UT Neutral citation number: [**2026] UKUT 00025 (TCC)**

UT (Tax & Chancery) Case Numbers: UT-2024-000100
UT-2024-000099

Upper Tribunal
(Tax and Chancery Chamber)

At the Rolls Building, London

INCOME TAX AND CAPITAL GAINS TAX – Limited Liability Partnership - whether amounts identified as "capital interests" were income or capital – if income, whether within Condition X and/or Condition Y of the mixed member partnership rules at ITTOIA s 850C –whether miscellaneous income under ITTOIA s 687 – if capital, whether within the occupational income rules – various procedural issues including considering the meaning and application of the statutory phrase "on behalf of" together with the requirement that carelessness cause the loss of tax

Heard on 14 and 17-21 November 2025
Judgment given on: 20 January 2026

Before

THE HONOURABLE MR JUSTICE THOMPSELL
JUDGE ANNE REDSTON

Between

MARK BENEDICT HOLDEN

Appellant

and

THE COMMISSIONERS FOR
HIS MAJESTY'S REVENUE AND CUSTOMS

Respondents

and between

THE COMMISSIONERS FOR
HIS MAJESTY'S REVENUE AND CUSTOMS

Appellants in cross-appeal

THE BOSTON CONSULTING GROUP UK LLP
MARK BENEDICT HOLDEN
AFONSO NASCIMENTO
PHILIP KRINKS
MICHAEL NIDDAM
THOMAS GARSIDE

Respondents in cross-appeal

Representation:

For the BCG parties:	Sam Grodzinski KC, Marika Lemos KC and John Machell KC, instructed by Freshfields LLP
For HMRC:	Thomas Chacko, Jeremy Callman, Ronan Magee, Elizabeth Atkinson and Helen Bunce, all of Counsel, instructed by the General Counsel and Solicitor to HM Revenue and Customs

DECISION

INTRODUCTION

1. This judgment deals with appeals and cross-appeals against the decision of the First-Tier Tribunal Tax Chamber (the "**FTT**") reported under the neutral citation [2024] UKFTT 00084 (TC) (the "**FTT Decision**"). The FTT Decision relates to a number of substantive and procedural issues arising out of arrangements put in place from April 2011 by The Boston Consulting Group UK LLP (the "**UK LLP**").

2. The underlying facts in relation to this matter are dealt with comprehensively within the FTT Decision and we will not seek to reproduce all those facts except insofar as the FTT's findings are under challenge. The following explanation is sufficient to set the scene.

3. The UK LLP is part of a privately-owned corporate group which we will refer to collectively as "**BCG**", headed by The Boston Consulting Group, Inc. ("**BCG Inc**"). BCG Inc holds (directly or indirectly) interests in a variety of different entities, which conduct BCG's business in each of the jurisdictions where it operates.

4. Since 2011 BCG has conducted its business in the UK through the UK LLP.

5. Prior to 2011, the UK business of BCG was carried on through BCG Ltd, a wholly owned subsidiary of BCG Inc. In 2011 BCG Ltd contributed its business to the UK LLP (of which it and another corporate member, which has never had a material interest in the UK LLP, were the founder members). In return for that transfer, BCG Ltd was credited with a sum in a capital account maintained for it by the UK LLP equal to the net asset value of the business assets transferred (but excluding any credit for any goodwill in the business transferred). BCG Ltd was appointed as the "Managing Partner" of the UK LLP.

6. BCG operates in accordance with a global partnership ethos, in which the senior individuals who run the business in every jurisdiction each participate in the ownership and management of the global group. These senior individuals are known as "Managing Directors and Partners" ("**MDPs**"). At the point that BCG Ltd contributed its business to the UK LLP the MDPs who had been senior employees of BCG Ltd and were of MDP status ceased to be employed and became members of the UK LLP ("**Members**").

7. To reflect its global partnership ethos, the BCG Group operates a single, global compensation and equity framework for all MDPs, including its UK MDPs (the "**Framework**"). The Framework is used to set out the principles which are applied to determine the amount of compensation and "equity" which each MDP will receive. However, it does not itself provide the MDPs with any legal right to compensation or stake in the group. Instead, MDPs derive such rights through the local "programmes" in place in the jurisdiction in which they operate.

8. There were four 'compensation components' in the Framework: (i) a "nominal" element, which represents the fixed amount of remuneration which each MDP receives each year in respect of their role as an MDP; (ii) a performance element reflecting BCG's assessment of that MDP's contribution to the business; (iii) an "office performance bonus" element, calculated by reference to the performance of an MDP's local office; and (iv) a "profit sharing retirement fund". This last element is calculated as a specified percentage of the MDP's remuneration under the first three elements and is either invested in qualified retirement savings vehicles or, if such vehicles are not available, paid to the MDP in cash, to enable them to make provision for their retirement.

9. In addition, the Framework provides for what BCG calls the "equity" component or "**LTCV**". This was originally introduced in 1994 to provide MDPs with an interest in the long-

term growth in value of the global business; to improve retention of MDPs; and to strengthen and increase the stability of BCG's capital base. When it was originally introduced, MDPs in different jurisdictions participated in the LTCV either through holding shares in BCG Inc or derivatives of those shares, or through a phantom stock programme.

10. To implement the LTCV in the UK, following the decision that the UK LLP would be the vehicle for the BCG business in the UK, the MDPs working in the United Kingdom were allocated certain rights, under arrangements set out in three Limited Liability Partnership Agreements ("**LLPAs**") executed in 2011 (the "**2011 LLPA**"); 2014 (the "**2014 LLPA**"); and 2016 (the "**2016 LLPA**"). These rights were referred to in the FTT Decision as "Capital Interests", adopting the terminology used in the 2014 LLPA and the 2016 LLPA (but not in the 2011 LLPA). For consistency we have used the same phrase, but should not therefore be taken to have accepted that the interests were capital in nature, as that is a key issue in dispute. The FTT also referred to the UK MDPs simply as "MDPs" and we have adopted the same abbreviation, other than where we need to distinguish between the UK MDPs and those in other locations.

11. The Capital Interests were specifically designed in a manner that was intended to cause them to be regarded as a capital asset for tax purposes so that payments in respect of the Capital Interests could be taxed under the regime for capital gains tax and would not be regarded as the receipt of income.

12. On the assumption that the Capital Interests fell to be treated as a capital asset and that the payments made under Schedule 3 were therefore payments for the sale of a capital asset, the UK LLP filed its Partnership Statement in each of the tax years 2012-13 to 2016-17 (the "**relevant years**") on the basis that payments made to MDPs in relation to the Capital Interests were not an allocation or distribution of its profits. The MDPs filed their self-assessment ("**SA**") tax returns on the same basis, treating the payments as capital gains and claiming Entrepreneur's Relief.

13. HMRC disagreed with this treatment and amended the UK LLP's Partnership Statement for the relevant years under Taxes Management Act 1970 ("**TMA**") s 30B, and issued certain MDPs with discovery assessments under TMA s 29.

14. The UK LLP and 63 MDPs appealed to the FTT. It was ordered that five of those MDPs (Mr Holden, Mr Nascimento, Mr Krinks, Mr Niddam and Mr Garside) be lead appellants under Rule 18 of the Tribunal Procedure (First-tier Tribunal) (Tax Chamber) Rules 2009, with the others being "followers".

15. By its judgment issued on 23 January 2024, the FTT decided a number of issues, including the following:

(1) the Capital Interests were not interests in the capital of the UK LLP or a share of its assets;

(2) no amounts were to be reallocated to the MDPs under s 850 of the Income Tax (Trading and Other Income) Act 2005 ("**ITTOIA**");

(3) the mixed member partnership rules (the "**MMRs**") at s 850C ITTOIA did not apply;

(4) sums paid to MDPs in respect of their Capital Interests were taxable on the MDPs as miscellaneous income under ITTOIA s 687;

(5) if (contrary to the FTT's other findings), the sums paid to the MDPs in respect of their Capital Interests were capital in nature, those sums were taxable as the sale of occupational income under Chapter 3 of Part 13 Income Tax Act 2007 ("**ITA**"); and

(6) a number of appeals made on basis that these assessments were procedurally invalid were allowed, and others were dismissed.

16. The overall effect of these findings was that the UK LLP succeeded in its appeal on the substantive issues concerning the treatment of payments made in respect of the Capital Interests. Although the FTT had found that the payments were taxable as miscellaneous income in the hands of the MDPs, all the lead appellants other than Mr Holden succeeded in their procedural challenges. In relation to Mr Holden, the FTT found that the discovery assessment issued to him for 2013-14 was valid, and it followed that the amounts paid to him in respect of Capital Interests were taxable as miscellaneous income.

17. Applications for permission to appeal to the Upper-Tier Tribunal Tax and Chancery Chamber (the "**UT**") were then made:

(1) HMRC received permission to appeal against the FTT's findings on the MMRs and its adverse findings on some of the procedural issues. The UK LLP and the lead appellants (together, the "**BCG Parties**") are the respondents in relation to that appeal.

(2) Mr Holden received permission to appeal to the UT against (a) the FTT's findings on the nature of the Capital Interests and (b) the application of the miscellaneous income and occupational income provisions. HMRC are the respondents in relation to that appeal.

(3) In addition, both parties' Respondents' Notices raised numerous points relating to the FTT's reasoning.

18. As well as the matters summarised at [15] above, the FTT made other findings which were either not appealed, or for which permission to appeal was not granted. We include those findings only to the extent that one or both parties referred to them when making submissions.

19. As can be seen even from the above summary, this was a complicated case. We were therefore particularly grateful for the submissions of the parties' counsel, and we also recognise the significant work carried out behind the scenes by their solicitors and legal teams.

THE ISSUES

20. The BCG Parties and HMRC provided separate "Lists of Issues" with multiple subheadings. It was however common ground that the following main issues (the "**Issues**") were before us to decide:

(1) whether the FTT was wrong to hold that the Capital Interests were not interests in the capital of UK LLP (the "**Capital Issue**");

(2) whether the FTT was wrong to decide that the MMRs did not apply, and if the answer to that question was "yes", what was a "just and reasonable" re-allocation to the MDPs (the "**MMR Issue**");

(3) if the MMRs did not apply, whether the sums paid to the MDPs were taxable as:

(a) miscellaneous income (the "**Miscellaneous Income Issue**"); or

(b) as proceeds from the sale of occupational income (the "**Occupational Income Issue**").

(4) In relation to certain assessments on the MDPs and the 2016-17 partnership return filed by the UK LLP, whether HMRC had shown that there had been carelessness within the meaning of the relevant statutory provisions and whether HMRC had shown, in relation to the 2015-16 partnership return filed by the UK LLP, that the "hypothetical officer" requirement at TMA s 30B(6)(a) was satisfied (the "**Procedural Issues**").

THE CAPITAL ISSUE UNDER THE 2011 LLPA

21. The FTT's findings on the nature of the Capital Interests are at [86]-[141]. Having surveyed some of the evidence, and the authorities on the nature of interests in LLPs, including *Reinhard v Ondra LLP and others* [2016] 2 BCLC 571 ("***Reinhard***"), the FTT concluded that the Capital Interests were not interests in the capital of UK LLP and did not constitute interests in UK LLP's goodwill.

22. For reasons that will become apparent, the BCG Parties' argument that the Capital Interests should be treated as interests in the capital of UK LLP, and that the payments made to the MDPs were the proceeds of sale of those interests, are at their strongest in relation to the 2011 LLPA, which was in force between 1 April 2011 until 30 November 2014. We will start by summarising the provisions of the 2011 LLPA that are most relevant to the Capital Issue.

Relevant provisions of the 2011 LLPA

23. First it should be noted that control of the UK LLP and of remuneration matters was very much in the hands of BCG Ltd as the Managing Partner of the UK LLP.

24. Clause 9 (amongst other things) dealt with the appointment and powers of the Managing Partner and the Remuneration Committee and included the following provisions.

25. Clause 9.1 provided for the appointment of a Managing Partner and that the initial Managing Partner was to be BCG Ltd.

26. Clause 9.2 afforded the Managing Partner:

> "full and exclusive authority, power and responsibility to make decisions on behalf of the Partnership in respect of the matters set out in Schedule 2 and any matters ancillary thereto".

27. The matters set out in Schedule 2 included many of the types of important decision that the UK LLP might need to make, including the admission of any new Member and various different types of transaction where the value of the transaction was in excess of certain amounts. The Managing Partner also was given various other powers within the LLPA including:

(1) a power (under clause 8.4 (ii)) to cast one more vote than the aggregate number of votes which all other Members are entitled to cast at a general meeting of Members, referred to as a "**magic vote**";

(2) a power (under clause 14.3) to require any Member to withdraw from the Partnership with no less than 12 weeks' prior notice; and

(3) a power (under clause 16.2(a)) to make a determination to dissolve the UK LLP (although it is unclear how this power sits with the statutory requirement for the winding up of an LLP to be approved by a 75% majority of its members).

(4) A power (under clause 17) to make any amendment to the LLPA that the Managing Partner "shall deem" to be "necessary or desirable" subject to approval by a resolution of Members (which as a result of the magic vote the Managing Partner could always procure).

28. Clause 9.3 provided for the Members to appoint a remuneration committee, the members of which may or may not be Members. The members of the Remuneration Committee may be removed by a notice given by a Member or Members who together are entitled to cast a majority of the votes at a meeting of the Members (assuming that all Members were to attend and vote) – as a result of the magic vote, in practice this power was available only to or with the participation of BCG Ltd as Managing Partner.

29. Clause 9.4 provided as follows:

> "The Remuneration Committee shall have regard to the global compensation policies and procedures of BCG, Inc. as such are in force from time to time in exercising discretion and making determinations within its mandate. Subject to the foregoing, the Remuneration Committee shall have full and exclusive authority, power and responsibility to make decisions on behalf of the Partnership in respect of the matters set out in clause 3 (Interests in capital, Profits of the Partnership and Partnership Loans) and other ancillary matters."

30. It is reasonable to conclude, therefore, that the policies put in place were intended, as closely as possible, to reflect the Framework. This conclusion also is in accordance with the evidence of Mr Holden, the BCG Parties' principal witness at the FTT hearing.

31. Turning next to issues relating to the Capital Interests, clause 3.1 of the 2011 LLPA provided as follows:

> "The extent of each Member's interest in the capital of the Partnership shall be determined and notified to each Member by the Remuneration Committee in its discretion from time to time. On each occasion on which a Member is notified of the granting of a new interest in the capital of the Partnership, such Member shall also be notified of the number of units in the capital of the Partnership that are being granted. No financial contribution shall be required to be made by a Member in order to acquire an interest in the capital of the Partnership."

32. It may be noted that the nature of the "interest" said to be determined by the Remuneration Committee is not explained at clause 3.1 - or anywhere else. Moreover, as we discuss further below, the phrase "number of units in the capital of the Partnership" is a somewhat misleading phrase.

33. It was originally put forward in argument on behalf of the BCG Parties that the discretion afforded by clause 3.1 did not extend to reducing as opposed to increasing a Member's "interest". HMRC contended that it did so extend. We agree with HMRC. This is the plain meaning of a power to determine "the extent of" a Member's interest and we see no occasion not to give these words their plain meaning (and also not to give the words in clause 9.3, discussed further below, their plain meaning). If any further reason were needed, we note that the same phrase "determined and notified to each Member by the Remuneration Committee in its discretion from time to time" is also used in clause 3.2 in relation to the separate matter of each Member's interest in the profits of the UK LLP and it is clear that in clause 3.2 that phrase conferred a power to reduce as well as increase such interest.

34. Clause 3.2 deals with the allocation of "Profit" among the Members. The 2011 LLPA is not particularly clear on which Members are to benefit from any capital profit (including one arising from a sale of goodwill not immediately followed by a winding-up). At clause 1.2 it recognises a distinction between income profits and "profits of a capital nature". However, the defined term "Profit" does not refer to this distinction and instead defines the term as "distributable profits" - not a very clear term outside the context of a limited company.

35. Presumably "distributable profits" could in theory encompass capital as well as income profits. However, as under clause 3.3, the Remuneration Committee "determines the extent of each Member's interest in the Profit for any Financial Year". Therefore ahead of any such determination in respect of any particular Financial Year no individual Member has any quantifiable (or saleable) entitlement to the proceeds of sale of a capital asset (including goodwill) other than that Member's capital account at any point, or certainly at any point before the winding-up of the UK LLP.

36. Further, given that BCG Ltd has a "magic vote", we can see nothing to stop BCG Ltd as Managing Partner bringing about a sale of the business of the UK LLP to a third party (or another BCG Group member); and through its control (with its magic vote) of the composition of the Remuneration Committee, ensuring that any capital profit created by a goodwill element in the price be allocated and paid out to BCG Ltd. Indeed in the 2014 LLPA and the 2016 LLPA it was clarified that only BCG Ltd had any interest in capital profits of the UK LLP, as we discuss later. There would be nothing unfair about BCG Ltd acting in this way. BCG Ltd would still in these circumstances theoretically be legally obliged to make payments under Schedule 3 on the events providing for a "sale" under Schedule 3 (assuming that the UK LLP was not insolvent or rendered insolvent by the arrangements) but that is different to saying that the BCG Members had any right to participate in a "sale" of goodwill except where this is realised on a winding-up. (We follow the FTT in placing words like "sale" in inverted commas because whether the circumstances constitute a sale is in dispute.)

37. Under clause 14.8:

> "If a Member shall die or become bankrupt, he shall forthwith, without notice, cease to be a Member notwithstanding any other provision of this Agreement."

38. Under clause 15, upon any Member dying, withdrawing or otherwise ceasing to be a Member in accordance with any provisions of the LLPA, that person (from that point being known as an "**Outgoing Member**") ceases membership; the provisions of Schedule 3 shall apply in respect of the Outgoing Member's "interest in the capital of the Partnership".

39. The provisions in Schedule 3 were applied (subject to certain rights of retention enjoyed by the LLP under clause 15.2) in addition to rights of the Outgoing Member or his personal representatives to receive:

(1) payment of that Outgoing Member's outstanding profit share for the year (including any tax reserve);

(2) payment of any amounts standing to the credit of that Outgoing Member's Distribution Account; and

(3) (under clause 3.3) repayment of any Partnership Loan that he may have made to the UK LLP within a year of his becoming an Outgoing Member.

40. Clause 15 thus provides the first introduction within the LLPA to Schedule 3 to the LLPA.

41. Schedule 3 is headed "Provisions for the sale of interests in the capital of the Partnership". Since clause 1.2 provides that headings are for convenience only and shall not affect the construction of the LLPA, we will ignore the heading in construing Schedule 3.

42. Nevertheless, it is clear that Schedule 3 is all about defining circumstances in which there is to be a "sale" of interests and in determining what is to be paid in respect of such a "sale".

43. Schedule 3 sets out a number of circumstances in which there is to be a "sale" of a "Sale Interest", which is defined as follows:

> "Sale Interest" means, in respect of a Member, his interest (or, if part only of his interest is being sold, that part) in the capital of the Partnership for the time being which is to be sold pursuant to the provisions of this Schedule".

44. It may be noted that this definition hinges on the concept of a Member's "interest in the capital of" the UK LLP, but what might be the nature or extent of that "interest" is nowhere defined. It must be the case, however, that it does not include the rights separately paid out on

the event of a Member becoming an Outgoing Member, as described at §39 above, since otherwise those rights would not be separately paid out.

45. The circumstances in which there is to be such a "sale" include:

(1) under paragraph 3.1 of Schedule 3, a mandatory "sale" upon cessation of membership for any reason;

(2) under paragraph 4.1 of Schedule 3, (unless otherwise determined by the Managing Partner") a mandatory "sale" where a Member has at least 20 years of service as an officer of BCG Inc, in each of the 10 years following a proportion of his "Sale Interest" being:

> "that proportion of the Member's interest in the capital of the Partnership equal to the total extent of that Member's interest in the capital of the Partnership as of the first day of such year divided by the number of years then remaining to the end of the above ten-year period";

(3) under paragraph 4.2 of Schedule 3,where the preceding sub-paragraph applies, an optional right for the Member to "sell" an additional amount of his "interest in the capital" of the UK LLP up to the amount to be "sold" under the previous paragraph; and

(4) under paragraph 5.1 of Schedule 3,where the Member (i) has at least five years of service as an officer of BCG Inc and is at least 45 years old or (ii) has 10 years of service as an officer of BCG Inc, but does not fall into paragraph 4.1, a right for the Member to opt to "sell" up to 10% of his "interest in the capital" of the UK LLP up to an aggregate cap of 50% for all such sales under this paragraph the amount to be sold under the previous paragraph.

46. In each case the "sale" is to be a sale to the "Purchaser", defined as BCG Ltd or such other person as shall be designated by BCG Ltd from time to time.

47. Paragraph 6 of Schedule 3 contains the following further provisions:

> "6 Optional Purchase of Sale Interests by BCG Ltd or its Designee
>
> 6.1 The Partnership shall be entitled to redeem (and BCG Ltd shall be entitled to purchase) any or all interests in the capital of the Partnership from any or all of the Members upon at least ten days' prior written notice at the Purchase Price calculated as of an Effective Date specified in that written notice…
>
> 6.2 The Partnership shall not exercise any right to redeem (and no other Purchaser shall have the right to purchase) any Sale Interests pursuant to the provisions of this paragraph 6 without a specific approval by BCG Ltd."

48. The price at which a "Sale Interest" interest is to be "sold" is defined in paragraph 2.1 of Schedule 2. The "Purchase Price" is determined (in broad summary) as:

(1) the value (as determined by the board or executive committee of BCG Inc) of "the Notional Number of Series D-2 Shares" (being a class of share in BCG Inc) (the "**BCG Inc Shares**") as at the latest year-end of BCG Inc prior to the effective date for the "sale"; minus

(2) the same value of such BCG Inc Shares similarly determined as at the date of grant of the relevant "Sale Interest"

(but so that if this calculation result in a negative sum, the calculation shall be deemed to be zero).

49. In our view, the stated definition of "Notional Number" makes no sense, and neither does the reference in clause 3.1 to "a number of units in the capital of the Partnership" mentioned at §32 above. It is not possible to construe the capital of the UK LLP (however defined) as being

divided into a number of units. If the capital were so divided, then the creation of new units would dilute the value of existing units and this does not happen either under the provisions for a "sale" under Schedule 3 or under the Clause 16.3 Waterfall (discussed further at §56 below in the context of our discussion of the rights of Members on a winding-up). The drafting of Schedule 3 only makes sense if you apply the term "Notional Number" in the way that it is used in the calculation of the "purchase price" of a "Sale Interest" – as a notional number of BCG Inc Shares used as a reference point for the calculation of a "sale" price.

50. The final provisions to note in Schedule 3 are those:

(1) in paragraph 8, which allow a redemption or a purchase of a Sale Interest by the UK LLP or BCG Ltd to be deferred if the UK LLP or BCG Ltd is insolvent or if either body would be rendered insolvent by the making of the redemption or purchase of such Sale Interest;

(2) in paragraph 7.1(a) which give the Purchaser (BCG Ltd or its designate):

> "the right to commit to or effect any purchase of Sale Interests on the assumption, and without specifically determining that it has sufficient funds legally available to discharge its liabilities on the assumption, and without specifically determining, that on or after the Effective Date of such purchase, the Purchaser will have sufficient funds legally available to discharge its liabilities other than the Sale Interests to be so purchased".

(3) In paragraph 7.1(c) that on the Effective Date for a purchase:

> "… all rights of a Member (and his successors and assigns) in relation to the capital of the Partnership comprised in the Sale Interest shall thereupon immediately and automatically terminate without further notice or other action by the Partnership or others, and thereafter such Seller (and his successors and assigns) shall have no right with respect to such capital. All rights in the Sale Interest shall automatically be assigned to and transfer to the Purchaser on the Effective Date."

51. Again, the drafting is somewhat problematic since it is difficult to see how an interest in capital can terminate so that the "seller" and his assigns have no right with respect to any interest in such capital, but at the same time the Purchaser (who is said to be an assignee) can be left holding those rights. However, in order to make sense of the provision we will construe it as meaning that the rights (whatever they may be) are assigned to the Purchaser, rather than being terminated. As is discussed below, if the Purchaser is BCG Ltd, there may not be much difference in the effect of these two possible outcomes.

52. Under clause 16.2 of the main body of the 2011 LLPA, it is made clear that if the UK LLP were to be wound up, the LLPA remains in force until the affairs of the UK LLP have been wound up.

53. Clause 16.3 is one of the key clauses in relation to the argument whether the MDPs have a capital interest in the UK LLP. Accordingly we will set this out in full:

> "In the event of the winding up of the Partnership, (a) all loans made by Members to the Partnership shall automatically be converted into and be treated as capital of the Partnership and each Member's Loan Account and Capital Contribution Account shall be debited or credited accordingly and (b) any surplus of assets of the Partnership over its liabilities remaining at the conclusion of the winding up after payment of all monies due to the creditors of the Partnership and all expenses of the winding up (the Remaining Assets) shall be payable by the liquidator to the Members in the following order of application:

(a) first, in paying to the Members the amounts (if any) standing to the credit of the Members' respective Distribution Accounts on the day before the commencement of the winding up (or, if there are insufficient Remaining Assets to pay such amounts in full, pro rata having regard to the amounts standing to the credit of each Member's Distribution Accounts);

(b) next, if there remain any Remaining Assets, the amount standing to the credit of the Capital Contribution Account of BCG Ltd to the extent of the purchase price for the transfer of the Business and assets of BCG Ltd to the Partnership under the Business Transfer Agreement dated 21 December 2010 between BCG Ltd and the Partnership for the transfer of the Business and assets of BCG Ltd;

(c) next, if there remain any Remaining Assets, in paying to each Member (other than BCG Ltd and BCG UK1 [the other corporate partner with only a nominal holding]) the Purchase Price (as defined in Schedule 3) to which each Member would be entitled if his interest in the capital of the Partnership was purchased pursuant to paragraph 6 of Schedule 3 with the date of the commencement of winding up being the Effective Date for the purposes of Schedule 3 (and if the Remaining Assets are insufficient to discharge all such sums, the Remaining Assets shall be allocated and paid to Members on a pro rata basis);

(d) next, if there remain any Remaining Assets, in paying to the Members the amount standing to the credit of the Members' respective Capital Contribution Accounts following the conversion referred to above (or, if there are insufficient Remaining Assets to pay such amounts in full, pro rata having regard to the amounts standing to the credit of each Members' Capital Contribution Account); and

(e) all Remaining Assets shall be paid to BCG Ltd."

54. We refer to these provisions as the "**Clause 16.3 Waterfall**".

55. It may be noted from the above that the effect of the right created for an MDP Member under paragraph (c) of the Clause 16.3 Waterfall (which we will call the "**Clause 16.3(c) Right**") is to provide that person with an amount equal to the calculated "sale" value of his "interest in the capital" as if there were to be a "sale" of that right under Schedule 3. That right would come in priority to both:

(1) any amounts due to any Member (other than BCG Ltd, which receives back the amount standing to the credit of its capital account earlier in the Clause 16.3 Waterfall), which by this point would have had credited to it any loans that Member had made to the UK LLP, which would automatically be converted into balances on the Capital Contribution accounts on the commencement of the winding-up; and

(2) the right of BCG Ltd at the bottom of the Clause 16.3 Waterfall to be paid or allocated any remaining assets.

56. It important to note that the only effect on the Clause 16.3 Waterfall of the issue of any "interests in the capital" under clause 3.1, or the "sale" of such interests under Schedule 3, is to increase or decrease what a Member might receive under clause 16.3(c). Given this point, and given that on retirement an Outgoing Member receives back from the UK LLP separately all other interests which that Member may have in the UK LLP (see §39 above) it must be that a Member's "interest in the capital" of the UK LLP is identified entirely with the Member's Clause 16.3(c) Right. This is the only thing that the Member gives up and BCG Ltd acquires as a result of a "sale" under Schedule 3.

57. There is no use within the Clause 16.3 Waterfall of the concept of "units in the capital of the Partnership" and it is notable that the issue of any "interest in the capital" has no effect in diluting the Clause 16.3(c) Rights of other holders of Clause 16.3(c) Rights. As we have seen, if there is a winding up, the value of the Clause 16.3(c) Rights issued may reduce the amounts available to repay the capital accounts of the MDPs or, if there is a sufficiently large surplus so that those amounts can be paid in full, would reduce the return that BCG Ltd obtains at the bottom of the Clause 16.3 Waterfall. However, the creation of any Clause 16.3 Right does not dilute the value of any other "units in the "capital" – they remain rights calculated by reference to increases in value of the BCG Inc Shares.

58. Clause 6 restricts a Member dealing with his rights "in the capital of the Partnership". It provides as follows:

> "Unless agreed by the Managing Partner with the relevant Member and except as provided in Schedule 3, no Member shall:
>
> (a) transfer, sell or assign (whether in whole or in part) his interest in the capital of the Partnership in any way; or
>
> (b) grant security over, charge or encumber in any way his interest in the capital of the Partnership."

