Characterization of Other States' Partnerships for Income Tax

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1. INTRODUCTION

1.1. The OECD Partnership Report

The OECD Partnership Report\(^1\) is a significant contribution to the discussion of how to treat partnerships for tax treaty purposes when two states categorize a partnership-like entity or body differently, either as transparent\(^2\) or as opaque. This article examines why different treatment of other states' bodies (to use a neutral term) for tax purposes can arise, particularly from the way in which states classify foreign bodies, thus giving rise to part of the problem addressed by the OECD Partnership Report. The focus of this article is more on categorization of partnerships than on differences in tax treatment, which is the main focus of the OECD Report.

1.2. Methods of characterization of bodies for income tax purposes

Categorization of a body for income tax\(^3\) purposes is needed by the source state in which another state's body is doing business to determine whether to tax the body or its members, the rate of tax, the taxable income and, in addition, where there is a tax treaty, whether the body is a resident of the other contracting state for purposes of the tax treaty\(^4\) so that, for example, the treaty rates of withholding tax on dividends, interest and royalties apply – in particular, the reduced 5% withholding tax on dividends which is applicable to payments to a "company (other than a partnership)".\(^5\) Categorization is required by the residence state of a partner in a body formed under the law of another state to determine what is the type of income to tax, whether profits or a dividend, the timing of taxation, when the income is earned or distributed, the cost base of assets in cases where co-ownership is taxed differently from partnerships, and whether a foreign tax credit is available for the underlying tax. Generally, states have clear rules based on the categorization of bodies in general (non-tax) law for taxing their own bodies; thus, categor-
ization problems do not arise internally.8 Other states’ bodies generally have to be fitted into the internal tax law categories or fitted by analogy into the list of internal law bodies subject to corporation tax. This is done by examining their characteristics under the general law governing them, because that is how domestic bodies are categorized, and seeing what the closest internal law equivalent is.7 This approach fails to deal with the problem that the other states’ bodies may be inherently different from one’s own. This is obvious when dealing with bodies which are unknown in the other state’s law, such as the Anstalt,8 foundation or trust, but it is equally true of partnerships which are looked at differently in common law and civil law systems and considerable differences between the types of partnerships are found. We shall concentrate on partnerships and similar bodies used for business9 transactions that are clearly not corporations, but without trying to cover all types of bodies comprehensively.

Not all countries follow the approach of fitting the other states’ bodies into the closest internal law equivalent. The United States allows the taxpayer to decide how bodies are categorized, with some exceptions (see 3.4).10 Italy treats all foreign bodies as corporate (see 3.1). Belgium taxes a foreign body as a body corporate if it has legal personality under the law of its formation or, where Belgian taxes on a source basis, the body has a form similar to a Belgian legal person (see 3.3). In Switzerland, if a foreign partnership has a permanent establishment or real estate in Switzerland, the foreign partnership is taxed in Switzerland as a legal entity in the same manner as the domestic legal entity which it most closely resembles legally or factually, i.e. either (i) as a corporation or (ii) as an association, foundation or other legal entity which benefits from a lower rate of tax than a corporation. In deciding whether a body is a corporation, France and Canada11 pay particular attention to whether the body is regarded by the other country as a corporation under its general (non-tax) law, although this is not the exclusive test. Canada has a statutory provision that states that, for purposes of all Canadian federal statutes, a partnership that is a separate legal entity under provincial law is not a corporation. This, however, does not deal with partnerships formed under foreign law (see 3.5).12 Swedish law provides that, if the other country treats a body as transparent and taxes the partners, Sweden will do the same, thus enabling credit relief to be given for the taxes imposed on the partners in the other country (see 3.9). Following the other country’s tax law in this way is unusual and, we shall argue, is advantageous when taxing a partner in a foreign partnership, as opposed to taxing a foreign partnership on a source basis.

For tax purposes, problems resulting from differences in categorization between partnerships and corporations arise, first, when a state considers another state’s partnership to be so different from its own that it taxes the partnership as a corporate body and, second, when it accepts that the other state’s body is a partnership but the other state taxes the partnership as a corporation.13 Of the first, the OECD Partnership Report suggests that, in most cases, similarities between legal systems ensure that partnerships are recognized as such,14 but, as we shall see, there are important differences between civil law and common law partnerships which cause difficulties in categorization. The OECD Partnership Report deals mainly with the second aspect, that the tax treatment is different in the other state, although, in the countries represented by the authors, there are for general (as opposed to limited) partnerships relatively few cases where partnerships are not transparent.15 It is more common for limited partnerships to be

6. The United States is an exception as the “check-the-box” regulations (see 3.4) apply to US bodies as well as foreign ones, although it is state law that governs the body and federal law that taxes. The Netherlands is also an exception because some domestic entities may or may not be transparent depending on their characteristics, such as whether the business is carried on for the account of the participants or whether the interests in the entity are transferable without the consent of all the members, and the same is therefore true of foreign entities. For a discussion of the case law, see Boekhoudt, André, National Report for the Netherlands on Subject I: Recognition of foreign enterprises as taxable entities, Cahiers de droit fiscal international, Vol. LXXIII (1988), at 511. For an account in English of the Dutch rules for classifying entities, see Daniels, T.H.M., Interleu, 1999, at 554, 373. The Netherlands Ministry of Finance has issued three decrees: the Decree of 17 March 1997 deals with treaty application to foreign hybrid entities that derive income from a Dutch source, and the Decrees of 18 September 1997 and 19 December 2000 deal with the classification of income derived through various types of foreign limited partnerships, the latter including the other state’s tax treatment (see 3.6). Regulating the Decree of 17 March 1997, see Engelen, F., Interleu, 1998, at 38, 42.

7. OECD Partnership Report, supra note 1, Para 14. For example, in a recent UK case, the issue was stated: “What in my judgment we have to do in the present case is to consider the characteristics of an English or Scottish partnership which make it transparent and then to see to what extent those characteristics are shared or not by the silent partnership in order to determine whether the silent partnership should be treated for corporation tax purposes in the same way.” Memec v IRC [1998] STC 754, at 764b. For Germany, see the decision of the Reichsgenossen von 12 February 1930 (RFH 27, 73), which classified as a partnership a Venezuelan limited partnership, which, unlike a Germany limited partnership, had legal personality, since it was otherwise similar to a German limited partnership. The starting point of looking at the other state’s non-tax law is also used in the Netherlands. In a 1924 decision of the Hoge Raad (B 3569, 31 December 1924), the Dutch court categorized a German formal partnership (see note 23, infra) as a partnership because it was similar to a Dutch formal partnership. This approach is in Japan.


9. There is a different approach between common law and civil law in making this distinction, which is dealt with in 2.5. We include professional and real estate transactions in the expression “business”.

10. Previously, the United States categorized foreign bodies by using four criteria (described in 3.4) which were designed to compare them with US bodies.

11. Some Swiss authors share the same view; see Alig, Kurt, Die Personenge sellschaften im internationalen und internationalen Steuerrecht (Brom, 1980), at 397 et seq.

12. See the definition of corporation in Interpretation Act, Sec. 35(1).

13. There are other possibilities, such as that the relationship might be co-ownership.

14. OECD Partnership Report, supra note 1, Paras 15-22. See notes 15 and 16, infra, for the cases where the income of a partnership is taxed as the income of a corporation in the countries represented by the authors.

15. The opposite, opaque, can arise either because the nature of the income changes when the income of a corporation is distributed as a dividend or because the participant has a purely contractual entitlement and not a right to a share of the underlying income, as in the UK case of Memec v IRC [1998] STC 754 concerning income from a German silent partnership. For general (not limited) partnerships, the only cases in the countries represented by the authors where the partnership is taxed as income as a corporation are (a) the Belgian société en nom collectif (SNC), (b) the Japanese goemon-kabushikigaisha which, because it has legal personality and is taxed as a corporation, is regarded as a corporation with unlimited liability, although we have included it with other partnership-like bodies because it is similar to other civil law formal partnerships (see note 23, infra), and (c) the Dutch vennootschap onder firma (VOF) if it has capital divided into shares.
taxed as opaque bodies, although sometimes only for the limited partners.16

We shall first examine the problems caused by states considering other states’ bodies to be different from their own by looking at the non-tax law characteristics in the countries represented by the authors, which is often the basis used for categorizing partnerships for tax purposes. Subsequently, we shall examine the way in which states have tried to determine whether a foreign body is similar to a domestic one. We shall consider whether it is possible to make such a determination on the basis of asking a series of questions about the body based on one’s own system of law and applying the questions to a body created under a different system of law. Finally, we shall examine some proposals for reducing the problems of the characterization of foreign bodies.

2. COMPARISON OF PARTNERSHIPS IN NON-TAX LAW IN CIVIL LAW AND COMMON LAW COUNTRIES

All civil law countries recognize two types of partnership,17 i.e. a body categorized by their law as a société de personnes rather than a società di capitale.18 The first type of partnership is more formal and its use includes commercial operations (enterprise); the other is less formal and its existence is not usually apparent to third parties. The difference between them depends on the legal tradition of the country concerned. At the risk of oversimplification, there are three main schools in civil law: the French, which has influenced Belgium, Italy and the Netherlands; the German, which has influenced Switzerland, Japan and also Italy; and the Scandinavian, which, unlike the other civil law countries, does not have a comprehensive civil code.19 These schools can be distinguished by the degree of influence of Roman law, which is the greatest in Germany and the least in Scandinavia. The differences between these schools seem to be less in relation to partnerships than is generally the case. Although the Netherlands seems different from the other civil law countries, it will become closer to them when the proposed new civil code comes into force. Sometimes the distinction between the two types of partnerships is that one is governed by the commercial code and the other by the civil code,20 but in some countries there is little difference between the partnerships governed by each code, and in many countries the two types are dealt with in a single code.21

The distinction between the two types of partnership is not rigid and, in many countries, a formal partnership can be used for non-commercial activities, such as professional activities and land transactions, and vice versa.22 We shall distinguish between the two types according to their

16 Limited partnerships are subject to corporate income tax in the following countries represented by the authors: Australia (Income Tax Assessment Act (ITAA) 1936, Sec. 94), although an amendment has been proposed that certain limited partnerships involved in venture capital investment will revert to transparent tax treatment); Belgium (société en commandite simple (SCS)/gevorne commanditaire vennootschap, société en commandité par actions (SCC/com- manditaire vennootschap op aandelen); France (as to the limited partners for an

SCS and all partners for an SCA); Germany (Kommanditgesellschaft auf Aktien as to the limited partners); Japan (goshi-kaisai, although, as from 1 November 1998, a new form of partnership limited partners was introduced for venture capital law by the concerning the Limited Liability Partnership Contracts for Small and Medium Enterprise Investment Business (Law No. 90, 1998, as amended); and the Netherlands (the Dutch open commanditaire vennootschap (CV), but only if the limited partners’ shares are freely transferable, and then only as a limited partnership.

17 There is a problem of terminology since civil law countries use the same term, “société”, “società”, “Gesellschaft”, “bolsa” and “vennootschap”, to include both partnerships and companies, and the same is partly true in common law countries where the word “company” can denote a partnership (as in Smith & Company) or a corporation (as in the often-used expression “company law”), although in current usage a company normally means a corporation. Recognition is given to this ambiguity in Canadian tax treaties which are concluded in both English and French, as well as the treaty partner’s language, as they normally include the following in the definition of “company” in Art. 3: “In French, the term “société” also means a corporation within the meaning of Canadian law.”

There is the further problem that the civil law expressions are not equivalent, “Gesellschaft” and “vennootschap” being directed to any common purpose and “société” having the purpose of sharing profits. France therefore needs a different vehicle for non-profit purposes, the groupement d’intérêt économique, which has led to the similar European vehicle, the European Economic Interest Grouping (see 2.2), although, in many other civil law countries, separate vehicles are not needed as the non-profit purpose can be carried out by a partnership “Company” in English does not imply a profit motive; there are companies limited by guarantee which are charitable. There is more similarity between partnerships and companies in civil law countries, where both are governed by similar provisions of the commercial code, whereas, in common law countries, they are less connection between the law governing companies and that governing partnerships. As stated in the text around note 9, supra, we shall cover partnerships and other bodies used for business transactions which are not clearly companies without specifying what constitutes a partnership.

18 Société de personnes: Personengesellschaft, personevennootschap and société à personnes: società di capitale. Kapitalgesellschaft, kapitaalvennootschap and società di capitali. In Belgium, the general tendency is to treat the BVBA/ASPR and cooperative companies with limited and unlimited liability (CVA/SCRL and CVOA/ASCR) as the latter, although this is a matter of debate; they are not dealt with here.

