THE LIMITED PARTNERSHIP

A UK vehicle for non-residents with non-UK income

by Milton Grundy and Michael Thomas[1]

The statutory provisions governing the tax liability arising on the income of a partnership – whether general or limited – are to be found in ss.111 and 112 of the Income and Corporation Taxes Act 1988. The partnership is not treated as an entity which is separate and distinct from the partners, and liability to tax only arises if the partners are chargeable to income tax by reference to their share in the partnership income. If therefore the partners are all non-resident and the income does not have a UK source, no liability to tax arises. It is not generally difficult to determine whether or not an item of income has a UK source; in this context, one has to remember that income arising from the carrying on of a trade in the United Kingdom has a UK source even if all the customers are overseas. Whether or not a trade has been carried on in the United Kingdom is – in that unhelpful phrase of which lawyers are so fond – a question of fact in each case. The test is, "Where do the profits really arise?" and an important fact is where the contracts are made: in the circumstances contemplated, the partnership should be prepared to offer evidence that the contracts it makes are made outside the United Kingdom. Strictly, there would be no harm in one or more partners seeing a customer in the United Kingdom, but since such a meeting might be taken – in the event of a disputed claim – to be evidence of the carrying on some part of the trade in the United Kingdom, this is

something to be avoided. Partnerships have a similar transparency for inheritance tax purposes, so that if the partnership assets are situated outside the United Kingdom and an individual partner is not domiciled in the United Kingdom, no charge to inheritance tax arises on his death. Partnerships are also transparent for capital gains tax purposes (Taxation of Chargeable Gains Act 1992, s.59), so that provided the partners are all non-resident and no trade is carried on through a branch or agency in the United Kingdom, the use of a limited partnership would not give rise to any charge to capital gains tax. Although non-residents are not (in general) liable to capital gains tax on the disposal of assets situated in the United Kingdom, they are subject to income tax on income which arises in the United Kingdom, so that if the limited partnership had UK-source income, each of the partners would be taxable on his share of it. It follows from this general fiscal transparency that distributions to partners are immaterial. An initially surprising result of the fiscal transparency of partnerships is that the concept of "management and control" has no relevance to partnerships, and, so long as all the partners are non-resident and the partnership does not have any UK-source income, it makes no difference whether or not the partners hold meetings in the United Kingdom.

The statutory provisions affecting all partnerships – limited as well as general – are to be found in the Partnership Act 1890. The Act is merely declaratory, and, except insofar as they are inconsistent with the express provisions of the Act, the rules of equity and of

common law applicable to a partnership are still in force. A limited partnership is also governed by the Limited Partnerships Act 1907. A limited partnership requires to be registered with the Registrar of Companies. There are separate registries in England, Scotland and Northern Ireland, and the appropriate one is in that part of the United Kingdom in which the principal place of business of the limited partnership is situated or proposed to be situated. There is a trifling registration fee and there are no annual fees. The partners send a signed statement to the Registrar, which includes particulars of the sums contributed by each of the limited partners, and whether paid in cash or how otherwise. This is open to public inspection, on payment of a small fee. A limited partnership does not have legal personality, except in Scotland – see Partnership Act 1890, s.4(2). It is not unlawful for the limited partners to participate in the management of a limited partnership, but if they do so they lose their limited liability. A general or limited partner can be any individual, wherever resident, or any company, wherever incorporated. The signed statement filed with the Registrar must contain particulars of the principal place of business of the limited partnership, in England, Scotland or Northern Ireland, as the case may be. The draftsman does not appear to have contemplated that a limited partnership would in practice carry on all its business outside the United Kingdom, but nothing in the Limited Partnership Act prohibits it from doing so. It is considered, therefore, that the principal place of business specified in the statement lodged with the Registrar is the place at which, if any business were to be carried on in the jurisdiction, such business would be

carried on. This is, of course, an important point, because – as appears from what is said above about the tax position – if a limited partnership if it were to carry on a trade in any part of the United Kingdom, a liability to UK tax would arise.

The essence of the partnership – whether general or limited – is a contract between the partners to engage in a business with a view to profit. Mere co-ownership of property does not, of itself, give rise to a partnership between the co-owners, whether or not they share any profits made by the use of it. The decided cases are replete with examples of facts which fall just on one side of the border or the other, but in practice the distinction between an active business and passive investment is plain. Confusingly, a limited partnership is a "collective investment scheme" for the purposes of the Financial Services Act, but this simply means that interests in the limited partnership cannot be offered for sale to the public without the compliance with the provisions of the Act, and does not bear on the question, whether there is a true partnership or a mere co-ownership of assets. Mutual funds are not established as limited partnerships but either as unit trusts or as companies.

It is unlawful for a person who has a place of business in Great Britain and carries on business there to do so (without Government approval) under a name which would be likely to give the impression that the business is connected with Her Majesty's Government, any part of the Scottish Administration or any local authority (Business Names Act, 1985). These provisions

do not of course apply in the circumstances contemplated, but it is considered that the Registrar would not register a limited partnership whose name would be prohibited by the Act. Only a limited company can include "Ltd" or "PLC" (or their full versions) in its name (Companies Act 1985. ss.33 and 34). Otherwise, a limited partnership can carry on business under whatever name it pleases. If all the partners are companies, the limited partnership must have audited accounts and these are open to public inspection (Partnerships and Unlimited Companies (Accounts) Regulations, SI 1993/1820, implementing EC Directive 90/605. Subject to some exceptions, which are not material here, the number of partners in any partnership – whether general or limited – cannot exceed twenty.

Some practitioners outside the European Union have been concerned that the use of a limited partnership formed in accordance with the Limited Partnership Act for the supply of services may expose the partners to value added tax on the grounds that the partnership "belongs" in the United Kingdom – Value Added Tax Act 1994, s.7(10). But for a partnership to be treated as belonging in the United Kingdom it must have a business establishment or some other fixed establishment in the United Kingdom – see Value Added Tax Act 1994, s.9(2), and this will not be the case in the circumstances contemplated.

A UK limited partnership is registered in the United Kingdom. It has a UK address and a registration number. As a tax-transparent vehicle, it has particular

appeal to trusts and companies established in offshore jurisdictions. In some onshore jurisdictions, a payment to a "tax haven" company is disallowed as a deduction. In others, it is the occasion for an investigation. But even where the consequences are less specific, one can find that one or more parties to a transaction simply do not want to participate, if an offshore company is involved. Such considerations have stimulated the search for cosmetic alternatives to the offshore company – a vehicle which attracts little attention and is on nobody's blacklist. And it is here that the fiscal transparency of the UK limited partnership is particularly advantageous.

[1] An earlier version of this article appeared in *The Limited Partnership*, edited by Milton Grundy (International Tax Planning Association, 2001).