59. In argument, Mr Grodzinski KC, acting for the BCG Parties, sought to persuade us that this should not be regarded as a complete prohibition on transfers made outside the provisions set out in Schedule 3, since (i) if asked the Managing Partner would need to deal with his discretion rationally and in good faith, in accordance with the principles outlined in *Braganza v BP Shipping Ltd* [2015] UKSC 17*,* and (ii) because a Member could borrow against his interest or assign the proceeds of his future sale of the interest.

60. We found those arguments unconvincing.

61. As to the first point, given the policy intentions behind these arrangements, as exemplified in the Framework, it seems to us vanishingly unlikely that the Managing Partner would allow any dealing in the Capital Interests outside what is envisaged in Schedule 3, except, perhaps, in some very unusual arrangements. An example might be if there were to be a husband and wife who were both Members and for some reason they wish to assign an interest from one of them to the other. Also, it is difficult to see how one could ever succeed in an argument that it was irrational or in bad faith for the Managing Partner to insist that any such interest is dealt with only in the way envisaged within the LLPA.

62. As to the second point, clause 6 is widely drawn in relation to restricting any grant of security over interests, and so it is wrong to think that a Member could borrow on the security of the Capital Interests. The fact that a Member might persuade someone to lend to on the basis of that Member's future expectations is not relevant to the question of whether a Member could deal with his or her interests outside the arrangements envisaged in Schedule 3.

63. Accordingly in our view, for all practical purposes, clause 6 should be regarded as an absolute prohibition on transfer or assignment outside the Schedule 3 arrangements.

64. Drawing together these provisions as they relate to the Capital Interests, we note the following as being points that are particularly salient:

(1) The Capital Interests are stated to relate to "interests in the Partnership" – but the nature of this interest is nowhere explained. It could not however comprise the other rights separately paid out on the event of a Member becoming an Outgoing Member, as described at §39 above, since otherwise those rights would not be separately paid out on

retirement. We conclude that the Capital Interests, to the extent that they exist, are identified with the Clause 16.3(c) Rights.

(2) The Capital Interests are granted without any payment being made for them.

(3) The Capital Interests have no value on their grant (as the result of the formula in Schedule 3). They acquire value only once and if there is an increase in the assessed value of the BCG Inc Shares.

(4) Despite the definition of "Notional Number", the Capital Interests do not involve the grant of anything recognisable as "units" in the capital (or goodwill) of the LLP. They are rights to receive payments by reference to increases in the value of a notional number of BCG Inc Shares.

(5) There are three ways that an MDP could benefit from the Capital Interests:

(a) through a "sale" on retirement to BCG Ltd (or its designate) or on one of the earlier occasions provided for in Schedule 3 and receiving the calculated price;

(b) through being redeemed by the UK LLP at the price calculated under Schedule 3, although it is difficult to see why the UK LLP would do this, as the redemption would not benefit the UK LLP itself, it would be likely to benefit only one of its Members (BCG Ltd) but the redemption price would be out of the common funds of UK LLP;

(c) on a winding-up of the LLP through receiving a payment under paragraph (c) of the Clause 16.3 Waterfall (being a payment equal to the calculated sale price), or if less the amount available on a winding up at that stage of the Clause 16.3 Waterfall.

(6) The Capital Interests do not include express rights to participate in any goodwill on the sale of the business of the UK LLP, and would not have that effect unless that sale were immediately followed by a winding-up of the UK LLP. No individual member has any contractual entitlement to the proceeds of sale of a capital asset (including goodwill) prior to a winding up unless or until that entitlement is granted by the Remuneration Committee.

(7) There is no practical likelihood of the Capital Interests (or any interest in capital or goodwill they might be said to embody) being sold outside the arrangements envisaged in Schedule 3.

(8) The Capital Interests of any MDP could be reduced or removed by the Remuneration Committee.

(9) The payment for a "sale" of Capital Interests of any MDP were subject to provisions for delay in payment and set-off.

The BCG Parties' Arguments in relation to Capital Interests under the 2011 LLPA

65. The BCG Parties argue that the provisions of the 2011 LLPA reflect the clear intention to give MDPs an interest in the capital of the UK LLP; have that effect; and as a result, when any of the events occurred under which they received payments from BCG Ltd on or before retirement, those amounts were payments for the sale of that capital asset.

66. The BCG Parties argue, therefore, that the FTT Decision was wrong in finding:

(1) at [138] that:

> "Given our findings we conclude that the Capital Interests were not interests in the capital of the UK LLP or a share in its assets. Indeed, the Capital Interest

> holders had no right as Capital Interest holders as against the UK LLP itself ...Their rights were against BCG Ltd to be paid an amount at a future date calculated by reference to the increase (if any) in the value of BCG Inc" and

(2) at [139] that:

> "Although the document appears on its face to suggest a sale of an interest in the UK LLP we have concluded that the substance of the Capital Interests is that they are rights against BCG Ltd to payment."

67. We first consider what we have termed the BCG Parties' overarching argument, and then their criticisms of the way the FTT construed the 2011 LLPA.

The overarching argument

68. The BCG Parties' overarching argument was advanced essentially as follows. Under the 2011 LLPA whenever the MDPs were provided with "units" under Schedule 3 and there was a later rise in value of the BCG Inc Shares, the MDPs held an interest in the capital of the UK LLP. This interest, they argue, was a form of chose in action which may be crystallised on the sale of the asset or dissolution of the UK LLP. As such it is a "share" in the UK LLP, or at least an "interest" in the UK LLP or its goodwill and is no different to any other asset in that it may be assigned to a third party or another Member.

69. The BCG Parties point to the Clause 16.3(c) Right as demonstrating that such a "share" or "interest" exists. In effect, the BCG Parties argue that the Clause 16.3(c) Right was a right on a winding up of the UK LLP to share in the goodwill of the UK LLP. From this they deduce that the BCG Members must have a continuing interest in the goodwill. It did not matter that this share was not calculated as a percentage of the goodwill, but instead was fixed by reference to a notional increase in value of a notional number of BCG Inc Shares– it was still a share in the goodwill of the UK LLP. This then provided the MDPs with a capital asset that could be (and was) sold on their leaving the UK LLP, or in certain circumstances, as outlined above, before leaving the UK LLP. Such a sale should, therefore, be regarded as the sale of a capital asset and should be taxed as a capital gain rather than as income.

70. The BCG Parties had a number of arguments to bolster their contention that this was the correct analysis. We will deal with these individual arguments after addressing our reasons why we consider that the BCG Parties are wrong in relation to their overarching argument.

71. In our view, the overarching argument is irredeemably flawed. There are three major points which we consider in turn below:

(1) Whether goodwill exists as an asset which MDPs can sell.

(2) Even if there is a capital asset, it is not owned by the MDPs individually.

(3) The payments made under Schedule 3 do not reflect a genuine sale price.

(1) Whether goodwill exists as an asset that MDPs can sell

72. The first is to consider whether there is in fact any capital asset that exists and is held by the MDPs that is being "sold" under Schedule 3.

73. The BCG Parties contend that the asset in question is in effect a share or interest in the UK LLP that represents a right to participate in the goodwill of the UK LLP.

74. The distinction between capital and income is central to our system of taxation but recognising what is capital and what is income can be difficult in some cases. Henderson LJ at [114] in the Court of Appeal's judgment in *HMRC v BlueCrest Capital Management LP and others [2023] EWCA Civ 1481 ("**BlueCrest**")* considered that it was:

> "a fact that the distinction between capital and income receipts is sometimes easier to recognise than to define, and that in reaching a conclusion there is a place for the intuitive common sense of judges or tribunals well versed in tax law."

75. Whilst (as we will consider further below) this matter needs to be considered in relation to the words of the taxing statute, Henderson LJ did find some use for the age-old metaphor of distinguishing between the "fruit" as opposed to the "principal or root of the tree". In the same paragraph he said:

> "The homely metaphor of fruit of the tree has often proved helpful in the search for a guiding principle to distinguish capital from income receipts".

76. In this case however, the "homely metaphor" is of little help, except that we would concur that the goodwill of a business does look more like the tree itself (the income-producing asset) than the "fruits" produced by the tree.

77. However, the argument that the Members were trading in interests in goodwill when payments were made under Schedule 3 faces first the counter-argument that no such goodwill existed as a recognisable asset at the point of any of the "sales" made under Schedule 3.

78. The accountancy points in that direction. No such asset was recognised on the balance sheet of the UK LLP. As noted in *Lindley and Banks on Partnership* (21st) Edition ("***Lindley & Banks***"), Lord Lindley pointed out:

> "It is only so far as the goodwill has a saleable value, that it can be regarded as an asset of any partnership ...

The BCG Parties argue that it would be wrong to rely on the accounting treatment to determine whether goodwill exists, and it is argued in *Lindley & Banks* that Lord Lindley went too far with this point and that goodwill, even if unmarketable, clearly exists as an asset and is capable of protection. We agree with both points. Goodwill can often be the most important asset of the business, whether or not it is recognised on the balance sheet of a firm (as noted in *Lindley & Banks* at para 10-410):

> "the goodwill of a firm will frequently be one of its most valuable assets, even though it may not feature as such in its annual accounts".

79. Accordingly, we will not place any reliance on any accounting treatment in relation to either the Capital Interests themselves or goodwill.

80. As used by the accountancy profession, goodwill means the amount that is paid for a business that is above the value of the fixed and current assets of that business that are sold. Clearly, under that definition, until the business is sold there is no such goodwill. However as we are dismissing that approach, then what other definitions are there? Goodwill, like "capital", is notably a difficult thing to define.

81. HMRC referred us to *Castledine v RSM Bentley Jennison* [2011] EWHC 2363 (Ch) [2012] Bus LRD 77 at [8]:

> "Although goodwill may be referred to as if it is a single asset, it may also be considered as a parcel of factors which could increase the opportunities of a successor to the business to enjoy the benefits that Lord Lindley referred to and so persuade him to pay more to become such a successor. The 'right' to use the name of the business is obviously one important factor, although as the author notes (para 10-195) it is doubtful whether that right is capable of being transferred independently of other elements going to make up goodwill. Other factors may consist of the ownership of assets associated in the minds of customers with the business itself, such as premises, registered trademarks

> or other intellectual property rights, even if those assets could be sold independently of any sale of the business. Others may relate to the involvement of particular individuals with the business, either in a positive sense in that they continue to work in the business under the ownership of the successor, or in the negative sense that they are prevented from offering services in competition with him."

82. This analysis built on the earlier cases, in particular *CIR v Muller & Co Margarine* [1901] AC 217 (per Lord Macnaghten, at 223):

> "What is goodwill? It is a thing very easy to describe, very difficult to define. It is the benefit and advantage of a good name, reputation, and connection of business. It is the attractive force which brings in custom. It is the one thing which distinguishes an old established business from a new business at its first start.

83. Mr Grodzinski referred us to the definition given by Justice Hill in the Federal Court of Australia in *Federal Commissioner of Taxation v Krakos Investments Pty Ltd [*1995] ALR545 when he referred to the difference in value between the tangible assets of the business and the value of the business if sold as a going concern and said:

> "While goodwill may be not difficult to recognise, it is difficult to define, at least in an exhaustive way. As an economic concept it may be seen as the difference in value between the tangible assets of a business and the value of the business if sold as a going concern. It is in this sense that it is often referred to as representing an 'added value'."

84. The learned judge went on to refer to a multitude of cases where this "*economic concept*" was recognised and explained.

85. It is not possible to own an "economic concept". However, Mr Grodzinski has sought to persuade us that you can own "an economic asset that is defined in that economic way".

86. The BCG Parties argue that even if it is not valued in the accounts since the value of the business of the UK LLP (if sold) was obviously in excess of the net value of the assets shown on its balance sheet, goodwill existed as an asset of the UK LLP and as such was attributable to the individual Members, providing them with an asset that could be sold.

87. There is a difficulty in considering goodwill as a separate asset that can be separately sold, as Lord Lindley explained (as set out in *Lindley and Banks on Partnership* (21st) Edition at 17-01):

> "The term goodwill can hardly be said to have any precise signification. It is generally used to denote the benefit arising from connection and reputation; and its value is what can be got for the chance of being able to keep that connection and improve it. Upon the sale of an established business its goodwill may have a marketable value, whether the business is that of a professional man or of any other person. But it is plain that goodwill has no meaning except in connection with a continuing business… the value of the goodwill of any business to a purchaser depends, in some cases entirely, and in all very much, on the absence of competition on the part of those by whom the business has been previously carried on."

88. Nevertheless we agree that the UK LLP could be regarded as owning goodwill, notwithstanding that this was not reflected in its accounts and would not be saleable except in the context of a sale of the business.

89. However, this does not answer the second issue, which is that MDPs were not the owners of that goodwill.

(2) Even if there is a capital asset, it is not owned by the MDPs individually

90. Even accepting that goodwill has some existence as a form of asset and that asset may be regarded as a capital asset rather than as a form of income, there remain two difficulties with the analysis that this was an asset in which individual Members held an interest that was saleable by individual Members (outside the circumstances of the sale of the entire business).

91. The first difficulty is that the individual assets of the UK LLP belong to the UK LLP and not to the Members and so the Members do not have that asset to sell.

The BCG Parties' argument based on s 863 ITTOIA

92. The BCG Parties counter this point by saying that this objection does not apply in relation to an analysis for tax purposes because of the deeming effect of s 863(1)(c) ITTOIA (and its equivalent provision in s 59A(1)(a) Taxation of Chargeable Gains Act 1992 ("**TCGA**"). These provisions (which we will refer to as the "**deemed look-though provisions**") have the effect, for income tax and capital gains tax purposes respectively, of looking through the corporate veil of an LLP and deeming the Members to be in the same position as they would be if they were members of a general partnership.

93. The BCG Parties acknowledge that for most legal purposes an LLP as a body corporate has a legal personality separate from that of its members, so that its members have no direct legal or beneficial entitlement to the assets of an LLP. However, they submit that it is relevant that "for income tax purposes", the position is modified in respect of LLPs that are carrying on a trade, profession or business with a view to profit, by the deemed look-though provisions. They argue that it was an error of law for the FTT to state at [141] that the deeming effect of these provisions was:

> "at most […] an overriding "fiction" for tax purposes, which treats membership of the partnership as meaning that the partner holds a share in the assets of it, reflecting the transparent treatment of partnerships for tax purposes"

and for the FTT to conclude that these provisions accordingly could not affect the nature of the Capital Interests.

94. By s 863(1) ITTOIA, the property of an LLP is to be treated "as held by the members as partnership property". The statutory deeming therefore, they argue, does clearly impact upon the analysis of the nature of the Capital Interests. Thus (for example), when at [138] the FTT stated that UK MDPs "had no rights as Capital Interest holders as against the UK LLP itself" the FTT should have gone on to consider the impact on its analysis of the nature of the UK MDPs' rights and the fact that for most income tax purposes, UK LLP did not have a legal personality at all.

95. As a result, the BCG Parties argue in relation to the FTT's analysis on the precise nature of the Capital Interests, that the FTT did not identify the correct starting point. To understand the nature of a Member's interest in a trading LLP for income tax purposes, and in order properly to construe the terms of the LLPAs for income tax purposes, in their submission it is necessary to understand the proprietary nature of the analogous (by virtue of the deeming) partnership share in a general partnership.

96. They argue that with a general partnership, the partnership agreement regulates how, as between the partners, the partnership property must be dealt with. But so far as the rest of the world is concerned, they quote Luxmoore J in *Re Fuller's Contract* [1933] Ch 652, at 656:

> "there is no limitation on the interests of the partners; the partners have the beneficial interest in the partnership assets, which are held together as an undivided whole, but they respectively have undivided interests in them."

and Hoffmann LJ in *IRC v Gray* [1994] STC 360 at 377c-e:

> "...As regards the outside world…, the partnership deed is irrelevant. The partners are collectively entitled to each and every asset of the partnership, in which each of them therefore have an undivided share…".

97. They point out that although it is customary to speak of a partner's "share" of the partnership assets, that is not an accurate description of his interest in them while the partnership is a going concern. No partner has an entitlement to any specific asset and, in consequence, no right (without the consent of the other partners) to require the whole or even a share of any particular assets be vested in him, and they (correctly) cite *Popat v Shonchhatra* [1997] 1 WLR 1367 at 1373C to support this proposition.

98. However, they argue, partners have a form of chose in action which may be crystallised on the sale of the asset or dissolution of the partnership, so that a "share" in a partnership is no different to any other asset in that it may be assigned to a third party or a co-partner. The part assigned may be a fraction of the assigning partner's share or all or part of any specific entitlements which go to make up that share, e.g. a right to share in prospective capital profits. Whatever entitlements are conferred on a partner (for example an entitlement to a 'share' of income or capital profits), the chose in action carries with it an undivided interest in the property of the partnership. This follows *a fortiori* in the case of members of a trading LLP, as it is a function of the statutory deeming in s 863(1)(c) ITTOIA.

99. In summary, the BCG Parties' case is that while UK LLP is a going concern, the Capital Interests constitute interests in the capital profits of UK LLP derived from goodwill (for brevity, sometimes referred to "an interest in the goodwill of UK LLP"). Those rights are assignable choses in action. The UK MDPs realise cash sums when the assets are assigned to BCG Ltd, for consideration. Those choses in action carry with them the right to a share in capital profits derived from goodwill, and the receipt of cash sums on the disposal of the Capital Interests is of a capital nature. As a result it was wrong for the FTT to say at [86] that "in essence, that the Capital Interests are simply cash rights which crystallise in certain circumstances". Under the relevant principles summarised above, every 'share' in a partnership or trading LLP to income or capital profits may be regarded as fitting this description.

The HMRC response to the argument based on the deemed look-through provisions

100. HMRC had two responses to this argument insofar as it is based on the deemed look-through provisions.

101. First HMRC argued that on close analysis these provisions did not apply in the way that the BCG Parties were contending. HMRC argues that the BCG Parties' reliance on the deemed look-through provisions is misplaced. The purpose of those provisions is to attribute to members or partners income or gains made by the partnership. They are necessary because a partnership does not have its own existence as a taxable entity and it is intended to put the members of an LLP in the same position. Accordingly for CGT purposes, the members of an LLP are deemed to own fractional shares in the assets of the LLP (including its goodwill). If that LLP sold its assets, the gain, if any, would be attributed to its members according to the way that they share the capital profits.

102. However, the Members do not in fact own the assets - and that is relevant to asking, when characterising the payment on departure of an MDP Member, what the proper explanation for that payment is. The deemed look-through provisions at s 863 do not mean that any payment made by one partner to another is deemed, for tax purposes, to involve a disposal of assets.

103. This, we consider does correctly follow from the drafting of s 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 as partners, and

(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."

104. We agree with HMRC that, whilst s 863(1)(c) appears to deem the members as holding the property of the UK LLP as partnership property, this is only for income tax purposes (as may be seen by the introductory words at s 863(1)), and therefore can have no bearing on whether the individual members can be seen as holding such interests for the purposes of capital gains tax.

105. The equivalent language in s 59A TCGA 1992 is as follows:

"**Limited liability partnerships.**

(1)Where a limited liability partnership carries on a trade or business with a view to profit—

(a) assets held by the limited liability partnership are treated for the purposes of tax in respect of chargeable gains as held by its members as partners, and

(b) any dealings by the limited liability partnership are treated for those purposes as dealings by its members in partnership (and not by the limited liability partnership as such);

and tax in respect of chargeable gains accruing to the members of the limited liability partnership on the disposal of any of its assets shall be assessed and charged on them separately.

(2) For all purposes, except as otherwise provided, in the enactments relating to tax in respect of chargeable gains—

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

> (b) references to members of a 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.

106. Again, the focus of this section is on chargeable gains made by the partnership or LLP and the purpose of the provision is to look through the partnership or LLP and to allocate tax amongst the members. Its purpose is not to suggest that the partners can themselves deal separately with an interest in the capital assets of the partnership on the basis that they are the deemed part-owners of those assets.

107. Secondly, HMRC argued that even if the effect of the deemed look-through provisions was to put the Members of the UK LLP in the same position as the partners of a general partnership that were operating under a Partnership Agreement with similar terms to the LLPAs, the effect would not be that contended for by the BCG Parties.

108. Mr Callman (for HMRC) referred the Tribunal to section 20 of the Partnership Act 1890 (the "**1890 Act**"). Section 20(1) provides as follows:

> "All property and rights and interests in property originally brought into the partnership stock or acquired, whether by purchase or otherwise, on account of the firm, or for the purposes and in the course of the partnership business, are called in this Act "partnership property", and must be held and applied by the partners exclusively for the purposes of the partnership and in accordance with the partnership agreement."

109. As a result, Mr Callman argues that even if the LLP Members can be treated for all purposes as partners in a general partnership, they have no separately saleable ownership of any of the assets of the partnership, including goodwill.

Our conclusion in relation to the argument based on the deemed look-through provisions

110. HMRC's argument, especially coupled with the point that the goodwill is not saleable apart from the sale and business, seems to us to be correct in general and certainly when you consider what rights Members had under the 2011 LLPA.

111. In argument Mr Machell (for the BCG Parties) identified the notion of "goodwill" with the ability of MDPs to receive a part of any surplus on a winding up. However, that future expectation does not of itself mean that the MDPs are at any earlier time holding any recognisable capital asset. As we have seen, outside the context of a winding-up, any surplus on the sale of the business or any part of the business would not accrue to the MDPs as of right. More likely it would accrue to BCG Ltd. The premise that the MDPs' Clause 16.3(c) Right means that they have a current right in the (unquantified and unrealised) goodwill of the UK LLP at any point prior to a winding-up, therefore amounts to a serious flaw in the BCG Parties' analysis.

112. Even though it may be fair to recognise that goodwill does exist as a saleable asset, the MDPs have no enforceable legal right to receive any part of that payment for that asset unless that payment were to be immediately followed by a solvent winding-up of the UK LLP, something that the MDPs have no right or ability either individually or collectively to procure (as a result of BCG Ltd's magic vote). Neither would it, in our view, be likely that BCG Ltd would exercise its rights in that way. It would not consider this to be unfair to the MDPs as it would still expect to pay them under Schedule 3.

113. It follows that it is impossible to sustain the proposition that MDPs own (ahead of a winding-up) some interest in the goodwill of the UK LLP that they are "selling" under Schedule 3. The most that can be said is that on a "sale" they are giving up the Clause 16(3)(c) Rights that they have under the 2011 LLPA (a future and contingent right under a contract) in return for a payment. It is difficult to see how that transaction can be characterised as the sale of a capital interest in the UK LLP or an interest in its goodwill.

(3) The payments made under Schedule 3 do not reflect a genuine sale price

114. Another serious flaw in the BCG Parties' contention that the payments in question received by the MDP Partners represented payment in relation to sales of an interest is that, even if (contrary to our finding) the MDPs could be seen as owning some kind of interest amounting to capital asset in the form of their Clause 16.3(c) Rights, the proposition that the payments that they receive on a "sale" under Schedule 3 represents a fair or proper payment for giving up their Clause 16.3(c) Rights is clearly incorrect.

115. As we have seen, an MDP could only expect a payment under clause 16.3(c) on a future winding-up of the UK LLP. Any fair valuation of that right would need to take into account that it:

(1) will only produce a return at an unknown point in the future on the solvent winding-up of the UK LLP (for which there were and remain no current plans), and then only if the MDP is still a Member at that point or the transferee is or can become a Member and will hold that right;

(2) can be redetermined at any point by the Managing Partner; and

(3) for all practical purposes is not transferable except under Schedule 3.

116. The position is even more stark if one considers this from the viewpoint of the parties to the "sale". At a point where an MDP is about to retire or is approaching retirement, unless the solvent winding up of the UK LLP was imminent at that point, the Clause 16.3(c) Right would have no value to that Member – by the time any payment might accrue he would no longer be a Member. Conversely, if the buyer is BCG Ltd, at this point BCG Ltd has little reason to wish to purchase the retiring Member's Clause 16.3(c) Right - if the Member retires without BCG Ltd purchasing it, the Clause 16.3(c) Right would disappear anyway with the retirement of the "selling" Member, and BCG Ltd's residual right on a winding up would be increased just as much as if BCG Ltd had gone ahead with the purchase. The only exception would be (as a result of the priorities under the Schedule 16.3 Waterfall) if at the point of the winding-up there was not enough surplus on the winding up to repay in full the capital interests of the Members and pay BCG Ltd an amount equal to the calculated value of the purchased right calculated in accordance with Schedule 3 at that time.

117. Neither side produced any expert valuation evidence, but expert evidence was not needed for us to reach the obvious conclusion that the provisions of Schedule 3 which determine the "price" of the "sale", which have the effect of valuing the Capital Interests at the same value as if a winding-up was already underway, without any discount for the factors mentioned in the previous two paragraphs, hugely overvalues the Clause 16(3)(c) Right.

118. It is equally obvious that the real value to the MDPs of being granted the Capital Interests is that BCG Ltd agrees to make the payments calculated in accordance with Schedule 3. The Capital Interests are, in the language suggested by HMRC, a "token" whose value derives overwhelmingly from the agreement embodied in Schedule 3 to buy back that token at the price calculated under Schedule 3. We agree with this analysis - the notion that what is being paid is a genuine sale price based on some rational valuation of the Schedule 16.3(c) Right is unsupportable.

119. This analysis is also supported by a consideration of how the 2011 LLPA is drafted. The drafting puts the primary emphasis on the calculation of a "sale price" under Schedule 3, and then uses this figure to define what a Member might receive under the Clause 16 (3)(c) Right. The drafting is topsy-turvy if the intention was to define an interest in goodwill and then separately provide for a price at which that interest might be sold.

120. In fact the drafting solidly points to the truth of the matter. It is not that the payments were being made under Schedule 3 because the Members have a capital interest that BCG Ltd wanted to buy out. It is rather that to accord with the Framework, it was desired to provide the BCG Members with payouts on or approaching retirement by reference to increases in the value of the BCG Inc Shares. Clause 16.3(c) was merely ancillary drafting, designed to ensure that an MDP Member obtained something like the same treatment on solvent winding up as he or she would have received on a retirement. In other words, Clause 16.3(c) was there because of Schedule 3 – not the other way round.

121. Whilst we do not suggest that the drafting of the later LLPAs can be used as an aid to the interpretation of the 2011 LLPA, nevertheless, the fact that in the later LLPAs BCG removed clause 16.3(c) suggests that we are not wrong in our analysis.

(iv) Our conclusion in relation to the BCG Parties' overarching argument

122. In summary, our view in relation to the BCG Parties' overarching argument that payments under Schedule 3 relate to "sales" of "capital interests", is that MDPs do not own any identifiable capital interest that is capable of being sold. The most one could say (under the 2011 LLPA) is that the MDPs are given a future contingent right on a winding-up to a payment under Clause 16.3(c) that they give up when they engage in a "sale" under Schedule 3. However the valuation that is placed on this right at the point of "sale" is so wholly divorced from the real value (if any) of the future contingent right given up that it is clear that something is going on here that is different than the sale of that right. The true intention of the arrangements to provide a payment to the MDPs on or in anticipation of their retirement by reference to the increase in the value of the BCG Inc Shares over the period that they worked in the UK LLP as MDPs. Accordingly, the FTT was correct in finding that the payments made under Schedule 3 were not payments made in respect of any interest in the capital of the UK LLP or in its goodwill.

123. We therefore agree with the FTT that none of the payments made under Schedule 3 can be regarded as payments in respect of an interest in capital or in goodwill.

Alleged errors in construction of the 2011 LLPA

124. The BCG Parties argue further that the FTT misinterpreted and/or failed to take important terms of the LLPAs into account.

125. In the rest of this section we deal solely with the points made that are relevant directly to the interpretation of the 2011 LLPA, in accordance with its terms and having regard to the background to this agreement, although for the most part these arguments are also relevant to the later LLPAs.

(i) Construing the 2011 LLPA by reference to the later LLPAs

126. At [136] the FTT set out its conclusions on the nature of the Capital Interests. Subparagraph (4) read:

> "the winding up provisions in the 2014 LLPA aim to make clear that they had no rights on the winding up of the UK LLP and given that we were consistently told that the agreements were to be construed as not giving rise to changes of substance we must therefore conclude that the original LLPA did not provide any real rights on a winding up."

127. The BCG Parties submit that the FTT was therefore wrong to construe the 2011 LLPA by reference to the later LLPAs. We agree. However, as we have explained above, it does not follow that the BCG Parties' overarching argument succeeds.

(ii) A failure to take account of the language of the 2011 LLPA

128. The BCG Parties submit that the FTT wrongly failed to take into account that clause 3.1 of the 2011 LLPA refers to "the extent of each Member's interest in the capital of the Partnership". The FTT was wrong in failing to realise that this implemented the intention of the parties to the LLPA, which was to create interests in the capital assets of the UK LLP. Further, HMRC did not allege that any terms of the LLPAs were shams, and the FTT accepted at [138] Mr Holden's evidence as to the intended or actual effect of the rights created by the agreements. The FTT should have been slow to conclude that the drafting failed to achieve the commercial purpose of the parties, such a purpose forming part of the relevant background factual matrix which informed the proper interpretation of the LLPAs and was therefore to be taken into account when interpreting them. The BCG Parties cited *Arnold v Britton* [2015] AC 1619 as authority for this approach.

