OPINIONS
OF THE LORDS OF APPEAL
FOR JUDGMENT IN THE CAUSE

Marks and Spencer plc (Appellants) v Her Majesty's Commissioners of Customs and Excise (Respondents)

Appellate Committee

Lord Hoffmann
Lord Scott of Foscote
Lord Walker of Gestingthorpe

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Hearing dates:
13 and 14 JUNE 2005

ON
WEDNESDAY 4 FEBRUARY 2009
LORD HOFFMANN

My Lords,

1. I have had the advantage of reading in draft the speech of my noble and learned friend Lord Walker of Gestingthorpe. I am in agreement with his conclusion that the House can now dispose of the appeal in accordance with paragraph 23 of his opinion.

LORD SCOTT OF FOSCOTE

My Lords,

2. I have had the advantage of reading the opinion prepared by my noble and learned friend Lord Walker of Gestingthorpe dealing with the implications and consequences of the manner in which the Court of Justice of the European Communities dealt with the five questions referred to that Court by the House’s order of 12 July 2006. I am in agreement with the conclusion reached by my noble and learned friend that the House can now dispose of the long drawn out appeal, that was heard by the House as long ago as July 2005, by making the order he suggests in paragraph 23 of his opinion.
Lord Walker of Gestingthorpe

My Lords,

The background to the second reference under Article 234

3. On 28 July 2005 this House, having earlier heard two days of oral argument, decided ([2005] STC 1254) to make a reference to the Court of Justice of the European Communities under Article 234 of the Treaty. It was not until 12 July 2006 that the terms of the reference (posing five questions: [2008] STC 1408, 1430-1431) were agreed between the parties and embodied in an order. Advocate General Kokott gave her opinion on 13 December 2007 and the Third Chamber of the Court of Justice gave judgment on 10 April 2008. The matter has now come back to the House in an uncontested form.

4. The House decided to make the reference with acknowledged reluctance, since there had been a previous reference in the same proceedings (Case C-62/00 [2003] QB 866; [2002] STC 1036) and in July 2005 this complex litigation had already been on foot for more than ten years. I attempted to summarise the tangled course of the litigation in my speech proposing the second reference ([2005] STC 1254, paras 27-50) and it is unnecessary to repeat it at length. Here I shall try to make my survey as brief as is consistent with explaining the significance of the five questions posed by the second reference.

5. Marks & Spencer Plc (“M&S”) had two basic claims against the Customs and Excise Commissioners (as they then were: “the Commissioners”). One was that chocolate-covered teacakes (which M&S sold in large numbers) were between 1973 and 1994 incorrectly treated by the Commissioners as subject to standard-rate value added tax (“VAT”) as chocolate-covered cakes instead of being zero-rated as chocolate-covered biscuits. In 1995 M&S claimed a repayment of £3.5m. The Commissioners admitted 10% of this claim but resisted 90%, relying on the “passing-on” defence in section 80 (3) of the Value Added Tax Act 1994. Their case was that 90% of the improperly charged tax had been passed on by M&S to its customers, so that M&S would be unjustly enriched by repayment in full.
6. Here two technical footnotes are called for. One is that zero-rating is correctly referred to in EU law as “exemption with refund of input tax” and it is, in EU legal theory, a transitional concession to the needs and wishes of particular member states. It operates principally (though not, as will appear, exclusively) under national legislation. Lord Hoffmann discussed this point in his speech on the second reference, [2005] STC 1254, paras 5-13).

7. The other technical point to be noted is that M&S was for almost all the relevant period a “payment trader” (mainly because a large part of its turnover consists of adults’ clothing which is not zero-rated) whereas another retailer which made large sales of comparable teacakes, Tesco Plc, was a “repayment trader” (because most of its turnover consists of zero-rated foodstuffs). This point was more fully explained in my speech on the second reference, paras 15-17.

8. M&S had a quite separate claim against the Commissioners for repayment of VAT in connection with gift vouchers sold at a discount to their face value. The correct VAT treatment of such vouchers was in some doubt until the decision of the Court of Justice in the Argos case, Argos Distributors Ltd v Customs and Excise Commissioners (Case C-288/94) [1997] QB 499; [1996] STC 1359. This was despite an amendment made in 1992 to section 10(3) of the Value Added Tax Act 1983, which was intended to correct an error in transposing the Sixth Directive into national law. M&S claimed repayment of £2.8m, part of it in respect of vouchers issued before the amendment correcting the error in transposition (“early vouchers”) and the rest in respect of vouchers issued after the amendment (“late vouchers”). During the period while the early vouchers were being issued the national legislature had failed to transpose the Sixth Directive correctly; during the later period the national legislation had been corrected but the Commissioners continued to apply the law incorrectly (the amendment had in fact been made to meet a rather different point).

