Appeal number: FTC/91/2011
FTC/92/2011
[2013] UKUT 0105 (TCC)

TAX CREDIT – Foreign income dividends – Claim by Trustees of exempt approved pension scheme – FIDS received from UK resident companies – ICTA 1988 s.231
TAX CREDIT – Cross-border dividends – Claims for tax credits based on ECJ decision in Manninen (Case C-319/0)2 – ICTA 1988 s.231
LIMITATIONS – Tax credit claims – Whether out of time – TMA s.43(1)

UPPER TRIBUNAL
(TAX AND CHANCERY CHAMBER)

THE TRUSTEES OF THE BT PENSION SCHEME	**Appellant and Respondent**
- and -	
THE COMMISSIONERS FOR HER MAJESTY'S REVENUE & CUSTOMS	**Respondents and Appellants**

TRIBUNAL: The President
The Hon. Mr Justice Warren
Judge Timothy Herrington

Sitting in public in London on 17, 18, 19, 20, 23 and 24 July 2012

Christopher Vajda QC and Conrad McDonnell, instructed by Pinsent Masons LLP for the Appellant

Rupert Baldry QC and James Rivett, instructed by the General Counsel and Solicitor to HM Revenue and Customs, for the Respondents

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ANNEX A

Background to BTPS and Hermes

ANNEX B

The Relevant Provisions Of The UK Tax Code

DECISION

I Introduction

1. These are appeals by the trustees of the BT Pension Scheme ("**the Scheme")** and by the Commissioners for Her Majesty's Revenue and Customs ("**HMRC**") from the decision of the Tax Chamber of the First-tier Tribunal (Sir Stephen Oliver QC and Julian Ghosh QC) ("**the Decision**" and "**the Tribunal**") released on 21 December 2011. There is a cross-appeal by the Respondents ("**HMRC**"). Until 2006, the trustees of the Scheme were a group of individuals. Since 14 December 2006, there has been a sole corporate trustee, BT Pension Scheme Trustees Limited. We will refer to the Scheme and to the trustees without distinction (save where necessary) as "**BTPS**". Since all of the material events relating to this appeal occurred before the Treaty of Lisbon, we adopt the Tribunal's approach of using pre-Lisbon terminology, that is we refer to the European Community ("**the EC**") rather than the European Union and to Community law; and we use the pre-Lisbon numbering in the EC Treaty.

2. There are three issues in the appeals. They are the same issues which were the subject matter of the Decision and which were identified by the Tribunal in this way:

> (1) whether BTPS is entitled to a payment of a tax credit under section 231 Income and Corporation Taxes Act 1988 ("ICTA") for certain dividends elected to be "Foreign Income Dividends" ("FIDs") within section 246A ICTA, which BTPS received from UK resident companies between 1st July 1994 and 2nd July 1997: we refer to these claims made by BTPS as the "FIDs claims";
>
> (2) whether BTPS is entitled to a payment of a tax credit under section 231 ICTAfor dividends paid by non-UK resident companies between 1st July 1990 and 2nd July 1997: we refer to these as "the Manninen claims" since these claims arise from the case law of the European Court of Justice, concerning the application of the EC Treaty ("the Treaty") to cross-border dividends, which commenced with the European Court's judgment in Case C-319/02 Manninen [2004] ECR I-7477, ("Manninen"); and
>
> (3) to the extent that the FIDs claims and the Manninen claims are good, in principle, whether these claims have been made in time ("the limitation issue").

3. The FIDs claims relate to dividends paid by UK tax-resident companies to BTPS which are funded out of non-UK source income by the dividend-paying companies; that non-UK source income arises both from sources located within the EC and from sources located in states outside the EC ("third countries"), so far as the dividend-paying companies are concerned. The Manninen claims relate to dividends paid by companies tax-resident within both Member States and third countries.

4. The Tribunal decided both the FIDs issue and the Manninen issue in favour of BTPS. Specifically, the Tribunal held that the domestic law provisions which denied BTPS any entitlement to a payment in respect of a tax credit had to be disapplied or given a conforming construction to give effect to BTPS's rights under Article 56 of the Treaty. HMRC appeal against the Tribunal's decision on both those issues. The Tribunal decided the limitation issue in favour of HMRC and BTPS appeal that part of the Tribunal's decision. Permission to appeal was granted to both parties by Sir Stephen Oliver QC on 25 October 2011.

5. The parties agreed that quantum be left to be decided after the determination of the questions of law so the Tribunal has not yet considered quantum issues.

6. Christopher Vajda QC and Conrad McDonnell appeared on behalf of BTPS. Mr Vajda presented the case for BTPS on the issues relating to the FIDs claims, the Manninen claims and the Community law issues relating to the limitation issue. Conrad McDonnell presented the case for BTPS on Community law issues relating to effective fiscal supervision and the domestic law issues relating to the limitation issue. Rupert Baldry QC and James Rivett appeared on behalf of HMRC.

II The Facts

7. There was an agreed statement of facts on the basis of which the Tribunal made its findings of fact. The Tribunal set out the agreed statement (omitting certain immaterial sections) in paragraphs 6 to 21 of the Decision. For convenience and completeness we set out those paragraphs of the Decision in Annex A to this decision.

III The UK Tax System

8. The parties produced for the Tribunal a summary of the uncontroversial aspects of the UK's legislation regarding corporation tax and the taxation of dividends during the relevant era from July 1990 to 1997. That summary was set out in paragraphs 22 to 31 of the Decision. It was not referred to significantly in this appeal, but we were taken to a similar (and if we may say so more succinct) overview of all the relevant provisions contained in the first instance decision in *Test Claimants in the FII Group Litigation v Revenue and Customs Commissioners* [2008] EWHC 2893 (Ch) ("***FII GLO***"). This decision considered a number of issues arising out of the preliminary ruling of the European Court of Justice ("ECJ") in *Test Claimants in the FII Group Litigation Order v Inland Revenue Commissioners* (Case C-446/04) ("***FII ECJ***"). The analysis of the UK legislation in *FII ECJ* formed the basis of the summary just referred to.

9. In paragraph 12 of his decision in *FII GLO*, Henderson J explained that from 1965 (when corporation tax was introduced) until 1973 the UK operated a "classical" system of corporation tax. Under the classical system, the profits of a company were subject to corporation tax and, as a quite separate matter, dividends paid to non-corporate shareholders were taxed in their hands.

10. He then explained that in 1973 the UK moved from the classical system to a partial "imputation" system. Under the partial imputation system a UK-resident company paid corporation tax on its profits but part of the corporation tax was imputed to non-corporate shareholders in the event of the profits being distributed to them. A UK-resident company was in principle obliged to pay advance corporation tax ("**ACT**") when it made a distribution (typically, by paying a dividend) to its shareholders, even if it had no corporation tax liability, and its UK-resident non-corporate shareholders (and certain entities such as pension funds) received a tax credit which could be set against their tax liability on the dividend or paid to them in cash if the credit exceeded their liability. He went on to give some further broad descriptions about the operation of ACT, surplus ACT and tax credits.

11. He then described the arrangements in detail in paragraphs 14 to 28 of his judgment which we set out in full:

“ACT and franked payments

[14] Where a UK-resident company made a qualifying distribution it was liable to pay ACT on the distribution: ICTA, s.14(1). The sum of the amount of the distribution and the ACT was called a franked payment: s.238(1). Before 6 April 1993, the rate of ACT was linked to the basic rate of income tax. For example, from 1988 to 5 April 1993, when the basic rate of income tax was 25%, the ACT rate was 25/75 (or 1/3) of the amount of the distribution. Between 6 April 1993 and 5 April 1994 the ACT rate was set at 22.5/77.5 (or 9/31). From 6 April 1994 until 5 April 1999 the ACT rate was linked to the lower rate of income tax: s.14(3). At that time the lower rate of income tax was 20%. The ACT rate was therefore 20/80 (or ¼).

Tax Treatment of dividends received by individuals and exempt entities

[15] Income tax was charged under various “Schedules” for different types of income. This is a peculiar feature of the UK tax system. Under Sch F (s.20) individual shareholders were liable to income tax on dividends and other distributions received. A UK-resident individual in receipt of a qualifying distribution from a UK-resident company was entitled to a tax credit equal to such proportion of the amount or value of the distribution as corresponded to the rate of ACT: s.231(1). Income tax was chargeable on the total of the distribution and the tax credit: s.20(1). The tax credit extinguished all or part of the taxpayer’s liability. Lower-rate taxpayers and non-taxpayers (e.g. taxpayers whose income did not exceed the personal allowances) could recover some or all of the tax credit in cash. Entities not subject to UK tax on investment income, e.g. pension funds, could before 2 July 1997 claim payment in full of the tax credit on dividends received.

Tax treatment of dividends received by companies

[16] A UK-resident company was subject not to income tax but to corporation tax: s 6(2). However, corporation tax was not chargeable on dividends and other distributions received from another UK-resident company, nor were such payments taken into account in computing the corporation tax liability of the company making the distributions. This follows from s. 208, which provides as follows:

“Except as otherwise provided by the Corporation Tax Acts, corporation tax shall not be chargeable on dividends and other distributions of a company resident in the United Kingdom, nor shall any such dividends or distributions be taken into account in computing income for corporation tax”

[17] A UK-resident company was, by contrast, subject to corporation tax on dividends received from non-resident companies. Such tax was charged under Case V of Sch D, set out in s 18, being:

‘tax in respect of income arising from possessions out of the United Kingdom not being income consisting of emoluments of any office or employment…’

The company was, however, granted relief for foreign taxes paid. Such relief was given either unilaterally under domestic rules (s 790) or under double taxation conventions entered into with other countries (s 788). The unilateral arrangements provided for the crediting against a company’s UK corporation tax liability of withholding taxes paid on foreign dividends. Where the UK-resident company either directly or indirectly controlled, or was a subsidiary of a company which directly or indirectly controlled, not less than 10% of the voting power of the company paying the dividend, the relief extended to the underlying foreign corporation tax on the profits out of which the dividends were paid, including underlying tax incurred by lower-tier companies (s 801). The foreign tax was creditable only up to the amount of the UK corporation tax liability

on the particular income. Similar arrangements generally applied under the UK's double taxation treaties with other countries: see, for example, the treaties with France, Spain and the Netherlands.

[18] The standard clause in such treaties, reflecting s 790(4) is usually to be found in the 'Elimination of Double Taxation' article. So, for example, art 22(b) of the UK-Netherlands Double Taxation Treaty reads:

'where such income is a dividend paid by a company which is a resident of the Netherlands to a company which is a resident of the United Kingdom and which controls directly or indirectly not less than one-tenth of the voting power in the former company, the credit shall take into account (in addition to any Netherlands tax payable in respect of the dividend) the Netherlands tax payable by that former company in respect of its profits'

Franked investment income

[19] A UK-resident company receiving a qualifying distribution from another UK-resident company was entitled to a tax credit: s 231(1). The total of the distribution and the tax credit was called franked investment income ('FII'): s 328(1). A UK-resident company receiving a distribution from a non-resident company was not entitled to a tax credit, and the income did not qualify as FII. Where a UK-resident company received FII, it was liable to pay ACT in relation to its own dividends only to the extent that those dividends and the ACT referable to them (ie its franked payments) exceeded the FII: s 241. Special arrangements applied under s 247 to dividends paid between UK-resident members of groups of companies. Provided that they satisfied certain minimum holding requirements – broadly speaking, the requirement was that more than 50% of the shares of the company paying the dividend had to be held by the parent – the UK-resident subsidiary and its UK-resident parent could make an election (called a group income election) under which dividends could be paid to the parent by the subsidiary without its having to account for ACT. Where a group income election was in force, the payment of dividends under it did not entitle the parent company to a tax credit, and the dividends were not included within its FII. The effect of a group income election was to postpone the payment of ACT until a distribution was made by the parent company.

Set-off and surrender of ACT

[20] A company was entitled to set ACT paid in respect of a qualifying distribution during an accounting period against its mainstream corporation tax ('MCT') liability for that and future periods. There was, however, a limit on the amount which could be set off based on the income tax rate (see at [14] above). Since the UK operated a partial imputation system, so that the UK corporation tax rate exceeded the ACT set-off rate, the company always faced a marginal corporation tax liability on its profits. Moreover, where a company received credit for foreign tax this reduced the amount of the corporation tax liability available for set-off of ACT: s797(4). Unrelieved ACT, known as 'surplus ACT', could be carried back or forward for set-off against MCT of other periods: s 239.

[21] A company was also permitted to surrender to its subsidiaries the benefit of ACT payments it had made: s 240. The subsidiaries to whom the surplus ACT could be surrendered were restricted to subsidiaries resident in the UK: s 240(1). The subsidiaries were then able to set the surrendered ACT against their own UK MCT liability.

[22] A company with surplus FII (that is, FII which exceeded franked payments) could, if it had losses, set the amount of those losses against the surplus FII under s 242 and

obtain a payment in cash of the tax credit comprised in that amount of surplus FII. This provision was abolished with effect from 2 July 1997.

The FID regime

[23] Experience with the arrangements described above showed that companies receiving significant foreign dividend income generated surplus ACT. This was because:

(i) foreign dividends did not attract a tax credit and therefore did not create FII which could be used to reduce the companies' ACT liability on distributions made by them; and

(ii) any credit given for foreign tax reduced the MCT liability against which the ACT could be set off.

Arrangements were introduced with effect from 1 July 1994 under which a UK resident company could elect that a cash dividend which it paid to its shareholders was a FID: ss 246A to 246Y. The election had to be made by the date the dividend was paid and could not be revoked after that date. ACT was payable on the FID but, if the company could match the FID with foreign profits, a claim for repayment could be made for ACT arising in respect of the FID.

[24] The reclaimed ACT became repayable at the same time as the MCT became payable, ie nine months after the end of the accounting period, and was set first against any MCT liability for the period and any excess was then repaid. As ACT was paid 14 days after the end of the quarter in which the dividend was paid, and the MCT was payable nine months after the end of the accounting period, this meant that ACT would remain outstanding under the FID system for between 8.5 and 17.5 months depending when the dividend was paid in that accounting period.

[25] A FID did not constitute FII, although a corporate shareholder could use a FID received by it to frank a FID paid, so that ACT was payable only on the excess of FIDs paid over FIDs received. Because a FID did not constitute FII the shareholder receiving the FID was not entitled to a tax credit under s 231 (1); but an individual receiving a FID was nevertheless treated as receiving income which had borne tax at the lower rate for the year of assessment. However, no repayment was made to individual shareholders of income tax treated as having been paid, nor could a tax exempt shareholder such as a UK pension fund reclaim a tax credit similar to that which would have been payable on a non-FID qualifying distribution.

Abolition of the ACT regime

[26] For distributions made on or after 6 April 1999, the ACT system was abolished. Companies no longer had to pay or account for ACT on shareholder dividends and other qualifying distributions. The FID rules were also abolished.

[27] For companies with brought-forward surplus ACT, a 'shadow ACT' system was introduced. The shadow ACT regulations allowed companies to access to their surplus ACT in an amount broadly similar to the relief allowable under the old rules. This meant that surplus ACT could only be utilised after the shadow ACT was notionally used and exhausted.

[28] UK-resident individuals now receive dividends with a tax credit equal to one-ninth of the dividend. The tax credit extinguishes lower and basic rate income tax liability on the dividend.

12. BTPS helpfully provided us with worked examples of how the provisions operated in practice and these are set out in paragraphs 14 and 15 below. The first example relates to the scenario that is the subject of the FIDs claims, that is where BTPS has invested in a UK resident company which has a non-UK resident subsidiary that makes a distribution to its parent which is subsequently distributed to BTPS as a FID. This example also shows by comparison the position where BTPS receives a dividend representing dividends received by the same UK resident company from a UK subsidiary, and also where it receives a dividend from a company which has not made a FID election in respect of dividends received from its non-UK resident subsidiaries. The second example relates to the scenario that is the subject of the *Manninen* claims, that is where BTPS has invested directly in a non-UK resident company and receives a dividend from that company. This also example shows by comparison the position where BTPS invests directly in a UK resident company and receives a dividend from that company.

13. The examples are based on the tax year 1996-1997 when the following tax rates were in effect:

Corporation Tax	33%	
ACT	20%	(based on the grossed-up dividend)
Lower rate of income tax	20%	(based on the grossed-up dividend)

The examples assume a company which earns profits of £100 per share before tax and decides to distribute all of its after-tax profits.

14. Examples relating to FIDS claim

(a) UK subsidiary of UK parent (for comparison)

	Income	*Tax cost*
UK subsidiary profits before tax	£100	
UK corporation tax:	(£33)	£33
UK subsidiary distribution to UK parent: (No ACT: group income election made)	£67	
(No corporation tax for UK parent: s.208 ICTA 1988)		
Available to distribute to UK exempt shareholder	£67	
ACT on distribution by UK parent	£16.75	

(of which, £16.75 is surrendered to the subsidiary and set off against its UK corporation tax liability already shown above, so no net tax cost) [1]

UK exempt shareholder receives dividend:	£67	
Plus section 231 ICTA tax credit paid by HMRC	£16.75	(£16.75)
Total receipt of UK exempt shareholder	**£83.75**	

(b) Foreign subsidiary of UK parent, FID election was made (assumes overseas company pays corporation tax at 30% on its profits)

	Income	*Tax cost*
Overseas company profits before tax:	£100	
Overseas corporation tax	(£30)	£30
Overseas company distribution to UK parent	£70	
UK parent's corporation tax on that :	(£3)	£3
(33% of the grossed up amount which is £100 including a £30 credit for the foreign underlying tax: s. 795 ICTA)		
Available to distribute to UK exempt shareholder	£67	
ACT on distribution	£16.75	
(of which, £3 meets the corporation tax liability already shown above and £13.75 is available for repayment to the company, so no net tax cost.)		
UK exempt shareholder receives:	£67	
No tax credit for UK exempt shareholder		
Total receipt for UK exempt shareholder	**£67**	

(c) Foreign subsidiary of UK parent, no FID election, for comparison

	Income	*Tax cost*
Overseas company profits before tax:	£100	
Overseas corporation tax	(£30)	£30
Overseas company distribution to UK parent:	£70	
UK parent's corporation tax on that:	(£3)	£3
(33% of the grossed up amount which is £100 including a £30 credit for the foreign underlying tax: s. 795 ICTA)		
	Income	*Tax cost*
Available to distribute to UK exempt shareholder	£56	
(that is £67 less the cost of surplus ACT to be borne by the company)		
ACT on distribution	£14	£11
(of which £3 meets the corporation tax liability already shown above and £11 is surplus ACT)		
UK exempt shareholder receives:	£56	
Tax credit for UK exempt shareholder:	£14	(£14)
Total receipt of UK exempt shareholder:	**£70**	

15. Examples relating to the *Manninen* Claims

(a) Investment in UK company, for comparison

	Income	*Tax cost*
UK company profits before tax:	£100	
UK corporation tax	(£33)	£33
UK company distribution:	£67	
ACT payable by UK company on distribution:	£16.75	
(no tax cost shown, because this ACT is fully set off against corporation tax)		
UK exempt shareholder receives:	£67	
s.231 ICTA 1988 tax credit on this dividend	£16.75	
Total receipt of UK exempt shareholder:	**£83.75**	

5 (b) Investment in foreign company (assumes overseas corporation tax rate of 33% to match the UK rate)

	Income	*Tax cost*
Overseas company profits before tax:	£100	
Overseas corporation tax	(£33)	£33
Overseas company distribution: (or less if there is foreign withholding tax)	£67	
No s.231 ICTA tax credit on this dividend		
Total receipt of UK exempt shareholder	**£67**	

16. There is one further point of detail relating to the operation of the FIDs regime which was not referred to in Henderson J's summary of the regime but was referred to in the Tribunal's agreed description of the UK tax system. This was the fact that some companies which paid FIDs enhanced the amount of their dividends, effectively 10 to compensate tax exempt shareholders such as BTPS for the fact that they were not entitled to a tax credit in respect of the FIDs. The enhancement was not always for the full amount of what would have been the tax credit on an ordinary dividend. In the example given in paragraph 14(b) above, relating to the payment of a FID, £67 is shown as available to distribute compared to £56 in respect of a company not making 15 a FID election as in the example given in paragraph 14(c) above. Therefore the £67 dividend is an "enhanced" dividend because it is more than the £56 payable if no FID election had been made. "Full" enhancement would have been for the company to pay a dividend of £70 in the case of a FID election, that is based on a dividend of £56 if no FID election were made and the equivalent of a £14 tax credit on it.

IV The UK legislation

17. We set out in Annex B to this decision the provisions of the UK tax legislation which are the subject of the FIDs claims and the *Manninen* claims respectively.

5 18. The FIDs claims concern tax credits conferred by section 231 (1), (3) ICTA and the disallowance of the tax credits by section 246C ICTA for dividends elected by the paying company to be FIDs. BTPS claims that the disallowance effected by section 246C of ICTA breaches its rights to the free movement of capital. The *Manninen* claims relate to the requirement that the tax credits conferred by section 231(1), (3) 10 ICTA are restricted to dividends paid by UK tax resident companies. BTPS claims that the non-availability of tax credits for dividends paid by non-UK tax resident companies also breaches its rights to the free movement of capital.

V Community law

19. In Sections E and F of the Decision, the Tribunal gave a description of the EC 15 legislation under the headings "The Relevant European Community Law" and "1992 Agreement on the European Economic Area". What follows in this Section V of our own decision is taken largely verbatim from those Sections of the Decision.

20. So far as the legislation is concerned, the relevant provisions are those that relate to the movement of capital.

20 21. Between 1 July 1990 and 31 December 1993, Directive 88/361/EEC ("the Capital Directive") provided directly effective rights relating to the free movement of capital. The relevant provisions are as follows:

(1) Article 1 provided:

> "1. Without prejudice to the following provisions, Member States shall 25 abolish restrictions on movement of capital taking place between persons resident in Member States. To facilitate application of this Directive, capital movements shall be classified in accordance with the Nomenclature in Annex 1…."

(2) Article 6 provided:

> 30 "1. Member States shall take the measures necessary to comply with this Directive no later than 1 July 1990. They shall forthwith inform the Commission thereof. They shall also make known, by the date of their entry into force at the latest, any new measure or any amendment made to the provisions governing the capital 35 movements listed in Annex 1."

(3) Heading III of the Nomenclature in Annex 1 included the following in the various classifications of capital movements:

> "A – Transactions in securities on the capital market
>
> 1. Acquisition by non-residents of domestic securities dealt in on 40 a stock exchange.

2. Acquisition by residents of foreign securities dealt in on a stock exchange.

3. Acquisition by non-residents of domestic securities not dealt in on a stock exchange.

5 4. Acquisition by residents of foreign securities not dealt in on a stock exchange."

22. The Capital Directive contained directly enforceable rights which secured the intra-Community free movement of capital. These rights did not (in contrast to Article 56 of the EC Treaty: see below) relate to capital movements between Member
10 States and third countries.

23. Article 56 of the EC Treaty (Free Movement of Capital) ("**Article 56**") replaced the Capital Directive with direct effect, from 1 January 1994. Article 56 provided that:

> "1. Within the framework of the provisions set out in this Chapter, all
> 15 restrictions on the movement of capital between Member States and between Member States and third countries shall be prohibited…"

Thus Article 56 extended the rights which guarantee free capital movement to capital movements between member States and third countries.

24. Article 58 provided:

> 20 "1. The provisions of Article 56 shall be without prejudice to the right of Member States:
>
> (a) to apply to the relevant provisions of their tax law which distinguish between taxpayers who are not in the same situation with regard to their place of residence or with regard to the place where the capital is invested:
>
> 25 (b) to take all requisite measures to prevent infringements of national law and regulations, in particular in the field of taxation and the prudential supervision of financial institutions, or to lay down procedures for the declaration of capital movements for the purposes of administrative or statistical information, or to take measures which are justified on grounds of public policy
> 30 or public security.
>
> 2. The provisions of this Chapter shall be without prejudice to the applicability of restrictions on the right of establishment which are compatible with this Treaty.
>
> 3. The measures and procedures referred to in paragraphs 1 and 2 shall not
> 35 constitute a means of arbitrary discrimination or a disguised restriction on the free movement of capital and payments as defined in Article 56."

25. By virtue of Article 40 of the 1992 Agreement on the European Economic Area ("**the EEA**") these procedures were extended to residents of member states of the EEA. We therefore proceed on the basis that our conclusions on the application of the

relevant European Community Law ("Community law") should be taken to apply equally to movements in capital involving residents in EEA member states.

VI Issues to be Determined

26. Put simply, the central issue to be determined in these appeals is encapsulated in the following two questions:

(1) Whether the absence of a tax credit for FIDs, by reason of section 246C ICTA, constitutes a breach of Article 56; and

(2) Whether the provisions of section 231 (1) ICTA which restrict tax credits on dividends to dividends received from UK-resident companies were in breach of Article 56 and previously of Directive 88/361/EEC.

27. If we decide the first question in the negative, the result will be that BTPS's claims for repayment of tax credits in relation to the FIDs claims will fail. If we decide the second question in the negative, BTPS's claim for payment of tax credits in relation to the *Manninen* claims will fail.

28. If we decide either or both of the two questions in favour of BTPS then we will then need to determine what the correct remedy is for the breach of Article 56.

29. Allied to the question of remedies, we need also to consider arguments raised by HMRC that if any breaches of Article 56 are found, they can be justified on the grounds of the need for "effective fiscal supervision" based on an asserted need to verify the amount of tax paid abroad in respect of the dividend income to which the tax credits claimed relate.

30. Finally, we need to consider the extent to which any of the claims are subject to a limitation period and so are out of time.

31. In relation to these issues the Tribunal held:

(1) Article 56 prohibited the UK from applying a tax treatment to dividends (FIDs) from companies investing in overseas subsidiaries which was less favourable than the tax treatment of dividends from companies investing in UK subsidiaries, and was thus liable to dissuade investment by pension funds in the former category of companies. The absence of a tax credit for FIDs, by reason of section 246C ICTA, constituted a *prima facie* breach of Article 56.

(2) The breach of Article 56 EC was not justified.

(3) On the question of remedies, but subject to questions of time limits (as to which see (5) below), section 246C ICTA fell to be disapplied for the purposes of determining BTPS's claims.

(4) Section 231(1) ICTA, in restricting tax credits on dividends to dividends received from UK-resident companies, was a clear breach of Article 56 and previously of Directive 88/361/EEC.

(5) On the question of remedies, but subject again to questions of time limits, section 231 ICTA should be construed in a manner which permitted the same

tax credits to be claimed on dividends received from companies resident in the EC but not in the UK as were available in relation to UK-resident companies.

(6) On limitation points, section 43 TMA specified a time limit of 6 years for claims to receive payable tax credits. Accordingly, most of the FIDs claims made by BTPS, and all of the *Manninen* claims, were properly rejected by HMRC on the basis that they were submitted out of time.

(7) In relation to the issue of justification of *prima facie* breach of Article 56 on the grounds of 'effective fiscal supervision' (which was only argued in respect of dividends from third countries):

(a) in relation to the FIDs claims, 'effective fiscal supervision' could not justify any difference between dividends from EC and non-EC sources and therefore, subject to limitation points, BTPS was in principle entitled to receive payable tax credits on all FIDs, that is to say both where the underlying income was from EC sources and where it was from non-EC sources;

(b) in relation to the *Manninen* claims, no concluded view was expressed on justification in relation to dividends received from companies resident in non-EC countries, other than as noted in (c) below;

(c) however, in the case of dividends from companies resident in a state within the EEA, and for periods from 1 January 1994 when the EEA Agreement was in force, its conclusions on the application of Article 56 to dividends from other EC Member States should be taken to apply equally to the application of Article 40 of the EEA Agreement prohibiting restrictions on the free movement of capital within the EEA.

32. Before the hearing commenced, we raised with the parties whether we should consider making a reference to the ECJ on any of the issues raised in these appeals. After hearing from the parties on this question it was agreed that, if we considered that a reference was necessary, the appropriate time to make one would be after the hearing of the appeals. We return to this aspect of the appeal at the end of this decision. In sections VII to X below, we discuss the FIDs claims, the *Manninen* claims and the Limitation issue. We express conclusions on each of those issues as we go along, including where necessary, conclusions on matters of Community law. Our conclusions on Community law are to be taken as subject to what we have to say in section XI headed "Reference to the ECJ".

VII FIDS and *Manninen* claims: the underlying principles of Community law

33. Before embarking on our discussion of the issues it is helpful to adopt the course adopted by the Tribunal, namely to examine some of the underlying principles of Community law that can impact on the national legislation of Member States through which they exercise their powers to levy taxes.

34. The primary objective of the Treaty is to establish an internal market (see Article 3 of the treaty). The Capital Directive and Article 56 form part of the "fundamental freedoms" which seek to achieve this objective. These fundamental freedoms are the free movement of goods: Articles 23-31, the free movement of workers: Articles 39 – 42, the free movement of persons: Articles 43-48 and the free movement of capital and payments: Articles 56-60, which as we observed in paragraph 23 above replaced the Capital Directive with effect from 1 January 1994.

35. As observed in paragraph 21 above Annex I to the Capital Directive set out a Nomenclature providing a list of classification of movements of capital, which included acquisitions of listed and unlisted securities where there was a cross-border element, either because the acquisition was by a non-resident of domestic securities or because it was by a resident of foreign securities. This is to be contrasted with a "wholly internal situation" within a single Member State which does not give rise to rights under Article 56: see the decision of the ECJ in Case C112-91 *Hans Werner v Finanzamt Aachen-Innenstadt* [1993] ECR I-00429 ("***Werner***").

36. Although the Capital Directive is no longer in force having been replaced by Article 56, it is common ground before us, as it was before the Tribunal, that the Nomenclature remains relevant for the purpose of identifying the types of capital movement that are protected by Article 56, and that it is not exhaustive as regards the notion of movements of capital: see the decision of the ECJ in Case C-450/09 *Ulrich Schroder v Finanzamt Hameln* [2011] ECR I-02497 at paragraph 25.

37. Consequently BTPS claims that both its investments in the securities of UK resident companies that pay FIDs and its direct investments in companies resident in other Member States and third countries which pay it dividends have necessarily involved movements of capital and are protected by Article 56. The former are the subject of the FIDs claims, and the latter are the subject of the *Manninen* claims on the basis that these investments are made less attractive than purely domestic investments by reason of what BTPS maintains is discriminatory treatment of FIDs and cross border dividends by the UK tax legislation.

38. It is common ground that the investments that are the subject of the *Manninen* claims represent a movement of capital by BTPS within the scope of the protection of Article 56, but HMRC dispute that the investments that are the subject of the FIDs claims fall within its scope, maintaining that this is a "wholly internal situation."

39. It is also common ground that Article 56 creates directly enforceable rights so that those whose rights are breached can rely on such breach to found an action under Community law. In so far as sections 231 and 246C ICTA are found to have breached those rights those provisions are to be treated, by virtue of section 2(4) of the European Communities Act 1972, as being without prejudice to those rights and the provisions are to be construed and take effect subject thereto: see *R v Secretary of State for Transport, ex parte Factortame Ltd* [1990] 2 AC 85 at page 140, per Lord Bridge.

40. Although direct taxation itself did not fall within the scope of the legislative powers of the EC regarding the internal market (and does not now fall within the scope of the same powers of the EU), national tax legislation must nonetheless be compatible with any relevant EC law. This principle has been stated in a number of judgments of the ECJ, for example in Case C-105/05 *Skatteverket v A* [2007] ECR I-11531 where the court stated at paragraph 19:

> "As a preliminary point, it is to be noted that, according to settled case-law, although direct taxation falls within their competence, the Member States must none the less exercise that competence consistently with Community Law (Case C-35/98 *Verkooijen* [2000] ECR I-4071, paragraph 32; Case C-319/02 *Manninen* [2004] ECR I-7477, paragraph 19; and Case C-292/04 *Meilicke and Others* [2007] ECR I-1835, paragraph 19)."

41. There is a line of cases from the ECJ which essentially addresses the tension between the fiscal autonomy of the Member States in relation to their direct taxing powers and the requirement of Community law that those powers must not be exercised in a way which discriminates against cross border investment in favour of investment in domestic securities.

42. An early example of the tension between these two principles is to be found in the ECJ's judgment in Case C-204/90 *Bachmann v Belgium State* [1992] ECR I-249. Briefly, the facts in that case were that Mr Bachmann, a German national, concluded various insurance and pensions contracts in Germany. A year later he took up residence and employment in Belgium and when completing his Belgium tax returns deducted from his income his contributions to the various contracts referred to above. These deductions were refused by the Belgian tax authorities because national legislation only permitted deductions made in respect of payments made to product providers in Belgium. The rationale for this apparent discrimination between Belgian and German schemes was that a deduction was available for payments to a Belgian scheme because the benefits that were paid out were taxed in Belgium, whereas if a deduction were allowed in respect of payments to a German scheme, there would be no corresponding tax in Belgium on the benefits paid in Germany.

43. Mr Bachmann argued that the difference in treatment infringed his rights to free movement to work and free movement of capital, the latter being infringed, he argued, because the legislation prompted those resident in Belgium considering such schemers to apply for them exclusively with Belgian companies.

44. These arguments failed, the ECJ finding in paragraph 35:

> "Consequently the answer to the question submitted by the national court is that legislation of a Member State which makes the deductibility of sickness and immobility insurance contributions and pensions and life assurance contributions conditional on these contributions being paid in that State is contrary to Articles 48 and 59 of the treaty. However, that condition may be justified by the need to preserve the cohesion of the applicable tax system. Such legislation is not contrary to Articles 67 and 106 of the EEC treaty."

45. Thus it can be seen that the ECJ, whilst accepting that the provisions of the Belgian tax legislation did infringe the relevant freedoms, those provisions might be (and in that case actually were: see paragraph 28) justified on the basis of preserving the cohesion of the Belgian tax system, namely that there should be symmetry between the ability within a Member State to obtain a deduction for contributions and the ability of the Member State to tax the benefits which arose out of those contributions. Although expressed in terms of fiscal cohesion, in our view this is an illustration of the wider principle of fiscal autonomy.

46. It appears however that the fiscal cohesion argument has been confined to circumstances such as those in *Bachmann* where only one taxpayer is involved. In later cases involving the taxation of shareholders receiving distributions from companies the argument has not found favour with the ECJ.

47. In Case C-35/98 *Staatssecretans Van Financien v Verkooijen* [2000] ECR I-4071 the issue for consideration was whether a provision in the tax legislation of the Netherlands which gave an exemption from income tax for dividends paid to shareholders who were individuals up to a limited amount on condition that those

dividends were paid by a company whose seat was in the Netherlands was compatible with the provisions of the Directive concerning free movement of capital. Under Netherlands tax law, dividends when distributed by a company with its seat in the Netherlands are subject to a deduction at source by way of income tax; tax collected in that way is known as dividend tax and can be set off by the recipient against his total tax bill when his aggregate income is assessed, being treated as a payment on account of income tax.

