THE STRAW THAT BROKE THE CLAIMANT'S BACK: AN ASSESSMENT OF THE SUPREME COURT'S REASONING IN FII (NO. 2)

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Abstract: Much of the development of the law of unjust enrichment has come off the back of two waves of cases: first were the swaps litigation which followed Thatcher policies affecting the borrowing powers of local councils and second came the overpaid tax litigation. The latter group of cases were mainly a product of EU law declaring that certain tax statutes were 'ultra vires' in that they discriminated between wholly UK groups and those with parents/subsidiaries abroad. This note considers the latest major development of the latter wave – *FII (No. 2)*. The importance of *FII (No. 2)* is mainly to be found in its treatment of the limitation period for restitutionary claims of payments made as a result of a mistake. Prior to this case, claimants enjoyed a generous limitation period, so they could be certain of success at the point at which they brought their case. The financial consequences of this for defendants (often public bodies) were nothing short of disastrous. In the aftermath of this decision, claimants can no longer benefit from such a favourable position due to the Supreme Court's interpretation of what 'reasonably discoverable' means. The decision has been described as a 'triumph of coherence in English limitation law'. That is certainly true, but parts of the decision are regrettable – mainly the lack of reckoning with jurisprudential questions on the nature of mistakes.

A. INTRODUCTION

The Supreme Court in *Test Claimants in the FII Group Litigation v HMRC (No 2)*[1] [FII (No. 2)] has notably impacted the law on unjust enrichment. In a four-to-three majority, the Court has limited the scope for claimants to rely on s32(1)(c) of the Limitation Act 1980 – a decision which will no doubt have a positive impact on the financial outlook at HMRC. Their Lordships have stated that the litigation has involved 'novel and developing legal claims raising legal issues of unparalleled complexity'.[2] Per *Banque Financiere de la Cite v Parc (Battersea) Ltd*,[3] claims in unjust enrichment are subject to the requirement of an 'unjust factor'. One of the main constituents

* UCL Laws LLB '22. I would like to thank Dr. Niamh Connolly for all of her helpful comments and suggestions. I am very thankful to Professor Charles Mitchell, Martin Fischer, and Dr. Connolly for many interesting discussions on the topic. All errors are my own.

[1] [2020] UKSC 47.

[2] ibid, [78].

[3] [1998] UKHL 7.

 DOI: https://doi.org/10.14324/111.444.2052-1871.1361.

of these claims are claims brought under the mistake factor. The advantage of bringing a claim under this heading is the ability to overcome limitation hurdles. Essentially, most claims are subject to a limitation period of six years. This period does not apply where the reason for the payment is a mistake – the limitation period in these cases is far more generous. Courts, acutely aware of this, have sought to lessen the expansive approach to unjust enrichment evident in earlier judicial decisions. The Supreme Court decision in *FII (No. 2)* is one of the recent decisions causing claimants much distress. It is submitted that the position prior was overly generous to claimants and the court was right to limit the danger to public finances, notwithstanding: a) the fact that a small part of the judicial reasoning fell short of convincing and b) valid rule of law concerns were raised.[4]

This note aims to cover the preceding cases in light of the judgment in *FII (No. 2)*, discuss the shift in the judicial understanding of the relevant part of the Limitation Act 1980, and provide some commentary on the above.

B. BACKGROUND TO THE CASE

Corporate groups paid Advanced Corporation Tax (ACT) under the Income and Corporation Taxes Act 1988, which pertained to the taxation of dividends coming to UK-resident companies from non-resident sources/subsidiaries. In the aftermath of their payments, it was held by the Court of Justice of the European Union (CJEU) that this part of English legislation was not compliant with EU law (*FII (CJEU) 1*),[5] in that it discriminated between wholly UK corporate groups and those with a foreign subsidiary. In other words, the legislation was an affront to freedom of establishment (Art 49 TFEU) and free movement of capital (Art 56 TFEU). Here, this describes the position of the respondent, the Franked Investment Income (FII) Group Litigation. Established by a Group Litigation Order (GLO), the test claimants were united in their desire to recover payment, though this varied slightly from claimant to claimant, as some were seeking recovery dating back to the 1973 UK accession to the EU and the subsequent introduction of ACT in April 1973. In the alternative, they made a compensatory claim under *Francovich v Italy* for damages.[6] This case represents the second time that the FII test claimants have reached the Supreme Court.

[4] Some estimates have placed the figure at £55bn, see HM Revenue and Customs, *Annual Report and Accounts 2015-16* (HC 388, 2016), para. 7.1.

[5] Case C-35/11 *Test Claimants in the FII Group Litigation v Inland Revenue Commissioners* [2013] Ch. 431.

[6] Case C-6/90 *Francovich v Italy* [1991] E.C.R. I-5357.