9. The final complication is that both of M&S’s claims were threatened with being reduced by retrospective legislation. The Finance Act 1997 introduced a new section 80 (4) of the Value Added Tax Act 1994 imposing a retrospective three-year limit on repayment claims (the teacakes claim, it will be recalled, went back to 1973). In the view of the Commissioners this reduced the teacakes claim (already limited to 10%) from £350,000 to about £88,000, and the vouchers claim from £2.8m to £1.9m.
10. In due course both claims came before the Court of Appeal on an appeal by M&S from Moses J ([1999] STC 205). The Court of Appeal (Stuart-Smith, Ward and Schiemann LJJ) held, so far as now material ([2000] STC 16):

(1) that M&S’s challenge to section 80 (4) (as infringing EU law) failed, as regards the teacakes claim, because the Becker conditions were not satisfied (*Becker v Finanzamt Münster-Innenstadt* (Case 8/81) [1982] ECR 53) and general principles of Community law could not be relied on in the absence of a directly enforceable right;

(2) M&S’s challenge to section 80 (4) failed, as regards the late vouchers claim, for similar reasons, since the Commissioners’ failure to apply the amended statute correctly was not equivalent to incorrect transposition; and

(3) M&S’s challenge to section 80 (4), as regards the early vouchers, should be referred to the Court of Justice. Schiemann LJ (with whom the other members of the Court agreed) stated ([2000] STC 16, 39):

“Marks and Spencer have an alternative submission which I shall consider in the next part of this judgment to the effect that the retrospective legislation is unlawfully discriminatory. I am not, for reasons which I shall shortly explain, persuaded that Marks and Spencer are entitled to judgment on that basis. It follows that a decision on whether it is compatible with Community law to enforce legislation which removes with retrospective effect a right under national law to reclaim VAT, which right has existed unexercised for more than three years, is in my judgment necessary to enable this Court to give judgment on the early vouchers claim. I would therefore be minded to refer this question to the Court of Justice.”

The argument which he went on to dismiss was to the effect that there was unlawful discrimination between payment traders and repayment traders.

11. The Court of Justice was not happy with the terms of the first reference ([2003] QB 866; [2002] STC 1036). Both Advocate-General Geelhoed and the Court of Justice rejected the distinction, accepted by the Court of Appeal, between the early vouchers claim and the late vouchers claim. The Court stated (para 28):
“As the Advocate-General has noted in para 40 of his opinion, it would be inconsistent with the Community legal order for individuals to be able to rely on a Directive where it has been implemented incorrectly but not to be able to do so where the national authorities apply the national measures implementing the Directive in a manner incompatible with it.”

The Court answered the referred question in general terms which did not distinguish between the two categories of voucher.

12. The Advocate-General also cast doubt on the Court of Appeal’s conclusion about the teacakes claim ([2003] QB 866, 873-874; [2002] STC 1036, 1044, para 30):

“The order for reference does not mention the claim for repayment of VAT erroneously paid in respect of teacakes. None the less, a similar problem arises in the case of the teacakes. In that connection, too, the question arises as to whether individuals have rights under Community law where a Directive has in itself been correctly transposed into national law but that law is applied in a manner clearly inconsistent with the scope of the Directive.”

There had been no submissions about exemption with refund of input tax (zero-rating) and the Court of Justice did not comment on this point.

13. The matter returned to a differently-constituted Court of Appeal (Auld and Chadwick LJJ and Newman J): [2004] STC 1. M&S’s vouchers claims were effectively conceded and there is no further issue on them. As to the teacakes claim Auld LJ (with whom the other members of the Court agreed) concluded that M&S still failed on the second Becker condition, that the relevant provision should be unconditional and precise. He stated (paras 69-70):

“As a matter of logic, and in the light of the Court of Justice’s reasoning in Ideal Tourisme a member state’s breach of its own domestic law maintained consistently with, but not as a requirement of Community law, is not a
breach of a Community law requirement to charge only a rate fixed by law within the meaning of arts 10 (1) (a) (b) and 12 (1). In addition, a zero-rate is a United Kingdom antonym; it is no rate at all within the meaning of the words in art 12 (1), ‘the rate . . . in force at the time of the chargeable event’.”