129. There is a short answer to this point. The FTT clearly understood the drafting and effect of the LLPAs, including the circumstances which would result in a payment to MDPs under Schedule 3 or under clause 16.3(c). The FTT was entitled to look at these provisions for their effect and to place little weight on the terminology chosen by the parties to characterise the nature of these payments in describing them as being in respect of a sale of "interests in the capital of the Partnership". In doing so, they were taking a similar approach to that taken by Henderson LJ at [117] in *BlueCrest*:

> "I add the obvious point that it is important not to be mesmerised by the word 'capital' in the phrase 'special capital'. The phrase is no more than a label, no doubt deliberately chosen to give the impression that a partner's special capital, and in particular the special capital of the corporate partner, was a form of partnership capital, and that its transfer would be analogous to a transfer of partnership capital or assets properly so-called."

130. The FTT were especially entitled to take the approach of putting little weight on the terminology chosen in the drafting of the 2011 LLPA given that it is a fair conclusion that the terminology chosen (such as talking about "units in the capital of the Partnership") had been chosen more for the impression it would give a reader rather than to reflect the nature of the rights.

(iii) A failure to take account of the position on an insolvency

131. The BCG Parties also submitted that the FTT did not take proper account of the fact that under the LLPA, UK MDPs were not entitled to any payment in respect of their Capital Interests were the LLP to become insolvent (e.g. under para 8.1 of Schedule 3 of the 2011 LLPA and should not have said (at [137]), that this was:

> "no more than a contractual term of the rights to payment on 'sale' of the Capital Interests".

132. This (the BCG Parties allege) was wrong: the FTT should have held that the position on insolvency supported the conclusion that the Capital Interests were interests in the capital profits of the LLP, rather than simply rights to payment measured by reference to any rise in the value of the BCG Inc Shares, since such a rise in value could clearly have arisen notwithstanding the insolvency of the UK LLP, but in those circumstances, the UK MDPs' interests in the capital profits of the UK LLP would not have entitled them to anything.

133. We see nothing in this argument to upset the conclusion that we have reached in relation to the BCG Parties' overarching argument.

134. The fact that no payment will be made under Schedule 3 in the circumstances described is not at all inconsistent with the conclusion that the FTT reached, with which we concur, that the MDPs had no interests in the capital or goodwill of the UK LLP that could be or were being "sold" under Schedule 3. There is nothing unnatural about the rights to a payment being subject to a term that there would be no payment on insolvency. That term is just as consistent with the "token" theory as it is with the "interest in capital" theory.

135. In fact, if anything it is slightly more consistent with the "token" theory. This is because it is possible that, even on an on insolvent winding-up, the Clause 16.3(c) Right would have value notwithstanding the insolvency of the LLP. This is because the holder of that right would, as we have seen, have priority over the return to the Members other than BCG Ltd of the balance of their capital accounts. If these were genuinely arrangements for BCG Ltd to buy out the Capital Interests of other Members, this raises the question why the sales should automatically be disapplied in circumstances where a Members' Capital Interests still might well have value to BCG Ltd. No similar question arises in relation to the "token theory" - the "token" could be issued on whatever terms BCG decided were appropriate.

(iii) Wrongly having regard to the sale price

136. The BCG Parties contend that the FTT also erred in regarding as legally relevant the fact that the payments made under Schedule 3 were not calculated by reference in the share of the goodwill or any asset of the UK LLP, but instead were calculated by reference to a rise in the value of the BCG Inc Shares.

137. This point was considered in the FTT Decision at various points:

(1) at [105]:

> "105. … "what is clear is that whatever scenario was envisaged, the Capital Interest holders would receive an amount calculated on a basis which had no direct relationship with the value of the UK LLP as again the amount is to be determined by applying the formula in the disposal provisions addressing the change in value of BCG Inc";

(2) at [116]:

> "116. However, in our view the way in which payments were calculated when paid to MDPs for their Capital Interests raises real questions as to the nature of those interests. It is clearly unusual to say the least for a departing partner to be paid for their share of the partnership on a basis which bears no direct relationship to the value of their stated rights in the partnership. It was possible for the value of the UK LLP to fall and the value of the BCG Inc shares to rise such that an MDP would be able to realise value relating to the worldwide group even when the UK business was struggling. The opposite was also possible – the value calculated by reference to the value of the global business could be less than the value of the UK business alone. The UK business only reflected about 5% of the value of the global business and therefore there was ample opportunity for a disparity to arise. Yet the Appellants argue that the rights were shares in the goodwill of the UK LLP. It is clearly unusual to say the least for a departing partner to be paid for their share of the partnership on a basis which bears no direct relationship to the value of their stated rights in the partnership";

(3) and at [133]:

> "133. Clearly arrangements under which a formula price is paid on disposal of members interests where that formula is not linked to the value of the business itself is unusual. The fact that the interest has no value on grant would tend to lead us away from the conclusion that the Capital Interests were in fact interests in the partnership itself."

138. The BCG Parties argue that:

(1) it was wrong for the FTT to put any weight on this feature, because as a matter of law, and as the FTT appears correctly to have accepted, an LLP and its members can decide to divide up the "shares" in an LLP in any way they wish;

(2) there is no legal requirement that shares in an LLP (including shares in capital profits from the disposal of its goodwill) must be attributed in proportion to a member's financial or other contribution;

(3) nor is there any requirement that the extent of an interest in capital profits should grow in direct proportion to the growth in the value of the LLP; and

(4) in this case, there was good reason for the arrangements adopted: to align the interests of the UK MDPs with the interests of the global group.

139. This point is linked to the further argument made by the BCG Parties that the FTT failed to understand the basis upon which the Capital Interests were a component of an MDP's "share" of UK LLP, i.e. one component of the bundle of rights or chose in action acquired by each MDP on becoming a Member in return for various liabilities accepted by the MDP, including liabilities to provide loan funding and capital contributions (contrary to the finding of the FTT at [64]. The fact that no separate purchase price was paid by the MDPs for the Capital Interests, or that no separate capital contribution was made specifically as "consideration" for a UK MDP's Capital Interest, does not render the Capital Interest any less a "right" or "asset", either as a matter of general law, or for tax purposes.

140. Those submissions are linked also to the BCG Parties' further argument that the FTT was wrong to find at [128] that because the Capital Interests had "no value" on grant, other than the hope that they would later rise in line with the value of the BCG Inc Shares, this pointed against them being an asset at all. They drew attention to the analogy, of an option to purchase a share at a future date at a price equal to its market value at the date of grant. Such an option is, they submitted, clearly an asset, even though it will only assume a positive value (aside from any "hope value") if the market value of the share subsequently rises above the option price. Similarly, a "growth share" which gives its holder a right to participate in the value of an entity above a hurdle which is set at the value of the entity on the date of issue is clearly an asset, even though it may have a nil value (other than "hope value") on the date it is issued.

141. We agree that there was a good reason for the arrangements adopted, and we agree that there is enormous freedom for the way that members of a UK LLP may divide up their interests amongst themselves through their LLP Agreement. Nevertheless, there are a number of problems with these arguments.

142. First, the concept of "shares in an LLP" does not have a recognised meaning, and certainly anything that was being "sold" under Schedule 3 is not recognisable as a share in the LLP in any meaningful sense. It is common when considering what constitutes the "share" of a member of an LLP or of a partner in a general partnership to take into account the various rights that a member or partner has as a result of his membership. These may include rights to income; rights to capital; voting rights or other rights to participate in the management or decision-making of the LLP. As we have seen, a "sale" under Schedule 3 of the 2011 LLPA involved no sale of any rights to income or voting rights, and the MDP Members of the LLP

had no ongoing right to capital that could be "sold". It would clearly be a misnomer to describe a "sale" under Schedule 3 as being the sale of the relevant Member's share in the LLP.

143. The more modest claim is that there might be an "interest" that is being "sold" under Schedule 3, but even this cannot withstand scrutiny.

144. As we have seen, the bundle of rights that might be said to comprise this "interest" appears to be limited to:

(1) the Clause 16.3(c) Right;

(2) the right and obligation to engage in a "sale" under Schedule 3 itself; and

(3) the obligation to allow the putative "interest" to be redeemed by the UK LLP for the calculated value.

145. Items (2) and (3) are the contractual provisions that are said to involve the "sale" or redemption of the Capital Interest, and so cannot themselves be or form part of the Capital Interest. Thus all that is left that could comprise the Capital Interest is the Clause 16.3(c) Right. As we have already discussed, this is merely a right of priority in the event of a future liquidation, and does not demonstrate any current interest in the LLP or any right of ownership in any particular asset (including goodwill) of the LLP.

146. Whether the Clause 16.3(c) Right is best described as a "right" or as an "interest" is perhaps a mere quibble about words, but the bigger point is that the FTT was not wrong in pointing to the artificiality involved in identifying the value of this right or interest with a rise in value of the BCG Inc Shares. This can be most clearly seen in the disjunct between what is paid under Schedule 3 (or would be paid on a redemption of the Capital Interest) and the real value of the Clause 16.3(c) Right at any point prior to an immediate liquidation of the UK LLP, as we have discussed above.

(iv) A failure to understand the effect of granting "interests"

147. The BCG Parties argue further that the FTT was wrong at [129] to assume that the introduction of new partners did not impact upon the value of the "interests" held by existing partners: in their submission, the introduction of new partners did have an impact on the value of the (residual) interest in the capital profits of the UK LLP, held by BCG Ltd.

148. As we have seen, it is true that the grant of Clause 16.3(c) Rights would in most circumstances come at the expense of the residual interest enjoyed by BCG Ltd on a winding -up (assuming that there was a sufficient surplus to pay out the capital accounts of other members, which was to take priority under the Clause 16 Waterfall). However, that is not to say that the FTT did not understand this point – at [129] it was not considering the effect on the interests held by BCG Ltd, but those held by MDPs. In any case, this has no bearing on the points that have caused us (in common with the FTT) to reject the BCG Parties' overarching argument.

(v) Wrongfully having regard to the nature of the purchaser of the Capital Interests

149. Finally the BCG Parties argue that for the purposes of analysing the tax consequences of the disposal of an interest in the LLP, it cannot matter that the interest in the LLP was acquired by another member of the LLP. The FTT therefore erred in law at [331] in holding that the disposal of Capital Interests did not involve the disposal of any interest in the UK LLP or its assets "as the money is paid by BCG Ltd".

150. We agree that the source of the consideration does not affect the analysis of the nature of the rights acquired. It is possible that there could be an arrangement where there was something that looked rather more like an interest or share in an LLP and where the sale of that interest to

another member of the LLP could be treated as the sale of a capital asset. However, for the reasons we have given, that was not what was happening here.

Conclusion in relation to the 2011 LLPA

151. In summary, none of the specific points put forward by the BCG Parties provide any good reason to overturn the FTT's overall finding, with which we concur, that the payments under Schedule 3 are not a payment for an interest in capital or in goodwill. They are also not a payment to buy-out a right created under clause 16.3(c) because the price paid at bears no relationship to the value of that right.

THE CAPITAL ISSUE UNDER THE 2014 LLPA AND THE 2016 LLPA

152. The 2014 LLPA is dated 1 December 2014 and the 2016 LLPA is dated 1 January 2016. We first consider the 2014 LLPA (including terms which are common to both LLPAs), followed by a discussion of the changes made in the 2016 LLPA.

The 2014 LLPA

153. As we have mentioned, the argument that the arrangements that are the subject of the FTT Decision involved the creation and sale of capital interests is even weaker as regards the arrangements under the 2014 LLPA. This is because the 2014 LLPA (amongst other amendments that are of lesser relevance) involved two changes from the provisions in the 2011 LLPA which are highly relevant to the Capital Issue.

154. The first is that under clause 3.7 it was provided that:

> "All capital profits shall belong to and be allocated to BCG Ltd."

155. The second is that the Clause 16.3 Waterfall was amended to delete Clause 16.3(c).

156. Given that no member other than BCG Ltd had any interest in any capital profits and that only BCG Ltd would receive any surplus that might be available on the sale of the business (for example as a result of a payment for goodwill), there is no conceivable "interest" that is being sold when payments are made under Schedule 3. The BCG Parties have nevertheless sought to maintain this argument on the basis of amendments made to definitions used in the 2014 LLPA.

157. Clause 1.1 of the 2014 LLPA introduced a new definition of "Capital Interests" as follows:

> "Capital Interests means, in respect of a Member, his interest (or, if part only of a Member's Interest is being sold, that part) in the capital of the Partnership for the time being represented by the Notional Number, such interest being:
>
> (a) a right to share, subject to the terms of this Agreement, in the assets of the LLP (including the right to participate in the proceeds of a disposal of the LLP or any of the LLP's capital assets (and in particular of the Business)) and
>
> (b) determined, at any date, by applying the A-B calculation specified in paragraph 2.1 of Schedule 3 as if that date were the Effective Date".

158. The "Notional Number" was then defined as:

> "Notional Number means a number of Series D.2 Shares (as defined in Schedule 3) as determined in accordance with the global policies of BCG Inc. Regarding the scope and extent of mandatory holdings of long-term capital in BCG (LTCV) by individuals who are both on the board of BCG Inc and members of The Boston Consulting Group, LLP. The Notional Number cannot be less than or equal to zero."

159. The BCG Parties argue that the FTT was wrong to pay any attention to clause 3.7 in the 2014 LLPA or to the same clause in the 2016 LLPA, submitting that those agreements needed to be read as a whole and in particular are "subject to" the rights "expressly created" by clause 1.1, clause 3.1 and Schedule 3.

160. However none of those provisions create any discernible interest. Clause 1.1 is not an operative clause. It contains definitions that are to be used in the operative clauses of the LLPA. The idea that this could be said to overrule the clear provisions of clause 3.7 in providing an ongoing interest for the MDPs in the capital profits of the UK LLP is not sustainable.

161. Clause 3.1, as redrafted for the 2014 LLPA (and appearing in the same form in the 2016 LLPA) provides as follows:

> "The extent of each Member's Capital Interests shall be determined solely by the board of BCG, Inc [sic] or the executive committee of that Board in accordance with BCG, Inc's global policies from time to time and the extent of such interest as so determined shall be notified to each Member by the Profit Allocation Committee. On each occasion on which a Member is notified of the granting of an additional Capital Interest, such Member shall also be notified of the Notional Number associated with such grant. No financial contribution shall be required to be made by a Member in order to acquire a Capital Interest. The value of the Capital Interest and the Notional Number shall not affect the level or amount of Profit which may (or may not) be allocated to the Member under this Agreement, and the Profit Allocation Committee shall not take into account the amount or value of Capital Interest held by any Member in determining the amount of Profit allocated to that (or any other) Member under clause 3.1 hereof."

162. The clause makes similar provision to that in clause 3.1 of the 2011 LLPA. The main changes are that it uses the defined term "Capital Interest" rather than the previously used phrase "interest in the capital of the Partnership"; it uses the defined term "Notional Number", rather than the previously used term "number of units in the capital of the Partnership that are being granted"; and that the granting of these interests is now to be made by the board of BCG Inc, rather than by the "Remuneration Committee" (which has been renamed the "Profit Allocation Committee in this and in the 2016 LLPA).

163. Schedule 3 makes similar provision to that made in Schedule 3 in the 2011 LLPA. The drafting is slightly modified to use the new defined terms, and there is a reduction in the number of occasions which give rise to a "sale" of a Capital Interest, so that this is limited to a sale on a Member becoming an Outgoing Member or on the member reaching at least 20 years' service as an officer of BCG Inc.

164. We do not accept the argument that, even taken together clause 1.1, clause 3.1 and Schedule 3 somehow create a genuine ongoing interest in the capital and/or goodwill of the LLP.

165. The BCG Parties' argument on this point boils down to an assertion that because the parties to the 2014 LLPA (and the later 2016 LLPA) had chosen wording that described the sale and purchase of interests in capital, such interests must exist, even if there is no identifiable content to such "interests".

166. This proposition is clearly wrong. As we have already mentioned, we are warned by the Court of Appeal in *BlueCrest* not to be mesmerised by the word "capital". The mere facts that in clause 1.1, clause 3.1 and Schedule 3 the term "Capital Interest" is used; and that term is defined by reference to the "interest" of the Member and as a right to share in the assets of the LLP, do not of themselves create any right that is recognisable as an interest.

167. The correct approach is that taken in *BlueCrest*. It is to identify what rights are granted to the Members that are said to be sold. Once this approach is taken then it is obvious that the BCG Parties' argument falls down. There is nothing in the LLPA that provides any content to any right that is said to be granted to the holders of a Capital Interest that amounts to any "share in the assets", for reasons we explain in the next following paragraphs.

168. Clearly, the right does not arise during the life of the UK LLP, as clause 3.7 allocates all capital profits to BCG Ltd. Neither does it arise on a winding up since this right is not represented at all in the Clause 16.3 Waterfall.

169. The definition of "Capital Interest" is used only in Schedule 3. There it is used only to define a notional asset that will be "purchased" under the Schedule 3 sale arrangements. But there is absolutely no right that is created that can be purchased under those arrangements.

170. The phrase could not refer to the interests of the MDPs in receiving their share of income profits. The profit sharing arrangements are expressly decoupled from the notion of Capital Interests.

171. Neither could the Capital Interest be considered to refer to the right to receive back the capital contributions that the MDPs were expected to contribute to the UK LLP (under the 2014 LLPA and the 2016 LLPA Members were required to contribute capital, to be credited to a capital account, rather than making a loan, as was required under the 2011 LLPA). These capital contributions were paid out following retirement separately to the "sale" being conducted under Schedule 3, and were also to be repaid in the event of a winding-up under the Clause 16.3 Waterfall.

172. Neither did the sale of a Capital Interest affect a Member's voting rights in the UK LLP.

173. The undeniable fact is that in "purchasing" Capital Interests under Schedule 3 to the 2014 and 2016 LLPAs, BCG Ltd was purchasing nothing. It obtained no further rights in the UK LLP after the "purchase" than it had before the "purchase".

174. At [109], the FTT recorded the evidence of Mr Holden that on a sale of the UK LLP's business, whilst BCG Ltd would receive the profits, UK MDPs would have a right to receive from BCG Ltd (or another nominated BCG entity) the current value of their Capital Interests. At [110], the FTT held that this evidence reinforced the conclusion that the new clause 3.7 overrode the definition of "Capital Interest" in clause 1.1. The BCG Parties argue that the FTT was wrong in concluding that payments to the MDPs were not payments in respect of the disposal of their interests in the UK LLP. But as we have shown, there was absolutely nothing that BCG Ltd would acquire through its purported "purchase", it follows that this argument must be wrong, and that the FTT's conclusion was right.

175. The BCG Parties put forward a curious justification as to why clause 16.3(c) had been removed from the Clause 16.3 Waterfall. They rely on the evidence of Mr Holden recorded in the FTT Decision at [108] that the reason for deleting clause 16.3(c) in the 2014 LLPA was that:

> "the assets of the UK LLP primarily comprise goodwill, so it was unlikely that Capital Interest holders would receive any value on an insolvent winding up."

176. This argument goes nowhere, except to reinforce the conclusion that the only thing which had been identified as something which the MDPs gave up on a "sale" of their "interest in the Partnership" under the 2011 UK LLPA had no real value and provided no justification for regarding the payments made under Schedule 3 as being payments for a capital asset.

177. It is undeniable that, under the provisions of the 2014 and 2016 LLPAs, BCG Ltd purchased nothing when it made payments under Schedule 3, and this provides a complete

answer which refutes the proposition that the Capital Interests involved a sale of some genuine interest in the UK LLP or its assets. However for completeness we will also address some further specific arguments raised by the BCG Parties in support of that proposition.

178. The first is that the BCG Parties argue that the defined "Capital Interest" referred to in clause 1.1 must be considered to create an interest in the capital of the UK LLP by reference to a principle of interpretation referred to as the "rule against redundancy". The argument was that, as clause 1.1 had defined an interest in the capital of the Partnership, it was incumbent on the Tribunal to give meaning to that phrase, even if that phrase was included in a definition and the operative clauses of the 2014 LLPA left no scope for any such interest. There are two problems with that argument that render it untenable.

(1) Firstly, it is impossible to say what meaning could be given to the phrase. These later LLPAs expressly ruled out any share for the MDPs in a capital surplus, either during the life of the UK LLP or on its winding up, and as we have explained, there is nothing else comprised in the interests of the MDPs that BCG Ltd would acquire through a "purchase". As a result, there is no conceivable interpretation of the defined phrase "Capital Interest" that would afford the Members any "interest" in the UK LLP that would not contradict the express words of the 2014 and 2016 LLPAs. It is patently the case that under the later LLPAs the Capital Interests issued had no existence except as a token to be redeemed through a "sale" (or redemption) under Schedule 3. The purchase back or redemption of such a token cannot properly be described as the sale of an interest under the UK LLP.

(2) The second difficulty is that there is no redundancy. The defined term "Capital Interests" does have a use in Schedule 3, so the definition cannot be otiose. It is used to define the circumstances in which there will be a payment under Schedule 3. It is not used to define, however, anything that is recognisable as an interest that is being sold under Schedule 3 other than the "token" created when Capital Interests are issued.

179. The BCG Parties also seek to make something of the argument that there was also an ability for the UK LLP to redeem the Capital Interests. However, such a redemption was not itself a valuable right of the MDPs - but rather was something that could be forced upon them. This right was merely another way in which the "token" that the Capital Interests represented could be cashed out. It was not something that BCG Ltd could be considered to be paying for when it made payments under Schedule 3.

180. The BCG Parties have a further argument that the interests created by the 2011 LLPA could not have been retrospectively extinguished by the terms of the later 2014 LLPA. This argument falls down, however, when one realises, as we have explained above, that the true value of the Capital Interests even under the 2011 LLPA was their value as a "token" to be cashed in through a sale under Schedule 3. That aspect was not changed through the adoption of the 2014 LLPA (or the 2016 LLPA). The fact that the changes were made in the 2014 LLPA (which occurred as far as we are aware without provoking any resistance from the MDPs), only serves to highlight the lack of importance to the arrangements of the clause 16.3(c) Rights under the 2011 LLPA.

181. Finally, we will address the argument that for the purposes of analysing the tax consequences of the disposal of an interest in the LLP, it cannot matter that the interest was acquired by another member of the LLP, that the FTT must have erred in law at [331] in holding that the disposal of Capital Interests did not involve the disposal of any interest in the UK LLP or its assets "*as the money is paid by BCG Ltd*". The source of the consideration does not affect the analysis of the nature of the rights acquired. The grant and subsequent sale of the

Capital Interests were ordinary transactions involving disposals of shares between (deemed) partners, in accordance with the terms of the LLPAs.

182. We agree that the fact that money was to be paid by BCG Ltd was not relevant if there was anything that was genuinely identifiable as being an interest in capital that was being paid for with that money. However as we have explained no such interest in capital can be discerned under the 2014 LLP or the 2016 LLPA and the only interest that might be considered to exist under the 2011 LLPA (if it can be considered an "interest", which is doubtful) is the Clause 16.3(c) Right and the quantum of the payment due under Schedule 3 payments is so divorced from any rational value of that right that the arrangement cannot be viewed as a sale.

The 2016 LLPA

183. The FTT described the reasons for the changes as between the 2014 LLPA and the 2016 LLPA as follows:

> "113. In 2016 further changes were made to the LLPA with the intention that MDP should be able to claim Entrepreneurs' Relief in respect of disposals of the Capital Interests. (In essence, where previously a MDP would have been required to sell a portion of their Capital Interests on a particular date prior to retirement, the changes meant that the value of those Capital Interests would be frozen until the disposal provisions applied on retirement. In the meantime the MDP received an additional amount by way of additional allocation of UK LLP profit calculated by applying a rate of interest to the value of the frozen Capital Interests.)
>
> 114. Notably Mr Holden describes the change in the following way: 'Specifically, BCG's concern, following discussions with PwC, was that the Capital Interests might be viewed as an interest in the goodwill of the UK LLP and BCG Ltd might be treated as a close company such that a sale of Capital Interests might not qualify for Entrepreneurs' Relief as a result of changes made in the Finance Act 2015'…".

184. The evidence here relied on by the FTT was from Mr Holden's first witness statement. The FTT said that BCG's approach as explained by Mr Holden was:

> "not consistent with the current position of the Appellants that the Capital Interests were very clearly interests in the goodwill of the UK LLP".

The BCG Parties challenged that conclusion on the basis that Mr Holden had given further evidence in his second witness statement, which the FTT had not taken into account. HMRC responded by saying that whether or not Mr Holden thought the disposal of Capital Interests was a disposal of goodwill is irrelevant. We agree. At its highest, this argument goes no further than to show that the parties to the 2016 UK LLPA *thought* that they had created a structure which involved trading in a capital asset. That does not provide any reliable guide as to whether they had been successful in doing so.

185. In oral submissions, Mr Callman drew our attention to the part of [113] where the FTT found as a fact that:

> "the changes meant that the value of those Capital Interests would be frozen until the disposal provisions applied on retirement. In the meantime the MDP received an additional amount by way of additional allocation of UK LLP profit".

He pointed out that "freezing" the value of the Capital Interest and paying that MDP an additional amount by way of profit share "doesn't sit at all comfortably" with the Capital Interests being an interest in capital. We agree. It is another indication that the Capital Interests were not interests in capital at all.

Conclusion in relation to the 2014 LLPA and the 2016 LLPA

186. For these reasons, and the other reasons we have already given in relation to the 2011 LLPA, we consider that the FTT was correct to find that there was no sale of a capital interest under the 2014 and 2016 LLPAs.

THE MMR ISSUE

187. In relation to the MMR Issue, the starting point is ITTOIA s 848, which is headed "Assessment of partnerships". It reads:

> "Unless otherwise indicated (whether expressly or by implication), a firm is not to be regarded for income tax purposes as an entity separate and distinct from the partners."

188. ITTOIA s 850 is headed "Allocation of firm's profits or losses between partners" and until 5 April 2014, subsection (1) provided:

> "For any period of account a partner's share of a profit or loss of a trade carried on by a firm is determined for income tax purposes in accordance with the firm's profit-sharing arrangements during that period.
>
> This is subject to sections 850A and 850B."

189. It was common ground that neither s 850A nor s 850B applied, and the FTT found at [272] that the Capital Interests should not be treated as part of the allocation of profit of the UK LLP under s 850. HMRC sought permission to appeal that finding, but permission was refused by the FTT, and HMRC did not renew that application for permission at the UT.

190. New sections 850C to 850E were inserted into ITTOIA by FA 2014 s 74 and Sch 17 para 7(1), (3), and were in force for the three years 2014-15 to 2016-17. The effect of the new provisions was to reallocate profits from a corporate partner to individual partners for tax purposes in certain circumstances. In *Walewski v HMRC* [2021] UKUT 0133 (TCC) at [2], the UT held that:

> "The purpose of the rule is to prevent individual partners making arrangements which seek to accumulate profits in a corporate partner at a lower tax rate – for example, benefitting from the rate of corporation tax which is lower than the higher or additional rate of income tax."

191. The FTT correctly said at [280]:

> "Benefiting from a lower corporation tax rate is only one example of the type of arrangements which *Walewski* describes as being the target of s850C. However the core element of the purpose of the rule is to prevent individual partners making arrangements which seek to accumulate profits in a corporate partner."

192. By s 850C(1), reallocation takes place if:

> "(a) for a period of account ("the relevant period of account")—
>
> > (i) the calculation under section 849 in relation to an individual partner ("A")…produces a profit for the firm, and
> >
> > (ii) A's share of that profit determined under section 850 or 850A ("A's profit share") is a profit or is neither a profit nor a loss,
>
> (b) a non-individual partner ("B")…has a share of the profit for the firm mentioned in paragraph (a)(i) ("B's profit share") which is a profit (see subsection (7)), and
>
> (c) condition X or Y is met."

193. It was common ground that s 850C(1)(a) and (b) were satisfied. The issue was whether Condition X and/or Condition Y was met.

194. The FTT made the following relevant findings of fact:

(1) In 2011, BCG Ltd contributed its business to the UK LLP; the book value of the assets of that business was £5.7m and that amount was credited to BCG Ltd's capital contribution account. In June 2013 BCG Ltd contributed a leasehold property to the UK LLP with a book value in excess of £3.5 million. That amount also was credited to BCG Ltd's capital contribution account with the UK LLP. A total of a little under £9.3m was thus standing to the credit of that account during the relevant years, see [71]-[73] and [102].

(2) The UK LLP's allocation of profits was made under the terms of the LLPAs by the UK LLP's remuneration committee applying the Framework after an initial retention of what was described as the "18% margin" to fund the future liability under the LTCV and also to fund the worldwide business[1], see [76] and [98(1)].

(3) The 18% margin so allocated was thus not included in the profit pool to be shared between the MDPs and BCG Ltd, see [288].