The first – and most significant – hurdle for the claimants, seeing as the claims go back decades, is limitation. Sections 2 and 5 of the Limitation Act 1980 (henceforth 'the 1980 Act') provide that a claimant has six years in which to bring a claim from the date of payment, with section 2 pertaining to *Francovich* claims and section 5 relating to claims arising from 'simple contract'. Thus, the orthodox position for claims arising from contracts and torts is that they must be brought within six years. To overcome the hurdle of the time bar (as the period that the claimants wanted recovery for extended beyond six years), the claimants needed to establish that the payments were mistaken, thus allowing them the benefit of section 32(1)(c) of the 1980 Act. This delays the date at which the 'clock starts' to when 'the plaintiff has discovered the ... mistake ... or could with reasonable diligence have discovered it' as opposed to the date at which the payment is made. In other words, it provides an exception to the orthodox position. The manner, in which this section is construed, is the question at the heart of the Supreme Court's judgment.

It is worth looking at the genesis of this area of law, as the Supreme Court does. Firstly, *Woolwich Equitable Building Society v Inland Revenue Comrs* laid the path for '*Woolwich* claims',[7] where taxpayers have a right to recover tax paid in response to an *ultra vires* law. The Woolwich Equitable Building Society paid £57m in tax without prejudice, suspecting that the underlying tax law was *ultra vires*. After judicial review, instigated by the taxpayer, Inland Revenue (known today as HMRC) repaid the principal. The 'real' issue arose out of the interest payments, which Inland Revenue refused to repay. Courts have a discretion, under section 35A of the Senior Courts Act 1981, to award simple interest, if they can prove entitlement to restitution of the principal – in *Woolwich*, the taxpayers were awarded interest on these grounds.

Later comes *Kleinwort Benson v. Lincoln City Council et al.*,[8] where it was found that section 32(1)(c) of the 1980 Act would cover claims for money paid under a mistake of law, where it had previously only been thought to cover money paid under mistakes of fact. The mistakes of law and mistakes of fact distinction has been well explored, but it is sufficient to say that in mistake of fact cases, the claimant was wrong about some fact which caused them to make the payment – an individual pays another £1,000 believing them to have some malady whereas they are perfectly healthy. In contrast, a mistake of law pertains to, for example, when an individual pays some quantum under a tax statute which is repealed or ruled to be 'ultra vires'. This distinction was very

[7] [1993] AC 70.
[8] [1999] 2 AC 349.

important before *Kleinwort Benson* but now that both may ground recovery the distinction ceases to be hugely relevant.

The importance of *Kleinwort Benson* is fully realised when one considers it in conjunction with *Metallgesellschaft and Others, Hoechst AG and Hoechst Ltd v Commissioners of Inland Revenue and H.M. Attorney General*.[9] The CJEU established in *Hoechst* in 2001 that the UK tax treatment of UK-resident subsidiaries to their foreign parents is incompatible with EU law. In effect, this rendered huge sums of money to become subject to overpaid tax claims. Further, the court asserted that a claimant who has a '*Woolwich* claim' is not prevented from having a concurrent claim arising on the ground of mistake.[10] The significance of this lies in the fact that the former claim is subject to a limitation period beginning from the date of payment, whilst the latter benefits from section 32(1)(c). This, in tandem with *Kleinwort Benson*, paved the way for the court in *Deutsche Morgan Grenfell Group Plc v Her Majesty's Commissioners of Inland Revenue and Another*[11] to say that the relevant date where the 'clock starts' for claims where money is paid under an *ultra vires* law is when a court, from which there is no appeal, has ruled on the matter. In other words, it is the date of judgment of a final court that counts for the purpose of section 32(1)(c). It is hard to appreciate quite how claimant-friendly this position was. Claimants could, in the aftermath of *Deutsche Morgan Grenfell*, watch as cases went from appeal to appeal knowing that they had the luxury of time which afforded them an unusual level of certainty when they eventually brought their claim.

In *Sempra Metals Ltd v Inland Revenue Commissioners*,[12] itself a test claim under a GLO, it was held that compound interest was payable on the amounts awarded and that claims could be brought for the time value of money, a benefit that was deemed to be separate to its use value. The importance could not be understated for the financial position of claimants; it meant that the sums of money they were due from public authorities were much larger because the authority also had to account for the benefit of being able to use the money. This was recently overruled in *Prudential*

[9] Joined Cases C-397 and 410/98 *Metallgesellschaft and Others, Hoechst AG and Hoechst Ltd v Commissioners of Inland Revenue and H.M. Attorney General* [2001] Ch 620.

[10] Some academics have argued that '*Woolwich* claims' should be exclusive, *see* Rebecca Williams 'Overpaid Taxes: A Hybrid Public and Private Approach' in Steven Elliott and others. (eds), *Restitution of Overpaid Tax* (Hart Publishing 2013).

[11] [2007] 1 AC 558.

[12] [2008] 1 AC 561.