19 For a general account of these differences, see Zweigert, K. and H Kötz, Introduction to Comparative Law (translated by T. Weir) (Oxford: Clarendon Press, 3rd ed., 1998). Zweigert and Kötz say (at 91) of the French “Code civil that it is a masterpiece from the point of view of style and language” Of the German Civil Code (BGb), they say (at 144): “In language, method, structure, and concepts the GGB is the child of the deep, exact, and abstract leaning of the German Pandectist School with all the advantages and disadvantages which that entails. Not for the GGB the clear and popular style of the Swiss Code, or the spurious diction of the Code civil, instinct with the ideal of equality and freedom abstract conceptions. The GGB is not addressed to the citizen at all, but only to the professional lawyer; it deliberately eschews easy comprehensibility and waffles all claims to educate its reader; instead of dealing with particular cases in a clear and concrete manner it adopts throughout an abstract conceptual language which the layman, and often enough the foreign lawyer as well, finds largely incomprehensible, but which the lawyer’s expert, after many years of familiarity, cannot help admiring for its precision and rigour of thought.”

And of the Scandinavian, they say (at 285): “But the tendency to undue conceptualism and the construction of large-scale integrated theoretical systems has never really been followed in the North, thanks to the realism of the Scandinavian lawyers and their sound sense of what is useful and necessary in practice.”

20 The distinction will mean that different courts will deal with disputes relating to each type of partnership. In France, for example, commercial disputes are dealt with by the Court of Commerce, whose judges are persons chosen for their business knowledge. In addition, only commercial entities can be declared bankrupt, they need to be registered in the trade registers, and different procedural rules of evidence apply. In Japan, in contrast with Germany which has influenced Japanese law, a body governed by the commercial code is a corporation and a body governed by the civil code is not.

21 In Italy, the Civil Code; in Switzerland, the Code of Obligations; in Sweden, the Partnerships Act 1980.

22 All the civil law countries represented by the authors, except the Netherlands, allow a formal partnership to undertake non-commercial activities, and all the civil law countries represented allow an informal partnership to undertake commercial activities. We have not treated the French société civile and the Italian società a capite as formal partnerships, but they are restricted to non-commercial.
appearance to third parties rather than their commercial or non-commercial nature. For convenience and in the absence of a generally accepted term, we shall refer to these two types of partnership as formal partnerships²⁴ and informal partnerships.¹⁰ Essentially, formal partnerships are registered and have an existence so far as third parties are concerned. Informal partnerships are not registered and, in some cases, may have an existence so far as third parties are concerned ("disclosed" in Table 1) while, in other cases, are purely internal contractual organizations not directly affecting third parties ("silent" in Table 1). Table 1 (see next page) summarizes how we categorize each country's general (i.e. not limited) partnerships and similar bodies.

Making the same distinction between disclosed and silent partnerships is not possible in common law because an undisclosed partner has the same liability as a disclosed one since a third party can elect to sue either the agent who made the contract in his name or, having discovered the identity of the undisclosed partner, the partner's undisclosed principal, in this case the other partners (see 2.1.). Common law general (as opposed to limited) partnerships are therefore of a single type, which is like an informal partnership in civil law countries in its informality, lack of capacity and personality, but like a formal partnership in the requirement that the partnership carry on business with the intention of earning a profit and in the way the partnership is bound by the actions of a partner. We shall treat the

mercarial activities. The owner of the business into which a silent partner invests will undertake commercial activities.

In Germany, see the decision of the Bundesgerichtshof of 29 January 2001, NJW 2001, at 1056, which held that a partnership formed under the Civil Code is subject to the provisions of the Commercial Code if it participates in transactions with third parties, in which case it can own assets, incur liabilities, sue and be sued and the partners are liable in the same way as a partnership formed under the Commercial Code. This means that a professional partnership is subject to the Commercial Code even though a profession is not regarded as a commercial activity. For this reason, we have included a Gesellschaft des bürgerlichen Rechts (GBR) as a formal partnership.

Similarly, we have included the Italian società semplice as a formal partnership since it can own assets, sue and be sued, its partners are restricted to individuals and is registered (Presidential Decree of 14 December 1999, No 558), although registration is for the purpose of informing the public and does not give any status to the partnership. In Italy, until a partnership with a commercial purpose is registered, relations with third parties are governed by the provisions relating to a società semplice (Civil Code, Art 2297).

If a Japanese formal partnership engages in matters other than commercial acts (defined in Commercial Code, Arts 501 to 503), it is still a formal partnership if its purpose is to make a profit (Commercial Code, Art 52(2)). A Dutch informal partnership can engage in commercial activities so long as it does not operate under a name, but professional activities can be conducted under a name without becoming a formal partnership. A Swedish formal partnership results from an agreement to carry on business (see the definition in note 23, infra), but there is nothing to prevent its continuing as a formal partnership without having to be liquidated if it does not do so (Partnerships Act, Chap 1, Sec 1). A Swiss formal partnership not carrying on a commercial activity becomes a formal partnership only on registration (Code of Obligations, Arts 553 and 595); otherwise, it is a simple (informal) partnership. A Quebec undeclared partnership can carry on an enterprise.

²³ We include as formal partnerships: Belgium: vennootschap onder firma (VOF)/société en nom collectif (SNC), "a partnership between members that are jointly and severally liable, the purpose of which is to carry on a commercial or non-commercial activity under a common name" (Code on Companies, Art 201).

France: SNC, "a partnership the members of which are all traders (commercants) and are individually liable without limit for the whole of the debts and obligations of the partnership" (Commercial Code, Art 221-1) and société civile (SC), "companies have a civil nature where the law does not attribute another feature by reason of their form, their nature or their purpose"; Germany: offene Handelsgesellschaft (OHG), "a partnership formed for the purpose of operating a commercial enterprise under a common firm name is a general commercial partnership," (Commercial Code, Art 105) and Gesellschaft bürgerlichen Rechts (GBR), "by a contract of partnership the partners bind themselves mutually to promote the attainment of a common object in the manner specified by the contract, in particular, to make the contributions agreed upon” (Civil Code, Art 705); Italy: società in nome collettivo, "by a contract of società two or more persons contribute property or services for the exercise in common of an economic activity for the purpose of sharing the profits thereof" and "in a società in nome collettivo all partners are jointly and severally liable and in an unlimited amount for the partnership's obligations. Any stipulation to the contrary has no effect on third parties" (Civil Code, Art 2247 read with Art 2291; see note 26, infra, for the reason for including the società semplice as a formal partnership);

Japan: gomei-fusuma, which we have included here because of its similarity to other civil law formal partnerships, although it is a body corporate; "the term 'company' (kaisha) [which includes a formal partnership] as used in this Code shall mean an association incorporated for the purpose of engaging in commercial transactions as a business" (Commercial Code, Art 52);

Netherlands: VOF, "a partnership that carries on an enterprise under a common name" (Commercial Code, Art 16);

Sweden: handelbolag, "a partnership exists where two or several persons have agreed to engage in business in common in a partnership and the partnership has been registered in the trade register" (Partnerships Act 1980, Chap 1, Sec 1); and Switzerland: société en nom collectif (SNC), "a company composed of two or more natural persons joining together to conduct, under a common company name, a trading, manufacturing or other business carried on in a commercial manner, without limitation of their liability towards company obligees".

This article does not deal with the French société par actions simplifiée, which is a corporation (taxed as such) with some partnership characteristics used for joint ventures.

²⁴ We include as informal partnerships: Belgium: "a maatschap is a contract pursuant to which two or more persons agree to contribute assets or services for the purpose of exercising one or more activities in common with a view to sharing the profits thereof" (Code on Companies, Art 1);

France: a société en participation, a purely private arrangement between the partners which, as a result, does not possess legal personality. For this reason, it is not subject to the publication formalities which are required of other companies and partnerships;

Germany: stille Gesellschaft, "one who participates as a silent partner by means of a capital contribution in a commercial enterprise operated by another must make his contribution in such a manner that it is transferred to the assets of the owner of the business. The owner alone has rights and obligations with respect to transactions concluded within the operation of the business" (Commercial Code, Art 230); Italy: associazione in participazione, "the associating party grants the associated party a participation in the profits of his enterprise or of one more transactions in return for a specified contribution" (unlike the position in other countries, this is not regarded as a société);

Japan: nii-kaisha, "the contract of partnership becomes effective when each of the parties agrees to carry on a joint undertaking by making a contribution thereto" (Civil Code, Art 667);

Louisiana: "a partnership is a juridical person, distinct from its partners, created by a contract between two or more persons to combine their efforts or resources in determined proportions and to collaborate at mutual risk for their common profit or commercial benefit" (Civil Code, Art 2801);

Netherlands: "a maatschap is a contract whereby two or more persons bind themselves to carry on something in common with a view to sharing the profits therefrom" (Civil Code, Art 1655);

Quebec: "a contract by which the parties, in a spirit of cooperation, agree to carry on any activity, including the operation of an enterprise, to contribute thereto by combining property, knowledge or activities and to share any resulting pecuniary profits" (Civil Code, Art 2168);

Sweden: "a non-registered partnership exists where two or more persons have agreed to engage in an activity as a partnership, but where a partnership does not exist pursuant to section 1 [i.e. a formal partnership]" (Partnerships Act 1980, Chap 1, Sec 3); note the distinction between business in the definition of formal partnership (see note 23, supra) and activity here, not implying a profit motive; and

Sweden: "a partnership is a contractual relationship between two or more persons to attain a joint purpose with joint endeavours or means" (Code of Obligations, Art 530).
United States separately as its state laws have changed partnership law substantially from the traditional common law partnership, and we shall concentrate on the Delaware Revised Uniform Partnership Act partnership as an example of a frequently used vehicle which also exhibits the greatest difference from other common law partnerships. We shall also treat the Scots partnership separately as it is a mixture of English and civil law.

There is more similarity between civil law and common law limited partnerships, both being partnerships with limited liability for the limited partners as long as the partners do not take part in the management of the enterprise. In civil law, it is a variety of the formal partnership. The liability of a partner, other than the partner who enters into a transaction with a third party, in an informal partnership is similar to that of a limited partner but, in all other respects, an informal partnership differs from a formal limited partnership in the ways described above. Some civil law countries have a limited partnership with shares, which is closer to a corporation. A further type of partnership, a limited liability partnership (as opposed to a limited partnership), was recently introduced in the common law jurisdictions represented by the authors, except Australia. In this type, the liability of the partners is similar to that of the partners in a civil law silent informal partnership. In the United States and Canada, this type is a normal partnership, but with some limited liability for all the partners. It is quite different in the United Kingdom, where a "limited liability partnership" is not a partnership at all, but a new type of corporation with full legal personality and legal capacity.

The silent partnership existing in civil law countries except the Netherlands, is essentially a type of informal

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<tr>
<th>Country</th>
<th>Informal</th>
<th>Formal</th>
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<tbody>
<tr>
<td>Belgium</td>
<td>maatschap/société de droit commun</td>
<td>vennootschap onder firma/société en nom collectif (SNC)</td>
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<tr>
<td></td>
<td>(commercial and non-commercial purpose,</td>
<td>(commercial and non-commercial purpose)</td>
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<td></td>
<td>disclosed); tijdelijke vennootschap/société</td>
<td>(incorporated)</td>
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<td></td>
<td>momentanée (commercial purpose,</td>
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<td></td>
<td>disclosed); stille handelsvennootschap/société</td>
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<tr>
<td></td>
<td>interne (commercial purpose,</td>
<td></td>
</tr>
<tr>
<td></td>
<td>silent) (all three types are unincorporated)</td>
<td></td>
</tr>
<tr>
<td>France</td>
<td>société en participation</td>
<td>société civile (SC)</td>
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<tr>
<td></td>
<td>(in principle silent, but may be disclosed)</td>
<td>(civil) and société en nom collectif (SNC)</td>
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<td></td>
<td>(commercial)</td>
<td>(commercial)</td>
</tr>
<tr>
<td>Germany</td>
<td>stille Gesellschaft (silent)</td>
<td>offene Handelsgesellschaft (OHG)</td>
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<td></td>
<td></td>
<td>und Gesellschaft des bürgerlichen Rechts</td>
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<td>(GbR) (civil)</td>
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<tr>
<td>Italy</td>
<td>associazione in partecipazione</td>
<td>società in nome collettivo (SNC); società</td>
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<tr>
<td></td>
<td>(silent)</td>
<td>semplice</td>
</tr>
<tr>
<td>Japan</td>
<td>nin'n kuimai (disclosed or silent)</td>
<td>gomei-kaisha</td>
</tr>
<tr>
<td>Netherlands</td>
<td>maatschap</td>
<td>vennootschap onder firma (VOF)</td>
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<td>(disclosed or silent)</td>
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<tr>
<td>Sweden</td>
<td>enkelt bolag (disclosed)</td>
<td>handelsbolag</td>
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<td>Switzerland</td>
<td>société simple/einfache Gesellschaft</td>
<td>société en nom collectif (SNC)</td>
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<tr>
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<td>(disclosed or silent)</td>
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25. For the reasons given in note 22, supra, we have included the German GbR, which cannot carry on an enterprise, as a formal partnership when it participates in transactions with third parties.

