[2020] UKFTT 0058 (TC)

TC07554

Mixed partnership rules – basis for re-allocation – whether profits earned by company or individual partner-no evidence of separate role of company – time apportionment rejected - appeal dismissed

FIRST-TIER TRIBUNAL
TAX CHAMBER

Appeal number: TC/2017/06783
TC/2017/07572

BETWEEN

NICHOLAS WALEWSKI **Appellant**

-and-

THE COMMISSIONERS FOR HER MAJESTY'S REVENUE AND CUSTOMS **Respondents**

TRIBUNAL: JUDGE Rachel Short
Mr Mohammed Farooq

Sitting in public at Taylor House, 88 Rosebery Avenue on 2 to 6 December 2019

Mr Patrick Soares and Mr Imran Afzal of Field Court Tax Chambers for the Appellant

Ms Aparna Nathan QC, counsel, instructed by the General Counsel and Solicitor to HM Revenue and Customs for the Respondents

DECISION

INTRODUCTION

1. The Appellant, Mr Walewski is appealing against two assessments made by HMRC under the "mixed partnership" rules at s 850C – 850E Income Tax (Trading and Other Income) Act 2005 ("ITTOIA 2005") arising from his interest in two UK entities in which he was a partner, Alken Asset Management LLP ("AAM") and Alken Finance LLP ("AF") for the 2014-15 tax year.

2. Mr Walewski appealed against

   (1) HMRC's decision in their closure notice of 31 March 2017 to re-allocate £18,088,195 of profits from AAM to him under s 850C ITTOIA 2005 giving rise to total profits chargeable to income tax of £18,103,962; and

   (2) HMRC's decision in their closure notice of 31 March 2017 to re-allocate £1,372,510 of profit from AF to him under s 850C ITTOIA 2005 giving rise to total profits chargeable to income tax of £1,434,315.

3. HMRC have assessed him to income tax under these rules on the basis that profits which were allocated to a UK company of which Mr Walewski was a director, Walewski Limited ("W Ltd") should instead be re-allocated to Mr Walewski as a partner in AAM and AF.

4. Mr Walewski argues that the additional profits, amounting to £19,460,705 should not be re-allocated because they have been earned by W Ltd and not by him in his capacity as a partner in AAM or AF. The majority of these profits were allocated to W Ltd from AAM. The remaining, much smaller amount (£1,372,510) was allocated to W Ltd from AF.

5. HMRC say that the profits were not earned by W Ltd but were allocated to W Ltd because of Mr Walewski's ability to enjoy those profits via an offshore trust fund to which W Ltd paid its profits and of which Mr Walewski's children were beneficiaries.

6. The burden of proof is on Mr Walewski to demonstrate, on the balance of probabilities, that W Ltd earned the profits which were allocated to it and that therefore those profits should not be re-allocated to him.

BACKGROUND FACTS

7. Mr Walewski is a successful investment adviser in London. Having managed funds for other people, in 2005 he set up his own equity fund, the Alken Fund, a Luxembourg SICAV (an open-ended vehicle).

8. That fund was managed by AAM in the UK which was set up on 5 July 2005. Trade execution was carried out by AF which was set up on 19 November 2010. AAM was a member of AF until 5 December 2011.

9. For the relevant years, AAM's total profits were £19,040,069. AF's total profits were £3,165,813.

10. Mr Walewski was a partner in AM and AF and also set up a company, W Ltd, in June 2006 which was a partner of both AAM and AF. Mr Walewski was W Ltd's only director. Mr Walewski became an employee of W Ltd on 1 April 2007. W Ltd had no other employees or directors.

11. AAM was a partner in AF until 5 July 2011 and was its managing member. AF's only other member was Mr Walewski. W Ltd took over AM's partnership interest in AF on 5 July 2011.

12. AAM and AF had other employees as well as Mr Walewski and clients other than the Alken Fund, but that fund generated more than 80% of AAM's income for the 2014-15 tax year and Mr Walewski was the only member of AAM's management committee.

13. The "mixed partnership" rules are anti-avoidance rules which were introduced in April 2014 having effect for tax years starting from 6 April 2014. They apply to LLPs such as AAM and AF if the partnership includes both individual and non-individual members.

14. The shares in W Ltd are held by an offshore company Molinos Capital Limited in the British Virgin Islands. Shares in that company are held by a trust, the Kleber Trust, in which Mr Walewski's children are named beneficiaries.

15. During the relevant tax year 2014-15, Mr Walewski's role and involvement in AAM, AF and W Ltd changed:

(1) Mr Walewski retired as a partner from AAM on 31 July 2014.

(2) Mr Walewski's capital contribution to AAM was taken over by W Ltd effective from 1 August 2014, although no actual repayment was made to Mr Walewski until 24 November 2014.

(3) Mr Walewski became an employee of AAM for the two months from 1 August to 30 September 2014.

(4) Mr Walewski resigned as an employee of W Ltd at the end of September 2014. Mr Walewski remained as a director of W Ltd.

(5) On 29 November 2014 the business of AAM and AAF were incorporated and Mr Walewski became a director of both of those entities.

16. The profit allocations with which we are concerned were made on 24 March 2015 for AAM and 28 October 2015 for AF and represented profits for the 2014-15 tax year during which (i) W Ltd was a partner in AAM and AF (until their incorporation in November 2014) and (ii) Mr Walewski was also a partner, in AAM (from April 2014 until July 2014), and in AF (from April 2014 until November 2014).

THE LAW

17. The detailed legislation setting out the "mixed partnership rules" is set out as an appendix to this decision. The main focus of the parties' arguments was s 850C ITTOIA and in particular s 850C(3)(a) and (b) – "Condition Y", in this instance "B" being W Ltd and "A" being Mr Walewski;

> "Condition Y is that –
>
> (a) B's profit share exceeds the appropriate notional profits (see subsections (10) to (17))
>
> (b) A has 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"

18. S 850C sets out a number of conditions which need to be fulfilled in order for the "mixed partnership" rules to apply to allow HMRC to re-allocate profits other than as they have been allocated under a partnership agreement. The parties accepted that all of those

conditions had been fulfilled other than the conditions at s 850C(3)(a) and (c)(i); HMRC say that both these conditions have been fulfilled, the Appellant says that the condition at s 850C(3)(i) has not been met.

19. The definition of "appropriate notional profits" in s 850C(3)(a) is made up of two elements (defined in s 850C(10)):

(1) "The appropriate notional return on capital" (set out in s 850C(11)) and

(2) "The appropriate notional consideration for services" (set out in s 850C(15))

20. We were also referred to these case authorities:

(1) *Hamilton & Kinneil (Archerfield)Ltd & ors v HMRC* [2015] UKUT 130 TCC

(2) *Fidex Limited v HMRC* [2013] *UKFTT 212*

(3) *Tiffin v Lester Aldridge* LLP [2012] EWCA Civ 35

(4) *Bates van Winkelhof v Clyde & Co LLP and another (Public Concern at Work intervening)* [2014] UKSC 32

(5) *Murray Group: RFC 2012 Plc (in liquidation)(formerly the Rangers Football Club plc) v Advocate General for Scotland* [2017] UKSC 45

(6) *In re Recovery of Medical Costs for Asbestos Diseases (Wales) Bill* [2015] UKSC3

21. We were also referred to an excerpt from the Hansard debates on the Finance (No 2) Bill 13 May 2014 discussing the introduction of the mixed partnership rules, including this statement*:*

> "Various structures have been used to allocate profits to a low-tax entity, such as a company, while losses were allocated to individual partners, who could make more tax-efficient use of the losses. The new measures aim to prevent these types of arrangements*"*

EVIDENCE

Oral evidence

22. We heard evidence and saw witness statements from Mr Walewski himself and from five other witnesses;

(1) Mr Vivas and Mr Canovas who advised clients to invest in the Alken Fund and dealt with Mr Walewski,

(2) Mr Tsatsaris who was W Ltd's head of operations and chief operating officer,

(3) Mr Everett who was an accountant providing tax compliance services to AAM, AF and W Ltd,

(4) Mr Woodgate who was an accountant providing services to W Ltd, AAM and AF.

23. Each of these witnesses was cross-examined by Ms Nathan.

24. We also saw a witness statement from Mr Hagerman. Mr Hagerman did not appear before the Tribunal.

Mr Walewski's witness evidence

Mr Walewski's role

Mr Walewski told us that:

25. His role at Alken was to manage the Alken Fund and other clients' investment decisions. For larger clients this included personally attending investor meetings and presentations. He also met with brokers, discussed research and made strategic decisions for AAM and AF.

26. AAM had a management committee of which he was the sole member. Mr Walewski said that decisions he made as a member of this committee were made in his capacity as director of W Ltd.

27. He held various FCA authorisations to carry out CFA functions, which allowed him to carry out these regulated activities through any entity including W Ltd. W Ltd itself was authorised as a CF4, allowing it to be a partner of AAM.

The entities

In respect of W Ltd Mr Walewski said:

28. W Ltd represented his personal interests, which he wanted to segregate from the two LLPs in which others were also involved. It also provided a reserve of capital which provided assurance to clients of the LLPs.

