

Thousands of contractors face backdated tax bills as BN66 case is lost in High Court

Many thousands of contractors who have participated in tax mitigation schemes run out of the Isle of Man potentially face substantial back taxes. This follows the [High Court ruling](#) against contractor Robert Huitson that the retrospective measures introduced by HMRC in its infamous [BN66 advisory note](#) do not breach the European Convention of Human Rights.

Huitson had sought to overturn elements of the Finance Act 2008, by claiming that it was a breach of his rights under the Human Rights Act 1998 for HMRC to apply retrospective taxes. But the ruling by Mr Justice Beatson has set a dangerous precedent that could result in HMRC applying retrospective taxation to other groups of contractors, as well as other taxpayers, who use tax mitigation schemes.

£100m tax claim from one scheme alone

Montpelier Tax Consultants (Isle of Man) Ltd had advised Huitson to use a scheme that took advantage of the double taxation arrangement between the UK and Isle of Man. When HMRC subsequently investigated, it found that the participants had been evading tax. It therefore issued notices demanding payment of back taxes, interest and penalties.

It is believed there were an estimated 2,500 participants, potentially liable for £100 million in income tax, plus interest and penalties.

According to Crawford Temple, CEO of contracting sector compliance body [Professional Passport](#), the ruling is a reminder of the lengths HMRC is prepared to go to generate tax revenue. "Contractors," he warns, "should think carefully before joining tax planning schemes created to avoid taxation.

Budget Note 66 - proof that HMRC will chase retrospective taxes

"BN66 proves that HMRC is prepared to apply retrospective taxation to manufactured schemes which have been created to avoid taxation," says Temple. "The lesson of this case is that BN66 should be viewed as a warning to all other tax avoidance schemes."

The Budget Note was released by HMRC in March 2008, with two aims. The first was to ensure that existing legislation, dating back to 1987, was clarified so that it had the effect intended. The second was to close a loophole that allowed UK residents to receive their income from the Isle of Man and use double taxation treaties. These were originally designed to ensure that an individual or organisation is not taxed twice on the same income, but exploited by offshore tax consultants to enable UK residents to avoid their UK tax liabilities.

Both objectives were written into the Finance Act 2008 and, despite attempts by opposition MPs to amend its specific wording, the government forced it through and the provisions were backdated to 1987. This allowed HMRC to calculate retrospective tax liabilities for scheme participants going back many years.

Avoidance is the new evasion

HMRC's treatment of contractors using legal tax avoidance measures as if they are criminal tax evaders has sparked criticism since the introduction of a new code of practice for tax inspectors in June 2009.

This suggests that HMRC can adopt a harsher line if "more tax would have been paid if Parliament turned its mind to the specific issue in question". This has given HMRC a great deal of leeway, and its resulting actions have been widely condemned by tax specialists and professional tax and accountancy bodies.

According to Temple, this should sound warning bells, particularly for contractors who are typically seen by HMRC as soft targets for increased tax takers. "HMRC has made it clear that they will treat tax avoidance like tax evasion and, where possible apply the same penalties," Temple points out.

"When contractors are evaluating trading structures they really need to think about their own attitude to risk. Some, like those involved with the schemes hit by BN66, were prepared to accept higher risk. Unfortunately these risks are not always made clear to contractors by the providers."

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Crawford Temple has been involved in the contracting market since the mid 1990's; and is Chief Operating Officer at Professional Passport.

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