26. For the reasons given in note 22, supra, we have also included the Italian società semplice as a formal partnership, rather than an informal one, which is how we have categorized its Swiss equivalent. It cannot be used for carrying on an enterprise (Civil Code, Art. 2249(2)), and it is not normally used for carrying on a profession, although it is used for real estate and other investment transactions.

27. For our reason for including this as a partnership-like body, see note 23, supra.

28. See Alig, supra note 11, at 17 et seq.

29. Belgium: sociëteit in commandite simple (SCS); gereon comanditair vennootschap (GCV); France: société en commandite; Germany: Kommandit Gesellschaft (KG); Italy: società in accomandita semplice, Japan: goishi-kaisha; Netherlands: commandite vennootschap (CV), literally "a company by way of making loans, otherwise named "en commandite"; Sweden: kommanditbolag. Although we have included the French SC, the German GbR and the Italian società semplice as formal partnerships, there is no limited partnership equivalent to them. In the Netherlands, a limited partnership is closer to an informal partnership since the business is treated as carried on by the general partner alone.

30. Belgium: société en commandite par actions (SCA); commanditaire vennootschap op aandelen (CVA); France: SC; Germany: Kommanditgesellschaft auf Aktien (KGaA); Italy: società in accomandita per azioni; but not the Netherlands.

31. The use of the word "partnership" has no significance (see note 17, supra), and some of these bodies are not classified as partnerships at all. Belgium: stille handelsvennootschap/société interne (Code on Companies, Arts 48 and 54); France: société en participation, whose existence is not disclosed; Germany: stille Gesellschaft (Commercial Code, Art. 230 et seq.); Italy: associazione in partecipazione (Civil Code, Arts 2549-2553); and Japan: tokumen kumiai (Commercial Code, Arts 535-542). The silent partnership is recognized in doctrine in the Netherlands, when a distinction is made between the "silent" maatschap and the "public" maatschap, depending on whether it is obvious to third parties that there is a partnership. Some authors (e.g. van Mourik, M. J. A., De Personenvennootschap, Para. 2.4), however, argue that, if the cooperation is to be secret, there can be no intention to carry on a joint activity; it will be formally recognized, although not treated as a legal person, in the new Civil Code (Art. 7.13.1.2(2)).

32. In common law, because of the different law on agency, a silent partnership does not create any different liabilities for the partners than a disclosed partnership; see 21

33. In the Netherlands, a limited partnership with one general partner has similar effect since the third party has rights only against the general partner; the partnership has no existence with respect to third parties and does not have any partnership assets.
partnership or a contractual relationship falling short of a partnership. It comprises an investment in a business whose existence need not be disclosed in any register, entitling the investor to share profits and, in some cases, requiring him to share losses, but only up to the amount of the investment, unless the parties agree otherwise. As regards third parties, the business is carried on and liabilities are incurred solely by the proprietor of the business in which the investment is made.\textsuperscript{34}

The difficulty faced by a country in categorizing another country's partnerships is that partnerships consist of a diverse group of organizations forming a spectrum. At one end of the spectrum is the civil law informal partnership, and at the other is the civil law formal partnership; the common law partnership is sandwiched in between in varying degrees, with the Scots and Delaware Revised Uniform Partnership Act (RUPA) partnerships having more of the characteristics of a civil law formal partnership than other common law partnerships.\textsuperscript{35} Virtually none of the attributes of a civil law informal partnership is applicable to a formal partnership. The different common law countries therefore provide a link between the two types of civil law partnership, having some of the attributes of each type of civil law partnership. This spectrum can be seen in Table 2, designed to give a general picture in which the results are broadly true for most of the countries concerned. Each item is then examined separately.

We shall now examine each of the attributes of partnerships in more detail, repeating the relevant rows of Table 2 as a reminder when discussing each one, showing that these differences are less material than they appear at first sight.

\begin{table}
\centering
\caption{Summary of the attributes of partnerships}
\begin{tabular}{|c|c|c|c|c|}
\hline
Who is bound by action of a partner? & silent partnership & all partners & all partners & partnership so long as the partner's power to represent the partnership is registered \\
\hline
Operating under name & yes & no & irrelevant & yes \textsuperscript{a} \\
\hline
Legal person & no & no & yes but does not survive changes in partners & yes \textsuperscript{a} (or a quasi-legal person) \\
\hline
Registration conferring status & no & no & no & yes \\
\hline
Who owns the assets? & partners in common or a partner individually, on account of the other partners & partners in common & partnership & partnership \\
\hline
Ability to sue and be sued in the partnership name & yes, but only as a convenience & yes & yes & yes \textsuperscript{a} \\
\hline
Type of activity & enterprise and non-enterprise & business & business (but Delaware RUPA can carry on non-profit activity) & enterprise and non-enterprise \textsuperscript{a} \\
\hline
Profit motive required & no, except in countries following the French tradition & yes & yes (but see exception above) & yes \\
\hline
Who carries on activity? & partners & partners & partners & partnership \\
\hline
Liability of a general partner & varies between states & joint in contract; joint and several in tort & joint and several & joint and several \\
\hline
Limited partnerships exist & yes & yes & yes & yes \textsuperscript{a} \\
\hline
Limited liability partnerships exist & yes in Ontario, not in New South Wales; in England it is a corporation & yes in Scotland, as in England, it is a corporation & yes (in Scotland, as in England, it is a corporation) & no \\
\hline
\end{tabular}
\end{table}

\textsuperscript{34} In Germany, this type is known as a "typical" silent partnership, although this is a tax, rather than a legal, distinction; alternatively, the silent partner may be given a vote in the partnership's affairs and a share in the goodwill, which is known as an "atypical" silent partnership. The former is similar to its economic effect to a loan, entitling the investor to a share of the profits of the business coupled with an undertaking to contribute to losses up to the sum invested, though different legally because there is a body pursuing a common purpose, which is different in nature from a profit-sharing loan under which each party pursues its own purpose. The latter has some similarities to a limited partnership. See the UK case Memec v IRC [1998] STC 754, 766a, concerning the categorization of a typical silent partnership. The silent partnership fell short of a partnership as understood in English or Scots law as there was no carrying on business in common; the business was wholly carried on by the company in which the silent partner invested. The investor was not liable to the creditors for the liabilities of the business, but his entitlement depended on the results of the business. Accordingly, from the UK point of view, the nature of the income was a contractual entitlement, not the underlying dividend income.

\textsuperscript{35} For a comparative treatment of the law of partnerships in various civil law and common law countries, see Encyclopaedia of Comparative Law, Vol. XIII: Business and Private Organisations (Conard, A., chief editor), Chap. 1: Partnership and other Personal Associations by J. Heenen (Mohr, 1975).
### 2.1. Agency, mandate and representation

<table>
<thead>
<tr>
<th>Civil law: informal</th>
<th>Common law: England, New South Wales, Ontario</th>
<th>US (Delaware RUPA) and Scotland</th>
<th>Civil law: formal</th>
</tr>
</thead>
<tbody>
<tr>
<td>Who is bound by action of a partner?</td>
<td>partnership: all partners</td>
<td>all partners</td>
<td>partnership so long as the partner's power to represent the partnership is registered</td>
</tr>
<tr>
<td>partnership: that partner; disclosed partnership: all partners</td>
<td></td>
<td></td>
<td></td>
</tr>
</tbody>
</table>

<table>
<thead>
<tr>
<th>Operating under name</th>
<th>Irrelevant</th>
<th>Irrelevant</th>
<th>Yes</th>
</tr>
</thead>
</table>

The common law of agency, dealing with how one person binds another legally, is very different from the law of mandate and representation in civil law. The differences have a significant effect on the differences between partnerships in the two legal systems, affecting not only whether informal partnerships can exist, but also such questions as who carries on the activity and the liability of the partners. This is why we deal with this topic first.

In both legal systems, the party who contracts is liable, but the two systems differ in their determination of the identity of the person who contracts. Common law sees only one contract, between the principal and the third party made through the agent, and it is of no consequence whether the principal is disclosed because the principal (through his agent) has still made the contract and is bound by it. If the principal is undisclosed, it is the third party who chooses whether to sue the principal, having found out his identity, or the agent. Both are liable in the same way. Thus, it makes no difference in common law whether the existence of the partnership (the principal) is disclosed, provided the partner (the agent) intended to contract on behalf of the partnership. The liability of a partner in the common law equivalent of a silent partnership in civil law is therefore no different from an ordinary partnership.

Civil law sees two contracts, between the principal and the agent and between the agent and the third party, and either the principal or the agent (but not both) is bound to the third party. If the principal is to be bound, the agent must contract “in the name of” the principal (direct representation, as in the case of the partner in a formal partnership contracting on behalf of a partnership, or, outside the partnership sphere, the commercial agent). Otherwise, the agent, not the principal, is bound to the third party because the agent made the contract (indirect representation, as in the case of a partner in an informal partnership necessarily contracting in his own name since an informal partnership does not have a name, or, outside the partnership sphere, the commissario). Following from this distinction in the liability of partners, civil law also distinguishes between internal management and the relationship between the partnership and third parties. It is possible in some civil law countries for partners to be excluded by agreement from taking part in internal management, which is not possible in common law because all the partners are liable to third parties. Mandate (the contract determining what the agent – here the partner – must do) is restricted to the internal relationship between the partners. The external relationship, dealing with the power to bind third parties, is governed by representation (this determines whether the agent (partner) can act), which derives either from the law as, for example, in the case of a partner having power to bind the partnership, or from the grant of such power by all the partners.

36. In some countries, for example the Belgian commerçiele maatschap and tijdelijke vennootschap (Tijlquin, T and V Simonart, Traité des Sociétés, T 2, at 12, 20 and 24) and the Dutch maatschap when carrying on a profession, an informal partnership may carry on business under a name.

37. For a comparison of the common law and civil law of agency, see the Hague Convention on the Law Applicable to Agency of 14 March 1978 and the reports made for the preparation of that convention by Michel Pelichet and I G F Karsten in Vol IV, Acts and Documents of the Thirteenth Session (1976), Hague Conference on Private International Law, Contracts of Intermediaries (1979), at 9, 32; and Zweigert and Kötz, supra note 19, Chap 32, Representation (a comparison made by the German authors which was translated into English). See also Avery Jones, J F and D A Ward, “Agents as Permanent Establishments under the OECD Model Tax Convention”, (1993) British Tax Review, at 341, 344; 33 European Taxation 5 (1993), at 154, 156; and Roberts, S J, “The Agency Element of Permanent Establishment: the OECD Commentaries from the Civil Law View”, Interact, 1993, at 396, 488. In relation to partnerships, representation is granted by law (see note 44, infra) and cannot be limited by contract.

38. This has a legal, rather than a descriptive, meaning, as there are circumstances where this is satisfied even though the principal is not expressly named, usually where the third party knows that the agent is contracting on behalf of the principal (see Avery Jones and Ward, supra note 37, at 345 (BTIR) and 157 (ET)) – hence, the reference to the agent contracting in the name of the enterprise in Art 5(3) of the OECD Model.

39. In some civil law systems, such as France, Germany, Italy (Civil Code, Art 1705), the Netherlands (Civil Code, Art 7:400 in the case of insolvency of the commissario, Sweden, Switzerland (Code of Obligations, Art 401), the principal under a contract made by a commissario may have an action against the third party on behalf of the commissario on the basis that it does not matter who enforces the contract against the third party but (except in the Netherlands and only in the case of the commissario’s insolvency (Civil Code, Art 7:421)), the third party never has a right against the principal.

40. Because the undisclosed principal is bound to the third party in common law, one cannot have a body that exists only internally, which is essentially the feature of an informal civil law partnership.

41. Since internal management is not relevant to the comparison we are making, the distinctions between states is not dealt with.

42. Auftrag, mandat, mandate, mandaat, lasteigeng. See Zweigert and Kötz, supra note 19, at 454-435. (Vertrouwens, representatie, rappresentanza, vertegenwoordiging.)

43. Belgium: “Unless otherwise provided in the partnership agreement, the representation belongs to each partner . . .” (Code on Companies, Art 36, 1p) “The partner who is entrusted with the representation of the partnership pursuant to a specific clause in the partnership agreement is entitled to perform all acts of representation, even if another partner opposes such act, provided that the former partner acts in good faith. Such power of representation cannot be revoked without cause. However, if such power has not been granted pursuant to the partnership agreement, but to a subsequent agreement, it can always be revoked as in the case of any representation” (Art 35).

44. Germany: “Each of the partners is authorized to represent the partnership if he has not been excluded from such representation by the terms of the partnership agreement” (Commercial Code, Art 125). The partner is regarded as an organ of the partnership so that there must be at least one partner who represents the partnership.

