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Upper Tribunal
(Tax and Chancery Chamber)

Hearing venue: Rolls Building
7 Rolls Buildings
Fetter Lane
London
EC4A 1NL

Heard on: 27, 28 and 29 June 2023
Judgment date: 18 September 2023

PAYE and NICs – salaried members legislation – sections 863A - G ITTOIA 2005 – whether the members of the Respondent met Conditions A and B – appeal and cross-appeal dismissed

Before

MR JUSTICE EDWIN JOHNSON
JUDGE JENNIFER DEAN

Between

THE COMMISSIONERS FOR HIS MAJESTY'S REVENUE AND CUSTOMS
Appellant

and

BLUECREST CAPITAL MANAGEMENT (UK) LLP
Respondent

Representation:

For the Appellant: Richard Vallat KC, Laura Poots and Calypso Blaj, Counsel, instructed by the General Counsel and Solicitor to His Majesty's Revenue and Customs

For the Respondent: Amanda Hardy KC and Oliver Marre, Counsel, instructed by Slaughter and May Solicitors

DECISION

Introduction

1. Bluecrest Capital Management (UK) LLP ("BlueCrest") is a UK registered Limited Liability Partnership ("LLP") which carries on business in the alternative investment industry as part of the BlueCrest Group providing investment management services to the Group's funds.

2. Its appeal to the First-tier Tribunal ("FTT") concerned the application of the salaried members legislation to certain individual members of BlueCrest which, in summary, applies where a member of a limited liability partnership is to be treated as an employee of that partnership for the purposes of income tax and national insurance contributions ("NICs").

3. The salaried members rules contain three conditions, each aimed at capturing a different feature of "*disguised employment*" in an LLP. To fall outside the scope of the legislation a member need only fail any one condition. This case is concerned with two conditions contained within the legislation:

(A) Condition A, which is met if a member's remuneration from the LLP is (a) fixed or (b) is variable, but is varied without reference to the profits or losses of the partnership or (c) is not in practice affected by the overall amount of those profits or losses.

(B) Condition B, which is met if a member does not have significant influence over the LLP's affairs.

4. BlueCrest appealed to the FTT against HMRC Determinations that it is liable to pay income tax under the pay-as-you-earn ("PAYE") regime and HMRC's decision that it is liable to pay Class 1 NICs for the tax years 2014/15 to 2018/19 inclusive on the basis that all but four members of BlueCrest satisfy both Condition A and Condition B and accordingly should be taxed as employees.

5. In its decision ("the Decision") released on 29 June 2022, the FTT allowed the appeal in part. It decided that all members of BlueCrest met Condition A and some members met Condition B. References below to paragraphs in the form [X] are, unless otherwise indicated, references to paragraphs in the Decision. References to partnerships mean, unless otherwise indicated, partnerships operating as LLPs pursuant to the Limited Liability Partnership Act 2000. References to traditional partnerships mean partnerships, often referred to as firms, as defined in the Partnership Act 1890.

6. With the permission of the FTT, HMRC ("the Appellant") appeals ("the Appeal") against the Decision of the FTT on the basis that no members had significant influence over the affairs of BlueCrest such that Condition B was met by all members (other than the Original ExCo). HMRC argue that the FTT erred in its construction of section 863C Income Tax (Trading and Other Income) Act 2005 and the application of the test contained therein.

7. With the permission of the FTT, BlueCrest ("the Respondent") cross-appeals ("the Cross-Appeal") against the Decision of the FTT on the grounds that Condition A was not met by any of its members. It argues that the FTT erred in its construction of Condition A and accordingly applied the wrong test.

8. Both parties' grounds of appeal also raise challenges to the FTT's findings of fact on the basis of *Edwards v Bairstow* [1956] AC 14.

9. BlueCrest was represented by Ms Hardy KC and Mr Marre. HMRC were represented by Mr Vallat KC, Ms Poots and Ms Blaj. We are grateful to Counsel for their written and oral submissions

and to those instructing Counsel for organising the hearing bundles. In this context we should add that the submissions, the hearing bundles and the authorities for this hearing were extensive. We have not found it necessary, in this decision, to make specific reference to all of the submissions or to all of the materials to which we were referred. In reaching this decision, we should make it clear that we have taken into account all the submissions and the materials to which we were referred.

Legislation

10. The salaried members rules are found in sections 863A to 863G ITTOIA 2005 (income tax) and section 4 SSCBA 1992 and regulation 4 SSC(LLP)R 2014 (NICs). The provisions, which were introduced by the Finance Act 2014 and came into effect on 6 April 2014, were designed to remove the presumption of self-employment for some members of LLPs and so tackle the disguising of employment relationships through LLPs. As explained by the FTT (at [5]) they are intended to apply to those members of LLPs who are more like employees than partners in a traditional partnership. They are designed to ensure that LLP members who are, in effect, providing services on terms similar to employment are treated as employees for tax purposes. In order for the rules to apply, an individual must satisfy Conditions A, B and C. Failure to satisfy any of these conditions means that the rules do not apply. It is common ground in this appeal that Condition C applies to the individual members of BlueCrest.

11. The relevant legislation is set out in the Appendix to this Decision. Definitions and abbreviations in that Appendix bear the same meanings in the body of this Decision.

Relevant background

12. There was no dispute in relation to the material facts, which the FTT helpfully set out at [16] – [44] and from which we have drawn the following summary.

13. The BlueCrest Group is involved in financial asset management around the world. BlueCrest forms part of the BlueCrest Group and was incorporated in England and Wales on 29 October 2009.

14. BlueCrest commenced business in London on 1 April 2010 providing investment management services to the Group's funds, as a sub-investment manager working under the "lead investment manager" (BlueCrest Capital Management LP (a Guernsey Limited Partnership)) from time to time; and providing back-office services to other Group entities.

15. Prior to December 2015, the Group managed the funds of external investors, and also 'internal funds'. External funds made up over 90% of the assets under management.

16. Since December 2015 all the Group funds have been closed to outside investors. The main investment fund is BSMA Ltd ("BSMA"). A further fund known as Millais Limited was set up in 2017. There are now $3.9 billion under management across the Group (held in BSMA and Millais (together the "Fund")).

17. BlueCrest Capital Management Limited (a Jersey-resident company) is the general partner ("General Partner") of the lead investment manager. In that capacity, it represents and carries on the business of the lead investment manager.

BlueCrest's activities

18. BlueCrest has two broad strands of activities:

(a) Investment management: the Fund is managed by the lead investment manager, and the Respondent acts as a 'sub-investment manager'. This activity is governed by a sub-investment management agreement made between BlueCrest and the lead investment manager. In turn, this investment management was undertaken firstly by discretionary investment managers, engaged in traditional decision based investment management, usually undertaken by individual portfolio managers who, within their set investment remit, decide what assets to hold and what transactions to enter into based on their views of a particular market and their particular expertise and experience; and secondly by systematic trading, often referred to as algorithmic trading, a computer-based investment management strategy in which algorithms determine when or where to enter and exit a series of trades.

(b) Support services: BlueCrest provides support services to entities within the Group, such as legal, finance and IT services (also described as back-office services). BlueCrest provides these support services under service agreements and receives fees for doing so.

19. Before the return of capital to external investors in 2016, the Group's lead investment management entity received management and performance fees from the Group's funds. Typically, the management fee received was 2% of funds under management, which was payable irrespective of the performance of the fund, and the performance fee was 20% of profits of the period. The lead investment management entity paid a proportion of these fees to each of its sub-investment managers, including the Respondent. During this period there was a "netting risk", i.e. the performance fee was only paid on profits above a certain level, and if there had been losses since the last performance fee payment date, those were recovered before any performance fees were paid. Furthermore, other investment managers' losses were netted against profits generally, so one investment manager could suffer from the poor performance of another.

20. During the period 2016 to 2018 there was a change to the method of calculating the performance fee payable to the Respondent. During that time the Respondent was paid 18% of the performance of each UK investment manager. The reason for this was that the Fund was closed to outside investors. However, from 2018, netting was reintroduced, and the performance fee increased to 20%.

21. Throughout the relevant period, the Respondent was profitable, as shown in the table below.

All figures rounded up to the nearest million

	Profit before tax (£m)
31 Dec 2014	85
31 Dec 2015	66
31 Dec 2016	107
31 March 2018	100

Relevant members

22. The individual members with whom this appeal is concerned can be viewed by reference to three broad categories:

(a) Infrastructure members;

(b) Discretionary traders or portfolio managers;

(c) Other front office members.

23. The infrastructure members are, in general terms, those who are responsible for providing the support or back-office services to the Group, such as technology, facilities, legal and compliance. The infrastructure members include: (a) The Original ExCo; (b) A number of "heads of department", such as the head of technology or head of human resources; (c) Other senior members of these departments.

24. As at 3 April 2014 there were 82 individual members. 16 of these were infrastructure members, including the Original ExCo.

25. Portfolio managers are responsible for managing an investment portfolio as part of the investment management services provided by the Respondent to the BlueCrest Group entities. Portfolio managers are allocated an amount of capital and have discretion as to how to invest that capital allocation.

26. The capital allocation of each portfolio manager can be described as their "portfolio" or "book".

27. This category also includes "desk heads" who manage a team of portfolio managers. Some of those desk heads have their own capital allocation, others do not but instead oversee a team of portfolio managers and/or a distinct fund.

28. As at 3 April 2014, there were 48 individuals in this category overall, and in 2014 seven of those were desk heads.

29. Miss Kerridge, former Head of Tax and current member of BlueCrest, who gave evidence at the FTT hearing described other front office members as follows: "Other front office members of the [Respondent] who do not have their own discretionary portfolios are very experienced researchers or technologists responsible for managing teams such as quant research teams and computer modellers."

30. As at 3 April 2014, there were 18 individuals in this category.

31. In this Decision, we will refer to discretionary traders as "portfolio managers", and the infrastructure members and other front office members as "non-portfolio members".

The LLP Agreements

32. At the beginning of the relevant years, the Respondent was governed by a Limited Liability Partnership Agreement, dated 22 March 2011 and amended on 10 July 2013 (the "LLP Agreement"). During the relevant years, the LLP Agreement was further amended or substituted on a number of occasions.

33. The allocation of BlueCrest's profits is governed by the LLP agreement, in particular clause 10.

Remuneration

34. There are three categories of remuneration received by individual members from BlueCrest:

(a) Priority distributions.

(b) Discretionary allocations.

(c) Income point allocations.

35. Priority distributions are, in essence, the individual member's fixed salary. Discretionary allocations can be described as the individual member's bonus and income point allocations do not represent a significant amount of any individual member's remuneration. It was common ground that the priority distributions fell within the definition of disguised salary and therefore the focus of the appeal before the FTT, and before us, was on the discretionary allocations.

36. As the FTT described (at [48]):

> "In dealing with discretionary allocations, the [Respondent] undertook arrangements known as a partner incentivisation plan or "PIP", under which, very broadly, amounts were allocated to a corporate member as a discretionary allocation and then ended up in the hands of individual members at a later date… For the purposes of this appeal, it is agreed that the amounts paid to the individual members, either directly or via the PIP Facilitators, together comprise discretionary allocations."