Assurance Co Ltd v HMRC,[13] because of the unjust enrichment requirement that requires the gain to have been achieved directly at the expense of the claimant.[14] But the effect of *Sempra Metals* was chilling for public finances: the day after judgment, section 107 of the Finance Act 2007 was enacted. It had the effect of prohibiting reliance on section 32(1)(c). This section was ruled to be incompatible with EU law because of the principle of equivalence.[15] The court had thought *Sempra Metals* incorrectly decided, asserting that compound interest is not to be paid on restitutionary awards.[16] In *FII (No. 2)*, their Lordships drew attention to the tax treatment of restitutionary awards which was unreasonable in that a claimant would get an award against HMRC but have that award be subject to higher levels of tax, which essentially meant that it was HMRC that benefited from a restitutionary award.[17]

This history paints the backdrop against which the Supreme Court dealt with issues of 'unparalleled complexity'.[18] It is only since *Kleinwort Benson* that the English courts have had to deal with claims arising from a mistake of law, but of course, the claims being subject to section 32(1)(c) have led to significant sums of money at stake.[19] Further, the implications of this for corporations paying tax under legislation that was held to be incompatible with EU law have become evident just as recently as *Hoechst* in 2001. The three-fold effects of *Sempra Metals, Prudential Assurance,* and *Littlewoods Retail Ltd. And Others v HMRC*[20] (supplying that compound interest is owed on sums paid as VAT where the tax was not lawfully due)[21] have all had bearings on this judgment. Tangentially, it must be appreciated that the points of EU law add further complexity, having generated three judgments in CJEU references. Indeed, the claimants found themselves at 'the frontier of legal developments'.[22] Furthermore, prior to reaching the Supreme Court, the aforementioned section 107 of the Finance Act 2007 and section 320 of the Finance Act 2004 were all relied upon by the Revenue to defend against the test claimants' use of

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13 [2019] AC 929.
14 *Banque Financiere* (n 3), [18].
15 *Test Claimants in the Franked Investment Income Group Litigation v Revenue and Customs Commissioners* [2020] UKSC 47 *(FII (No.1))*.
16 *Prudential Assurance* (n 17).
17 *FII (No.2*), [56].
18 ibid, [78].
19 HM Revenue and Customs (n 4).
20 [2014] EWHC 868 (Ch).
21 Applying Case C-398/09 *Lady & Kid A/S and Others v Skatteministeriet* [2011] ECR I-7375.
22 FII (No.2) (n 1), [78].

section 32(1)(c) which had the effect of precluding any need to rely on their ability to challenge *Kleinwort Benson* and *Deutsche Morgan Grenfell* because their effect was "to curtail the operation of section 32(l)(c) of the Limitation Act 1980, thereby removing the extended limitation period for mistake claims in relation to overpaid taxes".[23]

C. GROUNDS OF APPEAL

The Revenue appealed from the Court of Appeal decision, which found in favour of the test claimants insofar as saying that the effect of section 32(1)(c) is to postpone the 'relevant date' until the date at which a final court has ruled on the matter (in line with *Deutsche Morgan Grenfell*).

Interestingly, despite the long history of this case, the Revenue did not indicate that they wished to challenge the outcomes or correctness of *Kleinwort Benson* and *Deutsche Morgan Grenfell* until the Court of Appeal hearing in 2016. This argument, however, did not go very far then with the focus being on what the effect of those cases would be, rather than their correctness. On appeal to the Supreme Court, the test claimants therefore put forward that the Revenue could not make this argument on the grounds of res judicata, estoppel, and abuse of process.[24] In the alternative, they said that an appeal could be based on the question of the relevant date for the purposes of limitation under section 32(1)(c), but still, they argued that in the lower courts the Revenue had made concessions regarding the correctness of *Kleinwort Benson* and *Deutsche Morgan Grenfell*, and as such, it should not be open to them to now make such an argument. The policy basis for this is found readily in the case law, with judges pointing to public interest in general and 'to support the good administration of justice'.[25] The court noted that the test claimants' reference to res judicata is used to 'equate it with cause of action estoppel'.[26] On this point, the court declared that the Revenue were not stopped from making their challenge as the 'cause of action estoppel operates only to prevent the raising of points which were essential to the existence or non-existence of a cause of action',[27] and with the focus of the challenge on limitation, it naturally does not impact the presence of a cause of action.

[23] *Kleinwort Benson* (n 11).
[24] *FII (No. 2)* (n 1), [58].
[25] *Virgin Atlantic Airways Ltd v Zodiac Seats UK Ltd* [2013] UKSC 46, [55].
[26] *FII (No. 2)* (n 1), [60].
[27] ibid, [63].