45. Italy: “Unless otherwise provided in the contract, the representation belongs to each managing partner and extends to all acts within the partnership’s purpose” (Civil Code, Art 2766, emphasis added) and “...the relations between the partnership and third parties are governed by the provisions relative to [non-commercial partnership] ... However, it is presumed that each partner who acts for the partnership has the representation thereof even in lawsuits” (Art 2297). If a partner does not have power to bind the partnership, this is effective against third parties only if they know this, and “the manager who represents a partnership may perform all acts within the purpose of the partnership, except for the restrictions arising from the partnership agreement or from the power of attorney” (Art 2298, emphasis added). (Restrictions are valid against third parties registered under a partnership name.)
either to a partner or to a manager of a power of attorney that in some countries is registered. If, contrary to the general principle, the partners are deprived of the power of representation by the partnership agreement, this fact must be registered in order to bind third parties. Restrictions on the power of the representative (as opposed to not having the power at all) are ineffective against third parties in Germany and Japan, and, if the act is within the registered objects of the partnership, are ineffective in France, but restrictions are effective in Belgium, Italy, the Netherlands and Switzerland if they are registered, which will apply only to formal partnerships. There are cases, however, in which the partnership will be bound where a third party deals with a partner who creates the impression that he has authority to bind the partnership, but in fact does not.

As demonstrated by the name of a formal partnership in French (société en nom collectif) and systems derived from the French legal tradition, one of the most important attributes of a civil law formal partnership is its name. The name indicates the type of partnership, but more importantly, the only way in which a partner can bind the partnership is to act on its behalf in that name; showing an intention to bind the partnership is normally insufficient. In some countries, the management of a partnership, especially where the partnership is a legal person, is carried out by managers who, in fact or in law, may not be partners and who alone can bind the partnership; the other partners merely have a right to be informed about the business and have access to documents. On the other hand, a partner in a civil law informal partnership that does not have a name normally binds only himself. If all the partners of an informal partnership are to be bound, all the partners must act jointly either to enter into the transaction or to authorize someone to do so on their behalf, or a manager...

Japan: “Each of the partners who administers the affairs of the company shall represent the company...” (Commercial Code, Art 76).

Netherlands: “Each of the partners who is not excluded is authorized to act in the name of the partnership, to expend and receive money, and to bind the partnership with third parties or third parties to the partnership” (Commercial Code, Art 17(1)).

Sweden: “Each and every partner acts as agent of the partnership, save where otherwise agreed...” (Partnerships Act 1980, Chap 2, Sec 17).

Switzerland: “Absent any entries to the contrary in the Commercial Register, third parties acting in good faith are entitled to assume that every individual partner is authorized to represent the company” (Code of Obligations, Art 563).

Although not based on the German school of civil law and presumably deriving from common law, in a Quebec partnership each partner is a mandatory of the partnership in respect of third persons in good faith and binds the partnership for every act performed in its name in the ordinary course of its business (Civil Code, Art 2219).

In a Louisiana partnership, “a partner is a mandatory of the partnership for all matters in the ordinary course of its business other than the alienation, lease, or encumbrance of its immovables” (Civil Code, Art 2214).

Belgium: Code on Companies, Art 69, 95; Italy: Civil Code, Art 2298; Sweden: Partnerships Act 1980, Chap 2, Sec 19; but not France, Switzerland or the Netherlands. In Germany, only one Prokura (registered contractual power of attorney) can be granted by a partnership.

In Germany, it follows from the partner being regarded as the organ of the partnership (see note 44, supra) that there must always be at least one partner who represents the partnership.

Commercial Code, Art 126(2).

48. Italy: Civil Code, Arts 2295 and 2298; Sweden: Partnerships Act 1980, Chap 2, Sec 3; Quebec Civil Code, Art 2190. Although the type of business is not registered in Germany, a partner has authority to bind the partnership only in relation to the normal operation of the business; transactions outside this scope require a resolution of all the partners (Commercial Code, Art 116).

49. For example, a Belgian or French formal partnership puts “société en nom collectif” at the end of its name, and the initials “SNC” must be used in all documents. A Danish formal partnership must include “handelsboligm” in its name; and a Quebec partnership must indicate its judicial form in, or after, its name. In Italy (Civil Code, Art 2292) and Switzerland (Code of Obligations, Art 947), the partnership name must be that of one or more of the partners (or ex-partners). In the Netherlands, carrying on an enterprise under a name is the feature that distinguishes a formal partnership (VOF) from an informal one (maatschap), except in the case of a profession (Commercial Code, Art 16).

50. Belgium: Code on Companies, Art 204; Germany: Commercial Code, Art 125(1); Sweden: Partnerships Act 1980, Chap 2, Sec 17; Louisiana, except in relationship with an immovable property; Civil Code, Art 2814; Italy: Civil Code, Art 1388; Netherlands: Commercial Code, Art 17(1); Quebec: Civil Code, Art 2219, but limited to the ordinary course of business. A contract made not in the name of the partnership in Italy binds only the partner who made it: Supreme Court, 1 February 1984, No 936, Roberto v Mastrazzo e Passerino, in Favo II, 1984, I, at 1287. There can be exceptions to the statement in the text for apparent partnerships (where, in the absence of a partnership, persons act in a way that leads third parties to believe that there is a partnership).

51. In Belgium (Code on Companies, Art 50), Louisiana (Civil Code, Art 2816) and the Netherlands (Civil Code, Art 1681 and Supreme Court decision of 13 June 1958, NY 1958, at 352), a contract made in a partner’s own name binds the partnership if it is to the partnership’s advantage. In Quebec, an obligation contracted by a partner in his own name binds the partnership when it comes within the scope of the partnership’s business or when its object is properly used by the partnership (Civil Code, Art 2220). Both of these are presumably as a result of common law influence.

52. The rule in France: the management of an incorporated partnership is not necessarily a partner (van Rijn, Principes, I, 297, No 424); Italy: Civil Code, Art 2298; France: a person who can bind the partnership must be appointed as a manager (Commercial Code, Art 2221-3); Italy: a manager (amministratore), who must be a partner, can be appointed but, for an unregistered partnership, it is presumed that every partner can bind the partnership, exceptions being valid only if the person is aware of them (for a registered partnership, third parties will know from the register who can bind the partnership (Civil Code, Art 2297); Netherlands: Olmer, F X and W Rodenhuis, Maatschap, vennootschap onder firma en commanditaire vennootschap (Deventer: Kluwer, 1988), at 77-79; Quebec: a manager may be appointed in a Quebec partnership (Civil Code, Art 2213). The actions of a manager do not bind the partners in a French informal partnership (société en participation).

53. France: Commercial Code, Art 1.2221 8; Germany: by acting under a Prokura, a type of power of attorney filed in the commercial register, the Prokurator signs in the name of the partnership adding per procura (an expression misunderstood in English when one person signs on behalf of another without such authority); Italy: Civil Code, Arts 2261 and 2293.

54. Belgium: “a partner of an informal partnership cannot bind the other partners if he has not received a power of attorney to do so” (Code on Companies, Art 204; Italy: Civil Code, Art 1257; Netherlands: Commercial Code, Art 7A 1681, which requires a mandate; Sweden: Partnerships Act 1980, Chap 4, Sec 5 even if an agreement is made on behalf of the partners, only the partner making the agreement is bound); Switzerland: Code of Obligations, Art 543(1). Exceptions are that, in Japan, all the partners of an informal partnership are bound and in equal share if the creditor does not have their, their principal or their assistant’s agreement (Civil Code, Art 675) and, as noted in note 51, supra, in Belgium, Louisiana and the Netherlands, an act stated to be done by a partner on behalf of an informal partnership binds the other partners if it is to the partnership’s advantage; in Quebec, for an undetermined partnership where, to the knowledge of third persons, the partners act in the quality of partners, each partner is liable (Civil Code, Art 2223).

In the Netherlands, if an informal partnership carries on a profession under a name, all the partners are bound by virtue of an implied power of representation; and Civil Code, Art 7A:1679 provides that a partner in an informal partnership (maatschap) cannot bind the other partners unless he has been given a power of attorney. In doctrine, different positions are taken. One view is that the “authority to manage”, which the partners of an informal partnership may give to one of them, automatically includes the authority to act as an agent for the other partners. Mueijer, J M M, Maatschap, vennootschap onder firma, commanditaire vennootschap (Tjeenk Willink, 5th ed, 1989), at 110 (Part V of Asses-Serie, Bijzondere Overeenkomsten). Others, however, are of the opinion that the managing partner is not automatically an agent of the other partners and that the transactions entered into by such a managing partner do not automatically bind the other partners.

aging partner must be appointed who has the power of representation, except that a single partner of a Japanese informal partnership may bind the partners in conducting the ordinary affairs of the partnership so long as no other partner or manager objects.\(^{35}\)

In contrast, in common law, a name is an attribute of a corporation; a partnership is not sufficiently a separate body for its name to have any significance, other than as a convenience to avoid listing the names of all the partners. Each partner is an agent of the other partners, with the result that the actions of one partner in "carrying on, in the usual way, business of the kind carried on by"\(^{36}\) the partnership automatically bind all the partners. The result is similar to that of a civil law formal partnership, except that, unlike such a partnership, every partner will always be able to bind the partnership,\(^{37}\) and no restrictions on his powers will be effective against third parties who have no knowledge of the restrictions. An English partner therefore carries on business as a principal and as an agent of his partners. A consequence of this agency is that a partner of an English partnership cannot sue, or be sued by, the partnership except for an action for an account because he would be suing, or being sued by, himself together with his agents.\(^{38}\) This agency is different in a Scots or a Delaware RUPA partnership\(^ {39}\) as the partner is an agent of the partnership and his partners, but is not a principal because the partnership itself is the principal. In consequence and in contrast to the position in the other common law countries, it is possible in Scotland and Delaware for a partner to sue and be sued by the partnership.\(^ {40}\) The limitation on the power of a partner to bind the other partners when carrying on, in the usual way, business of the kind carried on by the firm involves a factual determination of what is usual. The only exception is where the partner has no authority and the third party either knows that he has no authority or does not know or believe him to be a partner. A person who is held out as a partner, although not actually a partner, has the same liability as a partner.\(^ {41}\) The partnership name has no significance; doing something in the partnership name binds the partnership, but so does anything done in any other manner showing an intention to bind the partnership.\(^ {42}\)

In a civil law formal partnership, each partner having the power of representation can bind the partnership by acting in its name. The situation is the same in Scots and Delaware RUPA partnerships, although expressed differently in accordance with the common law of agency, that each partner is an agent of the partnership. In other common law partnerships, the agency is quite different, that each partner is an agent of the other partners, but the result is again the same, that all the partners are bound by the action of one of the partners, which is another way of saying that the partnership is bound. One distinction between the two legal systems is that a partner's power to bind the partnership (or the other partners) necessarily applies to all the partners in a common law partnership but, in civil law countries, can be taken away or, in some countries, limited, so long as the restriction is registered. The differences relate to the underlying law rather than the result, which is that the body, whether one refers to it as the partnership or as the partners, is bound. The only different case is the civil law informal partnership, where the action of one partner will normally bind only that partner unless additional steps are taken to bind the other partners. Because an undisclosed principal is bound in common law, a similar result in terms of the liability of a partner who does not enter into the transaction with the third party can be reached only by creating a new vehicle, the limited liability partnership. See 2.6.3.

2.2. Legal person

<table>
<thead>
<tr>
<th>Civil law: Informal</th>
<th>Common law: England, New South Wales, Ontario</th>
<th>US (Delaware RUPA) and Scotland</th>
<th>Civil law: Formal</th>
</tr>
</thead>
<tbody>
<tr>
<td>Legal person no</td>
<td>yes, but does not survive change of partners(^ {43})</td>
<td>yes (or a quasi-legal person)(^ {44})</td>
<td></td>
</tr>
</tbody>
</table>

56. In the United Kingdom, see Partnership Act 1890, Sec. 5 (similar provisions can be found in New South Wales (Sec. 5) and Ontario (Sec 6)): "Every partner is an agent of the firm and his other partners for the purposes of the business of the partnership." This reference to a partner being the agent of the firm was added to the UK Bill when it was extended to apply to Scotland (Report of the English and Scottish Law Commissions, Partnership Law, a joint Consultation Paper, July 2000 (hereafter "Law Commissions") (available at www.lawcom.gov.uk), Para. 9.2, footnote 5), and is meaningful only for Scotland, although it has been copied in the legislation of other common law countries.
57. It is not possible to provide to the contrary in the partnership agreement in a way that would bind third parties, as it is possible to do by registration in relation to formal partnerships in civil law countries.
58. See Law Commissions, supra note 56, Para. 17.18 et seq.
59. Delaware RUPA § 15-301.
60. Delaware RUPA § 15-405(a), (b); Scotland, as a matter of principle. The position is the same for formal partnerships in all civil law countries.
61. The person claiming against a person held out as a partner must show that he relied on the person holding himself out as a partner; thus, it was insufficient that a receipt had been made in the name of the firm if the person held out as a partner had taken no part in preparing the report Nationwide Building Society v Lewis (1998) Ch 482.
62. Partnership Act 1890, Sec. 6: "An act or instrument relating to the business of the firm and done or executed in the firm-name, or in any other manner showing an intention to bind the firm, by any person thereto authorised, whether a partner or not, is binding on the firm and all the partners." The reference to something done in the firm name is presumably the result of civil law influence; see note 83, infra.
63. There is a proposal by the Law Commissions, supra note 56, Para. 4.17, to give an English partnership legal personality, making it the same in this respect as a Scots partnership.
64. This is an unresolved issue in Scotland: Law Commissions, supra note 56, Paras. 2.34-35 and 4.14-17 (references to Scotland rely heavily on the Law Commissions Report). The personality does not extend to holding title to immovable property (hospitable property in Scotland), although this will change when Abolition of Feudal Tenure, etc. (Scotland) Act 2000, Sec. 70 comes into force. See Walker, Principles of Scottish Private Law (2nd ed.), at 394. See note 73, infra, for statutory recognition of a Scots partnership as a corporation. Under Delaware RUPA § 15-201, "[a] partnership is a separate legal entity which is an entity distinct from its partners unless or to the extent otherwise provided in a statement of partnership existence and in a partnership agreement" (emphasis added). The partnership can be dissolved by a majority of partners when a partner dissociates (§ 15-801).
65. Formal partnerships which are legal persons are: Belgium: VOI/SNC; France: SNC and SC (Commercial Code, Art. L.2106 and Civil Code, Art. 1842); Japan: gomei-kaisha (Commercial Code, Art. 54); Louisiana partnership (Civil Code, Art. 2801); and Sweden: handelsbolag (automatically following from the partnership's rights and obligations in Partnerships Act, Chap 1, Sec. 4). Formal partnerships are not legal persons in Germany, Italy, Switzerland and the Netherlands. A proposal made in the Netherlands on 6 July 2001 gives a formal partnership (VOI) the option to be a legal person because this will affect the tax treatment. 

