34. It should be recalled at the outset that in the absence of Community rules on the repayment of national charges wrongly levied it is for the domestic legal system of each member state to designate the courts and tribunals having jurisdiction and to lay down the detailed procedural rules governing actions for safeguarding rights which individuals derive from Community law, provided, first, that such rules are not less favourable than those governing similar domestic actions (the principle of equivalence) and, second, that they do not render virtually impossible or excessively difficult the exercise of rights conferred by Community law (the principle of effectiveness) (see, inter alia, *Aprile Srl (in liquidation) v Amministrazione delle Finanze dello Stato* (No 2) (Case C-228/96) [2000] 1 WLR 126, para 18, and the judgments in *Dilexport Srl v Amministrazione delle Finanze dello Stato* [1999] ECR I-579, para 25, and *Metallgesellschaft Ltd v IRC* [2001] STC 452, [2001] Ch 620, para 85).”

“36. Moreover, it is clear from the judgments in *Aprile Srl (in liquidation) v Amministrazione delle Finanze dello Stato* (No 2) [2000] 1 WLR 126, para 28 and *Dilexport Srl v Amministrazione delle Finanze dello Stato* [1999] ECR I-579, paras 41-42 that national legislation curtailing the period within which recovery may be sought of sums charged in breach of Community law is, subject to certain conditions, compatible with Community law. First, it must not be intended specifically to limit the consequences of a judgment of the court to the effect that national legislation concerning a specific tax is incompatible with Community law. Secondly, the time set for its application must be sufficient to ensure that the right to repayment is effective. In that connection, the court has held that legislation which is not in fact retrospective in scope complies with that condition.”

55. The claimants also acknowledge that ignorance of the law, or rather development of the law by judicial decisions, does not generally, either as a matter of Community law or domestic law, nullify or suspend or modify national time limits. In Case C-231/96 *Edilizia Industriale Siderugica (Edis) v Ministero delle Finanze* [1998] ECR I-4951 (“*Edilizia*”) one of the questions referred to the ECJ was whether Community law prohibits a member state from resisting actions for repayment of charges levied in breach of a provision of Community law by relying on a time limit under national law, where the application of that time limit would restrict the effects in time of a preliminary ruling by the Court interpreting that provision. The ECJ held that the member state was not precluded from relying on the time limit. The ECJ said:

“20. The Court has thus recognised that it is compatible with Community law to lay down reasonable limitation periods for bringing proceedings in the interests of legal certainty which protects both the taxpayer and the administration concerned (see *Rewe*, paragraph 5, *Comet*, paragraphs 17 and 18, and *Denkavit Italiana*, paragraph 23, all cited above; see also Case C-261/95 *Palmisani v INPS* [1997] ECR I-4025,

[1997] ECR I-4085, paragraph 48). The fact that the Court has given a preliminary ruling on the interpretation of the provision of Community law in question is immaterial in that respect (see, to that effect, *Rewe*, cited above, paragraph 7).”

56. The claimants say, nevertheless, that Community law may, in exceptional circumstances, require domestic time limits to be ignored for the effective enforcement of directly enforceable Community rights, for example in circumstances where the member state has made it impossible or excessively difficult to exercise a Community law right, such as enforcement of a *San Giorgio* claim. They rely, in this connection, on Case C-208/90 *Emmott v Minister for Social Welfare* [1991] ECR I-4269, [1993] ICR 8 (“*Emmott*”). In briefest outline, that case concerned the issue whether the Irish Minister for Social Welfare was entitled to rely upon a national time limit for bringing judicial review (3 months), the effect of which would have been to bar Mrs Emmott’s claim under a Council directive, where the directive had not yet been correctly transposed into national law, and where she had delayed instituting proceedings following statements to her on behalf of the Minister that no decision could be taken on her claim until judgment had been given in then pending litigation over the directive. The ECJ held that the national time limits for bringing proceedings could not be relied upon so long as the member state had not properly transposed the directive into its domestic legal system.
57. That was, on its face, a judgment of potentially very wide application. It is now restrictively interpreted, as Mr Conlon accepted, as an example, on its particular facts, of the application of the Community law principle of effectiveness. It was analysed in detail by Advocate General Jacobs in Case C-2/94 *Denkavit International BV v Kamer van Koophandel en Fabrieken voor Midden-Gelderland* [1996] ECR 2827 (“*Denkavit*”), in which he said (at paragraph 76 of his opinion) that “in the interests of legal certainty, the obligation to set aside time-limits should be confined to wholly exceptional circumstances, such as those in *Emmott*”. Advocate General Jacobs also scrutinised *Emmott* in Case C-188/95 *Fantask A/S v Industriministeriet* [1997] ECR I-6783 (“*Fantask*”), in which one of the questions referred to the ECJ by the Danish national court concerned the issue whether, when a member state has failed to transpose a Council directive correctly, it is prevented from relying on a national limitation period to resist an action for the recovery of charges levied in breach of the directive. Advocate General Jacobs said the following in *Fantask*:
- “68. The Governments’ arguments concerning the financial consequences of *Emmott* also raise an important point of principle. As they correctly observe, the *Emmott* ruling, if read literally, would expose Member States to the risk of claims dating back to the final date for implementing a Directive ...
69. Moreover, such liability would arise even in the event of a minor or inadvertent breach. Such a result wholly disregards the balance which must be struck in every legal system between the rights of the individual and the collective interest in providing a degree of legal certainty for the state. That applies particularly to matters of taxation and social security, where the public authorities have the special responsibility of routinely