37. The process by which discretionary allocations were determined, which the FTT described as involving a provisional stage and a final stage, is as follows: the Global Remuneration Committee ("GRC") considers the position of the Group as a whole. It reviews the performance of members and the business and decides on amounts that each partner should be awarded. The checks which are carried out through this process are intended to ensure that drawings will not exceed the amounts that will eventually be available as profits, which amount cannot be certain until the relevant accounts have been finalised. The starting point of this exercise is the anticipated accounting profit.

38. The GRC then makes recommendations in relation to BlueCrest and its members to Group ExCo (an executive committee to whom the board of the General Partner has delegated its responsibilities, and which coordinates the approach to compensation across the Group).

39. Group ExCo then makes recommendations to the Board of BlueCrest which makes the final determination on discretionary allocations. The Board is not typically in a position to finalise profit allocations until at least six months after the accounting year end.

40. Once the discretionary allocations had been determined, they were credited to each individual member's "Distribution Account" from where they could be withdrawn by the individual member.

41. Clause 10.8 of the LLP Agreement provides as follows:

> "…. Discretionary Drawings made by any member shall be debited on each occasion they are made to the Distribution Account of such member. In the case of any individual member, the Board shall have the discretion to require the relevant member to immediately repay any Discretionary Drawings that have been so debited to the Distribution Account of such individual member to the extent they have not been reduced by any subsequent profit allocation. In the event that the amount of any Discretionary Drawings made by any member in any financial year of the Partnership shall exceed the amount of profits allocated to the relevant member pursuant to this clause 10, or if the Partnership has incurred losses (other than capital losses) in respect of such financial year, so that there is a negative balance on his Distribution Account following such allocation of profits or any allocation of losses then the Board shall have

> discretion to require the relevant member to immediately repay the excess amount of such Discretionary Drawings over the profits so allocated or, in the case of a loss, the whole amount of such Discretionary Drawings or to allow such negative balance to be carried forward to be set off against profits allocated to the relevant member in respect of future financial years of the Partnership……."

Management and governance

42. The Board of the General Partner has responsibility for the day-to-day management and control of BlueCrest. It has delegated its responsibilities to Group ExCo which meets approximately 10 times per year to discuss and make decisions regarding group strategy, operations, and performance.

43. In accordance with clause 14.11 of the LLP Agreement, the Board of BlueCrest has established an executive committee ("UK ExCo") which has responsibility for:

> (a) reviewing the operational performance of the Partnership, including, but not limited to, reviewing business units and financial performance and implementing any required changes;
>
> (b) reviewing the ongoing risk profile of the business of the Partnership (including in the context of its clients) and implementing any required changes;
>
> (c) any legal, compliance, operational, regulatory or human resource related matters affecting the Partnership or the Business;
>
> (d) the development and implementation of all matters relating to the day to day operations and the infrastructure of the Business; and
>
> (e) monitoring, reviewing and resolving all issues relating to the operational management of the Business.

44. UK ExCo delegated specific responsibilities to a number of committees.

Portfolio managers

45. Portfolio managers carry out market research to form a long-term view of the market of their investments before the rest of the market. They construct a portfolio which is within their desk and seek to minimise the amount of cash that backs up the market exposure they assume. That exposure is partly backed by cash with the balance being leverage from a counterparty such as a bank or broker.

46. Portfolio managers are also involved in hiring new portfolio managers and are best placed to decide the skills and business needs of a new portfolio manager although the final decision rests with the Board.

47. An individual portfolio managers' capital allocation is proposed by their desk head and the head of risk and is then considered by Group ExCo. A recommendation is made and the proposed allocation is then discussed and ratified by UK ExCo. The final allocation is ultimately reviewed and agreed by Mike Platt and Andrew Dodd at Group ExCo. Once a junior portfolio manager showed they were capable of fulfilling a partner's role, they would be allocated a capital allocation which generally started at $100 million. Capital allocations could fluctuate and during the relevant years, the total capital allocations amounted to approximately $15 billion.

48. Desk heads, the risk department and GroupExCo monitor portfolio managers. Day-to-day responsibility for portfolio risk management is delegated to the desk heads, the risk team, and the

individual portfolio managers. Each portfolio manager is responsible for their own investment decisions and has full discretion to incur risk regarding the investment positions they take. Some senior portfolio managers are appointed to operate as desk heads who are responsible for, amongst other things, monitoring the day-to-day performance of other portfolio managers on their desk, management of their desk generally, and the recruitment of portfolio managers onto their desk. The ratio of partner portfolio managers to employee portfolio managers is high. In the relevant years it was between 47.5% and 57.5% members.

49. BlueCrest operates a "stop-loss" policy which is monitored by the risk team on a daily basis. It takes effect if annual performance reaches -5% of portfolio manager's capital allocation. If the stop-loss limit is hit, a number of decisions need to be made including: whether the portfolio manager should continue to manage the risk; whether the manager should be dismissed; who should take responsibility for that manager's position; and what should be done with that risk.

50. In addition to the investment and commercial risks faced by BlueCrest, the FTT highlighted the risks that had been encountered by the Group. By way of example, in a five day period in March 2020, the Fund lost over $850 million out of a cash reserve of about $1 billion. The Fund avoided real financial difficulty due to the intervention of the US Federal Reserve. The Group had also faced commercial risk in December 2020 when the General Partner entered into a $170 million "no admit no deny" settlement with the US Securities and Exchange Commission.

51. Generally, a portfolio manager's standing within the firm reflected their capital allocation; the greater the allocation, the greater the experience and expertise of the portfolio manager and, in turn, the greater the weight attached to that manager's opinion about matters affecting the business. The figure of $100 million (which had been identified and accepted by the FTT as the threshold above which a portfolio manager exercised significant influence) was an arbitrary figure. However, portfolio managers who have capital allocations above that amount were recognised as individuals of high standing and whose opinions carried weight.

The April 2014 Resolutions

52. A tax department paper on the interpretation of the proposed salaried members rules was prepared for UK ExCo by Miss Kerridge and her tax team in consultation with Ernst & Young. In relation to Condition A, the paper stated:

> "We have been advised that this requirement should be met if after calculating all of the partners' discretionary profit allocation, using the methods that have historically been used, the total of all of these allocations is compared against the profits of [the Respondent] to determine whether there is sufficient profit to fund the aggregate of all of the discretionary allocations.
>
> It is therefore recommended that the ExCo confirm that its policy is that future profit allocations will be referenced to the total profits of [the Respondent] and if there is a year when the total profits of [the Respondent] were not sufficient to fund the discretionary profit allocations these allocations would be reduced accordingly. It would be preferable for this reduction to be effected pro rata across all discretionary allocations, rather than by reduction of some partners' discretionary allocations in priority to others. In such a case the profits should not be increased through an amendment to the transfer pricing policy or through some other means to ensure that there are sufficient profits to fund the profit allocations."

53. At a meeting on 3 April 2014 UK ExCo resolved to recommend to the Board that:

> "a) it reaffirm the fact that it would not make discretionary allocations in excess of profits available the purpose; b) in the event that discretionary allocations did exceed available profits then such allocations would be reduced; and c) the Partnership would not seek to artificially increase the amount of profits available for allocation to ensure compliance with b)".

54. The Board accepted the recommendation and, as noted by the FTT at [115]:

> "…by way of a written resolution dated 3 April 2014:
>
> (1) Noted, inter alia, that pursuant to the LLP agreement the Board is entitled to allocate income profits in any year as it may in its absolute discretion determine; that in certain circumstances it is possible for the Board to make allocations which might in aggregate exceed the total amount of profit available in a given year; and that the availability of unallocated profits is taken into account by the Board when determining potential allocations.
>
> (2) Resolved that future discretionary allocation of income profits in accordance with the LLP Agreement dated 22 March 2011 should not exceed in aggregate total profits available for that purpose for a given year; in the event that the proposed allocations exceed those total profits, the Board shall reduce the amount of such allocations accordingly; and the appellant should not seek to enter into any arrangement with the express purpose of increasing the profits available for the preceding purpose."

UK ExCo and other committees

55. Save for the valuation committee which was established in May 2014 and the regulatory affairs committee which was established in July 2014, the remaining committees were established in April and May 2012. The FTT was provided with the terms of reference for the operational risk committee which it described as follows (at [117] – [118]):

> "These terms of reference are, broadly speaking, in a common form and many include, under the heading "purpose" the following:
>
> "[UK Exco] and [Group Exco] (together "the Exco's") are responsible for the systems of internal controls and for managing the risks associated with the business and markets within which each entity operates. [The lead investment manager] has outsourced to [the appellant] the following support services: operations, product control, risk management, position valuing, legal, compliance, investor relations and human resources services."
>
> The terms of reference then go on to identify the core responsibilities delegated by the ExCo's to that particular committee together with the committee's duties, authority and reporting obligations. So, for example, the terms of reference for the regulatory affairs committee identifies its purpose as being to consider a number of matters including FSA and other regulatory visits, global regulatory developments, resourcing for compliance, resourcing for growing regulatory reporting requirements, issues relating to bribery corruption and money-laundering. Its duties include reviewing and improving compliance monitoring plans and policies, approve resourcing for compliance, consider responses to regulatory requirements and regulatory risks as they arise."

56. The committees reported to UK ExCo. The minutes of UK ExCo meetings appeared to the FTT Judge to follow a standard format, recording that under the LLP agreement the members have appointed UK ExCo to assist the Board in various strategic matters relating to the Respondent which

are set out in more detail at clause 14.11 of the LLP Agreement. The meetings were mainly chaired by Mr Cox and attended by the heads of various departments.

57. In relation to the meetings which dealt with profit allocations, the FTT stated at [121]:

> "The minutes of the UK ExCo which dealt, specifically, with profit allocation, are also in reasonably standard form. In each case it appears that a schedule of proposed allocations to each member was tabled. In each case it was noted that the calculations had been carried out in accordance with clause 10.3 of the LLP Agreement and following discussion it was resolved that the final allocations should be in accordance with the provisional allocations set out in the schedule."

Heads of department and back-office services

58. The evidence before the FTT from Miss Kerridge was that that the back-office is made up of the departments needed to run the Group's business. Only the most senior personnel such as department heads and others of similar seniority are members of BlueCrest. The department heads are responsible for providing the relevant services, hiring, performance review and terminations of the employed staff, setting policy and procedures, and all matters required for the efficient provision of the relevant services. Others, such as senior members of the legal team, are responsible for business critical matters such as advising on the law relating to derivative transactions and advising senior management on strategy and both new and existing business initiatives.

Mike Platt

59. Mike Platt is the Chief Executive Officer and Chief Investment Officer of the General Partner. He established the Respondent in January 2000 and is both the founder and principal investor in the Fund.

60. The FTT described Mike Platt's role (at [124]) as:

> "…to set the overall investment strategy for the Group; ensure that the Fund maintains appropriate cash and liquidity levels; recommend cash should be invested or divested from the Fund; take decisive actions and provide clear direction to help mitigate macro economic events which will affect the return of the Fund; identify risk areas and decide on the Fund's investment strategies."

61. Mike Platt, together with Andrew Dodd, is the main investor in the fund. Mr Platt utilised Group ExCo as a vehicle through which to change investment strategy as it is Group ExCo which determined the Group's overarching investment strategy.