(4) For tax purposes all the LLP's profits are allocated each year under s 850. The 18% margin was not allocated to the MDPs, so must therefore have been allocated to BCG Ltd, see [288].

(5) MDPs were given annual statements of how much their Capital Interests had increased in value each year, see [143(2)].

(6) The quantum of the profits allocated to BCG Ltd in the relevant years was as follows, see [14]:

Tax year	Profit allocated to BCG Ltd by UK LLP
2012-13	£42,376,848
2013-14	£22,317,086
2014-15	£29,841,003
2015-16	£17,504,385
2016-17	£29,783,247

(7) The 18% margin was said by the FTT to have been retained on the balance sheet of the UK LLP, see [98(1)]. This finding was challenged by the BCG Parties under *Edwards v Bairstow* [1956] AC 14, see §211 below.

(8) The Capital Interests were part of the MDP's reward for services provided, see [143]. This finding was also challenged, see §271 to §280 below.

(9) The Capital Interests were valued at each balance sheet date and were included as liabilities in the statutory accounts of BCG Ltd. Those accounts state that "the fair value of the services provided are recorded against investment in the UK LLP with the corresponding liability recorded within [the] company at each reporting period end", see [122]-[124].

[1] The 18% margin" was perhaps a misnomer as it appears this was not always the percentage applied, but it was common ground that something similar was applied, and we have therefore continued to refer to this prior charge on profits as the "18% margin".

(10) In practice the UK LLP satisfied BCG Ltd's obligation to pay MDPs on the "sale" of Capital Interests on behalf of BCG Ltd, and the resulting intra-group balance was settled on an annual basis, see [97].

Condition X

195. ITTOIA s 850C(2) provides as follows:

> "Condition X is that it is reasonable to suppose that—
>
> (a) amounts representing A's deferred profit (see subsection (8)) are included in B's profit share, and
>
> (b) in consequence, both A's profit share and the relevant tax amount (see subsection (9)) are lower than they would otherwise have been."

196. Section 850C(8) provides:

> "'A's deferred profit'—
>
> (a) is any remuneration or other benefits or returns the provision of which to A has been deferred (whether pending the meeting of any conditions (including conditions which may never be met) or otherwise), and
>
> (b) includes A's share (as determined on a just and reasonable basis) of any remuneration or other benefits or returns the provision of which to A and one or more other persons, taken together, has been deferred (whether pending the meeting of any conditions (including conditions which may never be met) or otherwise)."

197. Subsection (9) defines "the relevant tax amount" as "the total amount of tax which, apart from this section, would be chargeable in respect of A and B's income as partners in the firm".

198. The FTT held at [282] to [289] that:

(1) the Capital Interests were "deferred profit" of the MDPs because the amounts paid out to them were "benefits", the provision of which had been "deferred"; and

(2) amounts representing the deferred profit had been included in BCG Ltd's profit share.

199. The FTT then considered whether "in consequence" of the amount representing the MDPs' deferred profit being included in BCG Ltd's profit share, the MDP's profit shares and the relevant tax amounts were lower than they would otherwise have been. The parties termed this "the counterfactual test".

200. The FTT held at [290] that if the Capital Interests did not exist "there would be another structure or instrument tracking the value of BCG Inc used to provide the LTCV even if this was taxed on an income basis…rather than a capital gains tax basis and the 18% would still be retained by the group". The FTT therefore found that Condition X was not met. HMRC appealed on the basis that the FTT had made an error of law in its approach to the counterfactual test.

201. The BCG parties invited us to reject this challenge, submitting that the FTT had made an "evaluative judgment" with which we should be slow to interfere. Mr Grodzinski referred to *Designers Guild Ltd v Russell Williams (Textiles) Ltd* [2000] 1 WLR 2416 where Lord Hoffmann said at p 2423:

> "…because the decision involves the application of a not altogether precise legal standard to a combination of features of varying importance, I think that this falls within the class of case in which an appellate court should not reverse a judge's decision unless he has erred in principle."

202. We reject that submission. Condition X is part of a targeted anti-avoidance provision with specific prescriptive requirements, each of which must be satisfied for the Condition to apply. It is the polar opposite of a case which "involves the application of a not altogether precise legal standard to a combination of features of varying importance".

203. Although the BCG Parties also submitted that the FTT had approached the counterfactual test correctly, their Respondents' Notice also challenged the FTT's findings on the other parts of Condition X. We next consider each of the requirements for Condition X to apply.

Deferred profit

204. Section 850C(2)(a) requires that "amounts representing A's deferred profit… are included in B's profit share", with the meaning of "deferred profit" being set out at subsection (8), see §196 above.

205. The FTT, rightly in our view, held that the terminology used in subsection (8), being "remuneration, benefits, or returns" shows "a clear purpose of casting the net widely", and that the same is true of s 850C(8), which provides that a deferral is included if it takes place "pending the meeting of any conditions (including conditions which and may never be met) or otherwise". The FTT found that the amounts provided to the MDPs on the disposal of their Capital Interests were deferred benefits.

206. The BCG Parties submitted that no benefit had been deferred, because the Capital Interests conferred "an immediate entitlement to share in capital profits of the UK LLP measured by reference to any growth in the D2 share value". We reject that submission, and instead agree with the FTT that, given the wide scope of the provision, the sums payable to the MDPs on "sale" of the Capital Interests were a "benefit" within the meaning of the subsection, and the benefit was "deferred" until payment was made, which was some time (usually years) after the grant.

207. The BCG Parties also submitted that the statutory test is only met if it is possible to identify "a counterfactual scenario in which that benefit was to be provided to the relevant person at an earlier date", and it must be "possible to point to an entitlement that would have arisen but did not". In other words, only the deferral of a specific quantifiable entitlement satisfies the test.

208. We also reject that submission. The wording of s 850C(8)(b) provides that "deferred profit" includes a person's "share" of any deferred benefit to be provided to more than one person, with that share being determined "on a just and reasonable basis". As the FTT said at [285], the statute contains "no requirement that there is an entitlement which is crystallised prior to the deferral".

209. We therefore uphold the FTT's findings on deferred profit.

Included in profit share

210. The FTT found that amounts representing the deferred profit were included in BCG Ltd's profit share, saying at [288]:

> "18% of the group's 'adjusted margin' on a global basis is retained within the BCG group in order to fund the LTCVs. Quite how the adjusted margin precisely relates to the accounting profit is not addressed in the evidence but that does not matter. The important fact is that that a portion [*sic*] of the UK LLP's profits are set aside and are not available to be allocated by the Remuneration Committee. For tax purposes all of the profits are allocated each year under s850 and this amount is therefore allocated for those purposes to BCG Ltd. Therefore the 18% which is considered to provide for the liabilities arising on the "sale" of the Capital Interests is included in BCG Ltd's profit

> share for tax purposes. The fact that BCG Ltd does not then warehouse the 18% does not affect the underlying point that an amount which is seen to represent the potential liability under the terms of the Capital Interests is allocated to BCG Ltd."

211. The BCG Parties' first submission on this point was that the FTT's reasoning was underpinned by and depended on their earlier finding at [98(1)] that the UK LLP had retained the 18% margin on its balance sheet. That finding was, said Mr Grodzinski, an error of law which met the threshold set by *Edwards v Bairstow*, because it was clear from the evidence that the 18% was retained by BCG Inc in accordance with the Framework and it was not on UK LLP's balance sheet..

212. We agree that the FTT was wrong to say at [98(1)] that the UK LLP had retained the 18% on its balance sheet. But that error does not underpin its findings about Condition X. The FTT instead based their conclusion on the following facts, which were unchallenged:

(1) 18% of the group's "adjusted margin" on a global basis is retained within the BCG group in order to fund the LTCVs.

(2) All of the UK LLP's profit was allocated between the members of that LLP for tax purposes.

(3) For tax purposes 18% of the UK LLP's profit was not allocated to the MDPs, and therefore must have been allocated to BCG Ltd (alongside any further profit that might have been allocated to BCG Ltd).

(4) A portion of the UK LLP's profits had therefore been set aside and was not available to be allocated by the Remuneration Committee.

213. The BCG Parties' second argument under this heading was that (a) as Condition X requires that "amounts *representing* [an MDP's] deferred profit are included in [BCG Ltd's] profit share", and (b) as the 18% was not on the balance sheet of BCG Ltd, the statutory test was not met because there was "no decision to set aside in the UK either 18% or any particular percentage for that purpose". They said that in consequence it was an error of law for the FTT to find that amounts *representing* the deferred benefits payable to the MDPs had been included in BCG Ltd's profit share.

214. However, we agree with the FTT that it does not matter "quite how the adjusted margin precisely relates to the accounting profit" of BCG Ltd. That is because Condition X begins by saying "it is reasonable to assume that". On the unchallenged facts, the 18% was allocated to BCG Ltd for tax purposes; BCG Ltd (or its designate) was required to "purchase" the Capital Interests from the MDPs; BCG Ltd's profit share was more than sufficient to pay the MDPs on disposal of their Capital Interests; and although in practice the payments were made by the UK LLP, it made those payments on BCG Ltd's behalf and the resulting intra-group balance was settled on an annual basis. It is thus reasonable to assume that the MDPs' deferred benefits were included in BCG Ltd's profit share.

The counterfactual test

215. The final point in relation to Condition X was the requirement at s 850C(2)(b) that, in consequence of amounts representing the MDP's deferred profit being included in BCG Ltd's profit share, it was reasonable to assume that:

(1) the MDP's profit share was lower than it otherwise would have been; and

(2) the total amount of tax chargeable in respect of the MDP's income and BCG Ltd's income as partners in the firm was lower than it would have been had the Condition not applied.

216. The FTT held at [290] that if the MDPs' deferred benefit had not been included in BCG Ltd's profit share, it was reasonable to assume that the MDPs' profit share would not have increased, and as a result Condition X was not satisfied. The FTT came to that finding on the basis that:

(1) The LTCV was a global programme which applied to all MDPs worldwide.

(2) If the LLPAs did not exist, a different arrangement would have been implemented which would also have tracked the value of BCG Inc.

(3) That arrangement would not have increased the MDPs' profit shares, because UK MDPs would then have profit shares which were out of line with those of MDPs in other jurisdictions.

(4) The amounts received under that different arrangement might have been taxed on an income basis (as is the case in some jurisdictions) rather than a capital gains tax basis.

217. We agree with HMRC that this approach misunderstands what is required to satisfy Condition X. The statutory question is whether it is reasonable to assume that the MDP's profit share is lower than it otherwise would have been as a consequence of the MDP's deferred profits being included in BCG Ltd's profit share. When answering that question, the starting point is that:

(1) an LLP is not "to be regarded for tax purposes as an entity separate and distinct from the partners"; and

(2) the whole of an LLP's profit must be allocated to the partners for tax purposes, see ITTOIA ss 848 and 850. If an MDP's deferred profit had not been included in BCG Ltd's profit share, it is plainly reasonable to assume that it would have been included in the MDP's profit share. The only alternative would have been for it to be included in the profit share of a different MDP, and that is not a reasonable assumption.

218. As HMRC say in their skeleton argument, it was an error of law for the FTT to answer the statutory question on the basis that "a different system to provide deferred profit would be introduced". HMRC continued that submission as follows:

> "This cannot be the way that s 850C is intended to operate: the question is whether it is reasonable to suppose that the shares for the individuals would be higher if profit was not being deferred (and that deferred profit being represented in the corporate member's share). This cannot be answered by saying that there would be a different system for conferring later benefits on partners (i.e. deferring profit) which would also be represented in the corporate member's share, with the certain consequence that there would be no change in the individuals' shares. This would make it impossible to satisfy Condition X: it amounts to saying that if this system of deferring profit did not exist there must be some sort of alternative that would also defer profit, but somehow escape Condition X. The correct counterfactual has to ask whether the individuals would be allocated more profit if there was no system of deferred profit being used."

219. We agree with that submission. There is thus no need to speculate as to how the global business would have implemented the LTCV in the UK had it used a different approach instead of the LLPAs.

220. However, for completeness we make the following observations about the FTT's analysis. It was based on two key points, namely:

(1) that the global firm wanted all MDPs to participate in the LTCV, and

(2) participation in the LTCV would not have been achieved by allocating profits to the UK MDPs, because this would have created a disparity in terms of profit share as between UK MDPs and others.

221. We disagree. Although the LTCV was common to all MDPs, it was implemented differently in the various jurisdictions, so there was no need for there to be absolute parity. More importantly, the FTT did not here distinguish between the allocation of profit for tax purposes and the distribution of those profits. It would be perfectly possible for profits to be allocated for tax purposes, but for the business to implement a deferral of payment mechanism which sat outside the tax system and achieved parity of timing with MDPs in other jurisdictions. Thus, even using the FTT's incorrect counterfactual approach, the fact that there was a global LTCV did not prevent all of the UK LLP's annual profits being allocated to the MDPs for tax purposes.

222. The final point is whether, in consequence of amounts representing the MDPs' deferred profit being included in BCG Ltd's profit share, the relevant tax amount was also lower than it would otherwise have been. Since BCG Ltd pays tax on its profits at the corporation tax rate, which is lower than the tax rate charged to individual MDPs, this requirement was also met.

Conclusion on Condition X

223. We therefore find (agreeing with the FTT) that amounts representing the MDP's deferred profit share were included in the profit share of BCG Ltd, but we also find (disagreeing with the FTT) that in consequence, the MDPs' profit shares were lower than they would otherwise have been, and so too was the relevant tax amount. It follows that Condition X is met.

Condition Y

224. Section 850C(3) provides:

> "Condition Y is that—
>
> (a) B's profit share exceeds the appropriate notional profit (see subsections (10) to (17)),
>
> (b) A has the power to enjoy B's profit share ("A's power to enjoy") (see subsections (18) to (21)), and
>
> (c) it is reasonable to suppose that
>
> (i) the whole or any part of B's profit share is attributable to A's power to enjoy, and
>
> (ii) both A's profit share and the relevant tax amount (see subsection (9)) are lower than they would have been in the absence of A's power to enjoy."

225. The "appropriate notional profit" is defined by s 850C(10) as the sum of the appropriate notional return on capital and the appropriate notional consideration for services. Subsection (11) then reads:

> "'the appropriate notional return on capital' is —
>
> (a) the return which B would receive for the relevant period of account in respect of B's contribution to the firm were the return to be calculated on the basis mentioned in subsection (12), less
>
> (b) any return actually received for the relevant period of account in respect of B's contribution to the firm which is not included in B's profit share."

226. There are then further provisions about how “B's contribution to the firm” and the “return” mentioned in subsection (11) is to be calculated, but as those provisions were not in issue, we have not set them out here.

227. Subsection (18) to (21) explain what is meant by “power to enjoy”:

> “(18) A has the power to enjoy B's profit share if—
>
> (a) A is connected with B by virtue of a provision of section 993 of ITA 2007 (meaning of “connected” persons) other than subsection (4) of that section,
>
> (b) A is a party to arrangements the main purpose, or one of the main purposes, of which is to secure that an amount included in B's profit share—
>
> (i) is charged to corporation tax rather than income tax, or
>
> (ii) is otherwise subject to the provisions of the Corporation Tax Acts rather than the provisions of the Income Tax Acts, or
>
> (c) any of the enjoyment conditions (see subsection (20)) is met in relation to B's profit share or any part of B's profit share.
>
> (19) In subsection (18)(b) *“arrangements”* includes any agreement, understanding, scheme, transaction or series of transactions (whether or not legally enforceable)
>
> (20) The enjoyment conditions are—
>
> (a) B's profit share, or the part, is in fact so dealt with by any person as to be calculated at some time to enure for the benefit of A, whether in the form of income or not;
>
> (b) the receipt or accrual of B's profit share, or the part, by or to B operates to increase the value to A of any assets held by, or for the benefit of, A;
>
> (c) A receives or is entitled to receive at any time any benefit provided or to be provided (directly or indirectly) out of B's profit share or the part;
>
> (d) A may become entitled to the beneficial enjoyment of B's profit share, or the part, if one or more powers are exercised or successively exercised by any person;
>
> (e) A is able in any manner to control (directly or indirectly) the application of B's profit share or the part.
>
> (21) In subsection (20) references to A include any person connected with A apart from B.”

228. The FTT held that BCG Ltd’s share of the profit exceeded the appropriate notional profit, and that the MDPs had “power to enjoy” BCG Ltd’s profit share, see [307] and [314]. However, the FTT went on to find at [317] for the same reasons as in relation to Condition X, that the counterfactual test was not met, because an MDP’s profit share and the relevant tax amount were not lower than they would have been in the absence of the MDP’s power to enjoy. As a result, the FTT concluded that Condition Y was not met.

229. HMRC appealed on the basis that the FTT had made an error of law in its approach to the counterfactual test. The BCG Parties repeated their submission about the FTT having made an evaluative judgment, but we reject that submission for the same reasons as given above in relation to Condition X - see §202.

230. The BCG Parties also submitted that the FTT had approached the counterfactual test correctly, but in their Respondents' Notice they challenged some of the FTT's findings on other parts of Condition Y. We next consider those challenges and the counterfactual test.

Exceeds the appropriate notional profit

231. The FTT correctly summarised the "appropriate notional profit" as being "a return calculated on the basis of an amount of money equal to B's (BCG Ltd's) contribution to the UK LLP at a commercial rate of interest" - see [293].

232. It was common ground before the FTT that:

(1) the amount contributed as capital by BCG Ltd is the amount reflecting its contribution of the business to the UK LLP in 2011. together with the value of the lease it transferred in 2013; and

(2) the value of the lease contributed was in excess of £3.5m.

233. However, the parties did not agree as to how the value of the business contribution was calculated, with the appellants submitting that the increase in the value of the business should be taken into account on an annual basis. The FTT considered *Popat*[2] and *Hamilton and Kinneil* [2015] UKUT 130 (TCC) ("***Kinneil***") before rejecting the appellants' submissions and finding that the figure was the £5.7m contributed by BCG Ltd when the LLP was set up, see [305].

234. In their Respondents' Notice, the BCG Parties said that the FTT had made an error of law because "the approach in *Kinneil* does not apply" when interpreting s 850C. However, in their skeleton argument, they said this:

> "…because the BCG Parties recognise that the FTT's reasoning was largely based on the decision in *Kinneil* (a decision of the UT, Warren J), the BCG Parties do not repeat their detailed legal arguments on this point made below and do not invite the UT to determine the point in their favour at this level. Instead, they respectfully seek to preserve their right to argue the point, should the case proceed further, where BCG would (in so far as necessary) argue that the decision in *Kinneil* was distinguishable and/or wrong in law, and that the FTT's Decision on this issue was also wrong."

235. On the first day of the hearing, Mr Grodzinski essentially repeated that passage, adding:

> "…given how many other issues there are for the Tribunal to decide, and given that there would be no need to ever get to this complicated bit of statutory interpretation if we win on the last limb of condition Y, as we won on the last limb of condition X, we took the view that it would be better not to spend the time necessary to properly argue this point and to preserve our position on the question of statutory construction should, perish the thought, this case ever reach the Court of Appeal."

236. As a result, we heard no submissions challenging the FTT's finding that "the amount which BCG Ltd has contributed to the UK LLP as capital is £9.3m". We disapprove of the approach taken by the BCG Parties, for the following reasons:

(1) A UT panel can obviously distinguish the facts and/or law in one appeal from the facts and/or law considered by a different panel, and come to a different conclusion. Given that the BCG Parties' Respondents' Notice stated that "the approach in *Kinneil* does not apply" when interpreting s 850C, there was no good reason why they did not explain, as part of their case at this hearing, the reasons for distinguishing *Kinneil* from the facts of the instant case.

[2] Incorrectly transcribed as *Papat* in the judgment

(2) Even if the facts and law were essentially identical, a UT panel can come to a different conclusion from a previous panel, if convinced the earlier judgment was wrong, see for example *Medpro Healthcare v HMRC* [2025] UKUT 00255.

(3) If this case were to proceed to the Court of Appeal, the judges there will not have the benefit of our consideration of the issue after having heard full argument.

(4) As we pointed out to Mr Grodzinski at the hearing, a failure to put forward part of a party's case cannot be justified by reference to a trial timetable which had been agreed by the parties themselves. Had the BCG Parties decided to make submissions on this point, a different timetable could have been agreed.

237. For the avoidance of doubt, we did not give the BCG Parties permission to "reserve their right" or "preserve their right" to make submissions on this point at the Court of Appeal. Should the BCG Parties seek to raise it before that Court, it will be a matter for that Court to decide whether to allow it to proceed.

Power to enjoy

238. The "power to enjoy" test is satisfied if a person meets any one of three separate requirements. The FTT considered the third of these, namely whether "any of the enjoyment conditions were met", and concluded at [313] that condition (c) was satisfied, because the MDPs receive or are entitled to receive at any time any benefit provided or to be provided (directly or indirectly) out of BCG Ltd's profit share. The FTT held that:

(1) the term "benefit" was to be given a broad interpretation;

(2) the benefit was provided by the "sale" of the Capital Interests to BCG Ltd or another person nominated by that company; and

(3) "in the ordinary course, the expectation of the parties is that the 'benefit' will be provided out of that retention of profits allocated to BCG Ltd".

239. The BCG Parties challenged the FTT's finding that condition (c) was satisfied, saying that the enjoyment conditions had been based on the Transfer of Assets Abroad ("**ToAA**") provisions set out in the Income Tax Act Part 13, Chapter 2, but that as Parliament had decided to omit ITA s 722(3) and (4) when legislating to include s 850C-E in ITTOIA.

240. Those ToAA provisions read:

> "(3) In determining whether an individual has power to enjoy income for the purposes of section 721, regard must be had to the substantial result and effect of all the relevant transactions.
>
> (4) In making that determination all benefits which may at any time accrue to the individual as a result of the transfer and any associated operations must be taken into account, irrespective of–
>
> (a) the nature or form of the benefits, or
>
> (b) whether the individual has legal or equitable rights in respect of the benefits."

241. We were provided with no extra-statutory materials to support the BCG Parties' submission, and no precedent was cited in which a court has held that a provision in one Act should be interpreted with reference to an absence of words when compared to a different provision contained in another Act.

242. The correct principles of statutory interpretation were instead summarised by Lord Hodge in *R (O) v SSHD* [2022] UKSC 3; [2023] AC 255 at [29], when he said that the words of the statute "are the words which Parliament has chosen to enact as an expression of the

purpose of the legislation and are therefore the primary source by which meaning is ascertained" and that "[e]xternal aids to interpretation therefore must play a secondary role". The words we are required to consider are those at condition (c), which reads (our emphasis) "A receives or is entitled to receive at *any time any benefit* provided or *to be provided (directly or indirectly)* out of B's profit share or the part". As the FTT found, these are broadly drafted provisions.

243. The BCG Parties also challenged the FTT's finding that the "benefit" was provided or to be provided (directly or indirectly) out of BCG Ltd's profit share, saying that:

(1) the funds to purchase the Capital Interests may have been acquired out of funds other than those available to BCG Ltd; and

(2) BCG Ltd was not the only "purchaser", and the UK LLP might have redeemed the Capital Interests.

244. However, as the FTT correctly said at [288] in the context of Condition X:

> "For tax purposes all of the profits are allocated each year under s850 and this amount is therefore allocated for those purposes to BCG Ltd. Therefore the 18% which is considered to provide for the liabilities arising on the "sale" of the Capital Interests is included in BCG Ltd's profit share for tax purposes. The fact that BCG Ltd does not then warehouse the 18% does not affect the underlying point that an amount which is seen to represent the potential liability under the terms of the Capital Interests is allocated to BCG Ltd."

245. We agree with the FTT that condition (c) is satisfied, because the MDPs receive or are entitled to receive the value of their Capital Interests from BCG Ltd, and that sum is directly or indirectly provided out of its profit share. Neither of the points put forward by the BCG Parties changes that conclusion. In other words, whether BCG Ltd funded some or all of the "purchases" by borrowing money from a connected party, and/or that BCG Ltd could designate another person to "purchase" the Capital Interests and the UK LLP had a right to redeem the rights, do not prevent the condition from applying.

Attributable to "power to enjoy"

246. The FTT went on to hold at [314] it was "reasonable to suppose" that part of BCG Ltd's profit share was "attributable" to the MDP's "power to enjoy", and thus s850C(3)(c)(i) was satisfied. It made this finding "given the retention and allocation of the 18% amount to BCG Ltd to fund the future "purchase" of the [Capital Interests]."

247. The BCG Parties submitted that this conclusion conflicted with the FTT's finding of fact at [290(b)] that without the Capital Interests, "there would still be an allocation of the 18% margin towards the worldwide LTCV structure". There is, however, no conflict. The 18% retention was a global policy: as the FTT explain at [59], in some jurisdictions the LTCV is implemented by giving MDPs a specific class of shares. It was the way the LTCV was implemented in the UK which causes it to meet the "reasonable to suppose" test at s 850C(3)(c)(i).

248. The BCG Parties also submitted that the MDPs' profits from UK LLP "were calculated on exactly the same basis as they had previously been, when receiving salaries and bonus as employees of BCG Ltd", and it was thus not reasonable to assume that the MDPs had "power to enjoy" part of BCG Ltd's profit share.

249. We reject this submission. The position before the LLP was legally and factually different. At that time, the MDPs were employees, taxed according to the provisions which apply to employment income; BCG Ltd was their employer. Following the change to an LLP

and the introduction of the LLPAs, the MDPs received Capital Interests for the first time, and it is those which cause the statutory test to be met.

The counterfactual test

250. Finally, the FTT considered the counterfactual test, which provides that it is "reasonable to suppose" that "both A's profit share and the relevant tax amount are lower than they would have been in the absence of A's power to enjoy", see s 850C(3)(c)(ii).

251. The FTT held at [317] that:

> "For the same reasons as we have found in considering the application of s850C(2)(b) above [in relation to Condition X] we conclude that in the context of Condition Y the MDP's profit share and the relevant tax amount are not lower than they would have been in the absence of the MDP's power to enjoy."

252. The FTT thus decided the Condition Y counterfactual test in the BCG Parties' favour "for the same reasons" as it decided the Condition X counterfactual test. In other words, the FTT found that the MDPs' profit shares were not lower than they would have been in the absence of a power to enjoy, because (a) the global firm wanted all MDPs to participate in the LTCV, and (b) that participation would not have been achieved by allocating more profits to the UK MDPs because that would have created a disparity in terms of profit share between UK MDPs and others.

253. We again agree with HMRC that this is not the right approach to the counterfactual test. The statutory question is whether it is reasonable to suppose that the MDPs' profit shares would have been higher if they were not in the future going to receive a share of the profit which had been allocated to BCG Ltd, see subsection (3)(c)(ii) read with subsection 20(c) . The answer to that question has to be yes: that supposition is plainly reasonable.

254. The statutory question is not answered by assuming that an alternative arrangement would have been implemented as a result of which the MDPs obtain payments under the LTCV without having "power to enjoy" part of the profits allocated to BCG Ltd. That outcome would require a wholesale restructuring of the arrangements, for which there is no factual basis. And, as HMRC say, it would entirely undermine the purpose of the provision.

255. The other part of the counterfactual test concerns the "relevant tax amount", about which our findings are the same as in relation to Condition X, see §222.

Conclusion on Condition Y

256. We therefore find (agreeing with the FTT) that BCG Ltd's profit share exceeds the appropriate notional profit; that the MDPs have power to enjoy BCG Ltd's profit share and that it is reasonable to suppose that part of BCG Ltd's profit share is attributable to the MDPs' power to enjoy. We also find (disagreeing with the FTT) that it is also reasonable to suppose that the MDPs' profit shares are lower than they would otherwise have been, as was the relevant tax amount. It follows that Condition Y is met.

Adjustment to profit shares

257. As we have found that Condition X and Condition Y were satisfied, the next question is how to adjust the profit shares in consequence. Section 850C(4) provides that:

> "A's profit share is increased by so much of the amount of B's profit share as it is reasonable to suppose is attributable to -
>
> (a) A's deferred profit; or
>
> (b) A's power to enjoy,
>
> as determined on a just and reasonable basis."

258. HMRC's position was that it would be just and reasonable to ascribe to each MDP the increase in value (if any) of their potential Capital Interests each year. The BCG Parties submitted that the only "just and reasonable" basis for reallocation would be by reference to the amount of the proceeds received on disposal of the Capital Interests, so that allocation did not take place on a year by year basis, but only when an MDP was entitled to a payment.

259. We agree with HMRC for the following reasons:

(1) Income tax is an annual tax, and the purpose of s 850C is to reallocate profits arising in a tax year from the corporate partner to individual partners. It would not be just or reasonable to delay those adjustments until the MDPs obtained a payment, which could be in many years time.

(2) The UK LLP calculates the change in value of each MDP's Capital Interests each year for accounting purposes, and MDPs are also given individual annual statements of how much their Capital Interests had increased in value, see [143(2)]. There is thus no difficulty with calculation or quantification.

(3) Although there is a mismatch between receipt of cash and allocation of taxable profits, that is commonly the position in LLPs and partnerships where distributions frequently do not track the amounts allocated for tax purposes.