29. W Ltd paid "prudent dividends" to its offshore holding company each year.

30. W Ltd "was to manage his own assets, his own interests and represented his personal involvement in the company", but Mr Walewski struggled to explain why W Ltd was required as well as the LLPs or to differentiate his role for W Ltd from his role for the LLPs. He did stress that the main advantage of W Ltd was its ability to accumulate capital, which the LLPs could not do.

31. Although W Ltd was registered at Companies' House as a holding company, its activities were in fact wider than this.

32. Mr Walewski was the only employee of W Ltd. He had a contractual right to a salary of £200,000 per annum and a bonus. He could not recall getting a bonus from W Ltd. W Ltd held an investment in the Alken Fund.

33. Two other investors had briefly been involved with W Ltd (Mr Badel and Mr Festa), but they had been removed after a short time when it was realised that their involvement made things complicated.

34. The LLPs, AAM and AF were useful because they provided a very flexible way of managing the business, allowing for the participation of others.

35. However, when he dealt with clients, he always considered himself to be acting through W Ltd. Larger institutional clients would have done due diligence on the Alken structure and would have known that he was acting through W Ltd. Mr Walewski accepted that there were no documents to demonstrate that clients were dealing with W Ltd. He did not keep timesheets or other records to demonstrate which of the Alken entities he was working for at any one time.

36. In respect of the multiple hats which he wore for the Alken group Mr Walewski said of clients: "They don't care if I am employed or not, they just want my involvement" but of his

role as employee of W Ltd "I was acting always as a director of W Ltd, sometimes as an employee of W Ltd, especially for strategic decisions. But, also, I was acting as a partner of the various LLPs"

37. Mr Walewski also accepted that (i) his activities for AAM were the same before and after W Ltd had been set up and his W Ltd employment contract had been signed and (ii) it was not possible for him to be working full time for both AAM and W Ltd.

38. AF was intended to be a "junior partner" in the structure. More junior employees were made members of AF as a reward for services. AF's employees were mainly administrative. More senior employees were rewarded with a partnership in AAM.

39. AF, AAM and W Ltd all operated from the same office space at the relevant time.

40. As for the PWC advice given in July 2014 about the mixed partnership rules, Mr Walewski said he did not fully understand the details but just followed the advice given.

Mr Vivas witness evidence

41. Mr Vivas is a securities broker, managing accounts on behalf of third parties. In that role he recommended the Alken Fund to his clients and came into contact with Mr Walewski.

42. Mr Vivas stressed Mr Walewski's importance to the Alken Fund and knew that Mr Walewski was managing the fund through W Ltd. Mr Walewski made all the decisions about the Alken Fund. He accepted decisions did not have to be made through W Ltd, although it was important that Mr Walewski was involved, saying:

> "I wanted to ensure that Mr Walewski was effectively driving the investments of the Alken Fund, and my understanding at the time was that Mr Walewski was employed by Walewski Limited, and that the investment decisions were driven by Mr Walewski as a director of Walewski Limited." and
>
> "It would be the same as if you are in a restaurant and suddenly the chef left. I think, you know, maybe you think the second person will be as good as Nicolas, [Mr Walewski] but this is a very -- today it's still a very personalised fund."

Mr Canovas witness evidence

43. Mr Canovas works as a securities broker in Luxembourg, including with the Alken Fund.

44. Mr Canovas told us that he had known Mr Walewski when he was managing a previous fund and that his job was to introduce good fund managers to his clients. Like Mr Vivas, Mr Canovas accepted that while the details of the structure including W Ltd were known to him, and that he had done due diligence on the Alken Fund structure, for clients the only important fact was that Mr Walewski was involved.

Mr Tsatsaris witness evidence

AAM's business

45. Mr Tsatsaris said that he was involved with AAM and AF but not W Ltd, which was Mr Walewski's entity. He also said that he did not provide tax advice to any of the entities or Mr Walewski.

46. To explain AAM's business Mr Tsatsaris said:

> "What we do is we manage accounts for clients. Those accounts can be of different types. Either it's for one individual, either it's for a company, or it can be a regulated mature fund. Alken Asset Management manages accounts, and managed accounts, for all those types of clients. And one of the accounts we were managing was a fund called the "Alken Fund", and within the Alken Fund there were several strategies".

47. Mr Tsatsaris explained that a large percentage of AAM's turnover came from the Alken Fund in Luxembourg for which AAM acted as fund manager, appointed through a Luxembourg based management company. Clients signed an agreement with AAM (not W Ltd or AF).

48. He also explained how the three entities; W Ltd, AAM and AF were used to incentivise employees; junior employees could become members of AF, more senior employees became members of AAM. Mr Walewski was given an employment contract with AAM after he resigned as a partner to give Mr Walewski a link with AAM which was important for AAM's other employees.

49. Mr Tsatsaris gave some details about W Ltd's right to share in the profits of AAM; while the partnership deed conferred the right on W Ltd to obtain 99% of AAM's profits each year, there was no obligation for AAM to decide to allocate the full 99% in any given year. Clause 9.3 of the AAM LLP Agreement gave the management committee the discretion to decide how to allocate profits each year.

50. Mr Tsatsaris had learned about the "mixed partnership rules" after attending a PWC event. He and Mr Walewski had a follow up meeting with PWC. He understood that the rules would not apply if AAM was incorporated. He had also understood that since neither Mr Walewski nor his children were beneficiaries of the Kleber Trust, the mixed partnership rules should not apply to Mr Walewski.

Mr Walewski's role

51. Mr Tsatsaris described Mr Walewski's roles for the Alken group companies as "very interlinked". Mr Walewski provided oversight and management and provided services to clients as a partner of AAM. Mr Walewski did provide his services to AAM as well as to W Ltd but the work which he did for AAM could not be separated from his work for W Ltd. If Mr Walewski had acted alone, he would have acted through W Ltd; AAM allowed him to work with others.

52. Mt Tsatsaris said on this point:

> "All these companies work for the exact same purpose of delivering good products to our clients. So, whether Nicolas Walewski is doing it through Walewski Limited or through another entity, for me, it is irrelevant and I don't see any restriction in that clause which prevents Nicolas Walewski to provide services for Walewski Limited."

53. Mr Tsatsaris also accepted that clients were not concerned about which legal entity they dealt with, but only that the right people, including Mr Walewski were involved. Larger institutional clients would have done due diligence and would have known about W Ltd. Clients were not used to dealing with partnerships and W Ltd provided comfort to clients by providing a significant balance sheet. Mr Tsatsaris said:

> "At the end of the day, for the clients, they didn't care whether they were operating through Alken Finance, Walewski Limited or Alken Asset Management. The only thing they cared about is to make sure that the team of analysts were showing, the team

of fund managers, the team of traders, the team of risk managers, the team of finance, are really involved in the accounts for the clients."

Regulatory capital AAM and AF

54. Mr Tsatsaris confirmed that £10 million of drawings which remained in AAM during the relevant period was both unallocated and undrawn, which while not formally adopted as capital, was treated as regulatory capital by the FCA. It was treated as prudential capital by the FCA to show that AAM (or AF) had sufficient buffer against operational and market risk.

55. From a client perspective, they were also given comfort by the fact that profits were retained by W Ltd. This was especially true of European clients who were not used to dealing with partnerships and who could go to Companies' House and examine W Ltd's strong balance sheet.

56. Mr Tsatsaris confirmed that the position was the same for the £1.2 million of what he described as "regulatory capital" which had been left in AF as undrawn and unallocated profits.

57. W Ltd had paid tax on both the £10 million of unallocated drawings in AAM and the £1.2 million of unallocated drawings in AF.

Mr Everett witness evidence

58. Mr Everett is a tax accountant who acted for AAM, AF and W Ltd providing tax compliance but not tax advice services. He explained that while he was aware of the "mixed partnership rules" he had understood that no action needed to be taken by W Ltd because all of its arrangements were commercial, particularly because Mr Walewski was providing services to clients through W Ltd.

59. Mr Everett confirmed that W Ltd had paid tax on the "unallocated" profits which had been treated as capital in AAM (£10 million) and AF (£1.2 million).

Mr Woodgate witness evidence

60. Mr Woodgate is a chartered accountant who provided accounting compliance services to AAM, AF and W Ltd.

61. Mr Woodgate confirmed the mechanics of how £399,600 of W Ltd's drawings from AAM had been converted into capital of AF when W Ltd took over AAM's partnership interest in AF in December 2011 and referred us to AAM's relevant financial statement (for the year ended March 2012) and drawings summaries to support this.

62. Mr Woodgate took us to the bank statements of AAM for November 2014 and March 2015 to show the payments of capital made to AAM by W Ltd (on 24 November 2014) and its repayment (on 26 March 2015) in accordance with the partnership minutes of 1 July 2014 in which W Ltd agreed to contribute capital to AAM to replace the capital of the outgoing members.

Mr Hagerman witness statement dated 5 April 2018

63. We were also provided with a witness statement from Mr Hagerman, who worked on behalf of another finance company which invested in the Alken Fund.

64. Mr Hagerman did not appear before the Tribunal and was not cross-examined.

65. His brief witness statement is similar in content to that of Mr Vivas and in light of this and the fact that Mr Hagerman was not cross-examined by HMRC, we have not placed any weight on his written statement.