62. Many decisions within BlueCrest are managed by portfolio managers, desk heads and UK ExCo, however decisions could be escalated to Mike Platt. By way of example, the final allocation of an individual portfolio manager's capital allocation is reviewed and agreed by Mike Platt and Andrew Dodd.

63. Mike Platt's position was described in evidence before the FTT (at [128]) as:

> "Essentially we have one client, which is Mike. So he is the CEO… but he is also the client. And ultimately if his objectives change, and the things that he thinks we should be focusing on …and the way in which we should be trying to ultimately service his money…we're providing…a service for his investments -- he's able to move the goalposts…he's the top of the organisation. But that doesn't mean -- you know, the head

> of the Civil Service doesn't sort out my local parking permit. He doesn't make every decision but ultimately of course he can veto a decision if he chooses to get involved."

The Decision

64. Now that we have set out the relevant background, we can summarise the FTT's decision.

65. The hearing before the FTT occupied seven days comprising (i) a half day of opening submissions, (ii) two and a half days of oral evidence, and (iii) closing submissions over three and a half days.

66. The FTT allowed the appeal in respect of the portfolio managers with capital allocations of $100 million or more and the desk heads, but not in respect of the other portfolio managers and the non-portfolio managers (other than the Original ExCo).

67. The basis of the FTT's decision was, in summary:

i) The portfolio managers (including desk heads) meet Condition A;

ii) The non-portfolio managers meet Condition A;

iii) The portfolio managers with capital allocations of $100 million or more and the desk heads do not meet Condition B;

iv) The other portfolio managers and all of the non-portfolio managers (other than the Original ExCo) meet Condition B.

The Appeal

68. The Appellant (HMRC) rely on the following grounds of appeal:

i) The FTT failed to adequately consider the legal distinction between traditional partners and employees and further failed to apply that distinction in the context of Condition B;

ii) The FTT erred in its construction of "affairs of the partnership";

iii) The FTT erred in its construction of "influence" over the affairs of the partnership;

iv) The FTT erred in its construction of "significant" influence;

v) The FTT erred in failing to appreciate that any significant influence must ultimately derive from their "mutual rights and duties" under the LLP agreement;

vi) The FTT erred in applying the analogy with a traditional professional service firm;

vii) The FTT was wrong to conclude that the relevant portfolio managers had "managerial clout";

viii) The FTT's findings of fact in relation to "involvement" in operational decisions were not sufficient to demonstrate significant influence;

ix) The FTT was wrong to conclude that a capital allocation of $100 million was sufficient evidence to support a finding of significant influence or demonstrate that an individual with such an allocation had a status analogous to that of a traditional partner.

The Cross-Appeal

69. The Respondent relies on two grounds of appeal. We are grateful to Ms Hardy for confirming at the hearing that ground 3, which relied on the anti-avoidance rule in s863G ITTOIA 2005, is no longer pursued. The grounds can be summarised as follows:

i) The Tribunal erred in its construction of, and approach to Condition A. This ground comprised a number of particularised sub-grounds which we address in more detail below.

ii) The FTT reached a decision that no reasonable Tribunal could have reached on the evidence in deciding that more than 20% of the remuneration of the non-portfolio manager members was not variable and varied in practice by reference to the profits or losses of the partnership. This ground also comprised a number of particularised sub-grounds.

The law

70. The FTT Decision records that the evidence in the appeal comprised two significant bundles of documents, a statement of agreed facts and witness evidence from four members of BlueCrest. The Judge carefully analysed the evidence and made extensive findings of fact in the Decision.

71. As both the Appeal and Cross-Appeal include challenges to the Judge's conclusions on the evidence before him, it is as well to have in mind the guidance given by the courts in relation to appeals of this kind.

72. The classic articulation of the grounds on which findings of fact may be challenged on appeal as an error of law is in *Edwards v Bairstow* [1956] AC 14. In allowing the Revenue's appeal the House of Lords considered the basis on which such a conclusion based on the facts could be disturbed. Lord Radcliffe (with whom Lords Tucker and Somervell agreed) explained at [33]:

> "… there are many combinations of circumstances in which it could not be said to be wrong to arrive at a conclusion one way or the other. If the facts of any particular case are fairly capable of being so described, it seems to me that it necessarily follows that the determination of the Commissioners, Special or General, to the effect that a trade does or does not exist is not "erroneous in point of law"; and, if a determination cannot be shown to be erroneous in point of law, the statute does not admit of its being upset by the court of appeal. I except the occasions when the commissioners, although dealing with a set of facts which would warrant a decision either way, show by some reason they give or statement they make in the body of the case that they have misunderstood the law in some relevant particular."

73. Lord Radcliffe went on to consider the test for when an appellate court can intervene, at [36]:

> "I do not think that inferences drawn from other facts are incapable of being themselves findings of fact, although there is value in the distinction between primary facts and inferences drawn from them. When the case comes before the court, it is its duty to examine the determination having regard to its knowledge of the relevant law. If the case contains anything ex facie which is bad law and which bears upon the determination, it is, obviously, erroneous in point of law. But without any such misconception appearing ex facie, it may be that the facts found are such that no person acting judicially and properly instructed as to the relevant law could have come to the determination under appeal. In those circumstances, too, the court must intervene. It has no option but to assume that there has been some misconception of the law and that this has been responsible for the determination. So there, too, there has been error in

> point of law. I do not think that it much matters whether the state of affairs is described as one in which there is no evidence to support the determination or as one in which the evidence is inconsistent with and contradictory of the determination, or as one in which the true and only reasonable conclusion contradicts the determination. Rightly understood, each phrase propounds the same test. For my part, I prefer the last of the three, since I think that it is rather misleading to speak of there being no evidence to support a conclusion when in cases such as these many of the facts are likely to be neutral in themselves, and only to take their colour from the combination of circumstances in which they are found to occur."

74. Evans LJ (with whom Savill and Morritt LJJ agreed) elaborated on *Edwards v Bairstow* in *Georgiou (t/a Mario's Chippery) v C&E Comrs* [1996] STC 463 at [476]:

> "It is right, in my judgment, to strike two cautionary notes at this stage. There is a well-recognised need for caution in permitting challenges to findings of fact on the ground that they raise this kind of question of law. That is well seen in arbitration cases and in many others. It is all too easy for a so-called question of law to become no more than a disguised attack on findings of fact which must be accepted by the courts. As this case demonstrates, it is all too easy for the appeals procedure to the High Court to be misused in this way. Secondly, the nature of the factual inquiry which an appellate court can and does undertake in a proper case is essentially different from the decision-making process which is undertaken by the tribunal of fact. The question is not, has the party upon whom rests the burden of proof established on the balance of probabilities the facts upon which he relies, but, was there evidence before the tribunal which was sufficient to support the finding which it made? In other words, was the finding one which the tribunal was entitled to make? Clearly, if there was no evidence, or the evidence was to the contrary effect, the tribunal was not so entitled.
>
> It follows, in my judgment, that for a question of law to arise in the circumstances, the appellant must first identify the finding which is challenged; secondly, show that it is significant in relation to the conclusion; thirdly, identify the evidence, if any, which was relevant to the finding; and, fourthly, show that that finding, on the basis of that evidence, was one which the tribunal was not entitled to make. What is not permitted, in my view, is a roving selection of evidence coupled with a general assertation that the tribunal's conclusion was against weight of the evidence and was therefore wrong."

75. In *Eclipse Film Partners No 35 LLP v HMRC* [2015] EWCA Civ 95, which was an appeal in relation to a trading dispute, the Court of Appeal held at [112] and [113]:

> "…As an ordinary word in the English language "trade" has or has had a variety of meanings or shades of meaning. Its meaning in tax legislation is a matter of law. Whether or not a particular activity is a trade, within the meaning of the tax legislation, depends on the evaluation of the activity by the tribunal of fact. These propositions can be broken down into the following components. It is a matter of law whether some particular factual characteristic is capable of being an indication of trading activity. It is a matter of law whether a particular activity is capable of constituting a trade. Whether or not the particular activity in question constitutes a trade depends upon an evaluation of all the facts relating to it against the background of the applicable legal principles. To that extent the conclusion is one of fact, or, more accurately, it is an inference of fact from the primary facts found by the fact-finding tribunal.
>
> It follows that the conclusion of the tribunal of fact as to whether the activity is or is not a trade can only be successfully challenged as a matter of law if the tribunal made an error of principle or if the only reasonable conclusion on the primary facts found is inconsistent with the tribunal's conclusion. These propositions are well established in the case law*: Edwards v Bairstow* [1956] AC 14, 29-32 (Viscount Simonds), 33, 36, 38-

> 39 (Lord Radcliffe); *Ransom v Higgs* [1974] 3 All ER 949, 955 (Lord Reid), 964 (Lord Wilberforce), 970-971 (Lord Simon); *Marson v Morton* [1986] 1 WLR 1343, 1348 (Sir Nicholas Browne-Wilkinson V-C). An appeal from the FTT is on a point of law only: Tribunals, Courts and Enforcement Act 2007 s.11."

76. In *Fage UK Limited and another v Chobani UK Limited and another* [2014] EWCA Civ 5 the Court of Appeal gave the following guidance at [114]:

> "Appellate courts have been repeatedly warned, by recent cases at the highest level, not to interfere with findings of fact by trial judges, unless compelled to do so. This applies not only to findings of primary fact, but also to the evaluation of those facts and to inferences to be drawn from them…The reasons for this approach are many. They include:
>
> i) The expertise of a trial judge is in determining what facts are relevant to the legal issues to be decided, and what those facts are if they are disputed.
>
> ii) The trial is not a dress rehearsal. It is the first and last night of the show.
>
> iii) Duplication of the trial judge's role on appeal is a disproportionate use of the limited resources of an appellate court, and will seldom lead to a different outcome in an individual case.
>
> iv) In making his decisions the trial judge will have regard to the whole of the sea of evidence presented to him, whereas an appellate court will only be island hopping.
>
> v) The atmosphere of the courtroom cannot, in any event, be recreated by reference to documents (including transcripts of evidence).
>
> vi) Thus even if it were possible to duplicate the role of the trial judge, it cannot in practice be done."

77. With the principles set out above in mind, we turn now to our analysis of the Appeal and Cross-Appeal.

Analysis – the Appeal

Overview

78. HMRC appeals against the FTT's Decision that portfolio members with capital allocations of $100m or more and desk heads fail the requirements of Condition B. HMRC contend that the mutual rights and duties of the members of the LLP did not give the portfolio members or desk heads significant influence over the affairs of the partnership. Grounds 1 to 4 concern the FTT's construction of s 863C and Grounds 5 to 9 concern the FTT's application of the legislation to the facts as found.

79. As the FTT Judge observed at [172], the salaried members legislation is aimed at circumstances where the relationship between an LLP and its members is more like an employment relationship and we accept the submission of Mr Vallat that its purpose is to distinguish between persons in the position of an employee and persons in the position of a partner in a traditional partnership, involving what is effectively a joint venture between the partners.

