



HM Revenue  
& Customs

# Partnership taxation: proposals to clarify tax treatment

**Summary of Responses**  
March 2017

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# 1. Executive Summary

- 1.1. The government recognises that modern businesses can use a variety of structures. For many businesses the partnership structure provides the most suitable way to organise their activities and give them the flexibility to succeed.
- 1.2. The tax system should support partnerships, by being as clear as possible, but it also has to be fair.
- 1.3. The government wants to remove uncertainty and provide clarity for partnerships. The changes we propose will ensure the tax system fits with modern commercial practice. The proposals are also aimed at ensuring that there is greater transparency over the person ultimately entitled to the profits of the partnership.
- 1.4. At Budget 2016 the government announced a consultation on clarifying the tax treatment of partnerships. Many interested parties have engaged actively in the consultation and the government is grateful for the time and effort that has been put into the consultation process to date. We have taken account of all the responses in developing the detail of the proposals.
- 1.5. This document sets out the decisions that are informed from those representations. In summary:
- 1.6. The government intends to legislate to ensure that the beneficiary of a nominee or bare trust arrangement is treated as a partner and expect that person to be named on the partnership return, as they are potentially liable to tax on their allocation of the profits of the partnership
- 1.7. The government will not require a profit generating partnership to report the ultimate recipients of its profit through a partnership chain on its return. The partnership will be required to report the details of its partners with computations of taxable profit on all 4 possible bases (UK-resident individual, non-UK resident individual, UK-resident company, non-UK resident company). Where the details of all the ultimate recipients of a partnership profit have been provided to HMRC, the partnership will only have to prepare computations on the bases appropriate to those persons.
- 1.8. Partnerships which are reporting financial institutions as defined by the OECD Common Reporting Standard (CRS) and which have provided details of partners under CRS, will not be required to report the full details of those same partners on the partnership return (if they only receive investment profits).

- 1.9. The government does not currently intend to pursue the option of requiring a payment on account in situations where reporting requirements are not complied with.
- 1.10. The profit allocation stated in the partnership return will be the first point of reference for HMRC in determining the taxable profits of each partner. There will be no requirement for partnerships to notify HMRC of changes in their profit sharing arrangements.
- 1.11. Partners are treated as taxable on their share in profits or losses that arose during the period in which they were partners or members and any retrospective variation to a partnership's profit-sharing arrangements made after the period-end will not apply.
- 1.12. Profits of firms which have a company partner chargeable to income tax are calculated as if a non-UK resident company was carrying on the business.

## 2. Introduction

### Background to consultation

- 2.1. The government identified areas where the tax rules for partnerships may be seen as unclear or create an inappropriate outcome.
- 2.2. Following an announcement at Budget 2016, the government published a consultation document on proposals to clarify the tax treatment of partnerships on 9 August 2016. That document is available on the Budget 2016 section of the HMRC website, at:  
[https://www.gov.uk/government/uploads/system/uploads/attachment\\_data/file/544520/Partnership\\_taxation-proposals\\_to\\_clarify\\_tax\\_treatment.pdf](https://www.gov.uk/government/uploads/system/uploads/attachment_data/file/544520/Partnership_taxation-proposals_to_clarify_tax_treatment.pdf)
- 2.3. The consultation concluded on 1 November 2016.

### Purpose of consultation

- 2.4. The government wants to provide partnerships with clarity and certainty over their tax affairs. Additionally, the proposals aim to ensure there is sufficient clarity over the ultimate recipient of partnership profits, to assure HMRC that all tax is correctly paid.
- 2.5. The proposals should have no effect on the vast majority of partnerships. They seek to provide clarity in particular circumstances where the current rules are seen as creating uncertainty, and will reduce the scope for non-compliant taxpayers to avoid or delay paying tax.