Written evidence

Partnership Agreements

66. AAM original partnership agreement dated 5 July 2005 & re-stated 16 March 2010 by reference to resolutions of 7 July 2006, 16 August 2006 and 28 November 2006 including:

(a) Clause 4 –setting out a description AAM's business as an investment manager;

(b) Clause 9 – Explaining how allocations of profit are to be made each year at the discretion of the Managing Committee;

(c) Clause 17 - Management Committee – described as comprising representatives of the members but initially consisting of Mr Walewski.

(d) Schedule 3 setting out capital contributions and profit sharing proportions, allocating 99.9% of profits to W Ltd.

67. AF partnership agreement dated 19 November 2010 and re-stated 29 July 2011 including:

(a) Describing the business of the LLP as providing trade execution services;

(b) Clause 11 – Allocation of profits and losses – after costs and agreed drawings "such payments to Members as the Managing Member (AAM) may in its discretion allocate to Members";

(c) Clause 14 – Responsibilities of AAM as managing member. "responsibility for the day to day operation of the Business and the affairs of the LLP";

(d) Clause 16 – "When a Member is an Individual Member to devote his whole time and attention to the Business, or, with the approval of the Managing Member, to the business of any member of the Group" (AF and AAM);

(e) Schedule 1 showing profit share of members – AAM 99.9% Mr Walewski – 01%.

68. Agreement for services between AAM and AF of 29 July 2011.

69. Secondment Agreement between Alken AM Limited and AF 1 December 2014 setting out the names of employees assigned from AF to Alken AM Limited, not including any reference to Mr Walewski.

Client documents

70. ISDA Schedule entered into by the Alken Fund and Merrill Lynch International Bank Limited of 24 October 2013 including;

(1) Termination provision definitions – Additional Termination Event stated to include: "Key person. Nicholas Walewski ceases to direct the investment decisions in respect of Party B (Alken Fund) or be actively and regularly engaged in the day to day management of Party B or be employed by the Investment Manager (AAM)".

71. Investment Management Agreement between AAM and J P Morgan International Bank Limited of 16 August 2010 including:

(1) Clause 5.8 "The Investment Manager (AAM) shall immediately notify JPIMB in the event that any of the individuals listed in Schedule 5 hereof resign or their employment by the Investment Manager is otherwise terminated";

(2) Schedule 5 – Including Mr Walewski and no other named individuals.

72. Investment Management Agreement dated 25 May 2007 between Virmont, (the Luxembourg management company of the Alken Fund) and AAM, signed by Mr Walewski but having no "key man" clause referring to him.

W Ltd company and financial documents

73. W Ltd Memorandum and Articles of Association - 19 June 2016 describing W Ltd's business as: "To carry on business as a general commercial company"

74. W Ltd Company accounts for the year ended 31 March 2015

75. W Ltd Group Strategic Report & financial statements for years ended 31 March 2014 & 31 March 2015 showing

(1) dividends paid for those periods amounting to £27,720,000 (2014) and £43,520,000 (2015)

(2) Payment of salary to Mr Walewski of £130,000 (2014)

76. W Ltd Corporation tax computation for the year ended 31 March 2015

Mr Walewski employment documents

77. *Employment contracts*

(1) Mr Walewski and AAM – 15 July 2014

(a) Clause 16.1.2 Time to be devoted to the business, saying:

"Work business hours of 9:00am to 6:30pm Monday to Friday, subject to a one hour meal break, together with such additional hours as are necessary for the proper performance of his duties [reference to Working Time Regulations.....]"

The employee should "Devote the whole of his working time, skill ability and attention to the business of the Company....."

"The employee's general duties will involve managing the investment strategies of the Company, and defining strategy at firm level"

(2) Contract between Mr Walewski and W Ltd – 1 April 2007

(a) Stating his salary as £200,000 and an entitlement to a bonus and stating:

"APPOINTMENT

The company hereby appoints the Employee and the Employee agrees to serve the company as a Director."

(3) Clause 4.2 setting out the employee's duties: "work business hours of 9am to 6pm Monday to Friday, subject to a one hour meal break, together with such additional hours as are necessary for the proper performance of his duties and [reference to the Working Time Directive] and the employee shall "devote the whole of is working time, skill, ability and attention to the business of the Company".

(4) Clause 4.4 "The Employee will be reporting to the Board".

78. *Mr Walewski resignation letters*

(1) W Ltd (as employee) 20 October 2014

(2) AAM (as member) 1 July 2014

(3) AAM Termination Form (LLTMO1) – 31 July 2014

79. *Payslips*

(1) AAM – 31 August and 30 September 2014, showing gross pay of £9,166,67 for each of those two months

(2) W Ltd – 25 April – 25 September 2014, showing gross pay of £310,833.34 for each of those months.

AAM company and financial documents:

80. Turnover figures – AAM for year ending 31 March 2015,

(1) listing all of AAM's clients including the Alken Fund, whose payments amounted to £20,896,432 out of a total income of 326,323,566 approximately 80% of AAM's total turnover for that year.

(2) Demonstrating that all but two invoices were issued to clients before the end of September 2014.

81. Financial statements of AAM for year ending March 2012

(1) Showing drawings and allocated profits including W Ltd's allocation of drawings of £399,600 which was contributed to AF.

82. AAM drawings summary as at March 2012, showing drawings of £399,600.00 on 5 December 2011 described as "Investment by W Ltd in AF"

83. Financial statements of AAM for year ending March 2015

(1) Showing payments made to W Ltd for consultancy services of £61,175.

84. AAM bank accounts

(1) Bank statement for November 2014 showing £429,999.000 being paid on 24 Nov 2014 from W Ltd to AAM

(2) Bank statement for period 2 March 2015 to 31 March 2015 showing transfer of £430,000 from AAM to W Ltd on 26 March 2015.

85. AAM financial statement for year ending 31 March 2012 showing allocated profits of £5,399,600.

86. Letter dated 5 December 2019 from Meyer Williams to the Tribunal setting out

(1) W Ltd's share of AAM's profits for the periods 2006-7 to 2014-15

(2) W Ltd's share of AF's profits for the periods 2011-12 to 2014-15

87. AAM Minutes of committee meeting 1 July 2014, recording resignation of Mr Walewski, Mr Badel, Mr Festa and Mrs Ortega with an effective date of 31 July 2014 and stating that

> "W Ltd will make a contribution in order to replace the outgoing members and maintain the same level of capital."

88. AAM Minutes of Management Committee 24 March 2014 allocating profits for the period to end of July 2014, totalling £14,362,824 of which £13,808,392 is allocated to W Ltd and £14,251 is allocated to Mr Walewski. All the other three members of AAM are allocated £142,501 each.

AF company and financial documents

89. Financial statements of AF for year ended March 2015.

90. AF turnover for year ending 31 March 2015 showing total turnover of £5.794,332 of which £2,753,946 arises from services provided to AAM.

91. Minutes of Members meeting of 28 October 2015 concerning distribution of income profits for the year ended 31 March 2014[1]. A total of £1,799,687 of distributable profit was declared with 1% going to all members in accordance with clause 11.2.3 of the partnership agreement and the remainder being allocated in proportion to each members' share, resulting in W Ltd receiving £1,368,967.91 (plus its 1% share - being £17,996.87).

Regulatory documents

92. FCA authorisations –

(1) W Ltd – 19 December 2014

(2) AAM– 14 November 2014

(3) FCA Register – print out showing FCA approved persons working for AAM

(4) FCA Register – print out showing FCA approved persons and controlled functions for W Ltd, naming W Ltd as a CF4 partner in AAM.

(5) Mr Walewski – undated – print out of current information on Mr Walewski's regulated activities, his "controlled functions".

Other

93. Business transfer agreement – AAM to AAM Ltd 29 November 2014, detailing the transfer of AAM's business and assets to AAM Ltd.

94. Schedule of capital contributions made to AAM and AF (provided by the Appellant at the Tribunal)

[1] This appears to be an error, the reference should be to 2015.

95. Management Committee Meeting minutes of Vauban Asset Management dated 16 August 2006 – concerning the transfer of Mr Walewski's interest in VAM to W Ltd and amended LLP Agreement. The minutes state:

> "The chairman reported that the purpose of the meeting was to consider and if thought fit to approve:
>
> Confirmation of the change of control of VAM following the receipt of the FSA's approval of change of control"
>
> and
>
> "There was produced to the Meeting the following documents for consideration;
>
> (i) The FSA approval letter for the transfer of (a) 99.90 per cent (%) of the interest of Nicholas Walewski to Walewski Limited and (b) the entire interest (0.00025 per cent (%)) in VAM of Clotilde Walewski to Nicolas Walewski.....
>
> (iii) a draft amended LLP agreement
>
> IT WAS RESOLVED THAT:
>
> After careful consideration of the tabled documents the following matters being in the best interest of VAM
>
> (I) VAM's change of control be and is hereby duly completed and the confirmation of the same be sent to FSA and .....notice be to be given to the FSA of Mr Walewski's cessation of being a controller"

96. Ordinary Written Resolution of Vauban Asset Management LLP dated 30th November 2006, stating:

> "I the undersigned, being a member of the partnership holding more than 50 per cent (50%) of the total interest in the partnership, hereby resolve as follows":
>
> and referring to the change of name of Vauban to AAM and the resignation of Mr Walewski's wife as a member. This resolution was signed by Mr Walewski.

