

Salaried members of LLPs

Finance Act 2014 introduced a collection of anti-avoidance measures targeted at the taxation of partnerships. These measures covered:

- the tax treatment of salaried members of LLPs;
- 'mixed member' partnerships (those with both individual and company members);
- alternative investment fund managers operating through partnership structures;
- anti-avoidance rules dealing with the disposal of assets or income streams through partnerships.

Overview

The 'salaried members' rules affect individual members of LLPs who work for the LLP on terms that are equivalent to employment. They do not affect partnerships other than LLPs.

Ordinarily, a member of an LLP is treated as being a self-employed partner, rather than an employee of the LLP, for the purposes of income tax and national insurance contributions (NIC). Rather than have tax deducted at source through the PAYE system, the individual is liable to income tax through their self-assessment tax return on their share of the LLP's profits. Self-employed status means that the LLP is not liable to pay any employer's NIC (currently at a rate of 13.8%) and the individual is liable to the marginally lower rates of Class 2 (currently, although due to be abolished in April 2018) and Class 4 NIC, rather than Class 1 NIC.

However, if each of the 'salaried members' conditions are met, the member will be treated as an employee of the LLP for income tax and NIC purposes. In such cases, PAYE must be operated and a higher overall amount of tax is likely to be due. Tax and NIC on benefits provided may also be due. The deemed employment status applies for tax purposes only and does not apply for the purposes of general employment law.

The three conditions

The rules apply to any members of an LLP where all of the following three conditions are met:

Condition A

Condition A is met if it is reasonable to expect that at least 80% of the total amount payable by the LLP in respect of the performance of services will be 'disguised salary'.

'Disguised salary' includes amounts which are:

- fixed;
- variable, but unaffected by the overall profits or losses of the LLP; or
- amounts which are not, in practice, affected by the overall profits or losses of the LLP.

Condition B

Condition B is met where the mutual rights and duties subsisting between the members, and between the LLP itself and its members, do not give the member in question significant influence over the affairs of the LLP.

HMRC guidance indicates that senior members of a firm who may have little interest in day-to-day management may still have roles and rights within the LLP which mean that they can be considered to exert significant influence over the business as a whole. However, merely being able to vote or express a view on major decisions would not amount to 'significant influence'.

Membership of a management committee which has influence over the affairs of the LLP as a whole would normally indicate 'significant influence' unless its responsibility was largely administrative.

Condition C

Condition C is met where a member's capital contributed to the LLP is less than 25% of the disguised salary which it is reasonable to expect will be payable to the member in the tax year concerned.

The member's contribution to the LLP includes amounts contributed as capital, less any of the following:

- amounts previously withdrawn or received back;
- amounts that the member is entitled to withdraw or receive back; or
- amounts that may be reimbursed to the member by another person.

For these purposes, capital contributed includes only long-term contributions to the firm in line with the LLP agreement and does not include amounts in the member's current account.

Where an individual becomes a member with a firm commitment to contribute capital, two months are allowed to put the contribution in place.

Anti-avoidance

The legislation contains anti-avoidance provisions under which arrangements with a main purpose of circumventing the salaried member rules will be disregarded.

HMRC guidance refers in particular to the use of non-recourse or circular loans to finance capital contributions.

For further guidance on the above and partnership taxation generally, please contact your usual Moore Stephens adviser.

For further advice please speak to your usual contact at Moore Stephens.

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