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Legal person – like partnership – is a concept that each country understands within its own legal system, and one tends to assume, wrongly, that it means much the same everywhere. As “legal person” refers to the legal attributes of a person, in some countries, bodies may have varying degrees of legal personality – for example, a body may validly enter into an employment contract with an employee, but may not hold real property. In some countries, bodies which other countries would say had all the attributes of a legal person do not qualify, in the country in which they are created, as a legal person because in the country concerned a legal person has different requirements or attributes.

We can illustrate these differences by reference to a body which is identical in all European countries (except with regard to its status as a legal person), the European Economic Interest Grouping (EEIG), which, although it is not a partnership, has some partnership characteristics. An EEIG has the following extensive capacity from the date of its registration: “... the capacity, in its own name, to have rights and obligations of all kinds, to make contracts or accomplish other legal acts, and to sue and be sued.” The Regulation (Art. 1(3)) leaves it open for states to decide whether an EEIG registered in its state has legal personality. In general, European states have decided that it has legal personality, but in Germany and Italy it does not.

What a legal person is can be illustrated by comparing the approach of various European countries to deciding this question. The reason why Germany and Italy have not made an EEIG a legal person is that in the German legal tradition, which in this respect also applies in Italy, the state recognizes as legal persons entities which continue in being despite changes in their members. This results in a strict separation between the assets of the legal person and its members, with the result that the members of a legal entity cannot be liable for the entity’s liabilities. Since the members of an EEIG are so liable, it does not conform to the German and Italian domestic concept of legal person, and so those countries do not categorize an EEIG as a legal person in spite of its capacity. In contrast, in some other countries, the liability of the members is not a factor of any relevance to this question. In the French and Scandinavian legal traditions, as in England, being a legal person and having legal capacity go together. Thus, in these traditions, the EEIG’s capacities are such that it is naturally categorized as a legal entity. In England, there is no intermediate category of reduced legal personality into which an EEIG can be put; thus, it is a legal person; there are, with few exceptions, no degrees of legal capacity. An EEIG that is identical in all European countries in respect of its legal capacity, the liability of its members and all other attributes may, therefore, be a legal person or not, depending on each country’s concept of legal person.

The position of partnerships is the same. In Germany, Switzerland and Italy, partnerships are not legal persons because a partnership is a personal relationship that does not survive changes in the partners (except in Italy) and the liability of at least one of the partners is unlimited. It follows that, in those countries, a formal partnership, in

66. Personale morale, persona giuridica, juridisk person, rechtsperson, juristische Person.
67. European Company Regulation, No. 2157/2002, Art. 1.3 states that a European company has legal personality, which does not mean the same thing in all the Member States.
68. The legislative history of the German EEIG (Bundelstragsdrucksache zum EWWG 11/582, at 6) describes the EEIG as a special form of commercial code partnership (ohG), with the differences that an organ other than a member can act for the EEIG, a share in an EEIG can be transferred with the unanimous consent of the other members, an EEIG is not automatically dissolved on the death of a member, and the members of an EEIG are obliged to make up losses.
69. Council Regulation (EEC) No. 2137/85 of 25 July 1985, Art. 1(2). This is very similar to the capacity of German, Italian and Swiss formal partnerships; see text at notes 93 to 96, infra.
70. And also in Denmark, which is not represented by any of the authors.
71. In common law countries, corporations whose members had unlimited liability existed long before the introduction of limited liability, and so the connection between limited liability and legal personality is less strong in Australia and the United Kingdom, unlimited companies exist today. The EEIG is unique in the UK because it is a legal person whose members are liable in the first instance for the EEIG’s liabilities in the same way as partners in England, and not merely on liquidation as in the case of an unlimited company (Insolvency Act 1986, Sec. 74, liability not being restricted to the amount unpaid on the shares as in the case of a member of a limited company), or secondarily to the liability of the partnership in Scotland.
72. The International Tin Council had legal personality under the treaty creating it, including the capacity to contract and acquire and dispose of movable and immovable property and to institute legal proceedings, but the UK legislation giving effect to the treaty in internal law provided that the Council had the legal capacities of a body corporate, without making it a body corporate (which would have had the undesirable effect of making it, as an international body, subject to UK law as, for example, winding-up). This was held by the House of Lords in J.H. Rayner v. Department of Trade [1990] 2 AC 418 to have created a separate legal person, with the result that its members were not liable for its liabilities. The following quotation from an Australian case was cited: “...a body, which, as distinct from the natural persons composing it, can have rights and be subject to duties and own property, must be regarded as having legal personality, whether it is or is not called a corporation.” Cuff & Hay Acquisitions Committee v. J.A. Hempill and Sons Proprietary Ltd (1947) 74 C.L.R. 375, 385.
73. It is possible in the UK for a registered trade union (which has the power to contract in its own name and be sued in its name, and a judgement against the name can be enforced only against property held for its benefit, but not the power to hold property in its name) and for friendly societies to be legal persons, although not corporations; see Salmon on Jurisprudence (12th ed., 1966), at 306, quoted in Bumper Development Corporation v. Com. of Police of the Metropolis [1991] 1 WLR 1362. A registered trade union is sufficiently a separate person to enable a member to sue the trade union without it being said that he is suing himself and others. On the ground that any wrong was done by an agent for himself, as would be the case with a common law partnership (see note 58, supra). In Bensor v. Musicians Union [1956] A.C. 104, at 131, Lord Porter described the trade union as “a thing created by statute, call it what you will, an entity, a non-corporate, which by statute has in certain respects an existence apart from its members”.

The position in Australia is similar except that there are many more examples of bodies having partial legal capacity. Whether or not a body is a legal person is of little importance in common law countries. A Scots partnership is categorized as a corporation as there is no intermediate category into which can be put, and, accordingly, it has to be excluded from the tax definition of “company”, which determines that a body is liable to corporation tax, in TA 1988, Sec. 832(1). A Scots partnership is treated as a corporation in the Civil Jurisdiction and Judgments Act 1982, Sec. 50, giving effect to the Brussels and Lugano Conventions on Jurisdiction and the Enforcement of Judgments in Civil and Commercial Matters. A French SCC would be treated the same way for purposes of these Conventions. For a historical analysis of body corporate in common law, see Montagu, Gerald F.H., “Is a foreign state a body corporate?”, [2001] British Tax Review 421.

74. This is also currently the case for a Dutch formal partnership (VOF), although a proposal was made on 6 July 2001 to give it the option to be a legal person.
the same way as an EEIG, can have partial legal capacity, without being a legal person since it lacks the continuity necessary to be a legal person under their law. If a body identical to a German, Swiss or Italian formal partnership existed in most other civil law countries, its capacity would result in its being a legal person. In France, on the other hand, partnerships formed under both the Commercial Code and Civil Code, which partnerships we have classified as formal partnerships, are legal persons following registration despite the partners being liable for the partnership’s liabilities, but an unregistered (in our terms, informal) partnership is not a legal person. Belgian, Swedish, and Japanese formal partnerships also become legal persons on registration, but informal partnerships do not. In Japan, bodies governed by the Commercial Code are corporations. In the civil law state of Louisiana, a partnership is a legal person, and this was formerly the case in Quebec. Although normally in the common law system a partnership is not a legal person, and hence cannot have any legal capacity, because the common law equates the two, a Delaware RUPA partnership and a Scots partnership are legal persons and, accordingly, have the capacity to carry on business themselves, although it is still the partners that carry on the business because that is the definition of partnership. A proposal has been made to make an English partnership a legal person in line with a Scots partnership, with no suggestion that whether or not it is a legal person is fundamental to its nature. In practice, from a commercial, as opposed to a strictly legal, point of view, a common law partnership has many characteristics of a legal person: it normally has a name and a bank account in that name; it can issue invoices and receive cheques in that name; it can receive and deliver goods and services in that name; the partnership accounts are drawn up in a form similar to company accounts showing the partners as debtors and creditors to the partnership; and the partners appear to act as agents for the firm and appear liable in practice only to the extent that the partnership assets are insufficient to meet its liabilities because a creditor will normally first proceed against the partnership (or, more accurately, the partners jointly). In this way, the appearance, rather than the legal position, is closer to a civil law formal partnership.

Registration is important to a civil law formal partnership, which normally owes its existence, and, where relevant, its status as a legal person, to registration. If it is not registered, it can only be an informal partnership. A written partnership agreement is often required for registration. In the Netherlands, however, registration is merely for information and confers no status on a formal partnership (VOF); the same is true in Switzerland so long as the formal partnership carries on an enterprise; if it does not, registration is essential to its status as a formal partnership. In Belgium, there are two registers: the companies register, which makes a formal partnership a legal person, and the trade register, in which all persons, including partners in informal partnerships, carrying on acts of commerce are registered. In most other civil law countries, formal partnerships are registered in the trade register. In contrast, there is no registration of common law partnerships except