### Summary of consultation

- 2.6. The consultation sought the views of partnership businesses, advisors, representative bodies, legal professionals and others, about the proposals.
- 2.7. As part of the consultation process, we held a number of meetings and workshops with interested parties to discuss the proposals.
- 2.8. The government would like to thank those who responded to the consultation document and those who participated in meetings and workshops and recognises the time and effort that went into the comments and contributions.
- 2.9. A list of respondents and contributors to the consultation can be found at Annex A.
- 2.10. We received 43 formal written responses which covered all of the subjects of the consultation. There was general support for reform of partnership taxation and for clarifying areas of uncertainty. The most frequently raised concerns in the responses were regarding the potential effects on administration for partnerships, how the proposals considered a partnership's access to information and confidentiality issues. In particular, respondents were

concerned to maintain the UK as an attractive location for the investment sector and the need to support the government's investment management strategy which seeks to ensure that the UK continues to be competitive in the global investment industry.

- 2.11. In broad terms responses from the investment sector wanted to ensure any changes reflected the particular structures and operation of their businesses and not impose any unnecessary administrative and reporting burden on investment partnerships.

## 3. Responses

- 3.1. In light of the responses to the consultation the government has made changes to some of the proposals. These are explained in detail in the following sections.
- 3.2. The government intends to introduce legislation in Finance Bill 2017-2018 to implement the proposed changes to taxation of partnerships from the 2018-19 tax year.

### Clarification of who is the partner chargeable to tax

- 3.3. This part of the consultation is concerned with the clarification of who is treated as a partner for tax purposes, and the associated issue of partners who act as 'nominee' for another person. Of the 43 formal written responses to the consultation document, 34 commented on this aspect.
- 3.4. Throughout this section we use the term 'nominee' to refer to bare nominees whose status is known to and accepted by their co-partners. This should not be confused with the 'nominated partner', who is the partner responsible for managing a partnership's tax returns and keeping business records.
- 3.5. In the published consultation Proposal 1 was "The government proposes that for tax purposes a person will be treated as a partner in a partnership if they are notified to HMRC as partners in the partnership return".
- 3.6. This wording caused some concern among respondents, some of whom queried whether HMRC intended that persons should be included in partnership returns even where they are not a legally-defined partner, or if HMRC intended to treat a person acting as an agent or 'nominee' for another person as the taxable person.
- 3.7. One of the primary concerns expressed by respondents was that, for various reasons, nominee relationships might be used in a partnership structure for purposes of administrative convenience, with no intent to cause a tax effect. Some respondents pointed out that this is particularly likely in the case of investment partnerships, where a nominee partner (which may be a company) might invest on behalf of investors.
- 3.8. As well as practical and administrative concerns several respondents pointed to confidentiality concerns as a reason why a nominee structure might be in place, and why a nominated partner may not know the details of persons ultimately entitled to the partnership profit. It was suggested by some respondents that legislation making these structures less workable could be disruptive for the investment sector. A significant minority of respondents agreed with the proposal as it stood in the consultation document.
- 3.9. Most respondents supported the need for greater clarity in the legislation on the status of nominees, but tended to disagree with the assertion in paragraph

2.4 of the consultation document that “the application of the current law is clear and that a partner cannot act in the capacity of a nominee or agent for another person.”

- 3.10. Those respondents who disagreed tended to fall into two groups. Firstly, those who disagreed that the application of the current law is clear. These respondents believed that there is a lack of legal clarity in this area. For example, one respondent wrote “We are not certain the current law is as clear as the government suggests.” Another commented that “many legal commentators argue that a partner can be a nominee for someone else”.
- 3.11. Other respondents, including a higher proportion of larger firms, believed that legislation or current practice explicitly accepts the use of nominee partners. Some within this group felt that the legislation provided for this practice.
- 3.12. More generally, the majority of respondents felt that the reporting and payment of tax in arrangements involving ‘bare trustees’ or ‘nominees’ should simply follow the general principles of tax law, so that the beneficiaries are the taxable persons.

### **Government Response**

- 3.13. The government recognises the importance of clarifying who should be reported on the partnership return. The government intends to legislate to ensure that the beneficiary of a nominee or bare trust arrangement is treated as a partner and expect that person to be named on the partnership return, as they are potentially liable to tax on their allocation of the profits of the partnership. HMRC will continue to expect the nominee to be reported on the partnership return to ensure that we have a complete picture of the structure.
- 3.14. This draft legislation will deal only with bare trust arrangements between a nominee and a principal. The government does not propose any changes to the treatment of trustees that stand to be taxed under the rules in Part 9 of the Income Tax Act 2007.