Auld LJ continued that (if he was wrong on that point) M&S’s claim failed on other grounds, and he summarised his views as follows (para 105):

“(2) As to the teacakes claim, I would rule that, for want of satisfaction of the second Becker condition on which, in any event, we cannot go behind the first Court of Appeal’s ruling, there is no directly enforceable Community law right to which the Court of Justice’s reasoning in the reference can apply so as to render the retrospective curtailment of the right to claim repayment incompatible with Community law.

(3) If, contrary to the first Court of Appeal’s ruling and my view, Marks & Spencer were able to establish a directly enforceable Community law claim to zero-rating of its teacakes, I would hold that we would be entitled to re-open the issue in the light of that part of the Court of Justice’s reasoning on the reference that identified the existence of a right to repayment of overpaid tax independently of its exercise by way of a claim. But I would also hold that: (a) though the defence of unjust enrichment could operate in a discriminatory way as between payment and repayment traders where the overpayment resulted from, inter alia, failure to zero-rate outputs, its incompatibility with Community law would lie in its non-application to repayment traders, not in its application to payment traders; and (b) in any event, the claim would be barred under the new time limit because it was made well outside an adequate period after its introduction.”

14. In my speech on the occasion of the second reference I summarised the main issues before the House as follows ([2005] STC 1254, para 51):
“(1) Did M&S, under art 28 of the Sixth Directive (both before and after its amendment in 1992) have a directly enforceable right not to be required to account for the tax on its teacakes otherwise than in accordance with the zero-rating provisions properly applicable under UK national law?

(2) Even if art 28 did not give M&S a directly enforceable right of that type, was the United Kingdom (in giving effect to its discretion under that article) required by the principle of fiscal neutrality to avoid discrimination between different types of traders, so as to give M&S a directly enforceable right to complain of the discrimination?

(3) If so, does EC law require or permit the remedy granted by the national court to depend on proof of financial loss, and on the absence of unjust enrichment?”

The questions on the second reference

15. Protracted discussions between the parties and their advisers refined these issues into the five questions referred to the Court of Justice. The first two questions, as the Advocate-General observed (para 19) address the preliminary issue of whether “this is at all a situation to which Community law applies and which confers certain rights on taxable persons.” The third question raises the central issue. The fourth and fifth questions address particular points arising out of the third question.

16. The questions referred are as follows: ([2008] STC 1408, 1430-1431):

“1. Where, under art 28(2)(a) of the Sixth . . . directive (both before and after its amendment in 1992 by Directive 92/77), a member state has maintained in its domestic VAT legislation an exemption with refund of input tax in respect of certain specified supplies, does a trader making such supplies have a directly enforceable Community-law right to be taxed at a zero rate?
2. If the answer to Question 1 is in the negative, where, under art 28(2)(a) of the Sixth . . . Directive (both before and after its amendment in 1992 by Directive 92/77), a member state has maintained in its domestic VAT legislation an exemption with refund of input tax in respect of certain specified supplies but has mistakenly interpreted its domestic legislation with the consequence that certain supplies benefiting from exemption with refund of input tax under its domestic legislation have been subject to tax at the standard rate, do the general principles of Community law, including fiscal neutrality, apply so as to give a trader who made such supplies a right to recover the sums mistakenly charged in respect of them?

3. If the answer to Question 1 or Question 2 is in the affirmative, do the Community-law principles of equal treatment and fiscal neutrality in principle apply with the result that they would be infringed if the trader in question is not repaid the entire amount mistakenly charged on the supplies made by him in circumstances where:

   (i) the trader would be unjustly enriched by repayment to him of the entire amount;
   (ii) domestic legislation provides that overpaid tax cannot be repaid to the extent that repayment would lead to unjust enrichment of the trader; but
   (iii) domestic legislation makes no provision similar to that referred to in (ii) in the case of claims by “repayment traders”? (A “repayment trader” is a taxable person who, in a given prescribed accounting period, makes no payment of VAT to the competent national authorities but receives a payment from them because, in that period, the amount of VAT that he is entitled to deduct exceeds the amount of VAT due in respect of supplies made by him.)

4. Is the answer to Question 3 affected by whether or not there is evidence that the difference of treatment between traders making claims for the repayment of overpaid output tax and traders making claims for additional amounts by way of input tax deduction (resulting from the over-declaration of output tax) has, or has not, caused any
financial loss or disadvantage to the former and, if so, how?

