


***IT 2277 - Income tax: partners seek to provide their service to their partnership through interposed company or trust***

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TAXATION RULING NO. IT 2277

INCOME TAX: PARTNERS SEEK TO PROVIDE THEIR SERVICE TO  
THEIR PARTNERSHIP THROUGH INTERPOSED COMPANY OR TRUST

F.O.I. EMBARGO: May be released

REF

H.O. REF: 85/3049-1

DATE OF EFFECT:

B.O. REF: VJ 77/1 Pt. 3

DATE ORIG. MEMO ISSUED:

F.O.I. INDEX DETAIL

REFERENCE NO:	SUBJECT REFS:	LEGISLAT. REFS:	
I 1077849	PARTNERSHIP	82AAC	82AAK
	EMPLOYMENT	82AAD	82AAL
	SUPERANNUATION	82AAE	82AAM
	SERVICE, PRACTICE AND	82AAF	82AAN
	ADMINISTRATION	82AAG	82AAP
	COMPANIES AND TRUSTS	82AAH	82AAS
		82AAI	82AAT
		82AAJ	

PREAMBLE

By virtue of sections 82AAT and 82AAS of the Income Tax Assessment Act self-employed persons and employees not covered by employer-sponsored superannuation may be allowed income tax deductions up to \$1,500 per year for contributions made to a qualifying superannuation fund in a year. Other provisions in the income tax law provide for the exemption from income tax of the income of qualifying superannuation funds.

2. Sections 82AAC and 82AAD provide income tax deductions for contributions made by employers to superannuation funds established and maintained by them for the benefit of employees. The deductions allowable to an employer may exceed \$1,500 per year in respect of particular employees. Exemption from income tax is also provided for employer sponsored superannuation funds.

FACTS

3. This office had occasion recently to consider the operation of the provisions in the income tax law relating to contributions to superannuation funds in relation to an arrangement by which partners in a number of continuing partnerships seek to provide their services to their partnerships. The arrangement requires partners in a business operation to incorporate a company the sole shareholders in which are the partners. The sole purpose of the company is to provide the services of the partners, as employees of the company, to the partnership to conduct the partnership business. The company does not own any property nor does it have any interest in the partnership business - the partners continue to own the partnership assets and are required by the partnership agreement to conduct the partnership business.

4. The company pays "wages" to the partner/employees and



contributes to an employer-sponsored superannuation fund on their behalf. It receives a balancing amount from the partnership and thus has no taxable income. As a practical matter the arrangement seeks to convert what the partners might otherwise obtain as a distribution of partnership profits into a salary paid by the company. The purpose of the arrangement is to obtain income tax deductions for superannuation contributions in excess of the amount of \$1,500 per partner which would have been allowable had the arrangements not been entered into.

RULING

5. The arrangements are not acceptable for income tax purposes. It has been suggested that they are no different from a service company or trust arrangement, an administration arrangement or a practice company arrangement.

6. The ordinary service company or trust is illustrated in the decision of *FCT v Phillips*, 78 ATC 4361 : 8 ATR 783. A family company or trust is created to carry on a business of providing services to a partnership. The services may include the provision of premises, plant, equipment, clerical services and so on. Where the service arrangement is a commercially realistic one it is acceptable for income tax purposes. What is important to note is that an ordinary service company or trust does not employ the partners and provide their services to the partnership to carry out duties which the partners are required to carry out under the terms of the partnership agreement.

7. An administration company is one which provides administration services to a professional partnership. Partners may be employees of an administration company but they are only paid salaries by the administration company in respect of administrative services provided to the partnership. In the generality of cases salaries received by partners as employees of administration companies are only a fraction of what the partners might otherwise receive as a distribution of partnership profits.

8. A practice company arises where a business formerly conducted by a sole trader or partnership is taken over by a company created for the purpose. The sole trader or partners are then employed by the company. This is an ordinary commercial or business step to take.

9. The arrangements to which this Ruling refers are neither service company or trust arrangements nor administration company arrangements nor practice companies. Indeed, for various reasons it is not commercially practicable to incorporate the business activity in a number of cases to which the arrangements apply. The essence of the arrangements is an attempt by partners to employ themselves - it is considered to be ineffective both at general law and for income tax purposes.

10. In the result payments made by the companies to partners, ostensibly as salaries, should be treated as distributions of partnership profits and any income tax deduction for superannuation contributions reduced to \$1,500 per year per partner, i.e. the same as any other self-employed



person. Every assistance will be extended by this office to make sure that the relevant superannuation funds comply with the requirements of the income tax law so as to preserve exemption from income tax.

COMMISSIONER OF TAXATION

9 April 1986

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