



Aspects of Partnership Taxation



Aspects of Partnership Taxation

- Fixed-share partners
- Partnership enquiries
- Mixed-member partnerships
- Personal expenses of partners

Partner or employee?

Difference between partnerships and LLPs

Entrenched HMRC view that LLP members are not employees

- In fact, Tiffin v Aldridge says otherwise!

Perceived NIC abuse at both ends of spectrum

Any member is treated as an employee unless one of three conditions is breached

- PAYE and NIC due
- Remuneration deductible in computing partnership profit

Special rules for LLP members

Deemed employee unless at least one of three conditions met, based on

- Share of profit (Condition A)
- Being a boss (Condition B)
- Having capital at risk (Condition C)

LLP disguised employees

Condition B

- Do you have significant influence over the affairs of the partnership?
 - Probably yes in many small partnerships
 - In large partnerships, no unless you're on the management board etc
 - Significant influence over a limited area of the partnership business doesn't count

LLP disguised employees

Condition A

- Is it reasonable to expect that at least 80% of your remuneration in respect of your performance of services for the LLP for a “relevant period” will be “disguised salary”, i.e. is
 - Fixed or
 - Variable without reference to the overall profits or losses of the LLP or
 - Is not in practice affected by the overall profits
- If your profit share isn't in respect of services (e.g. gardening leave)
- “Relevant period” starts when you join the LLP (or 6 April 2014) and ends (usually) when the remuneration arrangements are changed
 - NB an alteration in the level of profits doesn't close a relevant period
- Example
 - Partner A has fixed salary £50,000 plus 5% of profit
 - Profit is expected to exceed £250,000 indefinitely
 - Expectation therefore £50,000 fixed plus £12,500+ variable. OK
 - Profits are actually £200,000 ☹️ so £50,000 + £10,000. But still OK

LLP disguised employees

- Example – Condition A
 - Project expected to last four years
 - A receives £50,000 pa plus 25% of profit
 - Years 1, 2, 3, minimal profits expected
 - Year 4 profit expected to be £400,000
 - Total expected remuneration in RP £300,000
 - Fixed element = £200,000
 - Variable by LLP profit = £100,000 = 1/3 total

LLP disguised employees

Condition C

Member's partnership capital as at 6 April is less than 25% of the amount reasonably expected to be "disguised salary" for the year

- Pro rata for short periods
- Capital = long term finance, excluding amounts which can be drawn out while remaining a member
- If circumstances change the Condition C test is re-considered

2 months grace for putting in capital after joining

LLP disguised employees

If you're a member, anything you do to avoid the impact of the rules doesn't work

Being a disguised employee via your company doesn't work

What about the "Gig Economy" cases?

Different rules for ordinary partnerships

Compliance points

Notice to file

- Most are invalid!
- 12AA(2) – notice to “the partners” requiring “such person as is identified in accordance with rules given with the notice”
- 12AA(3) – notice to “any partner”
- A return of partnership profits is made by “a person” (and not by a partnership)

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Tax Reference 32760 43464

Date 06 APRIL 2017
Issued by
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36900

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Make sure you complete your online tax return as early as possible

Tax year 6 April 2016 to 5 April 2017

Our records show that you need to send us a Self Assessment tax return to tell us about your income from 6 April 2016 to 5 April 2017. We will not be sending you a paper tax return so please file your tax return online.

By law, you must send us your tax return and any information we ask for on the return - even if you don't owe any tax or have already paid all the tax you owe.

If your circumstances have changed and you think you don't need to complete a 2016 to 2017 tax return, go to www.gov.uk/check-if-you-need-a-tax-return

You don't need to do anything further if:

- you've already sent us your tax return for the 2016 to 2017 tax year
- you've previously contacted us and we've told you that you don't need to send a tax return for the 2016 to 2017 tax year

Sending us your tax return online

To log in or sign up to send your tax return online, go to

Deadlines for sending your tax return

You must make sure we receive your tax return by:

- **31 October 2017** if you use **paper** (or 3 months after the date of this letter if that's later)
- **31 January 2018** if you file **online** (or 3 months after the date of this letter if that's later)
- **30 December 2017** if you file **online**, owe less than £3,000 tax for the 2016 to 2017 tax year and want us to collect it through your pay or pension in the 2018 to 2019 tax year.

Penalties for filing late

You'll get an automatic £100 penalty if we don't receive your return by:

- **31 October 2017** if you use paper

Penalty for failure to notify

TMA 1970 s7: “Any person who is chargeable to Income Tax or CGT...”

Time limit for filing

Where there is a company partner s12AA(5) applies
9 months (paper); 12 months (electronic) from end of
“relevant period”

“RP” = “the period in respect of which the return is
required”

s12AA(8) – “a notice may require different information,
accounts and statements for different periods...”