In the alternative to the res judicata argument, the test claimants argued that the Revenue would be guilty of an abuse of process, if they were to undermine the correctness of *Kleinwort Benson* and *Deutsche Morgan Grenfell*. Abuse of process, in contrast to *res judicata*, is not a 'rule of substantive law'[28] though they are both underpinned by the purpose of limiting 'abusive and duplicative' litigation.[29] The Supreme Court were not satisfied that the Revenue was abusing the process of the court by 'oppressing the other party by repeated challenges relating to the same subject matter'.[30]

All in all, the Supreme Court were not persuaded that the grounds of estoppel, res judicata, and abuse of process should stop the Revenue from challenging the correctness of *Kleinwort Benson* and *Deutsche Morgan Grenfell*. They were additionally persuaded by the fact that only the Supreme Court judges themselves would have the power to overrule those two cases, both of which also were decisions of the highest court. The claimants could not have done this until the first time they found themselves in that court, namely in 2012.

D. UNDERSTANDING MISTAKES AND SECTION 32(1)(C)

Section 32(1)(c) of the 1980 Act provides that, where an action would have been prohibited by a limitation, if the action is 'for relief from the consequences of a mistake' then 'the period of limitation shall not begin to run until the plaintiff has discovered the fraud, concealment or mistake (as the case may be) or could with reasonable diligence have discovered it.' The interpretation of this section has been the subject of much debate. This centred on the fact that there could be no recovery for mistakes of law, only mistakes of fact – this being the case since *Bilbie v Lumley*,[31] and continuing until the House of Lords decision in *Kleinwort Benson*. *FII (No.1)* gives us the requirement that the mistake must be an essential element of the claim for relief. Put simply, '[s]ection 32(1) applies where the claimant does not know and cannot reasonably be expected to discover a mistake which forms an essential ingredient of his cause of action'.[32]

1. *Kleinwort Benson*

[28] *Virgin Atlantic* (n 25), [25].
[29] ibid.
[30] *FII (No.2)* (n 1), [76].
[31] (1802) 2 East 469.
[32] *FII (No.1)* (n 15), [177].

The *ratio* of *Kleinwort Benson* has already been discussed, but the facts are worthy of elaboration. This case comes under the umbrella of the unjust enrichment interest rate swaps claims that arose out of Thatcher's policies in the 1980s which reduced the local authorities' taxing power. To get over the financial hurdle the restriction presented to the local councils, they resorted to borrowing money, an alternative to increasing taxes. These agreements were held to be void as the councils did not have legal capacity to enter into these contracts. With finesse, they then arrived at another plan to raise money: interest rate swap agreements with banks. The terms of these agreements with councils often had upfront payments made by the banks, in response to which councils would pay back a sum each month, functionally equivalent to interest with the result that the lender would receive the principal and an additional sum (which would correspond to interest). *Hazell v Hammersmith and Fulham London Borough Council* effectively put an end to these agreements,[33] holding that these contracts were beyond the borrowing powers of the council as per the Local Government Act 1972. In *Hazell*, Lord Templeman said that there had been 'about 400' of these swap agreements,[34] which indicated how significant these contracts would be in developing the law of unjust enrichment. Notable cases that followed *Hazell* included of course *Kleinwort Benson*, *Credit Suisse v Allerdale BC*,[35] and *Westdeutsche Landesbank Girozentrale v Islington LBC*.[36] Kleinwort were able to recover the sums paid where no limitation issues arose, those being the payments within the six years. Naturally, they had to rely on section 32(1)(c) of the 1980 Act in order to recover the earlier sums, but there were two issues arising that necessitated litigation: first, whether Kleinwort Benson had a cause of action based on a mistake and secondly, if so, whether they could rely on the relevant provision of the 1980 Act considering the nature of the mistake.

Counsel for Kleinwort Benson accepted that money paid pursuant to a settled understanding of the law is not money paid under a mistake, despite even subsequent authority changing the settled understanding. Instead, they argued that the law had not been settled until the decision of the House of Lords in *Hazell*. Counsel for the authorities relied on the idea, as articulated by their Lordships in *FII*, that 'recovery should not lie where a payment was made in accordance with a settled understanding of the law which was later changed by a judicial

[33] [1992] 2 AC 1.
[34] ibid, [26F].
[35] [1997] QB 306.
[36] [1996] HL 12.

decision.'[37] The Lords went further than counsel for the bank originally wanted, overturning the notion that one cannot recover for payments made under a mistake of law.

Lord Goff's dissent in *Kleinwort Benson* is of enormous interest jurisprudentially, notably pointing to *Hazell* and saying that '[j]udicial decisions declaratory of the law often have retrospective effect'.[38] In this way, he accepted that previous settled understanding leading to a payment, once overturned by a decision of the court, rendered that payment to be mistaken *at the time* that the relevant payment was made. He did not, however, accept the 'declaratory theory of judicial decision making',[39] leading to Lord Hoffmann using the language of 'deemed mistake'[40] as the previous understanding was a correct reflection of the law during the point at which the payment was made, in *Deutsche Morgan Grenfell* he said that, 'if one said that because the law was now deemed to have been different at the relevant date, he was *deemed* to have made a mistake'.[41] It is thus unfortunate that Lord Hope refrained from such a discussion.

