HMRC v BlueCrest Capital Management (UK) LLP [2023] UKUT 00232 (TCC)

This case concerned members of a UK Limited Liability Partnership which provided investment management and support services to entities within its group. Specifically, the case was concerned with whether the "salaried members rules" in Income Tax (Trading and Other Income) Act 2005, ss.863A-863G applied in respect of various individual members of the LLP.

The "salaried members rules" contain three conditions (A, B, and C). If all three conditions are met in respect of an individual member of an LLP, that individual is treated as if he or she were an employee of the LLP (and not a member of the LLP) for tax and NIC purposes. In this case, the parties agreed that Condition C (which relates to the amount of capital the individual has in the LLP) was met in respect of all relevant individuals, but they disputed whether Conditions A and B were met.

The case was heard by the First Tier Tribunal ("FTT") in March 2022, with the judgement being published in June 2022. Both parties subsequently appealed parts of the decision to the Upper Tribunal ("UT").

In practice, the case involved two categories of member of the LLP: portfolio managers, who were responsible for managing an investment portfolio as part of the LLP's investment management activities (which category included "desk heads" who managed a team of portfolio managers), and non-portfolio members, who broadly were responsible for providing support services, both within the LLP and as part of the LLP's provision of such services to its group.

The individual members of the LLP were each entitled to receive three categories of remuneration, being priority distributions (fixed amounts), discretionary allocations (which for portfolio managers were based on the performance of their portfolios, and which for non-portfolio members were based on a combination of factors including the LLP's financial performance, the individuals' performance, and current market rates for the individuals' roles), and income points allocations (which were not significant).

Condition A of the salaried members rules is met – in outline terms – where it is reasonable to expect that at least 80% of the amount payable by the LLP to the individual is "disguised salary". An amount is "disguised salary" if it is (a) fixed, (b) variable, but without reference to the overall profits or losses of the LLP, or (c) not in practice affected by the amount of those profits or losses. It was agreed in this case that the priority distributions constituted "disguised salary", but there was a dispute in respect of the discretionary allocations (with HMRC arguing these did constitute "disguised salary" and the LLP arguing they did not).

The LLP had argued before the FTT that, whilst the amounts of the discretionary allocations were based on the factors set out above, the amounts were "capable of variation" with reference to the overall profits or losses of the LLP because, if the LLP's profits were insufficient to cover the initially calculated discretionary allocations, these allocations would be abated. On this basis, the LLP argued, these discretionary allocations were not "disguised salary". The FTT rejected this argument, holding that "resolving to distribute no more than the accounting profit in any year, and providing what might happen to initial discretionary allocations if the profits are insufficient to cover them, does not provide the variability required [by] Condition A". The FTT held, therefore, that Condition A was met in respect of all the relevant members.

The LLP appealed to the UT on the grounds that, firstly, the FTT had erred in its construction of Condition A (having set the bar too high in terms of the link required between remuneration paid and the profits or losses of the LLP) and, secondly, that it reached a decision that no reasonable Tribunal could have reached on the evidence. The UT ultimately agreed with the approach taken by the FTT, holding that the LLP had not been able to show that the discretionary allocations were sufficiently linked to profits either as a matter of construction or on the evidence. On the second ground, the UT held that the judge was fully entitled on the material before him to make the factual findings that he did.

Condition B of the salaried members rules is met where the mutual rights and duties of the members of the LLP, and of the LLP and its members, do not give the individual “significant influence” over the affairs of the LLP.

HMRC had argued before the FTT that this condition looks to whether a member has significant influence over the affairs of the LLP generally (rather than over one aspect of the business or one department), and that it is concerned solely with managerial influence and not (say) financial influence. The LLP argued the opposite, and the judge agreed with the LLP in this respect, seeing no justification for restricting significant influence in the way HMRC had suggested.

The judge then turned to look at each of the two categories of member in turn. He held, firstly, that the investment and operational decisions made by the portfolio managers demonstrated that they had influence over the affairs of the partnership, notwithstanding the fact that they did not sit on any of the committees that were formally responsible for the management of the LLP. Ultimately, he concluded that each manager with a capital allocation of $100m or more should be regarded as having significant influence. As far as the non-portfolio members were concerned, the judge did not believe the LLP had established that any of these members could be said to have had significant influence over any of the activities of the LLP. Ultimately, therefore, portfolio managers with capital allocations of $100m or more did not meet Condition B, and so did not fall within the salaried members rules, whilst other members did meet Condition B and so – as they also met both Conditions A and C – were within the salaried members rules.

HMRC appealed against the decision in respect of Condition B (insofar as it related to those portfolio managers that were held not to have met Condition B) on nine separate grounds, with grounds 1 to 4 relating to the FTT’s construction of the legislation, and grounds 5 to 9 relating to the FTT’s application of the legislation to the facts. The UT rejected each of these grounds confirming, inter alia, that the legislation regarding significant influence does not refer to “the entirety of the affairs of the partnership”, and that “there is no warrant for demarcating particular types of activity as giving or not giving significant influence”.

Ultimately, in respect of both Conditions A and B, the UT considered that the FTT made findings of fact it was perfectly entitled to make, and that there was no error of law in either its approach to or its application of the legislation.

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