48. The facts of the case, so far as relevant, were that Mr Verkooijen, a Netherlands resident, was employed by a Dutch subsidiary of a Belgian parent company. In the context of an employees' savings plan Mr Verkooijen acquired shares in the Belgian parent and received dividends from that company. When assessing Mr Verkooijen's income for tax in the Netherlands, the tax inspector did not apply the exemption for dividends referred to above since the dividends had not been subject to Netherlands dividend tax.

49. The ECJ held that the provision restricting the exemption to dividends received from companies who had their seat in the Netherlands constituted a restriction on capital movements prohibited by the Directive. The reasoning of the court was set out in paragraph 34-36 of the judgment as follows:

> "34. A legislative provision such as the one at issue in the main proceedings has the effect of dissuading nationals of a Member State residing in the Netherlands from investing their capital in companies which have their seat in another Member State. It is also clear from the legislative history of that provision that the exemption of dividends, accompanied by the limitation of that exemption to dividends on shares in companies which have their seat in the Netherlands, was intended specifically to promote investments by individuals in companies so established in the Netherlands in order to increase their equity capital.
>
> 35. Such a provision also has a restrictive effect as regards companies established in other Member States: it constitutes an obstacle to the raising of capital in the Netherlands since the dividends which such companies pay to Netherlands residents receive less favourable tax treatment than dividends distributed by a company established in the Netherlands, so that their shares are less attractive to investors residing in the Netherlands than shares in companies which have their seat in that Member State.
>
> 36. It follows that to make the grant of a tax advantage, such as the dividend exemption, relating to taxation of the income of natural persons who are shareholders subject to the condition that the dividends are paid by companies established within national territory constitutes a restriction on capital movements prohibited by Article 1 of Directive 88/361."

50. The ECJ rejected arguments from the Netherlands Government that the restriction of the exemption to dividends illustrated by companies with their seat in the Netherlands was justified by the need to preserve the cohesion of the Netherlands tax system. It is to be noted also that paragraph 35 shows that the right to free movement of capital is capable of preventing tax measures which apply a different tax treatment to the **income** derived from overseas investments compared with that applicable to the income from investments in the Member State of residence.

51. The Netherlands Government argued that the exemption is restricted because only Netherlands based companies are taxed in the Netherlands on the profits they

realise and where the company paying the dividends is established in another Member State profits are taxed in the latter state with the result that in the Netherlands, there is no double taxation to be compensated for. Furthermore they submitted, the tax levied in the other Member State on the foreign company's profits cannot be offset by granting an exemption to residents of the Netherlands investing in such a company as that would entail a loss of revenue for the Netherlands tax authorities in that they received no tax on the profits of the foreign company concerned.

52. Referring to *Bachmann* the court noted that in that case there was a direct link between the deductibility of the contributions and the taxation of benefits which it was necessary to preserve in order to safeguard the cohesion of the Belgian tax system. In dismissing the arguments of the Netherlands Government the court distinguished *Bachmann* in the following terms in paragraph 58 of the judgment:

> "No such direct link exists in this case between the grant to shareholders residing in the Netherlands of income tax exemption in respect of dividends received and taxation of the profits of companies with their seat in another Member State. They are two separate taxes levied on different taxpayers."

53. It went on to deal with the loss of revenue argument as follows in paragraph 59:

> "As regards the arguments concerning the loss of revenue for the Kingdom of the Netherlands that would result from exemption of dividends received by its residents who are shareholders of companies with their seat in other Member States, it need merely be pointed out that reduction in such tax revenue cannot be regarded as an overriding reason in the public interest which may be relied on to justify a measure which is in principle contrary to a fundamental freedom."

54. A similar conclusion was reached in Case C-35/02 *Anneliese Lenz v Finanzlandesdirektion Fur Tirol* [2004] ECR I-7063, which considered a provision of Austria's tax legislation which allowed the recipients of dividends from companies established in Austria to choose between a tax of 25% on the dividends or allowing the dividends to be subject to ordinary income tax at half the rate that would otherwise be applied, whereas dividends received from companies established in other Member States were subject to ordinary income tax without any reduction in the rate. An Austrian resident would therefore make the election if his marginal rate of tax was less than the fixed rate. The question was whether such legislation constituted a prohibited restriction on the free movement of capital.

55. The facts in that case, so far as relevant were that Mrs Lenz, a German national fully liable to tax in Austria, received dividend income from companies established in Germany. She was assessed to income tax on these dividends at the ordinary income tax rate because the half-rate was only available where these dividends were received from a company established in Austria. Mrs Lenz complained that the application of the ordinary rate to the German dividends was contrary to the freedom of movement of capital provided by what is now Article 56. The court accepted this argument, its reasoning being set out in paragraphs 20 and 21 of the judgment as follows:

> "20. In this case, the tax legislation at issue has the effect of deterring taxpayers living in Austria from investing their capital in companies established in another Member State. The legislation allows such a taxpayer, in respect of the taxation of his domestic revenue from capital, to choose between definitive taxation at the fixed rate of 25% and ordinary income tax at a rate reduced by half, whereas his revenue from capital

> originating in another Member State is subject to the application of ordinary income tax, the rate of which may be as much as 50%."
>
> "21. That legislation also produces a restrictive effect in relation to companies established in other Member States, inasmuch as it constitutes an obstacle to their raising capital in Austria. To the extent that revenue from capital originating in another Member State receives less favourable tax treatment than revenue from capital of Austrian origin, the shares of companies established in other Member States are, for investors living in Austria, less attractive than the shares of companies established in that Member State"

56. In support of the proposition set out in paragraph 21 the court cited *Verkooijen* as authority.

57. The court went on to deal with the circumstances in which unequal treatment between dividends from domestic securities and those originating in another Member State could be justified and held in paragraph 27 of the judgment that for this to be so:

> "…the difference in treatment must concern situations which are not objectively comparable or be justified by overriding reasons in the general interest, such as the need to safeguard the cohesion of the tax system, the fight against tax avoidance and the effectiveness of fiscal supervision…"

58. The court rejected an argument based on *Bachmann* to the effect that the legislation was justified by the need to ensure the coherence of the national tax system because the tax advantages at issue were designed to attenuate the effects of double taxation of profits, there being a direct economic link between the taxation of the profits of the company and those taxation advantages. Thus, the argument went, since only companies established in Austria are subject to corporation tax in that Member State, it is justified to reserve those tax advantages to the recipients of dividends from companies established in Austria.

59. These arguments were disposed of by the court in paragraph 42 of the judgment as follows:

> "It should be noted in that regard that, in respect of capital from revenue [we think this must be a mistake for revenue from capital] of Austrian origin, the tax legislation at issue establishes no direct link between the taxation of company profits by means of corporation tax and the tax advantages enjoyed, in relation to income tax, by taxpayers living in Austria. In those circumstances, the level of the taxation of companies established outside Austrian territory cannot justify a refusal to grant those same financial advantages to persons receiving revenue from capital paid by those latter companies."

60. In relation to this line of cases it is helpful to introduce, *Manninen* itself, which we consider in greater detail in our discussion in the *Manninen* claims in Section IX below.

61. In *Manninen* the issue for consideration was whether the Finnish tax legislation on the taxation of dividends was compatible with Article 56. Under the relevant legislation dividends received by a person fully taxable in Finland whether from a Finnish or foreign established company were taxable in Finland as income. The relevant rate of tax in Finland was 29%.

62. Companies established in Finland paid a tax on their profits which is also at the rate of 29%. In order to avoid double taxation of such profits on the distribution of dividends shareholders receiving such dividends were allowed a tax credit equal to 29/71sts of the amount of dividends they received during the relevant tax year. The dividend and the tax credit constituted taxable revenue in the hands of the shareholder, the income tax on which is met by the tax credit, so that the total tax on profits distributed by the company amounts to 29%. The tax credit only applied to dividends distributed by Finnish companies to persons fully taxable in Finland.

63. Mr Manninen was fully taxable in Finland. He held shares in a Swedish company and received dividends from that company that had already borne corporation tax in Sweden. Those dividends were also subject to a withholding tax levied in Sweden at the rate of 15% which was deducted at source. Since dividends distributed by foreign companies to Finnish taxpayers confer no entitlement to a tax credit in Finland they were subject in that Member State to income tax at the rate of 29%. although by virtue of a double tax treaty the Swedish withholding tax was deductible from the income tax due on the dividend in Finland.

64. Mr Manninen claimed that the failure to give him a tax credit in respect of the Swedish dividends infringed Article 56. The ECJ agreed, its reasoning being set out in paragraphs 20 to 24 of its judgment as follows:

> "20 As for whether tax legislation such as that at issue in the main proceedings involves a restriction on the free movement of capital within the meaning of Article 56 EC, it should be noted that the tax credit under Finnish tax legislation is designed to prevent the double taxation of company profits distributed to shareholders by setting off the corporation tax due from the company distributing dividends against the tax due from the shareholder by way of income tax on revenue from capital. The end result of such a system is that dividends are no longer taxed in the hands of the shareholder. Since the tax credit applies solely in favour of dividends paid by companies established in Finland, that legislation disadvantages fully taxable persons in Finland who receive dividends from companies established in other Member States, who, for their part, are taxed at the rate of 29% by way of income tax on revenue from capital.
>
> 21. …
>
> 22. It follows that the Finnish tax legislation has the effect of deterring fully taxable persons in Finland from investing their capital in companies established in another Member State.
>
> 23. Such a provision also has a restrictive effect as regards companies established in other Member States, in that it constitutes an obstacle to their raising capital in Finland. Since revenue from capital of non-Finnish origin receives less favourable tax treatment than dividends distributed by companies established in Finland, the shares of companies established in other Member States are less attractive to investors residing in Finland than shares in companies which have their seat in that Member State (Case C-35/98 *Verkooijen* [2000] ECR I-4071, paragraph 35; Case C-334/02 *Commission v France* [2004] ECR I-2229, paragraph 24).
>
> 24. It follows from the above that legislation such as that at issue in the main proceedings constitutes a restriction on the free movement of capital which is, in principle, prohibited by Article 56 EC."

65. Once again, arguments in favour of justification of the unequal treatment of domestic and foreign dividends were advanced by various governments. They sought

to distinguish *Verkooijen* on the basis that in this case there was a direct link between the taxation of the company's profits and the tax credit granted to the shareholder receiving the dividends, pointing out that the tax credit is granted only on condition that the company concerned has paid the tax on its profits, the company being required to pay an additional tax if the corporation tax it has paid does not cover the minimum tax on the dividends to be distributed.

66. Once again those arguments were rejected, the court's reasoning being set out in paragraph 46 of the judgment as follows:

> "Having regard to the objective pursued by the Finnish tax legislation, the cohesion of that tax system is assured as long as the correlation between the tax advantage granted in favour of the shareholder and the tax due by way of corporation tax is maintained. Therefore, in a case such as that at issue in the main proceedings, the granting to a shareholder who is fully taxable in Finland and who holds shares in a company established in Sweden of a tax credit calculated by reference to the corporation tax owed by that company in Sweden would not threaten the cohesion of the Finnish tax system and would constitute a measure less restrictive of the free movement of capital than that laid down by the Finnish tax legislation."

67. Thus given that the whole purpose of the Finnish tax system was to ensure that Finland did not double tax a dividend from a Finnish company, account had to be taken of the underlying corporation tax paid in Sweden by the Swedish company paying the dividend.

68. Finally in the line of cases concerned with fiscal cohesion we mention, but only to postpone discussion until later, Case C-194/06 *Staatssecretaris van Financien v Orange European Smallcap Fund NV* [2008] ECR I-3747 ("***Orange Smallcap***") which Mr Baldry submits indicates that the ECJ is increasingly taking account of the principle of fiscal autonomy and, as we think he would have it, moving the *Bachmann* boundaries.

69. The Tribunal referred to Case C-9/02 *Hughes de Lasteyrie du Saillant v Ministère de l'Économie des Finances et de l'Industrie* [2004] ECR I-6051 ("***de Lasteyrie***"), a case concerning the freedom of establishment which is relied on by Mr Vajda. In that case, Mr de Lasteyrie transferred his tax residence from France and consequently under French law incurred an obligation to pay tax on an unrealised increase in the value of securities that he held. The ECJ observed in paragraph 45 of the judgment that

> "…even if [a charge of this nature] does not prevent a French taxpayer from exercising his right of establishment, this provision is nevertheless of such a kind as to restrict the exercise of that right, having at the very least a dissuasive effect on taxpayers wishing to establish themselves in another Member State".

70. The court stated further in paragraph 46 of the judgment that this difference in treatment between the position if he had stayed in France, where no tax would be payable until the securities were realised, and the position where he seeks to move to another Member State where a tax charge on an increase in value arises, "is likely to discourage a taxpayer from carrying out such a transfer [*ie* a transfer of tax residence]". The court therefore concluded in paragraph 48 of the judgment that the tax provision under consideration "is liable to hinder the freedom of establishment."

71. We derive the following principles from the analysis of the cases set out above:

(1) Any legislative provision which tends to discourage the exercise of an investor's rights under Article 56 is a breach of the right to free movement of capital afforded by that provision. Although the reasoning in the various discussions on freedom of movement on capital is to the effect that the relevant domestic tax legislation "has the effect" of "deterring" or "dissuading" cross border investment and "constitutes an obstacle" to foreign companies raising capital in the Member State concerned, it is clear that these conclusions are reached without reference to any specific findings of fact as to whether any cross-border investment was actually deterred in any particular case. Although *de Laysteyrie* concerned the freedom of establishment rather than the freedom of movement of capital in our view the principles to be applied are closely analogous. That being so, we agree with the Tribunal when it formulated the test (on the basis of the passages from *de Lasteyrie* quoted in paragraph 67 above) in this way:

> "46. It is also clear that the test for breach is applied on the basis of *a priori* reasoning and inference and not as part of any fact-finding or consideration of evidence. So for example, the European Court of Justice expressly observed that "any assessment of the facts in the case is a matter for the national court" (*De Lasteyrie*, supra, paragraph 41) but nevertheless observed that a charge to tax on a taxpayer who wishes to change his residence from one Member State to another has "… at the very least a dissuasive effect on the taxpayer wishing to establish themselves in another Member State" (paragraph 45) and is "likely to discourage a taxpayer from carrying out [a transfer of tax residence from one Member State to another]"

(2) Any such legislative provision (the "restrictive provision") is also in breach of Article 56 because as a consequence the securities of companies in which investment might be made on a cross-border basis are less attractive to investors residing in the Member State where the restrictive provision is to be found in that Member State's tax legislation. This situation, which again does not need to be found by reference to any specific findings of fact, constitutes an obstacle to those companies raising capital in the Member State whose tax legislation contains the restrictive provision. It seems to us from the cases that this conclusion will always follow as a corollary. The reason, of course, why the securities concerned will be less attractive to the cross-border investor will be that they will carry a lower net dividend yield than securities of a comparable company paying a similar rate of dividend situated in the Member State where the cross border investor is resident.

(3) Where the tax legislation concerned provides a tax credit in respect of the dividends that an investor receives from a company established in the Member State in which he is resident, such tax credit being provided as a means of avoiding double taxation on profits which are liable to corporation tax at the company level and are then distributed as a dividend, the provision of a tax credit to such an investor who has made an investment in the securities of a company established in another Member State of an amount calculated by reference to the underlying corporation tax paid by the latter company would preclude any breach of Article 56 and does not affect the cohesion of the first Member State's tax system. The fact that the granting of such a credit results in a loss of tax revenue to the first Member State because it represents a credit in respect of tax that has been paid in another Member State is irrelevant to this analysis.

(4) The overarching principle that leads to these conclusions is that situations which are objectively comparable must not suffer unequal treatment. Where the situations are objectively comparable a difference in treatment between dividends received from a domestic investment and those received from a cross-border investment cannot be justified except by overriding reasons in the general interest, such as the need to safeguard the coherence of the tax system: see in this regard paragraph 29 of the judgment in *Manninen*. The broad conclusion from *Verkooijen, Lenz* and *Manninen* is that a dividend received in a Member State from a company established in another Member State cannot be subjected to tax in a less favourable way than a dividend received in the first Member State, from a company established in that Member State.

72. We emphasise that we articulate those principles in the context of a difference in treatment of the resident of one Member State between his assets in that State and his assets in another Member State. In the context of the present appeals, the relevant difference is the different treatment afforded to dividends from a UK tax-resident company on the one hand and dividends from a company tax-resident in another Member State (or EEA State) on the other hand. Whether there are analogous principles where the assets concerned are all in one Member State is another question. In the context of the present appeals, that question is essentially the FIDs issue which relates to dividends paid by UK tax-resident companies to BTPS which are funded out of non-UK source income by the dividend-paying companies.

VIII The Tribunal's observations on the UK Tax Code

73. In Section I of the Decision (paragraphs 58 to 70), the Tribunal made some observations over three pages about the interrelation between the ACT for which the dividend-paying company is accountable and the tax credit to which the recipient of the dividend is entitled.

74. The relevant conclusions of the Tribunal, which can be briefly stated, are these. First, a credit available under section 231 ICTA 1988 is not dependent on the dividend-paying company having paid or suffered, underlying tax or ACT. Secondly, ACT is not a surrogate for tax suffered on a dividend by the recipient: ACT is a liability of the dividend-paying company which can be used to offset certain other liabilities of that company or, in some cases, of subsidiary companies. What the recipient of the dividend receives is a credit, that is to say the right to reduce what would otherwise be his liability, or to recover an excess of the credit over such liability.

75. In paragraph 60, the Tribunal was keen to point out that the right to the credit was not dependent on the company suffering a charge to ACT. Mr Baldry says that this is wrong, referring to passages from the speeches of Lords Nicholls, Scott and Walker in *Pirelli Cable Holdings NV v IRC* [2006] UKHL 4, [2006] 1 WLR 400 where each of the judges refers to the imputation of the ACT to the shareholders. Lord Nicholls observed that the legislation nowhere stated that liability to pay ACT was a precondition to entitlement to a tax credit, but "this unspoken linkage lay at the heart of the scheme, and the legislation was drawn in a form which achieved this result". And Lord Walker observed that it was central to the concept of a tax credit that some UK tax should have been paid, noting that it "would be an abuse of language, and contrary to common sense, to speak of granting a tax credit when no such tax has been paid".

76. ACT is, nonetheless, corporation tax: section 14(1) says as much: a company becomes liable to pay "amount of corporation tax ("advance corporation tax")……". Payment of ACT cannot be seen as payment of income tax in respect of the shareholder's liability. Indeed, as an advance payment of corporation tax, the company is able to reduce its MCT accordingly. Mr Baldry provides a simple comparison between the classical system and the imputation system where a company has distributable profits of £100. Under the classical system, the company would, in making a distribution of £100 to the shareholder, deduct income tax (at say 30%) and account to the shareholder for £70 and to HMRC for £30 by way of income tax deducted (not by way of corporation tax). The shareholder's income was £100; if the shareholder was an exempt pension fund, its actual income tax liability would have been nil and it could reclaim the £30 deducted from its income. Under the imputation system, a distribution of £70 is made. The result of that distribution is to trigger an ACT charge of £30. That £30 is corporation tax payable by the company and is not a deduction from the payment which the company would otherwise make to the shareholder. The ACT is available to offset against the MCT. So far as the shareholder is concerned, his income is £100 but he gets a credit against his own liability which corresponds to the tax (the ACT) which has been paid. The credit is properly called a tax credit because that is precisely what it is: a credit for (corporation) tax in assessing the shareholder's own tax position *vis a vis* HMRC.

77. Accordingly, whilst the language of the Tribunal in relation to the first conclusion may be slightly inapposite (although it should be noted that in paragraph 61, the Tribunal did state that in the normal course of events, a qualifying distribution attracted ACT), its second conclusion is one which we agree with. ACT is not a surrogate for tax suffered on a dividend by the recipient

IX Discussion: the FIDs claims

Liability

78. We deal at the outset with a discrete point in order to remove it from the picture. The point is how, if at all, the elective nature of the FIDs regime has any impact on the question of breach of Article 56. The Tribunal concluded at paragraph 76 that it made no difference to the result that the absence of a tax credit is triggered by an election. The ECJ, at paragraph 161 of its judgment in *FII ECJ* rejected the argument that a difference in treatment did not constitute a restriction on the freedom of establishment because the FIDs regime was merely optional. The Advocate General expressed the same view at paragraph 101 of his Opinion in dealing with the UK Government's argument that the FIDs regime could not infringe Articles 43 or 56 because it was an elective regime. He described the argument as fallacious where the underlying tax provisions (that is to say, those which would apply in the absence of election for the FIDs regime) were also discriminatory. In that regard, *FII ECJ* established among other things that it is a breach of Article 56 (as well as Article 43) to allow the deduction of ACT paid in respect of dividend received by a UK company from another UK company from the ACT payable by the receiving company in respect of dividends to its own shareholders, but not to allow a deduction in relation to the corresponding tax on distributed profits of a foreign dividend-paying company: see the answer to Question 2. Accordingly, the underlying tax provisions did not comply with Article 56. However, if they had complied, then neither *FII ECJ* nor any other case leads to the conclusion that the FIDs regime (although non-compliant with Article 56 viewed in isolation) would have rendered the UK tax provisions read as a

whole non-compliant; and for our part we do not understand how that could ever be the case.

79. In the light of the principles set out in paragraph 71 above, we have no hesitation in finding, as did the Tribunal (see paragraph 73 of the Decision), that the absence of a tax credit on a FID is a disadvantage to the recipients of those FIDs and that prima facie that disadvantage is a breach of the free movement of capital provisions in Article 56. Where a UK resident company pays a dividend funded out of UK sourced profits the recipient obtains a tax credit under section 231 of ICTA but if a dividend is paid out of non-UK sourced profits no tax credit is available by virtue of section 246C of ICTA. The payment of dividends by UK resident companies funded out of UK sourced profits is an objectively comparable situation to the payment of dividends by UK resident companies sourced from non-UK profits. We perceive it as self evident that the difference in treatment is liable to dissuade or likely to discourage investment in companies which pay FIDs and agree with what the Tribunal said at paragraph 73 of the Decision. The difference in treatment therefore causes the shares in foreign companies in which UK resident companies might invest to be less attractive than shares in purely domestic companies.

80. We do not understand HMRC to dispute that conclusion. But even if they do, it appears to us to be inevitable from the conclusion of the ECJ in *FII ECJ*, which we discuss in detail later, and in which it was held, inter alia, that one of the features of the FIDs regime, namely the absence of a tax credit for recipients of a FID when such a tax credit is available for recipients of dividends paid out of UK sourced profits amounts to a breach of Article 56 *vis a vis* the dividend-paying company. It is also the only conclusion which can be drawn from what the ECJ said in Case C-301/09, *Ministre du Budget, des Comptes publics et de la Fonction publique v Accor* [2011] ECR I -12845, which, again, we discuss in detail later. The dispute between the parties centres on whether that breach is purely a breach of the FID paying company's Article 56 rights or whether it also infringes separate Article 56 rights of the shareholder who has been denied the tax credit, in this case BTPS.

81. The first issue we have to consider in determining whether BTPS has Article 56 rights in this situation is whether BTPS's investment in UK resident companies that paid FIDs is a wholly internal situation and therefore outside the scope of Article 56.

82. It is helpful to remind ourselves of the type of investment that BTPS made which is the subject of the FIDs claims. The situation to be contemplated is a UK resident company (the parent company) with various subsidiaries, some of which are companies resident in the United Kingdom and some of which are companies resident overseas. These various subsidiaries pay dividend income to the UK resident parent company. That UK resident parent company in its turn, uses that income to pay dividends to its shareholders such as BTPS. An example of such a company referred to in paragraph 28 of *FII ECJ* was British American Tobacco plc ("BAT") and UK resident companies forming part of the BAT group were the test claimants in that case.

83. Where BAT received dividend income from its UK resident subsidiaries such income would constitute franked investment income. Consequently, BAT would not be obliged to pay any ACT when passing on that dividend to its own shareholders. The shareholder receiving the dividend was entitled to a tax credit equal to such proportion of the amount or value of the distribution as corresponded to the rate of

ACT: see the discussion of Henderson J in paragraphs 15 and 19 of *FII GLO* quoted in paragraph 35 above. Conversely, where BAT received dividend income from its non-UK resident subsidiaries that income would not constitute franked investment income so that BAT would be obliged to account for ACT when it paid that dividend on to its own shareholders. Assuming BAT had made an election to treat such a dividend payment as a FID it would be able to claim repayment of the ACT provided it could match the FID with the foreign dividends, although there would be a delay of between 8½ and 17 ½ months in its receiving the benefit of the claim (either by offsetting the amount of the claim against MCT or by repayment) as described in paragraph 24 of *FII GLO*. In addition, by virtue of Section 246C of ICTA the shareholder receiving the FID was not entitled to a tax credit, as described in paragraph 25 of *FII GLO*.

84. The ECJ in *FII ECJ* observed that these differences in treatment between the domestically sourced dividend and the FID amounted to less favourable treatment for the latter. Specifically it stated in paragraphs 146 to 149 of its judgment

> "146. As regards, in the first place, the ability to recover surplus ACT, the order for reference shows that, while ACT must be accounted for within 14 days of the quarter in which the company concerned pays dividends to its shareholders, surplus ACT is repayable only when corporation tax becomes due, that is to say, nine months after the end of the accounting period. Depending on when the company paid the dividends, it must wait between 8½ and 17½ months to obtain repayment of the ACT accounted for.
>
> 147. Accordingly as the claimants in the main proceedings contend, resident companies electing to be taxed under such a regime by reason of their receipt of foreign-sourced dividends are exposed to a cash-flow disadvantage which does not arise in the case of resident companies receiving nationally-sourced dividends. In the latter case, since the resident company making the distribution has already accounted for ACT on the profits distributed, a tax credit is granted to the resident company receiving the distribution, thereby allowing that the company to pay an equivalent amount by way of dividends to its own shareholders without have to account for ACT.
>
> 148. In the second place, a shareholder receiving a payment of dividends from a resident company which has its origin in foreign-sourced dividends treated as FIDs, is not entitled to a tax credit, but is treated as having received income which has been taxed at the lower rate for the tax year in question. In the absence of a tax credit, such a shareholder has no right to any repayment if he is not liable to income tax or where the income tax due is less than the tax on the dividend at the lower rate.
>
> 149. As the claimants in the main proceedings contend, that means that a company which has elected to be taxed under the FID regime must increase the amount of its distributions if it wishes to guarantee its shareholders a return equivalent to that which would be achieved from a payment of nationally sourced dividends."

85. The ECJ went on to observe in paragraph 166 that this difference in treatment had the effect of discouraging a UK resident company from investing its capital in a country established in another Member State and also had a restrictive effect on

companies established in other states in that it constituted an obstacle to their raising capital in the United Kingdom.

86. The ECJ therefore concluded, in paragraph 173 of the judgment, that Articles 43 and 56 of the Treaty:

5 "preclude legislation of a member state, which, while exempting from advance corporation tax resident companies paying dividends to their shareholders which have their origin in nationally-sourced dividends received by them, allows resident companies distributing dividends received by them to elect to be taxed under a regime which permits them to recover the advance corporation tax paid
10 but, first, obliges those companies to pay that advance corporation tax and subsequently to claim repayment and, secondly, does not provide a tax credit for their shareholders whereas those shareholders would have received such a tax credit in the case of a distribution made by a resident company which had its origin in nationally-sourced dividends".

15 87. Consequently, BAT would have a remedy for the breaches of Article 56, in relation to its freedom to move capital and make investments in its foreign subsidiaries. Whilst the detail is not relevant to this decision, that remedy would amount in essence to a claim for the time value of the ACT which it had paid and which was subsequently refunded. The ECJ however held that the payments they
20 made to enhance the dividends the relevant companies paid to compensate shareholders for the lack of a tax credit could not form the basis of an action under Community law as they resulted from decisions taken by the companies concerned and were not an inevitable consequence of the UK Government's refusal to extend tax credits to FIDs: see paragraph 207 of the judgment.

25 88. Mr Vajda relies on *FII ECJ* as having established that Section 246C of ICTA, which denied a tax credit to a shareholder in respect of a FID, infringed Article 56. Although the only claimants in *FII ECJ* were the companies who paid the dividends, and the ECJ, as discussed above, dealt with the remedies available to them as a consequence of its findings that aspects of the FIDs regime breached Article 43 and
30 56, the key question was whether the shareholders themselves can rely on that breach to found a claim of their own that their Article 56 rights have been breached.

89. Mr Vajda submits that a shareholder has, pursuant to Article 56, the right to invest capital in securities without restrictions based on whether the companies, in their turn, earn a substantial part of their income from foreign sources or from
35 domestic sources. In other words, the UK-resident shareholder's investment in a UK-resident company with a large proportion of its income derived from foreign subsidiaries is a movement of capital protected by Article 56 EC, notwithstanding that it is not a transaction expressly listed in the Nomenclature set out in Annex I to Directive 88/361/EEC (see paragraph 21 above) and notwithstanding that the
40 transaction is an acquisition by a UK resident of UK securities. Although Article 88/361/EEC was replaced by Article 56 the Nomenclature remains relevant for identifying the types of "movements of capital" which are protected by Article 56. Mr Vajda submits that the Nomenclature does not provide an exhaustive list of the protected transactions: and that Article 56 should be broadly construed.

45 90. The pensions funds' investment in a UK-resident company with a large proportion of its income derived from foreign subsidiaries, and the tax treatment of any resulting FID paid by that company, is not, Mr Vajda submits, a wholly internal

situation, in view of the necessary foreign element which is involved in the payment of a FID, namely that the company has income derived from foreign subsidiaries.

91. Mr Baldry, for his part, submits that the correct analysis is that a UK resident investor who invests in a UK-resident company is not exercising any freedom of movement to move capital between Member States or between a Member State and a third country within Article 56. Insofar as the distinction is between "wholly internal situations" and other situations, the present case is one of a "wholly internal situation". This is because:

(1) BTPS was not seeking to exercise its freedom to move capital to another Member State. BTPS therefore has no directly enforceable Treaty rights on which it can rely; and

(2) Article 56, on which BTPS relies, prohibits restrictions on the movement of capital *between* Member States and *between* Member States and third countries. The Nomenclature makes quite clear that this covers the acquisitions by non-residents of domestic securities and the acquisition by residents of foreign securities: see paragraph 21(3) above. It does not, however, cover an acquisition by a resident of domestic securities. Since there is no doubt that (a) BTPS is resident in the UK and (b) all the FID paying companies in which BTPS invested capital were resident in the UK Article 56 cannot be relied on by BTPS; and

(3) BTPS cannot rely on Article 56 to disapply section 246C because BTPS were not seeking to exercise any directly enforceable rights under the Treaty. Specifically, by investing its capital in a UK-resident FID-paying company, BTPS was not seeking to exercise its freedom to move capital, either between Member States or between Member States and third countries.

92. Mr Baldry submitted that the cases relied on by BTPS to show that a situation will not be a wholly internal situation if it has an effect, even indirectly, on the position of companies constituted under the law of other Member States do not support that proposition but rather deal with the question as to whether the person who was directly seeking to exercise his right to move capital or the person who was potentially hindered from receiving the cross-border movement had his freedoms interfered with.

93. In the first of these cases Case C-1/93 *Halliburton Services v Staatssecretaris Van Financien* [1994] ECR I – 1137, a case concerning freedom of establishment, Halliburton Services BV, a Netherlands resident company, made a claim against the tax it had to pay to the Netherlands tax authorities on the sale to it of property by a German company in the same group. The tax concerned therefore was being paid by the transferee company in the Netherlands, not the German transferor. Had the transfer been between two Dutch companies in the same group, an exemption from the tax concerned would have applied. The Netherlands government argued that the situation was purely internal to the Netherlands as the person liable to pay the tax was the Netherlands resident transferee, not the German transferor. The ECJ rejected this argument. Its reasoning was as follows;

> "19. In that regard, it should be noted that payment of a tax on the sale of immovable property constitutes a burden which renders the conditions of sale of the property more onerous and thus has repercussions on the position of the transferor. In a case such as this, the vendor is in a distinctly less favourable

position than if it had chosen the form of a public or private limited company instead of that of a permanent establishment for its business in the Netherlands.

> 20. Although the difference in treatment has only an indirect effect on the position of companies constituted under the law of other Member States, it constitutes discrimination on grounds of nationality which is prohibited by Article 52 of the Treaty."

94. The reason why it constitutes such discrimination can be found the Opinion of the Advocate General: it is

> "because a company exercising the right given by Article 58 of the Treaty to carry on business in another Member State through the intermediary of a branch or agency is at a disadvantage compared with the companies constituted in accordance with law of that Member State."

95. It is therefore clear that the unfavourable tax treatment the Netherlands company suffered had an indirect effect on the German transferor in that it was in a less favourable position as a non-resident company carrying out its business through a permanent establishment than it would have been had it done so in the Netherlands through a local subsidiary. Mr Vajda says, perfectly correctly, that the unfavourable treatment that the Dutch company suffered had an indirect effect on the German transferor which was in a different Member State: this was sufficient to engage the freedom of establishment provisions. He then draws a parallel between that situation and the position of BTPS as an investor in a company making cross-border investments; the unavailability of the tax credit to BTPS which is available when it made investments whose dividend income was derived solely from domestic securities had an impact on the non-resident UK companies in which BTPS was an indirect investor. It was on that basis that the Tribunal had held that this was not a wholly internal situation.

96. Mr Baldry characterises the breach differently from Mr Vajda; he submits that all this case established was that there was a direct breach of the right of establishment of the German company. He says that the Netherlands was imposing tax on a transfer from Germany less favourably than it would have imposed tax on the same sale from the Netherlands. That was liable to dissuade German companies from transferring their business assets and therefore establishing themselves in the Netherlands; that was the breach.

97. We think that Mr Baldry is right in that analysis. But whether he is right or wrong, we do not gain much, if any, assistance from Mr Vajda's suggested parallel. The facts of *Halliburton* are too far removed from the facts of the present appeals to draw any useful analogy. Further, the decision was concerned with what is now Article 43 rather than Article 56 and care must be taken in applying to Article 56 the jurisprudence relating to Article 43.

98. We do not consider, either, that the parallel which Mr Vajda perceives is the basis on which the Tribunal held that this was not a wholly internal situation. Rather, the reason the Tribunal said that the disadvantage was not such a situation was simply because that disadvantage was a consequence of the different tax treatment afforded to UK dividends and foreign dividends under the FIDs scheme. As the Tribunal said at paragraph 75 of the Decision: "This makes shares in UK companies which fund dividends out of non-UK source profits less attractive than shares in UK companies which fund dividends out of UK source profits. That is not a wholly internal situation". The Tribunal said nothing about the relative positions of a UK subsidiary

and a foreign subsidiary or the impact on such subsidiaries of a difference in treatment of their dividends.