At this point it is worth elaborating on the 'declaratory theory of judicial decision making'. This theory suggests that, when deciding cases, judges do not make law instead they declare what it is. There is, however, something to be said for the counterargument, namely that judges are making law. Lord Reid has been persuasive in his attempts to dismiss these theories, saying that judges deduce rather than discover and that the 'fairy-tale' of the declaratory theory is harmful in that it disguises what the judge is actually doing.[42] This counterargument is best illustrated in the swaps cases. The language of 'deemed mistake' and 'actual mistake' is at the heart of these cases. Frustratingly, some judges and academics have noted that there has never been a satisfactory definition of a mistake and that it is not obvious that defining a mistake is a worthwhile feat.[43] Actual mistakes do not require more elaboration, but deemed mistakes pose many jurisprudential problems and has implications for the declaratory theory of judicial decision making.

[37] *FII (no. 2)* (n 1), [144].
[38] *Kleinwort Benson* (n 11), [354].
[39] Allan Beever, 'The Declaratory Theory of Law' (2013) 33 Oxford Journal of Legal Studies 421.
[40] *Kleinwort Benson* (n 11), [23].
[41] ibid. For a wider discussion of deemed mistakes, *see* Daniel Tan 'Public bodies, unjust enrichment and the rule of law' 15 Oxford University Commonwealth Law Journal 99.
[42] Lord Reid, 'The Judge as Law-Maker' (1972) 12 Journal of the Society of Public Teachers of Law 22.
[43] Graham Virgo, *The Principles of the Law of Restitution*' (1st ed., Clarendon Press 1999); *Barrow v Isaacs and Son* (1891) 1 QB 417, [425].

Lord Goff in *Kleinwort Benson* can, at first glance, be seen to answer the question of whether a mistake of law should be recoverable in a way that supports the declaratory theory of the law. Lord Browne-Wilkinson similarly supported this theory. Their Lordships looked to the case law and statutes and tried to deduce a theory of underlying principle in order to answer the question before them. In trying to come to a conclusion that was in agreement with the *corpus* of the law before them, they satisfied themselves in thinking that they are revealing what the law always was. Since they did not wish to overturn the previous law, their interpretation is plausible.

The Supreme Court in *FII (No. 2)* regrettably did not engage in an analysis of the merits of this decision. It was sufficient for them to appreciate that *Kleinwort Benson* had the effect of rendering equivalent cases, where the law was determined for the first time and cases, where a court decision changes whatever the settled understanding may be. In other words, Kleinwort Benson had paid on a settled understanding that the payments were lawfully due until *Hazel*, when it became clear that they had been operating under a mistake of law. The law thus deemed the payment to be a mistake. There were suggestions that these 'settled understanding' cases should be exempted from recovery, but ultimately the House of Lords decided that this would be an issue for the legislature.

This 'deemed mistake' took care of the initial problem, posed in the first question – Kleinwort Benson had a cause of action grounded in mistake. For the second question to be resolved, there was still a further step of considering, whether the claim was covered by section 32(1)(c). The local authorities said that this could not be the case, due to the fact that the law had come into effect in 1980, where there was still the mistake of law bar. In other words, Parliament could not have intended this provision to apply to mistakes of law. The House of Lords were not persuaded by this and found in favour of the bank. The consequences of this were pointed out by Lord Goff:

> [T]he cause of action … may be extended for an indefinite period of time. I realise that this consequence may not have been fully appreciated at the time when this provision was enacted, and further that the recognition of the right at common law to recover money on the ground that it was paid under a mistake of law may call for legislative reform to provide for some time limit to the right of recovery in such cases. The Law Commission may think

> it desirable, as a result of the decision in the present case, to give consideration to this question ... as a matter of some urgency.[44]

2. *Deutsche Morgan Grenfell*

The claim in this case related to ACT payments – where there was a dividend paid, which triggered liability to pay ACT, the amount paid could be set off against the liability of the company to pay mainstream corporation tax (MCT) on profits – in effect making the company pay the tax they were liable to pay at an earlier date when compared with companies who had liability to pay MCT but not ACT (these would be wholly UK corporations). Since this only applied to companies where the parent was non-resident (wholly resident companies could make a group income election), it was declared to be incompatible with Union law (as per *Hoechst*). This described the predicament of Deutsche Morgan Grenfell, a UK subsidiary with a German parent.

Five months before the decision of the CJEU in *Hoechst*, Deutsche Morgan Grenfell brought a claim to recover money paid earlier than the date that the MCT had become due. This was on the ground that *Kleinwort Benson* established that one could recover money paid in mistake of law, and Deutsche Morgan Grenfell argued that this mistake described their payment of the tax. On the question of limitation, they said that the mistake was not reasonably discoverable until the Court of Justice gave their decision in *Hoechst* and as a result it is the date of judgment that should 'start the clock' for the imitation period. The Revenue argued that the relevant date for when the mistake was reasonably discoverable was when the company had learned that there was a legal challenge regarding the lawfulness of the ACT payments, this being in 1995.