### **Business structures that include partnerships as partners**

- 3.15. This part of the consultation was concerned with structures where partnerships are themselves partners in partnerships. Of the 43 formal written responses to the consultation document, 34 commented on this aspect.
- 3.16. Proposal 2 in the consultation document was as follows: “The government is looking to legislate to provide that those responsible for paying the tax on a share of partnership profit are treated as partners in the first partnership for the purposes of income tax, capital gains tax and corporation tax. Details of the partners, including those treated as partners under these proposals, and their share of the partnership profit or loss will be reported by the nominated partner of the first partnership on the partnership return and statement for the first partnership.”

- 3.17. Overall the responses were mixed; many respondents agreed in principle with the proposed 'look-through' approach, whilst others raised concerns.
- 3.18. The first main area of concern was that this proposal would lead to increased administrative burdens for partnerships. Some respondents specifically raised concerns about the additional obligations that could be placed on the nominated partner.
- 3.19. Many respondents pointed to the requirement to include large numbers of partners under this proposal, with several respondents referencing the fact that, where a partner is itself a separate partnership entity, that partnership's own members may also be partnerships, and so on. Correctly identifying the individuals or companies at the top of these 'partnership chains' could place an onerous burden on the nominated partner.
- 3.20. There were also concerns about the need for nominated partners to identify the profit share ultimately allocated to each partner. As one respondent noted, "Even if all stakeholders involved [were] willing and able to share the required information, this may still be practically impossible in advance of the filing deadline considering the level of coordination and work required to this end."
- 3.21. Confidentiality of data was the other main area of concern. The view expressed was that nominated partners might not have access to data on partners throughout a 'chain' of partnerships for confidentiality reasons, and under this proposal, could not comply with their filing obligations and therefore be penalised unfairly.

### **Government Response**

- 3.22. The government has amended the proposals in the light of the concerns expressed by respondents. The government will not require the profit generating partnership to report the ultimate recipients of partnership profit through a partnership chain on its partnership return.
- 3.23. Current legislation obliges a partnership to provide details of all of its immediate partners and the allocation of profit or loss to those partners, on a partnership return.
- 3.24. To ensure that under this approach the correct taxable income can be established for any ultimate beneficiary taxable in the UK, the government intends to legislate such that:
- where a partnership includes a partner which is itself a separate partnership entity, it must report to HMRC the details of that partner, and provide to both HMRC and the partner computations of taxable profit on all 4 possible bases (UK-resident individual, non-UK resident individual, UK-resident company, non-UK resident company);
  - where the details of all the ultimate recipients of the second partnership profit have been provided to HMRC, the partnership will only have to prepare computations on the bases appropriate to those persons.

- 3.25. This approach will ensure that every recipient of partnership profit is able to return any UK taxable profit computed on the correct basis.
- 3.26. The government believes the amended approach will address the concerns raised in responses to the consultation; principally that the identification of the 'beneficial partners' through a 'chain' of partnerships placed a disproportionate administrative burden on partnerships. It will also address the concerns raised that nominated partners would need to identify the profit share ultimately allocated to each partner.
- 3.27. Please note that the above proposals will also be subject to the proposals discussed in the section entitled 'Investment income – tax administration' below.

### **Investment income – tax administration**

- 3.28. This section of the consultation was concerned with partnerships whose income is derived from investment (as opposed to trading/property) income. The consultation document proposed the question: 'How do you think the tax administration of partnerships with investment income could be improved?'
- 3.29. Of the 43 formal responses received to the consultation document, 30 commented on this chapter and on investment partnerships.
- 3.30. Almost all of these respondents agreed that improvements could be made to the tax administration of investment partnerships. Some noted that it was important to take account of the global nature of investment, with one legal respondent raising the importance of ensuring any clarifications place partnerships formed in the UK 'on an equal footing with structures available to the industry elsewhere in Europe'.
- 3.31. The main area of concern was that that the current reporting process and partnership returns do not cater specifically enough for investment partnerships and investment fund structures. There was particular emphasis on the reporting of items such as management expenses, non-trading loan relationships and property profits and losses that may be of limited relevance to investment partnerships.
- 3.32. In making suggested improvements some of the respondents noted that there was already a significant compliance burden for investment partnerships and that it was important that any changes did not increase this.
- 3.33. Some respondents suggested that a streamlined regime could apply to investment partnerships which are already reporting under the Common Reporting Standard (or CRS) established under the OECD exchange of information protocols. Other suggestions were made in relation to current UTR processes.

