

VAT focus

Littlewoods: compound interest claims

Littlewoods Retail Ltd and others v HMRC (Case C-591/10) is the current lead case in relation to compound interest in the context of VAT. Given the high values at stake and the multiple cases proceeding on variants of the point, it was hoped the opinion of Advocate General Trstenjak would bring some welcome clarity to the complex legal issues involved.

Vos J in his preliminary judgment of May 2010 ([2010] EWHC 1071 (Ch)), rejected a right to compound interest under UK law as he determined that VATA 1994 ss 78 and 80 provided an exhaustive and exclusive statutory regime, but he referred four questions to the Court of Justice of the European Union (CJEU) regarding the application of European law principles:

- Question 1: Does the payment of simple interest as a remedy accord with EU law?
- Question 2: If not, does EU law require that the remedy should provide for payment of compound interest as the measure of the use value of the sums overpaid in the hands of the Member State and/or the loss of the use value of the money in the hands of the taxpayer?
- Question 3: If the answer to 1 and 2 is no, what must the remedy include?
- Question 4: If the answer to question 1 is no, does the EU law principle of effectiveness require a Member State to disapply national law restrictions (such as VATA 1994 ss 78 and 80) on any domestic claims to give effect to the EU law right established in answer to the first three questions, or can the principle of effectiveness be satisfied if the national court disapplies such restrictions only in respect of one of these domestic claims or remedies?

Principle of effectiveness

There are two aspects of Trstenjak's opinion that represent welcome clarification of EU law. First, Trstenjak candidly admits that it can be misleading to speak of the 'procedural autonomy' enjoyed by Member States in relation to claims for the reimbursement of tax collected contrary to EU law. As she points out, Member States have a duty to procedurally facilitate the enforcement of claims stemming from EU law in order to ensure its full effect. This, she rightly observed, is closely connected with the principle of effective judicial protection and the fundamental right to an effective remedy. National procedural autonomy is also constrained by the requirement to ensure that the national remedy is effective and equivalent.

Second, Trstenjak recognises that in cases of overpaid tax, EU law accords the taxpayer a right not only to reimbursement of the principal amount, but also to interest on that amount. In reaching this conclusion, Trstenjak openly favoured a line of cases beginning with *Metallgesellschaft Ltd v ICR and Others* (Joined Cases C-397/98 and 410/98) [2001] ECR I-1727 over an earlier line beginning with *Roquette Frères v Commission* (Case 26/74) [1976] ECR 677, which have sometimes been read as

SPEED READ: On 12 January 2012, Advocate General Trstenjak delivered her opinion in *Littlewoods* (Case C-591/10). The case concerns whether UK taxpayers can claim interest on a compound basis on VAT reclaimed from HMRC at a higher rate than the simple interest ordinarily payable under VATA 1994 s 78. The AG stated that although the principle of effectiveness is not breached by simple interest paid under s 78, s 78 may breach the principle of equivalence if there are more favourable rules governing the repayment of interest in 'similar domestic claims'. This is something which the High Court may have to examine, if the CJEU decision follows the reasoning of the AG and may be subject to a further CJEU reference.



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treating interest as entirely a matter for the national law.

The Advocate General further reasoned that the right to interest recognised in *Metallgesellschaft* applies not only where the tax is charged prematurely (as it had been in that case), but also where the tax should not have been charged at all. This is plainly logical and hopefully finally disposes of the contrary view, on which Vos J had rested his conclusions in the main action.

Trstenjak distils the principle from *Metallgesellschaft* and *FII* (Case C-446/04) as follows. She says that 'because of the unavailability of sums of money as a result of tax being levied (in breach of EU law), the taxpayer has suffered losses which are to be regarded as amounts retained by the Member State or paid to it in breach of EU law'. She concludes 'Member States ... must in principle ... pay interest in compensation for the unavailability of the sums paid'.