In the House of Lords, it was the argument put forward by counsel for Deutsche Morgan Grenfell that found favour. Lord Hoffmann relied on the fact that the 'true state of affairs' was not discoverable until the CJEU gave its judgment, saying that 'the truth did not yet exist' before.[45] This of course echoes himself and Lord Goff in *Kleinwort Benson*. Lord Hoffmann was joined by Lord Hope, who thought that litigation was necessary in order to allow a mistake to be '"discovered" in the sense referred to in section 32(1) of the 1980 Act'.[46] In a concurring speech, Lord Walker emphasised the importance of *Hoechst* to show that it is not the possibility of a mistake that is important, but the knowledge of it.

[44] *Kleinwort Benson* (n 11), 389.
[45] *Deutsche Morgan Grenfell* (n 15), 31.
[46] Ibid, 71.

Lord Brown dissented, which indeed was very influential for the Supreme Court in *FII (No.2)*. His Lordship's dissent centred on the idea that it is not when a final court has judged on the matter that a mistake becomes discoverable for the purposes of s32(1)(c), but rather when the claimant becomes aware that another party is challenging the relevant provisions – ie when they know that a worthwhile claim arises. In the case of *Deutsche Morgan Grenfell*, that would have been the date at which they learnt of the *Hoechst* proceedings. This is surely most plausible considering that they brought the claim prior to the decision, and therefore it must have been discoverable before. Any payments made after this point, Lord Brown notes,[47] are not made under a mistake of law. The Supreme Court here notes that this approach is consistent with other parts of the Act, where the limitation period runs from when the claimant knew, or could reasonably be expected to know, that they had a cause of action.[48]

E. FOUNDATIONS OF THE DECISION IN FII (NO. 2)

The decision could be broken down into two parts, each grappling with a different question. The first was whether it was right that payments made under a mistake of law can be recoverable. If the answer to the first question was positive, the second question was to determine when a mistake of law is discoverable for the purposes of the 1980 Act.

Persuaded by the dissent of Lord Brown, both Lord Reed and Lord Hodge emphasised the paradox that *Deutsche Morgan Grenfell* created, and the many flaws of this. There is an inherent illogicity with saying that a claim is only discoverable once a final court has ruled on the issue because, firstly, the claimant who awaits the decision of a final court has already discovered that there might be a worthwhile claim, and secondly, the claimant may bring a claim before a final court has ruled on the matter, meaning that the mistake was clearly discoverable before the judgment. The Court in *FII (No. 2)* were clearly very troubled by the result of *Deutsche Morgan Grenfell*. They stated '[o]ne might say more candidly that this approach has consequences which are illogical and which frustrate the purpose of the legislation'.[49]

[47] ibid, 165.

[48] The example given is section 11(4) with section 14(1) of the 1980 Act, pertaining to personal injuries. See also *AB v Ministry of Defence* [2012] UKSC 9. Lord Scott's dissent was not as influential as it was rather concerned with taxonomy, in that he says DMG's action is grounded in tort and therefore would not be covered under the 1980 Act.

[49] *FII (no. 2)* (n 1), [174].

On the one hand, the Court noted that discoverability is used to protect claimants whose mistake could not be reasonably foreseen until after their payment.[50] On the other hand, this is the simple reason that limitation periods exist: certainty[51] and public good.[52] The Court, for this reason, saw it as an unfortunate misstep that discoverability had been given the generous allowance of the date of the final court judgment. This allows the claimant the gift of time and certainty when he brings his claim, putting him in a 'uniquely privileged position'[53] in comparison to claimants in other cases. Further, the Court noted that the use of the limitation period in this way cannot have been what Parliament intended when enacting this Act.[54]

The court then relied on *Paragon Finance v DB Thakerar & Co* [55] to say that the burden of proof is on the claimant to show that they could not have discovered the sooner with reasonable diligence. This term is given meaning through *Law Society v Septon & Co*,[56] which provides that there is an implicit assumption that the claimant 'wants to know' whether there has been a mistake, namely there is an assumed investigative desire. This is not equivalent to actual knowledge that one has an entitlement to bring a claim.

In contrast to their treatment of *Deutsche Morgan Grenfell*, the Supreme Court upheld the decision in *Kleinwort Benson.* They discussed the 'always speaking' principle which is relevant in the consent of the 1980 Act,:

> The "always speaking" principle is also invoked where the question arises whether a statutory expression should be interpreted as including a novel invention or activity which does not naturally fall within its meaning and was not envisaged at the time of its enactment, but which may nevertheless fall within the scope of its original intention.[57]

Here we can see their Lordships grapple with the ways in which they might interpret mistakes of law in a way that would allow recovery. This is tangential to the issue at hand. A mistake of law is not a 'novel invention' of some kind that could not have been foreseen at the point of enactment of the 1980 Act (or the 1939 Act). But *Kleinwort Benson* stretches section

[50] ibid, [176].
[51] ibid, [175].
[52] ibid.
[53] ibid, [177].
[54] ibid, [179].
[55] [1999] 1 All ER 400.
[56] [2006] UKHL 22.
[57] *FII (No. 2)* (n 1), [218].