99. In the second of these cases, Case C-471/04 *Finanzamt Offenbach am Main-lund v Keller Holding GMBH* [2006] ECRI-217, a German resident holding company was denied a tax deduction for a loan made to its German subsidiary, because that German subsidiary derived part of its income from a company resident in Austria.

100. The taxpayer argued successfully that the restriction infringed the German parent's right to freedom of establishment. It had been argued against the taxpayer that the German parent had no relevant Community law right because its investment of capital had been in its German subsidiary which was a wholly internal situation. This argument was rejected at paragraphs 22 to 24 of the judgment as follows:

> "22. It is appropriate at the outset to reject the argument of the Finanzamt Offenbach am Main-Land and the German and United Kingdom Governments to the effect that the main proceedings concern a situation purely internal to a Member State such that there is no need to interpret the provisions of the Treaty on freedom of establishment or free movement of capital.
>
> 23. Although the main proceedings admittedly relate to a parent company having its registered office in Germany which challenges the decision of the German tax authorities refusing it the benefit of deducting expenditure incurred for the purpose of acquiring a shareholding in a subsidiary also established in Germany, that does not detract from the fact that that decision is based on national legislation which excludes the possibility of deducting that expenditure because of the direct economic link which is alleged to existing between it and dividends paid by an indirect subsidiary established in Austria and which, was such, are exempt from corporation tax in Germany, in accordance with Article 15 of the Tax Convention.
>
> 24. Given that legislation at issue in the main proceedings applies to situations related to intra-Community trade, the problem raised by those proceedings may fall within the scope of the provisions of the Treaty relating to the fundamental freedoms….."

101. The Court went on to conclude, at paragraph 34 of the judgment, that the tax position of the German parent having an indirect subsidiary in question was less favourable than it would have been had an indirect subsidiary been established in Germany, with the result that, as the Court concludes in paragraph 35:

> "In the light of that difference a parent company might be dissuaded from carrying on its activities through the intermediary of subsidiaries or indirect subsidiaries in other Member States"

102. Mr Vajda submits that this case is authority for the proposition that transactions between two parties in the same Member State fall within the scope of the right to free movement where there is a direct economic link between the denial of the benefit arising out of that purely domestic transaction and a prior movement of capital between two Member States.

103. The thrust of Mr Baldry's submissions, consistent with his submission on *Halliburton,* is that this case merely establishes that the German parent's right to establish a subsidiary in another Member State was infringed; it was well established that freedom of establishment applies where the ultimate parent has influence over the affairs of a lower tier company, whether the lower tier company is a direct or indirect subsidiary. He acknowledges the familiar theme of less favourable treatment arising from the fact that a company might be dissuaded from carrying on its activities

through the intermediary of subsidiaries or indirect subsidiaries. In *Keller*, the parent company, which was being taxed less favourably, was being dissuaded from carrying out its activities in its establishment in Austria. This demonstrated, he submits, another theme which is that the person who can rely on the Treaty freedom is the person who is seeking to do the very thing that the Treaty is giving him freedom to do. Thus in *Halliburton*, it was the German company which had the freedom of establishment in the Netherlands, a freedom which was infringed by the disadvantage suffered by having its own establishment in the Netherlands in contrast with conducting its business through a Dutch company; and in *Keller*, it was the German ultimate parent company which had the freedom of establishment in Austria, a freedom which was infringed by the imposition of a less favourable German tax regime in respect of its Austrian subsidiary than in respect of its German subsidiary.

104. The final case relied on by BTPS on this point, Case C-301/09, *Ministre du Budget, des Comptes publics et de la Fonction publique v Accor* [2011] ECR I - 12845, is a case concerning movement of capital. Under French law a French resident company was not taxed on dividends received from subsidiaries whether resident or non-resident provided it held a minimum shareholding. However, when it distributed that dividend to its shareholders it was required to make an advance payment of corporation tax and where the French company received a dividend from a French subsidiary it received a tax credit equal to half the dividend paid which enabled it to reduce the advance payment of corporation tax it had to make but where such a dividend was received from a non-resident company it did not. The tax credit had been introduced with a view to eliminating double economic taxation of dividends. Consequently the amount distributed by the parent in respect of dividends from non-resident subsidiaries would be less than in respect of the equivalent French-sourced dividends.

105. It was common ground that the rules at issue resulted in a difference in treatment between dividends distributed by a resident subsidiary and those distributed by a non-resident subsidiary.

106. The ECJ rejected an argument from the French Government that even if, as far as the French resident shareholders who received the dividends were concerned, the absence of a tax credit for the foreign dividends could be regarded as an obstacle to raising capital from French shareholders, that restriction would in any event concern a purely domestic capital movement between a French parent company and its French shareholders having no foreign element and not falling within the scope of Community law.

107. The Court's reasoning was set out in paragraphs 61 to 62 of its judgment as follows.

> "61. The fact that resident shareholders might have been deterred from acquiring shares in a parent company, due to the fact that dividends originating from that company's subsidiaries established in a Member State other than the French Republic were lower than dividends from resident subsidiaries, might in turn have deterred that parent company from carrying on its activities through the intermediary of non-resident subsidiaries.
>
> 62. It must be stated that, since it is related to intra-Community trade, such a situation may fall within the scope of the provisions of the Treaty relating to the fundamental freedoms (*Keller Holding* (para 24)) and that inasmuch as, from a taxation

perspective, they put Community situations at a disadvantage compared with purely domestic situations, the provisions of the CGI at issue in the main proceedings thus constituted a restriction which is, in principle, prohibited by the Treaty provisions relating to freedom of establishment"

5 108. The Court also held that this reasoning was equally applicable to a claim based on a breach of the freedom to move capital. This appears from paragraphs 64 and 65 of the judgment as follows:

"64. The reasoning set out in the above paragraphs applies in the same way where a parent company has received dividends on the basis of a holding which does not confer
10 on it a definite influence on the decisions of its distributing subsidiary and does not allow it to determine the latter's activities.

65. The difference in treatment in question in para 41 above might have had the effect of deterring parent companies established in France from allocating capital to companies established in another member state and also have had a restrictive effect as
15 regards companies established in other member states in that it constituted an obstacle to the raising of capital in France."

109. This reasoning is also consistent with the opinion of the Advocate General in this case. At paragraph 38 of his opinion he sets out the arguments of the French Government on this issue and he then responded to it at paragraphs 43 to 48 as
20 follows:

"38. Secondly, that government claims that, in so far as the advance payment was set off against the distributable results of the parent company, it did not constitute a charge on profits but a tax charge on the distributable results the cost of which was born in full by the shareholders who received a reduced dividend. The parent company was not
25 therefore affected by the regime. Moreover, the French government states that, in so far as the non-resident shareholders were able to obtain reimbursement of the advance payment if they did not benefit from tax credit, in accordance with the tax conventions concluded by the French Republic and/or French administrative doctrine, only the French shareholders of the French parent company were affected by the different treatment, a
30 situation which, because of its purely internal character, did not fall within the scope of art 56 EC."

"43. As regards the second argument set out by the French government, I must point out that it appears to underlie the subdivision of the first question referred by the national court, depending on whether the parent company (first part of that question) or the
35 shareholders in that company (second, alternative part of the question) are involved.

44. That subdivision appears essentially to be motivated by procedural considerations of domestic law, in so far as the dispute in the main proceedings brings the French authorities into conflict with Accor and not with that company's shareholders.

45. It does not, however, appear relevant for the purposes of interpreting art 56 EC, the
40 scope of which extends to national measures which deter cross-border investment, without it being necessary to ask whether that deterrent has a greater effect on the company as such, the competent organs of that company or, more generally, its shareholders. Endorsing the distinction put forward by the national court and the French government would, in my opinion, amount to making the application of art 56
45 subordinate to the national law of the member states and to the methods of organisation of companies established in their respective territories.

46. In any case, the case law of the Court illustrates that the same national measure can discourage residents (including corporations) in one Member State from investing their capital in another member state and also have a restrictive effect as regards residents of those other member states in that it constitutes an obstacle to their raising of capital in the first member state. Therefore, for the purpose of describing a national measure under Article 56(1) EC I do not see any obstacle to that measure also having a determent effect in regard to a company and/or its shareholders. After all, the existence of such dissuasion from cross-border movements of capital is not, by definition, including in the field of tax, subordinate to an arithmetical demonstration of the financial consequence borne by the parties concerned"

110. Mr Vajda submits that the reasoning in *Accor* taken with *Halliburton* and *Keller* shows the ECJ taking a broad economic approach and asking whether the national measure concerned has a dissuasive effect on a cross border movement of capital. If it does those who are dissuaded have Article 56 rights, whether that be the company seeking to make cross border investment or the shareholders of that company, even if they are resident in the same member state.

111. Mr Baldry, as he does with the other cases, puts another interpretation on the reasoning. He emphasises the finding in paragraph 65 that there is a detriment to the French parent exercising its right to allocate capital to companies in other member states, and submits that the ECJ looks precisely at who is the particular person whose freedom was hindered by the legislation in question and says nothing about an internal movement at all.

112. Having said that, we need to make two remarks.

(1) First, we are conscious that the Article 56 does not use the phrases "wholly internal situation" or even "internal situation": those are phrases used by the ECJ and must be read in context. We do not therefore, attach overdue weight to the phrases but concern ourselves with the meaning of Article 56 construed according to the methods of the European jurisprudence.

(2) Secondly, in the cases to which we have been referred where it has been argued that the situation was internal, the argument has been that because the situation is internal there is no breach at all of Article 56. There is, however, nothing in the case law to support the view that, where a breach is established (in the sense that domestic legislation is held, in some way, to be non-complaint with Article 56), that breach can be relied on by an affected person only if he, she or it is a person making a movement of capital from one Member State to another, although we accept that the case law says nothing express either way on the point. In the context of the present appeals, the FIDs regime is clearly non-compliant: *FII ECJ* established as much. It therefore cannot be argued that the FIDs regime is wholly internal even *vis a vis* a UK shareholder. In contrast, in *Halliburton* and *Keller*, the argument was that the relevant regime did not breach the relevant Articles at all because the matter was a wholly internal situation. Neither *FII ECJ* nor *Accor* deal with the point although we note that in both cases one reason for holding that Article 56 was infringed was that shareholders resident in the Member State (the UK and France respectively) might be deterred from investing in a resident company which carried on its undertaking through non-resident subsidiaries: see for instance paragraph 62 of *Accor* quoted above. We come back to those cases in a moment.

113. We now return to the example we gave at the outset of this discussion, namely the position regarding BTPS's investment in BAT. BAT is a global corporation whose business, whilst managed from London and organised in the form of a UK resident public limited company with its shares listed on the London Stock Exchange, derives its profits through a multitude of operations abroad carried out through local subsidiaries. It seems to us self evident that an investment manager taking a decision on behalf of BTPS to invest in BAT would not do so on the basis that BTPS thereby was obtaining exposure purely to the UK market. It would be an allocation of capital to procure a return from the global operations of BAT as a whole. To argue that because that investment is represented by shares issued by a UK incorporated public limited company the investment concerned was a "wholly internal situation" is to emphasise form over substance. It is an internal situation in the sense that BTPS makes its investment in a UK incorporated company but not "wholly internal" in the sense that the income of that company is substantially derived from investments made overseas.

114. We illustrate the absurdity of the formalistic approach by reference to an example of an investment company, incorporated in one Member State with its investors situated in the same Member State, but which invested all of its assets in a portfolio of securities listed on the stock exchanges of other Member States. The investors in such a vehicle would be seeking a return from exposure to the markets in those other Member States but for convenience may prefer to invest in a vehicle incorporated in their home state rather than directly in the underlying securities themselves. It could be that the vehicle concerned was tax transparent, that is it bore no tax itself but for tax purposes its shareholders were treated as having made a direct investment in the underlying securities. If in that situation the investor's home state taxed the dividends received in his hands at a higher rate than would be the case if the investment company had invested in a portfolio consisting purely of domestic securities, on Mr Baldry's analysis there would be no infringement of Article 56 because the only person making a capital movement on a cross-border basis was the investment company and not its underlying shareholders. It follows from this that we accept Mr Vajda's submission there where BTPS makes an investment in a multinational such as BAT there is a cross-border movement of capital that is made by BTPS which happens through two transactions, first, its investment in BAT plc and secondly the investment of the funds raised by BAT in the overseas subsidiaries.

115. This analysis is fortified by the nature of the FIDs regime itself. The effect of the regime is to provide a quite separate tax treatment for UK sourced dividends as opposed to dividends which are wholly derived from non-UK sourced dividends. A FID only carries the ACT benefit for the FID-paying company to the extent that it can be funded out of non-UK sourced profits and gives the UK shareholder a direct economic link with the underlying dividends received by the UK company making the distribution. These features formed the basis of the Tribunal's reasoning (with which we agree subject to the note at the end of the quote below) that the absence of a tax credit for a FID by virtue of the application of Section 246C of ICTA did not arise in a wholly internal situation. In paragraph 74 of its decision the Tribunal stated as follows:

> "….. it is true that the FIDs regime applies to a dividend paid by a UK tax-resident company to UK resident shareholders. But Section 246C only removes the tax credit if the dividend is paid out of non-UK source income. Otherwise the dividend would not be a FID. A dividend paid out of non-UK source income, which is elected to be a FID and thus carries no tax credit is disadvantaged in the hands of a recipient shareholder by

reason of the absence of the tax credit, as compared to a dividend paid by a company funded out of UK source income which carries a tax credit, by reason (only) that the FID is funded out of non-UK source profits. In other words the disadvantage of the absence of a tax credit on a FID is a direct result of the FID being funded out of non-UK source profits.This makes shares in UK companies which fund dividends out of non-UK source profits less attractive than shares in UK companies which fund dividends out of UK source profits. That is not a wholly internal situation."

[Note: it is not strictly correct that section 246C only removes the tax credit if the dividend is paid out of non-UK source income. In theory a dividend may be paid out of mixed UK and foreign sources. A FID election could be made. Section 246C then removes the tax credit from the whole of the dividend, not just the part of it which is non-UK source and in respect of which a matching election is made under section 246J. But nothing turns on this in relation to the point at issue.]

116. This conclusion is also entirely consistent with the approach of the ECJ in *Halliburton, Keller Holding* and *Accor*, as referred to above. We accept Mr Vajda's submission that these cases demonstrate that transactions between two parties in the same member state fall within the scope of the right to free movement where there is a direct economic link between the denial of the benefit arising out of that purely domestic transaction and a prior movement of capital between two member states. Whilst Mr Baldry is correct to state that each of the cases is concerned with the infringement of direct rights, that is in *Halliburton* the right of the German subsidiary to establish itself in the Netherlands, in *Keller Holding* the right of the German parent to establish itself in Austria though its sub-subsidiary and in *Accor* the right of the French company to establish itself though subsidiaries in other member states, it is also clear that the cases deal with the position of those who are the parties to a purely domestic transaction which is directly linked in the economic sense to the cross border movement.

117. Thus in *Halliburton* the fact that the Dutch transferee of the property received less favourable tax treatment where the transferor was a German as opposed to a Netherlands company amounted to an infringement because of the indirect effect on the German company. This formed the key part of the ECJ's reasoning as set out in paragraph 20 of the judgment referred to in paragraph 93 above.

118. Likewise in *Keller Holding*, the basis of the Court's reasoning is set out in paragraph 23 of the judgment referred to in paragraph 100 above, where reference is made to the "direct economic link which is alleged to exist between it and dividends paid by an indirect subsidiary established in Austria…". Finally in paragraph 45 of the Advocate General's opinion in *Accor* referred to in paragraph 109 above, which was consistent with the reasoning of the court in its judgment, it is made clear that once it is found that the national measure deters cross border investment it is not necessary to ask whether the deterrent has a greater effect on the company as such, or more generally, its shareholders.

119. We do not believe these cases can be distinguished on the basis that they primarily concerned freedom of establishment rather than the freedom to move capital. It was made clear in paragraphs 64 and 65 of the judgment in *Accor* that the reasoning in that case, following *Keller Holding*, was equally applicable to movements of capital.

120. Next, we record, if only to reject, Mr Baldry's submission that the receipt by BTPS of FIDs does not fall within the scope of Article 56 on the basis that the

Nomenclature only covers the acquisition by non-residents of domestic securities and the acquisition by residents of foreign securities. It is clear that the Nomenclature is only indicative of the matters that fall within the scope of Article 56. It cannot restrict the scope of Article 56 itself. Authority for this is to be found in Case C-450/09 *Ulrich Schroder v Finanzamt Hameln* [2011] ECR I-02497: see paragraph 25 of the judgment where it was stated that the Nomenclature is not exhaustive as regards the notions of movements of capital. For the reasons we have given above, an investment in the securities of a domestic company which has a direct economic link with investment by the domestic company in a company within another member state is capable of coming within the scope of Article 56, and such a direct economic link is established where the domestic company derives a substantial part of its income from foreign subsidiaries and distributes that income through FIDs to its shareholders.

121. Finally, before leaving this aspect of the appeals, we find confirmation for our conclusions by reference to the position of non-UK investors. Consider the position of a French national contemplating investing in UK companies including BAT. Suppose that he is tax-resident in the UK with significant UK taxable income. But his assets are substantially in France. The analyses in *FII ECJ* and *Accor* demonstrate that this investor may be deterred from investing in BAT rather than a company conducting its undertaking through UK subsidiaries as the result of the FIDs regime. The situation here, however, is clearly not one which is "wholly internal". The discrimination and the barrier to investment for a UK investor is no different from that for the French investor. It would, we think, be an unsatisfactory result if the positions of the two investors were different in relation to the non-compliance of the FIDs regime with Article 56 given that the underlying complaint (i) is the same in each case and (ii) relates to a foreign element.

122. BTPS advanced an alternative argument in resisting HMRC's argument that BTPS has no right to rely on Article 56 in seeking a remedy in relation to the discriminatory tax treatment of FIDs. It relies on three cases to establish the proposition that a person who is adversely affected by an infringement of the fundamental freedoms of another person is entitled to obtain a remedy for that disadvantage. Applying that principle to the present case, BTPS is a person entitled to a remedy in reliance on the breach of the relevant FID paying company's right to free movement of capital since BTPS as a shareholder is the party adversely affected by the less favourable tax treatment which constituted the breach of the company's right under Article 56. The way BTPS is adversely affected is the absence of a tax credit of the FID because of the operation of section 246C of ICTA. Mr Baldry submits that the cases referred to by Mr Vajda do no more than illustrate the principle that more than one party may have directly enforceable rights arising out of a breach of one party's rights which will give another party a remedy as well as the party whose rights have been infringed.

123. The first of these cases is Case C-360/96 *Clean Car Autoservice Gmbh v Landeshauptmann von Wien* [1998] ECR I – 2521. That case concerned the rejection of an application by Clean Car, an Austrian incorporated company, to register to carry on its trade in Austria on the ground that it had appointed as a manager a German national who did not reside in Austria. The question for the ECJ to determine was whether the right of equal treatment in the context of freedom of movement for workers (Article 48 of the Treaty) may also be relied on by an employer in order to employ in his home state, workers who are nationals of another member state. The

ECJ held that such an employer could so rely, its reasoning as set out in paragraphs 19 to 21 of the judgment being as follows:

> "19. Whilst those rights are undoubtedly enjoyed by those directly referred to – namely, workers – there is nothing in the wording of Article 48 to indicate that they may not be relied upon by others, in particular employers.
>
> 20. It must further be noted that, in order to be truly effective, the right of workers to be engaged and employed without discrimination necessarily entails as a corollary the employer's entitlement to engage them in accordance with the rules governing freedom of movement for workers.
>
> 21. Those rules could easily be rendered nugatory if Member States could circumvent the prohibitions which they contain merely by imposing on employers requirements to be met by any worker whom they wish to employ which, if imposed directly on the worker, would constitute restrictions on the exercise of the right to freedom of movement to which that worker is entitled under Article 48 of the Treaty".

124. Mr Vajda submits that the analogy between *Clean Car* and the position of BTPS in relation to FIDS is that, just as in *Clean Car* it was held first, that there was nothing in Article 48 to restrict it to workers, there was nothing in Article 56 to exclude shareholders from a remedy where the company's rights were infringed and secondly, that giving shareholders this remedy makes the enforcement of the right more effective, just as the worker's right was made more effective by allowing the employer to rely on it. The result was to give the employer a remedy which is different and additional to the remedy of the worker. That remedy would be a reversal of the refusal to register the business, the analogue in BTPS's situation would be the grant of the tax credit that has been denied.

125. Mr Baldry analyses the effect of the case differently: he accepts that Article 48 gives both the employer and the employee rights, but the correct analogue is that the corollary breach of the FID-paying company's rights is the breach of the right of the non-resident company in which the UK parent may invest to seek capital from the UK company. That corollary is found in the matters referred to in paragraph 71(2) above.

126. The second of these cases is Case C-294/97 *Eurowings Luftverkehrs AG V Finanzamt Dortmund-Unna* [1999] ECR I-7447 which was relied on by the Tribunal for its finding that BTPS as shareholders could rely on the breach of the Community law rights of the FIDs paying companies to found their own Community law action. Eurowings was a German company which leased an aircraft from an Irish company and was subject to less favourable tax treatment than would have applied had it leased the aircraft from a German company. The question before the ECJ was whether Eurowings was entitled to rely on Article 59 of the Treaty as it then was, which provided for the freedom to provide services, the services in this case being the lease of the aircraft provided by the Irish company to Eurowings. The ECJ decided Eurowings could so rely its reasoning being set out in paragraphs 33 and 34 of its judgment as follows:

> "33. Next, since leasing is a service within the meaning of Article 60 of the EC Treaty (now Article 50 EC), it should be noted that the Court has held that Article 59 of the Treaty requires not only the abolition of any discrimination on account of nationality against a person providing services but also the abolition of any restriction on the freedom to provide services imposed on the ground that the person providing service is established in a Member State other than the one in which the service is provided.

> 34. It has also consistently held that Article 59 of the Treaty conveys rights not only on the providers of services but also on the recipient…… As the recipient of the leasing services, therefore, Eurowings may rely on the individual rights conferred on it by that provision."

5 127. Mr Vajda observes that, as in *Clean Car*, the remedy for both parties would be different: Eurowings was seeking the same fiscal treatment that it would have obtained had it leased the aircraft from a German lessor, whereas the Irish lessor would be seeking a remedy for loss of business if it was able to show the difference of treatment caused it a loss. He submits that the case establishes that where you have a 10 breach of a treaty provision it is not necessarily the case that only one class of person can rely on it. In *Eurowings* the breach gave rise to two different potential remedies, one for each party. In the present appeals, because first, there is a close nexus – an economic link – between the shareholder, BTPS, and the company and a close link between the cross-border movement of capital by the UK resident company and the 15 dividend (the FID) received by BTPS and because secondly, this cross border movement of capital results in a denial to BTPS of the tax credit, Article 56 is engaged both for the company and its shareholder, BTPS. Mr Baldry makes the same submission as he did in relation to *Clean Car*: the case shows that Eurowings had its own right that arose out of the breach of Article 59, not rights that arose because the 20 rights of the Irish lessor were breached.

128. The final case relied on by BTPS is Case C-208/05 *ITC Innovative Technology Center GmbH v Bundesagentur Fur Arbeit* [2007] ECR I-181. ITC was a recruitment agency who found employment for an employee seeking work. The employee submitted to ITC a voucher issued to him by the German authorities which enabled 25 the recruitment agency receiving it to receive payment from the government for finding the employee work. When the voucher was presented by ITC payment was refused on the grounds that the employee concerned was not subject to compulsory social security contributions in Germany because the employment he was found was with a company established in the Netherlands. The issue in the case was whether the 30 refusal to pay the amount in respect of the voucher infringed Article 39 (now Article 48) of the Treaty regarding the free movement of workers.

129. The Court rejected the German Government's argument that Article 39 could not be relied on by ITC on the grounds that it was an intermediary and not an employee and therefore did not fall within the scope of the application of the right to 35 free movement. The Court relied on paragraphs 19 and 20 of the judgement in *Clean Car* set out in paragraph 135 above in concluding on this point that there was no reason why a private sector recruitment agency such as ITC may not, in certain circumstances, rely on the right directly granted to workers by Article 39 (see paragraph 25 of the judgment).

40 130. The Court explained in paragraphs 26 and 27 of its judgment why it was necessary to allow reliance in this case as follows:

> "26. In order to be truly effective, the right of workers to take up an activity as an employed person, and to pursue such activity, within the territory of another Member State without discrimination must also entail as a corollary the right of intermediaries, 45 such as a private-sector recruitment agency, to assist them in finding employment in accordance with the rules governing the freedom of movement of workers.

27. Such an interpretation of the rules in question is all the more necessary in circumstances such as those at issue in the main proceedings, where a private-sector recruitment agency has concluded a recruitment contract with a person seeking employment on the basis of a recruitment voucher issued to that person, in terms of which the Bundesagentur undertook to pay the costs of the private-sector recruitment agency, and not for the person seeking employment, to claim payment from the Bundesagentur in respect of the fee due to that agency"

131. The Court also rejected the argument that the issue was a purely internal one in paragraph 29 and 30 as follows:

"29. …… it must be noted, as regards the German Government's argument that ITC cannot rely on the rights laid down under Article 39 EC because the agency is established in only one Member State, that the Treaty rules governing freedom of movement for persons and measures adopted to implement them cannot be applied to activities which have no factor linking them with any of the situations governed by Community law and which are confined in all relevant respects within a single Member State….

30. However, even though a private-sector recruitment agency established in Germany, such as UTC, seeks to rely on the rules relating to freedom of movement for workers against the German authorities, that does not affect the application of those rules. The agency's complaint is precisely that it was placed at a disadvantage by the system of recruitment vouchers…., with the result that the person seeking employment for whom it found a job was also, or may also, have been placed at a disadvantage by reason of the fact that that job was in another Member State……. "

132. The Court's conclusion in paragraph 36 of its judgment was that the legislation only permitting the payment of the voucher where the employment concerned was subject to compulsory social security contributions in the Member State where it was issued:

"….. creates an obstacle which is capable of discouraging persons seeking employment, particularly those whose financial resources are limited, and accordingly, private sector recruitment agencies, from looking for work in another Member State because of the incumbent fee will not be paid by the Member State of the persons' origin….."

and was thus in principle prohibited by Article 39.

133. Mr Vajda submits that this case further illustrates the principles that more than one person can rely on a breach of Community law with different remedies for each person and also that Community law rights are engaged where there is a link with a cross-border situation and the test is whether there is a substantive link regardless of the form that the arrangements take.

134. In relation to each of these three cases, it is to be observed that it was desirable, and probably necessary, for one person to be given a directly enforceable right in order effectively to vindicate the right which another person (indisputably) had. In that sense, the former was the corollary of the latter. A similar argument can be put in relation to the present appeals. In order for the relevant company (*ie* a company in which BTPS is a shareholder, such as BAT) to be able to exercise its rights under

Article 56 effectively, the shareholder, too, needs to be given directly enforceable rights.

135. Mr Baldry again makes the same submission as he did in relation to the other cases relied on by BTPS, that whilst different parties have their own rights arising out 5 of the breach, it does not give rise to the analogy contended for it by BTPS, namely that the right of a company to move its capital between member states necessarily entails a corollary that the shareholder must be entitled to move capital to that company within the member state. Rather, the corollary is that the subsidiary in which the UK company invests is entitled to be treated in the same way as a UK 10 subsidiary.

136. In our view the cases relied on by Mr Vajda to support his alternative argument do reinforce the general proposition that arises out of the cases that he relied on for his first argument, namely that the ECJ has in all of these cases adopted a broad approach to the circumstances in which one of the fundamental freedoms can be said to have 15 been infringed. The common thread running through all the cases is that provisions of national legislation of a Member State directly applicable only to persons established in that member state are precluded if they create obstacles "capable of discouraging", to use the test set out in paragraph 36 of *ITC*, the person with the primary right to exercise that right. The rationale for giving the person who is subject to the national 20 law provision his own rights is to make the exercise of the primary right "truly effective": see paragraph 20 of *Clean Car* and paragraph 26 of *ITC*. It is also the corollary of the rights of the person exercising the relevant freedom that the person suffering the detriment through the infringement of those rights is entitled to a remedy in Community law.

25 137. We therefore accept Mr Vajda's submission that the cases establish that different parties can acquire their own rights where one of the fundamental freedoms is infringed. To be fair to Mr Baldry, it is not his case that a breach of Article 56 can only ever give rise to a claim by one person. But in accepting Mr Vajda's submission, we are accepting more than Mr Baldry acknowledges since we accept not only the 30 conclusion but agree with the reasoning.

138. To a minor extent, we part company with the Tribunal which based its reasoning on paragraph 34 of *Eurowings*, quoted in paragraph 125 above. The Tribunal's conclusion, at paragraph 75 of the Decision was that paragraph 34 :

> "…. makes it clear that consumers of a supply of services may rely on the breach of 35 Community law rights of the supplier of cross-border services. We see no reason in principle (and we were not shown any case law) why by analogy shareholders of a company whose Community law rights are breached cannot rely on such breach to found their own Community law action".

139. We express the principle slightly differently to the Tribunal; in our view, in the 40 *Eurowings* situation, the consumer of the supply of services is able to rely on the breach of the rights of the supplier to found their own Community Law action arising out of a breach of their own separate rights.

140. This difference does not, however, help Mr Baldry. We accept that the analogy drawn by the Tribunal and Mr Vajda is the correct one. Applying our reasoning, the 45 provisions of Section 246C of ICTA denying BTPS a tax credit on the payment of a FID amounts to an infringement of the Article 56 rights of, on our example, BAT.

That has been held to be the case in *FII ECJ*. That provision is capable of discouraging BAT from seeking to exercise its Article 56 rights and therefore gives rise to a separate right on the part of the person who is subject to that provision, namely BTPS, to found a Community law right. Such a right is a necessary corollary in order to make BAT's right "truly effective" because without it BTPS is likely to be discouraged from investing in companies such as BAT which invest a substantial amount of its capital raised from UK shareholders such as BTPS in foreign subsidiaries. We therefore reject Mr Baldry's submission that the only other rights that arise out of the breach of BAT's Article 56 rights are the rights of its foreign subsidiaries to raise capital from BAT in the UK. Mr Baldry could only be right on that point if, as he submitted, BTPS had no rights because the situation was one which was "wholly internal" to the UK. Both the line of cases relied on by Mr Vajda for his alternative argument, and those relied on for his primary argument shows that this is not a "wholly internal situation."

141. We therefore conclude that BTPS can rely on the breach of the FID-paying company's Article 56 right to found a claim of its own, whether it be on the basis that it has made a movement of capital of its own by investing in a FID-paying company which derives a substantial part of its income from investment in foreign subsidiaries or on the basis that it arises out of separate rights founded upon the breach of the FID-paying company's own Article 56 rights.

142. For completeness, we mention one further submission of Mr Baldry. He points out that the basis of the ECJ's decision in *FII ECJ* was that the shareholders were not entitled to a tax credit so that an enhanced dividend must be declared to achieve the same measure of return as that which would be achieved from nationally-sourced dividends: that was one of the reasons why the FID-paying company was disadvantaged in attracting investors in comparison with a company all of whose subsidiaries were UK subsidiaries. Mr Baldry submits that there is complete inconsistency between what the Tribunal has said and the premise of the case before the ECJ as just articulated. In other words, the ECJ's approach is consistent only with the proposition that the shareholders have no directly enforceable right to a tax credit as the result of the breach of Article 56.

143. We do not agree with that conclusion. The position under domestic law was clear, namely that shareholders receiving a FID were not entitled to a tax credit. Whatever their rights under Community law are eventually shown to be, it is beyond argument that potential investors could only invest on the basis of domestic legislation and against the background – if they were particularly astute – that following lengthy heavily opposed litigation, they might be able to establish rights under Community law to some sort of credit. It has not been suggested – hardly surprisingly we think – at any stage of the *FII* proceedings or in the present proceedings (before the Tribunal or ourselves) that the fund managers in BTPS invested in companies such as BAT with subsidiaries all over the world with the idea – let alone a hope or expectation – that they would be able to obtain a credit. Moreover, if that had been the expectation, there might have been considerable reluctance on the part of FID-paying companies to pay enhanced dividends. But that is speculation and we cannot take account of it. But what is not speculation is that the domestic legislation gave no tax credit and that that factor was sufficient – whatever the position under Community law might eventually be shown to be – to justify the approach of the ECJ in paragraphs 148 and 149 of its judgment.

Remedies

144. We now turn to the remedies available to BTPS as a consequence of this breach.

145. Mr Baldry submits that if we find (as we have) that BTPS's directly enforceable rights were infringed, the appropriate remedy would be to disapply section 246C of ICTA and to give section 231 of ICTA a conforming construction to enable BTPS to claim a tax credit on a FID to the extent they are so entitled under Community law.

146. BTPS's claims are made on the basis that they should be entitled to a full tax credit on the dividends paid by the FID-paying companies. However Mr Baldry submits that it was central to the concept of the UK granting a tax credit to a shareholder that ACT was payable in respect of the dividend. Under Community law, however the FID-paying companies are entitled to a credit (against their ACT liability) for the foreign corporation tax actually paid in respect of the dividend paid to BTPS. Moreover, under domestic law the FID-paying companies were entitled to repayment of the ACT to the extent it was not utilised against the mainstream corporation tax.

147. In HMRC's submission, the appropriate conforming construction to section 231 should therefore ensure that BTPS becomes entitled to a tax credit of an amount equal to the amount of the foreign tax which it has suffered in respect of the foreign dividend, as Mr Baldry put it in his skeleton argument. Such an amount, it is submitted, ensures that BTPS receives a tax credit for the ACT truly paid in respect of that dividend. Anything further would simply be a windfall for BTPS.

148. Mr Vajda submits that the detriment that BTPS has suffered is the denial of a tax credit on the payment of FIDs. Under Community law, the correct remedy where a tax is levied in breach of Community law is a refund of the tax so levied. In order to give effect to that principle in this case, HMRC are obliged to give to BTPS the same tax credit on FIDs as it would have given on UK sourced dividends. This he submits, can be illustrated by reference to examples (a) and (b) set out in paragraph 14 above; if BTPS is given the same tax credit where it receives a FID (worth £16.75 on the example given) as it receives when it receives a UK sourced dividend, the amount received will give the same return in both situations, namely a net distribution of £83.75.

149. The Tribunal decided this point very shortly in paragraph 95 of its decision, as both parties agreed that disapplication of Section 246C was the relevant remedy. The Tribunal stated:

> "In a case where there are directly enforceable rights (to the free movement of capital) sympathetic construction of Section 246C is out of the question. Section 246C would hardly be clearer that tax credits are not to be paid in the case of a FID. That leaves disapplication"

150. HMRC's changed position on this issue in this appeal is based on the Court of Appeal's decision in *FII GLO* [2010] EWCA Civ 103 which was not available when this issue was argued in the Tribunal. At first instance in *FII GLO* Henderson J held that the simplest and most appropriate way to achieve compliance as between the UK's ACT provisions and Community law would be to remove the UK territorial limitation on franked investment income so that it included foreign dividends received by a UK company resident from a company resident in another member state. As a result the foreign dividend would be treated as though it had carried an entitlement to

a tax credit and thus generated franked investment income in the hands of the FID-paying company. Accordingly, the FID-paying company would be entitled to a tax credit to set off against its own liability for ACT when making an onward distribution to its own shareholders.