80. We were referred to *Bates van Winkelhof v Clyde & Co. LLP* [2012] EWCA Civ 1207 [2013] ICR 883 which was an appeal in which a question arose as to whether a partner could be a "worker" for the purposes of the Employment Rights Act 1996. After summarising the cases which show that the nature of a partnership is inconsistent with the status of an employee, Elias LJ identified why a partner could not be a worker, at [64]:

> "…The very concept of employment presupposes as a matter of sociological fact a hierarchical relationship whereby the worker is to some extent at least subordinate to the employer. This is the characteristic which underpins the general understanding of what constitutes the essence of an employment relationship. Where the relationship is one of partners in a joint venture, that characteristic is absent. Each partner is agent for the other and is bound by the acts of the other and each partner is both severally and jointly liable for the liabilities of the partners. There is lacking the relationship of service and control which is inherent in both concepts of employee and [worker]. The partnership concept is the antithesis of subordination."

81. We found the observations set out above useful in distinguishing between the position of a person who is an employee and a person who is in the position of a partner. However, we note that we are bound to accept the words of Lady Hale DPSC in *Bates* in the Supreme Court ([2014] UKSC 32) at [39]:

> "There can be no substitute for applying the words of the statute to the facts of the individual case. There will be cases where that is not easy to do. But in my view they are not solved by adding some mystery ingredient of "subordination" to the concept of employee and worker. The experienced employment judges who have considered this problem have all recognised that there is no magic test other than the words of the statute themselves… While subordination may sometimes be an aid to distinguishing workers from other self-employed people, it is not a freestanding and universal characteristic of being a worker."

82. It does not seem to us, as the Respondent argues, that the Supreme Court was overruling the basis of the distinction between employee and partner suggested by Elias LJ. Rather, what is said by Lady Hale serves as an invaluable reminder, which is highly relevant in the present case, that there "*can be no substitute for applying the words of the statute to the individual case*". As Lady Hale also pointed out, there is not a single key to unlock the words of the statute in every case. So, while the concept of subordination may be useful in distinguishing between an employee and other categories of worker, it is not a single key which unlocks the words of the statute, either in *Bates* or in the present case.

83. In our view, the question to be asked, by reference to the wording of Condition B, is whether the mutual rights and duties of the members of the limited liability partnership, and of the partnership and its members, do not give the members significant influence over the affairs of the partnership. At first sight this requires focus upon the relevant agreement or agreements which set out the rights and duties of the members of the partnership. It has, however, been accepted by the Respondent in this case that it is permissible also to consider this question in terms of actual (de facto) influence, which may not necessarily derive from the LLP Agreement or any formal agreement governing the rights and duties of the members of BlueCrest.

Ground 1

84. HMRC aver that the FTT failed to consider adequately the legal basis for the distinction between employees and partners. Instead, HMRC submit, the FTT focussed on the role or function of a traditional partner to "*find, mind and grind*" (at [174]) (i.e. to find work, supervise others doing the

work and to do the work themselves). HMRC submit that in doing so, the FTT identified the role of a partner in a traditional partnership by reference to what a partner does, rather than by an analysis of the nature of the relationship between traditional partners as a matter of law and failed to consider the statutory question of influence and, in particular, the degree of subordination found in an employment relationship but which is absent in a partnership (relying on *Bates*).

85. We find that ground 1 is misconceived. The Judge was not required to approach the question of which members of the Respondent had significant influence by the application of the observations of Elias LJ in *Bates* at [64] on the difference between an employee and a partner, or by the application of any other rigid test of this kind.

86. Rather, the Judge was required to apply the words of Condition B to the facts of this case, as he found them. The distinction between an employee and a traditional partner may be a useful tool in this exercise, but it does not determine the answer. The exercise of applying the words of Condition B to any particular case is an acutely fact sensitive exercise. It is perfectly possible to have employees of a particular LLP who exercise significant influence over the affairs of the partnership. It is also perfectly possible to have members of the partnership who exercise very little influence over the affairs of the partnership. It all depends upon the facts of the particular case.

87. In our view, and contrary to the Appellant's submission, the Judge was correct to consider the question of significant influence by considering what the members of BlueCrest did within the partnership. We find the submission that, in doing so, the Judge lost sight of the difference between the role of an employee and the role of a traditional partner is both wrong and misconceived.

88. The *"find, mind and grind"* role, which the Judge correctly identified as the role of a traditional partner, was a useful tool in applying the words of Condition B to the facts of this case. There was however no one correct methodology for the application of the wording of Condition B to the facts of the present case, which the Judge was either right or wrong to follow. This is not how the test in Condition B works.

89. Mr Vallat submitted that *"find, mind and grind"* was a description of what partners in a traditional law firm do, and was a description of what anyone in a professional services firm is likely to be doing, regardless of the structure adopted by that firm. As such, so Mr Vallat submitted, it was not a function of being a partner that these things were done. The difficulty with this submission is the one which we have already identified. The Judge did not apply a test of *"find, mind and grind"*. The Judge applied the wording of Condition B to the facts, as he found them. In considering the question of significant influence, and as part of his analysis of that question, the Judge found it helpful to look at the role of partners in a traditional partnership and, in particular, their *"find, mind and grind"* role. There was no failure here to consider adequately the distinction between a traditional partner and an employee, let alone a failure adequately to consider the statutory question of significant influence. The Judge, as he was entitled to do, simply found it helpful to his analysis to consider the role of a partner in a traditional partnership.

Ground 2

90. HMRC submit that the FTT erred in its construction of "*affairs*". It submits that the test of significant influence applies to the affairs of the LLP generally, looking at the business as a whole as opposed to one or more aspects. The FTT concluded, wrongly say HMRC, that the test is not "*restricted to the affairs if the partnership generally but can be over any aspect of the affairs of the partnership*" (at [178]). HMRC argue that the ordinary meaning of the words "*affairs of the*

partnership" required the FTT to consider the affairs generally. The FTT's approach erroneously wrote in the words "*any aspect*".

91. We do not accept this submission. In our view, to do so would be to write additional words into Condition B. The legislation requires, if Condition B is to be failed, that the relevant member be given significant influence over the affairs of the partnership. The reference is not to the entirety of the affairs of the partnership. We consider that this would, in any event, be a highly unrealistic approach: save possibly for small partnerships, with only a couple of members, one would expect the members of a partnership to have individual areas of responsibility within the business of the partnership. Whether those individual areas of responsibility amount to significant influence over the affairs of the partnership is a fact specific inquiry.

92. It also seems to us that if the relevant significant influence has to be over the entirety of the affairs of the relevant partnership, this would be capable of producing strange results. In terms of examples, it is easy to think of persons within a partnership, in particular a large partnership, who might exercise very significant influence over the affairs of the partnership, while only being responsible for and involved in a part of the affairs of the partnership. Equally, and again particularly in the case of a large partnership, it is easy to think of particular parts of the business of the partnership which would qualify as part of the affairs of the partnership, but would not be sufficiently important to the business of the partnership to require the involvement of those with significant influence within the partnership. In the case, at least, of any medium sized or large LLP, there might be only one or two persons who could, on HMRC's case, be said to exercise significant influence. It might only be the managing partner or senior partner who could be said to have significant influence over the entirety of the affairs of the partnership, and conceivably even that person might fail to satisfy a test of this kind.

93. Mr Vallat's answer to this was that Condition B was only one of the conditions to be met before a partner could be taxed as an employee. It was therefore not necessarily surprising that a large number of partners in a partnership would not exercise significant influence, within the meaning of Condition B, and would therefore meet Condition B. The other Conditions also needed to be satisfied. In principle, we accept the point that Condition B is only one of the Conditions to be met. We also accept the point that if the wording of one of the Conditions did have the effect that almost every partner in a partnership would meet that Condition, this could be said to be justified on the basis that there are the other Conditions which must be met before a partner can be taxed as an employee. All this has its limits however. We do not think that an argument of this kind can justify reading into a Condition a restriction which is not present in the Condition. Nor do we think that an argument of this kind can justify a situation where, if Mr Vallat is right, one would expect almost every partner in a partnership of any size to meet Condition B, by reason of not having significant influence over the entirety of the affairs of the relevant partnership.

94. As a matter of construction of the wording of Condition B, and as a matter of the purpose behind this legislation, we consider that the bar is set too high if the significant influence in Condition B is read only to mean significant influence over the entirety of the affairs of the relevant partnership.

95. Accordingly, we reject this Ground.

Ground 3

96. HMRC submit that the FTT erred in its construction of "*influence*". It submits that the influence required by the legislation is influence over the management of the partnership business and not financial influence or impact. The FTT concluded that "*influence*" was not so limited and could

include financial influence or impact or an ongoing contribution "*from an operational perspective*" (at [173]). HMRC submit that the FTT erroneously approached the test from the perspective of what an individual might do or impact an individual might have, as opposed to focussing on the statutory word "*influence*". A person with influence can, to a degree, shape the business, not merely contribute to it.

97. In arguing that the FTT's approach failed to recognise that contributions to the success of the partnership can be equally true of partners and senior employees alike, the Appellant highlighted the Judge's observations at [174] – [176]:

> "The role of a partner in a traditional partnership is to "find, mind and grind". In other words, a traditional partner is expected to go out and find work, supervise others to undertake it, and to do the work themselves. The extent of each depends on the role of the partner, his or her particular qualities, and the nature of the partnership. Some partners are better at getting work than doing it, others at doing and supervising it than getting it. But in my experience an individual who is made up to be a partner in a traditional partnership must demonstrate each of these qualities. These are not limited to making management decisions, but to contributing to the success of the partnership. In professional services firms it has always been (and in the current financial climate is certainly the case) crucial to attract top quality individuals and then spend time investing in those individuals, since by doing so, the intellectual capital of the partnership is enhanced. And it is, frankly, that intellectual capital which is sold by partners who are seeking to attract work from clients. Without developing that intellectual capital, the partnership would have a less certain future.
>
> Furthermore, a partner's role is to undertake the work which has been commissioned by a client, both individually and by supervising the team of individuals to whom that work has been delegated. That is management on a local basis, and is absolutely crucial to the success of the partnership. And in terms of risk management, supervision by the appropriate partner of work being done by the appropriate lead qualified and experienced individual is essential.
>
> And so by doing the work and supervising the appropriate team to do the work, the partner is able to bill the client and thus contribute to the ongoing commercial activities of the partnership."

98. Equating financial impact or operational contribution with influence, HMRC contend, results in an unworkable test which does not differentiate between the roles of employees and partners.

99. For the same reason as set out above in respect of Ground 2, we reject this argument. In our view, HMRC seek to import words into the statute and there is no warrant for demarcating particular types of activity as giving or not giving significant influence. The inquiry is a fact sensitive one. Responsibility for operational activities may give rise to significant influence. Financial performance and/or financial responsibility may give rise to significant influence. Managerial responsibility may give rise to significant influence. Again, this all depends upon the facts of the particular case.

100. In our view, to say, as HMRC do, that financial impact upon the business of the partnership cannot qualify as a source of significant influence is misconceived. Those with experience of working within or for a partnership will be aware that financial performance and/or financial responsibility usually equals "clout" in any partnership, or for that matter in any entity or organisation. The fact that this may not be so in every case simply highlights the fact sensitive nature of the inquiry required by Condition B, and the lack of realism in trying to demarcate what kind of activities can and cannot give rise to significant influence.