applying tax and social security legislation to vast numbers of cases.

70. The scope for error in applying such legislation is considerable. Regrettably that is particularly so in the case of Community legislation, which is often rather loosely drafted ... The recent *Argos* and *Elida Gibbs* cases provide a further example of how huge repayment claims can arise from a comparatively minor error in implementing a Community tax directive. In those cases the Court found that the fiscal treatment accorded by the United Kingdom to voucher transactions – used extensively in that Member State as a business promotion technique – was not in accordance with the Sixth VAT Directive. The resultant repayment claims are reported to be between £200 and £400 million.

71. It might be objected that it is not unreasonable to require Member States to fund overpaid charges given that they were not entitled to collect them in the first place. However, that view disregards the need for States and public bodies to plan their income and expenditure and to ensure that their budgets are not disrupted by huge unforeseen liabilities. That need was particularly clear in *Denkavit*, in which repayment was sought of the annual levies imposed by the Netherlands Chambers of Trade and Industry in order to finance their activities. As I noted in my Opinion in that case, retrospective claims of up to 20 years would have had catastrophic effects on their finances.

72. In short, therefore, my main reservations about a broad view of the *Emmott* ruling are that it disregards the need, recognised by all legal systems, for a degree of legal certainty for the State, particularly where infringements are comparatively minor or inadvertent; it goes further than is necessary to give effective protection to directives; and it places rights under directives in an unduly privileged position by comparison with other Community rights. Moreover a broad view cannot be reconciled with the Court's subsequent case-law on time-limits.

...

85. An important factor in *Emmott* was that it would have seemed unjust in the particular circumstances of the case to permit the Irish authorities to rely on the time-limit laid down by national law. As I noted in my Opinion in *Denkavit*, the Court in its rulings in *Steenhorst-Neerings* and *Johnson* emphasised the following circumstances; Mrs Emmott had sought payment of the benefits in question on the basis of the court's judgment in *McDermott* and *Cotter*; the administrative authorities had declined to adjudicate on her claim until the litigation concerning the directive pending before the national

courts had been concluded; and the authorities sought to rely on the time-limit notwithstanding the failure correctly to implement the directive.

86. Consequently, as the Court stated in *Johnson* ‘the solution adopted in *Emmott* was justified by the particular circumstances of that case, in which a time-bar had the result of depriving the applicant of any opportunity whatever to rely on her right to equal treatment under the directive’.

87. Similar rulings based on principles of equity and good faith are to be found in the case-law of national courts. I do not in fact think it is necessary to develop any new principle of community law in order to explain the result in *Emmott*. As I suggested in my Opinion in *Denkavit*, the ruling can be seen as an application, albeit a new application, of the well-established principles laid down in *Rewe* and subsequent cases, in particular the principle that the exercise of Community rights must not be rendered excessively or unduly difficult. The ruling can be read as standing for the proposition that a Member State cannot rely on a limitation period where it is in default both in failing to implement a directive and in obstructing the exercise of a judicial remedy in reliance upon it, or perhaps where the delay in exercising the remedy is in some other way due to the conduct of the national authorities. In *Emmott* the Member State’s default in obstructing the remedy was compounded by Mrs Emmott’s particularly unprotected position as an individual dependent on social welfare.