- 3.34. However, many of the responses received went further and suggested HMRC relax partnership tax return requirements for the following:
- Limited partnerships with no UK income and no UK partners;
  - Limited partnerships with no UK partners and only investment income;
  - Limited partnerships which are not controlled and managed in the UK;
  - Limited partnerships which are dormant

### **Government Response**

- 3.35. The government has considered the responses in detail. Whilst the government recognises that investment partnerships often have complex structures and that existing administrative arrangements could be improved, the government does not see this as sufficient justification for the added complexity of a separate administrative regime specifically for investment partnerships. The government will continue to provide just one form of partnership return and will continue to expect investment partnerships, along with trading and property partnerships, to provide partnership returns.
- 3.36. However, the government recognises that the reporting obligations on trading partnerships and investment partnerships have substantial differences. Investment partnerships are subject to other reporting obligations, notably the Standard for Automatic Exchange of Financial Account Information (known as the Common Reporting Standard (CRS)) of the OECD. The government understands that a requirement to report the same information to HMRC more than once increases the administrative burden for businesses, including partnerships, and aims to minimise the situations in which this happens. In doing so, our approach will more closely align with the responses to the consultation document and will take account of the global nature of the investment community reporting arrangements, making use of them to minimise the burden on affected partnerships.
- 3.37. The government intends that partnerships which are reporting financial institutions as defined by the OECD Common Reporting Standard and which have provided details of partners under CRS, will not be required to report the full details of those same partners on the partnership return (if they only receive investment profits). Rather than full details, the reporting financial institution will only need to provide on its partnership return the identity and profit allocation of each partner whose details are reported under CRS.
- 3.38. The majority of investment partnerships are subject to CRS as reporting financial institutions, and the suggestion was made in responses to the consultation that reporting under CRS could be the criterion which defines an investment partnership. Non-financial institutions do not report under CRS and will continue to report their partners in the usual way. A partnership required to report under CRS will still need to return all partners in receipt of trading and property income from the partnership and show their profit allocations.
- 3.39. Where any investment partnership does not report the details of all of its partners through obligations under CRS, the partnership must continue to report the details of other partners not reported through CRS in the same way

as other partnerships. In this way the government can ensure that it has the required information throughout the chain of partnerships.

- 3.40. The government considers that this approach will address specific issues which arose in the responses to the consultation. The administrative burden on investment partnerships will be lessened as any dual-reporting of those partners whose details are reported under CRS will be reduced. This aligns with the wishes of many respondents to the consultation.
- 3.41. Where a partnership reports the details of a partner under its CRS obligations any individual partner who has a UK tax liability in relation to their share of the partnership profits will continue to be obliged to report that to HMRC.

### **Trading and property income – tax administration**

- 3.42. This section of the consultation is concerned with partnerships whose income is derived from trading and property (as opposed to investment). Of the 43 formal respondents to the consultation document, 30 responded to this chapter.
- 3.43. Proposal 4 in the consultation document was as follows: “The government wishes to explore options for protecting the Exchequer where the details of partners entitled to trading or property business partnership profits are not provided by the partnership. One such option could include a payment being made on account to HMRC on behalf of any partners who are not identified.”
- 3.44. Only a few of the 30 respondents to this section were positive towards the implementation of a payment on account, with the remainder being either firmly against the proposal or having concerns about its implementation.
- 3.45. A few respondents argued that the payment on account proposal would increase rather than decrease the compliance burden on partnerships and targeted compliant partners and/or partnerships. It was suggested that HMRC should better use its existing powers rather than ‘outsourcing the burden of compliance to the firm or nominated partner’. Most responders suggested that government should seek to pursue the disclosure of information rather than enforcing a payment on account.
- 3.46. Some responses referred to informal work-arounds that are being used in relation to current reporting requirements.