Ground 4

101. HMRC submit that the FTT erred in its construction of "*significant*" in failing to consider and/or apply the ordinary meaning of the term "*significant*" as a qualifier to the word "*influence*". The FTT failed to set out its approach to the word "*significant*" in general terms, however the Judge's comment at [194] that: *"$300 million over 10 years is, to my mind, significant. It is significant in absolute terms. It certainly cannot be said to be insignificant"* indicates that it considered the test to mean "not insignificant". The FTT also appeared to consider that significance can be identified in absolute terms rather than in the context of the particular business.

102. HMRC contend that the term "*significant*" must appreciably add to the concept of having "*influence*" with the result that there are (at least) three categories of influence:

i) Insignificant influence;

ii) Influence; and

iii) Significant influence.

103. It is said by HMRC that the FTT conflated (ii) and (iii) leaving "*significant*" as a redundant qualifier. Furthermore, the term must also be understood in the context of the LLP in question.

104. We consider that it would be a mistake to try to put a gloss on the expression "*significant influence*", either by imposing a tripartite distinction between insignificant influence, influence and significant influence or by trying to use the employee/partner distinction as a key to unlock the meaning of significant influence, or by any other means of construction.

105. There is no one size fits all approach to answering the Condition B question. Whether there is significant influence in the case of any individual member of a partnership depends upon the facts of the particular case. The present case is not a case where guidance is required for future cases, because there was no key issue of principle or construction at stake. What was at stake before the Judge, in this context, was whether the members of the Respondent met or failed Condition B, on the evidence before him.

106. We did not find HMRC's reliance on *HMRC v Pendragon* [2015] UKSC 37 [2015] 1 WLR 2838 assisted. Mr Vallat highlighted the function of the Upper Tribunal as ensuring that the FTT adopts a consistent approach to the determination of questions of principle. However, the present case bears no relation to *Pendragon* and we see no comparable issues with those considered by Lord Carnwath JSC at [47]-[51].

107. We observe, on the meaning of Condition B generally:

i) It is concerned with *"M"* which is defined to mean a member of a limited liability partnership in relation to which Section 863(1) applies. It follows that mere membership of a partnership cannot, of itself, constitute the significant influence referred to in Condition B. Something more than mere membership of the partnership is required.

ii) The use of the word *"significant"* has to be given effect. Something more than just influence is required. The influence must be significant.

iii) As we have said, we agree with Mr Vallat that all three of Conditions A, B and C must be met before a member of a partnership will be taxed as an employee. It is therefore

> necessary to be wary of an argument, of the kind which Ms Hardy advanced on day 2 of the hearing, to the effect that one would normally expect the member of, for example, a City firm of solicitors, to fail Condition B. A person whom one might think of as a conventional partner in a conventional partnership might well meet Condition B. If this was said to produce a wrong or unintended result, the answer would be that Conditions A and C must also be met. If such a person does meet Conditions A and C, one might think that this points to such a person not being a conventional partner in a conventional partnership, but a disguised employee, which is what the legislation is seeking to achieve.

108. We do not accept that the Judge made an error of construction in his application of the test of significant influence. The Judge clearly had in mind the need to find significant influence if Condition B was to be failed. The Judge's specific consideration of Condition B, starting at [168] and continuing through to [207] is littered with references to significant influence.

109. The futility of trying to argue that the Judge applied the wrong test is demonstrated by [194], which is worth setting out in full:

> "In my judgment, each individual portfolio manager with a capital allocation of $100 million does have significant influence over the affairs of the partnership. I say this from both a quantitative and qualitative perspective. As regards the former, and taking Mr Moore as an example, $300 million over 10 years is, to my mind, significant. It is significant in absolute terms. It certainly cannot be said to be insignificant. I think the same sort of level of overall returns will have been demonstrated by those portfolio managers with capital allocations of $100 million. They will have made a significant impact on the financial performance of the appellant. From a qualitative point of view, as I have already said, those portfolio managers who were made up to be members of the LLP, and thus in the same position as a partner in a traditional partnership, would have already demonstrated the personal managerial and operational qualities to justify that elevation, and that they were capable of performing the tripartite role of a partner, namely generating work, doing the work, and, if necessary, supervising work. These roles are absolutely fundamental to the core activity of the subinvestment manager, namely to maximise its sub-investment fees, and the evidence shows that these individual portfolio managers demonstrated "managerial clout" in the discussions with other portfolio managers concerning managerial and operational issues which, if necessary, were then ratified by the Board or UK ExCo. Each such individual's view was of significance, as was their influence."

110. Mr Vallat tried to suggest that the Judge had gone wrong in his reference to significance in absolute terms, and in his reference to influence which could not be said to be insignificant. However, [194] has to be read as a whole, and in context. On our reading, it is clear that the Judge was not saying that the fact of a person generating $300 million over ten years would equate to significant influence in all cases. He was simply observing, as was the case, that this was a significant sum of money. It is equally clear that the Judge was not misunderstanding what was meant by significant influence in his reference to $300 million not being insignificant. He was simply reiterating that $300 million was a significant sum of money, which is a perfectly reasonable observation.

111. The difficulties with Ground 4, and, we should add, with all those Grounds which seek to accuse the Judge of having gone wrong in his construction of Condition B are well illustrated by reading [194] in full. In particular, the last two sentences pose a significant problem for the Appellant for the following reason: Mr Vallat accepted that what one was looking for, in terms of significant influence, was *"managerial clout"*. Given that the Judge used just this phrase in considering from a "*qualitative point of view*" on the evidence before him whether the portfolio managers exercised significant

influence over the affairs of BlueCrest, it becomes extremely difficult to argue that the Judge misdirected himself in considering the question of who had significant influence and we reject this submission.

Ground 5

112. HMRC argue that the FTT failed to appreciate that any significant influence must ultimately derive from the LLP Agreement and failed to properly take into account the terms of that Agreement which left little room for the portfolio managers (and all members beyond the Board) to exercise influence over the affairs of the partnership.

113. HMRC highlight specific extracts from the LLP Agreement in support of its argument, for example Clause 14.1 which provides that the Board had responsibility for day-to-day management and control of the business and the affairs of the Partnership. It argues that although there may be circumstances in which an individual who does not hold a formal role in the management of the business may, as a matter of fact, wield considerable influence – for instance there can be no doubt that Mr Platt had significant influence above and beyond any formal role – the facts of the present appeal do not demonstrate that this was the case for portfolio managers, either individually or collectively.

114. It is correct to say that the focus of Condition B is on whether the mutual rights and duties of the members of the relevant partnership give an individual member significant influence over the affairs of the partnership. It was common ground in the present case that the Judge was entitled to consider the actual position and the inquiry was not restricted to the terms of the LLP Agreement.

115. This position was recorded by the Judge, at [188] (emphasis added):

> "Both parties accept that significant influence does not need to be exercised through a formal constitutional procedure, but requires a realistic examination of the facts. In the context of this appellant, the investment and operational decisions made by the portfolio managers demonstrate that they have influence over the affairs of the partnership notwithstanding that the portfolio managers themselves may not sit on any of the UK committees, the members of the Board, or are members of UK ExCo."

116. This remained the position in this hearing. Mr Vallat accepted that de facto influence was capable of qualifying as significant influence, within the meaning of Condition B.

117. Although this is, in our view, sufficient to dispose of Ground 5, the Judge in fact considered the evidence in significant detail, by reference to the LLP Agreement and the position on the ground, and came to the conclusion that the portfolio managers each exercised significant influence over the affairs of BlueCrest. It is clear that the LLP Agreement was not ignored, but the evidence of what had happened on the ground, in terms of who exercised significant influence, proved decisive in the decision of the Judge in relation to the portfolio managers. We note that the Judge undertook the same exercise in respect of the non-portfolio managers, and decided that they did meet Condition B. Accordingly, this Ground must fail.

Ground 6

118. HMRC submit that the FTT was wrong to apply the analogy with a traditional professional services firm in the way that it did, in particular referring to the role of a partner as being to "*find, mind and grind"* at [174]. To the extent that such an analogy is relevant, the portfolio managers were

limited to doing the work as they did not need to find work (the client was the Fund) nor did they, in most cases, need to supervise others.

119. We find that this Ground, in common with the remainder of the Appeal, does not respect the terms of the Decision. The reference to *"find, mind and grind"* is located in that section of the Decision where the Judge considered the argument of the Appellant that significant influence was limited to managerial influence. That section of the Decision contains part of the reasoning pursuant to which the Judge, quite correctly, rejected this argument of the Appellant. The Judge then proceeded, at [178], to reject the Appellant's argument that significant influence over the affairs of a partnership was restricted to significant influence over the affairs of the partnership generally. Having dealt with that argument, the Judge then proceeded to his lengthy and careful analysis of the evidence. Quite correctly, the Judge did not regard that analysis as depending upon his ability to find each of *"find, mind and grind"* on the part of each portfolio manager.

120.This Ground, in our view, attempts to force the test of Condition B into an artificial straitjacket and we prefer the submission by Ms Hardy that the question is a multi-factorial one, which requires a careful analysis of all aspects of the workings of the relevant partnership. We therefore reject this Ground.

Ground 7

121. HMRC submit that the FTT was wrong to conclude that the relevant portfolio managers had "*managerial clout*". The FTT conflated managerial and operational issues and its conclusions are inconsistent with the evidence of the witnesses (relying on *Edwards v Bairstow*).

122. For much the same reason as Ground 3, this Ground must fail. There is nothing in the wording of Condition B which restricts the types of activity or sources of influence within a partnership which can be considered for the purposes of deciding whether an individual meets or fails Condition B.

123. At [194] the Judge found on the evidence that the portfolio managers had demonstrated managerial clout. On HMRC's own case, this was the significant influence that the statute required and the very thing which the Judge was supposed to be looking for. We cannot see how it can be said that the Judge went wrong or misdirected himself, unless it was the case that the evidence did not exist to support this finding.

124.There is a high threshold for a successful *Edwards v Bairstow* challenge. The difficulty for HMRC is that we were taken to a few selected extracts from cross-examination before the FTT which, Mr Vallat submits, demonstrate that the Judge reached a finding that was not open to him.

125.As set out above at paragraph [65], the witness evidence was heard over two and a half days, in addition to the substantial volume of documentary evidence which was considered by the Judge. The limited extracts to which we were referred are, in our view, an example of "island hopping", as warned against by Lewison LJ in *Fage*. In those circumstances, we are in no position to conclude that the Judge was wrong in his findings on managerial clout. The Judge heard all the evidence. We have not. We have been taken to a few selected extracts from the cross-examination. The futility of the process was illustrated by the fact that Ms Hardy took us to her own extracts from the evidence, which supported the Judge's findings of managerial clout. Without being taken through all the same material at this hearing, we consider that we are in no position to interfere with findings of fact made by the Judge. We consider that this Ground falls far short of demonstrating an error of law on the basis of *Edwards v Bairstow* and we have no hesitation in rejecting it.

126. We also note that HMRC appeared to us to refer to the evidence before the Judge in a manner analogous to reliance on pleadings, whereby the HMRC's extracts from the evidence must be taken as decisive, unless challenged as to their effect by BlueCrest. As it happens, BlueCrest did make its own references to the evidence below which, unsurprisingly, made it clear that we would have been wrong to accept HMRC's argument that the Judge made irrational findings of fact on the question of managerial clout. Even if, however, BlueCrest had not referred us to other extracts from the cross-examination, we do not accept that we were bound to accept HMRC's extracts as comprising the totality of the relevant evidence on the question of whether the portfolio managers had managerial clout.