151. In considering this issue, the Court of Appeal did so by reframing it so it became a question as to whether the ACT provisions can be read in a manner which is compatible with Community law, following the well established principle that the Court must interpret a statute which is on the face of it inconsistent with Community law so far as possible so as to be compatible with Community law. The exercise was designed to see whether the Court could read in words or limit provisions provided that this can be done by the process of interpretation properly so called and does not go against "the grain" or cardinal features of the legislation: see paragraph 97 of the judgment.

152. The question to be determined was set out in paragraph 98 of the judgment as follows:

> "Attention has centred on ICTA, s231 which sets out the principal rule as to entitlement to a credit corresponding to the ACT paid. The question is whether that section can be read in conformity with Community law so that the entitlement to a tax credit is available not just to resident companies but also to all other persons entitled under Community law to be treated in the same way"

153. The Court of Appeal rejected Henderson J's approach of giving a tax credit for foreign sourced dividends on the same basis for UK sourced dividends, its reasoning as set out in paragraph 102 of the judgment being as follows:

> "The difficulty with the judge's approach is that it is liable to confer a windfall on taxpayers since it applies to all foreign-source dividends and not just those where Community law rights have been infringed. It is thus outside the scope of conforming interpretation unless mandated by the Community law principle of effectiveness….."

154. The Court of Appeal considered it could adopt a conforming interpretation instead. At paragraph 107 of its judgment it stated

> "It therefore falls to this court to determine the appropriate conforming interpretation. In our judgment, a conforming interpretation can be achieved simply by reading in words that make it clear that it is not just resident companies that can claim a credit under s 231 but also other persons entitled to do so by Community law to the extent that they are so entitled. The extent of that entitlement can then be investigated when the section falls to be applied, rather than the difficulties more properly arising at the point of application being erected as an objection to conforming interpretation. It will apply even if the extent of the entitlement is not fully ascertained until after the ECJ has answered any question put to it in a further reference".

155. We have found the expression of the conclusion and the reasoning of the Court of Appeal in the quoted passages slightly problematical. The first problem relates to the distinction between a conforming interpretation and disapplication, a distinction which the Court had well in mind as can be seen from paragraph 97. In any case, the Court can hardly have overlooked what Henderson J said at paragraph 143 of his own judgment on this aspect. It appears from paragraph 144 of that judgment that the parties before Henderson J did not suggest that a conforming construction was possible and the Judge himself agreed with their stance. The Court of Appeal,

however, referred to the claimants at the hearing before Henderson J having put forward alternative conforming constructions; but, with respect, we do not see how that can be correct given (a) what Henderson J said in paragraph 144 about the parties' positions and (b) how Mr Aaronson QC (for the claimants) put the matter, that is to say in terms of considerable textual changes. Be that as it may, the Court of Appeal saw the question as one of conforming interpretation and we are bound by its conclusions in relation to section 231 so far as concerns FID-paying companies at least.

156. The second problem is this. The question formulated in paragraph 98 is raised in the context of a regime which is non-compliant with Community law and is focused on the remedy for that breach. It seems to us that the relevant issue in the case before the Court of Appeal was how section 231 was to be interpreted in order to remedy that breach. Accordingly, the question was surely what, if any credit, the company receiving the dividend (that is to say in the present appeals the FID-paying company) which, *ex hypothesi*, is a UK company should be entitled to in respect of a dividend paid by a non-UK company. We do not understand how an issue ever arises in relation to a tax credit available to a non-UK company. Indeed, the issue in *FII* was whether UK companies should be entitled to tax credits: the foreign element did not concern credits available to a non-UK company but how foreign dividends sourced from foreign profits were to be treated.

157. Having said that, we think that the thrust of the decision is clear. The Court rejected Henderson J's solution which was to treat the UK dividend-paying company as receiving FII from the foreign dividend-paying company. Under that approach, the company obtained a tax credit in relation to the amount received in exactly the same way as a tax credit received from a UK company. Henderson J was not concerned with the tax position of a non-UK company other than that it might have suffered foreign corporation tax. The Court of Appeal considered that Henderson J's approach could result in a windfall for the UK dividend-paying company. We give an example: suppose a dividend was payable from a foreign company where the underlying profit had not been taxed at all, so that the UK company received 100% of the profit. To give that company a full tax credit would compensate it for a disadvantage which it had not suffered since, having received 100% of the profit from the subsidiary, it would actually have in hand the funds with which to pay the ACT on the dividend. Similarly, if the rate of tax on the foreign subsidiary was less than the rate of ACT, the dividend paying company should only receive a credit sufficient to reflect the underlying foreign tax actually paid by the subsidiary.

158. Accordingly, the Court of Appeal held that a conforming interpretation of section 231 required only that a credit should be given for the tax paid. That, at least, is how we understand the reasoning. The conclusion in paragraph 107 that it is not just resident companies that can claim a credit under s 231 but also other persons entitled to do so by Community law to the extent that they are so entitled is, we think, a mere infelicity in language.

159. The result of this would be that to the extent that the recipient of the foreign dividend, in this case the FID-paying company, could prove the amount of the foreign tax paid by the company paying the dividend it would claim a credit for that against the ACT it paid when passing that dividend on, thus giving the FID-paying company a claim for the time value of the excess amount of ACT that it paid in respect of the dividend.

160. The Court of Appeal in *FII GLO* was of course only dealing with the position of the FID-paying company. Mr Baldry relies on the analysis of the correct remedy for the FID-paying company to argue that the application of the "no windfall" principle formulated by the Court of Appeal should mean that BTPS's tax credit should be restricted to the amount equal to the ACT which was properly due to be paid by the FID-paying company under Community law and not repaid to the FID-paying company, thus replacing the blanket ban on a tax credit under section 246C with a conforming construction of Section 231 to that effect.

161. Mr Baldry's analysis is dependent on establishing a clear linkage between the payment of ACT by the FID-paying company and the right of BTPS to claim a tax credit on the basis that a tax credit under Section 231 of ICTA is dependent on the dividend paying company having suffered underlying tax or ACT. The Tribunal rejected that analysis, stating in paragraph 64 of its decision that the imputation mechanism in Section 231 (1) of ICTA is a "broad axe" approach which assumes that dividends will be subject to double economic taxation and mitigates that prospect by way of a credit which reduces the tax charge of a shareholder who receives a dividend, without enquiring whether the dividend paying company has actually suffered underlying tax on its profits. The Tribunal's analysis was that ACT is simply a prepayment of corporation tax by a dividend paying company and is in no sense a deduction of tax at source for the recipient shareholder.

162. We do not consider that that analysis can stand in the light of the decision of the Court of Appeal concerning the conformable construction of section 231. If the Tribunal's analysis were correct, then one would be left with Henderson J's interpretation of section 231 which has been rejected. Whether that is right or wrong may not matter. We have already found that the FIDs regime amounted to a breach of BTPS's own Article 56 rights and were not parasitical upon the FID paying company's rights. In our view in *FII ECJ* the ECJ clearly found that the way in which those rights were infringed was the denial of a tax credit upon the payment of a FID by virtue of Section 246C: see paragraph 173 of the judgment set out in paragraph 86 above. This is different to the way in which the FID paying company's rights were infringed; as is described in paragraph 173 of the judgment in *FII ECJ* their rights are infringed by having to pay ACT and then reclaim it which, as we describe in paragraph 87 above gives rise to a claim for the time value of the ACT which it had paid and which was subsequently refunded.

163. It is also clear that in *FII ECJ* the ECJ rejected the UK government's arguments that the difference in treatment between the payment of UK sourced dividends and the payment of non-UK sourced dividends does not amount to discrimination because it was based on a distinction between dividends on which ACT had been paid and on those on which no ACT has been paid, so that in the case of a company receiving dividends from a non-resident company where no ACT had been paid by the latter there is no risk of economic double taxation as regards ACT.

164. The argument was rejected in paragraphs 86 to 91 of the judgment as follows:

> "86. While it is true that under the national legislation at issue in the main proceedings the amount of ACT which a resident company must pay on a distribution by way of dividend to its own shareholders depends on whether that company has, or has not, received dividends form a company which has already paid ACT, the fact remains that the system leads, in practice, to a company receiving foreign-sourced dividends being less favourably treated than a company

receiving nationally-sourced dividends. On a subsequent payment of dividends, the former is obliged to account for ACT in full, whereas the latter has to pay ACT only to the extent to which the distribution paid to its own shareholders exceeds that which the company has itself received.

5 87. Contrary to what the United Kingdom government contends, a company receiving foreign-sourced dividends is, seen in the light of the objective of preventing the imposition of a series of charges to tax which the legislation at issue in the main proceedings seeks to avoid, in a comparable situation to that of a company receiving nationally-sourced dividends, even though only the latter 10 receives dividends on which ACT has been paid.

88. As the Advocate General states in paras 65 to 68 of his opinion, the ACT payable by a United Kingdom-resident company is nothing more than a payment of corporation tax in advance, even though it is levied in advance when dividends are paid and calculated by reference to the amount of those dividends. The ACT which 15 is paid on a distribution by way of dividend may, in principle, be set off against the corporation tax which a company must pay on its profits for the corresponding accounting period. Likewise as the court held when it ruled on the group income scheme established under the same tax legislation which was in force in the United Kingdom, the proportion of corporation tax which a resident company need not pay 20 in advance under such a scheme when paying dividends to its parent company is, in principle, paid when the liability of the first company to corporation tax falls due ….

89. In the case of companies which, because their seat is outside the United Kingdom, are not obliged to pay ACT when they pay dividends to a resident 25 company, it is clear that they are also liable to corporation tax in the state in which they are resident.

90. That being the case, the fact that a non-resident company has not been required to pay ACT when paying dividends to a resident company cannot be relied on in order to refuse that company the opportunity to reduce the amount of ACT 30 which it is obliged to pay on a subsequent distribution by way of dividend. The reason why such a non-resident company is not liable to ACT is that it is subject to corporation tax, not in the United Kingdom, but in the state in which it is resident. A company cannot be required to pay in advance tax to which it will never be liable ….

35 91. Since both resident companies distributing dividends to other resident companies and non-resident companies making such a distribution are subject, in the state in which they are resident, to corporation tax, a national measure which is designed to avoid a series of charges to tax on distributed profits only as regards companies receiving dividends from other resident companies, while exposing 40 companies receiving dividends from non-resident companies to a cash-flow disadvantage, cannot be justified by a relevant difference in the situation of those companies"

165. It is to be noted in rejecting the UK Government arguments, the ECJ found, in common with the Tribunal, that the ACT payable by a UK resident company is 45 nothing more than a payment of corporation tax in advance.

166. The Court then applied this reasoning to its findings that the absence of a tax credit on the payment of a FID is discriminatory in paragraph 158 and 159 of the judgment as follows:

> "158. As regards the fact that shareholders are not entitled to a tax credit under the FID regime, the United Kingdom government argues that such a tax credit is granted to a shareholder receiving a distribution only where there is economic double taxation of the profits distributed which must be prevented or mitigated. That does not apply to the FID regime inasmuch as, first, no ACT has been accounted for on foreign-sourced dividends and, secondly, the ACT which the resident company receiving those dividends must account for on making a distribution to its shareholders is subsequently repaid.
>
> 159. However, that argument is based on the same false premises that a risk of economic double taxation arises only in the case of dividends paid by a resident company subject to an obligation to account for ACT on dividends distributed by it, whereas the true position is that such a risk also exists in the case of dividends paid by a non-resident company, the profits of which are also subject to corporation tax in the state in which it is resident, at the rates and according to the rules applying there".

167. The double taxation situation is dealt with, as far as the FID paying company is concerned, in the light of the Court of Appeal's judgment in *FII GLO* in the manner described in paragraph 159 above. However, BTPS's claim for a tax credit in respect of FIDs is not dependent on the foreign tax that has been paid in respect of the dividend which it receives as a FID. The foreign tax will already have been taken into account in calculating the FID-paying company's UK Corporation tax liabilities.

168. On that basis, it can be said that the carrying out of the conforming construction exercise is applicable only to the remedies available to the FID-paying company and has no application to the separate remedy available to the shareholder, in this case BTPS. BTPS's claim is simply to receive the same tax credit in respect of the FIDs it receives as it does in respect of UK sourced dividends, both these payments being made by a UK resident company as the most appropriate way of dealing with the infringement of its Article 56 rights. To put this point more succinctly, once section 246C is disapplied, there is nothing more which needs to be done: section 231 can be given effect to according to its terms.

169. That is not an end of the story, however. The approach we have just considered involves two parts (disapplication of section 246C and continued application of section 231). That approach views the two parts as separate, whereas Article 56 simply requires effect to be given to a person's rights under that Article. If simple disapplication of section 246C results in the shareholders in a FIDs-paying company obtaining more than Article 56 requires, we see no reason why section 231 should not be interpreted (if that can be done in accordance with established principles) in a way which cuts down the shareholders rights under section 231 as it stands.

170. It is on that basis, we imagine, that Mr Baldry feels able to take a different approach which is set out in paragraph 146 and 147 above. He contends that his approach complies with Article 56 and that section 231 should be read as he would read it in order that shareholders are not given too much.

171. We turn, then, to consider what the result of his approach would be in the context of Article 56, in particular the difference in treatment, if any, from the shareholders' perspective of dividends from UK and foreign subsidiaries of the FID-paying company. For the years in question, a dividend from a UK subsidiary would have represented profits after payment of UK corporation tax; the dividend was not subject to corporation tax in the hands of the parent company. An onward distribution to shareholders was subject to ACT and the shareholders received a tax credit for an

amount equal to the amounts of the ACT. Broadly speaking, therefore, the shareholders received an amount of cash equal to the post-corporation tax profit of the subsidiary together with a tax credit equal to the amount of the ACT (not, it is to be noted, precisely equal to the amount of the underlying corporation tax). A dividend (a FID) from a foreign subsidiary represented profits after payment of foreign corporation tax. The FID-paying company was subject to corporation tax (under Schedule D Case V) on the total of (i) the cash payment (ii) and withholding tax and (iii) the foreign underlying tax (the case under consideration being one where the FID-paying company owned more than 10% of the share capital of the foreign company since, *ex hypothesi*, we are presently concerned with subsidiaries). The FID-paying company was entitled to relief under sections 788 and 790 ICTA 1988 for the withholding tax and foreign underlying tax.

172. Take an example of UK and foreign subsidiaries each with a pre-tax profit of £100. In the case of the UK subsidiary, and assuming a corporation tax rate of 30%, £70 is available for distribution. That sum is paid to the FID-paying company with a tax credit of £30 and the total amount is FII. The £70 is then distributed to the shareholders with a tax credit of £30, but there is no ACT. In the case of the foreign subsidiary, and assuming a foreign corporation tax rate of, say 20%, £80 is available for distribution. The FID-paying company receives a cash payment of £80 but its income for corporation tax purposes is £100. It is taxable on £100 but receives credit under section 788 and 790 for the £20 foreign tax. After making provision for the £10 additional tax, it has £70 available for distribution. On HMRC's approach, even if the whole £70 could be distributed (which may not be possible in the light of the obligation to pay ACT being almost immediate but recovery of surplus ACT being delayed), the shareholders would obtain a tax credit of £20. This contrasts with the tax credit of the comparator UK company of £30.

173. This, it seems to us, is to preserve precisely one of the features which led the ECJ, at paragraphs 148 and 149 of its judgment in *FII ECJ*, to conclude that there was a breach of Article 56. It follows that unless the shareholders are given the full credit which BTPS submits is the entitlement, there will remain in place a breach of Article 56 even *vis a vis* the FID-paying company. It shows that the shareholders' rights are the corollary of the FID-paying company's rights and supports our conclusion that the shareholders have directly enforceable rights.

174. We therefore come to the same conclusion as the Tribunal on the issue of remedies in relation to the FIDs claims. Although there is, in theory, scope for a conforming construction, we do not consider that HMRC's construction achieves it whereas BTPS's construction does so. The appropriate remedy is disapplication of section 246C of ICTA and nothing more.

175. If our reasoning is correct, we can see no justification for concluding that an exempt taxpayer such as BTPS should not be entitled to the full tax credit in the same way as a fully taxable person.

Fiscal Supervision

176. Finally in relation to the FIDs claims, we turn to the question whether the breach of Article 56 would, in relation to claims in respect of dividends from third country sources, be justified on the grounds of "effective fiscal supervision". The principle is engaged where, as part of the exercise to ensure the domestic legislation does not treat foreign sourced dividends less favourably than UK sourced dividends, it

is necessary to give credit for underlying foreign tax paid in respect of those foreign sourced dividends. At that point Article 58 (1) (b) of the Treaty, as set out in paragraph 24 above, is applicable to the extent that measures under Article 58(1)(b) may be justified where they require provisions to be put in place pursuant to which the amount of underlying tax can be verified, and in the absence of such provisions the Article 56 breach may be justified.

177. Consistent with his submissions on how to give a conforming construction to Section 231 as described above, Mr Baldry submits that the tax credit should only be given in respect of dividends from those third countries in respect of which under the relevant double tax treaty the United Kingdom has the power to verify the amount of foreign tax paid, that is where the tax treaty concerned contains exchange of information provisions which oblige the third country to produce information to the UK on the tax paid to it by the company in question. Where no such provisions are to be found in the relevant treaty, HMRC submits that the UK is justified in not providing any tax credit.

178. In the light of our conclusion in paragraph 173 above that the question of what underlying foreign tax was paid by the FID-paying company has no bearing on BTPS's FIDs claim and that the appropriate remedy is disapplication of section 246C, it follows that the concept of "effective fiscal supervision" of the foreign tax cannot be engaged at all. This concept could only come into play had we accepted Mr Baldry's arguments on the scope of a conforming construction.

X Discussion: the *Manninen* claims

Liability

179. We start by reminding ourselves of the factual scenario here: BTPS has invested a significant part of its equities portfolio directly in large quoted companies which are resident overseas. In these cases the investments are held purely as portfolio investments with no significant influence over the management of those companies.

180. The different tax treatment in the UK of dividends received by BTPS from UK resident companies and dividends received from companies resident outside the UK is explained by Henderson J in *FII GLO* in the passages we quote in paragraph 11 above. We do not need to repeat them here.

181. The UK tax system did not give tax credits to entities that were exempt from tax on their investment income, such as BTPS, in respect of dividends received from non-UK companies. By virtue of Section 592 of ICTA, BTPS would be exempt from tax on this income but the dividends would have been paid by companies who generally would have been liable to corporation tax on their profits in their home state. It is likely therefore that those companies would have paid underlying corporation tax to the local tax authorities on their profits and paid some of the net profits to their shareholders by way of dividends.

182. It is common ground between the parties that BTPS, by investing in non-UK resident companies, was exercising its right under Article 56 to move capital. The question is therefore whether the difference in treatment between the tax treatment of dividends sourced from UK companies and those sourced from non-UK resident

companies occasioned by the fact that no tax credit is available in respect of the latter infringes those rights in any way.

183. In paragraph 71 above we identified as one of the principles derived from the cases of *Verkooijen, Lenz* and *Manninen* that a dividend received in a Member State from a company established in another Member State cannot be subjected to tax in a less favourable way than a dividend received in the first Member State from a company established in that member state. In the case of *Manninen* the infringement of this principle arose because whilst the Finnish tax system allowed the Finnish taxpayer a credit for part of the corporation tax paid by a Finnish company at a rate of 29/71sts of the dividends paid, it did not do so in relation to dividends received from a company established in another Member State: see paragraph 20 of the judgment quoted in paragraph 66 above. So the result in *Manninen* was that, on receipt of a dividend from a Finnish company which was taxed at 29%, the shareholder would pay no further tax on the dividend he received because of the operation of the tax credit, whereas when he received a dividend from a Swedish company he was taxed at 29% on that dividend without the benefit of a tax credit. As the Swedish dividend had borne a withholding tax of 15% which the Finnish taxpayer was able to set against his liability to Finnish dividend tax, the absence of a tax credit for the balance of 14% meant there was less favourable treatment in a comparable situation for the dividends received from the Swedish company.

184. Mr Baldry submits that this principle does not go so far as to require the UK government to pay a tax credit to a person who is exempt from tax in the UK. Specifically, Mr Baldry submits that the *Manninen* line of cases is concerned solely with the situation where a Member State treats a foreign dividend less favourably than a domestic dividend by imposing tax on that dividend without giving credit for foreign tax paid (in circumstances where credit for domestic tax is given). He submits that *Manninen* is only dealing with a situation involving a "fully taxable" shareholder, that is a shareholder who is liable to tax on the dividends he receives from companies resident in his home state and dividends received from companies established in other member states. The essential difference with the present case is that the UK imposes no tax on foreign dividends or on domestic dividends received by BTPS. BTPS is exempt from UK income tax on all its dividends.

185. Under the Finnish tax system, the logic of the imputation system that it operated meant that the Finnish taxpayer should be granted a tax credit for the tax paid by the Finnish dividend paying company, so likewise when he received a dividend from a Swedish company in respect of which he was fully taxable he should be given a credit for underlying tax paid by that company in order to ensure there is no less favourable treatment in respect of the Swedish dividends. This outcome, he submits, is envisaged in paragraph 54 of the judgment in *Manninen* where it is stated:

> "In those circumstances, the calculation of a tax credit granted to a shareholder fully taxable in Finland, who has received dividends from a company established in Sweden, must take account of the tax actually paid by the company established in that other Member State, as such tax arises from the general rules on calculating the basis of assessment and from the rate of corporation tax in that latter Member State. Possible difficulties in determining the tax actually paid cannot, in any event, justify an obstacle to the free movement of capital such as that which arises from the legislation at issue in the main proceedings …"

186. Mr Baldry submits that the logic of the UK's imputation system was that BTPS should be granted a credit for the ACT paid by the UK resident dividend-paying company in respect of which by virtue of section 592 ICTA it was not liable to tax, so logic dictates that a tax credit should exist to enable BTPS to obtain repayment of that tax. Since BTPS, by virtue of section 592, pays no tax on any foreign dividends it receives and none of the foreign tax paid by the non-UK resident dividend paying company is imputed to BTPS there is no reason why it should be given a tax credit for any of that foreign tax.

187. In essence, Mr Baldry submits that there is nothing in *Manninen* to suggest that the UK government should be required to pay sums in cash to BTPS in respect of foreign tax paid by non-UK resident companies which would be the effect of granting it a tax credit. He submits that this position is supported by a line of cases that followed *Manninen*.

188. The first of these cases, Case C-292/04 *Wienand Meilicke and Others v Finanzamt Bonn-Innenstadt* [2007] ECRI-1835 ("*Meilicke I*"), was essentially a rerun of *Manninen* by reference to the German tax system. Mr Meilicke was a German national who had received dividends from companies resident in the Netherlands and Denmark which were taxable in his hands. Consequently he claimed the tax credit which he would have been entitled to had he received those dividends from German companies, very similar to the situation in *Manninen*. It was clear that the overseas companies had paid tax at a higher rate than in Germany, so Mr Meilicke was asking the German tax authorities to provide a credit not only for the German tax he had been charged (because tax credits were only available for dividends paid by German companies) but an additional amount to match the tax borne in the Netherlands and Denmark.

189. The ECJ came to exactly the same conclusion in relation to the German tax system as it had in relation to the Finnish system. In paragraph 31 of its judgment it stated:

> "In the light of the above matters, the reply to the question referred must be that Articles 56 EC and 58 EC are to be interpreted as precluding tax legislation under which, on a distribution of dividends by a capital company, a shareholder who is fully taxable in a Member State is entitled to a tax credit, calculated by reference to the corporation tax rate on the distributed profits, if the dividend-paying company is established in that same member State but not if it is established in another Member State"

190. It should be noted, however, that the court did not deal with the issue as to whether the German tax authorities were obliged to give credit for an amount higher than that available in Germany, to take account of the higher rates of tax in the Netherlands and Denmark. This issue was considered by the ECJ later in Case C-262/09 *Meilicke and others v Finanzamt Bonn-Innenstadt* [2011] ECR I- 0000 (*"Meilicke II"*) which is referred to in paragraph 200 below.

191. Mr Baldry referred us to Case C-194/06 *Staatssecretaris van Financien v Orange European Smallcap Fund NV* [2008] ECR I-3747 *("Orange Smallcap")* which was decided between *Meilicke I* and *Meilicke II*. He relied on this case to show how the ECJ had treated the situation of a taxpayer that was exempt from tax differently from the "fully taxable" shareholder in *Manninen.* He contended that *Orange Smallcap* supported his submission that the principles laid down in Manninen

had no application to a shareholder who was exempt from tax in his home state in respect of foreign dividends.

192. The facts of *Orange Smallcap* as far as relevant were as follows. Orange Smallcap was an investment company established in the Netherlands. A special tax regime applied to such companies which, like Orange Smallcap, met certain conditions including a requirement to distribute all of the income it received to its shareholders. Under that regime, Orange Smallcap was liable to corporation tax in the Netherlands but its profits were taxed at a rate of 0%. Where Orange Smallcap received a dividend from a company established in the Netherlands it did so under deduction of a withholding tax of 15% of the dividend made by the company paying the dividend. This withholding tax was treated under Netherlands law as an advance payment of the corporation tax payable on it for which the company receiving it would be liable but since Orange Smallcap was not liable to tax on its income it was able to obtain a full refund of it.

193. Where Orange Smallcap received dividends from companies established in other Member States where similarly a withholding tax had been levied it was unable to obtain a credit for any such withholding tax as Netherlands law only permitted such tax to be set off against Netherlands corporation tax attributable to the dividend in question and as Orange Smallcap was taxed at the rate of 0% no credit was available.

194. The objective of the special regime for investment companies was to ensure that investors in such companies received the same tax treatment in respect of the investment company's underlying investments as they would have done had they invested in those investment directly, thus as far as possible the investment company was tax transparent. Had the shareholders invested directly, they would have been able to obtain tax credits under the terms of various double tax treaties between the Netherlands and other countries. To achieve a similar position, the regime established a system of concessions for the investment company designed to take account of foreign tax deducted from dividends received by the investment company.

195. The Netherlands authorities declined to apply the concession so as to take account of the foreign tax deducted from certain dividends paid by companies resident in Germany and Portugal because at the material time the double tax convention between Germany and the Netherlands made no provision for a right of set off for tax deducted in Germany and there was no convention with Portugal at all at the time.

196. Orange Smallcap submitted that the difference in treatment between dividends from the Netherlands company, where the Netherlands authorities reimbursed in full the withholding tax in respect of those dividends, and dividends from Germany and Portugal, where those authorities refused to allow a credit for the tax deducted from such dividends, amounted to a breach of Article 56 on the basis that the Netherlands treated dividends paid by German and Portuguese companies less favourably than those paid by a Netherlands company.

197. The ECJ rejected this argument. In paragraph 34 of its judgment it observed that Orange Smallcap was not subject to tax on dividends under Netherlands law whatever the origin of the dividends and then set out its reasoning in paragraph 35 to 37 of its judgment as follows:

> " 35. Consequently, by not charging fiscal investment enterprises tax on dividends from Germany or Portugal, the Kingdom of the Netherlands treats those dividends in the

same way as dividends from Netherlands companies, in respect of which those enterprises are not taxed either. In addition, by refraining from taxing dividends from other Member States, the Kingdom of the Netherlands avoids the imposition of a series of charges to tax arising from the exercise of its own fiscal power, just as it does in respect of dividends paid by Netherlands companies.

36. Therefore, contrary to the assertions of OESF and the Commission, Netherlands legislation, such as that at issue in the main proceedings, does not treat dividends from Germany or Portugal differently from dividends distributed by Netherlands companies.

37. While, in those circumstances, dividends from Germany or Portugal are subject to a greater tax burden than are dividends distributed by Netherlands companies, that disadvantage is not attributable to the Netherlands legislation at issue in the main proceedings, but is the product of the parallel exercise of fiscal sovereignty by the Member States in which the distributing companies are established and the Member State in which the recipient company is established, whereby the former chose to impose a series of charges to tax on distributed dividends and the latter opted to refrain from any taxation of dividends with respect to fiscal investment enterprises …."

198. Mr Baldry submits that this result is exactly the same as what he contends should be the position in the United Kingdom with regard to the operation of the tax exemption available to BTPS under section 592 of ICTA and the operation of the imputation system. He submits that Orange Smallcap and BTPS are in the same situation; both are exempt in their home state from taxation on dividends whatever the origin of those dividends. BTPS's tax free position is achieved as far as domestic dividends are concerned by the grant of a tax credit, a position that the Netherlands achieves for Orange Smallcap by the refund of the withholding tax in respect of the domestic dividends. As far as the foreign dividends are concerned, neither jurisdiction taxes them in the hands of the recipient. There may be a lower dividend yield on those dividends as a result of the foreign taxes paid but that is because of the taxation systems of the foreign government concerned and not because of any decision by the UK or Netherlands government respectively. Mr Baldry submits that *Orange Smallcap* makes it clear that it is not for the UK government to pay BTPS a cash sum to compensate it for the foreign tax levied, as long as it does not tax the foreign dividend at all.

199. Mr Baldry also relies on *Meilicke II* to demonstrate that *Orange Smallcap* is not merely an expression of a narrow principle confined to the withholding tax that applied in that particular case, the Tribunal having distinguished *Orange Smallcap* on the basis that the withholding taxes at issue in that case were different in character to ACT which, as is common ground between the parties, is not a withholding tax.

200. *Meilicke II* dealt with the issue left over from *Meilicke I*, namely whether Mr Meilicke could claim a credit up to the amount of the rates of tax paid in the Netherlands and Denmark, which were higher than those prevailing in his home state of Germany. The Court rejected such a claim, finding that it was sufficient to ensure that there was no breach of Article 56 that the double taxation which the German tax system had caused by taxing the foreign dividends if the German authorities eliminated the double taxation by giving credit for the foreign tax actually paid up to the amount of the rate charged in Germany, but no further. The reasoning of the Court was set out in paragraph 32 to 34 of the judgment as follows:

"32. In a context such as that in the case in the main proceedings, the obligation of a Member State to eliminate double taxation on a natural person benefiting ultimately

from dividends of foreign origin is limited to the deduction of the corporation tax paid by the dividend-paying company on dividends distributed, according to the law of the Member State in which the company is established, from the income tax payable by the shareholder in respect of those dividends.

5 33. As the Finanzamt Köln and the German Government claim, the principle of free movement of capital, in Article 56(1) TFEU, cannot have the effect of requiring Member States to go beyond the cancelling of national income tax payable by a shareholder on dividends of foreign origin received and the reimbursing of a sum whose origin is in the tax system of another Member State.

10 34. In the light of the foregoing, the answer to the first question, read in conjunction with the two following, is that for the calculation of the amount of the tax credit to which a shareholder who is fully taxable in one Member State is entitled with regard to dividends paid by a capital company established in another Member State, Articles 56 EC and 58 EC preclude the application – if evidence required under the legislation of 15 the first Member State is not adduced – of a provision such as Paragraph 36(2), second sentence, point 3 of the EStG, under which corporation tax attached to gross dividends distributed by companies in the first Member State. The calculation of the tax credit must be made in relation to the rate of corporation tax on the distributed profits applicable to the dividend-paying company according to the law of its Member State of 20 establishment; however the amount to be imposed may not exceed the amount of the income tax to be paid on dividends received by the recipient shareholder in the Member State in which that shareholder is fully taxable."

201. Mr Baldry submits that this case, together with *Orange Smallcap*, which it expressly followed, articulates the principle that member states cannot charge tax less 25 favourably on foreign dividends but they are not obliged to reimburse investors for less favourable treatment caused by the levying of foreign tax, so that if the member state is not imposing a tax at all on the foreign dividends it is not obliged to make a cash payment to a shareholder who is exempt from tax in respect of the dividend concerned, equal in amount to the foreign tax paid.

30 202. Finally, Mr Baldry relies on the recent judgment of the ECJ in Case C-35/11 Test Claimants in the *FII Group Litigation v HMRC* which was given on 13 November 2012 ("*FII 2*"). This case was brought to our attention following the hearing of this appeal and we invited written submissions from the parties on it. *FII 2* dealt with various questions referred back to the ECJ by the High Court following the 35 determination of the reference in *FII ECJ*.

203. Question 5 of the judgment is concerned with that aspect of the ACT regime which permitted a UK-resident company which had surplus ACT for an accounting period to surrender it only to other UK-resident subsidiaries. At paragraph 106-107 of *FII 2*, the Court expressed the issue as follows:

40 "106. In Test Claimants in the FII Group Litigation, the Court held in reply to the referring court's third question that Article 49 TFEU precludes legislation of a Member State which allows a resident company to surrender to resident subsidiaries [surplus ACT]… but does not allow a resident company to surrender such an amount to non-resident subsidiaries where the latter are taxable in that Member State on the profits 45 which they made there.

107. The claimants in the main proceedings contend that this reply by the Court also applies where the profits of non-resident subsidiaries in respect of which such a surrender of surplus ACT is not possible are not subject to tax in [the UK], but are

subject to tax in other Member States. In their submission, it would be contrary to the objectives pursued by the national legislation at issue to limit the mechanism for surrendering surplus ACT to subsidiaries subject to tax in the United Kingdom The national regime at issue in the main proceedings should have provided for the possibility of matching the ACT paid by the parent company with the foreign corporation tax borne by the subsidiary paying the dividends and should have allowed the surplus ACT to be refunded in order to prevent a series of charges to tax from being imposed upon the companies of the group."

204. The Court concluded as follows:

"110: As regards …. ACT which …. [the UK] was entitled to impose, it is to be recalled that ACT is an advance payment of corporation tax in the United Kingdom. The right to surrender surplus ACT to subsidiaries ensures that a group of companies that are subject to tax in the United Kingdom does not- by reason only of the existence of the ACT – pay tax of an amount exceeding the aggregate liability that has arisen in the United Kingdom. The extension of that right to non-resident companies that are not taxable in the United Kingdom, which would result in the surplus ACT being repaid, would in effect deny the United Kingdom the right to levy additional tax on foreign-sourced dividends paid out of profits which are subject to a nominal rate of tax lower than that applicable in the United Kingdom and would thus jeopardise a balanced allocation of the power to impose taxes between Member States [see paragraph 33 of *Meilicke II*]."

205. Accordingly, there was no incompatibility:

"…. Where the subsidiaries established in other Member States to which ACT could not be surrendered are not subject to tax in [the UK]" (paragraph 111)."