### **Government Response**

- 3.47. The government has taken into account the responses to the proposal in the consultation. In response, the government does not currently intend to pursue the option of requiring a payment on account in situations where reporting requirements are not complied with.

- 3.48. With the changes being made to reduce current reporting requirements for investment partnerships also reporting under CRS, the government considers it is reasonable to expect all partnerships to know who its partners are, and to be able to report those partners (along with their UTRs where applicable) to HMRC. Where this is not the case, the current process and penalty provisions for incomplete and late submission of partnership returns will continue to apply.

### Allocation and calculation of partnership profit

- 3.49. Of the 43 formal respondents to the consultation document, 34 responded to this chapter. The chapter made 3 proposals on which respondents were invited to comment.
- 3.50. Proposal 5: “In order to provide certainty, the government considers that legislation should be introduced to confirm that the profit sharing arrangements as set out in the partnership or LLP agreement are the determining factor in identifying the partners’ profit shares. However, in order that the flexibility of partnerships is maintained this proposed default position could be overridden by notification to HMRC from the nominated partner of the partnership or LLP, in either written or electronic format, of any changes to this agreement.”
- 3.51. Proposal 6: “Legislation would be introduced to provide that the basis of allocation of tax adjusted profit should be the same as the allocation of the accounting profit or loss between the partners. This legislation would apply to both partnerships and LLPs. Partners or members would only share in profits or losses for the period in which they were partners or members.”
- 3.52. Proposal 7: “Legislation would be introduced to provide that the profits of company partners liable to income tax will be calculated as if a non- UK resident company were carrying on the business.”
- 3.53. In response to whether the proposed clarifications would provide certainty of treatment, some of the respondents were positive and in agreement with the proposals. Most, however, disagreed and stated the proposal would not provide the clarity expected.
- 3.54. Concern was based mainly around the flexibility of partnerships as a business structure. It was for this reason that many businesses chose a partnership structure.
- 3.55. There was a general feeling on the part of many respondents that the profit sharing arrangements proposal (proposal 5) placed undue responsibility and influence on the nominated partner at times of dispute, especially with the potential to override a profit-sharing arrangement by notification to HMRC. One legal consultee stated that the provisions should not ‘substitute the nominated partners for HMRC as an alternative, unofficial arbiter for tax purposes.’ In times of dispute it was felt that an appeal process should be

available for when an individual partner disputed the amounts provided by the nominated partner.

- 3.56. Regarding allocation of tax adjusted profit to partners (proposal 6), many respondents stated that partnerships are not legally bound to have a written partnership agreement and that profit sharing arrangements are commonly agreed informally even when a partnership agreement has been prepared. Such decisions may be made on a period-by-period basis, on the basis of performance, or by a remuneration committee. The view was also expressed that it is common for changes to be made to the profit sharing arrangements without partners being aware. Respondents felt it was important that partnerships should be able to retain these commercial practices.
- 3.57. The suggestion was made by a few respondents that if the government is concerned about a significant tax loss the government should consider targeted anti-avoidance legislation to 'focus on tax motivated allocations but otherwise leave commercial profit sharing arrangements unaffected for tax purposes.'
- 3.58. There was only a limited response to proposal 7 (on companies liable to income tax), that was generally in support of the proposal in the consultation document.

## **Government Response**

### Profit sharing arrangements (proposal 5)

- 3.59. The government has considered the responses to proposal 5, and noted the concerns regarding written partnership agreements and the potential burden of notifying changes to HMRC.
- 3.60. The government considers that it is reasonable to expect partnerships to know who their members are and the allocation of profit between them, and wishes to achieve certainty over the tax position of partners in situations where there is an inter-partner dispute over profit allocation. However, the government does not wish to reduce the flexibility with which partnerships can dictate their own profit sharing arrangements.
- 3.61. Where a partnership has been required to make a partnership return, that return must identify each partner and their respective allocation of taxable profit, as determined by reference to the firm's profit-sharing arrangements. The profit allocation stated in the partnership return will then be the first point of reference for HMRC in determining the taxable profits of each partner.
- 3.62. Where the allocation of profits between partners reported on the partnership return is disputed, the Government intends to legislate to protect the partners from being taxed on incorrect profit shares. This is a different approach to that originally consulted on, and we feel that this more closely matches the outcomes which partners expect and the views expressed in responses to the consultation.