260. The BCG Parties submitted that the value of the BCG Inc Shares might fall as well as rise, so that an MDP could be taxed in year 1 on the reallocated profits, but that figure might be reversed the following year. Mr Grodzinski did not know whether this had in fact happened, and from the detailed spreadsheets in the Bundle to which we were referred by HMRC it appeared that there had been increases in all the relevant years. There were also no findings of fact about how the BCG Inc Shares were valued. We decided it would be unwise for us to decide how these anti-avoidance provisions might apply in a year when the BCG Inc Shares fell in value, if that were ever to happen. It is not, however, the position in relation to the relevant years, and on the facts we do have it appears to us to be a remote possibility. Certainly it does not change our view as to the just and reasonable methodology for apportioning the profits from BCG Ltd to the MDPs in the relevant years.

261. In addition to the adjustments to increase the profit shares of the MDPs, reductions will also be needed to the profit shares of BCG Ltd on a just and reasonable basis, see s 850C(5). The application of that provision was not in dispute.

MISCELLANEOUS INCOME

262. We have decided under Issue (1) that the Capital Interests did not give the MDPs interests in capital, and we have also found under Issue (2) that the MMRs apply for the years 2014-15 through to 2016-17. The next Issue is whether, for the years 2012-13 and 2013-14, the miscellaneous income provision at ITTOIA s 687(1) applied. That provision reads:

> "Income tax is charged…on income from any source that is not charged income tax under or as a result of any other provision of this Act or any other Act."

The legal principles and the FTT Decision

263. At the FTT it was common ground that the relevant principles were set out in *Kerrison v HMRC* [2019] UKUT 008 (TCC) ("***Kerrison***") at [68] and that for a receipt to be chargeable as miscellaneous income:

(1) it must have the nature of "annual profits" such that it must be capable of being calculated in any one year although this does not mean it must recur every year;

(2) it must be of an income nature;

(3) it must be analogous to some other head of charge under what was previously Schedule D;

(4) it must be the recipient's income; and

(5) it must involve a sufficient link between the source and the recipient.

264. Having applied the principles in *Kerrison*, the FTT found at [346] that the payments made for the "sale" of the Capital Interests were miscellaneous income within the scope of s 687.

265. In *BlueCrest*, where Henderson LJ gave the leading judgment with which Falk and Lewison LJJ both agreed, one of the issues considered was whether the "PIP awards" made to the partners were miscellaneous income. Henderson LJ followed a similar approach to that in *Kerrison,* but emphasised that when deciding whether a payment was of an income nature it was "necessary to stand back and examine the commercial reality of the PIP scheme as a whole", saying it was "entirely legitimate to rely on an overall assessment of this nature when answering the question whether the awards were of an income nature".

266. In deciding whether the MDPs received miscellaneous income, we have looked at the factors listed in *Kerrison,* while also standing back and examining the commercial reality of the arrangements as a whole.

Annual profits

267. In *Ryall v Hoare* [1928] 2 KB 447 at 454-455, Rowlatt LJ explained that the word "annual" denotes only "calculated in any one year", and "annual profits or gains" means "profits or gains in any one year or in any year as the succession of years comes round". Henderson LJ said in *BlueCrest* that this "does not take the enquiry very far", but nevertheless "the potential for annual recurrence, coupled with the need to calculate the profits in any one year, are at least pointers to the awards having the quality of income".

268. The BCG Parties submitted that the FTT had failed to take into account that the "the payments were typically one off, being paid on or in the lead up to a UK MDP's retirement rather than having a quality of recurrence". However, the FTT made the following findings of fact at [62]:

> "On retiring an MDP would be required to sell their entire LTCV holding to an entity within the BCG group. On reaching 20 years of service as an MDP, that individual would be required to start selling down their LTCV interest in 10 annual tranches equal to 10% of that MDP's pre sell-down LTCV holding. Prior to 2014 an MDP going through the sell down process was also able to sell up to an additional 10% as part of each annual tranche. Also prior to 2014 an MDP who reached five years of service as an MDP and was at least 45 years of age would be entitled to sell up to 10% of their pre sell-down LTCV holding each year until they had sold a total of 50% of their presell down LTCV holding."

269. The Capital Interests were thus not only received on retirement, but following 20 years of service, they were typically paid out over the following ten years. Moreover, it is clear from the case law that the payment does not have to recur every year, although it must be "capable of recurrence", see the House of Lords judgment in *Leeming v Jones* [1930] AC 415, relied on and followed in *BlueCrest*. That is plainly the position here. Mr Grodzinski conceded in oral submissions that if the BCG Parties failed in their other submissions relating to miscellaneous income, they were "unlikely to succeed" by relying on this point. We agree.

270. In addition, the MDPs were given annual statements of how much their Capital Interests had increased in value, see [143(2)]. The amounts were thus not only "capable of being calculated in any one year", as the UT put it in *Kerrison,* but were in fact so calculated.

Of an income nature

271. At [143]-[145] the FTT listed eleven factors which pointed towards the Capital Interests being rewards for services. That list was followed by an explanation as to the weight placed on a new partner presentation, which had described the LTCV as part of the MDP's compensation, and by a paragraph assessing part of Mr Holden's evidence. The FTT concluded at [146]:

> "We have therefore concluded that considering the evidence overall and, in particular, the factors identified above, the Capital Interests should be found to have been part of the overall package of remuneration provided to senior personnel for the services they provided to the organisation."

272. The FTT subsequently decided at [337] that the payments received by the MDPs on "sale" of the Capital Interests were income in nature. They came to that conclusion by reference to the "findings made earlier" and in particular the following:

> "(1) they are awarded in recognition of a person's seniority as well as length of service;
>
> (2) they are designed to align the interests of the individuals with that of the business and consequently incentivise them;
>
> (3) they are in substance analogous to a pre-determined retirement/departure payment; and
>
> (4) in the accounts the UK LLP is treated as having the benefit of the services provided by the MDP with the [Capital Interests] being treated as connected to the provision of those services."

273. In their skeleton argument, the BCG Partners submitted that:

> "the FTT erred in relying on these factors (and/or in only taking account of these factors, and not taking account of relevant factors)".

In other words, this was a challenge to the FTT's finding of fact that the Capital Interests rewarded the MDPs for the services they provided.

274. In *Lifestyle Equities CV v Amazon UK Services Ltd* [2024] UKSC 8, the Supreme Court endorsed the *dicta* of Lewison LJ in *Fage UK Ltd v Chobani UK Ltd* [2014] EWCA Civ 5 ("***Fage***") at [114], which included the following:

> "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."

275. The Supreme Court at [49] also approved the following passage from *In re Sprintroom Ltd* [2019] EWCA Civ 932, where the Court of Appeal, having considered *Fage* and other authorities, concluded that on an appeal the court:

> "must ask whether the decision of the judge was wrong by reason of an identifiable flaw in the judge's treatment of the question to be decided, such as a gap in logic, a lack of consistency, or a failure to take into account some material factor, which undermines the cogency of the conclusion."

276. The Supreme Court added at [50] that to be "wrong" in law "it is not enough to show, without more, that the appellate court might have arrived at a different evaluation".

277. In *Megtian v HMRC* [2010] STC 840 ("***Megtian***") at [11], Briggs J (as he then was) said:

> "The question is not whether the finding was right or wrong, whether it was against the weight of the evidence, or whether the appeal court would itself have come to a different view. An error of law may be disclosed by a finding based upon no evidence at all, a finding which, on the evidence, is not capable of being rationally or reasonably justified, a finding which is contradicted by all the evidence, or an inference which is not capable of being reasonably drawn from the findings of primary fact."

278. In *Marlborough DP Ltd v HMRC* [2024] UKUT 00098 (TCC) ("***Marlborough***"), the UT (Edwin Johnson J and Judge Brannan) summarised the legal position as follows:

> "76. …a tribunal may arrive at a finding of fact in a way which discloses an error of law in the following circumstances
>
> 77. First, we have power to set aside a decision of the FTT if the FTT took into account irrelevant considerations or failed to take into account relevant considerations. On this ground, it must further be shown that the considerations wrongly taken into or left out of account must be material in the sense that they might (not would) have affected the outcome: see Henderson LJ in *Degorce v HMRC* [2017] EWCA Civ 1427 at [95]. Where such a flaw in the fact-finding process is identified, there is no additional requirement to establish "perversity" (as described in paragraph 78 below): see *WM Morrison Supermarkets PLC v HMRC* [2023] UKUT 20 (TCC) at [58]…
>
> 78. Secondly, we have the power to set aside a decision of the FTT if the FTT's overall conclusion on any issue if it was one that "no person acting judicially and properly instructed as to the relevant law could have come to" (or, as a shorthand, that it was "perverse") because in those circumstances we would be bound to assume that there has been some misconception of the law and that this has been responsible for the determination (*Edwards v Bairstow* [1956] AC 14 per Lord Radcliffe at 36)."

279. We have taken all those authorities into account when deciding whether the FTT made an error of law in finding that the Capital Interests provided "part of the overall package of remuneration provided to senior personnel for the services they provided to the organisation".

280. The BCG Parties' skeleton sets out a list of reasons in support of their challenge, of which only four directly relate to the specific factors identified by the FTT at [143]-[145]. We list those four factors below, followed in italics by our reasons for dismissing these points

(1) The FTT was wrong to place weight on the use of the word "compensation" in various documents to describe the LTCV. *The use of the word "compensation" was not an irrelevant consideration, and matters of weight are for the FTT to decide*.

(2) In making its correct finding that "the awards were increased with promotion", the FTT should also have given weight to Mr Holden's unchallenged evidence in his witness statement that the "primary reason for longer tenured MDPs having more [Capital Interests] was to ensure that their interests were aligned with that of the global firm". *Factor (4) of the FTT's list explicitly recognises that the role of the LTCV throughout was to align MDPs' interests with that of the business and to incentivise them. The FTT plainly took that dual purpose into account when coming to its overall finding as to the nature of the awards*.

(3) The FTT was wrong to place reliance on a statement made by the UK LLP's CFO that she viewed the Capital Interests arrangement as taking "old comp" (ie the MDP's

previous compensation as employees) and making it new capital gain. The CFO's view "disclosed an error of perception" because "there was in fact no 'old comp' that was turned into a 'new capital gain'". *The FTT was fully entitled to place weight on the CFO's description of the arrangements.*

(4) The FTT was also incorrect in its approach to the withholding of the proceeds for a year following "sale", when BCG had a sum of money against which it could set any penalty payable for breach of a restrictive covenant. The FTT rejected Mr Holden's characterisation of the withholding as being "a way of enabling BCG to protect its goodwill", instead finding that it "acted economically in much the same way as provisions in other share incentives where a 'bad leaver' is required to forfeit some or all of their award". The BCG Parties say only that the FTT was "wrong" to come to that finding. *There was no error of law in the FTT's approach; it was plainly entitled to identify and rely on the analogy with "bad leaver" provisions.*

281. The BCG Parties also make the following other submissions:

(1) The FTT's finding as to the nature of the Capital Interests was inconsistent with its separate finding that they "stand outside the four compensation elements of the Framework". *There is however, no inconsistency: the FTT accepted that the LTCV was additional to those four elements, see [52] and [54]; but it does not follow that the Capital Interests were not themselves also part of the MDPs' reward package*.

(2) Since the FTT had found that the value of the Capital Interests "was not linked to the service or the performance of an individual UK MDP, and could indeed fall as well as rise as time progressed", the FTT should also have found that they were not a reward for services. *The FTT expressly considered those facts at [145] and found that they were not determinative. In other words, this point was considered as part of the FTT's evaluative judgment, and there was no error of law in its approach.*

282. The BCG Parties end this part of their skeleton by saying that the FTT's findings "were based on irrelevant considerations and/or on ignoring or discounting relevant considerations". We have no hesitation in rejecting that submission. The FTT carefully considered the evidence and made a finding of fact that the Capital Interests "gave the MDPs part of their reward for services". That is a finding which the FTT was entitled to make on the evidence.

283. In oral submissions, Mr Grodzinski referred to Henderson LJ's *dictum* in *BlueCrest*, that in deciding whether a payment was of an income nature it was "necessary to stand back and examine the commercial reality of the…scheme as a whole". Mr Grodzinski said that:

> "…standing back, if you look at the position overall , these [payments] are of a capital nature and that is a question of law for this Tribunal not dependent upon an *Edwards v Bairstow* challenge to the FTT's findings..."

284. We agree with Mr Grodzinski that whether the payments made on "sale" of the Capital Interests were capital or income is a question of law. In *BlueCrest,* Henderson LJ said at [103]:

> "Before us, neither side displayed any enthusiasm for investigating the further question whether the issue of the proper characterisation of the final PIP awards as being of a capital or an income nature was one of law or of fact, or a mixture of the two… Nevertheless, it seems to me that the question cannot be ignored, however difficult it may be to answer. My own view, which has not been tested in argument and which I therefore state with some diffidence, is that the question is in principle one of law, to which there can be only one correct answer in any given factual situation. It is not a question of evaluation, or of mixed fact and law, for the tribunal of fact, whose decision could then

> only be challenged as erroneous in law on the limited grounds explained in *Edwards v Bairstow* [1956] AC 14."

285. It is thus for this Tribunal to decide whether the FTT made an error of law in deciding that the payments made to MDPs on "sale" of their Capital Interests were of an income nature. As Henderson LJ said, we must "stand back and examine the commercial reality of the…scheme as a whole". The BCG Parties submitted that, having carried out that exercise, the Capital Interests were capital in nature and not income, for the reasons set out under Issue 1, and also for the following reasons:

(1) As the FTT had accepted, see [145] and [282], the Capital Interests were a form of equity style investment in the business, which provided MDPs "with a stake in the business" and with "a potential/benefit return if the business prospers".

(2) Although the Capital Interests could be regarded as a reward for services, there is a distinction between a reward enjoyed by an owner of the business, and a reward for services provided to the business.

(3) The reward obtained by the MDPs on "sale" was "properly regarded as attributable to the sale of an ownership stake" and so was capital and should be taxed as such.

286. We do not agree, for the reasons explained under Issue 1, and for the following further reasons:

(1) Standing back and examining the commercial reality, the Capital Interests did not give the MDPs a capital interest in the UK LLP and the payments made on disposal of those Rights were not of a capital nature.

(2) Although it is clear from *BlueCrest* that this is a question of law, Henderson LJ also said that there can only be one correct answer to that question "in any given factual situation". The FTT found as a fact that the Capital Interests "gave the MDPs part of their reward for services". While it is true that owners of a business have rewards, they are not "rewards for services".

Eiusdem generis

287. The FTT found at [339] that the payments made on disposal of Capital Interests were *eiusdem generis* or analogous to other amounts taxed as income. The BCG Parties challenged that finding, saying:

> "…given the D share program which the Capital Interests replaced, the payments were much more analogous to the disposal of shares subject to the ERS provisions and acquired for full-market value. Such payments are not regarded by Parliament as of an income nature, presumably because Parliament recognised that the character of the growth in value of shares acquired in this way is derived from an ownership stake, and not from employment/for services.

288. However, the Capital Interests were not analogous to shares acquired for full market value. They did not give the MDPs any interests in the capital of the UK LLP (such as a shareholder would have in a company) and they were acquired for nil value. They are, as the FTT said, more analogous to a phantom share scheme, which as Mr Holden himself accepted under cross-examination gives rise to employment income.

289. HMRC addressed the *eiusdem generis* point in their skeleton by saying:

> "One of the classic types of income charged by section 687 and its predecessors is remuneration under a contract for work done or services rendered where that remuneration has not been otherwise charged to tax (e.g.

> as employment income or as part of the profits of a trade, profession or vocation): *Scott v Ricketts* at 831E; *Manduca* at [35]. HMRC's case is that the individual members' receipts when they "sold" Capital Interests fall squarely within this classic type of income not otherwise charged to tax.
>
> Further, it is very well established that where the agreed terms for rewarding an office or employment include that a payment will be made on retirement or resignation, that payment is income from the office or employment (and not a form of compensation for its loss), however it is described: see *Henry v Foster* (1930) 16 TC 605 as discussed in *EMI Group Electronics v Coldicott* [1999] STC 803 at 811-812. This precedes the introduction of deeming rules imposing tax on termination payments. Here, similarly, when someone becomes an MDP, the terms they agree to include provision for payments on retirement. Those are income payments arising from service as a member (and/or the rights under the LLP Agreement) and analogous to the payments described in those cases."

290. We agree with those submissions, and find that payments on the disposal of the Capital Interests are analogous to the receipt of income, and not to the disposal of capital assets.

Recipient's income

291. In *Kerrison,* the next identified factor is that the receipt must be the recipient's income. We have already considered this under Issue 1, and decided that the Capital Interests were not capital; it was common ground that if that were the position, the money received by the MDPs on disposal was income.

Source

292. The FTT held at [344] that:

> "The source of the payments is the terms on which the Capital Interests are allocated under the LLPAs. That is where the obligation to purchase the Capital Interests and make the payment is found. And there is a sufficient link between that source and the MDPs."

293. The BCG Parties submit that the source of the payments was the initial provision of the Capital Interests to the MDPs, and not the "sale" of those Rights to BCG Ltd. In their skeleton argument, they characterise the initial provision as analogous to a share option, saying that the value when provided was "only the hope value (if any)" of the Rights at that date.

294. Mr Chacko responded by saying that a share option was a separate asset which can be disposed of by the owner. It was thus clearly distinguishable from the arrangements in place here, where the Capital Interests do not have an independent existence, but arise under the terms of the LLPAs.

295. Both parties referred us to various judgments, including *BlueCrest* and *HFFX v HMRC* [2024] EWCA Civ 813 ("***HFFX***"), both of which referred to *Trustees of the Will of Florence Cunard v IRC* [1946] 1 All ER 159 ("***Cunard***") and to *Spritebeam v HMRC* [2015] UKUT 75 (TCC) ("***Spritebeam***").

296. The case of *Cunard* concerned payments made by trustees out of capital; the trustees had been directed to hold the residuary estate on trust to pay the income to the testatrix's sister (Miss McPheeters) and, if that was insufficient, to supplement the income from capital. Miss McPheeters was assessed to income tax on the receipts, and she and the trustees both appealed. Lord Greene, giving the only judgment with which MacKinnon and Morton LJJ both agreed, upheld the assessment, saying that "[t]he money, when received by Miss McPheeters, was received by her through the joint operation of the will and the exercise of their discretion by the trustees" and that "Miss McPheeters' title to the income arose when the trustees exercised

their discretion in her favour and not before. At that moment a new source of income came into existence". Although *Cunard* concerned Case III of Schedule D, Henderson LJ held at [123] of in *BlueCrest* that what Lord Greene had said was "equally capable of application" to the miscellaneous income provisions (previously "Case VI" of Schedule D). In *Spritebeam* the UT said at [68], having considered *Cunard,* that "[i]t is immaterial that the recipient cannot enforce payment; what matters is whether there is an obligation on the payer to pay".

297. As explained under Issue 1, the Capital Interests did not have an independent existence or value. The provisions at clause 6 of the 2011 LLPA prohibited transfer to anyone other than BCG Ltd or a designate, see §58 to §63 above. By Schedule 3, BCG Ltd or a designate was obliged to "purchase" the Capital Interests from the MDPs, but that obligation only arose when various conditions in the LLPA had been satisfied, such as reaching 20 years' service; retiring; leaving the firm or one of the other situations summarised at [62] of the FTT Decision.

298. By analogy with the situation in *Cunard,* it was the "joint operation" of (a) the MDP meeting a relevant condition, and (b) BCG Ltd meeting its consequential obligation to "purchase" the Capital Interests, that gave rise to the payments. Both those elements had the same source, ie the LLPAs[3]. We thus find that the FTT was correct to hold that the LLPAs were the source of the payments.

Conclusion on miscellaneous income

299. For the reasons set out above, we agree with the FTT that the payments received by the MDPs in 2012-13 and 2013-14 were taxable as miscellaneous income. The position is different for the following three years because s 687 only applies to "income from any source that is not charged income tax under or as a result of any other provision of this Act or any other Act", see subsection (3). We have already found that for 2014-15 through to 2016-17, the MDPs were taxable under the MMRs. Although assessments had been issued to MDPs for those later years on the basis of the miscellaneous income rules, HMRC agreed at the hearing that those assessments would be withdrawn if the MMRs applied.

300. However, for completeness, were our findings on the MMRs to be incorrect, the miscellaneous income provisions would have applied. That is because all the elements considered above were the same, including the source of the income. In 2014-15, 2015-16 and 2016-17, the relevant terms of the later LLPAs were identical to those considered above: clause 6 appears in all three LLPAs with essentially the same wording, and BCG Ltd or a designate has the obligation to "purchase" the Capital interests under Schedule 3 of all three LLPAs.

SALE OF OCCUPATIONAL INCOME

301. The charge on the sale of occupational income would only fall to be considered had we decided at Issue 1 that the Capital Interests were capital in nature. However, the occupational income issue was fully argued before us and both parties asked us to make findings.

The legislative provisions

302. The legislation is contained in Chapter 3 of Part 13 ITA. The BCG Parties submitted that the MDPs were not chargeable under these provisions because of the exemption at s 784. So far as relevant, that section reads:

> "(1) This section applies if a capital amount is obtained from the disposal-
>
> (a) of assets (including any goodwill) of a profession or vocation,

[3] In that respect the position is different to that in *Cunard,* where the joint operation of the will and the exercise of the trustees' discretion caused a new source of income to come into existence: here there was one source which was already in existence, but that makes no difference – the *ratio* of the case still applies.

(b) of a share in a partnership which is carrying on a profession or vocation, or

(c) …

(2) An individual is not liable to income tax under this Chapter in respect of the capital amount so far as the going concern condition is met (see subsections (4)…)

(3) …

(4) In the case of a disposal within subsection 1(a) or (b), the going concern condition is that the value of what is disposed of at the time of the disposal is attributable to the value of the profession or vocation as a going concern."

303. The FTT found that this exemption did not apply for two reasons, one of which was that the value of the Capital Interests was not attributable to the value of the UK LLP as a going concern. The BCG Parties submitted that this was an error of law for the following reasons:

(1) the Capital Interests were interests in the goodwill of the UK LLP;

(2) the value of the Capital Interests was not linked to individual UK MDPs' performance; and

(3) the Capital Interests would have been worthless if the UK LLP was no longer a going concern.

304. Those submissions are rejected for the following reasons

(1) We have already found (see §110 to §113) that the Capital Interests were not interests in the goodwill of the UK LLP.

(2) Although it is true that their value was not linked to the individual performance, it does not follow that it was attributable to the value of the UK LLP as a going concern. Instead, the value of the Capital Interests was linked to the increase in value of the BCG Inc Shares, not to the value of the UK LLP as a going concern.

(3) There was no finding by the FTT as to what would have happened if UK LLP was not a going concern, but at [116] the FTT did find as a fact that because the value of the Capital Interests was linked to the value of the BCG Inc Shares, it was possible for the value of the UK LLP to fall and the value of the BCG Inc shares to rise, such that an MDP would be able to realise value relating to the worldwide group even when the UK business was struggling. In other words, the Capital Interests were not attributable to the value of the UK LLP as a going concern, but to the value of the BCG Inc Shares. In any case we note that the payment due under Schedule 3 was not dependent of whether the UK LLP was a going concern. There were provisions in Schedule 3 allowing for the deferral of a "sale" or "redemption" of a Capital Interest where the UK LLP **or BCG Ltd** was insolvent or would thereby be rendered insolvent, and to defer payment if a sale was made if the board of BCG Ltd determines that such payment must be deferred in order to avoid jeopardising the financial position of BCG Ltd or such other person as is the Purchaser, but that is not the same thing as linking payment to the UK LLP being a "going concern". These provisions are more readily explicable as protections of the financial position of the Purchaser than as establishing a link between the value of the LLP and the price paid for the Capital Interests.

305. We uphold the FTT's finding that the value of the Capital Interests was not attributable to the value of the UK LLP as a going concern, and move on to consider the other provisions.

306. Section 773 ITA provides:

> “(1) This Chapter imposes a charge to income tax—
>
> > (a) on individuals to whom income is treated as arising under section 778,…
>
> (2) Income is treated as arising under those sections only if—
>
> > (a) transactions are effected or arrangements made to exploit the earning capacity of an individual in an occupation, and
> >
> > (b) the main object or one of the main objects of the transactions or arrangements is the avoidance or reduction of liability to income tax.”

307. Thus, for the provisions to apply, both subsections 2(a) and (b) must be satisfied. The BCG Parties conceded during the hearing that the main object or one of the main objects of the LLPAs (and in particular, the introduction of the Capital Interests) was the avoidance or reduction of liability to income tax, and thus subsection 2(b) was satisfied. The point we therefore had to decide was whether subsection (2)(a) was met, so that “income is treated as arising” to the MDPs under s 778.

308. ITA s 777 reads, so far as relevant:

> “(1) Sections 778 and 779 apply only if conditions A to C are met in respect of an individual.
>
> (2) Condition A is that the individual carries on an occupation wholly or partly in the United Kingdom.
>
> (3) Condition B is that transactions are effected or arrangements made to exploit the individual's earning capacity in the occupation by putting another person (see section 782) in a position to enjoy:
>
> > (a) all or part of the income or receipts derived from the individual's activities in the occupation, or
> >
> > (b) anything derived directly or indirectly from such income or receipts,
>
> (4) …
>
> (5) Condition C is that as part of, or in connection with, or in consequence of, the transactions or arrangements a capital amount is obtained by the individual.”

309. It was common ground that Condition A was met. The BCG Parties submitted that neither Condition B nor Condition C was met.

Condition B

310. In the context of this case, the statutory question can be reframed as whether:

> “transactions are effected or arrangements made to exploit the MDP’s earning capacity in the occupation by putting BCG Ltd in a position to enjoy all or part of the income or receipts derived from the MDP’s activities in the occupation, or anything derived directly or indirectly from such income or receipts.”

311. The BCG Parties submitted that we should approach this Condition on the basis that:

(1) the question of occupation income would not be in issue unless both the MMRs and the miscellaneous income rules had been found not to apply; and

(2) we should thus accept for the purposes of these provisions that the amounts received by the MDPs were not a reward for services.

312. We do not find that to be a helpful starting point. It is true that when considering the miscellaneous income rules, we have taken into account the FTT’s finding of fact that the

Capital Interests "gave the MDPs part of their reward for services" but that is not the only reason for our conclusion. We also rely on our findings under Issue 1 and on the commercial reality - see §286. In our judgment, when considering the occupational income provisions it is not correct to ignore the FTT's finding of fact that the Capital Interests "gave the MDPs part of their reward for services".

313. The BCG Parties also challenge the FTT's finding at [365] that Condition B was met because the UK LLP and the terms of the LLPAs were "arrangements" made to put BCG Ltd in a position to enjoy part of the income or receipts derived from the MDPs' activities in their occupation. In their submission, the setting up of the LLP and introduction of the LLPAs did not put BCG Ltd "in a position to enjoy all or part of the income or receipts" from the work carried out by the MDPs, because before the LLP was set up, BCG Ltd employed the MDPs, and so was entitled to the benefits of the work they carried out.

314. We agree with HMRC that this too is not the correct approach. The statute requires us to decide whether, in the year in question, arrangements had been put in place under which part of the fees earned by the UK LLP for the work carried out by the MDPs had been allocated to BCG Ltd. It does not import a comparative with previous years when different arrangements were in existence. The answer to that question is plainly yes, and Condition B is satisfied.

Condition C

315. As set out above, Condition C was that "as part of, or in connection with, or in consequence of, the transactions or arrangements a capital amount is obtained by the individual".

316. BCG's overall position in this appeal was that the MDPs had obtained capital amounts when they "sold" their Capital Interests. It was therefore surprising that the BCG Parties submitted that Condition C was not satisfied**.** The basis for that submission was that the Capital Interests were not "in connection with, or in consequence of" the LLPAs, but were instead "in connection with, or in consequence of the global policy operated by BCG through its Framework, and in particular the LTCV". We disagree: the Capital Interests were set out in the LLPAs which implemented the LTCV in the UK. Condition C is thus also satisfied.

Conclusion on sale of occupation income

317. For the reasons set out above, we find that if we were to be wrong on our findings relating to the MMRs and/or the miscellaneous income provisions, the sale of occupation income provisions would have applied. By s 778, the MDPs would be charged to income tax on "the capital amount receivable" by each of them.

PROCEDURAL ISSUES

318. Pausing there, we have so far decided that the Capital Interests are not capital; that the MMRs apply for years 2014-15 through to 2016-17, and that for the earlier years, the MDPs who "sold" their Capital Interests were taxable under the miscellaneous income rules.

319. However, those findings are subject to various procedural challenges, essentially whether amendments made to the UK LLP's Partnership Returns and various of the assessments issued to the MDPs were out of time because the relevant statutory tests were not met.

