Supreme Court Corrects Mistake in Limitation

Test Claimants in Franked Investment Income Group Litigations and others v Commissioners for HMRC [2020] UKSC 47

This tax decision of the Supreme Court will be of interest not just to tax specialists but to a broad range of civil practitioners.

The decision changes the law on the principles governing when a claimant has discovered or could with reasonable diligence have discovered a mistake of law in an action for relief from the consequences of such a mistake when considering the postponement of limitation pursuant to s.32(1)(c) of the Limitation Act 1980.

With respect to mistakes of law caused by changes in the law produced by judicial decisions the law laid down by a majority decision of the House of Lords in *Deutsche Morgan Grenfell Group Plc v Her Majesty's Commissioners of Inland Revenue and Another* [2007] 1 AC 558 ("*Deutsche Morgan Grenfell*") had been that the mistake was only reasonably discoverable when the truth was disclosed by the judgment overturning the previous law; *Deutsche Morgan Grenfell* per Lord Hoffman [31]; Lord Hope [71]; Lord Walker [144].

The Supreme Court in *Test Claimants in Franked Investment Income Group Litigations and others v Commissioners for HMRC* [2020] UKSC 47 ("*Test Claimants")* has invoked the 1966 Practice Statement and in a four to three majority judgment lucidly reasoned by Lord Reed and Lord Hodge (Lord Lloyd-Jones and Lord Hamblen agreeing) overruled *Deutsche Morgan Grenfell.*

The test of discoverability laid down in *Test Claimants* (drawing on the dissenting judgment of Lord Brown in *Deutsche Morgan Grenfell*) is now:

> "that a mistake of law is discoverable when the claimant knows, or could with reasonable diligence know, that he made such a mistake "with sufficient confidence to justify embarking on the preliminaries to the issue of a writ, such as submitting a claim to the proposed defendant, taking advice and collecting evidence"; or, as Lord Brown put it in *Deutsche Morgan Grenfell*, he discovers or could with reasonable diligence discover his mistake in the sense of recognising that a worthwhile claim arises." [209(1)]

The standard of reasonable diligence is:

> "how a person carrying on a business of the relevant kind would act, on the assumption that he desired to know whether or not he had made a mistake, if he had adequate but not unlimited staff and resources and was motivated by a reasonable but not excessive sense of urgency. The question is not whether the claimant *should* have discovered the mistake sooner, but whether he *could* with reasonable diligence have done so. The burden of proof is on the claimant. He must establish on the balance of probabilities that he *could not* have discovered the mistake without exceptional measures which he could not reasonably have been expected to take." [209(2)]

The application of the principles will turn on the facts. Where the mistake is due to ignorance of the law, it will normally

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have been discoverable immediately by seeking legal advice. [210] Where the mistake is due to a judicial decision changing understanding of the law "the question will be whether the claim was brought within the prescribed period beginning on the date when it was discoverable by the exercise of reasonable diligence that the basis of the payment was legally questionable, so as to give rise to a worthwhile claim to restitution." [210]

The requisite evidence will likely require focus "upon developments in legal understanding within the relevant category of claimants and their advisers". [211] The focus is objective and is on the claimant as part of a class and "does not depend upon the characteristics of the particular claimant: whether, for example, it was inclined to await further developments, and to allow other taxpayers to make the running." [255] If the claimant is a multi-national group based in the UK, for example, the test will be whether "a well advised multi-national group based in the UK would have had good grounds for supposing that it had a valid claim" [255]. It remains to be seen what standard of hypothetical legal advice is contemplated for individuals or SMEs or other classes and how classes of claimants are characterised. The relevant evidence "may well include expert evidence concerning the state of understanding of the law within the relevant categories of professional advisers during the relevant period." [211]

In *Kleinwort v Benson* [1999] 2 AC 349 the House of Lords held that money paid under a mistake of law was recoverable in restitution and that such mistake was within the scope of section 32(1) of the Limitation Act. The majority in *Test Claimants* has affirmed that aspect of the ruling in *Kleinwort v Benson* holding that although there was undeniable force in the argument that section 32(1)(c) should be construed as being confined to mistakes of fact they favoured "giving the language of section 32(1)(c) its ordinary meaning, so that it is applicable also to actions for relief from the consequences of a mistake of law." [243]

A powerful dissenting judgment in *Test Claimants* by Lord Briggs and Lord Sales (with Lord Carnwath agreeing) expressed the view that section 32(1)(c) of the Limitation Act 1980 did not and should not apply to payments made on the basis of a mistake of law and that *Kleinwort v Benson* should be overruled in respect of its interpretation of that provision. The minority judgment expressed "serious reservations about whether the test proposed by the majority…will prove to be workable". [259] Putting flesh on the bones of those concerns the dissenters observed that:

> "The test of discoverability proposed by Lord Brown is itself very uncertain, in a way that the test for discoverability of whether there has been a mistake as a matter of fact is not. The identification of a point in time, earlier than when the relevant claim was actually launched, when such a claim became worth pursuing requires a deeply speculative process of hypothetical fact-finding…In any given case it may be very difficult to say whether Lord Brown's threshold of discoverability has been crossed or not. The application of his test will often require a wide-ranging investigation at trial of something as inherently vague and intangible as the state of professional opinion as it changes year by year over what may be a very long period. It is unclear whether expert evidence would be of much assistance for such a speculative investigation into legal history. Moreover, the more one focuses on what was reasonable to expect of one claimant or particular type of claimant, as distinct from the general understanding of the legal profession, the greater the range of cases in which the court will have to produce speculative and uncertain judgments as to whether the relevant threshold of discoverability has been passed." [298 (iii)]

In some cases there may not be difficulty identifying, as far as the legal community at large is concerned, when the legal landscape changed. Where a new approach comes out of the blue it may be self-evident that the date of the unexpected judgment was the relevant date for discoverability purposes.

On the other hand, there will be cases of genuine difficulty in identifying the moment a particular class of claimants ought to have taken advice that the lone voice in the wilderness questioning the wisdom of the old law, whether in a

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dissenting judgment or law review article or legal blog, turned in to an irresistible clamour for the new law.

In cases where parties are out of pocket due to their reliance on law as understood at the time of payment and where the law ultimately changes following slow-burning disquiet about the state of the law, the enquiry as to when the "writing was on the wall" for the actual and/or hypothetical legal advisor for the class of claimant involved will be complicated. Issues may arise as to the extent to which legal practitioners do and should keep abreast of academic and/or practitioner literature on matters of prospective law reform and to the extent they do or should whether some sources are more telling than others. The question may arise whether legal advisors should be taking the temperature of legal developments in Scotland or the commonwealth or perhaps other jurisdictions depending upon the subject-matter in case the impetus for relevant law reform takes place beyond England.

A whole new field of legal archaeology appears to have been formed to address discoverability where postponement of limitation periods pursuant to s.32(1(c) of the Limitation Act 1980 is in issue in respect of restitutionary claims for mistake of law. The contours of this new area have been sketched by the majority in *Test Claimants* but will require to be more fully mapped out. Time will tell whether such a development was or was not a mistake.

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