32(1)(c) to fit mistakes of law.[58] The Supreme Court thus had to tackle the question of what interpretation of the statute is most in line with the policy for which it was enacted. In doing this, they found mistakes of law to be, if the statute was given its natural meaning, within the scope of section 32(1)(c). The Court was therefore satisfied that the House of Lords in *Kleinwort Benson* was correct to widen the scope of s 32(1)(c) to allow recovery for mistakes of law.

Their Lordships were joined by Lord Lloyd-Jones and Lord Hamblen in allowing HMRC's appeal and overturning *Deutsche Morgan Grenfell* on the limitations point. Lord Briggs and Lord Sales put forward a dissenting speech, with which Lord Carnwath agreed. The dissenting judges agreed with the majority in many areas, excluding their treatment of *Kleinwort Benson*. They believed the House of Lords was, in that case, wrong to extend the ambit of section 32(1)(c) to mistakes of law, that this cannot be what Parliament intended when enacting the 1980 Act following the recommendations of the Law Revision Committee. They agreed with Lord Lloyd in *Kleinwort Benson* in thinking that '[f]acts are immutable, law is not'[59] and therefore the case to allow recovery for mistakes of law was weaker. Furthermore, they see saw decision as one that undermined commercial certainty to a great extent.[60] Nor were they persuaded by the dissent of Lord Brown in *Deutsche Morgan Grenfell,* in his attempt to strike a balance between allowing claims for mistake of law (this point was not even challenged in that case) and not allowing claimants an overly generous period in which to realise they have a worthwhile claim. They thought that not only is this not what Parliament intended, but the test put forward by Lord Brown is overly uncertain, a point, which will be revisited later.

Thus, the test arrived at by their Lordships is to ask when a reasonable person in the claimant's position could have realised that it had a worthwhile or arguable case that its understanding of the law at the time of its payment had been wrong. Under this test, the burden is on the claimant to show that they could not have reasonably discovered their mistake sooner, taking into account their access to legal acumen and resources, financial or otherwise, that could have directed them towards a finding that there is an arguable case.

F. RECEPTION AND DISCUSSION

[58] Other jurisdictions maintained that a mistake included a mistake of law. See the Australian position in *Paciocco v Australia and New Zealand Banking Group Ltd* [2014] FCA 35.
[59] *Kleinwort Benson* (n 11), [392].
[60] *FII (No. 2)* (n 1), [277].

There is much to be lauded in the Supreme Court's judgment in *FII (No. 2)*. Focus on giving effect to the purpose of the limitation period – '[ensuring] that a claimant is not disadvantaged, so far as limitation is concerned, by reason of being unaware of the circumstances giving rise to his cause of action as a result of fraud, concealment, or mistake'.[61] It has been called a 'triumph for coherence in English limitation law' by some commentators.[62] It is hard to see the position prior to *FII (No. 2)* as anything but unduly generous to claimants in allowing them to be absolutely certain of success prior to bringing a claim and gain the benefit of leaping over the time bar. Another advantage of this judgment is its conformity with the rest of the 1980 Act. Sections 11, 14A and 32(1)(a), which pertain to personal injury, latent damage, and fraud all approach the limitation period in a way that is more reasonable to the defendant than the position for mistakes post-*Deutsche Morgan Grenfell*.

In their judgment, the court pre-empted a critique of the move from a certain date towards the approach whereby a court must calculate the date at which the mistake became reasonably discoverable, namely unworkability. The minority also raised this as a reason for their dissent. They said that '[i]t is true that this approach involves a more nuanced inquiry than a mechanical test based on the date on which an authoritative appellate judgment determined the point in issue. But it would be unduly pessimistic to conclude at this stage that it will prove to be unworkable in practice, or too uncertain in its operation to be acceptable'.[63] Furthermore, the Court noted that 'deemed mistake' cases, where the mistake is a result of a judicial decision with retrospective effect, are very unusual. That being said, there is no doubt that the test proposed in *FII (No. 2)* is less certain than the position the law was in post- *Deutsche Morgan Grenfell*. That case was, for all purposes, better suited to legal practitioners who could accurately give their clients a date on which the 'clock runs'. But we should not lament the loss of certainty, particularly where greater fairness and adherence to logic has been gained. The *Deutsche Morgan Grenfell* position had allowed claimants to argue that a mistake was reasonably discoverable at a point after they had already commenced proceedings.