320. We have decided that the most straightforward way to approach these challenges is to take one year at a time. For ease of reference, we discuss whether the UK LLP was careless at §328 to §351 and at §432 to §447 ; whether carelessness caused the loss of tax at §392 to §424 and at §448 to §453; what is meant in TMA s 29(4) by "a person acting on his behalf" at §352 to §391, and we consider the "hypothetical officer" test at §459 to §478.

TAX YEAR 2012-13

321. The only relevant assessment for this year was that issued to Mr Krinks, because HMRC issued it after the statutory time limit.

The legislation

322. TMA s 29 is headed "Assessment where loss of tax discovered" and at the relevant time it read as follows:

> "(1) If an officer of the Board or the Board discover, as regards any person (the taxpayer) and a year of assessment —
>
> > (a) that any income…which ought to have been assessed to income tax, or chargeable gains which ought to have been assessed to capital gains tax have not been assessed…
>
> the officer or, as the case may be, the Board may, subject to subsections (2) and (3) below, make an assessment in the amount, or the further amount, which ought in his or their opinion to be charged in order to make good to the Crown the loss of tax.
>
> (2) …
>
> (3) Where the taxpayer has made and delivered a return under section 8…of this Act in respect of the relevant year of assessment, he shall not be assessed under subsection (1) above…
>
> > (a) in respect of the year of assessment mentioned in that subsection; and
> >
> > (b) in the same capacity as that in which he made and delivered the return,
> >
> > unless one of the two conditions mentioned below is fulfilled.
>
> (4) The first condition is that the situation mentioned in subsection (1) above was brought about carelessly or deliberately by the taxpayer or a person acting on his behalf.
>
> (5) The second condition is that at the time when an officer of the Board—
>
> > (a) ceased to be entitled to give notice of his intention to enquire into the taxpayer's return under section 8…of this Act in respect of the relevant year of assessment…
>
> the officer could not have been reasonably expected, on the basis of the information made available to him before that time, to be aware of the situation mentioned in subsection (1) above.
>
> (6) For the purposes of subsection (5) above, information is made available to an officer of the Board if—
>
> > (a) it is contained in the taxpayer's return under section 8…of this Act in respect of the relevant year of assessment (the return), or in any accounts, statements or documents accompanying the return;
> >
> > (b) it is contained in any claim made as regards the relevant year of assessment by the taxpayer acting in the same capacity as that in which he made the return, or in any accounts, statements or documents accompanying any such claim;
> >
> > (c) it is contained in any documents, accounts or particulars which, for the purposes of any enquires into the return or any such claim by an officer of the Board, are produced or furnished by the taxpayer to the officer ; or
> >
> > (d) it is information the existence of which, and the relevance of which as regards the situation mentioned in subsection (1) above—

> (i) could reasonably be expected to be inferred by an officer of the Board from information falling within paragraphs (a) to (c) above; or
>
> (ii) are notified in writing by the taxpayer to an officer of the Board."

323. TMA s 34(1) provides that the "ordinary time limit" for making an assessment is four years after the end of the year of assessment to which it relates.

324. TMA s 36 is headed "Loss of tax brought about carelessly or deliberately" and subsection (1) provides:

> "An assessment on a person in a case involving a loss of income tax or capital gains tax brought about carelessly by the person may be made at any time not more than 6 years after the end of the year of assessment to which it relates (subject to subsection (1A) and any other provision of the Taxes Acts allowing a longer period."

325. TMA s 36(1B) reads:

> "In subsections (1) and (1A), references to a loss brought about by the person who is the subject of the assessment include a loss brought about by another person acting on behalf of that person."

The issues

326. The discovery assessment issued to Mr Krinks was dated 8 March 2019, more than four years after he filed his SA return on 24 January 2014. That assessment would be invalid unless the loss of tax had been brought about by his carelessness, or by the carelessness of another person acting on his behalf.

327. Although earlier in the appeal process HMRC had sought to argue that Mr Krinks had been careless, this part of their case was abandoned before the FTT hearing. HMRC had instead submitted that the loss was brought about by the UK LLP acting on behalf of Mr Krinks. It was common ground that the burden of proving carelessness rested on HMRC.

The FTT's finding of carelessness

328. At [411] the FTT said "we consider that the following facts lead to a conclusion of carelessness by the UK LLP/the representative partner of the UK LLP". This is followed by four reasons, and then a further passage at [412]. Those two paragraphs relate to both (a) the introduction of the Capital Interests, and (b) the UK LLP's approach to the MMRs.

329. Ms Lemos criticised the FTT for having issued "blended" findings, saying that it was required to address carelessness on a year by year basis. It is, however, clear that the FTT found that the UK LLP had been careless in relation to *both* the introduction of the Capital Interests in 2011 *and* their reintroduction in 2014. The findings which relate to each of these are clearly identifiable.

Was the UK LLP careless in relation to tax year 2012-13

330. The FTT found that the UK LLP had been careless in relation to 2012-13 by reference to the facts found at [165(1)] and [167] to [173]. Those findings included the following (for ease of reference we have italicised the particular facts challenged by the BCG Parties).

(1) PwC had prepared a Feasibility Report in 2010 comprising an overview of the key legal, tax and accounting considerations associated with the LLP Conversion. However, the report was predicated on the value of the Capital Interests reflecting the value of the UK LLP. In addition, it was envisaged that the MDPs were to contribute funds to obtain a capital interest in the LLP. The structure which was in fact implemented was significantly different from that in the Feasibility Report.

(2) On 22 March 2011, PwC issued a formal letter of advice to BCG Inc ("**the PwC Letter**"), summarising the US federal income tax and UK income and employment tax consequences of the LLP Conversion, for both BCG and the UK MDPs. By this stage the structure did not involve the MDPs paying for capital interests, but did involve BCG Ltd and the MDPs lending amounts interest free to the UK LLP to provide working capital to it in a way which meant that the loans could not be said to relate to the profit interest of the Capital Interests. *That step did not take place*. Instead, profits were retained by BCG Ltd to fund working capital. In addition, PwC advised that the value of all outstanding Capital Interests should not exceed the value of the UK LLP and there would be a process in place to monitor this

(3) The UK LLP's chief financial officer at the time identified that the structure had the sense of being *too good to be true*, and wanted to follow up the PwC letter with a phone call to understand the level of risk. She said in an email (where "comp" means "compensation"):

> "Anytime we can take old comp and make it new capital gain…my radar goes on high alert. And then my follow up question is that if it really works, why didn't we do it with all of their comp?"

(4) The PwC Letter *was stated not to be an opinion about the tax consequences of the* transactions. The FTT panel said that in their experience it would be standard practice for an opinion to be obtained in such situations setting out identified risks. That opinion may use "should" wording rather than the more definite "would" but would give the client the clear identification of the extent of risk of challenge to the tax treatment of such a structure. The need for such an opinion is particularly strong where the chief financial officer has identified a concern with the structure and advice.

(5) Mr Holden's general assertions that there would have been some conversations about the structure and differences between what had been assumed by PwC and what was to be implemented, *were not sufficient* to show that an opinion addressing the differences in structure between the PWC Letter and that implemented was in fact obtained.

331. The FTT went on to hold at [411] that the UK LLP had been careless, and listed the following reasons:

> "(1) the structure PwC advised upon in March 2011 *was notably different to that implemented*. It involved BCG Ltd and the MDPs lending amounts interest free to the UK LLP to provide working capital to it in a way which meant that the loans could not be said to relate to the profit interest of the Capital Interest held by the MDPs. That step did not take place. Instead, BCG Ltd profits were retained by the UK LLP/BCG Ltd to fund working capital. In addition, it was assumed that the value of all outstanding Capital Interests would not exceed the value of the UK LLP and *there would be a process in place to monitor this. That process was not put in place*.
>
> (2) The chief financial officer at the time identified that the structure had the sense of being 'too good to be true'. In that context our expectation is that those involved within BCG's UK tax department would have wanted to make sure there was clear advice on file to support implementing what was seen as a surprising result. We would expect to see an opinion on file from a professional firm assessing the risk of challenge to the structure, or at the very least an internal paper produced by the BCG tax department assessing the same."

332. In the following paragraph, the FTT said this about the advice taken before the 2011 LLPA was introduced:

> "We do not consider that the evidence of obtaining advice by the business is sufficient to counter the evidence that the UK LLP was careless. The advice from PwC was predicated upon different structural elements to those involved with the actual operation of the Capital Interests. The advice obtained from …PwC…*was lacking in depth and quality* given the concerns raised by senior management in BCG and by the adviser, PwC, themselves. We conclude that the level of care taken in this respect was not in line with what would be expected of a prudent and reasonable taxpayer in the position of the UK LLP."

333. We next consider each of the BCG Parties' challenges to the above findings of fact.

Interest free loans and/or no monitoring process

334. Ms Lemos submitted that the FTT's finding that interest free loans were not made and that there was no monitoring process were both findings which were "not available to the Tribunal on the evidence" and that it therefore also followed that there was "no evidence" on which the FTT could have held that the structure advised upon in the PwC Letter was notably different to that implemented.

335. We agree with Ms Lemos that there is no evidence to support those findings of fact because:

(1) Interest-free loans were made to the UK LLP from the MDPs; this is clear from Clause 3.3 of all the LLPAs and the related "Deeds of Adherence" for each of the lead appellants (which were included in the Bundle).

(2) There was evidence to show that there was a monitoring process in place; the FTT noted this earlier in their judgment, saying at [131]:

> "Although the evidence from Mr Holden was that the values were regularly reviewed by the business to ensure that the value of the Capital Interests did not exceed the value of the UK LLP, there is no evidence as to what would happen in such a situation".

(3) Although Mr Magee (on behalf of HMRC) submitted that the FTT did not expressly intend to accept Mr Holden's evidence, we disagree: the FTT made it clear when it was rejecting evidence. We thus agree with Ms Lemos that the FTT made a finding of fact that there was a monitoring process in place.

(4) The FTT's finding that "the advice from PwC was predicated upon different structural elements to those involved with the actual operation of the Capital Interests" was based on the interest free loan point and the lack of a monitoring process. It follows that we also agree with Ms Lemos that there was no basis for that finding.

Not an opinion about tax consequences

336. Ms Lemos also challenged the FTT's finding that the PwC Letter "was stated not to be an opinion about the tax consequences of the transactions". We agree: the PwC Letter began by saying that Part IV set out "an overview of the UK income and employment tax considerations"; although there was a disclaimer, this related to US tax.

Too good to be true

337. Ms Lemos criticised the FTT's reliance on the email from the CFO which described the arrangements as "too good to be true". She invited us to find that the FTT should also have taken into account Mr Holden's evidence that the comment was seen internally as "provocative" and that the CFO was subsequently reassured. That is a submission that the FTT

should have weighted the evidence differently, which is not a permissible basis for a successful *Edwards v Bairstow* challenge.

Lacking in depth and quality

338. Ms Lemos also asked us to decide that the FTT was wrong to find that "the advice obtained from…PwC…was lacking in depth and quality", both because (a) the FTT had misconstrued the PwC Letter, and (b) the FTT did "not properly take into account Mr Holden's evidence and the contemporaneous emails showing the several months of detailed discussions", and was "wrong to minimise" their importance.

339. In support of these submissions, Ms Lemos took us to the PwC Letter, while Mr Magee referred us to Mr Holden's related evidence under cross-examination.

340. The PwC Letter was sent by PwC LLP in Boston Massachusetts to Mr Broussard, BCG's Global Tax Director, also based in Boston. At Part IV of the PwC Letter is a summary of the VAT, SDLT, NIC, income tax, corporation tax and SDLT consequences of becoming an LLP. There is a brief reference to the Capital Interests under the heading "Income Tax":

> "There should be no income tax when Capital Interests in BCG UK LLP are given to UK Partners as they are not acquiring the interest in their capacity as employees (it is acquired in their capacity as members of BCG LLP."

341. There is further reference under the heading "Capital Gains Tax":

> "Any gain realized on a Capital Interest will be subject to 28 per cent capital gains tax rates and under current rules would be eligible for Entrepreneur's Relief. The effect of Entrepreneur's Relief is that the first GBP 5m of any gains should be subject to 10 per cent capital gains tax rates provided that the UK Partner has been a member of BCG UK LLP for at least one year. The GBP 5m relief is a lifetime limit and not an annual amount.
>
> The UK partners will not purchase their initial capital interest, and therefore there should be no income tax when the capital interests is awarded and no income tax when the capital interest is disposed of by a UK Partner. Under English law, the value of the capital interest may track to any index. When the UK Partner disposes of their capital interest, the sales proceeds should be subject to capital gains tax. The sale proceeds for the initial capital interest will equal the difference between the value of the Class D2 shares on the date of sale and the value of the Class D2 chares as marked on the date of grant.
>
> For the avoidance of doubt, any non-UK domiciled UK partners are subject to UK capital gains on the disposal of the capital interests as the capital interest is a UK situs asset."

342. At the FTT, Mr Rupert Baldry KC on behalf of HMRC cross-examined Mr Holden about the PwC Letter: there were the following exchanges:

> *Mr Baldry:* So did this not strike you as a sort of rather superficial analysis that doesn't really contain the sort of advice that you would expect if you were actually seeking to rely on this as an explanation of the UK tax treatment of a Capital Interest? It's just an outline written by a UK/US LLP to a US tax person.
>
> *Mr Holden:* Judge, no, it didn't. The reason for that was this paper, based on my memory, was the culmination of months of work, which I think we established started in August of the preceding year by members of PwC based in the UK and the US. And this final piece of advice that we received from PwC was written obviously with both parts of the team contributing, but, as counsel has pointed out, was sent to us from the US.

> *Mr Baldry:* But this is supposed to be the -- if this is the summary, the grand conclusion of all that work, it doesn't say anything. It doesn't give any analysis of what the tax -- potential tax treatment and risks associated with this proposal would be. It doesn't refer to a single section of the UK Taxes Acts under which the Capital Interest could be treated –
>
> Mr Holden: I agree.
>
> Mr Baldry: Does it?
>
> *Mr Holden:* Yep, I agree."

343. Mr Holden returned to the same issue soon afterwards:

> "*Mr Holden*: So, judge, what I am trying to explain is that we worked with PwC between August and March of the following year and through that process, we received advice, probably all, if not most of it, orally. And the March memo was intended to capture the advice we had been given during that process.
>
> *Mr Baldry*: So is the March advice the grand summary of all the advice that you had?
>
> *Mr Holden*: Judge, that's right, yes.
>
> *Mr Baldry*: Nothing more?
>
> *Mr Holden:* That's correct."

344. A little later came the following exchange:

> "*Mr Baldry*: Ordinarily, if you were obtaining tax advice on a major transaction with major financial consequences, wouldn't you expect to get advice which actually refers to the relevant statutory provisions and actually sets out what the risks are? Wouldn't you expect to do that in a normal commercial situation of high value with high tax at stake?
>
> *Mr Holden:* So I understand why you are saying that. My recollection was at the time we received this memo, I was very happy, on the basis of the context leading up to it, that this was a very good piece of advice on which to rely upon.
>
> *Mr Baldry*: But this advice doesn't - if this advice is the only advice that you will see because it summarises all the other advice, doesn't it put you on alert that it's totally superficial?
>
> *Mr Holden:* So that's not the feeling I had."

345. It is plain from the foregoing that the FTT had evidence to support their finding that the advice in the PwC Letter was "lacking in depth and quality". There were, as Mr Baldry pointed out during cross-examination, no references in the PwC Letter to any statutory provisions, and there was no analysis to support the statement that "when the UK Partner disposes of their capital interest the sales proceeds should be subject to capital gains tax". As the FTT said, the PwC Letter did not give the UK LLP "the clear identification of the extent of risk of challenge to the tax treatment" of the arrangements being put in place.

346. We also do not accept Ms Lemos's submission that the FTT should not have "minimised" Mr Holden's evidence about oral discussions and related emails: that too is a submission that the FTT should have weighted the evidence differently.

The remaining findings

347. Summarising the above, the following findings of fact survived Ms Lemos's comprehensive challenges:

(1) The advice in the PwC Letter was "lacking in depth and quality", given the complexity of the arrangements which were about to be put in place.

(2) There was no other written advice, so there was "no opinion on file from a professional firm assessing the risk of challenge to the structure".

(3) There was also "no internal paper produced by the BCG tax department assessing the same".

(4) The chief financial officer had "identified that the structure had the sense of being 'too good to be true'" and had thus "identified a concern with the structure and advice".

Is there an error of law

348. Although we have identified findings of fact made by the FTT for which there was no evidence, that is only an error of law if the FTT's mistakes were material in the sense that they might have affected the outcome (see *Marlborough* cited at §278 above). The "outcome" here is the FTT's conclusion that the UK LLP was careless in not obtaining detailed technical tax advice in writing on the structure (and not even having on file an internal paper assessing the risks).

349. Carelessness is the failure to act without the care which a reasonable person in the same situation would have exercised, see for example *Atherton v HMRC* [2019] UKUT 0041 ("***Atherton***") at [175]. HMRC summarised the UK LLP's situation at the time it was considering implementing the Capital Interests, see [408]:

> "…the arrangements involve very large sums of money, the UK LLP was aware that the structure was a means of saving very substantial income tax, the structure was perceived internally as a means of converting income to capital with serious tax risk and the arrangements involve the insertion of complicated[4]… provisions into the LLPA. The analysis in the PwC reports[5] is high level without detailed consideration of whether, in light of the terms of the Capital Interests, they are actually capital assets. Neither report considers whether the Capital Interests should be viewed as a vehicle for income benefits."

350. Although put forward by HMRC, we find that the above passage is a fair summary of the UK LLP's situation. In our judgment, the FTT's mistakes were not material to its conclusion on carelessness, because it is plain that a reasonable business in the same situation as the UK LLP would not have implemented the arrangements in reliance only on the very superficial paragraphs of the PwC Letter, which Mr Holden had confirmed was the "grand summary of all the advice" which had been obtained. The mistakes made by the FTT would therefore not have affected the outcome.

351. We thus uphold the FTT's finding that the UK LLP was careless when it decided that payments made on "sale" of the Capital Interests were capital in nature, because the LLP had failed to take adequate professional advice.

Person acting on behalf

352. On the basis of our findings earlier in this judgment, the payments made on "sale" of the Capital Interests were income in nature. The MDPs did not include those payments as income in their SA returns, but instead as capital. There was thus a loss of tax. However, the extended time limit in TMA s 36(1B) only applies if that loss was "brought about by the taxpayer or

[4] HMRC's summary included the words "and contrived" here, which we have ignored.

[5] As this passage refers to the implementation of the arrangements in 2011, we have understood this as a reference to the Feasibility Report and the PwC Letter.

another person acting on his behalf of. HMRC's case is that the loss of tax was brought about by the UK LLP acting on Mr Krink's behalf.

Whether HMRC pleadings were inadequate

353. The BCG Parties submitted that HMRC had advanced this "on behalf of" argument for the first time in their skeleton argument for the FTT hearing, which was served ten days before the proceedings commenced. The passage read:

> "for the individuals, the LLP instructed PwC on their behalf to advise them how to fill out their forms. Therefore carelessness by the LLP can be attributed to those individuals…"

354. The BCG Parties say that this point was not included in HMRC's Statement of Case, and that the FTT made an error of law when it allowed HMRC to advance this submission at the hearing.

355. HMRC did not agree. They relied first on the Statements of Case for the MDPs, of which there appear to have been two. The Statement of Case for Mr Holden, Mr Nascimento and Mr Krinks included the following passages (HMRC's emphasis):

> "HMRC's assessments of Mr Nascimento and Mr Krinks were made between four and six years after the end of the relevant tax year and therefore HMRC must show carelessness on the part of the taxpayer *or someone acting on his behalf*…The issue will be whether they did in fact rely upon advice and whether it was reasonable in all the circumstances for them to do so, and whether, if their returns *were filed by an agent, that agent (or anyone else acting on their behalf) was also taking reasonable care*.
>
> For all three Appellants, if HMRC succeeds in persuading the Tribunal that they *or someone acting on their behalf* did not take reasonable care, s 29(4) TMA allows HMRC to raise a discovery assessment.

356. The Statement of Case for Mr Holden, Mr Niddam and Mr Garside contained essentially the same passages.

357. HMRC also emphasised that, in the course of the FTT hearing, the BCG Parties had not submitted that HMRC had not properly pleaded this point: Mr Grodzinski had simply said:

> "If you look at the Revenue's skeleton, they are no longer putting in issue whether the MDPs received advice, they are no longer putting in issue whether they relied upon that advice, and they are no longer putting in issue whether it was reasonable for them to do so…[reads the passage from the skeleton]. That's their case, and we don't accept that is a good argument as a matter of principle."

358. Mr Grodzinski then advanced three reasons why the BCG Parties did not accept that HMRC's submission was "a good argument". He later said "[i]n another retreat from their pleaded case, the Revenue now only allege carelessness against the individual members on the sole basis that BCG is said to have acted on their behalf".

359. In *Mainpay v HMRC* [2024] UKUT 00233 (TCC) ("***Mainpay UT***"), Mr Firth (on behalf of the appellant) made a similar submission, which he had also raised at the FTT, but without success. The UT held at [129] that:

> "…the evaluation of whether or not HMRC should be permitted to rely on their pleadings in relation to carelessness involved an exercise of judicial discretion by the FTT. This Tribunal should be slow to interfere with such a decision unless the FTT applied the wrong principles, took account of the wrong factors, or otherwise reached a decision so plainly wrong that it must

> be regarded as outside the generous ambit of the discretion available to the FTT."

360. In *Mainpay v HMRC* [2025] EWCA Civ 1290 ("***Mainpay***"), the Court of Appeal endorsed the UT's approach, see [120]. In the instant case, HMRC point out that the BCG Parties "did not even ask the FTT to exclude this argument".

361. We agree with HMRC. First, the "on behalf of" point *was* pleaded in the Statements of Case, which say "if HMRC succeeds in persuading the Tribunal that they or *someone* acting on their behalf did not take reasonable care". It is true that there is no mention of the UK LLP having acted on behalf of the MDPs, and that point was first pleaded in the skeleton. However, if the BCG Parties had thought this was unfair, it was incumbent upon them to raise it before the FTT and they did not do so. It is too late to raise the point for the first time before us.

Whether the PwC Letter was obtained "on behalf of" the MDPs

362. HMRC's case was that in taking advice about the Capital Interests, the UK LLP was acting as agent for the MDPs. The BCG parties did not dispute that an LLP can act as agent for its members, but submitted that it was not doing so here, with Ms Lemos saying HMRC's position was "just an assertion".

363. However, as Mr Chacko pointed out, it had been Mr Holden's unchallenged evidence that "BCG obtained professional advice on the UK tax consequences (both for itself *and for the UK MDPs*) of each relevant change to its UK LTCV arrangements" (Mr Chacko's emphasis), and Mr Holden had gone on to list the advice, which included the PwC Letter. Mr Holden then said:

> "As the Capital Interests are held by, and disposed of by, the individual UK MDPs, those UK MDPs, rather than BCG, have ultimate responsibility for determining whether (and, if so, how) any disposal of Capital Interests should be reported on their individual UK self-assessment tax returns. However, to assist the UK MDPs in meeting their own UK tax compliance obligations, each year, BCG instructs PwC to prepare a letter of advice for each UK MDP, advising them on how each item of value received by them in the relevant year, in their capacity as an MDP, should be reported in their UK self-assessment return for that year (the PwC Advice Letters). The PwC Advice Letters are typically prepared around October each year, in respect of the tax year ended 5 April of that year, and are provided to each individual who was a UK MDP at any point during that tax year (including individuals who ceased to be UK MDPs during that tax year.
>
> The advice in the PwC Advice Letters reflect PwC's conclusions, as expressed in written advice to BCG, as to how those items of value should be treated for UK tax purposes (including as to how the holding and disposal of Capital Interests should be reflected in the UK MDPs' self assessment returns). The provision of these letters to the UK MDPs therefore allows the UK MDPs to benefit from that advice, without requiring them to review and consider that advice directly, or to obtain their own professional advice as to how those items of value should be treated (although they are entitled to obtain such additional advice, at their own cost, should they wish to do so)."

364. We agree with HMRC that in taking advice from PwC about the arrangements, including in particular the Capital Interests, the UK LLP was acting on its own behalf *and* on behalf of the MDPs.

The legislation

365. The parties also referred to the provisions in the TMA about the interaction between a partnership return, a partnership statement and a partner's individual returns.

366. TMA s 12AA(1) provides that the purpose of the partnership return is to facilitate the establishment of the amounts each partner is chargeable to income tax each year, and s 12AA(7) provides that the return must also include "the like particulars as if the partnership were liable to tax on any chargeable gain accruing on the disposal" of any partnership property. TMA s 12AB provides that a partnership return must be accompanied by a "Partnership Statement".

367. At the relevant time, TMA s 8(1B) read:

> "In the case of a person who carries on a trade, profession, or business in partnership with one or more other persons, a return under this section shall include each amount which, in any relevant statement, is stated to be equal to his share of any income, loss, tax, credit or charge for the period in respect of which the statement is made."

368. The following subsection defined "relevant statement" as follows:

> "In subsection (1B) above *"relevant statement"* means a statement which, as respects the partnership, falls to be made under section 12AB of this Act for a period which includes, or includes any part of, the year of assessment or its basis period."

369. By ITTOIA s 863(2)(a), those provisions applied to LLPs as they did to other partnerships. Thus, the MDPs were required to include exactly the same figures in their own SA returns as had been provided to HMRC by the UK LLP in its Partnership Statement.

What was provided to the MDPs

370. At [166] the FTT set out the following passage, which was taken from the parties' agreed Statement of Facts:

> "…in respect of each tax year within the Relevant Period, each UK [MDP] (including the individual Appellants) was provided with a letter of advice from PwC, setting out how PwC considered that that UK MDP should report the various amounts arising to that UK MDP out of his or her relationships with BCG in his or her UK self-assessment return for that year (the PwC Advice Letters). Where a UK MDP disposed of his or her Capital Interest in the year in question, the PwC Advice Letter sent to that UK MDP for the relevant year advised that UK MDP to report that disposal on the UK MDP's self-assessment return as a disposal of a capital asset (and, for certain of those UK MDPs, to claim entrepreneurs' relief in respect of that disposal, and to include a "white space" disclosure in their self-assessment return in respect of such claim). PwC was engaged to provide these letters by BCG and not by the individual UK MDPs themselves."

371. We asked Ms Lemos what was meant by "BCG" in that passage, and she referred to an engagement letter with BCG Inc, which we located after the hearing. It is between BCG Inc and PwC LLP in Boston, Massachusetts.

372. It appears from that letter (which is very general terms) and from subsequent invoices, that all PwC's services on a global basis were billed to BCG Inc. Ms Lemos went on to say that there was "no evidence in the Bundle" that the costs of the PwC Advice Letters had been recharged to the UK LLP or to the MDPs. However, Ms Atkinson, responding to those submissions on behalf of HMRC, identified a letter about PwC's professional fees for the *implementation* of the LLP having been recharged to the UK LLP, and after the hearing we located an email from PwC UK to Chris Joyce (elsewhere identified as "senior manager, partner services" at the UK LLP) which refers to their earlier discussions about the PwC Advice Letters; proposes a fee to be charged, and asks Mr Joyce to agree those fees. Although we were not taken to that email in the hearing, it is consistent with the letter located by Ms Atkinson.

We find that the UK LLP instructed PwC UK to provide the PwC Advice Letters, with both the UK LLP and PwC UK acting under the umbrella of the global agreement between PwC in Boston and BCG Inc and the costs being born by the UK LLP.

373. The FTT also found as follows:

> "180. Each letter included an appendix which was said to detail instructions on how to enter the individual's BCG income onto their tax return. The individuals were told that if they had a tax adviser they should pass those instructions onto them. Where Capital Interests were sold there was a section under the heading of "details of chargeable assets disposed of and gains and losses" which described the sale of a Capital Interest and the "disposal proceeds" resulting therefrom.
>
> 181. We find that the MDPs relied on the advice contained in the PwC letters in order to work out how to report their partnership income and the proceeds from "sale" of the Capital Interests."

374. We were taken to sample copies of the PwC Advice Letters, all of which included this wording:

> "These instructions are a guide to assist you in entering your BCG income on to your [year] UK tax return online using HM Revenue & Customs (HMRC) free online services. If you have a tax advisor who will prepare your UK tax return on your behalf, please pass these instructions on to them."

375. The FTT found at [182] that although some of the individual Appellants also engaged agents who filed their returns on their behalf, there was no evidence that any of those agents "took a different view to that stated in the PWC Advice Letters".

