


# ***TR 2005/7A1 - Addendum - Income tax: the taxation implications of 'partnership salary' agreements***

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# Addendum

## Taxation Ruling

### Income tax: the taxation implications of 'partnership salary' agreements

This Addendum is a public ruling for the purposes of the *Taxation Administration Act 1953*. It amends Taxation Ruling TR 2005/7 to include the taxation consequences of a partner's salary where the partnership is a corporate limited partnership.

#### TR 2005/7 is amended as follows:

##### 1. Paragraph 3

Insert after the paragraph:

3A. Additionally, this Ruling explains the implications of a 'partnership salary' in the context of a limited partnership<sup>1</sup> that is a corporate limited partnership.<sup>2</sup>

##### 2. Paragraph 7

Insert after the paragraph:

7A. Similarly, a 'partnership salary' is not an allowable deduction for the purposes of a corporate limited partnership<sup>3</sup> (CLP) under Subdivision C of Division 5A of Part III of the ITAA 1936.

##### 3. Paragraph 9

Insert after the paragraph:

9A. In the case of a CLP, section 94K of the ITAA 1936 specifically excludes the application of Division 5 of the ITAA 1936 provisions from applying. Instead, Division 5A of the ITAA 1936 applies such that if the partnership pays or credits an amount to a partner in the partnership against the profits or anticipated profits, the amount is taken to be a dividend<sup>4</sup> paid to the partner out of profits<sup>5</sup> and assessable to the partner pursuant to section 44 of the ITAA 1936.

<sup>1</sup> The term 'limited partnership' is defined in subsection 995-1(1) of the *Income tax Assessment Act 1997*.

<sup>2</sup> See section 94D of the ITAA 1936 for the meaning of the term 'corporate limited partnership'.

<sup>3</sup> Refer to section 94D of the ITAA 1936 for the description of what constitutes a CLP.

<sup>4</sup> The term 'dividend' is defined in subsection 6(1) of the ITAA 1936.

<sup>5</sup> See section 94M of the ITAA 1936.

## 4. Paragraph 13

Insert after the paragraph:

13A. The income from a CLP is not taxed to the partners. The scheme of Division 5A of the ITAA 1936 is that the partnership is treated as a company for certain taxation purposes and consequently the taxable income of the CLP is taxed as a company.<sup>6</sup>

## 5. Paragraph 18

Insert after the paragraph:

18A. For the same reasons, a 'partnership salary' is also not characterised as an expense of a CLP when calculating the net income of the CLP.

## 6. Paragraph 23

Insert after the paragraph:

23A. Sections 94L and 94M of the ITAA 1936 specifically address the taxation consequences of payments, credits and distributions made to a partner in a CLP.

23B. Section 94L of the ITAA 1936 includes a distribution, whether money or property, to a partner in a CLP, as a dividend, but not if the distribution is attributed to profit or gain from a year when the partnership was not a CLP.

23C. Likewise, section 94M of the ITAA 1936, deems that where a CLP pays or credits a partner from profits, anticipated profits, or otherwise in anticipation of profits, the amount is taken to be a dividend paid out of profits derived by the partnership.

23D. A salary paid to a partner in a CLP is not necessarily paid from profits and may be paid in anticipation of profits. In applying section 94M of the ITAA 1936, such payments are considered a distribution of profits and will be taxed as a dividend.

23E. Consequently payment of salary to a partner of a CLP will be assessable income and subject to taxation as dividends under subsection 44(1) of the ITAA 1936.

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<sup>6</sup> See section 94J of the ITAA 1936.

23F. Where the CLP makes a distribution of profits which includes an amount previously paid or credited in anticipation of such profits, the Commissioner must take such steps, if any, to ensure that a partner is not subject to double taxation (subsection 94M(2) of the ITAA 1936). This ensures that if a partner has been taxed on a distribution when it was credited, the partner will not be taxed again when the distribution is actually paid.

## **7. Legislative references**

Insert:

- ITAA 1936 6(1)
- ITAA 1936 44
- ITAA 1936 44(1)
- ITAA 1936 Pt III Div 5A
- ITAA 1936 94D
- ITAA 1936 94J
- ITAA 1936 94K
- ITAA 1936 94L
- ITAA 1936 94M
- ITAA 1936 94M(2)
- ITAA 1936 92(2)
- ITAA 1997 995-1(1)

This Addendum applies on and from the date of issue.

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**Commissioner of Taxation**

5 November 2014

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ATO references

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