- 3.63. This will continue to protect the rights of the person against being liable to tax on a share of the partnership profits, in circumstances where they are not, as a matter of fact, entitled to those profits as a partner. This is a different approach to that originally consulted on, and we feel that this more closely matches the outcomes which partners expect and the views expressed in responses to the consultation.
- 3.64. There will be no requirement for partnerships to notify HMRC of changes in their profit sharing arrangements.

#### Allocation of tax adjusted profit to partners (proposal 6)

- 3.65. The government acknowledges the value of flexibility in the allocation of profit to partners. We do not wish to undermine this flexibility. We want to reduce the scope for allocating profits for purely tax-motivated purposes, and will do so in the following ways:
- Clarifying how to apply a firm's profit-sharing arrangements consistently in allocating taxable profits among the partners, including in cases where different partners' taxable profits are computed on different bases
  - Legislation will provide that any retrospective variation to a partnership's profit-sharing arrangements made after the period-end will not apply.
  - Where a partner joins or leaves a partnership during an accounting period, we will provide that such partners would be treated as taxable on their share in profits or losses that arose during the period in which they were partners or members. The profit arising during the part of the accounting period when a person is a partner should be used as a basis and the allocation agreement in force at that time (the time of their joining the partnership) will be applied to that proportion to determine the partner's share of taxable profit.
- 3.66. These changes will prevent partnerships from diverging for tax purposes from the allocations set out in a partnership agreements. We do not want to restrict any partnership's ability to allocate profits between partners on a commercial basis.

#### Companies chargeable to income tax (proposal 7)

- 3.67. With regard to companies chargeable to income tax, the government intends to legislate to provide that the profits of firms which have a company partner chargeable to income tax are calculated as if a non-UK resident company was carrying on the business. This aligns with the responses to the consultation document - most respondents found this to be a sensible approach to address this issue.

3.68. This part of the proposal is subject to the government consultation on Non-resident Companies Chargeable to Income Tax and Non-resident Capital Gains Tax: March 2017.

## 4. Next steps

- 4.1. The government believes that the changes outlined in this document are necessary steps towards achieving its aims of greater clarity and the removal of uncertainty for partnerships over their tax affairs.
- 4.2. The government is grateful for all the responses to the consultation which have informed the development of the proposals originally set out in the consultation document.
- 4.3. It is the government's intention that legislation will be included in the second Finance Bill 2017 and that the changes will apply to returns for accounting periods starting on or after 5 April 2018.
- 4.4. Draft Finance Bill clauses are being published for consultation at a later date after this summary of responses.
- 4.5. The government recognises that businesses will require clear information and intends to work closely with interested parties, including partnership businesses themselves, to develop and road test effective guidance with businesses and agents.

# Annexe A: List of stakeholders consulted

Association of Accountancy Technicians  
Association of British Insurers  
Alternative Investment Management Association  
Association of Partnership Practitioners  
BDO LLP  
Berg Kaprow Lewis  
BlackRock  
British Property Federation  
Burness Paull LLP  
British Venture Capital Association  
City of London Law Society  
Crowe Clark Whitehill  
Deloitte LLP  
Ernst & Young LLP  
Freshfields  
FTI Consulting  
Goodman  
Institute of Chartered Accountants of England and Wales  
Institute of Chartered Accountants of Scotland  
Johnston Carmichael  
Kingston Smith LLP  
KPMG LLP  
The Law Society of Scotland  
The Law Society of England and Wales  
Low Income Tax reform Group  
London Society of Chartered Accountants  
Moore Stephens  
The Office of Tax Simplification  
Oxfam  
PriceWaterhouseCoopers  
Roderick L'anson Banks  
RSM  
Simmons & Simmons LLP  
Slaughter & May  
Smith & Williamson  
TriplePoint  
Weil Gotshal & Manges

7 Individuals also contributed to the consultation