97. PWC advice document to AAM –July 2014 "Mixed Member Partnership Options" including a description of W Ltd as "acting as a service company to AAM and remunerated at cost" and suggesting as a solution to the application of the mixed partnership rules as "Option 1" that all individuals become employees of AAM.

Kleber Trust documents

98. Declaration of Trust relating to the Kleber Trust – 20 December 2006

99. Letter excluding Mr Badel and Mr Festa as beneficiaries – 20 May 2016

100. Memorandum of wishes of the Kleber Trust - 22 December 2006 from Mr Walewski stating:

> "it is my overriding wish that the Trust Fund be used for the benefit of my children. I would therefore request that the Trustees and the Protector consider my wishes and in doing so hold the Trust Fund in the following manner: divide the Trust Fund equally between my children [list of his three children's names]".

101. Order of Supreme Court of Barbados in the High Court of Justice -18 April 2019 stating that Mr Walewski was not capable of benefitting from the Kleber Trust.

Other correspondence

102. Correspondence between the parties from 27 April 2016 to 14 August 2017 including:

(1) Letter from Meyer Williams to HMRC dated 27 July 2016 in response to HMRCs' letter of 25 June saying that " W Ltd was an early investor in the Alken business.....it provided support in terms of capital both for regulatory purposes and to demonstrate to investors in the funds managed by Alken that AAM had sufficient substance and to enable the business to maintain operations. Additionally it may have been required to contribute additional capital if the business required it to do so"

(2) Letter from HMRC to Meyer Williams dated 25 June 2016, pointing out that the only activity of W Ltd for the 2014-15 tax year was the paying and receiving of one transaction fee of £60,000.

THE PARTIES' ARGUMENTS

Mr Walewski's arguments - AAM

The interpretation of s 850C

103. The Appellant's interpretation of the conditions set out in this section is that they operate as a series of three discrete gateways. The only gateway on which Mr Walewski can rely is s 850C(3)(c)(i).

104. It is accepted that each of the conditions at s 850C(3)(a) and (b) are met. The only condition which is potentially not met is condition 850C(3)(c)(i).

105. In particular the Appellant accepts that

(1) he has "power to enjoy" profits allocated to W Ltd because of his children's interest in the Kleber Trust (s 850C(3)(b));

(2) any "notional consideration" attributable to services provided by Mr Walewski to AAM is nil, either because Mr Walewski did not provide services directly to AAM or because s 850C(17) applies to ignore the value of any services provided Mr Walewski to the partnership of which he is a partner, AAM;

(3) as a result, Mr Walewski's profit share does exceed the appropriate notional profit.

106. Of s 850C(3)(c)(i) Mr Walewski says:

(1) if the non-individual partner receives no more than an appropriate notional share of profits, no re-allocation of profits can be made;

(2) if a person is not a member of a partnership, profits cannot be re-allocated them;

(3) if a company contributes capital to a partnership, a reasonable return on that capital cannot be reallocated.

107. In respect of AAM, Mr Walewski says that s 850C(3)(c)(i) does not apply because W Ltd earned the profits which it received for the 2014-15 tax year. Even though the "appropriate notional profit" was nil, services were provided to W Ltd and those services had a value. They were earned as a result of the activities undertaken by Mr Walewski on behalf of W Ltd for the clients of AAM.

Services to the firm

108. In Mr Walewski's view this aspect of s 850C is not relevant. The exclusion for services provided to a firm of which Mr Walewski is a member would apply to both AAM and AF, but this element of s 850C only applies for the purpose of s 850C(3)(a) which is not the relevant "gateway" for Mr Walewski, who is relying on s 850C(3)(c)(i).

Attributable to Mr Walewski's power to enjoy

109. No part of the profits paid to W Ltd was "attributed to Mr Walewski's power to enjoy" because all of the profit allocated to W Ltd had been earned by Mr Walewski acting through W Ltd. The legislation is intended to catch diverted profits and in this case no profits have been diverted. As Mr Tsatsaris stressed: "It is totally obvious that Walewski Limited's profit share was proportionate to the contribution made by Mr Walewski as an employee and director of Walewski Limited."

110. The employment contract between W Ltd and Mr Walewski was "very strong". It set out clear and "all embracing" duties between Mr Walewski and W Ltd. Mr Walewski undertook extensive activities under that contract, as stated by him and Mr Vivas and Mr Canovas, described by Mr Walewski as:

> "involved in management, strategic decisions, making sure the business was thriving with the right partners in the LLP, having the right products and the right performance, so that investors were satisfied."

111. Mr Walewski's activities under that employment contract were what generated W Ltd's profits. That had to be respected, as did the fact that he was paid a monthly salary by W Ltd. The fact that clients were not concerned about which entity Mr Walewski was acting for does not mean that the legal structure including W Ltd should be ignored. Clients were only concerned that they dealt with him, and Mr Walewski was clear that he was providing his services on behalf of W Ltd.

112. The "key man" clauses in the ISDA and Investment Management Agreement were broadly drawn for the same reason; the capacity in which Mr Walewski was acting was irrelevant to clients, although in both cases the definitions were wide enough to cover Mr Walewski acting through W Ltd.

113. There was no tension between Mr Walewski's employment with W Ltd and his obligations for AF (and AAM), since AF's partnership agreement allowed for a member to be approved to work for other group undertakings, which was what Mr Walewski had done. Mr Walewski's role as managing member of AAM related to the management of the LLP, not the day to day investment decisions, which were taken by W Ltd.

114. There was no argument that Mr Walewski's employment contract with W Ltd was a sham or fraud. HMRC's suggestion that the employment contract was "artificial" ignored the fact that it was open to Mr Walewski to choose a structure for these arrangements; he had made a valid choice to enter into an employment contract with W Ltd. In fact that contract had existed since 2007. Mr Walewski would have acted through W Ltd even if AAM and AF had not existed.

115. W Ltd's activities were extensive and could be comprised in the definition of a "head office" referred to by HMRC, which was broad enough to encompass day to day management activities, in line with W Ltd's broadly drawn memorandum of association.

116. W Ltd earned the profits allocated to it, therefore none of those profits are attributable to Mr Walewski's "power to enjoy" under s 850C(3)(c)(i). There are therefore no excess profits to be re-allocated to Mr Walewski.

117. For the same reason s 850C(3)(c)(ii) does not apply; AAM's profits were not lower than they otherwise would have been, because those profits had been earned by W Ltd and were a proper profit share for the value given to AAM.

118. As the witness evidence made clear, W Ltd was important because it provided a strong balance sheet, gave comfort to clients and provided a corporate structure which European clients could understand. The reason for profits being attributed to W Ltd was not Mr Walewski's power to enjoy them.

119. It cannot be the case, as HMRC suggested, that Mr Walewski signed his contract with W Ltd only to ensure that the mixed partnership rules could not apply; his contract was signed in 2007, many years before those rules came into effect.

Other tax charges - CGT and IHT

120. If HMRC's analysis was correct and Mr Walewski had transferred his rights to profits from AAM to W Ltd, that would have given rise to a capital gains tax charge, but HMRC had never suggested that Mr Walewski should be assessed to capital gains tax.

121. If there was no CGT charge (because there was no transfer of capital asset) there would be a punitive IHT charge (because there had been a transfer to a beneficial trust).

Apportionment September – October 2014

122. Mr Walewski's contract with AAM (for the period from September to October 2014) was signed in error and could not, in reality, have been acted on. In any event, if HMRC's arguments were to be accepted, it had no legal existence (since a partner cannot be an employee of his own partnership). It had been implemented to cover the gap period while the AAM re-organisation was taking place and to demonstrate that despite no longer being a partner, Mr Walewski remained connected with AAM.

123. If that employment contract was to be respected, on a "just and reasonable basis", half of Mr Walewski's profit share for August and September 2014 should be attributable to his contract with W Ltd and the remaining half should be re-allocated to him as an employee of AAM.

124. In any event there can be no apportionment of profit away from W Ltd to Mr Walewski for the period during which Mr Walewski was not a partner of AAM (August, September and October 2014).

125. HMRC cannot rely on the anti–avoidance rules at s 850D as the basis to apportion profits to Mr Walewski for a period when he was not a partner; that is a separate charging head and not one under which Mr Walewski has been assessed by HMRC.

126. Any apportionment should be on a just and reasonable basis. The only just and reasonable basis is to apply a time apportionment of W Ltd's allocated profits, taking account of the different roles undertaken by Mr Walewski during the April to November 2014 period.

Capital contributions

127. £430,000 of capital (capital contribution) and £10 million of unallocated (and undrawn) profits (the latter described as regulatory capital) should be taken account of and treated as value provided by W Ltd to AAM. Applying an interest rate of 5% to this amount, that should reduce any profits which can be re-allocated to Mr Walewski.

128. It does not matter for this analysis that the unallocated drawings cannot be treated as "regulatory capital" for technical purposes. "Capital" is defined for these purposes at s 108 Income Tax Act 2007.

129. In any event, since Mr Walewski is relying in the gateway at s 850C(3)(i), the technical definition of capital does not apply, all that is relevant is whether value has been provided in some form from W Ltd to AAM; however that term is defined, value was provided of this amount by W Ltd to AAM.

130. The profits generated from this capital contribution (at an interest rate of 5%) should be time apportioned taking account of the period for which the capital was provided, from April to November 2014, eight out of twelve months.