127. Finally, in relation to this Ground we were invited by Mr Vallat, on the basis of *Pendragon*, to give some indication as to how the FTT should approach the weighing exercise in relation to the question of significant influence. For the reasons which we have set out in our analysis of Ground 4, we do not regard it as either necessary or appropriate to take this step.

Ground 8

128. HMRC submit that the FTT's findings in relation to "*involvement*" in operational decisions were not sufficient to demonstrate significant influence of the type required by Condition B. The operational activities identified by the FTT were:

i) Hiring and firing;

ii) Identifying and exploiting new business opportunities;

iii) Bringing on junior members of staff; and

iv) Managing counterparty relationships.

129. HMRC submit that the evidence submitted by the Respondent did not meet the burden of proof in demonstrating that any operational contribution by each portfolio manager was significant.

130.We consider that this assertion is no more than an attempt to re-argue the evidential case which was before the Judge. The Judge was satisfied, on the evidence before him, that the portfolio managers did have significant influence over the affairs of the Respondent. For the reasons set out at [125] above, we consider that HMRC's exercise of "island hopping" through selected extracts from the evidence before the FTT provides no basis for interfering with the Judge's conclusions. The Judge heard and read all of the evidence and we do not consider that we are in any position to conclude that the Judge erred in his findings, which were based on a careful and thorough analysis of the evidence. The futility of this process was, again, illustrated by the fact that Ms Hardy took us to her own extracts from the evidence, which supported the Judge's findings of significant influence.

131. In so far as this Ground relies upon findings made in the Decision, HMRC contends that the Judge made findings of activities in which employees at various levels of seniority might be involved. In our view, the answer to this is twofold.

132.First, the Judge made his findings in relation to the portfolio managers on the basis of all the evidence which he received and heard, which is reviewed and analysed at [168] to [195] of the Decision. The Judge then turned to the position of non-portfolio managers, at [196]. The Judge's analysis took all the evidence and all his findings into account. The Judge's reasoning was not based simply upon the paragraphs relied upon by the Appellant for the purposes of Ground 8. An example

of this is [190], in which the Judge dealt with the submission that operational activities were insufficient to demonstrate significant influence:

> "Mr Vallat suggests that in undertaking the operational activities mentioned above, they were doing no more than what was required of them in their role as portfolio managers, and to demonstrate significant influence, they need to do more. I can see no principled justification for this submission. I bear in mind that it is HMRC's view that the salaried member rules are intended to apply to members who are more like employees than partners in a traditional partnership. And to my mind the activities undertaken by the portfolio managers are directly analogous to those activities carried out by partners in a traditional partnership. They cultivate existing client relationships with their counterparties; they generate new work either by new product lines or tinkering with existing product lines; they undertake investment activities themselves; and, for those where there is a joint book, they actually conduct joint investment activities with junior members of staff. The evidence also shows that they disseminate their experience to junior members of staff, something which is fundamental to the role of a partner in a traditional partnership. So by undertaking their core role, they are acting as a partner would in a traditional partnership."

133. In addition to rejecting this argument, so far as it was an argument based on the construction of Condition B, the Judge also made a series of findings in relation to the activities carried out by portfolio managers, which he considered *"directly analogous to those activities carried out by the partners in a traditional partnership"*. We do not find any error of law in this approach, particularly given the stress laid by HMRC on the distinction between an employee and a partner in a traditional partnership.

134. Second, HMRC's argument assumes that any activity in which an employee might be involved cannot qualify as an activity to be taken into account when considering the question of significant influence. In our view, this is plainly wrong. The activities to be considered, when answering the Condition B question, are not demarcated or ring fenced in this way. The fact that a particular activity may be one normally carried out by an employee may be a factor which assists in determining whether a particular activity constitutes a source of significant influence within a partnership, but all depends upon the facts of the particular case.

Ground 9

135. HMRC assert that the FTT was wrong to conclude that a capital allocation of $100 million was sufficient evidence to demonstrate significant influence. HMRC contend that financial impact is not, on its own, sufficient to demonstrate "*influence*" of the type required by Condition B. Furthermore, to the extent that it is relevant, the Judge was wrong to apply a threshold of $100 million in capital allocation to the determination of whether significant influence had been demonstrated.

136. The difficulty for HMRC is that the Judge did not rely on financial impact alone. The Judge decided that the portfolio managers exercise significant influence for all the reasons set out in his discussion at [168]-[195]. Essentially, the Judge found that the activities carried out by portfolio managers with a capital allocation of $100 million or more did mean that they exercised significant influence (see [194]). Indeed, in the case of desk heads the Judge found that they exercised significant influence without making express reference to a specific level of capital allocation (at [195]). So far as the Judge did rely, as part of his reasoning, on capital allocation, we consider that this was a matter for the Judge, who heard and read all of the evidence.

137. The problem with Ground 9 and, it may be said with the Appeal generally, are well encapsulated in the following assertions in paragraph [111] of the Appellant's skeleton argument:

> "The level of capital allocation does not demonstrate that the individual has influence (significant or otherwise) akin to that of a typical partner in a traditional partnership, nor is it apparent why being on one side or the other of the $100m capital allocation 'threshold' should demarcate significant influence, rather than demonstrating the level of skill at investment management."

138. These assertions treat the Judge's decision on portfolio managers as depending upon a demarcation line of a $100 million capital allocation. This misrepresents the Judge's reasoning in relation to the influence exercised by portfolio managers, which was based upon all his findings as to the activities of portfolio managers. In the case of those portfolio managers with capital allocations of $100 million or more, the Judge was satisfied that their activities within the Respondent constituted significant influence upon the affairs of the Partnership. In our view, this was pre-eminently a matter for the Judge. Accordingly, the question of why being on one side of the line rather than the other should demarcate significant influence is a false question. It misrepresents the reasoning of the Judge. The actual reasons why the Judge thought that portfolio managers with capital allocations of $100 million or more did exercise significant influence are to be found in the Decision, and are summarised in [194]. They do not depend simply on a crude dividing line of $100 million of capital allocation.

139. Ground 9 also accuses the Judge of having erred in referring to returns made by portfolio managers as returns for the Respondent, as opposed to the Fund (as defined in the Decision). It is not clear from the Paragraphs referred to by the Appellant in this context ([95] and [194]) that the Judge did make this mistake.

140. In summary, we reject the arguments of HMRC in support of Ground 9.

Analysis – the Cross-Appeal

Ground 1

141. Ground 1 avers that the Judge erred in his construction of and approach to Condition A. The main thrust of the Respondent's argument is that the Judge set the bar too high, in terms of the link required between the remuneration paid to each member of the Respondent and the profits or losses of the Respondent. The wording of Paragraph (b) and Paragraph (c) within "*step 2*" of section 863B(3) is widely expressed, and is wide enough, so it is argued, to include a situation where the link exists because the relevant remuneration is limited by the amounts of profits or losses made by the relevant partnership.

142. The Respondent argues that the FTT was wrong to find as a matter of law that: "*the mechanism [for remunerating individual members] does not, in terms, entitle a portfolio manager [or any other member] to share in a proportion of the overall partnership profits*" ([140]). Furthermore, the FTT was wrong to conclude that the possibility of risks or losses is not *"relevant to the basis on which the profits of the partnership are distributed between its members"* (at [141]).

143. We consider that this is essentially a question of construction which should not be considered in the abstract, but rather it is better considered by reference to the circumstances of the present case.

144. The only contractual link between discretionary allocations and profits or losses of the Respondent to which Ms Hardy was able to direct us was Clause 10.8. All that Clause 10.8 does, in very crude terms, is to give the Respondent the ability to limit discretionary allocations, by clawing back Discretionary Drawings, where losses are incurred by the Respondent.

145. It is clear from the Judge's findings that discretionary allocations were not tied to the overall profits or losses of the partnership; they were the subject of independent calculation as stated at [138] and [140]:

> "I agree with Mrs Hardy when she says that there is no need for the individual members' remuneration to "track" the appellant's overall profits and losses. By this I think she means that there is no need for the profits of the remuneration of the individual members to increase if the overall profits and losses of the partnership increase. One of Mr Vallat's points was that the evidence clearly shows (which it does) that the individual portfolio managers might make losses on their individual profit and loss accounts even if the appellant made an overall profit and even if other portfolio managers made a profit on their individual profit and loss accounts. But having agreed with her on this point, I also agree with Mr Vallat that the appellant must show that there is a link between an individual's remuneration on the one hand and the overall profits and losses on the other. And that link cannot simply be that if there were fewer profits available for distribution, an individual member would receive a lesser amount.
>
> …
>
> But the difficulty faced by Mrs Hardy is that, whilst it is clear that the bonus of the portfolio managers varies, it varies by reference to their own personal performance. And although the initial bonus might then abate when the profits of the appellant are finally determined, and the overall total of those initial allocations is found to be equal to or greater than the accounting profit, she has not made out that the allocations are, essentially, variable and are computed by reference to, that overall profit. They are computed by reference to individual performance. There is no evidence that I have seen that the mechanism of computing the portfolio manager's bonus is intended to establish the share of the overall profits of the partnership to which the individual is entitled any more than computing an employee's bonus. Clearly there must be accounting profits to distribute, and equally clearly, if there are insufficient accounting profits to satisfy the bonuses, they will be abated in some way. But the mechanism does not, in terms, entitle a portfolio manager to share in a proportion of the overall partnership profits. On the one hand, there is the individual's profit and loss account. On the other, there are the accounting profits of the partnership. But it seems to me that the first is calculated without reference to the variability of the second for the reasons I have given above."

146. Profits or losses only came into the calculation by way of the obvious point that discretionary allocations, once calculated, could only be paid to the extent that there were profits out of which they could be paid as noted by the Judge at [152]:

> "…. It goes to the point made above, namely that if there are insufficient profits to fulfil the portfolio managers' preliminary allocations, then those allocations must reduce. You cannot dish out more than the accounting profits dictate."

147. The link found by the Judge was therefore a practical link. Discretionary allocations, once calculated, could only be paid to the extent that there were profits out of which they were paid. This link might also be said to be a contractual link, given the terms of Clause 10.8, but this contractual link did no more than reflect the practical link.

148. The Judge concluded that a link of this kind was insufficient to place the discretionary allocations outside the terms of either Paragraph (b) or Paragraph (c) of s 863B.

149. In our view, the actual question to be answered, in relation to Condition A, is whether it is reasonable to expect that at least 80% of the relevant remuneration payable will be disguised salary;

meaning (in the present case) remuneration falling within Paragraph (b) or Paragraph (c). The Condition A question is therefore concerned with what it is reasonable to expect. This question has to be answered at the relevant time, as defined in Section 863B(3). As we understood the submissions of the parties, this meant, in the present case, looking at the position on a year-by-year basis.