HMRC say “RP” = trading accounting period

So (at least for y/e later than 31 January) extended filing
date applies

Unusual partners

Nominees

Partnerships as partners

Enquiries

s12AC notice of enquiry to “representative partner”

Flaxmode – some flexibility allowed

s12AC(6) – deemed enquiry into partner returns made or subsequently made

HMRC practice but no legal obligation to tell other partners

s9A(3) – a (personal) return which has been the subject of one notice of enquiry may not be the subject of another...

What does the “deemed enquiry” notice cover?

Reid & Emblin [2018] UKFTT 236

Enquiries

Closure notice

- Who can appeal?
 - Representative partner
 - Any other partner (Gibbs, Phillips)

Consequential notice amending personal returns (and closing deemed enquiry?)

- No appeal
- No postponement even if closure notice appealed!
- So normally not issued until closure notice final

Penalties

Late filing and errors

- Partners are individually liable (not just the RP)
- But only the RP has the right of appeal!
 - Gorman, Dyson on previous legislation
 - FA2009 sch55 and FA2007 sch24 are explicit

Finance Act 2018

Disputes on partnership returns

Background - Morgan, Self, King

Changes

- Partnership return conclusive as to amount of partner's profit share
- Disputes referred to Tribunal
- Re-opens enquiry window as to matters relating to the dispute

Issues on disputes

- No referral if dispute is in substance about amount of partnership profit or loss
- Would seem to cover questions as to whether there was a partnership at all
- All partners and HMRC get notice of referral
- HMRC's status as third party?
- Only one referral possible (unless subsequent taxpayer amendment)
- Further appeal to UT?

Partners' "personal" expenses

"Personal" not personal

HMRC practice at BIM82075 – "adjustments are made before apportionment of the net profit between the partners"

Is it consistent with ITTOIA s25?

Condoc and draft legislation – taxable profits to be allocated in same ratio as accounting profits - not in FA 2018

Distinguish from expenses not incurred wholly and exclusively for purposes of partnership trade

Corporate partnerships

Companies as

- Partners
- LLP Members
- Partners in a Limited Partnership

Need for multiple computations

Tax deductible from interest paid unless to

- UK Co
- NR Co taxable on income as PE profits
- Local authority
- Charity
- Registered pension scheme
- Partnership of the above

Time-apportionment of partnership profits to CT APs

Companies House filing requirements for “qualifying partnerships”

Money debts of a partnership

Mixed Member Partnerships

The background

- Innocuous use of corporate members
- More aggressive use

The response in 2013

- A is an individual member
- B is a non-individual (usually corporate) member
- Condition X or Condition Y (but they may overlap)

Mixed member rules

Condition X

- Reasonable to suppose
- “Deferred profit” of A is included in B share
 - “Any remuneration or benefits the provision of which to A has been deferred”
 - Including just and reasonable share of a global amount
 - Even if subject to conditions
 - Even if A may never get it!
- Tax saved
- No motive test
- No requirement that A should have an interest in CM
- No adjustment if the “deferred profit” is never paid to A

Mixed member rules

Condition Y

- B's profit share exceeds "appropriate notional profit"
 - Return on capital + consideration for services
 - Interest return, not equity return
 - Ignore services involving A or other partners
- A has "power to enjoy" CM's profit
 - Think Transfer of Asset abroad rules
- "Reasonable to suppose" that
 - At least part of CM's profit share is attributable to A's power to enjoy it
 - A's profit share and the tax bill are lower than they otherwise would be
- No motive test

Mixed member rules

In either case

- Re-allocate from B to A on a just and reasonable basis

Historic partnership losses of B may no longer be available

- HMRC are obdurate

It gets worse

S850D

- A is not a partner but personally performs services for the firm
- B has a profit share
- Reasonable to suppose that A would have been a partner but for s850C
- Condition X or Y is met
- Then treat A as a partner and apply s850C

Would A have been a partner but for s850C?

Yes, if A is an “indirect partner”

What if

- Resigned following the change of legislation?
- Resigned in anticipation of the change?
- Has always been only a CM?
- Joins a partnership of CMs?
- Starts a new all-CM partnership?

Avoiding double tax...or not

Applies where

- Agreement in place in relation to excess part of CM's profit share
- As a result of agreement, CM makes a payment out of the excess
- Not made under tax advantage arrangements

Then payment is not

- Treated as income of recipient
- Regarded as distribution
- Taken into account in computing income or losses etc of CM

But...

- "As a result of the agreement" – what if payment made first?
- What if profits not available to be distributed – pension contribution?
- Single payment in excess of excess payment? – HMRC practice
- Indirect payments made via parent
- Profits already distributed to (e.g.) spouse