

Corporate Limited Partnerships and Art 7 of US/Australian Double Tax Agreement

Commissioner of Taxation v Resource Capital Finance IV LP
[2019] FCAFC 51

Appeal from:

Resource Capital Finance IV LP v Commissioner of Taxation
[2018] FCA 41

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Disconformity in tax treatment of corporate limited partnerships

Under Australian tax law, corporate limited partnerships are taxed as companies

Under US law, a corporate limited partnership is a “fiscally transparent” or “flow through” entity and not subject to tax:

- Partners in the corporate limited partnership are taxable on their individual share of Australian sourced income.

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ISSUES

Australia taxed the non-resident corporate limited partnership on Australian sourced income.

1. Is a corporate limited partnership a taxable entity for Australian tax law purposes and subject to tax?
2. Is a corporate limited partnership treated as a “resident” for the purposes of US/Australian Tax Treaty?
3. Were the US partners of the corporate limited partnership entitled to relief from taxation liability by reason of Art 7 of the US/Australian Tax Treaty?

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RCF IV: OUTCOME ON APPEAL

On appeal held by majority:

- a corporate limited partnership is a taxable entity for Australian tax law purposes and subject to tax
- the corporate limited partnership was not a resident of the US for the purposes of the US/Australia Treaty
- taxation relief under the US/Australia Treaty was not available to the corporate limited partnership because the Treaty did not apply to the partnership
- the US partners could not claim tax relief in the proceedings before the Court

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The Australia-USA DTA

- Art 1 provides that the DTA applies to “persons” who are residents of one or both of Australia and the USA
- Art 4 defines which entities are residents for the purposes of the DTA
- Art 7 states that business profits will be taxable in the country of residence, unless it is from a permanent establishment.

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RESIDENCE: Article 4(1)(b)

Residence for the purpose of the US/Australian Treaty

- Art 4(1)(b): defined term

Residence

(1) For the purposes of this Convention:

...

- (b) a person is a resident of the United States if the person is:
 - (i) a United States corporation;
 - (ii) a United States citizen, other than a United States citizen who is a resident of a State other than Australia for the purposes of a double tax agreement between that State and Australia; or

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Article 4(1)(b) cont.

- (iii) **any other person** (except a corporation or unincorporated entity treated as a corporation for United States tax purposes) **resident in the United States** for purposes of its tax, **provided that, in relation to any income derived by a partnership**, an estate of a deceased individual or a trust, **such person shall not be treated as a resident of the United States except to the extent that the income is subject to United States tax as the income of a resident, either in its hands or in the hands of a partner or beneficiary**, or, if that income is exempt from United States tax, is exempt other than because such person, partner or beneficiary is not a United States person according to United States law relating to United States tax.

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“PERSON”: Art 3(1)(a)

The word “person” for the purposes of Art 4(a)(b)(iii) includes a partnership – Art 3(1)(a):

For the purposes of this Convention, unless the context otherwise requires:

- (a) **the term “person” includes** an individual, an estate of a deceased individual, a trust, **a partnership**, a company and any other body of persons; ...

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RCF IV: at first instance

Taxpayer's argument:

- although a corporate limited partnership is treated as a company for tax purposes, a partnership is not a legal entity and not able to be taxed as a taxable entity separate from the partners
- Australian tax law did not authorise taxing of the partnership as a separate legal entity

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Commissioner's argument:

- Corporate limited partnerships are taxable entities under Australian tax law
- Corporate limited partnerships could not get relief from taxation under the US/Australia Treaty because they are not legal entities under US law

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DECISION AT FIRST INSTANCE

- a corporate limited partnership is not a legal entity and not a taxable entity
- correct taxpayers were the US partners
- the US partners of the partnership would be entitled to relief from liability by reason of Article 7(1) of the Treaty

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Construction of Art 4

Held:

Art 4 did not provide and did not warrant a construction that the partnership should be treated as a separate “person” with a separate residence.

- Article 3(1)(a) provides that “person” includes a partnership but the words “any other person” when used in Article 4(1)(b)(iii) do not create a category of taxable entities which is separate from the partners or agents through which the partners carry on an enterprise.
- The terms of Article 4(1)(b)(iii) do not suggest that a partnership was intended to be included as a person separate from, and in addition to, the partners who comprised it,
- and the proviso in Article 4(1)(b)(iii) would, in any event, exempt partnerships from the category of persons who are resident in the United States. That is because the article expressly excludes “such person” (that is, “a corporation or unincorporated entity treated as a corporation for United States tax purposes”) who “is not a United States person according to United States law relating to United States tax”.

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REASONING:

- The definition of “person” in Article 3(1)(a) ensures that the provisions apply to the activities carried on by partners in a partnership but does not require that the words “any other person” in Article 4(1)(b)(ii) be understood to give to the partnership a residence separate from the partners.
- That construction is supported by the proviso in Article 4(1)(b)(iii) which makes clear that persons resident in the United States for the purposes of its tax are encompassed within the phrase “any other person” to the extent that such a person derives income through a partnership.

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- The proviso expressly excludes “such persons” from the class of United States residents except to the extent that the income is subject to tax in the United States as income of a resident in the manner specified.
- The reference to “such person” in the proviso is to a category of person dealt with by the whole of Article 4(1)(b)(iii), which refers to the “any other person” appearing in the beginning of that clause.
- It follows that the partners of the RCF IV and RCF V partnership are entitled to relief under Article 7(1) of the United States Convention

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APPEAL DECISION

On appeal –

- held that corporate limited partnerships can be assessed to tax under Australian tax laws

Majority Decision:

- Treaty does not apply to relieve the partnership from tax because:
 - (a) for US tax purposes, the partnership is not a separate legal entity and thus could not be resident in the US
 - (b) in Art 4(1)(b)(iii) definition of “resident” has a dual requirement, namely, partnership was both a US resident and the income of the partnership had to be subject to US tax

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Dissenting judgment

- Proviso not a true proviso but only make sense if directed at identifying when a partnership is “treated as” having a residency for the purposes of the DTA
- Although the partnership under US law does not have residency, proviso would attribute a residency status to the partnership separate from its partners for the purpose of the DTA where income of the partnership is taxable in the hands of US resident partners
- Residency of the US partners which is relevant

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