88. It seems to me that so understood the *Emmott* principle, although confined to very exceptional circumstances, continues to provide an important safeguard notwithstanding the more recent developments in the case law which I have discussed above. An individual must be allowed to make use of all available remedies. The existence of another claim, for example a claim for damages in the competent courts, cannot justify the obstruction of a repayment or entitlement claim which an individual was seeking to exercise.”

58. The ECJ adopted a similar approach to that of Advocate General Jacobs. It said:

“47. As the Court has pointed out in paragraph 39 of this judgment, it is settled case-law that, in the absence of Community rules governing the matter, it is for the domestic legal system of each Member State to lay down the detailed procedural rules for actions seeking the recovery of sums wrongly paid, provided that those rules are not less favourable than those governing similar domestic actions and do not

render virtually impossible or excessively difficult the exercise of rights conferred by Community law.

48. The Court has thus acknowledged, in the interests of legal certainty which protects both the taxpayer and the authority concerned, that the setting of reasonable limitation periods for bringing proceedings is compatible with Community law. Such periods cannot be regarded as rendering virtually impossible or excessively difficult the exercise of rights conferred by Community law, even if the expiry of those periods necessarily entails the dismissal, in whole or in part, of the action brought (see, in particular, Case 33/76 *Rewe v Landwirtschaftskammer Saarland* [1976] ECR 1989, paragraph 5, Case 45/76 *Comet v Produktschap voor Siergewassen* [1976] ECR 2043, paragraphs 17 and 18, and Case C-261/95 *Palmisani v Istituto Nazionale della Previdenza Sociale* [1997] ECR I-0000, paragraph 28).

49. The five-year limitation period under Danish law must be considered to be reasonable (Case C-90/94 *Haahr Petroleum v Åbenrå Havn and Others* [1997] ECR I-0000, paragraph 49). Furthermore, it is apparent that that period applies without distinction to actions based on Community law and those based on national law.

50. It is true that the Court held in *Emmott*, at paragraph 23, that until such time as a directive has been properly transposed, a defaulting Member State may not rely on an individual's delay in initiating proceedings against it in order to protect rights conferred upon him by the provisions of the directive and that a period laid down by national law within which proceedings must be initiated cannot begin to run before that time.

51. However, as was confirmed by the judgment in Case C-410/92 *Johnson v Chief Adjudication Officer* [1994] ECR I-5483, at paragraph 26, it is clear from Case C-338/91 *Steenhorst-Neerings v Bestuur van de Bedrijfsvereniging voor Detailhandel, Ambachten en Huisvrouwen* [1993] ECR I-5475 that the solution adopted in *Emmott* was justified by the particular circumstances of that case, in which the time-bar had the result of depriving the applicant of any opportunity whatever to rely on her right to equal treatment under a Community directive (see also *Haahr Petroleum*, cited above, paragraph 52, and Joined Cases C-114/95 and C-115/95 *Texaco and Olieselskabet Danmark* [1997] ECR I-0000, paragraph 48).

52. The reply to the seventh question must therefore be that Community law, as it now stands, does not prevent a Member State which has not properly transposed the Directive from resisting actions for the repayment of charges levied in breach thereof by relying on a limitation period under national law

which runs from the date on which the charges in question became payable, provided that such a period is not less favourable for actions based on Community law than for actions based on national law and does not render virtually impossible or excessively difficult the exercise of rights conferred by Community law.

