



IT 2608 - Income tax: assignment of partnership interests

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 Note: ATO guidance on the potential application of Part IVA to assignments entered into after 30 June 2015 and certain other assignments is set out in [Everett assignments](#).

TAXATION RULING NO. IT 2608

INCOME TAX: ASSIGNMENT OF PARTNERSHIP INTERESTS

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| Reference no.: | Subject refs: | Legislative refs: |
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| I 1012315 | ASSIGNED PARTNERSHIP | 51 |
| | INCOME DEDUCTIONS | 90 |
| | ASSIGNMENT OF INCOME | 92 |
| | DISSOLUTION OF PARTNERSHIP | |

OTHER RULINGS ON THIS TOPIC: IT 2003, IT 2330, IT 2501, IT 2540

PREAMBLE

In Taxation Ruling IT 2501, it was stated that valid assignments of a partnership interest on all fours with the decisions of the High Court in *FCT v. Everett* (1980) 143 CLR 440; 80 ATC 4076; 10 ATR 608 and *FCT v. Galland* 86 ATC 4885; 18 ATR 33 will be accepted as effective for tax purposes.

2. This Ruling deals with two issues that arise in relation to such valid assignments. The first issue concerns the deductibility of expenses and losses relating to an assigned partnership interest. The second issue involves the effect of a partnership dissolution on an assignment.

RULING

A. Allowance of Deductions on Assigned Interests

3. Where a partner assigns a share of an interest in a partnership expenses incurred by the assignor partner in connection with the partnership may have to be apportioned in order to determine the deduction allowable to the assignor. Where the expenditure incurred relates to the partner's proportionate interest in the partnership, a deduction is only allowable to the assignor partner for the share of the partnership interest not assigned. For example, a partner who assigns one-third of his interest in the partnership would only be entitled to a deduction for two-thirds of interest expenditure incurred on borrowings used to purchase the interest in the partnership.

4. However, where the expenditure incurred by the assignor partner is unrelated to the partner's proportionate interest in the partnership, a deduction is allowable in full. Examples of such expenditure include subscriptions to professional publications, travel expenses and depreciation of the partner's personal professional library. This type of expenditure would be incurred by a partner irrespective of what share, if any, of the

partnership interest is assigned.

5. Whether any deduction is to be allowed for expenses referable to the assignee's share of the partnership income will depend upon the particular circumstances. It is clear from the decisions of the High Court that income flowing from the assigned interest in the partnership is income of a trust estate - comprising the assigned interest - for the purposes of Division 6 of the Income Tax Assessment Act 1936 (the Act). Under trust law a trustee is entitled to an indemnity from the trust estate in respect of expenses incurred in respect of the property held on trust (see Halsburys Laws of England Volume 48 paragraph 776). Where the assignor is reimbursed for expenses incurred as a trustee, deductible expenses referable to the income arising from the assigned interest should be taken into account in determining the net income of the trust estate in accordance with section 95 of the Act.

6. If the assignor is not reimbursed from the trust estate and the amount received from the trust by the assignee is not reduced by expenses incurred by the assignor, the assignee is assessable on the full amount received from the trust. However, an assignee will be entitled to claim deductible expenditure incurred by the assignee in connection with the income arising from the assigned interest.

Partnership Losses

7. In Everett (supra) the High Court held that a partner's fractional interest in a partnership is an entire chose in action which is capable of division by assignment into further fractions. The entitlement to share in profits, the Court said, could not be separated or severed from the interest of the partner (143 CLR 440 at 450; 80 ATC 4076 at 4081; 10 ATR 608 at 613). Similarly it would seem to follow that the liability to share in losses also attaches to the partnership interest and cannot be separated or severed from that interest (see Case Q53 83 ATC 285 at 287; 26 CTBR(NS) Case 123).

8. Accordingly, where the partner's interest is the subject of an assignment, the share of a partnership loss attributable to the assigned interest is deductible to the assignor in the capacity as trustee for the trust estate of the assigned interest. The loss is taken into account in determining the net income of the trust estate in accordance with section 95 of the Act. This effectively means that the trust estate will incur a loss which will be carried forward and applied against trust income in future years. No deduction is allowable to the assignee in the year in which the partnership loss is incurred.

B. Effect on Assignment of Dissolution of a Partnership

9. In cases that have come to the attention of this Office there has invariably been a clause in the partnership agreement to the effect that the partnership is not to be dissolved by the death, retirement or expulsion of one or more of the partners. The

presence of such a clause requires the surviving partners to reinvest their interests in the existing partnership in the reconstituted partnership.

10. Similarly deeds of assignment have included a clause which authorises the assignor as trustee to reinvest the assigned portion of a partnership interest in a new partnership should the existing partnership be dissolved or reconstituted for any reason. In addition, some deeds have contained a provision for a confirmatory conveyance to be made by the assignor to the assignee of the interest in the reconstituted partnership. This confirmatory conveyance will also usually contain a declaration of trust in favour of the assignee.

11. It has been suggested that, whilst not affecting the effectiveness of the present assignment, a clause requiring reinvestment of the assigned portion of the partnership interest would require, on the reconstitution of the partnership, the execution of a further deed of assignment assigning a portion of the assignor's interest in the reconstituted partnership. On a proper analysis of the situation this is not considered to be the correct conclusion.

12. As mentioned in paragraph 5, it is clear from the decisions in Everett and Galland (supra) that where there has been an assignment of a portion of an interest in a partnership the assigned interest is held on trust for the assignee. At the point of dissolution the assignee has an equitable interest in the appropriate portion of the surplus of the assets over liabilities of the old partnership. The reinvestment by the assignor partner of the interest in the old partnership into the new partnership would seem to compel the conclusion that the interest in the new partnership is fixed with the same trusts. The assignee therefore would be entitled to the same share of the partner's income from the reconstituted partnership as was the case in the former partnership.

13. Where at the time of the creation of the new interest the assignor executes a conveyance confirming that the assigned interest is subject to the obligations contained in the original deed of assignment and the trust therein created, it could well be argued that the confirmatory conveyance itself operates as an effective assignment of "present property" i.e., the interest in the reconstituted partnership.

14. Having regard to the above, it is considered that arrangements which provide for a reinvestment of the assigned partnership interest in a reconstituted partnership are effective for taxation purposes. It will be accepted in such cases that there will be no need to execute a further deed of assignment where changes occur in the constitution of a partnership.

COMMISSIONER OF TAXATION
23 August 1990