376. Mr Krinks' PwC Advice Letter included the information for the "Partnership" pages of his SA return, including his "share of the partnership's profit or loss". Under the heading "details of chargeable assets disposed of and gains and losses", the text read:

> "Please select 'yes' when asked 'Did you dispose of chargeable assets worth more than £42,400'. And select 'next'. You will then be asked 'do you want to use the capital gains computation worksheet for any of your disposals' please select 'next'. Please then enter the following details on the next screen:

Box	**Entry for your return**	**Additional information (not to be entered on your tax return)**
Your reference for this disposal	BCG capital interest	Sale of UK capital interests. Disposal of D2 shares
Type of asset	Unlisted shares & other securities	
Description of asset	3,508 BCG D2 shares	
Date of disposal	31/10/12	
Disposal proceeds or market value	£455,823	This is calculated as $731,871 @ $1 = £0.62171
Date of acquisition	1/4/2011	

Cost or market value	£249,436	As box above

377. When taken to this document during the hearing we expressed some surprise, because the disposal of the Capital Interests was described as a sale of "D2 shares", ie the shares in BCG Inc, although the Capital Interests related only to the growth in value of those shares. However, it was pointed out to us by the BCG Parties that HMRC had not raised this point and we have disregarded it.

378. The PwC Advice Letter continued by instructing Mr Krinks to complete the box "description of elections made and of reliefs claimed" by entering the words "Entrepreneur's relief", and also to include the figure £206,387 on the capital gains worksheet. It then said:

> "the final section to complete relating to capital gains is 'Any other information'. Please enter the following", being this text:
>
> > 'I hereby claim Entrepreneur's Relief under Section 169 of Taxation of Chargeable Gains Act 1992 on the sale of my partnership capital on 30 October 213.
> >
> > On 31 October 2012 I sold 3,508 Class D shares in the Boston Consulting Group LLP. These shares are not publicly traded and therefore a valuation was carried out by the LLP based on the net book value. This valuation has been independently reviewed. The value of the shares on the date of disposal was calculated to be USD 208.63 per share'."

379. Mr Krinks followed those instructions, and his SA return contains the information set out above. We were also taken by Ms Atkinson to Mr Holden's unchallenged witness evidence:

> "…members of my team obtained confirmation from each of the relevant UK MDPs that (i) they relied upon the PwC Advice Letters sent to them each year, in determining how to report their relationships with BCG on their UK self-assessment returns for that year; and (ii) where they had engaged a personal advisor to assist them in the preparation of their UK self-assessment return, that personal advisor followed the position recommended by PwC in the relevant PwC Advice Letter."

The LLPAs

380. Clause 5.7 of all the LLPAs provided as follows, consistently with the statutory requirements at TMA s 8(1B):

> "The Partnership shall provide to each Member such information as he shall require to enable him to make to the relevant taxation authority any return or self -assessment relating to his share of the Profit of the partnership."

381. Clause 11.6 included this text:

> "In discharging his duties, a Member who is an individual who does not have knowledge that makes reliance unwarranted is entitled to rely on information, opinions, reports or statements, including financial statements and other financial data, if prepared or presented by (i)…(ii) legal counsel, chartered accountants or other persons retained by the Partnership, as to matters involving skills or expertise the Member reasonably believes are matters: (A) within the particular person's professional or expert competence;…"

382. Clause 11.1(c) of all the LLPAs stated that each MDP was required to "comply with all statutes, regulations…professional standards and other provisions as may from time to time govern the conduct of the business".

383. We find that completing an SA return was a "duty" of the MDPs and that they were entitled to rely on information provided to them by PwC in order to complete their SA returns, which were required by law to be consistent with the Partnership Statement submitted by the UK LLP.

The case law

384. Both parties referred to *HMRC v Hicks* [2020] UKUT 0012 (TCC) ("***Hicks***"), where the UT considered what was meant by the term "person acting on behalf" of another. Mr Hicks had entered into a tax avoidance scheme (the "**Scheme**") designed by Montpelier Tax Consultants (IOM) Ltd ("**Montpelier**"). Mr Hicks' 2009-10 SA return was prepared by his accountant, Mr Bevis of Precision Accountancy, but as regards information relating to the Scheme, Mr Bevis relied entirely on input from Montpelier. Montpelier supplied the figures and information to be included in the return. It was common ground that Mr Bevis had acted "on behalf of" Mr Hicks, but the parties disagreed on whether Montpelier had also acted on his behalf.

385. At [122] of their judgment, the UT approved the following passage from *Trustees of the Bessie Taube Trust v HMRC* [2010] UKFTT 473 (TC) ("***Bessie Taube***") where the FTT had said that the expression "on behalf of":

> "connotes a person who takes steps that the taxpayer himself could take, or would otherwise be responsible for taking…Examples would in our view include completing a return, filing a return, entering into correspondence with HMRC, providing documents and information to HMRC and seeking external advice as to the legal and tax position of the taxpayer. The person must represent, and not merely provide advice to, the taxpayer.".

386. The UT went on to find that Mr Bevis had been careless. In relation to Montpelier, the UT first said at [154] that, in its role as seller of the Scheme, or "at most, an adviser to Mr Hicks", Montpelier was not acting on his behalf. The UT continued at [155]:

> "The second particular of carelessness on the part of Montpelier relates to its providing entries to Mr Bevis to be inserted into the tax returns. As we understand it, the information provided by Montpelier was of particular relevance in relation to the 2008/09 return which established the loss which was carried forward in the two subsequent years. Although we are not entirely clear as to this, the information provided appeared to relate to the figures for the dividends received by Mr Hicks and, possibly, the dates of those dividends. Although the provision of that information for the purposes of the 2008/09 return, producing a loss which was carried forward for the two subsequent years, brings Montpelier closer to the position of someone acting on behalf of Mr Hicks in relation to the returns for the two subsequent years, we regard the question as to whether Montpelier did cross the line into acting on behalf of Mr Hicks in relation to the relevant assessments as a difficult one. However, if we are right as to the nature of the information provided by Montpelier and in view of the FTT's finding that the transactions had taken place, it would seem to follow that the information provided by Montpelier was accurate and could not be said to have been carelessly provided. If the question as to the role of Montpelier were to be decisive of this case, we feel that we would need to investigate more thoroughly what precisely Montpelier did in relation to the completion of the tax returns. We might also need to consider whether there could be circumstances in which a third party who carelessly provides inaccurate information to a taxpayer to be used in a return could be regarded as acting on behalf of the taxpayer for the purposes of section 29(4). In view of the fact that these points are not necessary for our

> decision, in the light of our earlier conclusions, we do not think it appropriate for us to go further."

387. Thus, although the UT endorsed the description in *Besse Taube* as to what was meant by "on behalf of", the UT declined to express a view as to whether a person who "carelessly provides inaccurate information to a taxpayer to be used in a return could be regarded as acting on behalf of the taxpayer for the purposes of section 29(4)".

The FTT's conclusion

388. The FTT first cited the passage from *Bessie Taube* referred to in *Hicks* at [122], and then said:

> "The UK LLP obtained external advice from PwC as to the tax position of the individual Appellants. However, the UK LLP did not represent the individual Appellants. It merely arranged for advice to be provided to the taxpayers. We consider that this is too far removed to fall within the types of active engagement described in *Hicks* as falling within the term 'acting on his behalf'. HMRC have not argued that PwC was careless."

389. HMRC appealed that finding. The BCG Parties invited us to uphold the FTT's conclusion, adding that the MDPs each remained responsible for the completion and submission of their own SA returns.

Our view

390. Having taken into account both parties' submissions and the points set out above, we summarise our conclusions as follows.

(1) In taking advice from PwC about the arrangements, including in particular the Capital Interests, the UK LLP was acting on its own behalf and on behalf of the MDPs.

(2) The MDPs were entitled under the LLPAs to rely on that advice.

(3) Individual members of the UK LLP were required by TMA s 8(1B) to include exactly the same figures in their own SA returns as the UK LLP was required to provide in the Partnership Statement.

(4) PwC provided each MDP with an Advice Letter following instructions from the UK LLP and was thus acting on behalf of the UK LLP.

(5) The PwC Advice Letter stated that it contains "instructions" which were "a guide to assist" the MDP in completing the SA return. As it was a statutory obligation that the SA returns mirrored what was required to be included in the Partnership Statement, it is reasonable to infer therefore that each PwC Advice letter did set out that required information. The MDPs had to follow the instructions in the Advice Letter in so far as it contained information about the MDP's share of partnership income etc.

(6) The disposal proceeds were paid to MDPs by BCG Ltd and constituted miscellaneous income rather than a share of profits. There was thus no statutory obligation on the MDPs to follow the PwC Advice Letter in relation to the disposal of their Capital Interests.

(7) However, no such distinction was made in the PwC Advice Letter, and the MDPs followed all the instructions, including those about the Capital Interests.

(8) Turning specifically to Mr Krinks, his PwC Advice Letter set out exactly what was to be entered into the specified boxes on his 2012-13 SA return. Those entries included not only his share of the partnership's profit, but also details of the "chargeable assets"

disposed of and the exact wording of the text to enter in the "white space" about the disposal of his Capital Interests.

(9) In *Bessie Taube*, it had been held that a person acting "on behalf of" a taxpayer:

> "connotes a person who takes steps that the taxpayer himself could take, or would otherwise be responsible for taking…Examples would in our view include completing a return…".

(10) Had the UK LLP completed the boxes on Mr Krinks return, the position would be the same as the example in *Besse Taube.* Here, the PwC Advice Letter set out the content of the boxes and the white space and Mr Krinks simply copied that information. That cannot be enough to distinguish the two situations. To borrow the wording of the UT in *Hicks*, on the facts of this case the UK LLP did "cross the line into acting on behalf of Mr Krinks in relation to the 2012-13 assessment" because the PwC Advice Letters included instructions about how to complete the SA return in relation to the disposal of the Capital Interests; those instructions were issued on behalf of the UK LLP and reflected their incorrect understanding of the legal position, and Mr Krinks followed all the instructions, both those he was bound by statute to follow, and those relating to the Capital Interests.

391. We therefore agree with HMRC that the UK LLP was acting "on behalf of" Mr Krinks in relation to the completion of his SA return.

Causation

392. As set out earlier in this judgment, see §322, a discovery assessment made after the ending of the enquiry period is only valid if either of two conditions are met, the first of which that the loss of tax was (our emphasis) "*brought about* carelessly or deliberately by the taxpayer or a person acting on his behalf". The six year time limit in TMA s 36(1) similarly only applies if the loss was "*brought about* carelessly" by the taxpayer or a person acting on his behalf, see TMA ss 29(4) and 36(1) and (1B). In addition, TMA s 118(5) reads

> "For the purposes of this Act a loss of tax or a situation is brought about carelessly by a person if the person fails to take reasonable care to avoid bringing about that loss or situation."

Case law before Mainpay

393. At the time of the FTT Decision, there were two UT judgments in particular which had considered the meaning of "brought about", *Atherton* and *Bella Figura Limited v HMRC* [2020] UKUT 120 (TCC) ("***Bella Figura***"), but their approaches were difficult to reconcile.

394. In *Mainpay UT*, the parties made submissions on both *Atherton* and *Bella Figura*. HMRC relied on *Atherton,* saying that the position was as follows:

> "Because section 118(5) TMA provides that 'a loss of tax or a situation is brought about carelessly by a person if the person fails to take reasonable care to avoid bringing about that loss or situation'; thus, once a failure to take reasonable care is established, it inevitably follows that the taxpayer brought about the loss or situation…given section 118(5) 'there is no need to establish a separate causal link between the alleged carelessness and the loss of tax.".

395. The UT rejected that submission, saying:

> "156. What the Upper Tribunal was pointing out in *Atherton* was that the important word to focus on in section 118(5) was "avoid". If a taxpayer failed to take reasonable care to avoid the loss or situation, then they would have brought about the loss of tax. The point being emphasised was that that was not the same as a common law test of causation. However, the Upper Tribunal

> was not, in our view, saying that HMRC did not bear the burden of establishing that different test of causation. As we have said, if it was, then we would disagree.
>
> 157. As to what precisely HMRC must show in order to establish that a taxpayer has failed to take reasonable care to avoid the loss of tax, that depends entirely on the facts. To the extent that the carelessness which has been found relates to a deficiency in advice taken by a taxpayer we consider that HMRC do need to establish that the relevant deficiency could have been avoided by the taxpayer. How it could have been avoided will depend on the facts and on the nature of the deficiency. If, for instance, no advice was taken on a material issue, then the carelessness could have been avoided by taking advice on that issue. If the advice was from an adviser on whom it was unreasonable for that taxpayer to rely, then it could have been avoided by taking advice from a qualified adviser. If the relevant advice did relate to a material issue but was given on the basis of incomplete information or documentation, or of assumptions found not to be applicable in practice, then it could have been avoided by supplying the information or documentation or clarifying the position in relation to the assumptions.
>
> 158. To that extent, HMRC does in our view need to show what the taxpayer "should have done differently". Insofar as *Bella Figura* endorses the position we have just set out, we agree with its approach.
>
> 159. However, we do not consider that the burden on HMRC carries with it an obligation to prove a particular counter-factual outcome. In particular, in relation to carelessness said to result from deficient advice, it does not require HMRC to establish to the balance of probabilities what the result of remedying the deficiency would have been. For example, it does not require HMRC to establish that if the deficiency had been remedied, a failure in the arrangement to achieve its intended tax purpose, which led to the loss of tax, would have been remedied. Not all problems (or arrangements or schemes) can be "fixed", and the FTT should not be placed in the position of having to speculate as to a taxpayer's precise response to advice to a standard of reasonable care. If the Upper Tribunal in *Bella Figura* was indicating to the contrary, then we respectfully disagree."

396. The UT then turned to the situation of the appellant. Mainpay had acted on the basis that a particular contract was "an overarching contract of employment". However, that was not the case. The UT then said at [161]:

> "…the FTT was entitled to conclude that it was Mainpay's failure to take reasonable care in ensuring that the 2010 Contract was an overarching contract of employment which caused the loss of tax. On the facts found, what Mainpay 'should have done differently' was to have asked an appropriately qualified adviser whether the 2010 Contract as drafted (including a provision stating that it was not a contract of employment) was an overarching contract of employment, or otherwise effective to achieve the aim of the arrangements in relation to reimbursed expenses. In our view, the FTT was not required, by *Bella Figura* or otherwise, to put HMRC to proof of establishing what course of action Mainpay would have taken if that had been done, namely whether it would have amended the contract, introduced a retainer in an effort to create mutuality in the gaps, or decided not to claim the deductions which gave rise to the loss of tax."

397. Mainpay appealed to the Court of Appeal and the decision in *Mainpay* was published on 10 October 2025, just over a month before our hearing. Laing LJ gave the only judgment, with which King and Arnold LJJ both agreed.

398. Although in Mainpay, HMRC had not cross-appealed against the UT's rejection of their submission that "the words of section 118(5) of the TMA were a complete answer to Mainpay's argument on causation", Laing LJ confirmed that the UT had been correct. She said at [106] that the phrase "brought about" was a synonym for "caused".

399. In the context of the facts of Mainpay's case, she said:

> "116. On the F-tT's findings, it is obvious that had Mainpay taken reasonable care, the contracts would have been overarching contracts of employment. If they had been overarching contracts, the reimbursement of those expenses would not have been liable to tax... Mainpay did not take reasonable care to ensure that the contracts were overarching contracts. Mainpay nevertheless reimbursed the expenses free of tax, as if the contracts were overarching contracts, when, in law, those payments were liable to tax. Had Mainpay taken reasonable care, therefore, on the FtT's findings, that loss of tax would have been avoided.
>
> 117. On these particular facts, HMRC had, in the words of Mr Firth [counsel for Mainpay], 'done enough'. I do not consider that it was necessary for the F-tT to make any more findings about what would have happened if Mainpay had taken reasonable care. The F-tT nevertheless considered what would have happened if Mainpay had asked for specific advice…,even though that was not necessary on these facts. I do not consider that the F-tT was required to speculate about what might have happened if further advice had been sought, all the more so because a taxpayer cannot be required to waive legal advice privilege, so that the F-tT would not necessarily have and in this case did not have all the relevant evidence. I agree with the UT's analysis in paragraphs 159 and 161."

400. In the following paragraph, under the heading "the burden of proof" she said:

> "It is not in dispute that HMRC has the burden of proving that section 36(1) applies…On the facts of this case HMRC had made out a *prima facie* case that Mainpay had been careless, and that that carelessness had brought about a loss of tax. There was then an evidential burden on Mainpay, if it wished to contradict that *prima facie* case, to adduce evidence to show, on the balance of probabilities, that it had taken reasonable care, and/or that any lack of care did not bring about the loss of tax. Mainpay did not do that."

The FTT's approach in this case and the BCG Parties' Respondent's Notice

401. The FTT had rejected Mr Grodzinski's submission that there must be "a causal connection between the carelessness and the insufficiency in the tax assessments or returns", and referred to *Atherton,* see [415]. It is now clear that this was an error of law, although one which was unsurprising, given that the FTT Decision predated the publication of both *Mainpay UT* and Laing LJ's judgment in the Court of Appeal.

402. Although the FTT concluded that the UK LLP was careless, it went on to find that it was not acting "on behalf of" the MDPs. As a result, its finding only applied to the returns filed by the UK LLP and not to the SA returns filed by the MDPs.

403. The BCG Parties say in their Respondents' Notice (our emphasis):

> "…the FTT made no finding to the effect that any asserted carelessness on the part of UK LLP "brought about" the loss of tax in the UK MDPs' tax returns, and *HMRC have not challenged the FTT's failure to make a finding to that effect.* Accordingly, even if the UT were to hold that the UK LLP was acting on behalf of the UK MDPs and, even if the UT were to find that UK LLP had been careless for the reasons given by the FTT at [411], *it is not open to the*

> *UT to find that such brought about the relevant loss of tax, i.e. the loss of tax in each of the UK MDPs tax returns*."

404. However, HMRC had appealed the "on behalf of" point on the following basis (again, our emphasis):

> "Given that the FTT had concluded, correctly, that the UK LLP was careless the FTT *should therefore have further concluded* this was carelessness of a person "acting on…behalf of" the individual MDPs within the meaning of section 29(4) TMA such *that HMRC were entitled to raise the discovery assessments against the individuals to make good to the Crown the serious loss of tax which, as the FTT has found, has arisen in this case*."

405. We find that on a fair reading this ground of appeal includes a challenge to the FTTs' failure to find that the UK LLP's carelessness caused the loss of tax. Both parties made submissions on that issue and we have gone on to decide it.

The application of Mainpay to this case

406. In *Mainpay* at [117], the Court approved the analysis at [161] of the UT's judgment; we set this out at §396 above. Applying the same approach to the facts of this case, we find that it was the UK LLP's failure to take reasonable care in identifying the nature of the interests awarded to MDPs under the LLPAs which caused the loss of tax. On the facts found, what the UK LLP "should have done differently" was to have asked an appropriately qualified adviser whether the LLPAs as drafted gave the MDPs capital interests or revenue interests. In our view, the FTT was not required to put HMRC to proof of establishing what course of action the UK LLP would have taken if that had been done, namely whether it would have amended the LLPAs or introduced a different arrangement altogether or none.

407. We also find, consistently with *Mainpay* at [118], that HMRC had made out a *prima facie* case that the UK LLP had been careless, and that the carelessness had brought about a loss of tax. There was then an evidential burden on the UK LLP, if it wished to contradict that *prima facie* case, to adduce evidence to show, on the balance of probabilities, that it had taken reasonable care, and/or that any lack of care did not bring about the loss of tax. We consider that evidential question at §448 to §453.

Ms Lemos's submissions

408. We did not come to those conclusions without carefully considering Ms Lemos's submissions. She invited us to distinguish BCG's case from *Mainpay*, for several interlinked reasons. Her explanations were given over some five hours, and were interspersed with submissions about other matters. In setting out our understanding of her case, we have drawn from a number of different parts of her oral submissions.

(1) In *Mainpay,* Laing LJ said at [117] that her conclusions were based on the "particular facts" of that case, and she had gone on to say (Ms Lemos's emphasis) "the F-tT nevertheless considered what would have happened if Mainpay had asked for specific advice…even though that was not necessary *on these facts*". Ms Lemos submitted that *Mainpay* "is an example where the court considered that the question of causation was obvious"; she explained this by saying that Mainpay "was claiming deductions in respect of employees when the contract wasn't even a contract of employment", and this was a "glaring" error. In her submission, "the court in *Mainpay* did not give general guidance as to what HMRC must prove in cases where the answer to the question may not be obvious", as was the position here.

(2) In this case, HMRC had to show that "but for" the failure to take advice, there would have been no loss of tax.

(3) HMRC were therefore required to prove that if the UK LLP had taken advice, there would have been no loss of tax, and to do so HMRC had to "put forward an evidential basis for that assertion" by showing "that no reasonably competent advisor would have come to the view contrary to the one which they say is correct".

(4) Ms Lemos said it followed from the above that HMRC could only satisfy their burden of proving causation in relation to MDPs who were found to be taxable under the miscellaneous income rules "by proving that any other reasonably competent advisor, other than PwC…would have advised that the miscellaneous income charge…would have applied to tax the disposal proceeds of a Capital Interest as income in the hands of UK MDPs".

409. As set out above, Ms Lemos first sought to distinguish the approach taken in *Mainpay,* where there was an "obvious" error, from other cases, including this one. However, as Mr Magee pointed out, the error made by Mainpay was not that it was "claiming deductions in respect of employees when the contract wasn't even a contract of employment", as Ms Lemos had said was the case. Instead, it *was* a contract of employment, but not an "overarching" contract, so individuals did not remain employed between assignments[6] with the result that the travel expenses at issue in Mainpay were not allowable for tax purposes.

410. We agree with Mr Magee that Laing LJ did not limit the scope of her judgment to cases where the taxpayer made an "obvious" error, such as thinking a document was an employment contract when it plainly was not. Instead, she said at [116] that "[o]n the F-tT's findings, it is obvious that had Mainpay taken reasonable care, the contracts would have been overarching contracts of employment". In other words, what was obvious was the link between the failure to take advice and the loss of tax.

411. We also do not read the guidance in *Mainpay* as being limited to cases where there is an obvious link between a failure to take advice and a loss of tax, such that in other cases, HMRC have to do more than make out a *prima facie* case that (a) the taxpayer had been careless and (b) that carelessness had brought about a loss of tax, with the evidential burden then shifting to the taxpayer. We return to the evidential burden again in relation to Ms Lemos's points (3) and (4), which we discuss below.

412. Ms Lemos's second point was that in a case such as this, where the error was not "obvious", HMRC had to show that "but for" the failure to take advice, there would have been no loss of tax**.** She said:

(1) until changes were made to the TMA by FA 2008, HMRC had to show that a taxpayer had been negligent (or fraudulent) in order that HMRC could benefit from the extended time limit in TMA s 36.

(2) The word "negligent" here had the same meaning as in tort, and thus required HMRC to show that "but for" a certain action or a failure to act, there would not have been a loss of tax.

(3) Although the term "negligent" had now been replaced by "careless", that made no difference: HMRC were still required to satisfy the "but for" test.

413. The previous statutory wording was not included in the Authorities Bundle, but we located it after the hearing. It read:

> "An assessment on any person (in this section referred to as "the person in default") for the purpose of making good to the Crown a loss of income tax or capital gains tax attributable to his fraudulent or negligent conduct or the

[6] See [42] of the FTT Decision referred to in *Mainpay UT* at [13]

> fraudulent or negligent conduct of a person acting on his behalf may be made at any time not later than 20 years after the 31st January next following the year of assessment to which it relates."

414. Ms Lemos did not identify any direct authority for her submission that before the law changed in 2008, HMRC had to meet the same test as applies in tort. There is a helpful summary of what that requires in *Delphi Derivatives v HMRC* [2023] UKFTT 00722 (TC)[7]:

> "167…To establish liability in tort, it is necessary to prove the chain of causation whereby a duty of care existed between the parties, there was a breach of that duty (by omission or commission of a certain action), and that breach of duty is the proximate cause of the damage or injury sustained. The most important element of proof is the casual link between the breach and the injury, and causation in tort is often cast in terms of 'but for' the defendant's actions/omissions, the plaintiff's injury would not have occurred.
>
> 168. The 'but for' type of causation in tort requires *specificity* in order to establish the breach of a particular duty of care is the cause of injury. Specificity for each element of proof requires the pinpointing of an action or omission to establish the breach, and that it is a specific breach that is the immediate cause of the injury. Each element of proof in tort is primarily objective, and the causal link required to be established for each element needs to be tight to prove proximity whereby the breach in question is the *immediate* cause of the injury in question."

415. Ms Lemos also did not take us to any authority which supported her submission that there had been no change to the meaning of the provision as the result of the amendments made by FA 2008. We noted that in *Tooth v HMRC* [2021] UKSC 17[8], the Supreme Court had considered the same changes in relation to the move from "fraudulent" to "deliberate" and in so doing took into account the related Explanatory Notes, see [33] and [45]. Those Notes say that the change to TMA s 36 "corresponds to the terms used in paragraph 3 of Schedule 24 to FA 2007", which prescribes penalties for submitting an inaccurate return. The Explanatory Notes for Schedule 24 say that it:

> "brings together a single penalty framework for a number of different taxes where there were previously different ones. It makes explicit that the penalty is behaviour related and uses new terms to describe behaviour."

416. The Notes then say:

> "These definitions of behaviour are designed to replace the current concepts of misdeclaration, repeated misdeclaration, dishonest conduct and reasonable excuse (in relation to inaccuracies) for VAT, and for direct taxes they replace fraudulent and negligent conduct. They provide a uniform language for behaviours, using more accessible language across the taxes covered."

417. The new wording of TMA s 36, which piggybacked on these earlier changes to the penalty regime, therefore changed the "concept" from negligence to carelessness, as well as standardising terms across different taxes and using more accessible language.

418. Although Ms Lemos did not cite case law which referred explicitly to the "but for" test, or refer us to any extra-statutory material, she did rely on various earlier judgments as well as on *Mainpay* for her submission that the "but for" test had always applied and continued to

[7] We were told on the final day of the hearing that this case had been appealed to the UT and judgment was awaited, but neither party asked for this case to be stayed pending the publication of that judgment.

[8] Referred to in the BCG Parties' Respondents' Notice in the context of causation

apply, because there had been no change when s 36 was amended by FA 2008. We were, however, unconvinced.

419. Ms Lemos' third point was that HMRC had to prove that "no reasonably competent advisor would have come to the view contrary to the one which they say is correct". That submission is inconsistent with *Mainpay,* where Laing LJ had held that HMRC was not required to prove that countfactual, but only to make a *prima facie* case that the loss of tax had been caused by the taxpayer's carelessness; it was then for the taxpayer to "to adduce evidence to show, on the balance of probabilities, that it had taken reasonable care, and/or that any lack of care did not bring about the loss of tax". Ms Lemos submitted that this approach was limited to "obvious" errors, but we disagree: the Court of Appeal endorsed the following passage from the UT's judgment, which was not limited to "obvious" errors:

> "In particular, in relation to carelessness said to result from deficient advice, it does not require HMRC to establish to the balance of probabilities what the result of remedying the deficiency would have been…the FTT should not be placed in the position of having to speculate as to a taxpayer's precise response to advice to a standard of reasonable care."

420. In other words, HMRC is not required to lead evidence or otherwise prove what would have happened had advice been taken, and they are therefore also not required to prove that "no reasonably competent advisor would have come to the view contrary to the one which they say is correct".

421. We therefore reject Ms Lemos's submission that HMRC could only satisfy the causation requirement in relation to Mr Krinks if they could show that "any other reasonably competent advisor, other than PwC…would have advised that the miscellaneous income charge would have applied". That submission is inconsistent with *Mainpay.*

Evidential burden

422. It follows from our analysis above that it was for the BCG Parties to adduce evidence to show, on the balance of probabilities, that UK the LLP had taken reasonable care, and/or that any lack of care did not bring about the loss of tax. The first part of that requirement has already been considered: we have found that the UK LLP did not take reasonable care in obtaining advice about the tax consequences of introducing the Capital Interests; it then provided that information to Mr Krinks via the PwC Advice Letter and acted on his behalf in relation to his 2012-13 SA return.

423. However, the BCG Parties submitted that, even if the UK LLP was careless, that carelessness did not bring about the loss of tax. They relied on Mr Holden's evidence, which they said showed that no professional adviser had suggested that disposal of the Capital Interests would give rise to miscellaneous income. However, that evidence was robustly challenged by Mr Baldry on behalf of HMRC. It is also clear from the superficial summary in the PwC Letter (which constituted the "grand summary of all the advice" that the UK LLP had received from that firm) that it falls well short of evidence that the lack of care did not bring about the loss of tax.

Conclusion on causation

424. For the reasons set out above, we find that the UK LLP's carelessness caused the loss of tax.

Overall conclusion: tax year 2012-13:

425. For the reasons set out above, we find that (a) the UK LLP acted carelessly; (b) it was acting on behalf of Mr Krinks; and (c) the carelessness caused the loss of tax, and we therefore uphold the assessment on Mr Krinks.

TAX YEARS 2013-14 AND 2014-15

426. The only 2013-14 assessments under appeal before us were those issued to Mr Holden and Mr Nascimento. There were no procedural issues arising in relation to Mr Holden's appeal, so HMRC's success on the miscellaneous income issue means that his assessment for that year is upheld.