206. Mr Baldry submits that the ECJ's decision in relation to question 5 of *FII 2* supports HMRC's case for the following two reasons:

(1) In paragraphs 110 and 111, the Court expressly states that EU law does not require the UK to repay an amount of UK tax (*ie* surplus ACT) to a non-resident company which is not subject to tax in the UK. It should therefore follow as a matter of logic that EU law does not require the UK to pay a tax credit equal to the foreign tax suffered by a person which is resident, but not subject to tax on its dividend income, in the UK. To so require would jeopardise the balanced allocation of the power to impose taxes between Member States.

(2) The Court's conclusion reinforces HMRC's interpretation of *Meilicke II*. The very paragraph on which they rely in these appeala (paragraph 33 – where the Court said that EU Law "cannot have the effect of requiring Member States to go beyond the cancelling of national tax payable by a shareholder on dividends of foreign origin received and the reimbursing of a sum whose origin is in the tax system of another Member State") is cited by the Court in *FII 2* as authority for the proposition that the UK need not repay surplus ACT to foreign-resident companies which are not subject to tax in the UK. It must therefore follow that the UK is not, where it exempts persons from UK tax on their foreign dividend income, obliged to pay them a tax credit on account of tax suffered overseas.

207. The foundation on which Mr Baldry's submissions are built is the significance of the fact that, in relation to a dividend from a UK resident company, ACT has been

paid whereas this will not be so in the case of a foreign dividend. The significance of ACT having been paid is that the shareholder has a tax credit of a corresponding amount which effectively means that a tax exempt shareholder such as BTPS pays no tax on the dividend. Consequently, Mr Baldry contends there is no different treatment of comparable solutions if no tax credit is been paid in respect of that dividend and that dividend like the UK dividend is not subject to tax in the UK.

208. Mr Baldry referred us to *Pirelli Cable Holding NV v Inland Revenue Commissioners* [2006] 1 WLR 400 where the House of Lords considered the effect of the relationship between ACT and the grant of a tax credit. We have referred to the passages from the speeches of Lord Nicholls, Lord Scott and Lord Walker at paragraph 75 above to support the proposition that liability to pay ACT was a precondition of entitlement to a tax credit.

209. Mr Vajda accepts that as a matter of UK domestic law this is correct. However we do not think that this fact in itself helps Mr Baldry. Although the tax credit may be linked to the ACT and indeed the payment of a dividend by a UK company triggered the requirement to pay ACT, ACT is corporation tax paid by the company paying the dividend. But as we have explained at paragraphs 74 to 77**,** the tax credit is not a credit in respect of tax payable by the shareholders themselves, which is paid on their behalf by the company (in contrast to a withholding tax which does fall into that category) but is, as is implicit from its name, a payment in advance of the corporation tax payable by that company in respect of its profits. As a means of avoiding economic double taxation the amount of that ACT is imputed to the shareholders receiving the dividends concerned and generates a tax credit.

210. In essence therefore the UK's imputation system was no different to the Finnish system as considered in *Manninen*, the only difference being that under the Finnish system the dividend paying company did not have to make a payment of ACT, but there was an equivalent mechanism in that, if the corporation tax the company was due to pay turned out to be less than 29/71sts of the amount of dividends it had distributed, then the difference was charged to the company by way of an additional tax: see paragraph 11 of the judgment.

211. It is to be remembered also that the ECJ also rejected the UK Government's arguments that the difference in treatment between the payment of UK sourced dividends and the payment of non-UK sourced dividends does not amount to discrimination because it was based on a distinction between dividends on which ACT had been paid and on those on which no ACT had been paid: see paragraph 87 of the judgment quoted in paragraph 164 above.

212. It is also clear that the reasoning of the ECJ in *FII ECJ* covers both the position of the dividend paying company and the shareholder receiving that dividend as we have pointed out in our discussion of the FIDs claim. Although in *FII ECJ* the scenario being considered by the Court did not cover the position of an investor making a direct investment in a non-UK resident company, it is clear in our view that the reasoning that it applied in relation to payment of FIDs is equally applicable to direct investment. This logically follows because a FID is no more than a pass through of the net dividend received from the non-resident company in which the FID paying company invests: see paragraph 148 of the judgment. The principle which we say is equally applicable to the *Manninen* claims is set out in paragraph 152 of the judgment in *FII ECJ* as follows:

> "Nevertheless, as was held in paras 87 to 91 of this judgment, since profits distributed by a company are subject to corporation tax in the member state in which the company is resident, where a system of advance payment of corporation tax which applies to the company receiving the dividends determines the amount due by having regard to the tax paid abroad by a non-resident distributing company, such a system treats a company receiving foreign-sourced dividends less favourably than a company receiving nationally-sourced dividends, even though the situation of the former is comparable the latter".

213. We accept Mr Vajda's submission that the reason that the ECJ says in paragraph 152 of its judgment that the situations are comparable is because corporation tax has been paid in both cases. As a result, where a Member State imputes all or part of the corporation tax which a company resident in that state pays to the shareholder in the form of a tax credit when that company pays a dividend, it must equally do so where a shareholder in a company resident in another Member State receives a dividend from that company. This is the basis of the judgment in *Manninen* (see paragraph 54 of the judgment) and is consistent with the principles we set out in paragraph 97 above.

214. We therefore reject Mr Baldry's submission that *Manninen* was decided on the basis that the less favourable treatment of foreign dividends arose purely because (in that case) the Finnish authorities imposed tax on a foreign dividend without giving credit for the foreign tax paid in respect of that dividend; it is quite clear, in our view, that the reasoning of the ECJ went further than that and focused on the way in which credit for the underlying corporation tax was paid because of the imputation system that was operated in Finland.

215. Nor do we accept what we see to be the basis of Mr Baldry's submission that the principle laid down in *Manninen* does not require the UK government to give a tax credit where the shareholder concerned is exempt from tax on dividends, namely that the reasoning in *Manninen* and *FII ECJ* is concerned with the elimination of economic double taxation, and since BTPS pays no tax on the foreign dividend there is no double tax to eliminate.

216. In our view the essence of the judgments in both *Manninen* and *FII* is that if a Member State has a tax system designed to mitigate economic double taxation in respect of domestic dividends, such as an imputation system which gave all shareholders (whether taxable or exempt) relief for the underlying corporation tax paid by the company distributing the dividend through the giving of a tax credit, then it must extend the same system to dividends paid by companies resident in other Member States. It was clearly a matter of choice for the Member State concerned *how* (if at all) it sought to mitigate economic double taxation but if it did so through an imputation system giving credit for underlying corporation tax then it must do the same for foreign dividends.

217. This point is clearly brought out in *FII ECJ* where the Court rejected the argument that there is no economic double taxation to eliminate in the case of foreign dividends because no ACT has been accounted for them in paragraph 159 of its judgment as follows:

> "However, that argument is based on the same false premise that a risk of economic double taxation arises only in the case of dividends paid by a resident company subject to an obligation to account for ACT on dividends distributed by it, whereas the true position is that such a risk also exists in the case of dividends paid by a non-resident company, the profits of which are also subject to corporation tax in the state in which it is resident, at the rates and according to the rules applying there".

218. It is clear that in coming to this conclusion the ECJ had in mind the position of tax exempt shareholders and was not confining its conclusion to the position of fully taxable shareholders. This is apparent from paragraph 148 of the judgment which introduces the discussion on whether the absence of a tax credit for foreign dividends amounts to less favourable treatment, which states

> "148. In the second place, a shareholder receiving a payment of dividends from a resident company which has its origin in foreign-sourced dividends treated as FIDs, is not entitled to a tax credit, but is treated as having received income which has been taxed at the lower rate for the tax year in question. In the absence of a tax credit, such a shareholder has no right to any repayment if he is not liable to income tax or where the income tax due is less than the tax on the dividend at the lower rate."

219. Indeed it is clear from this paragraph that the only shareholders who suffer the disadvantage are those who are exempt from tax, because taxable shareholders are treated as having received income on which the lower rate of tax for the year in question has been paid, which puts such a shareholder in the same position as if he had received a tax credit: see paragraph 15 of the judgment of Henderson J in *FII GLO* as set out in paragraph 11 above.

220. We do not, therefore, accept that the position of a pension fund like BTPS receiving a tax credit in respect of a dividend from a UK resident company was not comparable to that when it received a FID or a foreign dividend from a direct investment. This is clearly the effect of paragraph 168 of the judgment in *FII ECJ* where the Court stated that the "difference in treatment concerns situations which are directly comparable and constitutes a restriction on the free movement of capital for which no justification has been provided".

221. Our analysis of *Orange Smallcap* and the other cases referred to by Mr Baldry (*Meilicke II* and *FII 2*) do not affect our conclusions on this point.

222. In our view, the factual situation in *Orange Smallcap* is not comparable to the factual situation in *Manninen* or that faced by BTPS in this case. The *Manninen* situation involves less favourable treatment of underlying corporation tax paid by a foreign dividend paying company than that which occurs where a domestic dividend is paid. The reason that difference arose was because of the mechanism that the Finnish government put in place to address the issue of economic double taxation. Having put such a mechanism in place for domestic dividends it could not fail to provide comparable treatment for foreign dividends. In *Orange Smallcap* there was less favourable treatment for dividends paid from German or Portuguese companies because there were no provisions in any relevant tax conventions between those countries and the Netherlands which made provision for any withholding tax paid in those countries to be set off against any tax due in the Netherlands. This unfavourable treatment did not arise, however, because of any mechanism for the elimination of double taxation put in place in the Netherlands but because of the exercise of the taxing powers of the German and Portuguese states which made provision for a withholding tax when dividends were paid. It reflected the right of fiscal autonomy enjoyed by Member States.

223. The Netherlands legislation relating to investment companies such as Orange Smallcap treated domestic dividends and foreign dividends in exactly the same way – they were both liable to be taxed at 0%. The withholding tax levied in the Netherlands on payment of dividends by Netherlands resident companies is on

account of the tax payable by the shareholder in respect of the dividend he has been paid by the paying company and is not, unlike ACT, an imputation of any of the corporation tax paid by the dividend paying company. On that basis, the refund of that withholding tax to a non-taxpayer such as Orange Smallcap does not amount to more favourable treatment because it is simply ensuring that the fund pays no Netherlands tax on the dividend, as it does not on any foreign dividends.

224. This analysis is supported by the reasoning of the Advocate General *in Orange Smallcap,* in particular paragraph 89 to 92 of his opinion as follows:

> "89. In the light of this analysis the fact that dividends originating in Germany and Portugal are subject to a heavier tax burden than dividends originating in the Netherlands follows, not from a difference in treatment attributable to the tax scheme applicable in the Netherlands, but from the decision of the German and Portuguese Governments to tax OESF on the dividends paid to that enterprise by companies established in their respective territories.
>
> 90. The situation in this case is therefore different, in our view, from that at issue in *Manninen*, which was referred to both by the Hoge Raad and by OESF and the Commission. In *Manninen*, the Finnish rules granted to persons primarily taxable in Finland a tax credit in respect of dividends paid by companies established in that Member State. The tax credit was intended to prevent the economic double taxation of those dividends. It involved setting off the tax payable in the form of corporation tax by the company distributing the dividends against that payable by the shareholder in the form of income tax.
>
> 91. The tax credits differs in two ways from the refund system at issue in the present case.
>
> 92. First, as has been seen, the purpose of the refund is not to take account of the corporation tax payable by companies established in the Netherlands but to exempt a fiscal investment enterprise from tax on dividends. Second, the legislation at issue in *Manninen* provided for different treatment in comparable situations in that the tax credit was reserved for dividends paid by national companies, while a Finnish shareholder was also taxed in Finland on dividends originating in other Member States and there was no provision in Finnish law to take account of the corporation tax paid by companies making distributions abroad."

225. This reasoning is reflected in the conclusions of the Court on this issue where it states in paragraph 41 and 42 of its judgment:

> "41. However, the status of Member State of residence of the company in receipt of dividends cannot include the obligation for that Member State to offset a fiscal disadvantage arising where a series of charges to tax is imposed entirely by the Member State in which the company distributing those dividends is established, since the dividends received are neither taxed nor treated differently by the first Member State as regards investment enterprises established in that State.
>
> 42. It follows that, in a situation where the greater tax burden imposed on dividends distributed by companies established in Germany or Portugal to a fiscal investment enterprise established in the Netherlands than that which is imposed on dividends distributed to that same enterprise by companies also established in the Netherlands does not arise as a result of a difference in treatment attributable to the tax regime in the Netherlands, but stems from the decision of the Federal Republic of Germany and the Portuguese Republic to make a deduction at source from those dividends, and from the decision of the Kingdom of the Netherlands not to tax those dividends, the fact that

the latter Member State was not granted a concession in respect of the deduction at source for which the first two States have opted does not constitute a restriction on the free movement of capital."

226. We therefore reject Mr Baldry's submission that the basis of the decision in *Orange Smallcap* was that the reason the fund could not receive a repayment of the foreign withholding tax was because of its tax exempt status and that this equates with the position of BTPS which cannot similarly expect payment of a cash sum for a tax credit in respect of foreign income on which it pays no tax in the UK. As we have demonstrated above, the two cases deal with different situations.

227. With respect to *Meilicke II* we see the ratio of that case, as set out in paragraph 33 of the judgment quoted in paragraph 200 above, as being that when applying the principles in *Manninen* there is no need to give credit beyond the amount of tax levied in the shareholder's home state on the foreign dividend. *Orange Smallcap* is quoted simply to support that proposition, and as the Advocate General stated in *Orange Smallcap* the situation in *Orange Smallcap* is factually different to that in *Manninen.*

228. With regard to *FII 2*, Mr Baldry relies on the Court's endorsement of paragraph 33 of *Meilicke II* but as we have stated above we regard this as merely dealing with the principle that credit need not be given beyond the tax levied in the shareholder's home state on the foreign dividend, and consistent with that principle as determined in *FII 2*. In our view the comparison Mr Baldry seeks to make between the finding of the Court that the UK government was not required to repay surplus ACT to a non-resident company which is not subject to tax in the UK and his submission that the UK should not be required to give to a UK resident a tax credit for a foreign dividend to which he is not subject to tax in the UK is a false analogy; the issue at the heart of this case as we have discussed at length above is the difference in treatment in terms of tax credits given for domestic dividends and their absence for foreign dividends.

229. We therefore conclude on the *Manninen* claims as follows:

(1) The absence of a tax credit for entities such as BTPS which are not liable to tax on their investment income in respect of foreign sourced dividends when such a tax credit is available for UK sourced dividends is liable to discourage BTPS from exercising its rights under Article 56 and is therefore a breach of the right to free movement of capital afforded by that provision;

(2) The absence of a tax credit for foreign sourced dividends as described above is also a breach of Article 56 because as a consequence the securities of companies in which investment might be made on a cross border basis are less attractive to investors such as BTPS;

(3) An investor such as BTPS receiving foreign sourced dividends is in a comparable situation to such an investor receiving UK sourced dividends even though only the latter receives dividends on which ACT has been paid because the company paying the foreign sourced dividend will have been liable to corporation tax in its home state on the profits out of which the dividend is paid;

(4) Consequently if a Member State has a tax system designed to mitigate economic double taxation in the case of dividends paid by a company resident in the Member State concerned, as was the case with the UK's imputation

system, then the Member State should extend the same system to dividends paid by companies in other Member States. The UK system went beyond relieving economic double taxation and gave investors such as BTPS partial relief for the underlying corporation tax even though the pension funds themselves were tax exempt; and

(5) The fact that BTPS was exempt from tax on the foreign sourced dividends and therefore paid no tax on them is irrelevant as is the fact that the granting of credit in respect of such dividends results in a loss of tax revenue to the UK because it represents a credit in respect of tax that has been paid in another Member State. That is the inevitable consequence of the imputation system that has been put in place.

Remedies

230. We therefore turn to the appropriate remedy for the breach of Article 56. On this there is no dispute between the parties. The answer is to be found in paragraph 46 of *Manninen* which states as follows:

> "Having regard to the objective pursued by the Finnish tax legislation, the cohesion of that tax system is assured as long as the correlation between the tax advantage granted in favour of the shareholder and the tax due by way of corporation tax is maintained. Therefore, in a case such as that at issue in the main proceedings, the granting to a shareholder who is fully taxable in Finland and who holds shares in a company established in Sweden of a tax credit calculated by reference to the corporation tax owed by that company in Sweden would not threaten the cohesion of the Finnish tax system and would constitute a measure less restrictive of the free movement of capital than that laid down by the Finnish tax legislation".

231. *Meilicke II* establishes the principle that credit need not be given beyond the amount of credit given in the Member State of the investor receiving the foreign dividends. So in the *Manninen* case itself, where the Finnish legislation gave a tax credit equivalent to 29/71sts of the dividend paid, and the Swedish dividend had already suffered a withholding tax of 15% when received by the investor, the application of the principle would result in the Finnish government being obliged to grant a credit of 14% of the dividend, so that in total the investor received a total credit of 29/71sts of the dividend. Were the Swedish corporation tax rate less than 29% then the credit to be paid in Finland would be consequently reduced but were it more than 29% there would be no obligation to give a credit in excess of that. The same principles should therefore apply in relation to BTPS's *Manninen* claims: it should receive an appropriate credit limited to the amount of the underlying corporation tax paid: see paragraph 54 of *Manninen.*

232. We arrive at this result by giving Section 231 of ICTA a conforming construction, that is it must be construed so that BTPS is entitled to the tax credits which it is entitled to under Community law. As a result of this, in relation to example (b) given in paragraph 15 above in respect of the *Manninen* claims, BTPS would claim a tax credit of £16.75 on the foreign sourced dividends thus giving it £83.75 in total receipts, the same as is derived from its investment in a UK resident company as shown in example (a).

Fiscal Supervision

233. Finally in relation to the *Manninen* claims, we turn to the question as to whether the breach of Article 56 would be justified on the grounds of "effective fiscal

supervision". As we observed in paragraph 176 above in relation to the FIDs claims, this principle is engaged where as part of the exercise to ensure the domestic legislation does not treat foreign sourced dividends less favourably than UK sourced dividends it is necessary to give credit for underlying foreign tax paid in respect of those foreign sourced dividends. As we also observed in paragraph 176 above at that point Article 58(1)(b) of the Treaty, as set out in paragraph 24 above may be applicable.

234. Our understanding is that HMRC have only raised the question of justification in respect of dividends sourced from non-member states ("third countries") and in that context we do not include dividends from companies resident in a state within the EEA for periods after 1 January 1994 when the EEA Agreement was in force, as found by the Tribunal and referred to in paragraph 31(7)(c) above, there being no dispute on this point.

235. BTPS's primary submission on this issue is that, since Section 231 of ICTA provided a complete bar on tax credits for dividends received from non-UK companies, that is without making provision for claims to be made where the underlying tax paid abroad can be verified, there is no scope for HMRC to advance "effective fiscal supervision" as its justification for the restriction of free movement of capital in this case. BTPS relies on the judgment of the ECJ in case C- 436/08 *Haribo Lakritzen Hans Riegel BetriebsgmbH and another v Finanzamt Linz* [2011] ECR 1-0000 ("*Haribo*") to support this proposition, as well as a passage in *FII ECJ*.

236. Mr Baldry rejects BTPS's primary submission and contends that BTPS is not entitled to rely on Article 56 in relation to dividends from third countries in respect of which the UK had no entitlement to obtain information relevant for ascertaining the amount of tax paid on the relevant foreign profits. This is because the UK is justified in not providing a tax credit to BTPS where it has no means of verifying the foreign tax actually paid which forms the basis of the credit being paid. We do not need to consider this submission if we adopt BTPS's primary submission so we will deal with the latter first.

237. On the question as to when it is legitimate to refuse to give effect to the freedom to move capital on the grounds of justification we were referred to Case C 101-05 *Skatteverket v A* [2007] ECR1 -11531 ("***A***") . The facts of that case, so far as relevant, were that Swedish tax legislation excluded from income tax dividends distributed by a Swedish company in the form of shares in a subsidiary, subject to various conditions. This law was subsequently extended to distributions of such shares by foreign companies established in the EEA or in a state with which Sweden had conducted a tax convention that contained a provision on exchange of information.

238. The ECJ held that although the restriction of the right to companies established in countries with whom Sweden had a tax convention of the type described was a restriction of movement of capital, that restriction was justified. The Court referred to the fact that a restriction would not be justified in relation to companies established in EEA states because of the extensive provisions in Community Law allowing tax authorities in the various Member States to co-operate and then stated, at paragraph 63 of the judgment:

> "It follows that, where the legislation of a Member State makes the grant of a tax advantage dependent on satisfying requirements, compliance with which can be verified

only by obtaining information from the competent authorities of a third country, it is, in principle, legitimate for that Member State to refuse to grant that advantage if, in particular, because that third country is not under any contractual obligation to provide information, it proves impossible to obtain such information from that country."

5 239. The justification argument was relied on by the UK Government in *FII ECJ* in respect of what it perceived to be the difficulties in extending tax credits in respect of FIDs where the underlying foreign dividends were sourced from third countries. The ECJ refers (in paragraph 171 of the judgment) to the fact that it may be that a Member State will be able to rely on justification in relation to a third country in circumstances 10 where the reason to do so would not constitute a valid justification for restriction of capital movements between member states and then concludes in paragraph 172 as follows:

"Nevertheless, the United Kingdom government has, as regards the national legislation at issue, relied on the difficulties arising from the verification of the tax paid abroad 15 only in order to explain the period of time between the time when ACT is accounted for and the time when it is repaid. As was held at para 156 of this judgment, that is not a reason justifying legislation which refuses completely to allow a resident company receiving a payment of foreign-sourced dividends to offset the tax charged on profits distributed abroad against the amount due in respect of advance corporation tax, 20 whereas, for nationally-sourced dividends, that amount is automatically deducted from the tax paid, albeit only in advance, by a resident company making a distribution"

240. Mr McDonnell submits that what the ECJ was saying in paragraph 172 of *FII ECJ* was that a provision in national law which had a blanket prohibition on receiving equivalent treatment in respect of foreign sourced dividends to that applying in 25 respect of domestic dividends is not justified and what was required was language in the national law similar to that to which he found in the Swedish law and referred to in *A*. In the absence of such language, Mr McDonnell submits there is no process by which Community law can mould the national legislation so that it is restricted to circumstances which are justified.

30 241. In *Haribo* the ECJ was considering a provision of the Austrian tax legislation which restricted the availability of an exception from corporation tax to companies established outside the EEA. At paragraph 129 to 131 of its judgment the Court set out the Austrian Government's "effective fiscal supervision" argument and the principle decided in *A* namely that in third country cases, because of the absence of 35 the EEA framework for mutual assistance, where as a matter of the national legislation the grant of a tax advantage depended on conditions, and the verification of compliance with those conditions needed the co-operation of the foreign authorities, then restrictions could be justified.

242. In paragraphs 132 and 133, the Court then set out its conclusions:

40 "132. However, the national legislation at issue in the main proceedings does not provide that any exemption of portfolio dividends received from a company established in a non-member State other than a State party to the EEA Agreement, or any credit for the tax paid in such a non-member State. Under Paragraph 10 of the KStG, portfolio dividends from non-member States other than States party to the EEA Agreement are 45 always subject to corporation tax in Austria and the national legislation at issue does not provide for any tax advantage for such dividends in order to prevent their economic double taxation.

> 133. In those circumstances, the difference which exists, as regards cooperation between tax authorities, between the situation obtaining, on the one hand, between Member States within the European Union and, on the other hand, between Member States and non-member States cannot justify a different tax treatment of nationally-sourced portfolio dividends and portfolio dividends from non-member States other than States party to the EEA Agreement."

243. Mr McDonnell submits that the reasoning in *Haribo* is equally applicable to BTPS's *Manninen* claims. Here, as in paragraph 132 there, the national legislation does not provide that the "credit for tax paid in a non-member State is conditional upon the existence of an agreement for mutual assistance". Section 231(1) ICTA 1988 provided that only dividends from UK resident companies qualify for the tax credit, it did not provide for any tax credit for portfolio dividends received from other countries, whether they be Member States or third countries.

244. We reject BTPS's principal submission. In our view the passages quoted in the *FII ECJ* and *Haribo* do not go so far as to preclude the question being dealt with during the exercise of conforming section 231 so that it is compliant with Community Law. In *A*, the ECJ decided that a provision in national legislation which made the grant of a tax advantage conditional upon compliance with verification requirements and refused the grant where it proved impossible to obtain the information under the laws of the relevant tax convention was consistent with Community Law. This principle was followed in Case C – 201/06 *Test Claimants in the CFC and Prudential GLO v HMRC* [2008] ECR I – 2875, *("CFC")* which Mr Baldry cited to us, at paragraphs 95 and 96 of that judgment.

245. It appears to us that *Haribo* and *FII ECJ* go no further than to say that in these particular cases the claim for justification failed because there was nothing in the national legislation that confined the refusal to grant the relevant claim to circumstances where it could not be verified. It is not for the ECJ in that situation to rewrite the Member State's legislation for it so as to ensure that the refusal was confined to circumstances in which it could be justified.

246. Our finding in relation to the *Manninen* claims is that section 231 ICTA must be given a conforming construction, that is it must be read and construed so that BTPS is entitled to the tax credits which they are entitled to under Community law. We set out in paragraph 232 above how that could, on the basis of the decision in *Manninen*, be achieved in practice. As part of that conforming construction we can also find that, consistent with the principles laid down in *A* and *CFC,* that such entitlement will extend to claims in respect of dividends sourced from a third country where the claims can be verified by obtaining information from the competent authorities of third countries under rights conferred under the relevant double taxation convention.

247. In the light of that finding we need to consider the extent to which the terms of the double tax conventions concerned will govern the extent to which they may be relied on to meet the requirements of the principle laid down in *A*.

248. The parties agree that for this purpose double tax conventions can be divided into three categories:

(1) those which provide for exchange of information for any purpose of the tax legislation of the contracting states;

(2) those which provide for exchange of information only for the purposes of preventing fraud or tax avoidance; and

(3) those with no information exchange provisions at all.

249. Clearly those conventions falling within category (1) will meet the requirements and those in category (3) will not.

250. In relation to those conventions which fall into category (2) there are two issues to determine as follows:

(1) where a treaty provides for exchange of information only for the purposes of preventing fraud or tax avoidance, does that mean there is "no right" to obtain information; and

(2) where different treaties have been in force at different times, is it appropriate to consider (a) the treaty in force at the time the dividends were paid; (b) the treaty in force at the time the claims were made; and (c) the treaty in force at the time of the decision by HMRC which is under appeal.

251. With regard to the first issue, Mr McDonnell submits that a power to require exchange of information for the purposes of preventing fraud or tax avoidance means that there is a right to obtain information. HMRC, if they wish to verify any of the taxpayer's claims for tax credits, would have the right to obtain information from the competent authorities in the third country in order to confirm that they are not fraudulent. The fact that HMRC might then use the information so obtained also for other verification checks – *eg* that the claims are not made negligently – is neither here nor there: HMRC have a right to obtain the information required for verification.

252. We cannot accept that submission. Unless HMRC have reasonable grounds for suspecting that the claim is fraudulent it would not be appropriate for them to seek to use the convention, narrowly cast as it is, in order to obtain information for an entirely different purpose. The authorities of the contracting state at the receiving end of the request for information will be concerned not to provide information that goes beyond the scope of the relevant convention and whilst it is to be expected they will give mutual assistance consistent with the terms of the treaty, they are under no obligation to go any further than that. On that basis unless the convention falls within the first of the three categories identified in paragraph 263 above it cannot be said that there is a right to obtain information. Consequently, unless the convention concerned falls within that category HMRC will be justified in rejecting the claim concerned.

253. With regard to the second issue, it appears to us that the relevant treaty will be that in force at the time HMRC comes to consider BTPS's claims, since it is at that point HMRC will need to consider the extent to which it is justified in requiring the claim to be verified and if it is, whether it can at that time request from the authorities in the relevant third country the information it needs to verify the claim under the double tax convention in force at the time.

XI Limitation

254. We can now turn to the question of limitation.

General

255. For a purely domestic claim relating to the taxation of a FID or a foreign dividend in the context of a statutory appeal, the procedure for making a claim is set

out section 42 Taxes Management Act 1970 ("**section 42**") and the time limit for making the claim is laid down by section 43 of that Act, ("**section 43**"). For the years relevant to the present appeals up to an including 1995-96, section 43 was in the following terms:

"43. Time limit for making claims

> (1) Subject to any provision of the Taxes Acts prescribing a longer or shorter period, no claim for relief under the Taxes Acts shall be allowed unless it is made within six years from the end of the chargeable period to which it relates…."

For the self-assessment years 1996-97 and 1997-98, the period of 6 years was replaced, in relation to income tax, with the period of 5 years from the 31st January next following the year of assessment to which it relates.

256. The Tribunal decided that the time-limit under section 43 applied to the FIDs claims and the *Manninen* claims and did not need to be reset in order to be compliant with Community law. It decided that the claim made by BTPS in the High Court for 1996-97 (which would have been in time had it been a claim under section 43) could not be treated as a statutory claim for tax credits. On that footing, all of BTPS's claims were time-barred save for the FIDs claim in respect of the year 1997-98 which it is accepted by HMRC was brought within time. Mr Baldry submits that the Tribunal was right to reach the conclusion which it did for the reasons which it gave. He says that it is now well established law that reasonable limitation periods for bringing proceedings such as those contained within section 43 TMA are entirely compatible with Community law (see for example Case C-188/95 *Fantask A/S and Others v Industriministeriet (Erhvervsministeriet)* [1997] ECR I-6783 at paragraph 48; *Biggs v Somerset County Council* [1996] 2 All ER 734 ("Biggs") and *HMRC v Marks and Spencer PLC* [2011] EWCA Civ 1156). We agree with that last proposition; there can, we think be no doubt about that general principle in the light of those authorities. Thus in *Fantask* at paragraph 48, the ECJ said this:

> "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 time limitation period for bring 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" reference being made to Case 33/76 *Rewe v Landwirtschaftskammer Saarland* [1976] ECR 1989 paragraph 5 and Case C-45/76 *Comet v Produktschap voor Siergewassen* [1976] ECR 2043, paragraphs 17 and 18.

257. *Fantask* is relevant, too, in relation to what it has to say about the decision in Case C-208/90 *Emmott v Minister for Social Welfare and the A-G* [1991] ECR I-4269 which is referred to by Mr Vajda. In *Emmott*, the applicants and the Commission considered that a Member State may not rely on a limitation period under national law as long as the Directive, in breach of which charges had been wrongly levied, had not been properly transposed unto national law so that the limitation period under national law did not begin to run until the Directive had been properly transposed. But the Danish, French and UL Governments considered that a Member State was entitled to rely on domestic time-limits which, as they asserted in *Fantask* itself, complied with the two conditions of equivalence and effectiveness laid down in the case law (in

particular Case 199/82 *Amministrazione delle Finanze dello Stato v San Giorgio* [1983] ECR 3595 and Case C-312/93 *Peterbroeck v Belgian State*. [1995] ECR I-4599. In their view, *Emmott* was to be confined to the quite particular circumstances of that case as the ECJ had confirmed in subsequent case-law. The Court effectively accepted that approach (so that, as we see it, *Emmott* has been distinguished virtually out of existence) saying at paragraph 51:

> "…it is clear from [Case C-338/91*Steenhorst-Neerings*] 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…….".

258. In order to address the issue of the time limits (if any) applicable to BTPS's claim, it is to be remembered that the way in which BTPS is able to assert, in this Tribunal at least, its rights under Community law (that is to say, the FIDs claims and the *Manninen* claims) is through an appropriate disapplication and/or moulding of domestic legislation in the manner which we have already discussed.

259. In *Rewe* (see above), the taxpayer had paid certain charges for inspection of its imports (French apples imported to Germany) which were regarded as equivalent to customs duties which meant that the charges had been illegally imposed. The taxpayer therefore had a Community law right to claim repayment of the illegally levied charges. But the exercise of that right was barred by a domestic time limit. The ECJ held that a domestic limitation period could be a defence to the exercise of a Community right so long as the domestic rules satisfied the principles of equivalence and effectiveness: it was

> "for the domestic legal system of each Member State to designate the Court having jurisdiction and to determine the procedural actions at law intended to ensure the protection of the rights which citizens have from the direct effect of community law, it being understood that such conditions cannot be less favourable than those relating to similar actions of a domestic nature."

260. As the Upper Tribunal (Warren J and Judge Hellier) in *HMRC v GMAC UK plc* [2012] UKUT (TCC) 279 noted at paragraph 161, the judgement of the ECJ does not (and nor does the opinion of the Advocate General) go so far as to say that where domestic legislation offers a system for enforcing a right parallel to a community right, then that system must be adopted for the right under Community law but it recognises that a domestic system can apply to such a right. In that case, it needs to be considered whether section 42 provides a mechanism for making a claim and, if so, whether section 43 provides the relevant time-limit.

261. We do not understand BTPS to suggest that its claim is not properly to be made under the provisions of section 42. But it does contend that section 43 is not applicable, with a fall-back in relation to the FIDs claim for 1996-97 that the claim commenced in the High Court is a "claim" within the meaning of section 42 and, as such, was brought in time. In summary, BTPS puts forward the following five grounds of appeal.

(1) Ground 1: section 43 is inapplicable as a matter of construction for all years. This is purely a question of UK domestic law.

(2) Ground 2: section 43 is to be disapplied by reason of the principles of legal certainty, equivalence and effectiveness for all years.

(3) Ground 3: section 43 is to be disapplied by reason of the principles of legal certainty, equivalence and effectiveness in the case of claims where the same claims have been made in time in the High Court for all years.

(4) Ground 4: section 43 is to be disapplied by reason of the principle of equivalence for all years.

(5) Ground 5: the 1996-97 FIDs claim in the High Court was or is to be treated as a "claim" within the meaning of section 42 and as such was a claim made within the time-limit laid down by section 43.

UK law: Ground 1

Section 43 is inapplicable as a matter of construction for all years.

262. The Tribunal did not deal with the point. Mr Baldry says, in his skeleton argument, that the point was not raised before the Tribunal. BTPS's position is that the point was raised in a written submission dated 26 November 2010. It does not matter which is correct since HMRC do not submit that we should not deal with the point. We propose to do so.

263. BTPS's argument is straightforward. We set it out in the following paragraphs 264 to 277 which are taken principally from Mr Vajda's and Mr McDonnell's skeleton argument.

264. The time limit in section 43 on its terms applies only to claims "for relief" and not to other types of claims: see section 43(1).

265. The present claims are not claims for relief, they are claims of a different type. Indeed, in his oral submissions, Mr McDonnell said that what BTPS asserts in these appeals are not "claims" at all, let alone "claims for relief".

266. His first point in logical order is that the ordinary operation of the ACT regime does not give rise to a claim at all. Instead, on payment of a qualifying distribution, the paying company comes under a liability to pay ACT. The recipient actually receives a payment of cash plus a tax credit, the total of which represents his taxable income. He does not need to make any sort of claim to offset the tax credit against his tax liability. It is automatic so that this offsetting does not amount to a claim, let alone a claim for relief.