150. Given the link found by the Judge, the question of what it was reasonable to expect fell to be considered at two levels:

i) First there was the question of whether the possibility of the discretionary allocations being affected by the amount of profits or losses, either on a contractual basis or on a practical basis, was capable of being a sufficient link for the purposes of placing the discretionary allocations outside Paragraph (b) and Paragraph (c). If it was not, then it was *"reasonable to expect"* (indeed inevitable) that the discretionary allocations would fall within Paragraph (b) and Paragraph (c).

ii) If, however, the link found by the Judge was capable of being a sufficient link for the purposes of placing the discretionary allocations outside Paragraph (b) or Paragraph (c), this did not necessarily mean that the discretionary allocations actually fell outside Paragraph (b) or Paragraph (c). The question which, it may be said, then arose was whether it was reasonable to expect that the discretionary allocations for the relevant year would actually be affected by profits or losses, which in turn depended upon what it was reasonable to expect for the relevant year, in terms of whether there would be sufficient profits to pay discretionary allocations. It could be argued that if it was reasonable to expect, for the relevant year, that there would be sufficient profits available to pay the discretionary allocations, the link found by the Judge would not take effect, with the consequence that the discretionary allocations would fall within Paragraph (b) or Paragraph (c). This second question could only however be answered if findings of fact were made, for each relevant year, as to what it was reasonable to expect, in terms of the availability of profits to pay discretionary allocations.

151. The Judge made clear findings on the question at (i) above. The Judge decided that the link which existed was the obvious one that the amount of a discretionary allocation, once calculated, might be affected by there being insufficient profits to pay that discretionary allocation. The Judge did not think that a link of this kind was sufficient to take the discretionary allocations outside Paragraph (b) or Paragraph (c).

152. The Judge's findings on the question at (ii) above are encapsulated within the same reasoning. The wording of Paragraph (b) and Paragraph (c) is open in its terms. Paragraph (b) requires that variation be without reference to the overall amount of profits and losses. This, it can be said, clearly requires something more than the possibility of there being insufficient profits to pay discretionary allocations. The Judge made a clear finding, at [140], that discretionary allocations were calculated without reference to the variability of profits. Profits could only become relevant, at a second or separate stage, if it turned out that they were insufficient to pay the discretionary allocations already calculated.

153. We consider that the wording of Paragraph (b) is not wide enough to encompass an indirect relationship of this kind; comprising the two stages found by the Judge set out above. What the legislation is seeking to do, in both Paragraph (b) and Paragraph (c), is to isolate payments of the kind one would find in a traditional partnership, where the partners share in profits and losses. There may be many ways of organising the sharing process, but the essential point is that each partner receives a share of the profits or shoulders a share of the losses. The partners' remuneration is thus tied to

whatever amount of profits is realised, or whatever amount of losses is incurred. The FTT's finding in [140], that discretionary allocations were calculated without reference to profits or losses, amounts to variation without reference to the overall amount of profits and losses, as referred to in Paragraph (b).

154. The wording of Paragraph (c) is more open by inclusion of the phrase: "*not, in practice, affected by"*. It seems to us clear that this wording was intended to encompass a less direct relationship between remuneration and overall profits and losses than that contemplated by Paragraph (b), otherwise Paragraph (c) would serve no useful purpose.

155. Returning to the Judge's finding at [140], if discretionary allocations were set without reference to overall profits and losses, we cannot see that discretionary allocations: *"were, in practice, affected"* by the overall amount of profits and losses. The question of whether there were going to be sufficient funds to pay the discretionary allocations, once set, is a separate question, and not one affecting the amount of the discretionary allocations.

156. Even if we are wrong in construing the statutory requirement in this way, we note that the burden rested with the Respondent to demonstrate to the Judge that it was reasonable to expect that the discretionary allocations calculated for the relevant years would be affected by a reduction in profits or the incurring of losses. Although we consider that the Decision could have been clearer in this respect, we are satisfied that the Judge gave adequate reasoning in the Decision to constitute sufficient findings that the Respondent failed to discharge this burden, both for portfolio managers (see [143], [144] – [146], [154] and [156] and non-portfolio managers (see [160]-[162]).

157. In summary, we consider that the threshold test in Paragraph (b) and in Paragraph (c) is set fairly widely. In the case of the discretionary allocations however, the Respondent was unable to show the link required to take the discretionary allocations outside Paragraph (b) or Paragraph (c), either as a matter of construction or on the evidence.

Ground 2

158. Ground 2, in summary, is that the Judge came to a decision on Condition A which was irrational and which no reasonable tribunal could have come to on the evidence. The FTT did not apply the evidence of the witnesses, for example regarding the different processes for remuneration.

159. As we noted earlier, there is a high threshold to meet in an *Edwards v Bairstow* appeal.

160. We do not think it is necessary to set out each criticism particularised in the Respondent's Grounds of Appeal. We consider that the Respondent, in reality, seeks to do the same as the Appellant in relation to Grounds 5-9 of the Appeal; namely to re-argue the evidential case before the Judge, by reference to selected extracts from the cross-examination. This was another exercise in "island hopping". The Judge heard all the evidence, and made the findings based upon that evidence. We have considered each of the extracts relied upon by the Respondent and we conclude that the Judge was fully entitled on the material before him to make the factual findings that he did. The extracts highlighted by the Respondent ignore the totality of the evidence and there are no grounds for us to interfere with the Judge's findings.

A comment on the Appeal and Cross-Appeal

161. We observe that the Appeal and, albeit to a lesser extent, the Cross-Appeal both proceeded on the implicit assumption that there was no difficulty in our delving into and overturning detailed

findings of fact made by the Judge, in a lengthy and carefully reasoned decision, following half a day of opening, two and a half days of oral evidence, not far short of four days of closing submissions, and scrutiny of the contents of a trial bundle running to thousands of pages of documents.

162. The reality was, and is that, in the absence of the Judge making some mistake in his construction of and approach to the Condition B question and/or the Condition A question, it was always going to be a difficult task to persuade this tribunal, as an appeal tribunal, that the Judge had made an error in his findings of fact of the kind which would permit this tribunal to interfere with those findings. This was borne out in the relevant parts of the oral argument, which illustrated the wisdom of what was said by Lewison LJ in *Fage*.

163.We consider it appropriate to return to the words of Lady Hale DPSC in *Bates* in the Supreme Court at [39], and to note that, in the present case, the Judge did what he was required to do, namely applying the words of the statute to the facts of this case, as he found them to be.

Conclusion

164. We have set out above our reasons for concluding why the Appeal and Cross-Appeal should be dismissed. Returning to the FTT's Decision, having carefully analysed the evidence, both oral and documentary, the Judge made extensive findings of fact. With the purpose of the legislation in mind, the Judge construed the legislation and applied the Conditions in issue to the facts as found. The Judge's reasoning on Condition A was summarised at [161] and [162]

> "The evidence does not demonstrate a link between the variable remuneration on the one hand and the profits of the partnership on the other. Whilst I appreciate, as does Mr Vallat, that the variable remuneration calculation for non-portfolio managers takes into account the financial performance and future financial stability of the appellant, that is very different from demonstrating a link to that calculation and the appellant's profits.
>
> There is no evidence that either during the iterative process of establishing the preliminary discretionary allocation, nor during the process of the Board approving it and thus making it final, that the profits of the appellant were taken into account, other than to the extent that the Board was fettered by the accounting profits which had been reported for the relevant financial year. There is no evidence that the discretionary allocations for the non-portfolio managers were capable of variation by reference to the profits of the LLP."

165. The Judge's conclusion on Condition B is summarised at [194] in relation to portfolio managers (above at [104]), [206] and [207] (in relation to non-portfolio managers):

> "As I have set out above, it is my view that financial contribution is a factor in wielding significant influence, and that is the submission made by Mrs Hardy. And whilst it is possible in empirical terms to identify the financial contributions made by the portfolio managers, I am not in the position to come to a conclusion regarding the financial contributions of those supplying the back-office services, since I simply have no evidence before me of those financial contributions. I do not know, for example, the amount generated by the head of legal, or the legal team. Nor by the tax department, nor by the IT department. My understanding is that, for transfer pricing purposes, they were cross charged on an arm's length basis using an appropriate transfer pricing methodology. But I have no evidence of the precise amounts of cross charges which are attributable to the individuals or departments.
>
> I am therefore unable to determine what financial or other contributions were made by the non-portfolio managers to the provision of the external services provided by the

> appellant to other members of the Group and which comprise a significant element of its overall activities. I am therefore forced to the conclusion that no non-portfolio manager exercised significant influence over those affairs of the appellant."

166. In conclusion, the Judge decided that:

i) All members meet Condition A because their remuneration from the LLP is not variable by reference to the profits or losses of the Partnership because the link between the profits and/or losses and the discretionary allocations is insufficient;

ii) The portfolio managers with capital allocations of $100 million or more and the desk heads do not meet Condition B because they have significant influence over the affairs of the Partnership as a result of the activities they carry out within the LLP which includes managerial as well as financial influence;

iii) The other portfolio managers and non-portfolio managers (other than the Original ExCo) meet Condition B because they do not have significant influence over the affairs of the Partnership.

167. We consider that the FTT made findings of fact that it was perfectly entitled to make and that there was no error of law in its approach to and construction of the legislation, or in its application of the legislation to the facts of the present case, as found by the FTT.

Decision

168. For the reasons set out above, our conclusion is as follows:

(1) The Appeal should be dismissed.

(2) The Cross-Appeal should be dismissed.

RELEASE DATE: 18 September 2023

APPENDIX

Income tax

1. The relevant legislation is set out in the following sections of the Income Tax (Trading and Other Income) Act 2005 ("ITTOIA"):

863 Limited liability partnerships

(1) For income tax purposes, if a limited liability partnership carries on a trade, profession or business with a view to profit–

> (a) all the activities of the limited liability partnership are treated as carried on in partnership by its members (and not by the limited liability partnership as such),
>
> (b) anything done by, to or in relation to the limited liability partnership for the purposes of, or in connection with, any of its activities is treated as done by, to or in relation to the members as partners, and
>
> (c) the property of the limited liability partnership is treated as held by the members as partnership property.
>
> References in this subsection to the activities of the limited liability partnership are to anything that it does, whether or not in the course of carrying on a trade, profession or business with a view to profit.

(2) For all purposes, except as otherwise provided, in the Income Tax Acts–

> (a) references to a firm or partnership include a limited liability partnership in relation to which subsection (1) applies,

(b) references to members or partners of a firm or partnership include members of such a limited liability partnership,

(c) references to a company do not include such a limited liability partnership, and

(d) references to members of a company do not include members of such a limited liability partnership.

(3) Subsection (1) continues to apply in relation to a limited liability partnership which no longer carries on any trade, profession or business with a view to profit–

(a) if the cessation is only temporary, or

(b) during a period of winding up following a permanent cessation, provided–

(i) the winding up is not for reasons connected in whole or in part with the avoidance of tax, and
(ii) the period of winding up is not unreasonably prolonged.

This is subject to subsection (4).

(4) Subsection (1) ceases to apply in relation to a limited liability partnership–

(a) on the appointment of a liquidator or (if earlier) the making of a winding-up order by the court, or

(b) on the occurrence of any event under the law of a territory outside the United Kingdom corresponding to an event specified in paragraph (a).

863A Limited liability partnerships: salaried members

(1) Subsection (2) applies at any time when conditions A to C in sections 863B to 863D are met in the case of an individual ("M") who is a member of a limited liability partnership in relation to which section 863(1) applies.