427. Mr Nascimento filed his SA return on 26 January 2015, and HMRC issued an assessment under TMA s 29 on 8 March 2019, more than four years after the ordinary time limit in TMA s 34. For the same reasons as set out above in relation to Mr Krinks, we uphold the 2013-14 assessment on Mr Nascimento because we find that (a) the UK LLP acted carelessly; (b) it was acting on behalf of Mr Nascimento; and (c) the carelessness caused the loss of tax

428. There were no individual assessments for 2014-15 under appeal before us, and no procedural challenges to HMRC's amendment of UK LLP's return.

TAX YEAR 2015-16

429. UK LLP filed its 2015-16 return on 21 January 2017. HMRC amended that return on 26 March 2021, after the four year ordinary time limit given by TMA s 34. That amendment therefore only takes effect if TMA s 36(1) was satisfied, in other words, the loss of tax was "brought about carelessly" by the UK LLP.

430. We have already upheld the FTT's finding that the UK LLP was careless in relation to the years 2012-13 and 2013-14. We have also found that for the tax years 2014-15 to 2016-17, the MMRs applied. As the UK LLP filed its Partnership Return on the basis that it was outside the scope of those provisions, the next question is whether the UK LLP was careless in so doing.

431. The legislation which applies to a discovery assessment issued to a partnership, including an LLP, is TMA s 30B. This is a mirror of the s 29 provisions which apply to individuals (see §322), and is set out at [435] of the FTT Decision. TMA s 36(1) applies in the same way to discovery assessments issued under TMA s 30B as it does to those issued under TMA s 29.

Whether the UK LLP was careless

432. The FTT made the following findings of fact about the MMRs, see [147], [148] and [173]:

(1) On 20 May 2013, HMRC published a consultation document about the introduction of the MMRs.

(2) Given the perceived risk of tax costs arising from the proposals it was decided that BCG Ltd would purchase all the UK MDPs' Capital Interests with effect from 31 March 2014.

(3) Before the 2014 LLPA was implemented, PwC wrote a report which included this passage:

> "PwC believe that the proposed changes to the LTCV will segregate the profits that are subject to tax on the partners and any gain realised on the growth in value of the LTCV; however to gain further comfort on the likely interpretation of the tax tribunals and courts would apply [sic] the 'reasonable to suppose' test we would recommend that BCG seek specialist counsel's opinion before implementing the new LTCV in the UK."

433. Ms Lemos took us to the text of that advice, which was dated June 2014. The passage set out above is from the Executive Summary. In the main body of the advice, PwC set out a

number of concerns about the "reasonable to suppose" test which forms part of Condition Y, before concluding as follows:

> "We believe that under the new LTCV there will be a power to enjoy. It will then come down to a question of fact as to whether it is reasonable to suppose that the individual partners' profit shares would be lower than they would be absent the new LTCV. The clear policy of not giving an additional profit share to individual partners who do not participate in the LTCV should put the matter beyond doubt. But the possibility that the tax tribunal would take a different view of what is reasonable to suppose cannot be eliminated. Therefore, there remains a risk that Condition Y would be satisfied. In such circumstances, we would recommend for further comfort that tax counsel's opinion is sought on the likely interpretation by the tribunals and courts on the 'reasonable to suppose' [test]."

434. The FTT made the following findings of fact about a different report produced by Ernst & Young LLP ("**EY**"):

> "178. In mid to late 2014 EY were engaged by BCG to consider options for re-introducing the LTCV for MDPs including the Capital Interests. EY provided a note of advice in draft form. A finalised version of that note has not been provided and given the fact that Mr Holden told us that BCG relied on the EY note as well as the PwC advice it is somewhat surprising that a final version was not obtained. Furthermore, the advice obtained was limited to a few briefly stated conclusions with little underling analysis. Without any explanation of the factors considered in relation to the Capital Interests EY simply state that as the UK LLP is transparent, they would argue that the LTCV is treated as a disposal of goodwill on sale. The tax risks associated with the MMRs are dealt with in one short paragraph concluding that EY would "argue" that the rules would not apply primarily because of the "defence" that the LTCV is mandatory and has no effect on the level of the UK LLP partnership profits which accrue to the partners.
>
> 179. In using the words "argue" and "defence" the reader is put on notice that this is a potentially contentious area. Yet EY were not asked to provide a fuller analysis of the risks or even to finalise the draft."

435. In relation to advisers other than PwC and EY, the FTT found at [174]:

> "There is also reference in the evidence to the business also working with multiple external advisers to analyse the draft MMR rules. However, there is little evidence beyond that, showing what those multiple external advisers said, save for the evidence of advice from PWC and a very generalised level of evidence from Mr Holden."

436. On the basis of its findings of fact, the FTT held that the UK LLP was careless in relation to its return for 2015-16, and relied in particular on the following, set out as the final two subparagraphs of [411]:

> "(3) In 2014 the potential for challenge increased as the MMRs were drafted and then implemented. There had been sufficient concern for BCG to decide that the MDPs should all sell their Capital Interests. Before reintroducing the structure advice was obtained from PwC which clearly indicated a risk of challenge under the new s850C and which recommended that BCG obtained tax counsel's opinion, but that step was not taken. In that context we consider it would be entirely reasonable to expect a large corporate with a large amount at stake and clear advice to obtain a specialist opinion, to do just that;

> (4) The advice received from EY in 2014 was very high level with minimal analysis of the tax position or risks and was never finalised. Its wording, using terms such as "argue" and "defence" made clear, however, that the treatment of the Capital Interests was potentially contentious."

437. HMRC invited us to uphold those conclusions, submitting that the actions of the UK LLP fell below the standard of a very sophisticated taxpayer "operating a bespoke remuneration arrangement dealing with very large sums of money", which had acted upon "tentative and draft advice which explicitly warned them to seek counsel's opinion".

The right question?

438. The BCG Parties submitted in their skeleton argument that the FTT had wrongly focused on the advice given to the UK LLP about whether the MMRs would apply if they reintroduced the Capital Interests, and it should instead have focused on the advice given by PwC to the UK LLP on the basis of which it filed its Partnership Return. The skeleton continued:

> "Had it considered the right question, the FTT should have concluded that UK LLP's tax returns were indeed filed consistently with the 'implicit reassurance' provided by PwC that the profit allocations made in each of the tax returns were correct, (i.e. including the profit allocation made each year to BCG Ltd after the MMRs came into force)."

439. The phrase "implicit reassurance" is taken from *Bella Figura*, where the UT considered the FTT's finding that Bella Figura Ltd ("**BFL**") had been careless because it had failed to take further advice. The UT said at [61(1)] of its judgment that the FTT:

> "…should have gone on to consider…whether even in the absence of specific advice, BFL obtained implicit reassurance that the loans would qualify which was enough to amount to the taking of reasonable care. By analogy, a person who instructs a lawyer to act on the purchase of a house might be said to obtain implicit advice to the effect that the documents will operate to convey title simply from the fact that the lawyer prepares those documents and identifies no problem with them."

440. We do not agree that the FTT asked "the wrong question". As HMRC pointed out, there was no evidence before the FTT as to any separate advice having been given by PwC about the completion of the Partnership Returns: Mr Holden's witness statement did not say that UK LLP had relied on PwC in order to prepare the Partnership Return and in the skeleton prepared for this hearing the only evidence referred to by the BCG Parties was that PwC was named as UK LLP's "agent" on its Partnership Return. The FTT was fully entitled to consider the evidence with which had been provided as to the advice received by the UK LLP before the Partnership Return was filed.

441. Moreover, in this case, any "implicit reassurance" that the UK LLP obtained from PwC can only have been based on the views that firm had expressed when they gave advice about the possible application of the MMRs. PwC did not give unqualified advice: instead, they said that a tax tribunal may take a different view, and recommended that counsel's opinion be sought. The position was thus very different from that in *Bella Figura.*

Not a requirement?

442. Ms Lemos also submitted that the passage from the PwC advice (see §433 above) provided the UK LLP with a "clear and unqualified view", adding that PwC did not "mandate" obtaining counsel's opinion, but instead made a "recommendation" for "further comfort". She said that as the UK LLP had "its own sophisticated tax department", it acted entirely reasonably in not following PwC's recommendation. She also placed reliance on the fact that the UK LLP subsequently obtained further advice from EY.

443. We reject those submissions. The MMR legislation is complex, targeted anti-avoidance legislation, about which the UK LLP was so concerned that it terminated the 2011 LLPA. As the FTT rightly said "[i]n that context we consider it would be entirely reasonable to expect a large corporate with a large amount at stake and clear advice to obtain a specialist opinion, to do just that". Obtaining a draft note of advice, which was never finalised, from EY was no substitute for obtaining the opinion of specialist tax counsel, particularly as EY's advice note was brief with "little underlying analysis" and used the words "argue" and "defence" which, as the FTT said, put the reader "on notice that this is a potentially contentious area".

Advice predated the 2014 LLPA

444. When we were taken by Ms Lemos to the advice given by PwC, we observed that it had been prepared before the drafting of the 2014 LLPA: the executive summary says that "It is now proposed to introduce a new LTCV", and the "assumptions" section of the advice begins "we have assumed that the new LTCV will work as follows".

445. Ms Lemos responded to our point by saying that the FTT had not found as a fact that PwC's advice predated the 2014 LLPA. However, it is self-evident from the wording in the advice, and consistent with the dates: the advice was provided in June 2014, while the 2014 LLPA was dated 1 December 2014.

446. It follows that there is no evidence that PwC advised on the changes between the 2011 LLPA and the 2014 LLPA, in particular new clause 3.7 which provided that "All capital profits shall belong to and be allocated to BCG Ltd" and the deletion of Clause 16.3(c) from the Clause 16.3 Waterfall, see our earlier discussion at §152 to §182 . These were significant changes, and it was plainly careless not to obtain advice about how they affected the tax treatment of the Capital Interests. However, HMRC did not make this point at the FTT or in their submissions at the UT, and we have come to our conclusion below without relying on it.

Conclusion on carelessness

447. We agree with the FTT for the reasons it gave that the UK LLP was careless in filing its return for 2015-16 on the basis that the MMR did not apply.

Causation

448. The next question is whether that carelessness caused the loss of tax. We agree with HMRC that the starting point is as set out below:

> "Having found that the UK LLP had implemented arrangements of this complexity without proper advice supporting their tax analysis, and that this fed into how they filed their returns, there was a *prima facie* case that any errors in those returns were brought about by that failure to take advice. It was, as the Court of Appeal has made clear [in *Mainpay*], for the BCG Parties to prove, if they sought to do so, that their failure made no difference to the way they chose to return the tax consequences."

449. Ms Lemos submitted that it was clear from the evidence that had the UK LLP taken further advice, that advice would have confirmed its view that the MMRs did not apply. She relied on the following:

(1) PwC's overall conclusion in their 2014 report, which was as follows:

> "On balance, we do not believe that the new legislation should apply to the new LTCV on the basis that:
>
> - the new LTCV does not involve deferred profits, and
> - it is not reasonable to suppose that, absent participation in the new LTCV, the individuals would receive a higher profit share."

(2) EY's conclusion that, on balance, the MMRs ought not to apply to the UK LLP if the Capital Interests were re-introduced.

(3) The FTT's decision that neither Condition X nor Condition Y applied.

450. In addition, Ms Lemos submitted that the application of s 850C to the facts of a case involve:

> "evaluative judgments in respect of which there was no case law guidance [and] is (almost *par excellence*) an issue in respect of which different experts might reasonably come to different conclusions."

451. Ms Lemos accepted that this would mean that in complicated cases, carelessness could not be demonstrated, saying "it wouldn't be a surprising outcome if the Revenue couldn't go back to reopen something that's really complicated and that different people might have reasonably come to different views".

452. Having considered those submissions, we find as follows:

(1) We do not agree that the PwC report is evidence that had the UK LLP taken further advice, it would have confirmed that the MMRs did not apply: PwC had concluded that "there remains a risk that Condition Y would be satisfied" and recommended that the position be checked with tax counsel.

(2) We come to the same conclusion in relation to the EY report, which (as already noted) was both brief with "little underlying analysis" and also used the words "argue" and "defence".

(3) As to the FTT's decision, this plainly cannot be evidence in the appeal and cannot be used to meet the evidential burden that the UK LLP needs to satisfy, see *Mainpay* at [118]. It is at best an indication that a tax specialist could reasonably have concluded that the MMRs did not apply.

(4) However, it is not sufficient that in a complex area a tax specialist *could* have come to a view which supported the position taken. The taxpayer is required to show that it was not careless *because it received and relied on that advice*. We agree with Mr Magee that it would be "clearly wrong" if "where a taxpayer has done an aggressive tax avoidance scheme that is complicated or in a sufficiently complicated area of law, they can never be found to be careless where they have failed to take adequate advice".

(5) We find that the BCG Parties have not met their evidential burden for this tax year.

Conclusion: tax year 2015-16

453. For the reasons set out above, we find that the UK LLP was careless, and that the carelessness caused the loss of tax.

TAX YEAR 2016-17

454. The UK LLP filed its 2016-17 return on 15 January 2018, and HMRC amended that return on 26 March 2021. This was within the four year ordinary time limit given by TMA s 34. However, it was outside the "enquiry window" for that return, so the assessment is only valid if one of the two conditions at s 30B(4) are satisfied.

455. Both of these conditions cross-refer to "the situation in subsection (1)", which is that:

> "an officer of the Board or the Board discover, as regards a partnership statement made by any person (the representative partner) in respect of any period—

> (a) any profits which ought to have been included in the statement have not been so included, or
>
> (b) an amount of profits so included is or has become insufficient…"

456. The first condition is that "the situation mentioned in subsection (1) above was brought about carelessly or deliberately by (a) the representative partner or a person acting on his behalf". Our conclusion on this point is the same as for the previous year.

457. The second condition is that:

> "at the time when an officer of the Board
>
> (a) ceased to be entitled to give notice of his intention to enquire into the representative partner's partnership return
>
> (b) …
>
> the officer could not have been reasonably expected, on the basis of the information made available to him before that time, to be aware of the situation mentioned in subsection (1) above…"

458. This is generally known as the "hypothetical officer" test. Although HMRC invited us to call it the "insufficient disclosure test", that term is not used in the case law and we have therefore continued to call it the "hypothetical officer" test.

The hypothetical officer test

459. It was common ground before the FTT that the focus of this test is on the quality of the taxpayer's disclosure and whether it clearly alerts the hypothetical officer to the insufficiency in the assessment or return.

460. In *Langham v Veltema* [2004] EWCA Civ 193, [2004] STC 544, Auld LJ, giving the leading judgment, said at [33] by reference to essentially the same provisions in TMA s 29:

> "…it is plain from the wording of the statutory test in s 29(5) that it is concerned, not with what an Inspector could reasonably have been expected to do, but with what he could have been reasonably expected to be aware of. It speaks of an Inspector's objective awareness, from the information made available to him by the taxpayer, of 'the situation' mentioned in s 29(1), namely an actual insufficiency in the assessment, not an objective awareness that he should do something to check whether there is such an insufficiency."

461. In *HMRC v Lansdowne Partners LP* [2011] EWCA Civ 1578 ("***Lansdowne***") Morritt C gave the leading judgment; Moses LJ delivered a concurring judgment and Patten LJ agreed with both judgments. Morritt C said at [56]:

> "I do not suggest that the hypothetical inspector is required to resolve points of law. Nor need he forecast and discount what the response of the taxpayer may be. It is enough that the information made available to him justifies the amendment to the tax return he then seeks to make. Any disputes of fact or law can then be resolved by the usual processes."

462. Moses LJ said at [68] that on the facts, HMRC had been provided with certain key information some 10 months before the closure of the enquiry window. He continued at [69]:

> "But even if the information had been obtained shortly before the time for enquiry expired, I would have taken the view that an officer could have reasonably been expected to be aware that the profits stated were insufficient. The legal points were not complex or difficult. As the Chancellor points out (at [56]), awareness of an insufficiency does not require resolution of any potential dispute. After all, once an amendment is made, it may turn out after

complex debate in a succession of appeals as to the facts or law, that the profits stated were not insufficient. I have dwelt on this point because I wish to leave open the possibility that, even where the taxpayer has disclosed enough factual information, there may be circumstances in which an officer could not reasonably be expected to be aware of an insufficiency by reason of the complexity of the relevant law."

463. He added at [70] that "[t]he statutory condition turns on the situation of which the officer could reasonably have been expected to be aware. Awareness is a matter of perception and of understanding, not of conclusion."

464. In *HMRC v Charlton* [2012] UKUT 770 (TCC) ("***Charlton***"), the UT said at [60] that "the correct focus of s 29(5)…is on the quality and extent of the information made available, and not on the qualities of the hypothetical officer", but then continued at [65]:

> "Our conclusion on this point, therefore, is that s 29(5) does not require the hypothetical officer to be given the characteristics of an officer of general competence, knowledge or skill only. The officer must be assumed to have such level of knowledge and understanding that would reasonably be expected in an officer considering the particular information provided by the taxpayer. Whilst leaving open the exceptional case where the complexity of the law itself might lead to a conclusion that an officer could not reasonably be expected to be aware of an insufficiency, the test should not be constrained by reference to any perceived lack of specialist knowledge in any section of HMRC officers. What is reasonable for an officer to be aware of will depend on a range of factors affecting the adequacy of the information made available, including complexity. But reasonableness falls to be tested, not by reference to a living embodiment of the hypothetical officer, with assumed characteristics at a typical or average level, but by reference to the circumstances of the particular case."

465. In *Sanderson v HMRC* [2016] EWCA Civ 19, [2016] 4 WLR 67 ("***Sanderson***") Patten LJ gave the only judgment, with which Briggs and Simon LJJ both agreed. He said at [17]:

> "It is clear as a matter of authority: (1) that the officer is not the actual officer who made the assessment…but a hypothetical officer; (2) that the officer has the characteristics of an officer of general competence, knowledge or skill which include a reasonable knowledge and understanding of the law: see *Revenue and Customs Comrs v Lansdowne Partners LP* [2012] STC 544[9]; (3) that where the law is complex even adequate disclosure by the taxpayer may not make it reasonable for the officer to have discovered the insufficiency on the basis of the information disclosed at the time: see *Lansdowne* at para 69; (4) that what the hypothetical officer must have been reasonably expected to be aware of is an actual insufficiency: see *Langham v Veltema* [2004] STC 544 per Auld LJ, at paras 33–34."

466. At [25], Patten LJ expanded on the distinction between the "actual officer" and the "hypothetical officer", saying:

> "I do not accept that sections 29(1) and (5) import the same test and that the Revenue's power to raise an assessment is therefore directly dependent on the level of awareness which the notional officer would have based on the section 29(6) information. The exercise of the section 29(1) power is made by a real officer who is required to come to a conclusion about a possible insufficiency based on all the available information at the time when the discovery assessment is made. Section 29(5) operates to place a restriction on the

[9] The reference should be to *Charlton*

> exercise of that power by reference to a hypothetical officer who is required to carry out an evaluation of the adequacy of the return at a fixed and different point in time on the basis of a fixed and limited class of information. The purpose of the condition is to test the adequacy of the taxpayer's disclosure, not to prescribe the circumstances which would justify the real officer in exercising the section 29(1) power. Although there will inevitably be points of contact between the real and the hypothetical exercises which sections 29(1) and (5) involve, the tests are not the same."

The FTT's view

467. The FTT held at [444]:that by 31 January 2019, when the "enquiry window" for the 2016-17 return closed, the hypothetical officer would have had the following information:

(1) the descriptions of the Capital Interests in the UK LLP's accounts alerting the officer to a description of payments made for services and potentially of an income nature;

(2) the 9 November 2018 package of information from PwC which included a schedule of Capital Interests; a schedule of grants of Capital Interests; a slide deck explaining profit allocation methodology; written resolutions of the Remuneration Committee, profit allocation statements; and the PwC Letter; and

(3) the disposal values for "sales" of the Capital Interests which would have been included in the MDPs' SA tax returns, albeit on the basis of disclosing the disposal of assets chargeable to tax on a capital gains tax basis.

468. The FTT then applied the law as summarised in *Sanderson,* saying at [430] that:

> "Our decision about the hypothetical officer test turns on what the hypothetical officer needed to know in order to make the assessment… we agree with Mr Baldry that the hypothetical officer could not have reasonably been expected on the basis of the information made available to him before January 2019 to have been aware of the way in which sums were put aside to fund future purchases of the Capital Interests. That would be a key element of any charge under the profit sharing rules and the MMRs. Consequently, the hypothetical officer test would have been met."

469. In other words, the FTT found that HMRC would have succeeded on the hypothetical officer point. However, those findings were *obiter* because the FTT had previously found that neither Conditions X or Y were met. The BCG Parties challenged the FTT's conclusion in their Respondents' Notice.

Submissions on behalf of the BCG Parties

470. The BCG Parties' first submission under this heading was that the FTT was wrong to have found that the hypothetical officer was unable to make the assessment by 31 January 2019 because he would have been unaware "of the way in which sums were put aside to fund future purchases of the Capital Interests". The BCG Parties said that the hypothetical officer would have been aware that sums had been allocated to BCG Ltd (the figures are set out at §194(6) above), and would also have been aware that those amounts were significant in the context of the UK LLP's overall profit: in 2015-16, BCG Ltd was allocated 22.7% of the UK LLP's profits.

471. Although the BCG Parties accepted that there was a difference between the actual officer who made the assessments (here, Mr Taylor), and the hypothetical officer, their second submission was that *in this case,* what Mr Taylor knew was a good proxy for what the hypothetical officer would have known. They drew attention to a letter sent by Mr Taylor on 10 January 2019, and thus within the enquiry period, following receipt of a package of

information from PwC on 9 November 2018. The BCG Parties relied on a passage in that letter under the heading "Mechanism to defer profit entitlements of individual members in favour of BCG Ltd", where Mr Taylor had said:

> "Under the Capital Interests Scheme arrangements, profits allocated to the corporate member (which are then subsequently paid to the UK individual members under the Capital Interests Scheme arrangements) would give rise to a significant tax advantage (both in timing and amount) for the UK individual members, by virtue of an increase in the D2 share value within BCG Inc (broadly commensurate to the profits allocated to and retained in BCG Ltd)".

Discussion

472. We began by considering the distinction between the actual officer and the hypothetical officer. In *Sanderson*, Patten LJ said that the hypothetical officer was "required to carry out an evaluation of the adequacy of the return at a fixed and different point in time on the basis of a fixed and limited class of information". However, in this case, the information which would have been available to that hypothetical officer was the same as that available to Mr Taylor: the detailed correspondence between the parties allows us to know what that information was. We therefore agree with the BCG Parties that the hypothetical officer would have had the same information as Mr Taylor.

473. We had no submissions on the competence, knowledge or skill of the hypothetical officer, but the UT in *Charlton* held that he "must be assumed to have such level of knowledge and understanding that would reasonably be expected in an officer considering the particular information provided by the taxpayer". We find that this too supports the BCG Parties' submission that Mr Taylor was a good proxy for the hypothetical officer.

474. Having accepted that point, we move on to consider Mr Taylor's assessment of the information with which he had been provided. Ms Lemos submitted that "all the hypothetical officer needed to know [to make the MMR assessments] is that there were sums put aside" and that information to that effect had been provided by PwC before the closure of the enquiry window. HMRC disagreed, saying that the passage in Mr Taylor's letter of 10 January 2019 which was relied on by the BCG Parties envisages "a direct deferral of profit share by individuals to BCG Ltd in a manner that would be challenged under s 850…and not the much more complex set of tests applicable to s 850C".

475. We agree with HMRC: the information provided to Mr Taylor was insufficient to allow him (or the hypothetical officer) to amend the Partnership Return on the basis that s 850C applied; for that he would have needed to know how much profit had been deferred and in relation to which MDPs. The FTT made essentially the same point when it held at [468] that no amendment could be made to the Partnership Return before the closure of the enquiry window without knowledge of "the way in which sums were put aside to fund future purchases of the Capital Interests", and that information had not been provided.

476. In addition, we add a further point (not relied on by HMRC), namely that deferral of profit share was only one of a list of possibilities and concerns set out by Mr Taylor in that letter. The others were whether there had been a "deemed distribution" from BCG Ltd to the MDPs; whether the awarding of Capital Interests to the MDPs was the creation of new capital interests and whether the MDPs "do in fact have an entitlement from the capital interests of BCG UK LLP".

477. The information available to the hypothetical officer in this case would therefore have alerted him to a number of different possibilities, one of which was a deferral of profits; it would not have alerted him to "an actual insufficiency" caused by the failure to apply the

MMRs. Instead, there was too much uncertainty for the hypothetical officer to have been in a position to issue an amendment to the Partnership Return on or before 31 January 2019.

478. The BCG Parties also submit that it is inconsistent with that conclusion that Mr Taylor was able to assess individual MDPs. However, as HMRC say, making those assessments only required HMRC to have information sufficient to recategorise the sums on the MDPs' returns from capital to income. More information would have been required for the hypothetical officer to amend the Partnership Return filed by the UK LLP.

Assessments on Mr Niddam and Mr Garside

479. Mr Niddam filed his 2016-17 SA return on 31 January 2018, and Mr Garside filed his on 26 December 2018. HMRC issued both assessments on 26 March 2021, after the closure of the enquiry window on 31 January 2019. However, these assessments fall away because of our finding that HMRC had validly amended the Partnership Return and because HMRC rightly accepted that enforcing these assessments in addition would amount to double taxation.

480. Had the MMRs not applied, these assessments would only have been valid if one of the two conditions at s 29(4) had been met. The FTT had found that the hypothetical officer condition was not satisfied, see [445], and HMRC did not appeal that finding. Thus, the assessments are only valid if (a) the UK LLP had been careless; (b) the UK LLP had acted on behalf of these MDPs and (c) that carelessness caused the loss of tax. We would have come to the same conclusions on those issues as we have done in relation to other years, and would thus have dismissed the appeals.

Conclusion: tax year 2016-17

481. For the reasons set out above, we uphold the validity of the assessment issued to the UK LLP on the basis that:

(1) UK LLP was careless, and that the carelessness caused the loss of tax; and

(2) the hypothetical officer test was met.

OVERALL CONCLUSION

482. We therefore uphold the FTT's decision in part. There was no error of law in the following findings, some of which were *obiter*:

(1) The Capital Interests were not interests in the capital of the UK LLP for any of the relevant years.

(2) The payments received by the MDPs were taxable as miscellaneous income for years in which the MMRs did not apply.

(3) If, contrary to the above findings, the payments received by the MDPs were capital receipts, they were within the sale of occupation income provisions.

(4) The UK LLP had been careless in relation to the introduction of the Capital Interests in 2011 and their reintroduction in 2014.

(5) The UK LLP's carelessness caused the loss of tax in 2015-16 and 2016-17 if the MMRs did apply to the UK LLP.

(6) The hypothetical officer test was not met in relation to the UK LLP's Partnership Return for 2016-17.

483. We set aside the following findings of the FTT:

(1) That the MMRs did not apply. For the reasons given under Issue 2, we have found that they did apply.

(2) That the UK LLP was not acting "on behalf of" Mr Krinks in relation to the filing of his 2012-13 return or on behalf of Mr Nascimento in relation to the filing of his 2013-14 return. We have found that it was so acting, and that the UK LLP's carelessness caused the loss of tax in relation to both Mr Krinks and Mr Nascimento.

484. Section 12 of the Tribunals, Courts and Enforcement Act 2007 allows us either to remit the case to the FTT with directions for a rehearing, or to re-make the FTT Decision.

485. We decided it was in the interests of justice to take the latter course. We are able to do so on the basis of the FTT's findings of fact and our analysis of the legal provisions. Remaking the FTT Decision also avoids the delay and the additional costs which would be incurred were the case to be remitted, and it makes proportionate use of the resources of the tribunal system.

486. In summary therefore the position is as follows:

(1) For the years 2012-13 and 2013-14, the payments received by the MDPs on "sale" of their Capital Interests were taxable as miscellaneous income.

(2) The MMRs did apply, so for 2014-15 through to 2016-17, the UK LLP and the MDPs are taxable under those provisions, including:

(a) in 2015-16, when HMRC amended the Partnership Return after the ordinary time limit, because the UK LLP was careless and that carelessness caused the loss of tax; and

(b) in 2016-17, when HMRC amended the Partnership Return outside the "enquiry window", both because the UK LLP was careless and that carelessness caused the loss of tax and because the hypothetical officer test was met.

(3) Mr Krinks is taxable on the payments received for the "sale" of his Capital Interest in 2012-13 despite the assessment having been made after the ordinary time limit.

(4) Mr Nascimento is similarly taxable on the payments received for the "sale" of his Capital Interests in 2013-14, despite the assessment having been made after the ordinary time limit.

487. Any application for costs in relation to this appeal must be made in writing within one month after the date of release of this decision and be accompanied by a schedule of costs claimed with the application, as required by Rule 10(5) and (6) of the Tribunal Procedure (Upper Tribunal) Rules 2008.

THE HONOURABLE MR JUSTICE THOMPSELL

JUDGE ANNE REDSTON

Released on: 20 January 2026