The restrictive approach taken in *FII (No. 2)* is consistent with recent decisions by the Supreme Court concerning unjust enrichment, though other decisions pose much more of a

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[61] *FII (No. 2)* (n 1), [193].
[62] Samuel Beswick, 'The Overpaid Tax Litigation: Roadblocked' (2021) 84 Modern Law Review 1105.
[63] *FII (No. 2)* (n 1), [212].

problem from a 'rule of law' standpoint. Earlier, reference was made to *Prudential Assurance*, a case that is worth revisiting on this point. The claimants in this case were also joined together by a GLO, evidencing the zeal with which accountancy groups have sought to challenge the legitimacy of sums paid under taxes.[64] Again, the legislation in question was held to be in violation of freedom of establishment and free movement of capital. In its tax treatment of dividends paid by non-resident subsidiaries of UK resident parent companies, it prejudiced these companies and put them at a disadvantage to UK companies. Clearly, the financial implications would be huge, if the claimants could rely on *Sempra Metals* to recover compound interest. Acutely aware of this, the Supreme Court overruled Sempra Metals and decided that compound interest was not available due to the directness rule, namely that the defendants enrichment had to arise 'at the expense of' the claimant, and added that the problems created for the defendants are not able to be fully addressed by legislation. This shows that the Supreme Court is eager to revisit and overturn key cases in unjust enrichment that had exposed defendants (usually public bodies) to significant financial damage.

Some commentators have not been convinced that the Supreme Court acting in this way is reasonable.[65] The idea that legislation would not be sufficient to address the disruption to public finances hence the need for the Supreme Court to make decisions bearing significant implications is, with respect, unconvincing. It is difficult to see why the judiciary would act in this manner, if they were not guided by concern for the taxpayer and HMRC. Seeing as judges do not have the democratic legitimacy that Parliament does, they know best that they are to develop the law from the bottom-up, working on a smaller and incremental basis. The problem, of course, is that every claimant will now have to grapple with decisions that were arrived at with a concern for public finances. Fundamentally, the savings to the government come at a social cost – a violation of the principle that there is 'no taxation without Parliament'.[66] It is alarming that the liability of HMRC to repay sums under *ultra vires* laws has been reduced, regardless of whether the sums of money at stake and the threat to public finances may justify this reasoning. That being said, it is submitted

[64] Antony Seely, 'Tax Avoidance: A General Anti-Avoidance Rule – Background History (1997-2010)' (2015) House of Commons Briefing Paper No 02956.
[65] Charles Mitchell, 'End of the Road for the Overpaid Tax Litigation?' (2019) 9 The UK Supreme Court Yearbook 225.
[66] Article 4 of the Bill of Rights 1688 provided that no tax can be levied without parliamentary approval; see also: Woolwich (n 7).

that the better course may have been legislation. This is because of an understanding in English law that the legislature when creating statutes may have regard for policy, whereas the judge when deciding a question of law may not.[67]

The biggest problem with the judgment in *FII (No. 2)* is that the Court avoided engaging with the theoretical basis on which 'deemed mistakes' are unproblematic. This is a similar criticism to the earlier one levied, with respect, on Lord Hope in *Deutsche Morgan Grenfell*. Their Lordships treated deemed mistakes as being equivalent to actual mistakes, and it is not obvious that this was the best course. Whilst it allowed the Court to simplify the reasoning and approach the issue in a more straightforward way, it has left many questions unanswered. In this regard, the arguments of the minority were more persuasive. In thinking that a mistake of law ought not to come under the ambit of section 32(1)(c), the minority effectively removed the need to differentiate between deemed mistakes and actual mistakes. According to this view, all claims of this nature would have to be brought within six years (sections 2 and 5 of the Limitation Act 1980). On this point, the minority's reasoning is more convincing not just as a matter of jurisprudence but also from a logical standpoint. The disadvantage of this, however, is that it takes us back to the position we were in prior to *Kleinwort Benson* and causes some upheaval to the law, considering that a lot of jurisprudential ink has been spilled (and parties' money spent) in deciding that mistakes of law ought to be able to ground recovery. To essentially run in a circle by returning to a position in which only mistakes of fact are recoverable would be unsatisfying yet rewarding by accepting that the prior position was better in terms of adherence to logic.

G. CONCLUSION

At the cost of losing some certainty, the judgment in *FII (No. 2)* has brought the law to a much more balanced position. The journey that parties, practitioners, and judges have travelled in the overpaid tax cases has been long, expensive, and, at times, unsatisfying. It appears that the law in this area is starting to settle, and the threats to public finances have been assuaged, to a large extent. In this way, *FII (No. 2)* represents a balanced and fair step taken by the Supreme Court. Prior positions were claimant-friendly to an unsustainable degree. Some would argue that this is justifiable given they were taxpayers, whose money was paid under an invalid law. The judgment

[67] Ronald Dworkin, *Law's Empire* (Harvard University Press 1986) 113.

however falls short of satisfying, when it avoids the complex theoretical issues surrounding the legitimacy of a deemed mistake, which the Supreme Court was in the best position to decide.