Mr Walewski's arguments – AF

Capital contributions

131. HMRC originally contested whether the £399,600 plus £1.2 million of capital injected into AF by W Ltd could be treated as a capital contribution. On the basis of the evidence provided during the Tribunal hearing, HMRC had accepted that W Ltd provided £399,600 of regulatory capital to AF and that interest at 5% on this amount should not be re-allocated to Mr Walewski**.**

132. As regards the £1.2 million of what Mr Walewski described as "regulatory capital", this was in the form of undrawn and unallocated drawings and while it may not fall within the strict definition of capital, it does represent value provided from W Ltd to AF and so should interest on that amount should be excluded from any re allocation under s 850C(3)(i).

Attribution of profits

133. Mr Walewski's argument about the attribution of profits from AF differed from his arguments in respect of AAM; he accepted that because he had been provided his services to AF through W Ltd for only half of the relevant period, profits for the remaining six months could not be attributed to the value of those services and had to be treated as attributable to his power to enjoy those profits via W Ltd and the Kleber Trust.

134. Profit apportionments from AF to Mr Walewski should reflect the time for which W Ltd had provided services to AF through W Ltd, which was for half of the relevant time. Mr Walewski provided his services to AF via W Ltd for six months of the year in question (from April until September 2014). For the remainder of the time he provided his services directly as a member of AF. 50% of AF's profits should be attributed to the services provided to clients by Mr Walewski as an employee W Ltd; only the remaining 50% should be re-allocated to Mr Walewski in his capacity as a partner of AF.

135. Mr Walewski accepted that for the purpose of s 850C(3)(c)(ii) for the six month period for which profits could be attributed to his power to enjoy, AF's profits were lower than they would have been had profits not been allocated to W Ltd and this condition is therefore satisfied for that six month period.

Other arguments (AAM and AF)

136. Mr Walewski's advisers stressed that there were no provisions in the mixed partnership rules which made it a condition of the rules applying that the way in which profits had been allocated had a tax avoidance purpose. In any event, W Ltd had not been used by Mr Walewski for tax avoidance purposes. W Ltd had been used to retain profits and a strong balance sheet, (even taking account of dividends which had been paid to its parent company) and this gave re-assurance to clients. Using a limited company also gave continental European clients, who did not understand UK LLPs, legal comfort.

137. If HMRC's arguments were correct, the result would give rise to extreme tax effects on Mr Walewski; Mr Walewski would potentially be liable to a combination of taxes resulting in a 90% tax rate, income tax, capital gains tax and inheritance tax all potentially being in point.

HMRC's arguments

Approach to the legislation

138. HMRC say that the correct approach to interpretation in this case is as set out in *Fidex*, a purposive interpretation of the statute and a realistic view of the facts should be applied to decide whether or not the facts fit the statute as construed:

> "We approach this issue as one in respect of which we must apply orthodox methods of statutory construction to a realistic view of the facts. By this we mean that we must discern and apply to the facts of this case, viewed realistically, parliament's purpose in enacting [the legislation]" [175]

139. This does not mean that, without a challenge based on fraud or sham, the Tribunal is bound to take a literal view; because something is documented in a particular way does not necessarily determine its character. It is necessary to take a realistic view of the facts.

The interpretation of s 850C

140. HMRC take a different approach to the application of a 850C, applying each of the conditions in s 850C(3) as a series of cumulative steps. They conclude that Mr Walewski fails each of those conditions because:

> (1) S 850C(3)(a) W Ltd's profit share exceeds the "appropriate notional consideration" because only a small amount of the capital contributions made to AAM and AF can be taken account of and the value of Mr Walewski's services provided to W Ltd is discounted because they are services provided to the firm. (S 850C(17))
>
> (2) S 850C(3) (b) It is accepted that Mr Walewski had the power to enjoy W Ltd's profits through the Kleber Trust.
>
> (3) S 850C(3) (c) (i) The whole of the profit allocated to W Ltd is attributable to Mr Walewski's power to enjoy. It cannot be attributed to the services provided by Mr Walewski, through W Ltd to AAM and AF. Mr Walewski was motivated by an intention to reduce the tax paid on these profits by diverting them to W Ltd where they would suffer tax at the lower corporate tax rate

AAM Consideration for services s 850C(3)(a)

141. HMRC argue that W Ltd did not earn any of the profits which were allocated to it for the 2014-15 tax year. All of these profits should be re-allocated to Mr Walewski.

142. Mr Walewski needs to provide substantiated, objective evidence to support his contention that W Ltd's profits were earned through the services he provided to AAM. He has not provided sufficient evidence of this.

143. No written evidence has been provided of any clients of AAM or AF having contracted with W Ltd. All clients cared about was that Mr Walewski was involved in managing the fund and making money for them, they did not care which particular entity he used to provide his equity investing skills. The documents referred to by the Appellant (the ISDA agreement and the Investment Management Agreement) did not support the fact that Mr Walewski was required to be employed by W Ltd.

144. No written evidence has been provided to show that Mr Walewski was acting for W Ltd when he says he was. Mr Walewski did not keep time sheets to demonstrate which of the three entities he was working for at any given time. There was no evidence that clients had actually checked (eg through Companies' House) that Mr Walewski acted through W Ltd or that W Ltd had capital to support AAM and AF.

145. The natural entity for Mr Walewski to act through was AAM. Profits had been paid to W Ltd only in order to provide a more tax efficient result. Mr Walewski knew that W Ltd would pay tax at a lower rate than the income tax rate chargeable on profits received as a individual partner of AAM (or AF). Mr Walewski was a founding partner of AAM and had started by providing his services as a member of AAM before he entered into his employment contract with W Ltd. As the sole managing member of AAM, this was the natural entity through which he would provide his services to clients.

146. AAM also had all of the relevant FCA authorisations to carry on investment management activities in the UK. W Ltd only had one FCA authorisation, a CF4, which meant it could be a participator in AAM.

147. AAM and W Ltd had been set up before Mr Walewski entered into an employment contract with W Ltd in 2007, so for the two years prior to that, he must have been providing his services in his capacity as a member of AAM.

148. It was not possible, as the employment contracts suggested (at least for August and September 2014) for Mr Walewski to act full time for both AAM and W Ltd, suggesting that there was at best confusion and some artificiality about which entity Mr Walewski was treated as working for at that time.

149. The PWC report on the mixed partnership rules demonstrated that Mr Walewski had been seeking advice on ways to plan around these rules (which explained the introduction of his employment contract with AAM) when they were introduced. Mr Tsatsaris explained the incorporation of AAM in November 2014 as in response to the need for a limited entity, but as LLPs AAM and AF were already limited entities for legal (if not tax) purposes.

Services to the firm – s 850C(17)

150. If the Appellant is correct that Mr Walewski has provided his services to AAM and AF by providing services through W Ltd to the clients of AAM and AF, then the value of those services cannot be taken account of in deciding whether W Ltd earned an appropriate notional share of AAM and AF's profits (s 850C(17)).

151. HMRC did not accept Mr Walewski's argument that the services which he provided to AAM (and AF's) clients were not "services to the firm" because they were provided directly from W Ltd to AAM and AF's clients. In providing services to clients W Ltd must have been acting on behalf of AAM and AF.

Attributable to Mr Walewski's power to enjoy

152. HMRC say that the test in s 850C(3)(c)(i) is objective. The question is whether Mr Walewski would have given away the lions' share of the profit which he earned if he could not benefit from those profits; HMRC say the answer is that he would not have done so. Mr Walewski was the main profit earner for the Alken group and there is no reasonable explanation for why he would have been prepared to give away such a large percentage of those profits unless he could somehow benefit from this.

153. This is supported by the fact that no one else in the Alken group was allowed to be involved in W Ltd.

154. There is no other reasonable explanation for why profits were accumulated in W Ltd, the suggestion that funds were held in W Ltd as "insurance" for clients does not make commercial sense, there was no legal obligation on W Ltd to hold cash or protect AAM or AF's clients in any way.

155. There was no evidence that any of AAM of AF's clients had actually done due diligence and checked W Ltd's balance sheet at Companies' House.

156. The suggestion that W Ltd provided the comfort of a corporate structure did not make sense given that AAM and AF were LLPs and so themselves, for legal purposes, were corporate.

157. S 850C(3)(c)(ii) is also satisfied because the tax charge would have been higher had the profits not been allocated to W Ltd where they were taxed at the lower rate of corporation tax**.** W Ltd's profit share is larger than its appropriate notional share of profits, Mr Walewski's profit share is lower as a result. Mr Walewski accepted that lower share because his children were beneficiaries of the Kleber Trust, therefore overall Mr Walewski's tax charge is lower than it would have been had the profits not be allocated to W Ltd.

Apportionment

158. HMRC do not accept that the "apportionment" in s 850C(4) refers to a time based apportionment. In Ms Nathan's view any apportionment should be by reference to participation in the partnership "for a period of account", so that the whole of any profits which had been earned by Mr Walewski in his capacity as a partner in AAM or AF could be apportioned to him, for whatever period of time they arose.

159. This approach is supported by the drafting of s 850D ITTOIA which was introduced as part of the same package of anti-avoidance measures.

Capital contributions

160. HMRC accepted, having heard the evidence given to the Tribunal, including the banking evidence provided by Mr Woodgate, that £430,000 should be treated as capital contributed to AAM by W Ltd (provided on 24 November 2014 and repaid on 26 March 2015) and that a time apportioned return of 5% on that amount should be treated as value provided by W Ltd to AAM.