267. Section 42(1) relates to both claims "for relief to be given" and claims for "any other thing to be done". For the Self-Assessment years, section 42(1A) relates to "a claim for a relief, an allowance or a repayment of tax". BTPS accordingly submits that the legislation recognises that not all claims are claims "for relief".

268. Section 43(1) is expressly applicable only to claims "for relief". Those words are plainly intended to have some meaning, that is to say to restrict the operation of the time limit in section 43(1) to claims for relief, as opposed to other types of claim. Any other interpretation would give no meaning to the words "for relief" there.

269. BTPS'claims are, in the language of section 42(1), claims for "another thing to be done", namely for payable tax credits to be paid. They are not claims for relief. They cannot be claims for relief, because BTPS was not, in respect of its investment income, subject to any tax from which relief could be given.

270. The concept of a claim for "relief" is one that is well-established in UK revenue law. The consistent approach of the courts, albeit there is no case specifically construing section 43, is that a "relief" is something which reduces the tax which would otherwise be payable by a taxpayer (possibly to nil). Examples include loss relief, group relief, and relief under a double taxation convention for tax paid overseas.

271. Mr McDonnell has referred us to a number of authorities. We start with *Taylor v MEPC Holdings Ltd* [2003] UKHL 270, [2004] 1 WLR 82, a case concerning group relief, where, at paragraph 10, Lord Hoffmann said:

> "The word "relief" is not a term of art but has been used in tax legislation since the earliest statutes to refer to a provision which reduces the tax which would otherwise be payable."

272. At paragraph 14 of his speech, Lord Hoffmann explains that no-one would regard the deduction of an expense in the computation of trading profits as a "relief" saying that it "is not a deduction from what would otherwise be taxable under [Schedule D], but part of the computation of the taxable amount." And so, in the present appeals, BTPS says, as we understand the argument, that the tax credit is not a deduction from what would otherwise be taxable, firstly because, being exempt, the amounts in respect of which it claims a tax credit are exempt from income tax and secondly because, as we would put it, even in the case of a fully taxable person, the tax credit is not a relief from income which would otherwise be taxable, but a reflection of the tax which actually is payable.

273. A similar approach was taken by the Court of Appeal in *HMRC v UBS AG* [2007] EWCA Civ 119, [2007] STC 588 in the context of an overseas parent company's claim for a payable tax credit representing the ACT paid by its UK subsidiary. UBS, a Swiss company, sought the ability to make a claim under section 243 ICTA 1988. That claim, not normally available to a non-UK parent company, would have given rise to an entitlement to a tax credit under section 231 ICTA 1988 if the claim was accepted, see paragraph 32 of the judgment of the Court of Appeal. (We say normally, because this is subject to the decision in Joined Cases C-397/98 and C-410/98 *Metallgesellschaft* [2001] ECR I-1727, in the case of an EU resident parent company: but UBS AG was not EU resident.) UBS sought the ability to make that claim, relying on the Double Taxation Agreement between Switzerland and the UK. As a matter of domestic law, its rights depended on section 788 ICTA 1988. One of the issues before the Court of Appeal was whether that claim (if it could be made) would be a claim "for relief … from corporation tax" within the meaning of section 788(3)(a) ICTA 1988. Moses LJ held that it would not, citing *Taylor v MEPC Holdings* and reasoning, at paragraph [48]:

> "In seeking to secure equal treatment under art 23(2) [of the UK/Switzerland Double Tax Treaty], UBS is not seeking relief from anything; it has no liability. It seeks payment of a tax credit, in an amount calculated by reference to the distributions it has received. It is not seeking relief because there is no liability to an amount of tax which would otherwise be payable."

274. In the present case, BTPS likewise seeks payment of tax credits, in amounts calculated by reference to the distributions it has received, but its claim is not a claim for "relief" because there is no liability to an amount of tax which would otherwise be payable.

275. The meanings of the words "relief" and "repayment" were also briefly considered by the Court of Appeal in *IRC v Trustees of the Sema Group Pension Scheme* [2002] EWCA Civ 1857; [2003] STC 95. The case concerned section 231(3) payable tax credits for a pension fund – so precisely the same type of claim as in the present case. A company had bought back some of its own shares and in accordance with the normal rule, the purchase price was deemed to be a distribution for UK tax purposes and so the pension fund shareholders had the right to payable tax credits under section 231. On the facts of that case, HMRC claimed that the amount distributed was "abnormal" and therefore sought to invoke the anti-avoidance rule in section 703 ICTA 1988 to counteract the claimed tax advantage. "Tax advantage" was defined in section 709 ICTA 1988 as meaning "a relief from, or repayment of, tax". The Court of Appeal allowed the pension fund's appeal on the basis that the amount distributed was not "abnormal". Consequently, the Court of Appeal's views on the meaning of "tax advantage" in section 709 ICTA 1988 were *obiter* and were set out only briefly, as the Court itself noted in paragraph [106]. At paragraph [111], Jonathan Parker LJ reached the conclusion that the receipt of payable tax credits by the pension fund was a "tax advantage". At paragraph [109], he explained his reasoning as follows:

> "In my judgment, "relief" in section 709(1) is intended to cover situations where the taxpayer's liability is reduced, leaving a smaller sum to be paid, and 'repayment' is intended to cover situations in which a payment is due from the Revenue."

Accordingly, all that Jonathan Parker LJ was saying was that "repayment" covers a situation where a payment is due from HMRC. It follows that in terms of section 709(1) the situation is one of payment and not of relief.

276. Mr McDonnell says that the same approach is to be taken to section 231(3). He submits that although that decision of the House of Lords and both of those decisions of the Court of Appeal related to the meaning of "relief" in statutory provisions other than section 43 TMA 1970, the same reasoning must apply in relation to section 43, in particular noting Lord Hoffmann's comment on the way in which the word "relief" has been used in tax legislation since the earliest statutes. Given that the Taxes Acts are to be construed as one – s.119(3) TMA 1970 provides "This Act, so far as it relates to income tax or corporation tax, shall be construed as one with the principal Act" and "the principal Act" means ICTA 1988 – it would be extraordinary if the expression "relief" in section 709 ICTA 1988 and in section 788 ICTA 1988 meant something different from the meaning of that word in the very sections in the TMA 1970 which provided the mechanism for such claims to relief to be made. By means of section 709(2A) ICTA 1988, the legislation had later been amended so that the definition of "tax advantage" expressly included the receipt of payable tax credits, but the questions arising in the *Sema Group Pension Fund* case related to events pre-dating that amendment.

277. For the rule of construction that the same word bears the same meaning in different parts of an Act of Parliament, see *R v Islam* [2009] UKHL 30, [2009] 1 AC 1076 per Lord Walker at paragraph 23. On the above reasoning, these claims are not claims for "relief". Possibly, on the approach of the Court of Appeal in *Sema Group Pension Scheme*, they are claims for "repayments", more generally in the language of section 42(1) they are claims for some "other thing" to be done namely the payment of payable tax credits. But on any view, since they are not claims for "relief", they fall outside the ambit of section 43(1).

278. Those, then, are BTPS's arguments. Mr Baldry submits that the arguments are hopeless. The framework of his argument is as follows.

(1) First of all, a claim in respect of a tax credit falls naturally within the concept of a "relief" and within the words of section 43(1).

(2) Secondly, section 43 must be read with section 42. Any claim within section 42 is subject to the time-limit provided by section 43. This is true of section 42 as it stood prior to the introduction of self-assessment even ignoring section 43(5A): but it can be said that that subsection lends support to HMRC's approach referring as it does to a "claim by a company for payment of a tax credit". It can also said to be supported by section 42(1A) inserted by Finance Act 1995 referring as it does to "a claim for relief, an allowance or a repayment of tax".

(3) Thirdly, BTPS's construction would have a result which Parliament cannot have intended. Consider a case where the credit was claimed by a taxpayer with an income tax liability of an amount less than that value of the credit claimed. There would be no time limit (whether under the 1970 Act or elsewhere in the statutory code) for the bringing of a claim for the excess credit under section 231(3) ICTA 1988.

279. Developing those points, Mr Baldry draws attention to the words "with respect to" in section 43(1). Cases such as *UBS* are, he says, different, needing to focus on "relief from" rather than "relief in respect of". The wording of section 43(1) thus cuts across the need for a particular liability which is being relieved from. The distinction is drawn by the Special Commissioners at paragraphs 36 to 39 of their decision.

280. There is no doubt, he says, that section 231 is in respect of income tax, a proposition with which it would be difficult to disagree. BTPS is claiming a tax credit in respect of its income, another proposition with which it would be difficult to disagree. The question therefore is "whether it is claiming a relief within the fair and normal meaning of that word and in the light of the judicial authorities". Subject to Mr McDonnell's point that there is not a claim at all, Mr Baldry has identified the correct question in our view.

281. As to that, section 231(3) provides for a claim to be made: a person may have the tax credit set against tax on his total income and where the credit exceeds the income tax, he can claim payment of the excess. He submits that the claim operates as a relief from tax in substance. As a matter of form, a taxpayer has to go through the process of setting the credit against liability and then claiming the excess. The claim is, he says, operating in substance as a relief because, in a case such as the present appeals, it is enabling an exempt pension fund to obtain a payment in respect of a tax credit which has been included as part of its statutory income which payment falls within the ordinary meaning of relief.

282. Mr Baldry does not accept Mr McDonnell's analysis of the operation of the ACT regime. He submits that in all cases a claim has to be made under section 231(3) before a taxpayer is entitled either to offset the tax credit against tax in respect of his income under section 3 or his total income or claim payment of any excess. He says that, whatever may be the position in relation to fully taxable persons as a matter of practice, the formal position in relation to such a person, and both the practical and formal position in relation to an exempt taxpayer such as BTPS, it is an absolute requirement to put in a formal claim. This is what section 231(3) requires; it is true

that section 231(1) gives rise to an entitlement to a tax credit but it says nothing about how the benefit of that tax credit is to be obtained, a matter dealt with in section 231(3). He points out that an exempt taxpayer such as BTPS is not exempted from income tax on all of its income: for instance, trading profits remain taxable. Accordingly, such an taxpayer would be entitled to set off the tax credit against income tax in respect of its trading profits with the excess being subject to a payment claim. There is a composite claim, in essence, in respect of a single item (the tax credit) which can fairly be described as a relief. It falls within the words of Lord Hoffmann in *MEPC Holdings* as something which reduces the tax which would otherwise be payable.

283. It is convenient to note, in this context, that Mr McDonnell accepted in oral argument that the only juridical basis on which BTPS could obtain actual payment of any sum was under section 231(3), at least in a statutory appeal. What, if any, other rights he could assert in the High Court is not a matter for us.

284. Returning to *MEPC Holdings*, Mr Baldry draws attention to Lord Hoffmann's observations that "relief" is not a term of art and to the examples which Lord Hoffmann gave of "reliefs". The first example was that it (the relief) "may be simply a deduction from the overall tax which would otherwise be payable". It is not stretching the meaning of the word "relief" to include within its concept an exemption from tax. Thus, in the situation just considered of an exempt taxpayer having non-exempt income (*eg* the trading income of an exempt pension fund), it is appropriate, he would say, to describe the exemption given in relation to investment income as a "relief" from income tax.

285. He also draws attention to Lord Hoffmann's observation that, in applying the relevant treatment to what would otherwise be taxable profits, that treatment may create a loss which can form the subject of group relief. Accordingly, the relief can produce a negative figure such as a loss and, he adds, it can produce a figure such as section 231 produces.

286. Mr Baldry finds support for his approach in the decision of Mr Charles Potter QC sitting as a Special Commissioner in *Getty Oil Co v Steele* [1990] STC 434. Mr Potter's conclusion is highly supportive of Mr Baldry's argument. But Mr Potter did not, of course, have the benefit of the conclusions and reasoning of the authorities which we have already mentioned in this context. His decision is not, in any case, binding on us and if, and to the extent, that we find the reasoning of those other cases to be persuasive or even binding, we must follow them.

287. In relation to the other cases referred to by Mr McDonnell (*Sema* and *UBS*), Mr Baldry distinguishes them from the present case. Each of those cases was considering not so much the meaning of the word "relief" but the meaning of a wider phrase a "relief from, or repayment of, tax" or "relief from corporation tax". Neither of those cases decided that the circumstances in question did not involve a relief: what they were concerned with was whether the relevant relief was from the tax concerned. That is not the position in the present appeals where, on Mr Baldry's submission, the relief is "in respect of" income tax.

288. We have sufficiently identified the context of *Sema* at paragraph 275 above. The Judge in the High Court (Lightman J) had agreed with the Special Commissioners concluding (in favour of the Revenue) that as a matter of construction of the definition of "tax advantage" in section 709(1), the tax credit was a tax advantage because it was a "relief", following Vinelott J in *Colchester Estates (Cardiff) v Carlton Industries plc* [1986] Ch 80: see paragraph 38 of the judgment of

Jonathan Parker LJ in *Sema*. As Mr McDonnell has pointed out, what Jonathan Parker LJ had to say on this topic in his judgment was, strictly speaking, *obiter*. Although Mr McDonnell relied in particular on the passage from paragraph 109 of that judgment, we think that it is important to read it in the context of paragraphs 108 to 111 as a whole.

289. The following points are to be noted:

(a) In paragraph 108, the judge rejected the submission on behalf of the trustees based on the conceptual difference between exemption and relief as involving a degree of sophistication running entirely counter to the general approach to be adopted to the construction of anti-avoidance provisions.

(b) What the draftsman was attempting to do when defining "tax advantage" was to cover every situation in which the position of the taxpayer *vis a vis* the Revenue is improved. The distinction between "relief" and "repayment" in section 709(1) was not based on any conceptual different between the two. The true interpretation was simpler. It was as set out in the quotation at paragraph 275 above, an explanation which must be read in the light of the opening words of paragraph 109.

290. Accordingly, Mr Baldry submits that *Sema* provides no support for Mr McDonnell's argument.

291. Turning to *UBS AG*, the decision in the Court of Appeal was that Special Commissioners (Dr Avery Jones and Julian Ghosh) had held, unequivocally, that the payment of the tax credit in that case was a "relief" within section 788 ICTA 1988. They referred to *MEPC Holdings* and to Lord Hoffmann's observation that the term "relief" was not a term of art. They concluded that, in the broad sense, a repayment could be a relief and that "on the ordinary meaning of the language the payment of a tax credit in the circumstances of section 243 is a relief from tax….". But they went on to hold that it was not a relief from corporation tax. The judgment of Etherton J, upholding the conclusion of the Special Commissioners, focused on the ultimate question whether there was a relief from corporation tax and did not address "relief" as a separate or prior issue.

292. In the Court of Appeal, Moses LJ dealt with the issue at paragraphs 42 to 50 of his judgment (with which the other members of the Court agreed). We have already quoted the passage on which Mr McDonnell particularly relies at paragraph 273 above. Moses LJ went on, in the same paragraph, to say that it was for that reason "which attempts merely to echo the reasoning of the Special Commissioners" that he rejected the contention that UBS was entitled to invoke Article 23(2) of the UK/Switzerland Double Tax Treaty. It is to be noted, also, that in paragraph 42 of his judgment, Moses LJ recorded his agreement with the conclusions of the Special Commissioners at paragraphs 36 to 39 of their decision. Accordingly, it can be seen that he agreed with the conclusion in paragraph 7 that the tax credit was a relief within the meaning of section 788(3)(a).

293. In our judgment, Mr McDonnell's argument that neither the FIDs claims nor the *Manninen* claims fall within section 43 is incorrect. In the light of the analysis of the authorities and the submission made on this topic, our reasons rejecting the argument are set out in the following paragraphs.

294. In the first place, we consider that the claim made by BTPS for the tax credits to which we have held, in our decisions in principle on the FIDs claims and the

Manninen claims, it is entitled, are "claims" within section 43. We accept Mr Baldry's submissions concerning the structure of section 231 and consider that a taxpayer is entitled to the set-off or payment referred to section 231(3) if, but only if, he makes a claim. The formal claim will, ordinarily, be made in a tax return. But even if Mr McDonnell is right in saying that set-off is automatic and does not need to be claimed, he cannot, we think, be right in saying that a request or demand by a taxpayer for payment under section 231(3) is not a claim. That of itself lends strong support to the view that even a set-off has to be claimed, otherwise a distinction – unwarranted, it seems to us – would have to be drawn between set-off and payment in terms of time-limits.

295. In the second place, we consider that the claim to a tax credit is a claim to a relief. As already mentioned, the term "relief" is not a term of art. We do not feel constrained by the authorities relied on by Mr McDonnell to conclude that the claim to a tax credit is not a "relief". Quite the reverse: it seems to us that *UBS AG* lends strong support to the conclusion that it is a "relief". Indeed, it may even be that we are bound by the judgment of Moses LJ expressly agreeing with the conclusions of the Special Commissioners as we have pointed out, binds us to reach the conclusion that there is a "relief". There is nothing, in our view, in *Sema*, which points to a contrary conclusion.

296. There is one additional point which occurs to us and which we would like to mention. It has not influenced our decision and we have not, given our conclusion, thought it sensible to seek the parties' views. It is that the purpose of giving a tax credit, in the case of fully taxable persons, is to avoid double taxation; that is how the matter has been addressed in *Manninen* itself and in *FII EJ*. Accordingly, the tax credit is surely to be seen as giving rise to a claim "in relation to" income tax. The claim therefore gives rise, as we see it, to a relief from double taxation and is therefore a "claim for relief in respect of income tax" in relation to the recipient of a dividend who would otherwise suffer an economic double tax burden. It is therefore the case, we consider, that a claim in relation to a tax credit raised by a fully taxable person falls fairly and squarely within section 43(1). It would be an anomalous situation if an exempt taxpayer were not also subject to section 43. We should construe section 43 so as to avoid the anomaly.

297. We gain comfort from, without relying on, the decision in *Getty Oil Co* and are pleased to be able to follow the decision of such an eminent practitioner as Mr Potter.

Community law concerning limitation

General

298. To start with, Mr Vajda relies on four propositions which he says are established by the authorities in relation to limitation periods under national law which may operate to bar claims brought in reliance on Community law.

299. First, under the principle of effectiveness, the limitation period must not operate so as to render it virtually impossible or excessively difficult for claimants to exercise the rights conferred by Community law. As a general statement of principle, that is obviously correct and easy to state. What is far more difficult is to decide, in a particular case, is whether that principle is infringed.

300. It is worth referring to a passage from the judgment of the ECJ in the *Peterbroeck* case at paragraph 14 as follows:

"14. For the purposes of applying those principles, each case which raises the question whether a national procedural provision renders application of Community law impossible or excessively difficult must be analysed by reference to the role of that provision in the procedure, its progress and its special features, viewed as a whole, before the various national instances. In the light of that analysis the basic principles of the domestic judicial system, such as protection of the rights of the defence, the principle of legal certainty and the proper conduct of procedure, must, where appropriate, be taken into consideration."

301. Reference can also be made to Case C-327/00 *Santex SpA v Unità Socio Sanitaria Locale No 42 di Pavia* [2004] 2 CMLR 30. This case concerned procurement notices for public supply contracts and the question was whether the imposition of time limits which purported to rule out any challenge to the validity of those notices could be relied upon by the national authority. In principle, a time limit was valid and the 60 day limit in fact applying appeared reasonable. But this result is to be qualified by what was said by the ECJ at paragraphs 56 to 58 of the judgment:

"56. However, for the purpose of applying the principle of effectiveness, each case which raises the question whether a national procedural provision renders application of Community law impossible or excessively difficult must be analysed by reference, in particular, to the role of that provision in the procedure, its progress and its special features, viewed as a whole [reference being made to *Peterbroeck*].

57 Consequently, although a limitation period such as that at issue in the main proceedings is not in itself contrary to the principle of effectiveness, the possibility that, in the context of the particular circumstances of the case before the referring court, the application of that time-limit may entail a breach of that principle cannot be excluded.

58 From that point of view, it is necessary to take into consideration the circumstance that, in this particular case, although the disputed clause was brought to the notice of the parties concerned at the time of the publication of the notice of invitation to tender, the contracting authority created, by its conduct, a state of uncertainty as to the interpretation to be given to that clause and that that uncertainty was removed only by the adoption of the exclusion decision."

302. The actual decision turned very much on the particular facts of the case: the public authority had by its conduct created a state of uncertainty (*ie* about the true meaning of the disputed clause) and it was only once it had made the exclusion decision (*ie* the decision to exclude the applicant from the tendering process) that the uncertainty was removed, by which time it was too late for the applicant to challenge the notice of invitation to tender. Thus it was held that

"the changing conduct of the contracting authority might be considered, in view of the limitation period, to have rendered excessively difficult the exercise by the harmed tenderer of the rights conferred on him by Community law."

303. Mr Vajda points out that the phrases "virtually impossible" and "excessively difficult" do not mean the same things. The fact that a claimant was not barred from bring a claim sooner than he did does not answer the separate question whether to do so would have been excessively difficult. Whether a right is rendered excessively difficult has to be considered by reference to the facts of the particular claim including the conduct of the Member State.

304. In that context, he says that the exercise of a Community law right could be rendered excessively difficult in a case where the claimant is required to pursue his claim in a jurisdiction (Jurisdiction A) in which jurisdiction the claimant is out of time, but in circumstances where the claimant has in fact brought his claim in another jurisdiction (Jurisdiction B) where the claim would be in time. The principle of effectiveness requires, he says, Jurisdiction A to disapply its time-limits. He also says that it does not follow from the fact national legislation sets out a time limit (as in the case of section 43) that it necessarily complies with the principle of effectiveness.

305. Mr Vajda's second proposition is that the limitation period and associated national procedural rules must be fixed in advance and with sufficient certainty that a claimant will be able to determine, from the statute book, which limitation period will be accorded to it for the purpose of bringing proceedings, so as to be able to bring a claim within that period. He relies on Case C-62/100 *Marks and Spencer* [2002] ECR I-6325 [2003] QB 886 ("***M&S I***") and Case C-456/08 *Commission v Ireland* [2010] ECR I-859 as examples.

306. The third proposition is that the conduct of the national authority combined with the national procedural rules and the existence of the limitation period must not result in totally depriving a person of the opportunity to enforce his rights before the national courts. This is a specific instance of the principle of effectiveness. He refers to Case C-208/90 *Emmott v Minister for Social Welfare and Attorney General* [1991] ECR I-4269 as an extreme example of this. It was, indeed, an extreme example as subsequent cases have shown as we have already mentioned. Mr Vajda says that the basic principle underlying *Emmott* was recently reaffirmed in Case C-452/09 *Iaia and others v Ministero dell' Istruzione and others* [2011] ECR 1-0000. We set out paragraphs 21 to 23 of the judgment to which we will need to refer in due course:

> "21. EU law does not preclude a national authority from relying on the expiry of a reasonable limitation period unless, by its conduct, it was responsible for the delay in the application, thereby depriving the applicant in the main proceedings of the opportunity to enforce his rights under an EU directive before the national courts.
>
> 22. It should also be made clear that, in accordance with settled case law, the fact that the court may have ruled that the breach of EU law has occurred generally does not affect the starting point of the limitation period.
>
> 23. This is a fortiori the case where, as in the main proceedings, the breach of EU law was not in doubt. In such a situation, a ruling by the Court that there has been such a breach is not necessary to enable the beneficiaries to ascertain the full extent of their rights. The fact that the period starts to run before the Court has given its ruling does not therefore render it virtually impossible or excessively difficult to safeguard the rights derived from EU law"

307. The Court in *Iaia*, however, recognised that the decision in *Emmott* depended on its exceptional circumstances, and hence qualified its decision in the way just quoted, following *Steenhorst-Neerings* and Case C-228/96 *Aprile* [1998] ECR I-7141 ("***Aprile II***") and referring to *Santex SpA*.

308. Mr Vajda also refers to Case C-427/10 *Banca Antoniana Popolare Vebeta SpA v Ministero dell'Economia e delle Finanze, Agenzia delle Etrate* [2011] ECR I-000, [2012] STC 526, a case to which we will need to return.

309. Mr Vajda's fourth proposition is that whilst accepting that there is no general rule that national limitation periods fall to be suspended, or 're-set', by reference to decisions of the ECJ which clarify the substantive law, there may be special

circumstances in which the starting point of the limitation period will be affected by rulings of the ECJ, at least in cases where the breach of Community law was previously in doubt. He relies on the use of the word "generally" in the discussion of the commencement of the limitation in paragraphs 22 and 23 of *Iaia*. He is somewhat critical of the reliance of the Tribunal on *Biggs* which, as he points out, cannot override the rules of Community law regarding the principle of effectiveness.

310. Before dealing with Mr Vajda's detailed submissions, we say something more about the general propositions which are relied on.

311. There are two lines of cases in the ECJ which we need to mention. The first line is where a person has a Community law right but does not know it and fails to take the necessary action to assert it within a reasonable domestic law time limit. The principle of legal certainty, which trumps the principle of effectiveness, means that he loses the right.

312. The second line of cases applies where a person has a Community law right which he is in time to assert but, before he does so, it is taken away without any transitional provision. In such a case, the principle of effectiveness allows him to assert the right in spite of the domestic time limit. That is not the case in the present appeals. We are not therefore concerned with cases such as *Fleming (t/a Bodycraft) v HMRC* and *Condé Nast Publications Ltd v HMRC* [2008] UKHL 2, [2008] 1 WLR 195.

313. As to the first line of cases, paragraph 35 of the judgment in *M&S I* shows, the ECJ had previously held that, in the interests of legal certainty, which protects both the taxpayer and the administration, it is compatible with Community law to lay down reasonable time-limits for bringing proceedings (reference being made to *Aprile II*). Such time-limits (*ie* reasonable domestic time-limits) are not, at least by themselves, liable to render virtually impossible or excessively difficult the exercise of the rights conferred by Community law.

314. It is clear that reasonable time-limits are compatible with Community law even if the consequence is that the claimant's action is dismissed: see for instance Case C-90/94 *Haahr Petroleum Ltd* [1997] CR I-4085 at paragraph 48. It will often make no difference to that proposition that the substantive Community law principles applicable to the claim might only have been clarified by the ECJ after the expiry of the applicable time limit: see *Aprile II*. There is support for this in the Court of Appeal decision in *F J Chalke Ltd and another v HMRC* [2010] EWCA Civ 313 where it is confirmed that Community law rights may be lost where the claimant fails to exercise within applicable time limits those rights due to his ignorance of their existence or the development of the law by judicial decisions (see [55] and [69]).

315. *Aprile II* concerned a claim for repayment of charges unlawfully levied in respect of customs transactions and which Italian finance authorities had refused to repay. The charges were levied in November 1990 as is apparent from paragraph 7 of the Opinion of Advocate General Ruiz-Jarabo. The judgment in *Aprile II* explains, at paragraphs 6 and 7 as follows:

> "6. By judgment of 5 October 1995 in Case C-125/94 *Aprile v Amministrazione delle Finanze dello Stato* [1995] ECR I-2919 (hereinafter 'Aprile I'), the Court held, first, that Directive 83/643, as amended by Directive 87/53, was not applicable to customs formalities in respect of goods from non-member countries, and, second, that the Member States were not entitled unilaterally to impose charges having equivalent effect in trade with those countries.

7. Following the judgment in Aprile I, it fell to the national court to consider an objection raised by the defendant administration to the effect that Aprile's claimed right to reimbursement had become statute-barred by virtue of [the relevant Italian legislation]”

316. It can be seen that the charges were unlawfully levied in November 1990 but that the clarification of the applicable substantive law was only obtained in 1995 when the Court gave its decision on the preliminary reference. This was after expiry of the Italian time limit, which was 3 years. Italy was permitted to rely on that time limit provided that it applied in the same way to actions based on Community law for repayment of such charges as to those based on national law. Further, it was held that Community law does not prohibit a Member State from resisting actions for repayment of charges levied in breach of Community law by relying on a time-limit under national law even if that Member State had not yet amended its national rules in order to render them compatible with those provisions.

317. It does not follow from *Aprile II* that national time-limits can always be relied on even where the time limit is *prima facie* of a reasonable length. They cannot be relied on, for instance, where national legislation has effect in relation to an existing accrued Community right, for example where the Member State shortens a limitation period with retroactive effect without providing an adequate transitional period (the second line of cases where the applicable principles are summarised in paragraphs 36 to 42 of the judgment of the ECJ in *Marks & Spencer I*). Nor can they be relied on in cases, such as *Santex SpA* and *Iaia.*

318. There has been recent clarification in this area by the Supreme Court in *BCL Old Co Ltd v BASF plc* [2012] UKSC 45 (“***BCL***”). In that case, the Supreme Court considered whether a statutory limitation period which would otherwise have barred the claim of BCL against BASF for damages for participation in an unlawful cartel was contrary to the principles of effectiveness and legal certainty.

319. The facts can be taken from paragraphs 2 to 4 of the judgment of Lord Mance:

“2. The cartel related to the supply of vitamins within the European Union. By Commission Decision COMP/E-1/37.512 of 21 November 2001, the European Commission found that the cartel infringed Article 81 of the EC Treaty (now TFEU 101) and imposed fines accordingly. Members of the cartel had until 31 January 2002 to appeal against the Commission's decisions. In the event, on 31 January 2002, only BASF appealed, and BASF only appealed against the fine levied. Notice of its appeal was published in the Official Journal on 4 May 2002 (C109/49). The Commission's Decision to which the appeal related was only published in the Official Journal of the European Communities on 10 January 2003. The Court of First Instance on 15 March 2006 reduced the fine imposed on BASF. The deadline for any further appeal by BASF to the European Court of Justice expired on 25 May 2006 without any further appeal being lodged.

3. Under the Limitation Act 1980, section 2, BCL had six years to bring an action for tort in the High Court, running or "almost certainly" running (as Mr Vajda QC for BCL accepted in the notice of appeal and his oral submissions) from 21 November 2001. However, on 20 June 2003 section 47A of the Competition Act 1998, as inserted by section 18(1) of the Enterprise Act 2002, came into force, giving BCL the alternative possibility of a claim for damages in proceedings brought before the Competition Appeal Tribunal. The possibility was exercisable under certain conditions, the effect of which, as

now conclusively established by the Court of Appeal, is that the time for bringing such a claim expired on 31 January 2004, two years after the time allowed for appeal against the Commission's decision on infringement, without any possibility of extension. No High Court proceedings were brought, but proceedings were in January 2004 issued in the Tribunal against other cartel members. The first intimation by BCL to BASF of any intended claim was on 21 November 2006, and proceedings were not issued in the Tribunal by BCL against BASF until 12 March 2008. BASF responded by contending that the claim was time-barred.

4. Reversing the Tribunal, the Court of Appeal held on 22 May 2009 that the claim was time-barred and could proceed, if at all, only with an extension of time, [2009] EWCA Civ 434. The Tribunal on 19 November 2009 assumed that it had power to grant an extension, but declined to do so on the merits, [2009] CAT 29. The Court of Appeal held on 12 November 2010 that the Tribunal had no power to extend time under United Kingdom law: *BCL Old Co Ltd v BASF SE (No 2)* [2010] EWCA Civ 1528, [2011] Bus LR 428. It held further that European law did not override the United Kingdom time bar or require a power to extend to be treated as existing. On this basis, the merits of any application for an extension, if there had been such a power, became irrelevant. With the Supreme Court's permission, BCL now appeals to the Supreme Court against the Court of Appeal's decision of 12 November 2010, but solely on the issue of European law."

320. BCL sought to argue that the decision of the Court of Appeal dated 22 May 2009 had been unforeseen and unforeseeable, and had the effect of cutting down the time for bringing its claim down by over 4 years, from May 2008 to January 2004, and of doing so at a time when the relevant period had long since expired. BCL sought to argue (among other points) that in the circumstances the European law principles of legal certainty and effectiveness required the Tribunal to extend the period in which claims could be brought.

321. In the Court of Appeal (that is to say, the decision at [2010] EWCA Civ 1258), BCL's appeal was dismissed on the basis that (among other matters):

(1) the limitation period in section 47A of the Competition Act 1998 was not intrinsically uncertain notwithstanding that the Court of Appeal had reached a different view as to its effect to that of the Tribunal (see paragraph 65 of the judgment); and

(2) the fact that it was only following the judgment of the Court of Appeal in 2009 that the correct construction of section 47A was identified did not mean that the limitation period itself was either unclear or not reasonably foreseeable in late 2003 and at the beginning of 2004 (when the period expired) (see paragraph 73 of the judgment); and

(3) in the circumstances there was nothing within section 47A or its application in those circumstances which offended the principle of effectiveness or legal certainty, notwithstanding that its effect was to operate as a bar to the claimants' claims.

322. The Supreme Court described the reasoning of the Court of Appeal as "impeccable" (see paragraph 29 of the decision of the Supreme Court).

323. Lord Mance set out the relevant EU law at paragraphs 11 to 18 of his judgment. We do not propose to set out the passages (found in paragraphs 12 and 16) where Lord Mance identifies different expressions describing what is meant by "excessively difficult" under the principle of effectiveness, but we do mention the expressions themselves: "[ascertainable] with a reasonable degree of certainty", "sufficiently foreseeable", "sufficiently precise, clear and foreseeable", "sufficient clarity" and "sufficiently clear and precise".

324. He referred to *Commission v Ireland* where these different tests were mentioned. At this stage we need only note that it appeared to Lord Mance (see paragraph 18) that all the statements of principle in *Commission v Ireland* were readily reconcilable: the requirement is "that the true effect or interpretation should be sufficiently foreseeable or clear". In explaining the test in that way, he rejected BCL's argument that complete certainty in limitation periods was required and that the existence of any arguable doubt as to the limitation period would breach the principle of effectiveness.

325. We do note, however, that there may be scope for a more onerous test where the relevant claim is brought by a citizen against the State. As Lord Mance put it at paragraph 23:

> "When considering what test may be appropriate, some relevance might be suggested to attach to the relief available for any infringement of the principles of effectiveness and legal certainty. If the only remedy is against the State for introducing a law which is uncertain in its impact, that might make it easier to accept a broader principle of certainty than if the remedy is, as claimed by the present appeal, against the other party to civil litigation. But that approach is of no assistance to BCL on this appeal, in which the State is not involved"

326. We do not read this as a ringing endorsement of the proposition that a different test should be applied. The issue did not arise for decision and Lord Mance is to be seen as saying no more than that his decision in relation to a dispute between private parties was not determinative in the case of a dispute between a private person and the State.

327. In the present case, of course, BTPS' claim is a claim against the State. BTPS notes that a similar point was made, specifically in the context of a claim by a taxpayer against the member state, by Peter Gibson LJ in *Test Claimants under Loss Relief GLO (Autologic)* [2004] EWCA Civ 680, [2005] 1 WLR 52, at paragraph 23:

> "The fact that it is the member state itself which has benefited from the breach of Community law at the expense of the taxpayer militates in favour of the taxpayer being entitled to recover what he has lost without obstacles being put in the taxpayer's way."