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75. This is the view of the "modern" school based on Fabricius, "Rechtsgültigkeit, 1965, and Palmgren/Heinrichs, "Kommersial zum BGB, Obüberblick vor § 1 Bln 1 (61st ed.) This view is in contrast to the "old" school, which regards Commercial Code, Art. 124 (see at note 93, infra) not as giving the partnership a legal capacity, but merely enabling the partners to act jointly in their legal relations (Larmann, "Zu einem Teil des deutschen Bürgerlichen Rechts, § 12 B 2) The Netherlands follows the "old" school in this respect.
76. See at notes 93 to 96, infra.
77. Belgium: Code on Companies, Arts. 2 § 4 and 68; Sweden: Partnerships Act 1980, Chap. 1, Sec 1; Japan: Commercial Code, Art. 57. Before 1995, a formal partnership in Sweden had legal personality from formation, not from registration, but the law was changed and is now the same as in other civil law countries where, if a partnership has legal personality, it is as a result of registration.
78. Louisiana Civil Code, Art. 2801: "A partnership is a juridical person, distinct from its partners, created by contract between two or more persons to combine their efforts or resources in determined proportions and to collaborate at mutual risk for their common profit or commercial benefit." Louisiana was formerly a French colony which retained its French law on admission to the Union in 1812 and which has since been heavily influenced by common law.
79. Quebec was also originally a French colony which, in accordance with British tradition, was permitted to retain its law, the Coutume de Paris, on being ceded to the British in 1774. The Coutume was later codified into the Code Civil de la Province de Québec of 1866. That Code was silent on whether a partnership had legal personality, but the weight of authority was that it did. The current Civil Code, which took effect on 1 January 1994, does not give legal personality to a partnership; see Tavasso v. LAR [1999] TCI No. 135, a case concerning the Unemployment Insurance Act. See "The Nature of a Partnership" by Guy Pericin, Contemporary Utilization of Non-corporate Vehicles of Commerce, 1997 Meredith Memorial Lecture, at 3; Faculty of Law, McGill University. The common law influence from the rest of Canada in Quebec has been less than that from the common law US states in Louisiana.
80. A decision of the European Court of Justice on VAT held that the references in the Sixth Directive to "establishment" or "organisation" are wide enough to include a Northern Irish partnership (which is the same as an English one), inferring that, by using these expressions, it was not intended to restrict the provision (Arts. 13A 1(b), 1(b)), to legal persons. Gregg v. Customs and Excise Com., C-216/97, [1999] STC 934, 850b.
81. Scots law had been heavily influenced by the "Auld Alliance" with France and was preserved on the union with England in 1707. Thus, the main French influence ceased before the time of codification. Scots law has largely remained separate from English law.
82. Law Commissions, supra note 56, Para. 4.17.
83. See Lindley and Banks on Partnership (Sweet & Maxwell, 17th ed., 1995), Chap. 3 Historically, the treatment of a partnership as an entity had a basis in the law merchant and in the courts of equity, which looked on a partnership as more of an entity than did the common law, but the common law view predominated in the UK Partnership Act 1890, although some of the rules of that Act were later retained (see note 101, infra, for an example of this). The development of partnership law in England may also have been influenced by the civil law, particularly the developments in the 18th century by Lord Mansfield, who had been trained in both the common law and civil law.
84. Belgium: Code on Companies, Arts. 2 § 4; France: Civil Code, Art. L 210-5; Germany: Commercial Code, Art. 123; Italy: Civil Code, Art. 2296; Japan: Commercial Code, Art. 64; Netherlands: Commercial Code, Art. 23; Switzerland: Code of Obligations, Art 554; Sweden: Partnerships Act 1980, Chap. 1, Sec. 1. In Germany, however, if a commercial partnership begins business before registration, normally it is effective from when business starts (Commercial Code, Art. 123(2)). In the UK case of Dreyfus v IRC, 14 TC 560, 565 (see at note 220, infra), the evidence was (correctly) that a French formal partnership (SNC) owed its existence, not to the contract between the parties, but to the written document registered with the Registrar of the Commercial Court and officially published. Registration of the specimen signatures of the partners who are to represent the partnership is required in Germany (Commercial Code, Art. 108(2)) and Switzerland (Code of Obligations, Arts 553 and 595).
85. Belgium: Code on Companies, Arts 67-69; France: Civil Code, Art. 1835; Italy: Civil Code, Art. 2296; Japan: Commercial Code, Art. 62; Netherlands: Commercial Code, Art. 22, although Art. 22 also provides that the omission of a written agreement cannot be used against third parties, suggesting that the partnership nevertheless exists. A written agreement is not required in Germany, Sweden or Switzerland. In Louisiana, immovable property can be acquired in the partnership name only if the partnership agreement is in writing (Civil Code, Art. 2807).
86. Code of Obligations, Art. 553.
87. Laws on the trade register of 20 July 1964, Arts. 4, 5 and 6.
for limited partnerships and, even then, registration does not confer any status on the partnership other than limited liability for the limited partners. Registration of the business name exists in several common law countries for the purpose of giving information.88

These differences are merely differences in what is meant by “legal person” in different countries. It is not clear that asking the question whether another state’s partnership is a legal person and obtaining an answer based on the other state’s meaning of the term will result in a meaningful answer.89 In civil law, a partnership’s capacity and name are more important than whether it is a legal person but, in common law, a partnership does not have legal capacity except in the few cases, such as a Delaware RUPA partnership or a Scots partnership, where it is a legal person. This difference in legal capacity between civil law and common law is more a feature of the difference in the laws dealing with agency than any real difference.

2.3. Ownership of the business and assets

<table>
<thead>
<tr>
<th>Civil law: informal</th>
<th>Common law: England, New South Wales, Ontario</th>
<th>US (Delaware RUPA) and Scotland</th>
<th>Civil law: formal</th>
</tr>
</thead>
<tbody>
<tr>
<td>partners in common</td>
<td>partnership on account of the other partners</td>
<td>partnership</td>
<td>partners in common</td>
</tr>
</tbody>
</table>

Ownership is another expression with different meanings in different countries (and indeed within a country), and it should not be assumed that one country’s statement that a partnership owns assets is necessarily different from another country’s statement that a partnership does not.90

In the discussion below, we record what countries say about ownership of assets by partnerships without trying to make a comparison. In all cases, a partnership that is a legal person91 owns its assets in its name,92 but it does not follow that a country cannot regard a partnership that is not a legal person as owning its assets. In Germany, Italy and Switzerland, where formal partnerships are not legal persons and the concepts of capacity and legal person are not equivalent, a body that is not a legal person may have sufficient capacity to own assets and to register the assets in the name of the partnership, with the result that the partners do not own them. This can be seen in the following provisions:

Germany:

“The general commercial partnership can acquire rights and enter into obligations, acquire ownership and other rights in real property and sue and be sued in its own name.”93

Switzerland:

“The Company [including a partnership] may, under its company name, acquire rights and incur liabilities, sue in court and be sued.”94

Italy:

“A company [including a partnership] acquires rights and assumes obligations through the partners who have the power to represent it, and shall appear in judicial proceedings in the person of such partners.”95

88. In Ontario, a partnership that carries on business with the public under a name that does not list the names of the partners must use the generic Business Names Act; if a partnership is not registered, it cannot sue in its own name. The position on registration is the same in New South Wales, but litigation by a partnership is in the names of the partners unless the partnership is unregistered, in which case an action against the partnership is made using the business name, presumably because the names of the partners are unknown (Higgins and Fletcher, The Law of Partnership in Australia and New Zealand (Sydney: LBC Information Services, 8th ed., 2001)). Professional partnerships are not required to be registered. The UK has no registration of business names, although it did before 1985. Currently, partnerships with fewer than 20 partners must include certain particulars, including the names of the partners, on their business documents; partnerships over that limit must make available a list of the partners for inspection during office hours.

89. As was stated in a Belgian tax case concerning a Michigan (US) partnership (Court of Appeals of Brussels, 30 April 1998, discussed in 38 European Taxation 8 (1998), at 249), “with respect to the issue whether the plaintiff possessed a permanent establishment in the US, [the Michigan partnership] does not have legal personality under the standards of the USA, nor under the standards of Belgium.”

The UK has tax provisions not relating to partnerships which apply to foreign bodies corporate. The provisions relate, first, to group relief for losses that apply between bodies corporate (TA 1988, Sec. 41(3)(2)) and, second, to transfers within a group for capital gains that apply between bodies corporate or unincorporated associations, but not partnerships (see the definition of “company” in TCGA 1992, Sec. 288(1); for this purpose, a limited liability partnership (LLP) formed under the law of a country or territory outside the UK is a partnership while it is transparent for UK tax purposes (TCGA 1992, Sec. 170(9))). Presumably, these provisions incorporate the other country’s meaning of body corporate because whether something is a body corporate can be answered only by the other country. This seems to have been the test applied in Osnard Financing v. Rohn [1998] 1 WLR 1465 (although the second relief (intra-group transfers) also applies to unincorporated associations). The provisions also incorporate the UK’s meaning of partnership (including an LLP) in the exception from the second relief because that can be answered by comparing the body to an English or Scots partnership, as was done in Memec v. IRC [1998] STC 754. The first (group relief) provision can therefore include a partnership which is a body corporate as the parent company of a group, even, it seems, a Scots partnership or an LLP, but not as a subsidiary as it will not have the necessary share capital. On the other hand, an unincorporated association, not being a body corporate, cannot be a member of a group for group relief purposes even though it is liable to corporation tax.

90. An objective test of ownership by a partnership might be that the partnership’s creditors can take an asset in priority to the partners’ creditors, but such a test does not fit the language used by many countries. While the creditors of a common law partnership take priority, a common law partnership (apart from a Scots or a Delaware RUPA partnership) would not be regarded as owning its assets because only a legal person can own assets.91 See note 65, supra, for formal partnerships being legal persons in Belgium, France, Japan and Sweden, plus common law Delaware RUPA and Scots partnerships.

92. France: Civil Code, Art 1842; Sweden: Partnerships Act, Chap. 1, Sec. 4; Delaware RUPA §§ 15-203 and 15-501; “a partner is not co-owners of partnership property and has no interest in specific partnership property”; Scotland: following from the partnership being a legal person.

93. Commercial Code, Art 124. In relation to a GbR, which we have also classified as a formal partnership, the partners are recorded as the owners of real property (as a tenancy in partnership) (Civil Code, Arts. 706(2) and 719).

94. See note 17, supra.

95. Code of Obligations, Arts 562 and 602. A Swiss formal partnership was described in Osnard Financing SA v. Rohn [1998] 1 WLR 1465 by Mummery LJ (at 1470E) as “... a separate entity with many of the characteristics of a corporation.” It is suggested that Vinelott J’s statement (at 1470F) that “[i]n this case it cannot be said that the ownership of the property vested in the general partnership is something separate from the ownership of the partners” is applying an English view of capacity to a Swiss body where the concept of capacity is different.

96. Civil Code, Art 2266. See Galgano, F., Società di persone (Milan, 1982) at 133, and Galgano, F., Il principio di maggioranza nelle società di capitali (Padova, 1960), at 20. Such a body has power to hold real property (Art. 2659)
Thus, in these countries, a formal partnership, like an EEIG, has sufficient legal capacity to own assets, even though it is not a legal person. The partnership name, therefore, is an attribute of legal capacity, rather than of legal personality. The Netherlands does not fit into either of these two categories: a formal partnership (VOF) is not a legal person and is not treated as owning property, although the concept of separate partnership property is recognized. Accordingly, the partners own the property, although property can be registered in the name of the partnership.  

An informal civil law partnership and a common law partnership, neither of which is a legal person, do not have the capacity to own assets, with the result that the partnership property is owned by the partners in common or by one of the partners. This joint ownership is often different from joint ownership unrelated to a partnership. There is a clear difference between the partner's property and the partnership property. In two separate instances, the UK Partnership Act 1890 and other similar common law legislation even describe partnership property as property belonging to the partner. In practice, in common law countries, although a partnership name is often used, for example on bank accounts, this is a convenience and has the same effect as setting out the partners' names. It is not possible to register other personal property, such as shares, or real property in a partnership name. Registration of real or personal property is in the names of the partners (or trustees for them). Such partnership property is co-owned but subject to the partnership agreement, so that a partner cannot realize his share in the property except by retiring from the partnership and receiving his entitlement under the partnership agreement or by the partnership being wound up.  

In order to overcome the disadvantage of an informal partnership in Germany not being able to hold assets in the partnership name, which at the time was thought to apply to a professional partnership, a new type of professional partnership (Partnerschaftsgesellschaft) was created. In other countries, for example Belgium, an incorporated (or formal) partnership can carry on a profession, and it is thus unnecessary to create a different type of partnership. The partners in a German Partnerschaftsgesellschaft have the same liability as the partners in an informal partnership, so that there is no liability for the other partners in tort, but the partnership enjoys the same capacity to own assets in the partnership name as a formal partnership.  

Where a partnership is not a legal person, in both civil and common law, the partnership assets are clearly different from a partner's personal assets because the former are assets available in the first instance to pay the creditors of the partnership. German, Swiss and Italian law describes this as the partnership owning the assets, with ownership being registered in the partnership name, but the underlying concept seems to be the same as partnership property  

98. Another distinction is that no contribution of assets or of services is required in a common law partnership, whereas such a contribution is required in an informal partnership.  

99. Belgium: a generally accepted principle; Finnish: "the contribution made by each partner and the other property of the partnership shall belong to all the partners jointly" (Civil Code, Art. 668 and 249); Netherlands: co-ownership by the partners is a special form of co-ownership governed by Book 7A, rather than the general rule in Book 5 of the Civil Code; Sweden: the right of the partners to the legal rights in Partnerships Act, Chap. 1, Sec. 4, the Joint Ownership Act does not apply to assets held by the partners in a simple partnership (Joint Ownership Act, Sec. 19); Switzerland: Code of Obligations, Art. 544(1). In Belgium, the type of joint ownership of partnership property is the same as for non-partnership property. In a Belgian silent partnership, a French societé en participation and a Quebec (Civil Code, Art. 2252) unregistered partnership, contributions remain in the ownership of the partner concerned, unless the partners agree otherwise.  

100. In common law jurisdictions, the main differences between joint ownership generally and joint ownership of partnership assets are that (a) a co-owner (in joint ownership generally) may transfer his share without the consent of the other co-owners to a third party who will stand in his shoes and (b) a partner can assign a right to his share in the profits, but not any other rights as a partner, such as taking part in the management or inspecting the books of the partnership (UK Partnership Act 1890, Sec. 31, and similar provisions in New South Wales (Sec. 51) and Ontario (Sec. 31)). A partner's interest in a Delaware RUPA partnership may be freely transferred, but the transferee retains the rights and duties of a partner other than the economic interest transferred (§ 15-503). In Australia, a partnership is defined for tax purposes as including persons in receipt of income jointly, so that joint owners are taxed as a partnership. In addition, unlike a partnership, a co-owner is not the "owner" of the property and other co-owners do not have the right to participate in the management of the partnership. Co-ownership does not necessarily result from an agreement and does not necessarily involve a community of profit or loss; a co-owner has no lien for expenses; one co-owner can compel the sale of jointly owned land; and co-ownership does not necessarily have as its purpose the realization of gain (see Lindesay v. Parr in Partnership, supra note 83, Para. 5-05). For tax purposes in Canada, the view of the tax authorities is that the partners do not own the partnership assets.  