161. HMRC do not accept that a further £10 million can be treated as a capital contribution.

162. The unallocated profits of £10 million which were held by AAM were unallocated profits of W Ltd. They could not be treated as capital for s 108 Income Tax Act 2007 (and s

850C(13) ITTOIA) purposes. These profits have not been specifically designated as capital in the partnership. HMRC relied on statements in *Hamilton & Kinneil* to support the fact that there must be a specific act to capitalise profits:

> "It may well be correct that capitalised profits are to be treated as contributions. The act of capitalisation precludes the profits being withdrawn as profit..... It is appropriate to see the act of capitalisation as equivalent to the making of a contribution" [53]

163. If, as was established by Mr Walewski, those profits were both unallocated and undrawn, they did not belong to W Ltd and so could not possibly be treated as a contribution by W Ltd to AAM.

164. No part of the unallocated profit retained in AAM could be treated as a capital contribution and there should be no deduction from the profits allocated to Mr Walewski to take account of this.

AF

165. In most respects HMRC's arguments about the allocation of AF's profits were substantially the same as those made for AAM.

Capital contributions

166. HMRC accepted during the course of the hearing, on the basis of the financial evidence provided by Mr Woodgate, that a capital contribution of £399,600 had been made by W Ltd to AF (by way of offset; W Ltd allocating drawings from AAM to take over AAM's capital investment in AF on 5 December 2011) and that a deduction could be made against the profits otherwise allocated to Mr Walewski equal to a 5% interest rate on that capital contribution for the period from April 2014 to March 2015.

167. HMRC contested the Appellant's statement that Mr Walewski could have been both an employee and partner of AF at the same time (from 1 October 2014); under English law it is not possible for a member to be both a partner and an employee (see *Tiffin v Lester Aldridge LLP*, and *Bates van Winkelhof* discussing section 4(4) of the Limited Liability Partnerships Act 2000).

168. The Appellant later clarified that Mr Walewski had been acting as a member and not as an employee of AF from 1 October 2014 and we have therefore not treated this issue as in dispute.

FINDINGS OF FACT

169. On the basis of the evidence seen and heard by the Tribunal we make these findings of fact:

(1) W Ltd was incorporated on 8 July 2005 and became a member of AAM on 16 August 2006.

(2) Mr Walewski was a partner in AAM from 2005. He continued in that role after his employment contract with W Ltd was signed in April 2007.

(3) W Ltd was allocated the right to 99.9 % of AAM's profits in 2006, before Mr Walewski became an employee of W Ltd in 2007.

(4) W Ltd did not sign any agreement with AAM or AF setting out how Mr Walewski's services would be provided to their clients.

(5) Clients of AAM and AF did not sign any agreements with W Ltd.

(6) Mr Walewski did not himself take any tangible steps to divide his role between W Ltd, AAM and AF.

(7) While client documents did (in some cases, but not all) refer to Mr Walewski as a "key man" in this business, they did not include a specification of which entity Mr Walewski had to work for and did not refer to W Ltd at all

(8) The business carried on by AAM did not materially alter during the 2014-15 period when Mr Walewski resigned from W Ltd as an employee, resigned as a partner of AAM and became an employee of AAM.

(9) The majority of AAM's profits for the 2014-15 tax year were earned for the period before 30 September 2014, the time during which Mr Walewski was a partner and subsequently an employee of AAM.

(10) Changes to the Alken group structure, including introducing Mr Walewski's employment contract with AAM, were made in response to suggestions in the PWC advice document of July 2014.

DISCUSSION

170. Our overall conclusion, based on these findings of fact, is that Mr Walewski's work for W Ltd, AAM and AF was fungible; it is not possible on the basis of any evidence which we saw, to separate his role into discrete components; his work for one was his work for each and all of those entities. Mr Tsatsaris described Mr Walewski's roles for the three entities as "very interlinked", we think they were more than interlinked, we think Mr Walewski was essentially playing only a single role, but for the benefit of all three entities.

171. Mr Walewski was described as "wearing a number of hats", again, in our view this does not do justice to the truly fungible nature of his activities for these entities, all of whose decisions and strategies began and ended with Mr Walewski, as the only director and employee of W Ltd, as a member of AAM and only member of its management committee and as an employee and member of AF.

172. There was no commercial, physical or temporal separation of Mr Walewski's activities. A more accurate description of Mr Walewski would be to say that he wore one hat in many places. The entity on whose behalf he wore that hat was essentially irrelevant.

Interpretation of s 850C(3)

173. We have approached this appeal on the basis that the only point in contention between the parties is whether Mr Walewski can satisfy the condition at s 850C(3)(c)(i). However, to get to that point we have considered HMRC's arguments relating to s 850C(3)(a) because many of the points raised by HMRC in the context of s 850C(3)(a) were addressed by the Appellant in the context of s 850C(3)(c)(i). While these are discrete tests, they are two sides of the same coin; if W Ltd's profit allocation cannot be explained by Mr Walewski's earning power as its employee, what other alternative reasonable explanation can there be for the profits being allocated to W Ltd other than Mr Walewski's power to enjoy them ?

Other taxes

174. Mr Soares and Mr Afzal spent some time pointing out that if Mr Walewski's appeal failed, he could be charged to income tax, capital gains tax and inheritance tax on the sums paid to W Ltd. None of those taxes were under appeal before us and, without wishing to entirely dismiss the technical analysis on which the Appellant's assumptions were based, we do not consider it appropriate to give this analysis much weight in coming to a decision about the tax which is actually under appeal; the income tax chargeable on Mr Walewski.

S 850C(3)(a) Appropriate notional profit – W Ltd

Consideration for services (s 850C(10))

175. We do not agree that W Ltd earned all of the profits allocated to it by either AAM or AF by reason of Mr Walewski's activities for the clients of those entities. We have concluded this because:

(1) In our view the test which we must apply to determine whether W Ltd has earned its share of attributed profits is a test of substance and not just form. In fact, we were provided with little evidence of either substance or form to support the Appellant's arguments about what W Ltd did to earn its allocated profits. In particular, we saw no commercial agreements between W Ltd and clients, or similar agreements between AAM and AF to govern how they would obtain Mr Walewski's services through W Ltd. The only descriptions which we saw of W Ltd's role in the group suggested that it was a service company (the PWC advice) or a holding company (Companies' House documents).

(2) The Appellant did not provide any clear evidence that his activities for W Ltd could be separated in any meaningful way from his activities for AAM and AF. We saw no evidence, other than Mr Walewski's own assertions, that even he knew when he was working for W Ltd rather than AAM or AF.

(3) There was a clear confusion, if not a direct conflict, between Mr Walewski's employment contract for W Ltd and his employment contract with AAM, obliging him to work full time for both entities at once. Suggesting that in substance no real distinction was made between Mr Walewski's activities for each of those entities.

(4) Equally, we did not see any evidence that clients made a distinction between AAM and W Ltd or AF and W Ltd either. None had a separate legal agreement with W Ltd and there is no evidence that economically or commercially they drew a distinction between W Ltd and the other entities through which Mr Walewski acted. We agree with HMRC that they were interested in knowing that Mr Walewski was involved, but they had very little interest in how that involvement was structured.

(5) The agreements which we saw (ISDA agreement and Investment Management Agreement) do not refer to W Ltd at all, but do refer to Mr Walewski as an employee of AAM.

(6) The other reasons given for clients wanting W Ltd involved in their deals did not seem to us to be convincing; we were not given evidence of clients actually checking that W Ltd held capital for them. In fact, we know that during 2014-15 W Ltd did the opposite of conserving capital to keep investors happy: W Ltd left unallocated (undrawn) profits in AAM (and AF).

(7) The Management Committee Meeting notes (of VAM) from 2006 stated that W Ltd was entitled to 99.9% of AAM's profit share as of right. It cannot be said therefore

that W Ltd earned those profits as a result of Mr Walewski's employment contract or the services he carried out for AAM and AF clients under that employment contract.

176. For these reasons we have concluded that in respect of both AAM and AF W Ltd's profit share "exceeds the appropriate notional consideration for services" (s 850C(3)(a) and s 850C(10)) and that the profits allocated to W Ltd were not allocated as consideration for Mr Walewski's services.

Appropriate notional return on capital

AAM

177. We agree with HMRC that the £10 million of unallocated, undrawn capital retained in AAM for the 2014-15 period cannot be treated as "capital" for these purposes.

178. We say this for three reasons:

(1) In order to constitute a "contribution" of capital, it must first belong to the entity (W Ltd) which is making the contribution. The evidence which we heard, particularly from Mr Tsatsaris was clear that this £10 million had not been allocated to W Ltd and therefore did not belong to W Ltd. In accordance with AAM partnership agreement, profits had to be allocated by the management committee and unallocated profits were held in a retention account for the benefit of AAM (clause 9.4). We do not see how the fact that W Ltd had paid tax on this amount under the specific tax code applying to LLPs alters this conclusion.

(2) Even if we are wrong on this, we did not see any evidence that this £10 million had been properly characterised as "capital" by AAM, certainly not in the technical sense required by s 850C(3) and not in any other meaningful sense, such as in accordance with the relevant SORP.