59. Community law does not, therefore, prevent a member state, which has not properly transposed a directive, from relying on a national limitation period to resist a claim for repayment of charges levied in breach of the directive, provided that such period is not less favourable for actions based on Community law than for actions based on national law (the principle of equivalence) and does not render virtually impossible or excessively difficult the exercise of rights conferred by Community law (the principle of effectiveness); and the decision in *Emmott* is to be regarded as turning on its own exceptional facts. Mr Conlon submitted that *Emmott* remains good authority that, if a member state is in breach of Community law, for example by failing to implement a directive and by obstructing the exercise of a judicial remedy, or there is some other reason for the delay in bringing the proceedings which is due to the conduct of the member state, then, as an application of the principle of effectiveness, the member state will not be allowed to take advantage of its own wrong by relying on the strict rigour of a domestic limitation period. Mr Conlon submitted that the present case is analogous to *Emmott* in that the United Kingdom made the enforcement of the claimants' *San Giorgio* rights impossible or at any event excessively difficult.
60. In that regard, he said that there were the following obstacles in the way of the claimants enforcing their right to compound interest until April 2005 at the earliest or, arguably, July 2007. There was the three year cap, which was only declared unlawful by the ECJ in July 2002. Mr Conlon emphasised that it was not unreasonable, in the light of section 80(7) of VATA 1994, for the claimants to believe that the three year cap applied to all claims relating to the overpaid VAT, whether statutory or otherwise. Further, he submitted that, even after *Metallgesellschaft* was decided by the ECJ in 2002, it would not have been possible prior to the Court of Appeal's decision in *Sempre* in April 2005 for the claimants to sue for interest in respect of principal sums which had already been repaid. That, Mr Conlon submitted, was the consequence of the decisions of the House of Lords in *London, Chatham and Dover Railway Co v South Eastern Railway Co* [1893] AC 429 and *President of India v La Pintada Compania Navigacion SA* [1985] AC 104. He further said that, until the decision of the Court of Appeal in *Sempre*, the claimants could only have recovered at most simple interest under the Supreme Court Act 1981 section 35A, and that it was not until the decision of the House of Lords in *Sempre* in July 2007 that it was finally clear that the claimants might have a right under the domestic law of restitution to compound interest. He relied on Henderson J's view (paragraph 141) that it was only after the judgment of the High Court in *Sempre* in June 2004 that the possibility of claiming compound interest might first have appeared seriously arguable; and only after the Court of Appeal had in April 2005 affirmed the judgment of Park J that one might reasonably have expected a company like Chalke to have submitted a claim for compound interest. There is no suggestion that Barnes was in a different position.

61. In addition to those points, the claimants rely on section 121 of the FA 2008 (“section 121”) in support of their case on this issue. Section 121(1), which by virtue of subsection (4) was treated as having come into effect on 19 March 2008, provides:

“(1) The requirement in section 80(4) of VATA 1994 that a claim under that section be made within 3 years of the relevant date does not apply to a claim in respect of an amount brought into account, or paid, for a prescribed accounting period ending before 4 December 1996 if the claim is made before 1 April 2009.”
62. The section was introduced following the decision of the House of Lords in *Fleming v Revenue and Customs Commissioners* [2008] UKHL 2, [2008] 1 WLR 195 (“*Fleming*”) that, until an adequate prospective transitional period was announced, the three year cap had to be disapplied in the case of all claims that had accrued before the cap was introduced. Mr Conlon submitted that the effect of the enactment of section 121 was to alter, in favour of the claimants, the tension between the rights of individuals to an effective remedy for breach of Community law, on the one hand, and the interest of the member state to legal certainty by way of the imposition of proportionate and reasonable time limits, on the other hand, as set out in the ECJ’s jurisprudence, including the passages in *Fantask* cited above. Section 121 had that effect, he contended, because Parliament had in effect given way on certainty by stipulating a new limitation period.
63. Mr Conlon also submitted that the Court should bear in mind that it would be very strange if Parliament had not intended, at the same time as extending the time limit for making claims under section 80 of VATA 1994, to reflect and give effect to the jurisprudence in *Metallgesellschaft* and *Sempra* by also extending the time for making *San Giorgio* claims for compound interest by the domestic route of restitution for mistake. If so, that would give rise, he said, to inequality of treatment between those entitled to benefit from section 121 and persons, like the claimants, who had already received repayment of their principal. Such inequality of treatment would itself be a breach of Community law.
64. Mr Conlon argued these points with skill, but in my judgment they clearly fail, essentially for the reasons given by Henderson J.
65. The imposition of the three year cap, and its legality, were relevant only to recovery under the statutory scheme. It never affected the claimants’ directly effective *San Giorgio* claims.
66. Even if the three year cap, combined with section 80(7) of VATA 1984, together with Business Briefs and possibly other communications issued by the Commissioners, could be regarded as making it excessively difficult for the claimants to have brought their proceedings prior to the ECJ’s decision in *Marks & Spencer* in July 2002 that the cap was unlawful, no such difficulty within the principle of effectiveness existed after that date. The Judge found that Chalke discovered both the *Italian Republic* and the *Elida Gibbs* liability mistakes by the end of June 1997. It was accepted, on behalf of Barnes, that it was also aware of each of the liability mistakes by June 1997. The extended limitation period under section 32(1)(c) of the 1980 Act therefore expired by the end of June 2003. That meant that Chalke and Barnes had approximately one year

