

CRA updates its position on US LLLPs and LLPs

May 2017

On April 26, 2017, the Canada Revenue Agency (CRA) announced that it will offer “administrative grandfathering” for Canadian taxpayers who hold an interest in Florida and Delaware Limited Liability Partnerships (LLPs) or Limited Liability Limited Partnerships (LLLPs). Previously, the CRA was of the view that such LLPs or LLLPs had to be treated as corporations both prospectively and retroactively. However, having considered the complexities and administrative issues arising from the transition from partnership filings to corporate filings, as would have been previously required by their earlier administrative announcement made in May 2016, the CRA—subject to the conditions outlined below—will allow LLPs and LLLPs to continue to be treated as a partnership for Canadian tax purposes.

Transitional relief

The CRA’s administrative grandfathering allows existing LLPs and LLLPs to be treated as partnerships (rather than corporations, as was required under its May 2016 announcement) for Canadian tax purposes provided that the LLP or LLLP was formed before April 26, 2017 and none of the following conditions are met:

- one or more members of the entity, or the entity itself, takes inconsistent positions from one taxation year to another, or for the same taxation year, as between partnership or corporate treatment;
- there is a significant change in the membership or the activities of the entity; or
- the entity is being used to facilitate abusive tax avoidance.

Should any of these conditions apply, the CRA *may* issue assessments on the basis that the entity (LLP or LLLP) is a corporation. This is a more practical solution than was originally proposed in May 2016, and later updated in November 2016, that would have required case-by-case relief having sought permission from a CRA working group to file as a corporation going forward without having to amend prior year returns that would have been filed in respect of the LLP or LLLP being considered to be a partnership.

At this point, it is unclear whether the requirement for consistency of positions and membership applies equally to non-arm’s length residents and non-residents, and arm’s length residents and non-residents. That is, a given taxpayer may have no control over the characterization of an LLP and LLLP interest of another investor, particularly if that investor is an arm’s length non-resident of Canada. Similarly, it is also unclear whether a change in ownership by an arm’s length party or an expansion of the business would prevent access to the administrative grandfathering, again, particularly where the changes are beyond the control of the particular taxpayer. While it is hoped that the actions of arm’s length parties should not prevent access to the administrative relief, we expect more certain answers to these issues as the CRA works through the implementation of the relief above in upcoming months.

Notwithstanding the above, any LLP or LLLP that has consistently filed as a corporation must continue to do so for both prior and future taxation years. This may require amended filings to prior period returns for both the entity and the partners. In addition, for any LLP or LLLP treated as a corporation for Canadian tax purposes, the CRA will afford the same treatment as a LLC for the purposes of Article IV(6) of the Canada-U.S. Tax Treaty, as well as apply section 93.2 in the same manner as applied to LLCs. While dependent on the facts, treatment as a corporation may prove advantageous in mitigating filing obligations for large groups of investors, provided access to the Canada-U.S. Treaty is readily determinable.

How we can help

If you have invested in a US LLLP or LLP, this new administrative position may provide certain relief in respect of your investment. We can help determine whether you qualify for relief under the CRA's most recent administrative position and whether a restructuring option makes sense in your situation. If you would like to learn more about this matter, please consult your tax advisor.

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