(3) Finally, Mr Walewski's interpretation, that the provision of any "capital like" funds which generated value for AAM should be taken account of as part of the notional consideration provided by W Ltd, however defined, is not tenable in the context of this legislation which has a specific provision dealing with returns on capital as defined.

179. The only amount of capital which can be taking account of in determining W Ltd's appropriate notional return on capital from AAM is the agreed £430,000 of capital.

180. That capital was committed by W Ltd from 1 August 2014 (the date when W Ltd took over Mr Walewski's membership of AAM), but no payment was actually made until 24 November 2014, just before AAM ceased to be an LLP. The capital was not re-paid until 26 March 2015.

181. In our view, since the return calculated under s 850C(12) is "by reference to the time value of an amount of money equal to B's contribution to the firm" W Ltd can be treated as providing value to AAM only when that capital payment was actually made to AAM. Any value provided can only have been for the period from 24 November 2014 until repayment on 26 March 2015.

182. This gives a notional consideration for capital provided for the period as 5% of the agreed £430,000 of capital.

AF

183. The parties agreed that £399,600 of capital in AF could be treated as capital for the purposes of s 850C(10). A return at 5% on that amount can therefore be treated as "appropriate notional profit" for AF.

184. Our position on the "regulatory capital" amount of £1.2 million said to have been provided by W Ltd to AF is the same as our position in respect of AAM; the £1.2 million represents unallocated profits of AF. Those profits do not belong to W Ltd and therefore cannot be value given by the entity for the purposes of s 850C(3)(i).

185. We consider in more detail below to what extent we think the appropriate notional profits are exceeded in both AAM and AF taking account of these conclusions.

S 850(C)(3)(i) Mr Walewski's power to enjoy

186. To some extent our conclusion above must inform our conclusions on this point, although it is a separate head of s 850C(3). If the allocation of profits to W Ltd cannot be explained by the efforts made by W Ltd to earn those profits, we have to find another reason why those profits were allocated to W Ltd other than Mr Walewski's power to enjoy them through the Kleber Trust.

187. We do not consider that Mr Walewski has provided any other reasonable explanation for the profits having been paid to W Ltd by AAM and AF.

(1) The other reasons given for transferring profits to W Ltd were not compelling; the need to hold cash as an "insurance" or to provide comfort for clients does not stand up to scrutiny. We did not see or hear any evidence which directly confirmed that this was a concern for clients. Mr Vivas and Mr Canovas asserted that clients were interested in W Ltd and its status, but we saw no evidence of due diligence on W Ltd actually being undertaken by clients. On the contrary, the willingness of W Ltd to pay dividends to its parent company and to leave unallocated profits in AAM suggests that W Ltd was not maximising its role as holding a buffer of cash to protect clients.

(2) The share of profits of AAM allocated to W Ltd for earlier years are consistent with a desire to direct those profits to W Ltd and the Kleber Trust for reasons other than Mr Walewski's activities as an employee of W Ltd:

(a) For the year ending 30 March 2007 W Ltd's profit allocation was £6,036,059 ie 77.45 % of the total profits achieved by AAM. Mr W was not even employed by W Ltd as this stage (his employment contract started on 1st April 2007) and yet W Ltd was allocated more than three-quarters of the profits of the partnership.

(b) The profits allocated to W Ltd during various years varied from 49.67% to 99.9 % with an average of 71%, including for periods when Mr Walewski was not an employee.

(c) This suggests that W Ltd had the profits of AAM allocated to it because of its 99.9% interest in the partnership from 16th August 2006; the interest which had been handed over to the company by Mr Walewski himself.

(3) We saw no evidence, either from the witnesses or from the documents which we were shown, to suggest that in substance the arrangements between various parties changed at all from 1st April 2007 onwards when Mr Walewski did become an employee of W Ltd.

188. There are also some documentary discrepancies which suggest that there is at best some confusion between the roles which Mr Walewski is undertaking and the relationship between those roles and the profits paid to W Ltd. For example:

(1) VAM (later called AAM) needed the approval of FSA for change of control of the partnership. This approval had been given by the FSA by the date of the VAM meeting (16th August 2006). Change of control of VAM was considered and duly completed on this date and Mr Walewski stopped being a controller of VAM. W Ltd became a member of VAM and took a controlling interest in the partnership. Despite this Mr Walewski signed the later resolution of November 2006, at which point he only had a very small interest in VAM (AAM).

(2) Mr Walewski was appointed a director of W Ltd on 3 June 2006 on the basis of the documents which were shown, but he is also described as being appointed a director on 1st April 2007, in his employment contract with W Ltd.

189. These discrepancies support our view that, while documentary changes may have been introduced, including Mr Walewski signing an employment contract with W Ltd (and later with AAM), in substance it made no difference to the commercial arrangements between the parties that Mr Walewski became an employee. The payment of profits to W Ltd was independent of this and cannot be attributed to the services provided under that contract.

190. For these reasons we have concluded that Mr Walewski has not provided a reasonable explanation for why profits should be allocated to W Ltd from AAM and AF for the 2015-15 tax year.

191. On the contrary, our view is that the only reasonable explanation for the allocation of profit to W Ltd from AAM and AF is by reason of Mr Walewski's ability to enjoy those profits.

192. This conclusion is supported by the fact that:

(1) The 2006 amended partnership agreement of AAM gave W Ltd a right to 99.9% of AAM's profits, independent of any services provided by Mr Walewski or the terms of any employment contract.

(2) Mr Walewski's salary from W Ltd, while significant, was modest in terms of the industry in which he worked and the level of profit which was being generated in AAM and AF. Mr.Walewski was contracted to take £200,000 from his employment but he took £130,000.

(3) Mr Walewski did not take a bonus from W Ltd under his employment contract.

(4) We find it hard to understand why someone in Mr Walewski's position would have been willing to give away such a large percentage of the profits which he had generated if there was not some benefit to himself. In our view, the only reason he would do that is if he knows that he has the power to enjoy the profits of the company in some other way.

(5) Mr Walewski would be an unusual, if not unique, member of the finance industry if he not only failed to take the full amount of his contracted salary, but also did not claim any amount of bonus and allowed a company to take all of the fruits of his labour; his salary of £130,000 equated to 0.722 % of what he claims he was generating by way of profit for W Ltd for 2014-15.

(6) At the relevant time there was a significant difference between the 45% income tax which Mr Walewski suffered on payments made directly to him and the 21% corporation tax suffered by W Ltd.

(7) It seems reasonable to conclude that changes made in the Alken group structure were made not for commercial reasons, but in response to the PWC advice given about

ways to mitigate the impact of the mixed partnership rules and ensure that the tax differential between W Ltd and Mr Walewski could be retained.

193. In respect of AF the arguments are the same, but if anything, the fact that Mr Walewski changed roles during the period and, as the Appellant accepted, the profit share allocated to W Ltd remained the same (while Mr Walewski was an employee of W Ltd and after the end of his employment contract, when his only relationship with AF was a member of AF), goes further to support our conclusion that there was in substance no difference in the commercial arrangements between the parties whether Mr Walewski was employed by W Ltd or not.

194. Mr Walewski's employment through W Ltd cannot be a sufficient explanation for the allocated of profits to that entity. The only other reasonable explanation is Mr Walewski's power to enjoy those profits through W Ltd and the Kleber Trust.

Mr Walewski's profit share Just and reasonable basis s 805C(4)

195. Even taking account of the inclusion of a return on capital in both AAM and AF to determine W Ltd's appropriate notional profit, we have concluded that W Ltd's profit share does exceed the "appropriate notional profit" and this is attributable to Mr Walewski's power to enjoy those profits.

196. The Appellant's appeal must therefore fail.

197. We have gone on to consider to what extent Mr Walewski's profit share should be increased by reference to the "just and reasonable basis" referred to in s 805C(4).

198. We have not been provided with any compelling evidence of W Ltd's activities being distinct from those of AAM and AF. All of W Ltd, AAM and AF were creatures of Mr Walewski who controlled them.

199. We have seen the amended AAM partnership agreement of 2006, giving W Ltd 99.9% of the profits of AAM and we know that W Ltd took over AAM's right to 99.9% of the profits in AF in December 2011.

200. Since W Ltd had a right to 99.9% of AAM and AF's profits independent of any activities of Mr Walewski, we do not see how any of the profits allocated to W Ltd can be said to have been earned by that entity through Mr Walewski's activities as an employee.

201. Mr Tsatsaris attempted to argue that because the allocation of profit was discretionary, it could not be said that payment was automatically made under the LLP Agreement and not for any other reason. We do not agree that this refutes the point that W Ltd was entitled to a 99% share of AAM's profits whatever Mr Walewski might or might not have done. We note in particular that there is nothing in the AAM LLP agreement which makes any profit share dependent on the activities of Mr Walewski.

202. For these reasons, other than the small fee recorded as paid to W Ltd for the 2014-15 tax year, we do not consider that W Ltd should be treated as receiving any of the profits allocated to it by AAM as consideration for services provided by Mr Walewski in his capacity as an employee of W Ltd. All of these profits (subject to any amounts attributable to capital contributions) are attributable to Mr Walewski's power to enjoy them.