after the decision in *Marks & Spencer* in which to institute proceedings to enforce their Community law rights before being barred under the domestic limitation period. That was certainly adequate time for that purpose. In *Fleming* Lord Neuberger considered (at paragraph [84]) that a transitional period for the introduction of the three year cap adequate to satisfy the requirements of Community law would have been between six and twelve months, and that he found it “hard to conceive of circumstances which would require a transitional period of more than a year, at least where a time limit is retrospectively created or reduced in relation to commercial tax claims”. There is no logical reason for reaching a different conclusion in a case, such as the present, concerning the adequacy of the remaining period of an existing limitation period. More to the point, the actions of Chalke and Barnes at the time show clearly that they had adequate time to institute proceedings within the domestic limitation period. Pursuant to the Business Briefs issued by the Commissioners in August and October 2002, introducing a retrospective transitional regime in response to the ECJ’s judgment in *Marks & Spencer*, Chalke submitted its uncapped claim on 13 June 2003 and Barnes submitted its uncapped claim on 23 June 2003. Indeed, it is no part of the claimants’ argument that, had they been aware of the law as clarified in *Sempre*, there would have been insufficient time to institute proceedings between the date of the judgment in *Marks & Spencer* and the expiry of the limitation period by the end of June 2003.

67. Even if it was excessively difficult, within the Community law principle of effectiveness, for the claimants to have brought their proceedings before the ECJ’s judgment in *Marks & Spencer*, I do not accept the submission that the 6 year limitation period (from discovery of the mistake for the purposes of section 32(1)(c) of the 1980 Act) only began to run from the date of that judgment. The purpose of the principle is to ensure that there is an effective domestic remedy for directly enforceable Community law rights, such as *San Giorgio* claims. A limitation period will only contravene that principle if it is so short as to render the exercise of such rights impossible or excessively difficult. For the reasons I have given, it did not do so in the present case in view of the period of approximately one year between the ECJ’s judgment in *Marks & Spencer* and the expiry of the extended limitation period in section 32(1)(c). The Community law principle of equivalence does not require a further extension of the limitation period since the extended period expiring by about the end of June 2003 was applicable equally to ordinary domestic claims as to *San Giorgio* claims.
68. What is highlighted by that analysis is that the claimants’ real and only argument for invoking the Community law principle of effectiveness in respect of the period after the ECJ’s judgment in *Marks & Spencer* is that, until the judgments of the Court of Appeal in *Sempre*, they were unaware of their right to recover compound interest in domestic law and any proceedings to enforce that right would have been dismissed.
69. The claimants’ reliance on the state of domestic law between *Marks & Spencer* and the judgments of the Court of Appeal in *Sempre* in 2005 is, in my judgment, plainly misplaced. As I have said, it is common ground between the parties that Community law rights may be lost in circumstances where the failure to exercise the right is due to the individual’s ignorance of its existence: see, for example, in addition to *Edilizia*, Case C-228/96 *Aprile Srl v Amministrazione delle Finanze dello Stato* [1998] ECR I-7141 (at para. 19 of the ECJ’s judgment), and Case C-90/94 *Haahr Petroleum v*

Åbenrå Havn and Others [1997] ECR I-4085 (paragraphs 46-48 of the ECJ's judgment). I can see no reason why that principle should not apply in the present case. I do not accept Mr Conlon's contention that, for the purposes of the present case, by the enactment of section 121 the United Kingdom has taken out of the balancing exercise underlying the Community principle of effectiveness, or in some way diminished, the desirability of certainty introduced by domestic limitation periods. Section 121(1) is concerned only with the statutory scheme. It does not address in any way restitutionary common law claims for payment of compound interest. In my judgment, it has no relevance to the claims in these proceedings or the limitation period in respect of them.

