

Canada Revenue Agency expands relief for Canadian taxpayers with US LLLPs and LLPs

Elan Harper MBA
April 28, 2017

During the Canada Revenue Agency (CRA) roundtable at the International Fiscal Association (IFA) conference in Toronto earlier this week, the CRA announced “administrative grandfathering” for some Canadian taxpayers with investments in US Limited Liability Limited Partnerships (LLLLPs) and US Limited Liability Partnerships (LLPs). Practically, this announcement will allow some Canadians who hold investments in US LLLPs and LLPs formed prior to April 26, 2017, to continue to treat these entities as partnerships on a go-forward basis. The CRA indicates that this additional relief resulted from the submissions which have been received by the CRA and the apparent complexities of transitioning from a partnership to a corporation.

It was a year ago at the 2016 IFA conference where the CRA announced its conclusion that US LLLPs and LLPs should be treated as corporations for Canadian tax purposes, rather than as partnerships – like they are in the US. While this helped clarify the treatment of these entities, this announcement raised new issues for affected taxpayers, as discussed in our May 27, 2016, [blog](#). And, as we reported on [December 1, 2016](#), the CRA extended some relief with their announcement at the Canadian Tax Foundation conference in November 2016, by indicating that some of these entities (on a case by case basis after applying to a special CRA working group) could simply begin to file as corporations going forward, rather than having to go back and amend prior year filings.

The CRA’s most recent announcement of administrative grandfathering is a welcome accommodation for taxpayers but comes with some conditions. Firstly, the grandfathering is for Delaware or Florida LLPs or LLLPs^[1] formed prior to April 26, 2017, provided that they have not:

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

Where the above conditions do apply, the CRA *may* assess the taxpayer and/or the entity for one or more taxation years, on the basis that the entity is a corporation. US LLLP and LLPs, which have consistently filed as a corporation for Canadian income tax purposes, may continue to file as corporations and where a Canadian taxpayer files as if they hold an interest in a corporation then they will be required to do so both retroactively and prospectively for all taxation years. Additionally, the CRA clarified that these entities will fall under paragraph IV(6) of the Canada – US Income Tax Treaty which provides for limited applicability of this treaty for some hybrid entities.

We applaud the CRA’s ongoing efforts to treat Canadian taxpayers with the utmost fairness, but as often happens, a new announcement raises some additional questions for taxpayers. Unfortunately, announcing this relief days before the personal tax filing deadline for Canadians provides little time for answers.

Given the CRA's initial pronouncement on May 28th, 2015, (as described in our June 1, 2015 [blog](#)) that in all likelihood they were going to classify these entities as corporations, many conservative taxpayers started filing their Canadian taxes accordingly – as if their investment in a US LLLP or LLP was, in fact, an investment in the shares of a corporation. The most obvious sign of a taxpayer who has taken this filing position would be that they reported their holdings on a T-1134 form. If taxpayers have reported their US LLLP or LLP on a T-1134 form, then they are likely not eligible for the administrative relief described above. In this case, we would advise taxpayers to consider approaching the CRA working group for special consideration. Clearly, these taxpayers were trying to comply with the evolution taking place in respect of these entities, and we hope that the CRA will recognize this.

Interestingly, if the tax reforms proposed by US President Trump are implemented, the US partners of these LLLPs and LLPs may no longer care what type of entity they hold. Under the Trump proposals, corporate and personal taxes on business income would be integrated to a 15% tax rate, with the result that – at least from a tax perspective – Americans would be indifferent as to whether they invested in a corporation, a partnership, or some other type of flow through entity.

Stay tuned... this issue will continue to evolve with events both north and south of the 49th Parallel having an impact.

[\[1\]](#) The CRA has stated that the grandfathering will also apply to LLLPs and LLPs in other US states.