203. Given AF's "junior" role in the arrangements, and the fact that its focus was on trade execution on behalf of AAM's clients, rather than on strategic equity investment activities, we can see no reason why any of its profits should be allocated directly to W Ltd either. If we

cannot make the argument in respect of AAM, it does not seem possible to make the argument for AF, given that AF is essentially a creature of AAM.

204. In particular, we saw no suggestion that W Ltd contributed to the specific types of services which were provided by AF or in any other particular way to AF, other than that Mr Walewski viewed himself as working through W Ltd on behalf of all of the Alken group entities. The Secondment Agreement entered into between Alken AM Ltd and AF after AAM's incorporation refers to the employees of AF who are to be seconded Alken AM Ltd to enable it to carry out its duties, who are all administrative and analyst staff. No reference is made to Mr Walewski.

205. For these reasons we agree with HMRC that W Ltd should not be treated as receiving any of the profits allocated to it from AF as consideration for services provided by Mr Walewski in his capacity as an employee of W Ltd and that all (subject to any deduction for capital contributions made) are attributable to Mr Walewski's power to enjoy those profits.

206. We have considered whether, given the "fungible" nature of Mr Walewski's activities and the fact that we have said that each of his activities were actually activities which potentially contributed to all of W Ltd, AAM and AF, a "just and reasonable" approach would be to allocate the relevant profits equally between those entities.

207. We have decided that this is not "just and reasonable" in these circumstances because of

(1) The very limited evidence which we have seen that W Ltd featured commercially in these arrangements in any significant way, (in contrast to AAM);

(2) The descriptions which we do have of W Ltd's activities (from PWC and Companies' House) do not suggest that W Ltd had a significant commercial role in its own right;

(3) the prior allocation of profits arising under the two LLP agreements, which also suggests that profits were not intended to be split by reference to the actual input of Mr Walewski acting though W Ltd.

Time apportionment

208. Finally, we have considered, whether we should also take account of the time apportionment basis for which Mr Walewski argued:

(1) In respect of the time for which Mr Walewski was not a partner in AAM

(2) In respect of the time for which Mr Walewski was an employee of AAM

(3) In respect of the time for which W Ltd was not a partner of AF.

209. HMRC are correct to say that there is no specific reference to time apportionment in the relevant legislation which refers at s 850C(1) only to the "relevant period of account", but we think that even without a specific reference, the concept of "just and reasonable apportionment" can connote a concept of time apportionment unless that is clearly inappropriate.

210. Time apportionment is an appropriate way of allocating profits if there is a correlation between the passage of time and the generation of profit. Time does not generate profit, but it can be a proxy for determining when profits should be treated as arising if profits are generated from a constant source in a regular pattern.

211. That can be said of the interest deemed to arise from the capital contributions made to AAM and AF. It cannot be readily said of the other profits which were said to have been

earned by W Ltd through Mr Walewski. We have established that those profits could not be confidently ascribed to a single source other than Mr Walewski himself and he acted for all three of the relevant entities (W Ltd, AAM and AF) at the same time.

212. For that reason we do not agree that a linear, time apportionment approach is appropriate here, since it in effect divides Mr Walewski's profits sequentially between these three entities on a basis which does not reflect the commercial reality of these arrangements.

AAM

213. Specifically, we are not convinced that in these circumstances it is reasonable to take account of the three month period for which Mr Walewski was not a partner in AAM. During this period he was an employee of AAM (this is legally possible since he was no longer a partner) and so was still legally and more importantly, commercially, involved in that entity. We did not see any evidence that Mr Walewski's change of status (from partner to employee) impacted the profits or activities of AAM during this three month period.

214. We have also noted that AAM's turnover figures show that the majority of its profits were earned before 31 September 2014, the time during which Mr Walewski was a partner and subsequently an employee of AAM.

215. For this reason we do not accept Mr Walewski's suggestion that any allocation of profits should be time apportioned to reflect the period during which Mr Walewski was not a partner in AAM.

216. For the same reason we reject the Appellant's argument that there should be some time apportionment to reflect the period during which Mr Walewski was not an employee of W Ltd (September and October 2014), since it is not clear to us that in substance his role changed at all during this period.

AF

217. The Appellant argued that time apportionment would lead to a split of AF's profits on a 50/50 basis, taking account of the fact that W Ltd was a partner in AF for half of the period of account and it was only for the remainder of the time that Mr Walewski operated directly as a partner of AF.

218. Given our overall conclusion that it is not possible to split Mr Walewski's activities between the various roles which he carried on (including between AF and W Ltd), we do not accept that this time apportionment based on a change in the form in which Mr Walewski provided his services to clients is justified.

219. For these reasons we reject the Appellant's contentions that we should split the profits available to be re-allocated to Mr Walewski by taking account of the fact that he was only acting through W Ltd for half of the relevant period.

Conclusions

220. This decision is issued in principle without attempting to reconcile the various figures provided to us by the parties (which appeared to us to be contradictory in some cases and not based on common starting assumptions).

221. We leave it to the parties to apply to the Tribunal to confirm the final figures on which Mr Walewski should be taxed if they cannot be agreed.

222. AAM

(1) W Ltd provided services to AAM in the form of its capital contribution of £430,000 of capital. A return of 5% on that amount for the period from November 2014 until March 2015 should be deducted from any profits which can be reallocated to Mr Walewski.

(2) All remaining profits which were allocated to W Ltd should be reallocated to Mr Walewski for the 2014-15 tax year.

223. AF

(1) W Ltd provided services to AF in the form of its capital contribution of £399,600 of capital. A return of 5% on that amount for the period from April 2014 until March 2015 should be deducted from any profits which can be reallocated to Mr Walewski.

(2) All remaining profits which were allocated to W Ltd should be reallocated to Mr Walewski for the 2014 -15 tax year.

Right to apply for permission to appeal

224. This document contains full findings of fact and reasons for the decision. Any party dissatisfied with this decision has a right to apply for permission to appeal against it pursuant to Rule 39 of the Tribunal Procedure (First-tier Tribunal) (Tax Chamber) Rules 2009. The application must be received by this Tribunal not later than 56 days after this decision is sent to that party. The parties are referred to "Guidance to accompany a Decision from the First-tier Tribunal (Tax Chamber)" which accompanies and forms part of this decision notice.

RACHEL SHORT
TRIBUNAL JUDGE

RELEASE DATE: 30 JANUARY 2020

Appendix– The Mixed Partnership Rules

"**850C Excess profit allocation to non-individual partners**

850C(1) Subsections (4) and (5) apply 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") (see subsection (6)) 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") (see subsection (6)) 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.

(2) 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.

(3) 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.

(4) 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.

But any increase by virtue of paragraph (b) is not to exceed the amount of the excess mentioned in subsection (3)(a) after deducting from that amount any increase by virtue of paragraph (a).

(5) If B is chargeable to income tax, in applying sections 850 to 850B in relation to B for the relevant period of account, such adjustments are to be made as are just and reasonable to take account of the increase in A's profit share under subsection (4).
(This subsection does not apply for the purposes of subsection (7) or section 850D(7).)

(6) A partner in a firm is an "**individual partner**" if the partner is an individual and "**non-individual partner**" is to be read accordingly; but "**non-individual partner**" does not include the firm itself where it is treated as a partner under section 863I (allocation of profit to AIFM firm).

(7) B's profit share is to be determined by applying section 850 and, if relevant, section 850A in relation to B for the relevant period of account (whether or not B is chargeable to income tax) on the assumption that the calculation under section 849 in relation to B produces the profit for the firm mentioned in subsection (1)(a)(i).

(8) "**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).

(9) "**The relevant tax amount**" is 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.

(10) "**The appropriate notional profit**" is the sum of the appropriate notional return on capital and the appropriate notional consideration for services.

(11) "**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

(12) The return mentioned in subsection (11)(a) is to be calculated on the basis that it is a return which is—

(a) by reference to the time value of an amount of money equal to B's contribution to the firm, and

(b) at a rate which (in all the circumstances) is a commercial rate of interest.

(13) For the purposes of subsections (11) and (12) B's contribution to the firm is amount A determined under section 108 of ITA 2007 (meaning of "contribution to the LLP").

(14) That section is to be applied—

(a) reading references to the individual as references to B and references to the LLP as references to the firm, and

(b) with the omission of—
(i) subsections (5)(b) and (9), and
(ii) in subsection (6) the words from "but" to the end.

(15) "**The appropriate notional consideration for services**" is—

(a) the amount which B would receive in consideration for any services provided to the firm by B during the relevant period of account were the consideration to be calculated on the basis mentioned in subsection (16), less

(b) any amount actually received in consideration for any such services which is not included in B's profit share.

(16) The consideration mentioned in subsection (15)(a) is to be calculated on the basis that B is not a partner in the firm and is acting at arm's length from the firm.

(17) Any services, the provision of which involves any partner in the firm in addition to B, are to be ignored for the purposes of subsection (15).

(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.

(22) Subsection (23) applies if—

(a) the increase under subsection (4), or any part of it, is allocated by A to the firm itself under section 863I (allocation of profit to AIFM firm), and

(b) B makes a payment to the firm representing any income tax for which the firm is liable by virtue of section 863I in respect of the amount of the increase allocated to it.

(23) For income tax purposes, the payment—

(a) is not to be income of any partner in the firm, and

(b) is not to be taken into account in calculating any profits or losses of B or otherwise deducted from any income of B.