101. UK Partnership Act 1890, Sec. 20(2) (and equivalent provisions in New South Wales (Sec. 20(2)) and Ontario (Sec. 21(2)): "Provided that the legal estate or interest in any land, which belong to the partnership shall devolve in the nature and tenure thereto attached."; and Sec. 21 (New South Wales, Sec. 21, and Ontario, Sec. 22): "... property bought with money belonging to the firm..." (emphasis added)  

102. In Canada, see The Queen v. Robinson, 98 DTC 6232 (F.C.A.), in which joint owners through a nominee leased real property to themselves in their capacity as partners; it was held that there was no lease because the partners, not the partnership (which is not a legal entity), were the tenants under the purported lease and the lease therefore did not exist as persons cannot create valid contracts with themselves.  

103. In Ontario, if the partnership name is registered in accordance with the Business Names Act or the Limited Partnerships Act, the Personal Property Security Act requires that security on partnership property be registered in the partnership name.  

104. See the New Zealand Privy Council case of Hadlev v. Comm. of Inland Revenue (1993) 3 TC 294 in which the taxpayer assigned a part share in a partnership to a third party and it was held to remain liable on the partnership's profits on ground that he had no interest of a capital nature to assign and the profits were derived from his duties as a partner. The Australian High Court case of Comm. of Taxation v. Everet (1980) 143 CLR 440 is to the contrary, stating that a partner's share in the partnership consists of a right to a proportion of the surplus after the assets are realized and the debts and liabilities of the partnership are paid. In reaching FT 2540, the Australian Taxation Office took the view that the partner with, for example, a 25% interest in a partnership should be treated as owning a 25% interest in every partnership asset for capital gains tax purposes. This was widely criticized, but was eventually enacted into law (see ITAA 1997, Division 106). In the UK, the statute dealt with this point for capital gains tax from the beginning (see now TCGA 1992, Sec. 59). In Rogers v. Armstrong [1926] S.C.R. 328, the Supreme Court of Canada stated (at 329) that, under the law of Canada's common law provinces, a partner does not have the right to deal with his share of partnership property as his own separate property. A partner can assign his rights to a division of profits and, as to the corpus, to a sale and division of the proceeds on dissolution after discharge of liabilities, but he cannot transfer to another person an undivided interest in the partnership property in specie. These problems reflect the mix of entry and non-entry thinking about partnerships in common law countries.  

105. See the case in note 22, supra, which means that an informal partnership participating in transactions with third parties is governed by the Commercial Code and has the capacity to own assets.
of an English partnership. The difference is a matter of form only. A Dutch formal partnership (VOF) is not a legal person and does not own property despite the property being registered in the name of the partnership. Registration of assets in the name of the partnership is not possible in England, but that is merely a difference in the system of registration.

The differences between the two legal systems concerning the ownership of assets, therefore, follow either from whether the body is a legal person, which, as we have seen, relates to different understandings of what a legal person is or from differences in terminology or rules on registration. It is not clear that the differences should be critical to the categorization of a body created under the other legal system.

### 2.4. Ability of a partnership to sue and be sued

<table>
<thead>
<tr>
<th>Civil law: informal</th>
<th>Common law: England, New South Wales, Ontario</th>
<th>US (Delaware, RUPA) and Scotland</th>
<th>Civil law: formal</th>
</tr>
</thead>
<tbody>
<tr>
<td>Ability to sue and be sued</td>
<td>yes, but only as a convenience</td>
<td>yes</td>
<td>yes</td>
</tr>
</tbody>
</table>

Generally, in all civil law countries, formal partnerships may be party to court proceedings in the partnership name whether or not the partnership is a legal person; informal partnerships cannot, except in Japan and except for Dutch informal partnerships carrying on a profession under a name. Normally, in common law countries, a partnership can be party to court proceedings, but often only as a rule of court rather than a rule of law. A Delaware RUPA partnership can sue and be sued in its own name.

A Scots partnership, which, as a legal person, one would expect to be able to sue and be sued in its own name, can do so only if its name comprises the names of real people. All these are essentially differences in court procedure rather than substantive differences.

### 2.5. Carrying on the activity

<table>
<thead>
<tr>
<th>Civil law: informal</th>
<th>Common law: England, New South Wales, Ontario</th>
<th>US (Delaware, RUPA) and Scotland</th>
<th>Civil law: formal</th>
</tr>
</thead>
<tbody>
<tr>
<td>Type of activity</td>
<td>enterprise and non-enterprise</td>
<td>business</td>
<td>enterprise and non-enterprise</td>
</tr>
<tr>
<td>Profit motive required</td>
<td>no, except in countries following the French tradition</td>
<td>yes (but see exception above)</td>
<td>yes</td>
</tr>
<tr>
<td>Who carries on activity?</td>
<td>partners</td>
<td>partners</td>
<td>partnership</td>
</tr>
</tbody>
</table>

"Enterprise" in civil law and "business" in common law are similar except in relation to professions, which are excluded from the former term and included in the latter, but this is not the occasion to make a detailed comparison. The only significant difference in the type of activity.

106. See notes 93, 95 and 96, supra, for Germany, Switzerland and Italy. Belgium: Code on Civil Procedure, Art. 703; France: under general principles; Italy: Civil Code, Art. 2266 (any partnership can take part in legal proceedings); also Civil Procedure Code, Art. 75 and Corti di Cassazione, 28 January 1993, No. 1027, and 25 July 1989, No. 3498, Netherlands: Code on Civil Procedure, Arts. 4(4) and 5(1); Sweden: Partnerships Act 1980, Chap. 1, Sec. 4 (a Swedish registered partnership "may institute proceedings in courts and before other public authorities"); Quebec: Code Civil, Art. 2225. For Japan, see note 107, infra.

107. Japan: Code of Civil Procedure, Art. 29. This provides that associations and foundations which are not legal persons but have a representative or administrator may sue or be sued in their own name. This provision applies to Civil Code partnerships and foreign partnerships that are not legal persons so long as they have an independent existence on the basis of their organization and activities.

108. Except for New South Wales (where actions are generally in the names of the partners) (Higgins and Fletcher, supra note 88, at 300) and the United States (where actions in the partnership name are permitted by state law in many states). A New South Wales partnership cannot sue in the partnership name. This difference between the two legal systems causes problems when the partnership being sued is from the other system. For a UK case in which it was accepted that, under English procedural rules, a Swiss general partnership (SNC, a formal partnership, see note 23, supra) could be sued in England in the names of the partners, making it clear that they were being sued in their capacity as partners rather than in the partnership name, see Osmann Financing SàRL v. Ruhl and others [1998] 1 WLR 1465. It could equally well have been sued in the partnership name. An earlier case, von Helfift v. B Rechtsmit and Mayer Frères & Co [1914] 1 Ch 748, had decided that a French SNC (see note 33, supra) could not be sued in the partnership name on the ground that it was a partnership and the rules of court enabled only an English partnership to be sued in the firm name.

109. For example, Delaware RUPA § 15-307(a).

110. If it has a descriptive name, it can use the firm's name in the Sheriff Court but not in the Court of Session, where the names of three partners must be added. Law Commission, supra note 56, Para 17.8.

111. See note 22, supra.

112. "Partnership is the relationship between persons carrying on business with a view to profit" (UK Partnership Act 1890, Sec. 1 and equivalent provisions in New South Wales (Sec. 1) and Ontario (Sec. 2)); The expression "business" includes every trade, occupation or profession" (UK Partnership Act 1890, Sec. 45 and equivalent provisions in New South Wales (Sec. 1B) and Ontario, Sec. 1(1), which adds "(enterprises") In Spire Freezers Ltd. v. The Queen, 2001 DTC 5158, the Canada Supreme Court held (at 5162) that the passive receipt of rent may constitute a business for purposes of the common law definition of a partnership. For purposes of the Income Tax Act, however, the same decision in Canada is narrower: Wermann v MNR, 64 DTC 5158. Many common law countries have a limit of 20 partners with exceptions for professional firms, but this does not apply in the US or Canada. The UK is proposing to abolish the limit (Removing the 20 Partner Limit, Department of Trade and Industry, consultation document of 4 April 2001; a draft Regulatory Reform Order was laid before Parliament on 7 May 2002). In New South Wales, there is no limit on the numbers of partners for limited partnerships.

113. Delaware RUPA § 15-202(a); Partnership is the association of two or more persons (i) to carry on as co-owners a business for profit and (ii) to carry on any purpose or activity not for profit. Note the possibility of partnerships other than "for profit", which does not exist in other common law countries.

114. As an exception, although we have categorized the French SC, the German GbR and the Italian società semplificata as formal partnerships, they will not carry on an enterprise as they are civil law bodies. In civil law countries, a formal partnership can only carry on an activity that is not an enterprise, but not in the Netherlands, where a VOF is defined as a maatschap (informal partnership) that carries on an enterprise under a common name (Commercial Code, Art. 16). In countries having a distinction between civil and commercial bodies, a civil body may carry on non-profit making activities (which are not dealt with in this article).

115. See note 114, supra.

116. There can be differences in interpretation. A US limited partnership owning land as a passive investment which would have been regarded by the US as carrying on a business could not be equated with a Dutch CV because it did not carry on an enterprise: Tax Court of Amsterdam, 5 October 1988, No 643/86, Vanstaden-Nieuw, 1860. See also the Spire Freezers case (Canada), supra note 112.
ity that informal civil law partnerships are likely to be carrying on a profession, whereas common law makes no difference between professions and other businesses. There is also little difference in the requirement for a profit motive, the only exception being that informal partnerships do not require a profit motive, except in countries following the French tradition.

There is a difference in who carries on the activity: it is the partnership in a formal civil law partnership, except in the Netherlands, and the partners in all other cases. Surprisingly, it is still the partners who carry on the business in a Scots or a Delaware RUPA partnership, even though the partnership is a legal person and thus has the capacity to do so. This is because carrying on a business by the partners in common (Scotland) or as co-owners (Delaware) is essential to the definition of partnership. The civil law formal partnership is the only type where the partnership carries on the activity. The difference results from a difference in capacity, and it is not clear that this is a real distinction.

2.6. Liability of partners and limited and limited liability, partnerships

<table>
<thead>
<tr>
<th>Civil law:</th>
<th>Common law:</th>
<th>US (Delaware RUPA)</th>
<th>Civil law:</th>
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<tbody>
<tr>
<td>informal</td>
<td>informal</td>
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<td>formal</td>
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<tr>
<td>Norway, Scotland</td>
<td>New South Wales, Ontario</td>
<td>England, Scotland</td>
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</tbody>
</table>

Liability of a general partner:
- varies between countries (see below);
- joint in contract; joint and several in tort;
- joint and several, joint and several.

Limited liability partnerships:
- no (but liability is similar);
- yes in Ontario, but not in New South Wales; it is a corporation;
- yes in England, as it is a corporation (Scotland).

2.6.1. General partnerships

In a civil law formal partnership, liability is on the partnership first, followed by liability on the partners jointly and severally, although in most countries there is nothing to prevent a person from suing both the partnership and the partners at the same time, in case enforcement should be made against the partnership first. A partner's liability is similar to a guarantee of the partnership's liability: in some countries, only an individual can be a partner. A partner joining a formal partnership assumes liability for the existing debts of the partnership, in the same way as a shareholder to whom new shares are issued bears the existing liabilities of the corporation. As we have noted in other respects, the Dutch formal partnership (VOF) is in this regard closer to the common law in not making an incoming partner liable for the existing debts. In a civil law informal partnership that is undisclosed, a partner binds only himself to a third party.

2.6.2. Control of partners and limited and limited liability partnerships

2.6.2.1. General partnerships

In a civil law formal partnership, the partners jointly control the partnership and have equal power, as in each country, although the procedures for passing a decision may differ. In England, for example, if a majority of partners agree, the partnership can be dissolved. The partnership may also be dissolved by the court if it is not possible to agree on the dissolution or if the partnership is dissolved.

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a disclosed informal partnership, the partners are normally equally liable, but in some cases, liability is joint and several (meaning that each partner is liable for the whole with a right to recover a proportionate part from the other partners), but in Sweden only the partner contracting is liable. Liability in tort is personal on the ground that the act of the defaulting partner was not authorized by the other partners. Where an informal partnership operates under a name in, for example, carrying on a profession, a partner acting in the name of the partnership with the authority to do so binds all the partners.