328. This is a convenient point in our decision to refer to the *Autologic* litigation. This was a group litigation case where the claimant companies alleged that UK tax rules relating to group relief denied them a benefit to which they were entitled under Community law and sought restitution and damages against the Inland Revenue Commissioners. Park J (see [2004] EWHC 3588, [2004] STC 3588) considered that issues of tax law which were disputed between a taxpayer and the Inland Revenue ought to be resolved on appeals to the Commissioners as provided for in UK tax legislation and not on cases brought before the High Court, He decided that either the High Court had no jurisdiction or, if it did, that it ought in its discretion to refuse to

deal with the basis of the group relief issue. The Court of Appeal (in the decision cited in the preceding paragraph of this decision) allowed the appeal. It concluded that it was a principle of Community law that every court of a Member State in a case within its jurisdiction was obliged to apply that law in its entirety and set aside any provision which conflicted with Community law. The importance of the principle of effectiveness could not be overstated: any provision of national law which makes the exercise of a right conferred by Community law practically impossible or excessively difficult cannot prevail.

329. The Inland Revenue appealed to the House of Lords, whose decision is found at [2005] UKHL, [2006] 1 AC 118. The claimants were identified as falling into two categories. The first group comprised those companies which, if their claims under Community law were good, would be able to obtain in full the group relief which they claimed following an appeal to the Special Commissioners. The second group comprised those companies for which that course was not open due to procedural requirements such as the claim being outside a relevant statutory time limit.

330. There was a fundamental difference of approach between the majority (Lord Nicholls with whose speech Lord Steyn and Lord Millett agreed, the latter giving a short speech of his own) and the minority (Lord Hope and Lord Walker: Lord Walker gave a speech with which Lord Hope agreed, although he did add a short speech of his own).

331. In accordance with the majority view, the Inland Revenue's appeal in relation to the first category was allowed. The High Court proceedings would be an abuse of the Court's process since the dispute was one which Parliament had assigned to the specialist tribunal so that the taxpayer should follow the statutory appeal route. It was recognised that it was for the Member State to determine the question as to which court or tribunal had jurisdiction to hear disputes involving rights derived from Community law, provided that full effect was given to such rights. The Special Commissioners had the same powers and duties as the High Court in giving effect to all directly enforceable rights by disapplying or adapting domestic statutory requirements to the extent necessary. Confining claimants in the first category to the statutory route was not regarded as "excessively onerous": see paragraph 25 of Lord Nicholls' speech.

332. In the course of considering the first category, Lord Nicholls referred to the decision of the ECJ in *Hoechst AG & Another v IRC and Attorney General* and *Metallgesellschaft Limited v IRC and Attorney General* (Joined Cases C-397/98 and C-410/98) ("***Hoechst***") a decision which had been regarded by the Court of Appeal as determinative of the test cases in *Autologic* in not requiring the claimants to proceed by claiming group relief (which would inevitably be refused) and then appealing to the Special Commissioners. Lord Nicholls disagreed with the Court of Appeal about that, considering (see paragraph 29) reliance to be misplaced:

> "…The taxpayers are seeking to apply the European court ruling out of context. In the Hoechst case this ruling was directed at rejecting a governmental defence based on the taxpayers' alleged lack of reasonable diligence in pursuing its claims. The Hoechst ruling was not directed at a situation where, as here, the claimants' claims have yet to be decided by the national court and there exists a statutorily prescribed route by which the claimants are able to obtain the tax relief they say is their entitlement under Community law. Which court or tribunal has jurisdiction to hear disputes involving rights derived from Community law is a matter for determination by each member state…"

333. Then, after noting the need for the remedial route to be compliant with the principles of equivalence and effectiveness, Lord Nicholls went on, in paragraph 30, to say this:

> "The statutory route prescribed for group relief claims was not designed for claims in respect of non-resident companies. So, as United Kingdom law presently stands, at the initial step a taxpayer's group relief claim will inevitably be refused by the revenue. Further, as already noted, some statutory requirements will need adaptation to accommodate claims in respect of non-resident companies. But neither of them renders the statutory route "practically impossible or excessively difficult"…..".

334. At paragraph 37 of his speech, Lord Nicholls made some important general observations concerning cases where a person has been deprived of benefits to which he is entitled under directly applicable provisions of Community law. He noted that in cases like the appeals before the House, the primary remedy for non-receipt of such benefits is to have recourse to the tribunal (*ie* the Special Commissioners in the test cases). He went on, at paragraph 38, to say this:

> "No doubt in such cases there may have been a violation of Community law. Community law requires that national law must ensure rights conferred on individuals by Community law are fully effective in each member state. This obligation can hardly said to be fulfilled when and so long as national authorities, such as government departments, rely on the terms of the national legislation as the reason for declining to afford an individual benefits to which he is entitled under directly applicable provisions of Community law. The right of individuals to rely on directly applicable provisions of the EC Treaty before national courts is not sufficient in itself to ensure full and complete implementation of the Treaty….. But a claim for damages for breach of Community law is not, in general, the appropriate remedy when currently it is still open to an applicant to obtain the benefits to which he is entitled by making an application to the statutory tribunal: provided always that the statutory route accords with the Community law principles of equivalence and effectiveness."

335. In relation to the second group, the conclusion was that the Special Commissioners had no jurisdiction: the remedy lay in claiming restitutionary and other relief in respect of the UK's failure to give proper effect to Community law. Claimants in the second group should therefore seek an extension of time limits from the Inland Revenue to enable them to use the statutory route and, if their applications were refused, their High Court claims could continue.

336. In more detail, Lord Nicholls saw no reason to suppose that the statutory time bars applicable to the group relief claims were in themselves inconsistent with Community law:

> "40. ……… This means that, in respect of this class of cases, it is now too late for the taxpayers to obtain group relief by following the statutory route. A similar view has, rightly, been expressed by the Court of Appeal in respect of an employment tribunal's jurisdiction to entertain claims for unfair dismissal involving directly applicable Community rights outside the statutory time limits: see Biggs v Somerset County Council….
>
> 41. In such cases the taxpayer's remedy necessarily lies elsewhere. In such cases, the taxpayer's remedy is of a different character. The taxpayer's remedy lies in pursuing proceedings claiming restitutionary and other relief in respect of the UK's failure to give proper effect to Community law… Difficult questions, both of

domestic law and Community law, may arise about the time limits applicable to High Court claims of this character…."

337. But he subjected that to the caveat (see paragraph 42) that both the Revenue and the appeal commissioners have power to extend time limits for late amendments and late appeals (and HMRC have a power relevant in the present cases under section 49 TMA 1070). He also (see paragraph 43) noted that a single taxpayer might have to take his claims to different courts for different remedies: this he regarded as unfortunate but was inherent in the distinction between the two classes of case, the one to obtain the tax relief, the other to obtain damages for unlawful failure to make such relief available.

338. Lord Walker disagreed with Lord Nicholls' conclusion in paragraph 41 that the companies' remedy was to be found elsewhere if they were time-barred before the commissioners. His view (see paragraph 126) was that if the companies were compelled to seek their remedy before the Special Commissioners, that tribunal would have the power and indeed the duty to disapply any time-limit incompatible with Community law even if this involved an extension of their jurisdiction. In contrast, if the time limit was compatible with Community law, then the companies whose claims were out of time in the statutory tribunal could go no further.

339. *Autologic* was, it must be remembered, a case concerned with the appropriate forum for the hearing of disputes and not directly with time limits. It seems to us, however, that in some of the test cases the reason why the case fell in the second group rather than the first group was precisely because the statutory time limit had passed so that the statutory tribunal had no jurisdiction. This is underlined by the possibility of the grant by the Inland Revenue of an extension of time, thus giving the commissioners jurisdiction and throwing the taxpayer back into the statutory appeals system and out of the High Court.

340. That is not to say that the Tribunal itself cannot ever be required, as part of the moulding or disapplication of legislation to disapply a time limit: in this respect, we can see no reason to treat time limits differently from any other provision. Thus, in cases such as *Fleming/Conde Nast*, the time limit specified in the UK statute fell to be disapplied because the absence of a transitional provision meant that the time limit breached Community law principles. The Tribunal would have to give effect to Community law by disapplying the time limit in the same way as a Court would have to do.

341. But if the time limit is inherently reasonable, then the position is different. The reasonable time limit will be effective as against a taxpayer seeking to enforce his Community law right even if he did not learn of his right until after the expiry of the time limit: that is the general rule shown in cases such as *Aprile II*, *Fantask* and *Haahr Petroleum*. If the case is exceptional and falls within the ambit of cases such as *Emmott* or *Iaia*, then the Tribunal, as much as the court, will have to recognise that fact and disapply the (unreasonable) time limit accordingly. That, it seems to us, does not cut across what Lord Nicholls said. He surely had in mind a case of the first type and was envisaging a situation where the domestic time limit in relation to the statutory claim was valid. In that case, the statutory appeal route would not be open and the taxpayer would then have to enforce his Community law right in the High Court relying on the failure of the UK to comply with its Community law obligations. That, of course, would only avail him if he brought his claim in the High Court within the limitation period applicable to such claims (which may be different from the time limit for the statutory appeal route).

342. After that diversion into *Autologic*, we return to *BCL*. Lord Mance referred in some detail to *Commission v Ireland.* As he explained, the case arose from a challenge to the award to Celtic Roads Group ("CRG") of a contract for the construction of the Dundalk Western Bypass by the Irish National Roads Authority ("NRA"), a statutory body with the overall responsibility for the planning and supervision of works for the construction and maintenance of national roads. SIAC Construction Ltd ("SIAC"), a member of a rival consortium (EuroLink), was informed on 14 October 2003 that the NRA had decided to designate CRG as the preferred tenderer, in terms indicating that this meant that the NRA would be proceeding with discussions with CRG, but that, if they broke down, it might still enter into discussions with EuroLink. However, on 9 December 2003 the NRA decided to award the contract to CRG, and on 5 February 2004 it signed a contract with CRG accordingly. Proceedings were commenced by SIAC on 8 April 2004, on the basis that their time for bringing an action started to run on 5 February 2004. But the proceedings were dismissed by the Irish High Court on 16 July 2004, as out of time under Order 84A(4) of the Court's Rules.

343. Order 84A(4) provided:

> "An application for the review of a decision to award or the award of a public contract shall be made at the earliest opportunity and in any event within three months from the date when grounds for the application first arose unless the Court considers that there is good reason for extending such period."

344. The Irish High Court held that any action had to be brought no later than three months from 14 October 2003. This might be thought to be a surprising decision. And that was no doubt one of the reasons why the ECJ emphasised the need for clarity. As Lord Mance described the position:

> "Order 84A(4) *on its face* allowed review within three months of *either* the decision to award *or* the award of a public contract. It would have been hard to anticipate, without clear warning, that time for a challenge to the latter would run from the former. Under the equivalent English Rule of Court, which was in effectively identical terms to the Irish, it had been established at the highest level by May 2002 that a challenge to a grant of planning permission could be made within three months of the grant, and need not be brought within three months of any earlier resolution conditionally authorizing the grant: *R (Burkett) v Hammersmith and Fulham LBC* [2002] UKHL 23, [2002] 1 WLR 1593, per Lord Slynn para 5 and Lord Steyn para 42. The English courts would not have taken the same limiting view of Order 84A(4) as the Irish High Court did. Where a rule like Order 84A(4) points on its face to a course being open to a litigant, it is necessary for it to be made clear if a contrary result is intended."

345. This makes clear that the reason why *Commission v Ireland* was decided in the way in which it was flowed from application of the established tests (as referred to in paragraph 323 above) and not from the fact that Order 84A(4) might admit two meanings and was, in that sense, not clear. The existence of an arguable doubt or of a need for interpretation is not of itself sufficient to render national law insufficiently foreseeable or to make it excessively difficult for the subjects of the law know their position: see Lord Mance at paragraph 28. The contrary view would, in effect, be consistent only with a requirement of certainty, a view which has been roundly rejected by the Supreme Court as representing the jurisprudence of the ECJ.

346. It is not, therefore, enough for a claimant to succeed in a claim to enforce a directly enforceable right that the national procedures may be open to different interpretations. Thus in BCL (see at paragraph 31), Lord Mance professed himself to be

> "unimpressed by BCL's reliance on the fact that it did not itself commence legal proceedings either in the High Court or before the Tribunal within what has been established to have been the available limitation period. An individual party's conduct cannot serve as an assay of the clarity or otherwise of statutory provisions. In any event, the account of the relevant thinking and of the advice which is said to have led to it is so exiguous and to some extent puzzling that I could not attach to it any real significance in this context."

347. With that review of the law, we return to Grounds 2 to 5 of BTPS's Grounds of Appeal.

Ground 2
Section 43 is to be disapplied by reason of the principles of legal certainty, equivalence and effectiveness for all years.

Ground 3
Section 43 is to be disapplied by reason of the principles of legal certainty, equivalence and effectiveness in the case of claims where the same claims have been made in time in the High Court for all years.

348. We have found it convenient to discuss Grounds 2 and 3 together. We have set out at paragraphs 298 to 309 above a summary of Mr Vajda's legal submissions and his four propositions. His first proposition (see paragraph 299 above) concerning the principle of effectiveness is, as general statement, uncontroversial. Further light has been thrown on the subject by the decision of the Supreme Court in *BCL* which we have already considered at some length. And, to repeat, it must be remembered that ECJ authority is clear that a reasonable time-limit fixed in advance does not, of itself, offend the principle of effectiveness.

349. His second proposition (see paragraph 305 above) relates to the fixing of time-limits in advance in such a way that they can be seen from the statute book. We do not, ultimately, derive assistance from the cases cited in his skeleton argument – *M&S I* and *Commission v Ireland. M&S I* is concerned, as we have said, with the introduction of a new time limit without any transitional provisions, a situation in respect of which special considerations apply. *Commission v Ireland* is an example of the principle in practice but its facts are so far away from the present case that it provides no guidance, in our view, to how the principles stated are to be applied in the present case. As to being able to derive the limitation period from the statute book, this is not how it is put in the cases. Community law simply requires that such time-limits as are imposed (assuming that they are not inherently defective for some reason, such as being too short on any objective assessment) are (1) no less favourable than those which apply to domestic claims (the principle of equivalence) and (2) not framed so as to render virtually impossible or excessively difficult the exercise of rights conferred by Community law and therefore contrary to the principle of effectiveness. There can, we think, be no uncertainty of any sort about the limitation period applicable to BTPS's claims if and to the extent that they are properly to be brought before the tribunal so that section 43 applies. Whether that time limit should be disapplied as a result of Community law is another matter. But so far as certainty from the statute book is concerned, there can be no doubt. We deal separately with

the issue concerning the uncertainty about the forum (tribunal or court) in which BTPS should assert its Community law rights and the impact which the answer to that may have on limitation issues.

350. We are perfectly satisfied that the 6 year time limit in section 43 is a reasonable time limit and the same goes for the revised time-limit applying to 1996-97. We do not understand that to be an issue: the issue, so far as BTPS is concerned, is when that reasonable time limit should begin to run.

351. Mr Vadja's third proposition (see paragraph 306 above), that a taxpayer must not be totally deprived of his Community law rights as the result of the imposition of a limitation period may be relatively uncontroversial, qualified as it is by the recognition that *Emmott* was an extreme example and that a Member State can rely on a limitation defence unless by its conduct it was responsible for the delay in the application (in the present case, the application would be the commencement of proceedings in the First-tier Tribunal or the High Court). Mr Baldry has referred us to the way in which Ward LJ identified them in *Walker-Fox v SoS for Work and Pensions* [2005] EWCA 1441 at paragraph 49, as being that in some unconscionable way the state has obstructed the exercise of the individual's judicial remedy or contributed to his failure to exercise it. In the light of *Iaia*, we think that is pitching it too high.

352. We should, however, return as we said we would (see paragraph 308 above) to Case C-427/10 *Banca Antoniana Popolare Vebeta SpA*. That is an example of a case where the conduct of the national tax authority was relevant to time limits. In effect, the national tax authority had changed its mind on a substantive issue of VAT law, as appears from paragraph 13 of the judgment, as a result of which taxpayers became entitled to claim refunds of VAT if their claims were in time, and furthermore their customers became entitled to claim reimbursement of VAT from the taxpayers under civil law claims. The relevant services had been provided between 1984 and 1994 (see paragraph 1 of the Opinion of the Advocate General and paragraph 12 of the Judgment: the headnote is wrong in referring to 1984 to 1999). Accordingly, all claims were, under national law, outside the period for making a claim by the time of the 1999 circular under which the change of mind was announced. But the time-limit for the civil claims (eventually successful) made by recipients of the supplies against the supplier for VAT incorrectly invoiced had not expired. The taxpayer was thus faced with a liability to pay a refund to recipients of the supplies but with no ability to recover the VAT for which it had accounted to the national authorities. What is more, it had never had the opportunity to make such a claim prior to the expiry of the time limit since it was operating the system properly in accordance with the law as understood.

353. It is not entirely surprising that the ECJ answered the question in the way which it did, saying that the legislation was compatible with Community law but only if it is possible for the taxable person effectively to claim reimbursement. That condition was not satisfied where the application of national rules has the effect of totally depriving the taxpayer of the right "to obtain from the tax authority a refund of the VAT paid but not due, which the taxable person has himself had to pay back to the recipient of his services". It is that factual context that the paragraph 31 and 32 of the judgment relied on by Mr Vajda must be read:

> "31. Likewise, the Court has held that a national authority may not rely on the expiry of a reasonable time-limit if the conduct of the national authorities, combined with the existence of a time-limit, means that a person is totally deprived of any possibility of

> enforcing his rights before the national courts (see, by analogy, *Q-Beef and Bosschaert*, paragraph 51).
>
> 32.In the case before the referring court, it should be noted, first of all, that – as the European Commission pointed out at the hearing – **it would have been impossible or, at the very least, excessively difficult** for BAPV to obtain, by means of an action brought within the two-year time-limit, a refund of the VAT paid in the years from 1984 to 1994, **particularly in view of the position adopted by the tax authority – and confirmed, according to the information provided by the referring court, by the case-law of the national courts – which dismissed the possibility that the services supplied by BAPV fell within the exemption** provided for under Article 10(5) of DPR No 633/72." [emphasis added by Mr Vajda.]

354. Moreover, paragraphs 40 to 42 of the judgment indicate the factors which weighed heavily with the Court in reaching its decision. Thus (paragraph 40) the circular effectively reopened the question whether transactions consisting of the collection of those contributions were subject to VAT, (paragraph 41) the national authority must take account of the particular situations of economic operators and, where appropriate, provide for adjustments to the way in which this new legal assessments of those transactions are applied. This is just the sort of situation envisaged in paragraph 21 of *Iaia* (see paragraph 306 above) where the Member State is responsible for the delay in the taxpayer's application for a refund. We do not think that what the Court said in paragraphs 31 and 32 can be taken as lending support to the proposition that whenever a tax-collecting authority collects tax on the basis of its understanding of the law (including Community law) which is later shown to be wrong by a judicial assessment (and not by a change of view on the part of the authority) it necessarily follows that the principles of legal certainty or effectiveness are not met.

355. Mr Vajda's fourth proposition (see paragraph 309 above) concerns the suspension or resetting of national time limits. He may well be right that there are special circumstances in which the general rule, which he accepts, does not apply, the general rule being that national time-limits are not suspended or reset following clarification of substantive Community law by the ECJ. The question is whether there are special circumstances in the present case.

356. We do not agree that paragraphs 22 and 23 of *Iaia*, as set out in paragraph 309 above disturb the general rule which appears so clearly from the cases including *Aprile II, Fantask* and *Haahr Petroleum*. One can only speculate why the Court used the words which it did, but those words would be apposite to cover, for instance, a case such as *Emmott*.

357. Mr Vajda is no doubt correct in saying that *Biggs* is merely an example of a case where the general rule applies even where there are important decisions of national courts which clarify the law. He relies particularly on the passage from the judgment of Neill LJ at [1996] 2 All ER 742g-h:

> "Since 1 January 1973, and certainly since the decision of the Court of Justice in *Defrenne v Sabena*, there was no legal impediment preventing someone who claimed that he had been unfairly dismissed from presenting a claim and arguing that the restriction on claims by part-time workers was indirectly discriminatory."

358. He submits that the words "certainly since the decision of the Court of Justice in *Defrenne v Sabena*" are significant, indicating that the 1976 decision of the ECJ was, indeed, relevant to the question of whether there was a legal impediment to potential claimants. He is no doubt right in saying that *Biggs* does not override Community law – it could not do so – but it does not follow from that that there would have been a

relevant legal impediment even before the decision in *Defrenne v Sabena*. Lord Nicholls referred to *Biggs* with approval in *Autologic* in a passage which we have cited (see paragraph 336 above) without drawing attention to the fact of the decision in *Defrenne v Sabena*.

5 359. There is one further authority to which we must refer and on which Mr Vajda relies. It is Case C-268/06 *Impact v Minister for Agriculture and Food and others* [2008] ECR 1-2483 in which the ECJ determined that where as a matter of procedure in national law, a certain type of claim is to be determined by a specialised court, then the principle of effectiveness requires the specialised court to have jurisdiction to 10 determine <u>all</u> of the issues arising in the related claims, and for all periods, where the alternative would result in procedural disadvantages for claimants.

360. In that case the specialised court only had jurisdiction for claims relating to certain periods, but the claimant had the ability to bring claims for the remaining periods in the ordinary courts. At paragraph 51 the Court said this:

15 > "In those circumstances, where the national legislature has chosen to confer on specialised courts jurisdiction to hear and determine actions based on the legislation transposing Directive 1999/70, the obligation which would be placed on individuals in the situation of the complainants – who sought to bring a claim based on an infringement of that legislation before such a specialised court – to bring at the same 20 time a separate action before an ordinary court to assert the rights which they can derive directly from that directive in respect of the period between the deadline for transposing it and the date on which the transposing legislation entered into force, would be contrary to the principle of effectiveness if – which is for the referring court to ascertain – it would result in procedural disadvantages for those individuals, in terms, *inter alia*, 25 of cost, duration and the rules of representation, such as to render excessively difficult the exercise of rights deriving from that directive."

361. Mr Vajda submits that the approach in *Impact* has a bearing on the decision of the House of Lords in *Autologic*, We have already drawn attention to the difference between what Lord Nicholls said at paragraph 41 and what Lord Walker in the 30 minority said at paragraph 126 and have given our view on how *Autologic* affects taxpayers procedurally: see paragraphs 336 to 339 above. Mr Vajda submits that *Impact* shows that that discretion of the specialist tribunal is one which should be exercised where the alternative would – as Lord Nicholls indicated – result in procedural disadvantages for the claimants (which Mr Vajda submits is the position in 35 relation to BTPS).

362. We do not consider that *Impact* throws any light on the correct answers to the issue of time-limits in the present case. That case was not concerned with time limits, but was concerned with the allocation of a substantive issue to the correct tribunal. It 40 is true that it was a timing issue which might have resulted in different courts or tribunals hearing different aspects of a claimant's claim. But the result of the timing difference was, on the approach rejected by the Court, that a claim to directly enforceable rights in respect of a period before transposition of the directive should be dealt with by the High Court in Ireland and the claim once the directive had been 45 transposed should be dealt with in the Labour Court.

363. In our case, the position is entirely different. The taxation provisions with which we are concerned do not implement, or purport to implement, any treaty or directive obligation. The complaint is that the statutory charging provisions result in a breach of treaty provisions concerning the free movement of capital. The remedy for 50 that breach is, it is claimed and as we have held, a moulding or disapplication of certain of the statutory provisions. The First-tier Tribunal has the power, and indeed

the duty, to give effect to the statutory provisions as so moulded. The procedural route to the First-tier Tribunal is through section 42; and *prima facie*, a claim must be brought within the time-limit specified in section 43.

364. Either that time-limit as applied to BTPS and other taxpayers in a similar position is compatible with Community law or it is not. If it is, see paragraphs 366 to 371 below. If it is not, see paragraph 372 below.

365. If it is compatible *vis a vis* BTPS and other taxpayers in a similar position, then any failure on the part of BTPS or other taxpayers to bring their statutory appeals within the section 43 time-limit must be an end of the matter so far as the statutory appeal route is concerned. It does not matter, in that context, whether Lord Walker was correct in saying that the relevant test claimants in *Autologic* would have reached the end of the road if the time limit in that case was compatible with Community law (and so that BTPS would have reached the end of the road in the present case) or whether those claimants (and BTPS) might have some other claim in the High Court based on their directly enforceable rights having a different time-limit and providing a different remedy.

366. The point here is that the test claimants (and the same applies to BTPS) had a right to make a statutory appeal in accordance with a procedure that, on the hypothesis under consideration, was compliant with Community law in terms of its time-limits and, having failed to bring their claims within that valid time limit, lose their rights to invoke that statutory procedure. Whether that brings to an end the right to assert a High Court claim for a different remedy in respect of the same breach to which a different time limit may apply, is not a matter for us. We should make clear that we are leaving aside for the moment the position where a High Court claim has been commenced within the time limit for a statutory appeal.

367. It cannot be the case, we consider, that the First-tier Tribunal is to have an extended jurisdiction, following Mr Vajda's argument based on *Impact*, in relation to out-of-time claims simply because there is some other claim over which the High Court has jurisdiction. This is clearly so if the time for making the High Court claim has expired according to domestic law. We reject the conclusion that the principles of legal certainty and effectiveness could result in the disapplication of the time limit in the Tribunal if (i) the alleged uncertainty is whether to begin proceedings in the Tribunal or in the High Court and (ii) the domestic time limit in both of the forums, the Tribunal and the High Court where the claim might be brought, has expired. Whatever the arguments for applying the longer time-limit in each forum, it cannot be right to disapply time limits altogether. Indeed, if that result were correct then, by parity of reasoning, the High Court time limit would also have to be disapplied. The result would be that, absent the imposition of an overarching EU time limit (an area where the law is developing: see Case T-433/10P *Allen v Commission* 14 December 2011), there would be no time limit for BTPS to assert its claims at all.

368. We reach the same conclusion where the High Court claim has been made within the time-limit applicable to the High Court but where that claim is outside the time limit under section 43.

369. To put these points another way: In *Autologic*, the test claimants had directly enforceable rights under the EC Treaty as a result of a failure by the UK to provide group relief in their particular circumstances. There were two potential ways in which the rights of the test claimants could be vindicated assuming that the Inland Revenue continued to refuse to recognise those rights. The first was to provide them with group relief *via* the appeal route. The second was to give them a restitutionary or

some other common law right in an action in the High Court for failure by the UK to implement its treaty obligations. The two routes provide different remedies and have different time-limits as a matter of domestic law. The two routes do not necessarily result in the same financial consequences. The majority decision in the House of Lord in *Autologic* was that the first route provided the exclusive route where an appeal was still in time. Where it was out of time, it was permissible to go along the second route. We think that Lord Nicholls was not saying anything different from that. In particular, he said what he did in the context of a time-limit which he saw as valid under Community law. That is made clear by the first two sentences of paragraph 40 and the reference to *Steenhorst-Neerings* and *Johnson v Chief Adjudication Officer*, which we do not think we need to address specifically.

370. In the context of High Court claims, there may then be an argument that, having failed to bring its statutory appeal in time, that is an end of the matter for BTPS so that its claims should be struck out. If that argument is unsuccessful, there may be further arguments about (i) whether the High Court has power to direct HMRC to give effect to the tax legislation, moulded and disapplied as we have decided they should be (ii) if it has such power, whether it can be exercised notwithstanding the expiry of the time-limit for a statutory appeal and (iii) if it has no such power which can now be exercised, the extent to which BTPS has any remedy for breach by the UK of its treaty obligations. But those matters are for the High Court, not for us. We are concerned only with the question whether a statutory appeal can be brought outside the time-limit specified in section 43. On the assumption that that is a valid time-limit under Community law, the answer to that question must be that the statutory appeal cannot be brought even if a (different) claim has been brought in the High Court in time.

371. In contrast with the hypothesis just considered, if the section 43 time-limit is not compatible with Community law *vis a vis* BTPS, then as we see it, BTPS should be entitled to pursue its claim in the context of a statutory appeal before the First-tier Tribunal (provided that such an appeal has been brought within the time-limit, if any, which applies as a result of the interaction of Community law and domestic law). The Tribunal will, in our view, have to disapply the statutory time-limit. We do not read what Lord Nicholls said in *Autologic* as inconsistent with that view. We understand him to be saying, in paragraph 41, no more than that where the time-limit in relation to a statutory appeal is valid in accordance with Community law, such an appeal cannot be launched after the expiry of that period. In saying that the taxpayer's remedy lay elsewhere he was recognising that the taxpayer had a directly enforceable claim under Community law which was not exhausted by his right to proceed with a statutory appeal at least once the time limit had passed.

372. Applying all of this to the facts of the present case, it is said by Mr Vajda that the barring of BTPS's claims by section 43 would collide with the four propositions just discussed. There are two complaints. First, the absence of any clear procedure in national law for bringing the claims and secondly the characteristics of the particular claimants as trustees of a pension fund, meant that it was virtually impossible or excessively difficult for these claims to be brought before a date in 2003 (in the case of the FIDs claims) or a date in 2005 (in the case of the *Manninen* claims).

373. As to the lack of clarity of national procedural law (*ie* whether to bring a claim in the High Court or the First-tier Tribunal) we do not consider that this is a factor which made it virtually impossible or excessively difficult so as to breach the principle of effectiveness. In particular, there was no lack of foreseeability such as

that addressed in *BCL*. The position is, in our view, as set out in the following paragraphs.

374. BTPS cannot rely on any uncertainty about the substantive law to postpone the application of any otherwise valid limitation period. This is clear from the authorities including *Aprile II, Fantask* and *Haahr*.

375. Whatever uncertainty BTPS now identifies about the correct forum in which to bring its claims, it knew, or must be taken to have known, that the time-limit in relation to a statutory appeal was that laid down in section 43. There was never any uncertainty about the statutory time limit – it is clearly stated to be 6 years – nor was there any difficulty, let alone excessive difficulty, in bringing a claim within 6 years if BTPS had considered that that was the correct route for asserting its directly enforceable rights. Nor was there any difficulty, let alone excessive difficulty, in bringing in the High Court a claim seeking relief for breach by the UK of its treaty obligations (seeking restitution or whatever other remedy BTPS considered it was entitled to) within the appropriate time limit applicable to such claims.

376. As to the relief sought, the statutory appeal could only have had an impact on the amount of tax properly due; the tribunal had no power to grant a restitutionary remedy or any of the other relief claimed in the High Court proceedings. The remedies which could be, and were, sought in the High Court were declarations concerning the non-compliance of the ACT and FIDs regimes with Community law and monetary claims in restitution and damages. It did not need the decision in *Autologic* to establish those propositions; that decision was concerned with what the appropriate route was, not with the consequences of pursuing one or other route.

377. The only difficulty which can be alleged by BTPS relates to uncertainty about which route was the correct route in accordance with national procedural rules. As to this, Mr Vajda cannot contend, in the light of *BCL,* that the test is one of absolute clarity (as he had, in effect, submitted before the decision in *BCL* was known). At best, from his point of view, the less exacting test summarised by Lord Mance applies namely that the true effect or interpretation should be sufficiently foreseeable or clear.

378. For our part, we think that consideration of the correct test is something of a diversion. *BCL* it will be remembered concerned uncertainty about the time-limit applicable to a particular claim in a particular court: there was no uncertainty about where the claim should be brought and no question arose about different time limits applying in different courts. The only relevant decision concerning different courts or tribunals to which we have been referred is *Impact.* But as we have already pointed out that decision had nothing to do with time limits but was concerned with the relief which the Labour Court could give in relation to a directly enforceable right prior to transposition of the relevant directive into national law. The principle of effectiveness in that case led to the conclusion that the claimant should be able to assert its claim in a single tribunal without having to go to different tribunals in respect of different periods. It cannot be taken as lending any support to the proposition that a time limit imposed in one tribunal must be applied to proceedings in another tribunal.

379. There is no parallel, we consider, between those cases and the present case. Even if the principle of effectiveness were breached because of the uncertainty about the correct route for BTPS to adopt, it does not follow that the statutory time limit is to be disapplied in relation to proceedings before the First-tier Tribunal. Thus, in a case where a taxpayer such as BTPS has failed to bring a statutory appeal within time because it considered that the correct route was proceedings in the High Court, then his rights can be vindicated in the High Court. This is provided, of course, that it has

brought a claim within the time limit appropriate to the High Court: if its claim is time-barred in all courts and tribunals, the principle of effectiveness could not apply to remove the time-limit altogether, a result which would not be required by Community law. Indeed, it would, in fact, put the taxpayer in a better position than in a wholly domestic situation, contrary to the principle of equivalence. If it said against such a taxpayer that he should have brought his claim in the tribunal, but he is out of time for doing so, he still has his remedy in restitution or damages in the High Court on the hypothesis now under consideration *ie* that he has brought a claim in time in the High Court and that the principle of certainty was breached as a result of the uncertainty about the correct forum.

380. Accordingly, we are of the view that uncertainty about the correct forum in which to assert the Community law right does not entitle a taxpayer to commence proceedings in whichever forum he likes and to claim the longest of the limitation periods which would apply across all the forums which he might have chosen. Thus suppose there is uncertainty sufficient to engage the principle of effectiveness; and suppose that a taxpayer, in the light of that uncertainty, considers Forum A (*eg* High Court) to be the correct forum and commences his claim there within its limitation period but after the expiry of the limitation period in Forum B (*eg* tribunal). In such a case, we can see that the taxpayer may be able to continue with the claim in Forum A otherwise it could be excessively difficult to vindicate his rights. But we do not understand why the taxpayer should be allowed to rely on the limitation period applicable to Forum A (High Court) in order to bring an out-of-time claim in Forum B (tribunal). Nor do we do understand why the position should be any different if claim in Forum A was commenced within the limitation period applicable to Forum B.

381. However, whether that is right or wrong, we should address another argument for saying that the time limit under section 43 should not be disapplied and that neither the uncertainty itself, nor the fact that BTPS did not bring its statutory claims within the 6 year time limit, give rise to a claim that the principle of effectiveness has been breached. The argument rests on three propositions.

382. In the first place, as we have demonstrated, the mere fact that a domestic procedure is not free from doubt does not necessarily entail a breach of the principle of effectiveness. *BCL* shows that certainty is not a requirement. A doubt about procedural requirements is no different in that respect from a doubt about substantive law. In the second place, particular difficulties asserted by BTPS do not necessarily amount to a breach of the principle of effectiveness. In that context, we remind ourselves of paragraph 31 of *BCL* set out in paragraph 346 above.

