HMRC guidance on the salaried members rules: CIOT comments

Personal tax OMB

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The CIOT has written to HMRC outlining concerns about the application and fairness of their updated guidance on the salaried limited liability partnership members rules.

The 2014 salaried members rules (‘the rules’) remove the self-employment presumption of members whom HMRC believe are effectively employees. In February 2024, they updated some of their guidance.

The rules, introduced through the Finance Act 2014 and now contained within Income Tax (Trading and Other Income) Act 2005 ss 863A-G, impose three conditions upon members of limited liability partnerships (LLPs) and if all are met, the member is treated as an employee for income tax purposes. The conditions concern:

- Condition A (disguised salary);
- Condition B (significant influence); and

- Condition C (capital contribution).

A targeted anti-avoidance rule (TAAR) is also embedded within s 863G, which disregards those arrangements where the main purpose is to ensure a member is not deemed an employee under the rules.

Of particular concern is HMRC’s approach to Condition C. HMRC’s February 2024 updates to guidance seem to suggest that instances of a member contributing their own capital and accepting the corresponding business and personal risks, might still render themselves susceptible to the TAAR. In one example within the guidance, a member tops up their capital contribution having already fallen foul of Condition C four years previously. HMRC’s updated guidance seems to suggest that this latest contribution will fall foul of the TAAR as the (presumed) intention behind it was to extricate themselves from Condition C. Elsewhere in the guidance, HMRC state that a genuine contribution made by the individual will not trigger the TAAR, but that this is subject to its main purpose not being to avoid the rules.

The CIOT understands there can be a fine line between genuine commercial arrangements and those deliberately made to avoid the salaried members rule. However, while the TAAR was supposed to be reserved for those few ‘abusive’ arrangements, some genuine capital contributions now seem susceptible to finding themselves in the same category.

In addition, this approach by HMRC will be applied to those contributions made in good faith many years beforehand and which followed prevailing guidance; to subject members to enquiries on historic transactions with this new approach is arguably unfair.

The CIOT believes that HMRC’s application of the TAAR goes beyond the original intention behind the rules and that it should be restricted to those cases which are clearly abusive. When a member contributes to an LLP, they are providing a valuable source of working capital. That member also takes on a corresponding share of risks and personal liabilities, especially as most have to take out a bank loan to fund their contribution. A genuine, self-employed LLP member would not undertake this lightly.

In our letter, we therefore urged HMRC to reverse the February 2024 guidance updates and cease compliance activities based on this new practice where the member complied with prevailing advice.

The full CIOT letter to HMRC can be found here: www.tax.org.uk/ref1364

Chris Thorpe *cthorpe@ciot.org.uk*