5. If, in the situation described in Question 3, the Community-law principles of equal treatment and fiscal neutrality apply and would otherwise be infringed, does Community law require or permit a court to remedy the difference of treatment by upholding a trader’s claim to a repayment of overpaid tax in such a way as to enrich him unjustly or require or permit a court to grant some other remedy (and, if so, which)?

The answers given by the Court of Justice

17. The Court of Justice answered the first question in the negative. Under art 28 (2) of the Sixth Directive zero-rating is permitted as a matter of derogation, but is not required. M&S could get no assistance from art 12 (1) of the Sixth Directive.

18. However the Court’s answer to the second question was favourable to M&S. The Court stated (para 33):

“It must be noted at the outset that the actual wording of art 28 (2) (a) of the Sixth Directive, in the version resulting from Directive 92/77, states that the national legislation which may be maintained must be ‘in accordance with Community law’ and satisfy the conditions stated in the last indent of art 17 of Directive 67/228. Although the addition relating to being ‘in accordance with Community law’ was made only in 1992, such a requirement, which forms an integral part of the proper functioning and the uniform interpretation of the common system of VAT, applies to the whole of the period of erroneous taxation at issue in the main proceedings. As the Court has had occasion to point out, the maintenance of exemptions or of reduced rates of VAT lower than the minimum rate laid down by the Sixth Directive is permissible only in so far as it complies with, inter alia, the principle of fiscal neutrality inherent in that system (see, to that effect, Gregg v Customs & Excise Commissioners (Case-216/97) [1999] STC 934, [1999] ECR I-4947, para 19, and EC Commission v France
19. In answering the third question the Court of Justice made the preliminary observation that disallowance of repayment claims on the ground of unjust enrichment is in principle compatible with Community law, but must be implemented in accordance with general principles such as that of equal treatment. The existence and degree of any unjust enrichment requires a full economic analysis, which is a matter for the national court.

20. The Court of Justice went on to consider fiscal neutrality, observing that it is a fundamental principle of the common system of VAT. It is the reflection, in the context of VAT, of the principle of equal treatment. The difference in the national legislation’s treatment of payment traders and repayment traders is not, the Court concluded, objectively justified, a conclusion illustrated by the amendment of section 80 (3) of the Value Added Tax Act 1994 by section 3 of the Finance (No 2) Act 2005. This conclusion was spelled out as follows (para 54):

“The answer to the third question must therefore be that, although the principles of equal treatment and fiscal neutrality apply in principle to a case such as that in the main proceedings, an infringement of those principles is not constituted merely by the fact that a refusal to make repayment was based on the unjust enrichment of the taxable person concerned. By contrast, the principle of fiscal neutrality precludes the prohibition of unjust enrichment from being applied only to taxable persons such as ‘payment traders’ and not to taxable persons such as ‘repayment traders’, insofar as those taxable persons have marketed similar goods. It will be for the national court to determine whether that is the position in the present case.”

The Commissioners accept that the prohibition applies in this case (Tesco Plc being a repayment trader which sold chocolate-covered teacakes) and the Commissioners have now satisfied the whole of the disputed claim in respect of teacakes.
21. On the fourth question the Court of Justice ruled that the answer to the third question was not affected by evidence that the repayment trader in question has not suffered any financial loss or disadvantage.

22. The fifth question explored whether, if the repayment trader would be unjustly enriched, Community law required or permitted the national court to grant some other remedy in respect of an infringement of the principle of equal treatment. The Court of Justice’s answer was that this was a task for the national court itself, but that the national court must comply with principles of Community law, and in particular the principle of equal treatment. The Court observed (para 62):

“The national court must, in principle, order the repayment in its entirety of the VAT payable to the trader who has suffered discrimination, in order to provide compensation for the infringement of the general principle of equal treatment, unless there are other ways of remedying that infringement under national law.”

The Commissioners do not seek to persuade the House that there is in this case any alternative method of remedying the infringement of the principle of equal treatment.

Conclusion

23. The Court of Justice’s answers to the third and fifth questions did therefore raise the possibility of further issues having to be decided by the national court. But the Commissioners have, after thirteen years of litigation, decided that they do not wish to pursue these matters. The House can therefore dispose of the matter by allowing the appeal from the order dated 21 October 2003 of the Court of Appeal, and inviting submissions as to costs (if necessary) within fourteen days.