70. Furthermore, *Sempre* itself concerned the domestic implementation of the *San Giorgio* claims of taxpayers to interest representing the time value of the prematurely paid tax in issue in *Metallgesellschaft*. It was or should have been obvious, following the ECJ's judgment in *Metallgesellschaft*, that the *San Giorgio* principle required the national law of the United Kingdom to afford by one means or another an effective remedy for those rights. Accordingly, since the claimants accept that they cannot rely on the Community principle of effectiveness after the Court of Appeal judgments in *Sempre*, they should not be able to rely on that principle after *Metallgesellschaft* itself merely by virtue of the established state of the domestic law on the recovery of interest.
71. There are other reasons why I do not accept the claimants' basic submission that, prior to the Court of Appeal's decision in *Sempre*, any proceedings commenced by them for compound interest on overpaid VAT would undoubtedly have been dismissed. *Metallgesellschaft* arose out of domestic proceedings brought by *Sempre*, then called *Metallgesellschaft Ltd*. The proceedings were not dismissed, but were stayed pending the reference to the ECJ, which was ordered as long ago as October 1998. Following the ECJ's decision, *Sempre* brought its proceedings in restitution for compound interest. Those proceedings succeeded at first instance before Park J, and successive appeals by the Revenue to the Court of Appeal and the House of Lords were dismissed. Although *Sempre* itself concerned the remedy for premature payment of tax, Park J expressed the view at first instance (paras [37] to [40]) that he could see substantial arguments that the entitlement to interest on unutilised ACT (that is, ACT not set off against MCT and so, in effect, overpaid tax) should also depend on the principles of Community law explained in *Metallgesellschaft* rather than section 35A of the Supreme Court Act 1981. In the Court of Appeal Chadwick LJ (at para.[53]) endorsed that view. In the circumstances, I see no reason to think that, if the claimants had instituted their proceedings at any time prior to *Sempre*, they would have been dealt with in any more disadvantageous way than the actions commenced by *Metallgesellschaft/Sempre*.
72. Mr Conlon invited the Court to consider a reference to the ECJ for a ruling on the application of *Emmott* on the facts of the present case. I can see no reason to do so. The relevant principles of Community law in relation to this part of the appeal are clear, and the only question is the application of those principles to the facts. For the reasons I have given, this ground of appeal must fail.

Defences to restitutionary claims

73. The Commissioners argued before the Judge that, if the claimants' restitutionary claims were not time-barred, the claimants could nevertheless not succeed in view of the Commissioners' change of position as a consequence of the claimants' overpayments of VAT such that it would now be inequitable and unconscionable to require the Commissioners to make restitution of the sums claimed in the proceedings; alternatively, the extent of any sum recoverable by the claimants should be restricted to the actual benefit accruing to the Government by reason of the overpayment, and such overpayment would have been "exhausted" by the end of a single budget cycle following its receipt. The Judge considered and rejected the change of position defence. He did not deal expressly with the "actual benefit" defence, and the Commissioners contend that, by implication, he rejected it.
74. The rejection of both of those defences is challenged in the Respondents' notice, but, because I have concluded that the claimants' claims are time-barred, it is not necessary, and I do not consider it appropriate, to deal with them. Both defences are fact specific, but all the relevant facts have not been found by the Judge. The change of position defence in particular raises issues of principle of some difficulty. Mr Swift invited us to direct a reference to the ECJ in respect of them, or at all events the "actual benefit" defence, but, for the reasons I have given, I consider that it is neither necessary nor appropriate to do so.

FII CA

75. Following the conclusion of the oral hearing before us and the handing down of *FII CA*, we invited the parties to make brief written submissions on any points they wished to raise in the light of the Court of Appeal's judgment in that case. The Commissioners made written submissions in which they referred to the decision in *FII CA* that the cause of action in *Woolwich Equitable Building Society v IRC* [1993] AC 70 applies to any case where tax has been unlawfully exacted by the State, whether pursuant to a demand or by voluntary compliance by the taxpayer with the legislative imposition of the tax. They submitted that, consequently, the proper route in domestic law for Barnes and Chalke to pursue their *San Giorgio* claims was by a *Woolwich* cause of action rather than, as they have done before Henderson J and us, by a mistake based cause of action. They submitted that Henderson J should have so held; he should have recognised that any such cause of action would have failed on limitation grounds; he should have concluded that in those circumstances there was no requirement as a matter of Community law to disapply the effect of sections 80 and 78 of VATA 1994 in order to permit Barnes and Chalke to pursue mistake based claims; and he should have further concluded that, even if mistake based claims could be pursued, the Commissioners would be entitled to rely on a change of position defence since a mistake based claim was not a cause of action necessary to give effect to the remedy required by the *San Giorgio* principle.
76. None of those submissions was made at the oral hearing. Further, apart from the general point that Henderson J was wrong to conclude that the Community law principle of effectiveness overrode the exclusion by the statutory scheme in VATA 1994 of the restitutionary claims of Barnes and Chalke which are the subject of the appeal, none of them was raised in the Respondents' notice. In any event, I do not consider that it is necessary or desirable to address them in view of the discussion and

conclusions earlier in this judgment, and in particular that the appeal should be dismissed on other grounds.

Conclusion

77. For those reasons, I would dismiss the appeal.

Lord Justice Patten

78. I agree.

Lord Justice Mummery

79. I also agree.