383. In the third place, BTPS's case is that it was not until the decision of the House of Lords in *Autologic* that the correct procedure for bringing its claim became certain. A similar argument was advanced by the claimants in *BCL* where it was said that it was not until the decision of the Court of Appeal in May 2009 that the true construction of section 47A of the Competition Act 1998 was made clear. In the hearing before the Court of Appeal in *BCL,* Lloyd LJ characterised BCL's case in the following way:

> "Mr. Vajda pointed out that the circumstances of the present case are unusual in that, from May 2009 onwards, parties will have known how section 47A worked in terms of the effect of an appeal against an infringement decision, and would have no good reason for not bringing a claim under section 47A within time. By contrast, he argued (not in these terms) that the goal posts had been moved by the Court of Appeal's previous decision to the Claimants' disadvantage and that it should be regarded as

> entirely unacceptable, as a matter of European Community law, even if not of UK law, that (to adopt a different metaphor, also not one used by him) the rug should be pulled from under his clients' claim by a finding that there was no power to extend time."

384. In *BCL* both the Court of Appeal and the Supreme Court rejected the claimants' argument that the position as to the correct procedure was not sufficiently foreseeable prior to the Court of Appeal decision in May 2009. In this regard the Supreme Court held as follows:

> "39. The Tribunal decisions considered in paragraphs 32 to 38 above were irrelevant to BCL's actual conduct. But do they demonstrate objectively the existence of such uncertainty in English law as to infringe the relevant European legal principles? Clearly, it is unfortunate if Competition Appeal Tribunals arrive at conclusions on the commencement of a limitation period and on the power to grant an extension of time which are held erroneous on appeal to the Court of Appeal. But an appellate system is there to remedy error and to establish the correct legal position. I do not accept that its ordinary operation is the hallmark of a lack of legal certainty or effectiveness. The language and effect of the Competition Act were subsequently, and rightly, held by the Court of Appeal to be clear. The *Emerson Electric* and *BCL* Tribunals gave the words 'any' and 'decision' significance which they could not bear. They also failed to interpret section 47A in the context of the statute and its other sections read as a whole. It was by any standard readily foreseeable that an opposite view would be taken on appeal. The Tribunal decisions do not in my view lead to a conclusion that English law was insufficiently certain or that it made the bringing of a claim in time excessively difficult. At the very least, the risks of not bringing proceedings against BASF by 31 January 2004 were or should have been evident."

385. And so, in the present case Mr Baldry submits that the position is, if anything, clearer than that considered by the Court in *BCL* since (1) the consistent approach of the Revenue has been to insist that the appropriate course is for these type of proceedings to be brought before the statutory tribunal under the Taxes Management Act 1970; and (2) in the *Autologic* proceedings themselves that view was approved by the High Court (Park J) on the basis of a consistent line of authorities to that effect dating from 10 years previously *(Re Claimants under Loss Relief Group Litigation Order* [2004] STC 594 at paragraph 32).

386. Indeed, he submits that the only confusion as to the correct procedure for bringing these claims has arisen by the creative attempts of BTPS and others to circumvent the fundamental point that the statutory regime provides the exclusive remedy for the claims here in issue of which these particular taxpayers are out of time to avail themselves. BTPS has also failed, he says, to offer any explanation as to why the alleged state of confusion as to the correct procedure for bringing claims as a result of the *Autologic* litigation could possibly be responsible for its failure (apart from on one occasion) to make claims for tax years in respect of which the limitation period in section 43 TMA 1970 had already expired by the time of Park J's judgment in *Autologic* in March 2004.

387. Mr McDonnell (having taken responsibility for the case following the departure of his leader to take up his post as the UK Judge in the ECJ) submits that for a claimant in the position of BTPS, at the times these claims were made, it appeared that claims in the High Court were both an available route and the more appropriate mechanism for these claims. Whether the mechanism was more appropriate may be a matter for debate, although it clearly held some advantages for the test claimants. It is, nonetheless, pertinent to note the reference of Peter Gibson LJ in the Court of Appeal in *Autologic* at [29] to the "obvious convenience" in all parts of the claims being subject to the GLO.

388. Mr McDonnell draws attention to the fact that BTPS issued its FIDs claims in the High Court and only sought afterwards to make statutory claims for FIDs. He suggests, that the May 2004 judgment of the Court of Appeal in *Autologic* seemed to confirm that that had been the correct approach. BTPS adopted a similar approach when it later made its *Manninen* claims, following the September 2004 decision of the ECJ in *Manninen*: only High Court claims were made at first. It was not until July 2005, however, the House of Lords in *Autologic* reversed the Court of Appeal (and even then only by a 3:2 majority).

389. And so he concludes that in these circumstances, the position can hardly be said to have been "sufficiently precise, clear and foreseeable", at least prior to July 2005. Although HMRC have argued that it would have been a simple matter for BTPS to make statutory claims at an early point, that is not an answer where it was the High Court claims which both seemed more appropriate and apparently had the **longer** limitation period. HMRC's argument would imply, he says, that a prospective claimant with a claim based in EU law should commence proceedings using every available mechanism in national law, in parallel. That, according to Mr McDonnell is contrary to the approach indicated by the ECJ in *Impact.*

390. As to *Impact*, we have already explained why we do not consider it to be of assistance. In addition to what we have already said, *Impact* was not concerned with a right which could be asserted in different ways in two different forums: rather, the domestic law required what were in essence the same claim for different periods to be dealt with in different forums. In the present case, however, it is the result of the application of a limitation period (under section 43) which precludes BTPS from asserting its claim in a forum which it now prefers. This, it seems to us, has nothing to do with the principle of effectiveness.

391. As to the submission that the position was not sufficiently precise, clear and foreseeable, we see the uncertainty as falling within the ambit of lack of clarity which it is the function of the judicial process to resolve, an uncertainty which does not involve any breach of the principle of effectiveness.

392. However, if that is wrong, we go back to our earlier point that the uncertainty does not result in the disapplication of an otherwise applicable limitation period. The uncertainty relates to the correct forum: if the principle of effectiveness is engaged it is to remedy that uncertainty so that the commencement of proceedings in the wrong forum is not to prejudice the claimant. If the taxpayer has a remedy at all, the solution is to be allow him to continue with the claim, for the remedy which he has in fact sought, in the forum which is seised of the claim, applying its limitation period (unless it can easily be made within a current time limit in the correct forum). The correct remedy is not to allow the taxpayer to rely on the longer limitation period to commence claims for different relief in the other forum.

393. We would add this to emphasise that last point: In a sense, the whole debate about time limits misses the point. The reason why BTPS wants to assert its Community law rights in the tribunal is because it perceives (no doubt correctly) the moulding and disapplication of the legislation in the manner we have indicated earlier in this decision as providing it with a more certain and valuable remedy than a claim in the High Court for restitution and/or damages. The uncertainty in the law, if there was one, was not so much about the time limit as about the remedy. This emphasises, in our view, that the uncertainty issue in the present case is no different in principle from any other legal uncertainty about the law. We do not consider that the principle of effectiveness is infringed.

394. For completeness, we must add that we do not regard the procedural advantages which BTPS would wish to rely on in the High Court (in particular the power to award costs and the power to make a GLO) as resulting in an infringement of the principle of effectiveness. Community law gives a remedy for breach of a Community obligation. Where a statutory appeal is made in time (for instance in relation to BTPS's appeal for 1997/1998) and effect is given to the directly enforceable rights by the moulding and disapplication of the legislation which we have decided should take effect, BTPS's rights are fully recognised. Community law does not require the imposition of a "costs follow the event" regime or the provision of a GLO procedure.

395. There is, however, the second limb of BTPS's case with which we must now deal, namely its allegedly special position as trustee of a pension scheme. The argument comes down to this. There was such uncertainty in the law (resolved gradually through development of the case law in Case C-35/98 *Verkooijen* [2000] ECR I-4071, *Hoechst*, *Manninen* and Case C-315/02 *Lenz*), an uncertainty recognised in *FII ECJ*, that a properly advised trustee would not have commenced the *Manninen* claims until after the 7 September 2004 judgment in *Manninen* itself. Until then, it was excessively difficult for a trustee to bring a claim of this type. Alternatively, as a fall-back, BTPS submits that time should not begin to run until the decision in *Verkooijen* on 6 June 2000.

396. We reject this submission. We do not consider that the principle of effectiveness can be applied in different ways to different taxpayers in the way in which BTPS contends. It would lead to considerable, and increased, uncertainty in relation an area where national courts already have enough problems in applying the guidance for the ECJ about what does and does not amount to an infringement of the principle of effectiveness. It would result in an unjustifiable distinction being drawn between different types of taxpayer. In domestic law, trustees are subject to limitation periods in the same way as individuals and corporations. We can see no justification, but every objection, to affording a different treatment in relation to Community rights.

397. We therefore reject Grounds 2 and 3 of the appeal.

Ground 4
Section 43 is to be disapplied by reason of the principle of equivalence for all years.

398. This ground of appeal is based on an Extra-Statutory Concession ESC B41 published by HMRC on 10 February 1992. It reads as follows:

"**Claims to repayment of tax**
Under the Taxes Management Act [TMA 1970], unless a longer or shorter period is prescribed, no statutory claim for relief is allowed unless it is made within six years from the end of the tax year to which it relates.

However, repayments of tax will be made in respect of claims made outside the statutory time limit where an overpayment of tax has arisen because of an error by the Revenue or another Government department, and where there is no dispute or doubt as to the facts."

399. There is a short answer to this Ground of Appeal. It is that the First-tier Tribunal has no jurisdiction, for reasons which we will explain in a moment, to give effect to public law claims, and in particular Extra-Statutory Concessions. If that is right, then a refusal by HMRC to give the benefit of ESC B41 to BTPS could only be

challenged by a judicial review application in the Administrative Court (an application which could be transferred to the Upper Tribunal but not to the First-tier Tribunal). In that respect, the position of BTPS is no different from that of a taxpayer in a wholly domestic situation who considers that he is entitled to the benefit of ESC B41 and who must also bring his claim in the Administrative Court. There is no breach of the principle of equivalence in requiring BTPS to bring a public law challenge in the Administrative Court.

400. If the matter were to become subject to a judicial review application, the Administrative Court or the Upper Tribunal will then have to address the arguments put by each side as to whether BTPS is entitled to the benefit of ESC B41. We doubt very much that it is so entitled. We consider that there is considerable force (and are inclined to agree) with Mr Baldry's submission that ESC B41 is essentially concerned with administrative errors and has no application to disputes concerning the proper meaning of the legislation. As he say, if it were otherwise, the time-limit set out in section would become redundant whenever the interpretation of the law adopted by HMRC turned out to be incorrect. Mr Baldry also submits that the provisions of ESC B41 have not in fact been applied by HMRC in such circumstances (*ie* an incorrect interpretation of the law by HMRC subsequently held to be incorrect). There was, in any case, no evidence before the Tribunal to support BTPS's assertions in relation to ESC B41. It is far too late for BTPS now to seek to rely on the point in these appeals.

401. Our reasons for saying that the Tribunal has no jurisdiction to give effect to the Extra-Statutory Concessions stems from the recent decision of the Upper Tribunal in *HMRC v Hok Ltd* [2012] UKUT 363 (TCC) ("***Hok***") a decision of Warren J and Judge Bishopp. Mr Vajda has relied on the decision of Sales J in *Oxfam v. HMRC* [2009] EWHC 3078 (Ch), [2010] STC 686 ("***Oxfam***"), paragraphs 61 to 79 to demonstrate that the Tribunal does have jurisdiction. However, that decision turned on a construction of section 83(1)(c) of the Value Added Tax Act 1994 which Sales J held gave jurisdiction to the VAT Tribunal to deal with legitimate expectation in the context of an appeal as to the amount of input tax. It lends no support at all to the view that the Tribunal has a general jurisdiction to deal with public law matters, whether in the context of direct tax or indirect tax, in particular to require, in the exercise of some sort of supervisory jurisdiction, HMRC to give effect to a concession. The suggestion that there is a jurisdiction in the context of direct tax is refuted by the decision in *Hok*.

402. Accordingly, Ground 4 is also rejected.

Ground 5: **the 1996-97 FIDs claim in the High Court was or is to be treated as a "claim" within the meaning of section 42 and as such was a claim made within the time-limit laid down by section 43**.

403. The Tribunal rejected this argument quite shortly at paragraph 219 of the Decision:

> "The High Court FIDs claim for tax credits is in terms a claim for damages. It is not a claim for tax credits. We cannot construe it, either on its terms (Mr McDonnell did not rely on any specific terms to make good his submission that the High Court claim was a claim for tax credits), or by reference to its function, as such. The High Court claim arises on the basis that tax credits have not been conferred (and thus is inconsistent with its being a claim for tax credits). Thus the High Court claim cannot be treated as a claim made within time for the Category B FIDs claim."

404. Mr McDonnell says this is all wrong. His argument is this.

405. BTPS issued a claim in the High Court on 31 January 2003 for payment of tax credits on FIDs it received including, *inter alia*, a claim for the year 1996-97. That claim for the year 1996-97 was on any view in time in the High Court, and it was also an in time claim for the purposes of section 43 TMA 1970. In this context, section 43 as it applied to 1996-97 required BTPS to make its claim "within five years from the 31st January next following the year of assessment to which it relates" that is to say by 31 January 2003.

406. He contends that the High Court claim was itself a "claim" within the meaning of section 42 alternatively that it is to be treated as such a claim in the circumstances of this case. The argument is advanced on both domestic law and EU law grounds.

407. As a matter of domestic law, paragraph 2(3) schedule 1A TMA 1970 allows the Board (that is to say, the Commissioners of Inland Revenue) to determine the form for making a claim. There was no such form at the time when the High Court claim was made. Mr McDonnell submits that, in the absence of a specified form for a claim pursuant to 42, a claim can be made in any form: see *Gallic Leasing Limited v Coburn* [1991] STC 699. As such a formal claim made by way of a claim form issued in the High Court which sets out the amounts of tax credits claimed and the reasons why they are claimed, must, he says, be a "claim" on any view.

408. As a matter of EU law, having regard to the circumstances set out above, specifically in relation to the FIDs claim for 1996-97, it would be contrary to the principles of legal certainty and effectiveness for the High Court claim not to be treated as a "claim" for the purposes of section 42 given that it was made in time (that is to say, within the section 43 time limit) and in accordance with what appeared to be the only available, or at least the most appropriate, procedure at the time in question.

409. In particular, applying the principles in *Impact* and *Commission v Ireland* which we have considered at some length already, Mr McDonnell submits that it would be contrary to the principles of legal certainty and effectiveness for the statutory claim for 1996-97 to be barred on limitation grounds, when a claim for exactly the same matters was made within time in the forum which reasonably appeared at the time to be the correct forum for making such claims: to treat the statutory claim as time-barred on the basis that the High Court claim was not a statutory claim would be excessively formal, would be based on a time limit which was not apparent to claimants at the time the claim was made and was based at least in part on subsequent judge-made law, and in all the circumstances would render the exercise of the claimants' EU law rights excessively difficult.

410. In the context of Ground 5, the correct approach according to BTPS is to treat the High Court claim as a "claim" for the purposes of section 42 and the date of that claim as being the date it was issued in the High Court.

411. Mr Baldry submits to the contrary. It is denied that the High Court claim issued by BTPS on 31 January 2003 was a statutory claim for tax credits in relation to FIDs.

412. First, it is pointed out that the High Court Claim was a common law claim for compensation for being *denied* credit. It could not on any view have been construed as a statutory claim for tax credits. Mr Baldry submits that the Tribunal got it absolutely right.

413. Secondly, the High Court Claim did not comply with the prescribed statutory form for a claim under section 231(1) ICTA and section 42(11) since (i) it was not made to an officer of the Board: this is said to be contrary to paragraph 2(1) schedule 1A TMA 1970 which provides that, subject to any provision requiring a claim to be

made to the Board, every claim shall be made to an officer of the Board and (ii) the bringing of a High Court common law action was not the prescribed form for claims under section 42. In this respect, by 2003 any claim for tax credits would have either had to be made *via* the trustees' tax return or by Form R63N.

414. Thirdly, the High Court Claim was not in any event served on the Revenue before 15 May 2003 at the earliest, which was after the expiry of the time-limit in section 43 (a fact which Mr Baldry says is evident from the fact that the Revenue did not file any Acknowledgement of Service until 12 June 2003).

415. In our view, BTPS cannot rely on the High Court claim form as a claim under section 42 brought within the time limit provided by section 43. As matter of domestic law, we agree with the Tribunal and with Mr Baldry that the claim as formulated in the claim form cannot be interpreted as a claim for a tax credit. The relief sought is for declarations concerning non-compliance with the Treaty and for compensation or damages for losses and restitution of amounts by which HMRC had been unjustly enriched. We do not consider that these can, on any interpretation, been seen as claims for tax credits.

416. But even if the claim form in the High Court proceedings was, contrary to our view, capable of amounting to a claim, it would not be a claim until, at the earliest, brought to the attention of the Board or an officer of the Board. In the absence of any evidence that the claim form was served on 31 January 2003, as to which there was none before the Tribunal or before us, we are not willing to assume that it was in fact served on that date, the very day of its issue. If it was served or otherwise brought to the attention of the Board or an officer of the Board after that date, it was out of time.

417. Accordingly, we reject Ground 5.

XII. REFERENCE TO THE ECJ

418. The question arises whether there is any issue of Community law arising out of our conclusions which we should refer to the ECJ for a preliminary ruling.

419. All three issues – the FIDs claims, the *Manninen* claims and the limitation issue – raise points of Community law. Some of the points are not easy to resolve. This does not mean that it is appropriate for us to make a reference. We should do so only if there is a question of Community (now EU) law which we cannot answer without the guidance of the ECJ (and even then, at this level, we do not have to do so).

420. We take the three issues in turn, starting with limitation. In the field of time-limits, the ECJ has given a great deal of guidance over recent years. The application of that guidance in particular cases is not always straightforward, particularly as the Court regularly reminds the national courts that the detailed implementation of EU law is generally a matter for Member States. We have reached, however, a clear view about how the present appeal should be decided in the light of the requirements of Community law. We do not consider that we need further guidance from the ECJ to reach our decision and think it unlikely that the ECJ would be able to provide useful further guidance.

421. Turning to the *Manninen* claims, if we are right on limitation, there is no need for a reference in relation to these claims since they are all time-barred. But even if they were not time-barred, we do not consider that we would need further guidance from the ECJ. There is no doubt following *Manninen* and *FII ECJ* that the UK FIDs regime fails to comply with the UK's treaty obligations and fails to reflect the requirements of Community law. We consider that the conclusions which we have

reached follow inevitably from the existing jurisprudence of the ECJ for the reason which we have given at length in this decision. We do not, therefore, consider that it would be necessary or appropriate to make a reference even if the *Manninen* claims were not time-barred. And that is so even though the point may not, perhaps, properly be regarded as *acte clair*: we see BTPS's case as being sufficiently strong to deter us, at this level, from making a reference.

422. So far as the FIDs claims are concerned, they are all time-barred save for the year 1997-98 in relation to which the claim was made in time. The issue of a reference is therefore a live one. However, in relation to all of the FIDs claims (assuming they were in time), we repeat what we have said in relation to the *Manninen* claims and do not consider that it is necessary or appropriate to make a reference.

423. A further reason for refusing a reference of any sort at this stage is this. A higher court, if this matter goes to the Court of Appeal and perhaps to the Supreme Court, might take a different view about the need for a reference in relation to limitation and the FIDs claims; and it might consider that, if it were not for the time-bar in relation to the *Manninen* claims, a reference would be needed in relation to those claims as well. We think that the whole question of what, if any, reference should be made is best left to a higher court (in the event of an appeal from our decision) in the light of its views on the three major issues with which this decision is concerned.

XIII. DISPOSITION

424. BTPS's appeal on the limitation issue is dismissed. HMRC's appeals in relation to the FIDs claims and the *Manninen* claims are dismissed.

Mr Justice Warren	**Timothy Herrington**
CHAMBER PRESIDENT	**UPPER TRIBUNAL JUDGE**

RELEASE DATE: 28 February 2013

ANNEX A

Background to BTPS and Hermes

The BT Pension Scheme (formerly known as the British Telecom Pension Scheme)
5 was formed in the 1980s and is the largest defined benefit pension fund in the United Kingdom. BTPS was at all material times an exempt approved scheme.

BTPS was formed as a result of the separation of the Post Office Staff Superannuation Fund ("**POSSF**") into the Post Office Staff Superannuation Scheme ("**POSSS**") and the British Telecommunications Staff Superannuation Scheme ("**BTSSS**") on 1 April
10 1983. BTSSS later merged with British Telecommunications Plc New Pension Scheme ("**BTNPS**") to form BTPS with effect from 1 January 1993. Accordingly, in respect of periods before 1 January 1993, the claims are maintained by the trustees of BTPS on behalf of the two funds, BTSSS and BTNPS, which now constitute BTPS.

Until 2006, the trustees of the BTPS were a group of nine individuals. Since 14
15 December 2006, BTPS has had a corporate trustee, BT Pension Scheme Trustees Limited ("**BTPSTL**") and the individual trustees became directors of BTPSTL.

The investment fund management team of POSSS and BTPS, originally known as PosTel Investment Management Limited ("**PosTel**"), was formed in 1982 from the existing investment fund management team of POSSF. From that time until 1995,
20 PosTel was jointly owned by the Trustees of POSSS and the Trustees of BTPS.

On 31 March 1995 the Trustees of the BT Pension Scheme acquired the 50% holding in PosTel owned by the POSSS, and PosTel's name was changed to Hermes Fund Managers Limited ("**HFML**"). HFML is now 100% owned by BTPS.

HFML is the parent company of a number of companies falling within the Hermes
25 group, some of which are separately authorised and regulated by the Financial Services Authority.

Hermes Investment Management Ltd ("**HIML**") (known from February 1990 to March 1995 as PosTel Financial Asset Management Limited) is a wholly owned subsidiary of HFML. HIML is an institutional fund manager which invests funds on
30 behalf of approximately 209 clients including pension funds, insurance companies, government entities, financial institutions, charities and endowments. HIML is the principal manager of the BTPS and undertakes the day to day management of the pension fund's assets.

Hermes Administration Services Limited ("**HASL**") is a wholly owned subsidiary of
35 HFML. HASL provides administration services to BTPS and other clients.

The investments of BTPS are registered in the name of Britel Fund Trustees Limited and Britel Fund Nominees Limited (or in certain cases, another nominee such as Britel (MAM) Nominees Limited). These companies hold all such assets purely in their capacity as nominees on behalf of the Trustees of BTPS. For all tax purposes,
40 the Trustees of BTPS are the relevant taxable entity and BTPS is the beneficial owner of the relevant assets.

Investments of BTPS

At all material times, approximately 70% to 75% of the investments of BTPS (by market value) were in the form of equities.

Of BTPS' holdings of equities, some were investments in companies resident in the United Kingdom ("**United Kingdom equities**"), and some were investments in companies resident in the EU and elsewhere ("**overseas equities**"). The proportion of overseas equities has varied over time. Between March 1990 and 31 December 1992, approximately 81% of the holdings (by market value) were United Kingdom equities and 19% were overseas equities. On 31 December 1993, 31 December 1994, 31 December 1995 and 31 December 1996, in each case approximately 73% of the holdings were United Kingdom equities and 27% were overseas equities. On 31 December 1997 and in subsequent years, approximately 67% of the holdings, or less, were United Kingdom equities, and 33% or more were overseas equities.

BTPS invests a very small proportion (approximately 3%) of its equities portfolio in selected smaller companies, in which it may take up to a 10% interest. These investments in small companies are not included in these claims.

The vast majority (at least 97%) of BTPS' equities portfolio was invested in large publicly quoted companies in the United Kingdom and overseas. These are the investments which are the subject of these claims. In each case, BTPS would typically hold less than 2% of the company's share capital, and always less than 5%. BTPS' relationship with the investee companies was purely as shareholder.

High Court Claims

FIDs claims

On 31 January 2003, the Trustees of BTPS (together with Britel Nominees Limited and Britel (MAM) Nominees Limited) brought a claim in the High Court of Justice against the Commissioners of Inland Revenue for payable tax credits in respect of Foreign Income Dividends (Claim Number HC03C00426). This claim constitutes what is referred to in this decision as the FIDs claims.

Manninen claims

On 1 April 2005 the Trustees of BTPS (together with Britel Nominees Limited and Britel (MAM) Nominees Limited) brought a claim in the High Court of Justice against the Commissioners of Inland Revenue for tax credits in respect of overseas dividends received directly (Claim Number HC05C00770). This claim constitutes what is referred to in this decision as the *Manninen* claims.

Group Litigation Order

The FIDs Claims brought by BTPS was one of several claims brought around this time by trustees of various pension schemes.

On 13 May 2004 the solicitors acting for BTPS, McGrigors, issued an application in the High Court for an order that the Court grant a group litigation order under Parts 19 (rules 19.10 and 19.11) of the Civil Procedure Rules.

The hearing of the application took place on 7 July 2004 before Chief Master Winegarten and an agreed Order by Consent between BTPS and HMRC was sealed by the Court on 21 July 2004. It was held that BTPS would be appointed as Test

Claimant in the group litigation. The application was therefore brought in the name of 'The Trustees of the BT Pension Scheme and the Claimants listed in Schedule 1 to this Order'. The Order provided that claims in connection with the FIDs regime would constitute the 'FIDs Group Litigation' and provided that a group register of claims should be set up and maintained by McGrigors as lead solicitors.

A Case Management Conference took place on 4 October 2005. At this conference draft directions were agreed. In addition, Park J ruled on whether certain questions of Community law should be referred to the ECJ. He decided that the questions should not be referred to the ECJ at that stage.

A further Case Management Conference took place on 4 July 2007, where it was directed by Rimer J that the High Court claims of BTPS as the test claimant be stayed pending the outcome of the appeal to the Special Commissioners. The parties agreed that:-

> (1) the Special Commissioners should consider the FIDs claims and the *Manninen* claims (including those made outside the ordinary Taxes Management Act 1970 time limits); and
>
> (2) if any tax return claims are rejected for being out of time, then the relevant claimants will be able to revert to the High Court route.

Following the Case Management Conference on 4 July 2007 the High Court claims have been stayed and the tax return claims were pursued before the Special Commissioners, whose functions have now been transferred to the First-tier Tribunal.

Tax Credit Claims
FIDs claims

On 4 February 2003, Mr D W Burrowes of HASL, on behalf of BTPS, wrote to Mrs E Bowman of HM Inspector of Taxes, Glasgow Large Business Office, stating that BTPS had been advised that it had a case under EU law that section 246C of ICTA contravened EU law and in particular was contrary to the principle of free movement of capital enshrined in Article 56 of the EC Treaty; that Hermes were seeking, on behalf of BTPS, a payment of tax credits on all FIDs received on or after 1 July 1994; and that a claim had been filed in the High Court on 31 January 2003 for recovery of tax credits on FIDs received in respect of the years of assessment 1994/5, 1995/6, 1996/7 and 1997/8.

The High Court claim filed on 31 January 2003 was in the following amounts:

(a) 1994-95 £2,357,508.65;

(b) 1995-96 £3,481,698.50;

(c) 1996-97 £5,097,286.97; and

(d) 1997-98 £1,651,508.66

On 28 October 2003, Mr D W Burrowes wrote to Mr Pigott of HM Inspector of Taxes, Glasgow LBD (CT) on behalf of BTPS attaching a list of all the FIDs incorporated in the claim and providing lower claim numbers for 1996/1997 representing a claim for payable tax credits relating to the FIDs received by BTPS in the following amounts:

(a) 1994-95 £2,357,508.65;

(b) 1995-96 £3,481,698.50

(c) 1996-97 £4,514,291.22; and

(d) 1997-98 £1,651,508.66.

5 On 23 January 2004, Mr D W Burrowes wrote to the Inland Revenue, Glasgow Large Business Office enclosing a further copy of the schedule representing a claim for payable tax credits relating to the FIDs received by BTPS in the 1997/1998 period and listing in detail the tax credits being claimed.

On 28 January 2005, BTPS wrote to Mr N Gay, HM Inspector of Taxes, Glasgow 10 Large Business Office, enlarging on the claim for payable tax credits in respect of FIDs received in the 1994/1995 and 1995/1996 periods of assessment.

Manninen claims

On 17 October 2005, BTPS wrote to HMRC, Audit & Pension Schemes Services notifying HMRC of its claim under section 231(3) of ICTA for a payment of excess 15 tax credits totalling £90,617,473.06 in respect of non-United Kingdom dividends received in the 1990/1991 to 1995/1996 periods of assessment. The true amount of the claim was £90,917,015.88, after the correction of an error in calculation. On the same date, BTPS wrote separately to HMRC, Audit & Pension Schemes Services notifying HMRC of its claim under section 231(3) of ICTA for payment of excess tax 20 credits totalling £32,952,214.67 in respect of non-United Kingdom dividends received in the 1996/1997 and 1997/1998 periods.

ANNEX B

The Relevant Provisions Of The UK Tax Code

5 **Section 231 ICTA**

231. Tax credits for certain recipients of qualifying distributions

(1) Subject to sections [231AA], [231AB] … [, 247 and [469(2A)]], [section 171 (2B) of the Finance Act 1993 and section 219 (4B) of the Finance Act 1994,] where [,in any year of assessment for which income tax is charged] a company resident in
10 the United Kingdom makes a qualifying distribution and the person receiving the distribution is another company or a person resident in the United Kingdom, not being a company, the recipient of the distribution shall be entitled to a tax credit equal to such proportion of the amount or value of the distribution as corresponds to [the tax credit fraction in force when] the distribution is made.

15 [(1A) The tax credit is one-ninth.]

[(2) [Subject to sections 231and Section 241 (5)], a company resident in the United Kingdom which is entitled to a tax credit in respect of a distribution may claim to have the amount of the credit paid to it if –

(a) the company is wholly exempt from corporation tax or is only not exempt
20 in respect of trading income; or

(b) the distribution is one in relation to which express exemption is given (otherwise than by section 208), whether specifically or by virtue of a more general exemption from tax, under any provision of the Tax Acts.].

(3) [Subject to section (3AA) below,] a person not being a company resident in the
25 United Kingdom, who is entitled to a tax credit in respect of a distribution may claim to have the credit set against the income tax chargeable to his income under section 3 or on his total income for the year of assessment in which the distribution is made [and [subject to subsections (3A) to (3D)below] where the credit exceeds that income tax, to have the excess paid to him.]

30 [(3A) Subject to subsection (3B) below, where ….., in any accounting period of a company at the end of which it is a close investment-holding company-

(a) arrangements relating to the distribution of the profits of the company exist or have existed the main purpose of which or one of the main purposes of which is to enable payments, or payments of a greater
35 amount, to be made to any one or more individuals under subsection (3) above in respect of such an excess as is mentioned in that subsection, and

(b) by virtue of those arrangements, any eligible person –

(i) receives a qualifying distribution consisting of a payment made by the company on the redemption, repayment or purchase of its own shares, or

(ii) receives any other qualifying distribution in respect of shares in or securities of the company, where the amount of value of the distribution is greater than might in all the circumstances have been expected but for the arrangements,

The entitlement of the eligible person to have paid to him under subsection (3) above all or part of a tax credit in respect of any distribution made by the company in the period shall be restricted to such extent as [is] just and reasonable.

[(3B) Subsection (3A) does not apply in relation to a tax credit in respect of a dividend paid by a company in any accounting period in respect of its ordinary share capital if-

(a) throughout the period, the company's ordinary share capital consisted of only one class of shares, and

(b) no person waived his entitlement to any dividend which would have become payable by the company in the period or failed to receive any dividend which had become due and payable to him by the company in the period.]

[(3C) In subsection (3A) above –

"arrangements" means arrangements of any kind whether in writing or not,

"close investment-holding company" has the meaning given by section 13A, and

"eligible person", in relation to a qualifying distribution, means an individual resident in the United Kingdome who would (apart from subsection (3A) above) be entitled to have paid to him under subsection (3) above all or part of a tax credit in respect of the distribution.]

[[3D) In determining under subsection (3) above whether a person is entitled to have any excess of tax credit paid to him in a case where subsection (3A) above applies, tax credits shall be set against income tax in the order that results in the greatest payment in respect of the excess.]

(4) Where a distribution mentioned in subsection (1) above is, or falls to be treated as, or under any provision of the Tax Acts is deemed to be, the income of a person other than the recipient, that person shall be treated for the purposes of this section as receiving the distribution (and accordingly the question whether he is entitled to a tax credit in respect of it shall be determined by reference to where he, and not the actual recipient, is resident);..

(5) …"

Section 246A, Section 246C ICTA

[246A Election by company paying dividend

(1) Where a company [resident in the United Kingdom] pays a dividend, the dividend shall be treated as a foreign income dividend for the purposes of this Chapter if the company elects for it to be so treated in accordance with this section and section 246B.

(2) An election may not be made under this section as regards a dividend unless the dividend is paid, or to be paid, in cash.

[(2A) An election under this section cannot be made as regards a dividend which is paid, or to be paid, to a person by virtue of his holding a share in respect of which there are arrangements for the holder to choose whether, or in what form, dividends are to be paid; and the arrangements may be for the holder to choose to be paid in dividend by a company other than the one which issued the share.

(4) Where at a given time –

(a) a company pays one dividend in respect of each of two or more shares of the same class, and

(b) payment is on the same terms as respects all the shares involved,

An election may not be made under this section as regards any of the dividends unless an election is made as regards each of the dividends.

(5) Where at a given time –

(a) a company pays two or more dividends in respect of each of two or more shares of the same class, and

(b) payment is on the same terms as respects all the shares involved,

An election may not be made under this section as regards any one of the dividends in respect of a given share unless an election is also made as regards the corresponding dividend in respect of each of the other shares involved.

(6) Subject to subsection (7) below, a company which has more than one class of share capital may not make an election under this section as regards any dividend.

(7) In a case where –

(a) a company has more than one class of share capital,

(b) at a given time the company pays a dividend in respect of each share of each such class, and

(c) all of those dividends are paid on the same terms, the company may elect that each of those dividends is to be treated as a foreign income dividend.

(8) For the purposes of subsection (7) above a dividend is paid on the same terms as another dividend if the relevant proportion in the case of each dividend is the same; and the relevant proportion, in relation to a dividend, is the proportion which the amount of the dividend bears to the nominal value of the share in respect of which the dividend is paid.

(9) For the purposes of subsections (6) and (7) above fixed-rate preference share shall not be treated as constituting a class of share capital; and "fixed-rate preference shares" shall be construed in accordance with [paragraph 13(6) of Schedule 28B].

(10) Where an election is made under this section as regards a dividend in respect of which an election is in force under section 247(1) –

(a) the election under this section shall effect as if it were also a notice to the collector under section 247(3) stating that the paying company does not wish the election under section 247(1) to have effect in relation to the dividend as regards which the election under this section is made;

(b) if the election under this section is revoked, the revocation of the notice deemed by paragraph (a) above;

(c) the notice deemed by paragraph (a) above may not be revoked otherwise than as mentioned in paragraph (b) above;

(d) if the notice deemed by paragraph (a) above is revoked it shall be treated as never having been made.]

246C No tax credit for recipient

Section 231(1) shall not apply where the distribution there mentioned is a foreign income dividend.