(2) For the purposes of the Income Tax Acts—

(a) M is to be treated as being employed by the limited liability partnership under a contract of service instead of being a member of the partnership, and

(b) accordingly, M's rights and duties as a member of the limited liability partnership are to be treated as rights and duties under that contract of service.

(3) This section needs to be read with section 863G (anti-avoidance).

863B Condition A

(1) The question of whether condition A is met is to be determined at the following times—

(a) if relevant arrangements are in place—

(i) at the beginning of the tax year 2014-15, or

(ii) if later, when M becomes a member of the limited liability partnership,

at the time mentioned in sub-paragraph (i) or (ii) (as the case may be);

(b) at any subsequent time when relevant arrangements are put in place or modified;

(c) where—

(i) the question has previously been determined, and

(ii) the relevant arrangements which were in place at the time of the previous determination do not end, and are not modified, by the end of the period which was the relevant period for the purposes of the previous determination (see step 1 in subsection (3)),

immediately after the end of that period.

(2) "Relevant arrangements" means arrangements under which amounts are to be, or may be, payable by the limited liability partnership in respect of M's performance of services for the partnership in M's capacity as a member of the partnership.

(3) Take the following steps to determine whether condition A is met at a time ("the relevant time").

Step 1

Identify the relevant period by reference to the relevant arrangements which are in place at the relevant time. *"The relevant period"* means the period—

(a) beginning with the relevant time, and

(b) ending at the time when, as at the relevant time, it is reasonable to expect that the relevant arrangements will end or be modified.

Step 2

Condition A is met if, at the relevant time, it is reasonable to expect that at least 80% of the total amount payable by the limited liability partnership in respect of M's performance during the relevant period of services for the partnership in M's capacity as a member of the partnership will be disguised salary. An amount within the total amount is "disguised salary" if it—

(a) is fixed,

(b) is variable, but is varied without reference to the overall amount of the profits or losses of the limited liability partnership, or

(c) is not, in practice, affected by the overall amount of those profits or losses.

(4) If condition A is determined to be met, or not to be met, at a time, the condition is to be treated as met, or as not met, at all subsequent times until the question is required to be re-determined under subsection (1)(b) or (c).

(5) In this section "arrangements" includes any agreement, understanding, scheme, transaction or series of transactions (whether or not legally enforceable).

863C Condition B

Condition B is that the mutual rights and duties of the members of the limited liability partnership, and of the partnership and its members, do not give M significant influence over the affairs of the partnership.

863D Condition C

(1) Condition C is that, at the time at which it is being determined whether the condition is met ("the relevant time"), M's contribution to the limited liability partnership (see sections 863E and 863F) is less than 25% of the amount given by subsection (2) (subject to subsection (7)).

(2) That amount is the total amount of the disguised salary which, at the relevant time, it is reasonable to expect will be payable by the limited liability partnership in respect of M's performance during the relevant tax year of services for the partnership in M's capacity as a member of the partnership. In this section "the relevant tax year" means the tax year in which the relevant time falls and an amount is "disguised salary" if it falls within any of paragraphs (a) to (c) at step 2 in section 863B(3).

(3) The question of whether condition C is met is to be determined—

(a) at the beginning of the tax year 2014-15 or, if later, the time at which M becomes a member of the limited liability partnership;

(b) after that, at the beginning of each tax year.

(4) If in a tax year—

(a) there is a change in M's contribution to the limited liability partnership, or

(b) there is otherwise a change of circumstances which might affect the question of whether condition C is met,

the question of whether the condition is met is to be re-determined at the time of the change. This subsection is subject to section 863F(3).

(5) If condition C is determined to be met (including by virtue of subsection (7)), or not to be met, at the relevant time, the condition is to be treated as met, or as not met, at all subsequent times until the question is required to be re-determined under subsection (3)(b) or (4).

(6) Subsection (7) applies if—

(a) the relevant time coincides with an increase in M's contribution to the limited liability partnership, and

(b) apart from subsection (7), that increase would cause condition C not to be met at the relevant time.

(7) Condition C is to be treated as met at the relevant time unless, at that time, it is reasonable to expect that condition C will not be met for the remainder of the relevant tax year (ignoring this subsection).

(8) If there are any excluded days in the relevant tax year (see subsections (9) to (11)), in subsection (1) the reference to M's contribution to the limited liability partnership is to be read as a reference to that contribution multiplied by the following fraction—

(D − E) / (D)

where—

D is the number of days in the relevant tax year, and

E is the number of excluded days in the relevant tax year.

(9) Any day in the relevant tax year—

(a) which is before the day on which the relevant time falls, and

(b) on which M is not a member of the limited liability partnership,

is an "excluded" day for the purposes of subsection (8).

(10) If, at the relevant time, it is reasonable to expect that M will not be a member of the limited liability partnership for the remainder of the relevant tax year, any day in the relevant tax year—

(a) which is after the day on which the relevant time falls, and

(b) on which it is reasonable to expect that M will not be a member of the limited liability partnership, is an "excluded" day for the purposes of subsection (8).

(11) If the relevant time coincides with an increase in M's contribution to the limited liability partnership, any day in the relevant tax year—

(a) which is before the day on which the relevant time falls, and

(b) on which condition C is met, is an "excluded" day for the purposes of subsection (8).

(12) In subsections (6) and (11) references to an increase in M's contribution to the limited liability partnership include (in particular)—

(a) the making of M's first contribution to the capital of the limited liability partnership, and

(b) M being treated as having made a contribution by section 863F(2).

863G Anti-avoidance

(1) In determining whether section 863A(2) applies in the case of an individual who is a member of a limited liability partnership, no regard is to be had to any arrangements the main purpose, or one of the main purposes, of which is to secure that section 863A(2) does not apply in the case of—

(a) the individual, or

(b) the individual and one or more other individuals.

(2) Subsection (4) applies if—

(a) an individual ("X") personally performs services for a limited liability partnership at a time when X is not a member of the partnership,

(b) X performs the services under arrangements involving a member of the limited liability partnership ("Y") who is not an individual,

(c) the main purpose, or one of the main purposes, of those arrangements is to secure that section 863A(2) does not apply in the case of X or in the case of X and one or more other individuals, and

(d) in relation to X's performance of the services, an amount falling within subsection (3) arises to Y in respect of Y's membership of the limited liability partnership.

(3) An amount falls within this subsection if—

(a) were X performing the services under a contract of service by which X were employed by the limited liability partnership, and

(b) were the amount to arise to X directly from the limited liability partnership, the amount would be employment income of X in respect of the employment.

(4) If this subsection applies, in relation to X's performance of the services, X is to be treated on the following basis—

(a) X is a member of the limited liability partnership in whose case section 863A(2) applies,

(b) the amount arising to Y arises instead to X directly from the limited liability partnership,

(c) that amount is employment income of X in respect of the employment under section 863A (2) accordingly, and

(d) neither that amount, nor any amount representing that amount, is to be income of X for income tax purposes on any other basis.

(4A) Section 863A (2) does not apply in the case of a member of a limited liability partnership if, apart from this subsection, it would apply in consequence of arrangements the main purpose, or one of the main purposes, of which is to secure that section 850C does not apply for one or more periods of account in relation to—

(a) the member, or

(b) the member and one or more other members of the limited liability partnership.

(5) In this section *"arrangements"* includes any agreement, understanding, scheme, transaction or series of transactions (whether or not legally enforceable).

National Insurance Contributions ("NICs"):

2. Under the Social Security Contributions and Benefits Act 1992 ("SSCBA 1992"):

4A Limited liability partnerships

(1) The Treasury may, for the purposes of this Act, by regulations—

(a) provide that, in prescribed circumstances—

(i) a person ("E") is to be treated as employed in employed earner's employment by a limited liability partnership (including where E is a member of the partnership), and

(ii) the limited liability partnership is to be treated as the secondary contributor in relation to any payment of earnings to or for the benefit of E as the employed earner;

(b) prescribe how earnings in respect of E's employed earner employment with the limited liability partnership are to be determined (including what constitutes such earnings);

(c) provide that such earnings are to be treated as being paid to or for the benefit of E at prescribed times.

(2) Regulations under subsection (1) may modify the definition of "*employee*" or "*employer*" in section 163, 171, 171ZJ, 171ZS or 171ZZ14 below as the Treasury consider appropriate to take account of any provision falling within subsection (1)(a) to (c).

(3) If—

(a) a provision of the Income Tax Acts relating to limited liability partnerships or members of limited liability partnerships is passed or made, and

(b) in consequence, the Treasury consider it appropriate for provision to be made for the purpose of assimilating to any extent the law relating to income tax and the law relating to contributions under this Part,

the Treasury may by regulations make that provision.

(4) The provision that may be made under subsection (3) includes provision modifying any provision made by or under this Act.

(5) Regulations under this section are to be made with the concurrence of the Secretary of State.

(6) Section 4(4) of the Limited Liability Partnerships Act 2000 does not limit the provision that may be made by regulations under this section.

3. Under the Social Security Contributions (LLP) Regulations 2014 ("SSC(LLP)R 2014"):

3.— Salaried members of LLPs: Great Britain

(1) This regulation applies where—

(a) for the purposes of the Income Tax Acts an individual is treated by section 863A of ITTOIA 2005 (limited liability partnerships: salaried members) as being employed by an LLP under a contract of service, including where that is the case by virtue of section 863G of ITTOIA 2005 (anti-avoidance), ("the deemed tax employment"); and

(b) if the services performed, or to be performed, by the individual as a member of the LLP in the relevant period (as defined in section 863B(3) of ITTOIA 2005) were actually performed (or to be performed) under a contract of service with the LLP, the employment under that contract of service would be employment in Great Britain.

(2) For the purposes of SSCBA 1992—

(a) the individual ("the salaried member") is to be treated as employed in employed earner's employment by the LLP (being the deemed tax employment);

(b) any amount treated by virtue of section 863A or 863G(4) of ITTOIA 2005 as employment income from the deemed tax employment, other than employment income under Chapters 2 to 11 of Part 3 of ITEPA 2003 (the benefits code), is to be treated as an amount of earnings paid to or for the benefit of the salaried member in respect of the salaried member's employed earner's employment with the LLP;

(c) the secondary contributor in relation to those earnings is the LLP; and

(d) in the case of an amount of earnings which is an amount of employment income by virtue of section 863G(4) of ITTOIA 2005, the earnings are to be treated as being paid by the LLP to the salaried member when the amount mentioned in section 863G(2)(d) of that Act arises.

(3) The reference in paragraph (1)(b) to services performed (or to be performed) by the individual as a member of the LLP includes services personally performed by the individual for the LLP under arrangements by virtue of which section 863G(4) of ITTOIA 2005 applies.

(4) The definitions of "*employer*" and "*employee*" in—

(a) section 163 (interpretation of Part 11 and supplementary provisions);

(b) section 171 (interpretation of Part 12 and supplementary provisions);

(c) section 171ZJ (Part 12ZA: supplementary); and

(d) section 171ZA (Part 12ZB: supplementary)

of the SSCBA 1992 have effect as if the salaried member were gainfully employed in Great Britain by the LLP under a contract of service with the earnings mentioned in paragraph (2)(b).