Trstenjak considered the UK had fulfilled its duty to provide an interest claim through VATA 1994 s 78, which would comply with the principle of effectiveness provided that the resulting interest award is not 'so low that it largely deprived the interest claim stemming from EU law of substance'.

This conclusion is entirely new and a creature of Trstenjak's own creation. It is also starkly at odds with the CJEU's prior jurisprudence. Contrast the principle stated by the CJEU at para 205 of *FII*

‘where a Member State has levied charges in breach of ... Community law, individuals are entitled to reimbursement not only of the tax unduly levied but also of the amounts paid to that State or retained by it which relate directly to that tax’; ‘that also includes losses constituted by the unavailability of sums of money’. The only way to rationalise this with Trstenjak’s proposition would be if a payment of interest which did not fully compensate the loss suffered by the taxpayer or reimburse the benefit retained by the Member State is to be taken as being so low as to deprive the interest claim of substance.

Here, Littlewoods had received some £268m in simple interest under s 78. This payment, Trstenjak says, ‘readily complies with the principle of effectiveness’ seemingly on the basis that it exceeded the principal tax sum by more than 25%. The amount of interest Littlewoods received was, perhaps, large in absolute terms but that does not of itself lead to the conclusion that the payment is either adequate compensation for the loss suffered by the taxpayer or reimbursement of the amount retained by the Member State as the CJEU required in *FII*.

This aspect of the opinion is open to a number of criticisms. First, it is the role of the CJEU to provide guidance on the interpretation of EU law and the principles that domestic courts must adhere to. The question of whether the actual amount of interest received by Littlewoods complies with the principle of effectiveness is a matter for the domestic court and is not within the CJEU’s competence. This is rightly so as the approach taken by Trstenjak belies confused economics.

The amount of interest received was large because the tax amount itself was large and it had remained outstanding for a long period of time. It is incorrect to look at the amount of interest as a percentage of the total tax repaid; interest compensates for the fact that the real value of an amount of money declines with the effluxion of time. What is required, as per the CJEU in *FII*, is to ask what was the loss suffered by the taxpayer or the benefit retained by the Member State? In proportionate terms, the simple interest payment represented only 20% of the total amount of the interest benefit Littlewoods said that the UK had enjoyed, calculated on a compound basis. Or put another way, the Member State has retained 80%

of the benefit of tax levied in breach of Community law, which we have been told by the CJEU it is obliged to reimburse. It is difficult to see how this does not largely deprive the right to interest of substance. The influence of current political and economic considerations is clear.

Principle of equivalence


The most significant aspect of the opinion is understanding the AG’s conclusion that ‘... rules governing the claim for payment of interest on VAT collected in breach of EU law may be no less favourable than the detailed rules governing similar interest claims stemming from a breach of domestic law’ (para 39).

The AG identifies potential categories of similar domestic interest claims to be used for comparison, for example, whether interest on VAT collected in breach of EU law should be compared with interest on unlawfully levied direct taxes. Unfortunately, she does not provide her own views on what the comparators should be but says that this should be the subject of a further detailed reference to the Court. Should the CJEU reiterate that position, a further reference seems inevitable. It is worth noting that when considering the principles set down, inter alia, in *San Giorgio* and *FII* the CJEU saw no need to delineate between indirect or direct taxes levied in breach of Community law. What mattered was the breach of Community law, not the nature of the tax. This point is now of utmost importance as if claims for interest on direct taxes are the correct comparator then the principle of equivalence will be breached (compound interest having been available in *Sempra Metals* [2007] UKHL 34).

Finally, where multiple causes of action are available to a claimant, such as a *Woolwich* claim or a mistake of law based claim, the AG confirms that it is for a taxable person to choose which to pursue, rather than for the courts to restrict the taxable person to a particular avenue and thus a particular remedy.

Where does this leave us?

There is a long way yet to go for Littlewoods in this case. In particular it remains to be seen how the CJEU will deal with the difficulties in rationalising Trstenjak’s opinion with its earlier case law. ■

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