Tax Advisers win limitation arguments in Professional Negligence claim

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Halsall v Champion Consulting Ltd is another in a line of cases emphasising the difficulties frequently faced by claimants suing their tax advisors outside of the standard 6 year limitation period. In a favourable decision for professional advisers, the court not only found against the claimants under s14A of the Limitation Act 1980 (the "**Act**"), but also found, albeit obiter, that a contractual limitation period was enforceable. This article focuses on the accrual date of claims and the limitation issues raised in the case.

Facts

The Claimants were four (litigation) partners in a solicitors firm who instructed the Defendants to advise on tax mitigation schemes. The Defendants recommended two tax schemes:

1. a charity scheme which provided tax relief through gift aid; and
2. a 'Scion' scheme which provided tax relief through film finance investment.
   (the "**Schemes**")

The Claimants alleged that the Defendants negligently described the charity scheme as a 'no-brainer', and negligently advised the Scion film scheme had a 75% chance of success. They should have advised that there was a significant risk the charity scheme would be vulnerable to challenge by HMRC, and that the Claimants could lose more than the initial sums they invested in the Scion scheme.

The charity scheme advice was given in 2003 and the Scion film scheme advice was given in 2007.

In addition, there was a clause in the Defendants' Terms of Business (**TOB**) which stated that any claim had to be brought *"within six years of the act or omission alleged to have caused the loss in question"* (the "**limitation clause**") In other words, the TOB sought to exclude s14A of the Act, which can extend the limitation period for tortious claims beyond 6 years.

Both Schemes were rejected by HMRC and the Claimants issued negligence proceedings in March 2015.

Decision

In determining whether the Defendants had breached their duty, the court applied the *Bolam* test which provides that a professional is not negligent if a significant body of reasonable practitioners would have acted in the same way, even if there are others that might not have. The judge found the Defendants negligent because no reasonably competent tax adviser would have given unconditional assurances in respect of the charity scheme, or failed to advise as to the potential additional liabilities which could arise in respect of the Scion film scheme.

Notwithstanding this, the court held that on the facts, the Claimants' claim was time barred. The claim was brought in tort rather than for breach of contract. Ordinarily, pursuant to s.2 of the Act, a negligence claim must be pursued within 6 years of the date on which the cause of action accrued i.e. the date on which the damage was suffered ("**the 6 year period**"). However, under s.14A of the Act, the claimant has a further period of 3 years to bring a claim from the date when the claimant has sufficient knowledge to know that he has a claim. This is deemed to arise when he knows enough to be put on notice to start investigating ("**the S14A period**").

In determining when the damage was suffered and the 6 year period started to run, the judge held that this was when the Claimants entered the Schemes, notwithstanding the fact that at that time there was no certainty whether the Schemes would succeed or fail as tax relief vehicles. The judge's reasoning was that, at that stage, *"the 'defect' in…advice was incapable of cure"* and the Claimants *"were tied into the 'commercial straightjacket'"* of the Schemes (Pegasus Management Holdings SCA v. Ernst & Young [2010] EWCA Civ 181 and Shore v Sedgwick Financial Services Ltd [2008] EWCA Civ 863). Therefore, the 6 year period expired in respect of the charity scheme and the Scion film scheme in 2009 and 2013 respectively.

As regards the s14A period, noting that time started to run for the Claimants when there was enough information to cause them to start investigating the possibility of defective advice, the court held that the relevant period started to run, at the

latest, in 2011 in respect of both Schemes. This was on the basis that not only had the Claimants by that stage written to the Defendants asking them to put their professional indemnity insurers on notice, but further, the Claimants had received letters from HMRC confirming that they were investigating and disputing the tax relief efficiency of both Schemes.

Further, albeit obiter, the court considered that the limitation clause in the Defendants' TOB did not breach the fairness or reasonableness requirements of the Unfair Contract Terms Act 1977 ("**UCTA**"). The court found that, bearing in mind the Claimants' experience as litigation solicitors, they understood the significance of the limitation clause, but took no steps to have it removed from the contract. The clause was clearly worded and, moreover, it was not necessary for the clause to expressly refer to s.14A of the Act in order for the s14A period to be contractually excluded.

Comment

Tax advisors and their insurers will take comfort from this decision and should view the obiter remarks on the contractual exclusion of s14A as of considerable interest.

Following tax advice, it may not be known for many years whether HMRC will raise a challenge to tax mitigation schemes and thus whether the tax advice will produce a loss. In this case, HMRC's decision on the tax efficacy of the Schemes was pending at the date of the advice but this did not matter. Following *Pegasus* and similar authorities, the 6 year period runs from the date the defendant's negligent tax advice is acted upon by the claimant: from this date the claimant is locked into a scheme or tax arrangement, and from this date it is possible that a loss will be suffered.

As regards the s14A arguments, the Claimants' submission that they did not appreciate that they might have a claim from the date they wrote putting the Defendants on notice that they should notify their PI insurers, was on the face of it highly ambitious. The fact that the Claimants were not only lawyers, but litigation lawyers at that, would have counted against them and perhaps largely explains the outcome.

When it comes to the judge's obiter decision on the arguments under the contractual limitation clause, we question whether a court would enforce the clause on different defendants, who are not solicitors who would or should know the legal effect of the clause. Tax advice inherently leads to situations where knowledge of potential tax losses might not arise until many years later. It is not uncommon for HMRC to only start investigating (let alone make a final decision), years after the original tax advice was given, and well after the 6 year period has expired. To deny potential claimants the opportunity to rely on s.14A of the Act is arguably neither fair nor reasonable under UCTA. Although welcome for its confirmation that clearly worded contractual limitation clauses will be enforced by the courts, this decision should not be relied upon as necessarily providing judicial support for contractual limitation periods in the context of tax advice.

Authors

Richard Highley
London - Walbrook
+44 (0)20 7894 6470
rhighley@dacbeachcroft.com