In common law, the liability of partners in contract is joint (meaning that all the partners are liable for the whole, but one partner can be sued for the whole with a right of contribution from the others) and joint and several (which has substantially the same meaning as joint) in tort. Liability in tort is primary, being incurred as a principal or agent of the other partners, and not secondary to the liability of the partnership, as in a formal partnership in civil law. Also, in contrast to the position in civil law, except for the Netherlands, a partner joining a partnership is not liable for the debts incurred by the partnership before he joined because they are the debts of the partners who incurred them; this is also the case in a Scots or a Delaware RUPA partnership in spite of the partnership being a legal person. Liability under a Scots or a Delaware RUPA partnership is joint and several, although the result in Scotland is substantially the same as in England. This liability in Scotland and Delaware is a direct liability that can be enforced against a partner in spite of the partnership being a legal entity but, because the claim must be made against the partnership first, it is similar to a guarantee of the partnership's liability. In both Scotland and Delaware, the partners can be sued in the same action as the partnership. In a Delaware RUPA partnership, however, unlike the position in Scotland, a separate judgement is necessary against a partner before a judgement against the partnership can be satisfied against the partner’s assets, which, subject to some exceptions, cannot be carried out until all the remedies have been exhausted against the partnership assets, thus giving a Delaware RUPA partnership greater entity characteristics than a Scots one. The partner’s separate liability in a civil law informal partnership is an advantage for partners in professional partnerships since it prevents the other partners from being liable for the negligence of one partner. In common law countries, amendments to partnership law were necessary to achieve the same result by creating limited liability partnerships (see 2.6.3.).

The difference in the liability of partners between common law and civil law formal partnerships does not seem to be significant; in both, ultimately all the partners are liable. The difference is that, in an informal civil law partnership, the liability of partners is less than the other types of partnership.

2.6.2. Limited partnerships

Limited partnerships are very similar in common law and civil law. In civil law systems, limited partnerships are a type of formal partnership whose name indicates that it is a limited partnership. In addition to the general partners, there are partners whose liability is limited to their capital contribution and who must not represent the partnership; otherwise, their limited liability is lost. Because civil law makes a distinction between acts of internal and external management, this requirement is less strict than it is in common law countries because some internal manage-

persons, the partners act in the quality of partners (Art 2253). Exceptions are:

Italy: unless there is a stipulation to the contrary, Civil Code, Art. 2251; Netherlands: where the contract is for the benefit of the partnership, Civil Code, Art. 1681; and Japan: where the partners are severally liable, Civil Code, Art. 675 (if the creditor does not know the ratio, he may claim against each partner equally, Art. 675); if the partnership engages in commercial activities, the partners are jointly and severally liable (Commercial Code, Art. 511).

Belgium: Code on Companies, Art. 52. In the Netherlands (Civil Code, Art 1680) and Japan (Civil Code, Art. 675), liability is in equal shares if the creditor does not know the loss-bearing ratios.

Belgium: Code on Companies, Art. 52, for unincorporated partnerships formed to carry on commercial activities (which we have classified as informal partnerships); France: Civil Code, Art. 1872-1, 2nd para.; Switzerland: Code of Obligations, Art. 544(3); Germany: only if all the partners contracted or committed the wrong.

Partnerships Act 1980, Chap. 4, Sec. 5. Liability is also normally joint and several if a name is used which indicates that a partnership is a formal partnership when it is not; see, for example in Sweden, Partnerships Act 1980, Chap. 4, Sec. 6.

Belgium: Code on Companies, Art. 50; Germany: Civil Code, Art. 714; Netherlands: Civil Code, Art. 1679.

UK Partnership Act 1890, Secs. 9 and 12 and similar provisions in New South Wales (Secs. 9 and 12) and Ontario (Secs. 10(1) and 13). The law commissions, supra note 56, propose (in Para. 10.10) that liability in contract be changed to joint and several. Joint and several liability may apply more widely than tort and include all wrongful acts or omissions (see Dubai Aluminium Co Ltd v Salaam [2000] 3 WLR 910), but breaches of trust by a trustee-partner are treated as outside the ordinary course of business of the partnership and are dealt with exclusively by Sec. 13 (see Walker v Stones [2000] 4 All ER 412).

Delaware: RUPA § 15-306(a); Scotland: as a matter of general principle.

Delaware: RUPA § 15-306(c); Law Commissions, supra note 56, Para 4.10 In Scotland, “joint” means liable only for a proportionate share, whereas “joint and several” means that each partner is liable for the whole with a right to recover a proportionate part from the other partners, which is the same as joint liability in England.

“Partners are of course liable jointly and severally in a question with a firm creditor for the obligations of the firm, but the theory of Scots law views them as so liable only subsidiarie, the partners being in substance guarantors or cautioners for the firm’s obligations and each being entitled on payment of a firm debt to relief pro rata from the others.” Mint v Wool, 1948 SC 85, 86, per Lord Presider. See Law Commissions, supra note 56, Para 10.6 This subsidiary liability is different from the liability of a shareholder in an Australian or UK unlimited company, which is solely a liability to contribute in a winding-up of the company.

Scotland: Law Commissions, supra note 56, Para 10.6; Delaware: RUPA § 15-307(c).


The German Partnerschaftsgesellschaft was created for professional partnerships to combine the advantages of having the capacity of a formal partnership with the already existing separate liability in tort of a partner in an informal partnership.

Belgium: société en commandite simple (SCS)g, sgwone commanditaire vennootschap (GCV); Netherlands: commanditaire vennootschap (the open form merely being a type that is taxed differently because the limited partners’ interests are freely transferable). Italy: società in accomandita semplice; Germany: Kommanditgesellschaft (KG); Sweden: kommanditbolag (KB); Japan: goshi-kaisha and, as from 1 November 1998, a new form of transparent limited partnership was introduced by the Law concerning the Limited Liability Partnership Contracts for Small and Medium Enterprise Investment Business (Law No. 90, 1998).

In some countries, only a natural person can be a general partner, e.g. Italy: Civil Code, Art. 2295; Japan: Commercial Code, Art. 55; and Switzerland: Code of Obligations, Art. 594. On the other hand, Louisiana specifically permits a limited partner to be a shareholder of a general partner (Civil Code, Art. 2848(2)). In Sweden, only foundations and non-profit organizations cannot be general partners (Partnerships Act 1980, Chap. 5, Sec 2).
ment is often permitted.\textsuperscript{144} The registration will show who the general partners and the limited partners are and the amount of their capital contributions.\textsuperscript{144} A Dutch limited partnership is closer to an informal partnership since the rights of third parties are against the general partner only, and there are no partnership assets.\textsuperscript{145}

A common law limited partnership shares all the other attributes of a general partnership except, first, that it is registered, although registration is for the purpose of establishing limited liability and does not confer any greater capacity or entity characteristics on a limited partnership than a general partnership; second, that the liability of the limited partners is limited to their capital so long as they do not take part in the management of the partnership;\textsuperscript{146} and third, that the limited partner must put up some capital. The general partners therefore act on behalf of the limited partners, who have no power to bind the partnership, as well as on their own behalf.

Limited partnerships are used extensively in Germany, particularly the type known by the name “GmbH & Co KG”,\textsuperscript{147} where the general partner is a limited company,\textsuperscript{148} often taking no share in the profits of the partnership and with its shares being held by the limited partners, who can be authorized by the general partner by power of attorney to manage the partnership without losing their limited liability.\textsuperscript{149} In this way, the partners, either as limited partners or as shareholders in the limited company, all have limited liability, but the partnership is transparent for tax purposes.\textsuperscript{150} Limited partnership interests in a GmbH & Co KG are often sold to the public accompanied by the issue of a prospectus. Such a partnership may have a board which oversees the business activities and provides information to the limited partners.\textsuperscript{151}

2.6.3. Common law limited liability partnerships
Limited liability partnerships, i.e. partnerships where all the partners have some limited liability, as opposed to limited partnerships, were first introduced in Texas in 1991\textsuperscript{152} in order to limit the liability of professionals compared to the normal liability of the partners in a common law partnership. The scope of the limitation of liability varies. The liability of a Delaware limited liability partnership, for example, whether in contract or in tort, is solely the obligation of the partnership; a partner’s liability is in respect of

\textsuperscript{144} See note 146, infra, for the common law position. For the distinction between internal and external management in civil law, see text at note 40, supra. In addition to a limited partner being able, or being required to, participate in changes to the constitution of the partnership, in France (D 23 March 1967, Art 18) there is no prohibition on limited partners participating in meetings and approving contracts exceeding the powers of the managing partners. In Italy, limited partners are required to approve the appointment of managers (Civil Code, Art 2319), and they can give authorizations and opinions for specified transactions and act for the partnership by virtue of a special power of attorney for individual transactions (Civil Code, Art 2320). In Sweden, the partners can agree to the limited partners taking part in the internal management (Partnerships Act 1980, Chap 3, Sec 4), and they can jointly take part in the management of a partnership in liquidation (id.), but then right to examine the books of the partnership can be excluded by the partnership agreement (id., Sec 6). In Quebec, a limited partner is prohibited from giving more than an advisory opinion with regard to management and from negotiating on behalf of, or acting as an agent for, the partnership. On the other hand, in Germany (Commercial Code, Arts 164 and 170) and Switzerland (Code of Obligations, Art 600), a limited partnership can object only to an extraordinary transaction. In Japan (Commercial Code, Arts 156 and 159), a limited partner may not participate in the affairs of the partnership. Louisiana sets out a detailed list of what a limited partner is permitted to do, including consulting with and advising a general partner with respect to the business of the partnership and attending a partners’ meeting (Civil Code, Art 2844). In Germany, it is not unusual for a limited partner to be appointed by 

\textsuperscript{145} Belgium: Code on Companies, Arts 67-69; France: Commercial Code, Art L 222-4 (legal capacity follows from registration); Germany: Commercial Code, Art 162; Italy: Civil Code, Art 2296; Japan: Commercial Code, Art 149; Netherlands: Act on Commercial Registration, Arts 6 and 7; Sweden: Trade Register 1974, Sec 4; Switzerland: Code of Obligations, Art 255.

\textsuperscript{146} If there is a single general partner, his personal creditors and those of the partnership rank equally. The partnership creditors rank first only if there is more than one general partner.

\textsuperscript{147} Under the UK Limited Partnerships Act 1907, Sec 6(1) and the New South Wales Partnership Act, Sec 67(4), a limited partner may “inspect the books of the firm and examine into the state and prospects of the partnership business, and may advise with the partners thereon.” Under the Ontario Limited Partnerships Act, Sec 12(b), a limited partner may examine into the state and progress of the business and may advise as to its management The UK Law Commissions Consultation Paper on the Limited Partnerships Act 1907 (available at www.lawcom.gov.uk) says (Para 4.12) that “the precise meaning of the words “advise with” is particularly obscure.” It is thought that “advising with” the partners and “advising as to its management” stop short of attempting to persuade the management or to influence management decisions. The Delaware Revised Uniform Limited Partnership Act (\$ 17-303(b)(2)) is wider, permitting the limited partner “to consult with or advise a general partner or cause a general partner … to take or refrain from taking any action, including by proposing, approving, consenting or disapproving, by voting or otherwise, with respect to any matter, including the business of the limited partnership.”

\textsuperscript{148} Because common law does not distinguish between internal and external management in the way civil law does, limited partners may not administer the affairs of the partnership in any internal management; cf civil law formal partnerships in note 143, supra. In New South Wales and three other Australian states, it is necessary to include the words “a limited partnership” immediately adjacent to the firm name on any document issued by the limited partnership (Partnership Act 1892 (NSW), Sec 75). It is not necessary to register a limited partnership under the Business Names Act 1962 (NSW) (Partnership Act 1892 (NSW), Sec 59), though it is in some other states. It seems that there is no need for a UK limited partnership to indicate in its name that it is a limited partnership (and it is prohibited from having the word “limited” in the name; use of “limited” is restricted to corporations) The Ontario Limited Partnerships Act, Sec 6(1) states that the surname of a limited partner shall not be included in the firm name Sec 6(3) is permissive and states that the words “Limited Partnership” may be included in the firm name.

\textsuperscript{149} There were 74,360 such partnerships in 1999, 233 AG & Co Kgs, and a further 25,095 ordinary limited partnerships (KGs). In Sweden, on 31 December 2001, there were 31,354 limited partnerships. By contrast, a limited partnership is rarely used in France. In the UK, in June 2001, there were 8,858 limited partnerships in England and Wales, of which 5,000 to 4,000 are still functioning, and about 3,555 limited partnerships in Scotland, most of which are still functioning (Revenue and Customs’ 20 Partner Limited Liability Partnerships consultation document of 4 April 2001, Para 5.20). In Australia, in 2001, there were 2,412 limited partnerships with an Australian Business Number, which may include some foreign partnerships with a permanent establishment in Australia In the Netherlands, in May 2001, there were 6,658 CVs. In Belgium, there were 1,309 limited partnerships in 1993. In Ontario, there were 9,705 active limited partnerships recorded on 6 December 2001.

\textsuperscript{150} This is not permitted in some countries, see note 142, supra. Limited partnerships having a corporation with limited liability as the general partner were frequently used in the United States before limited liability companies were introduced. Limited partnerships with a corporation as a general partner are commonly used in Australia and the UK.

\textsuperscript{151} This is a common practice with private equity funds as it avoids the characterization of the income of the partnership as business income, which normally applies if the partnership is represented by corporate general partners only or by persons who are not partners.

\textsuperscript{152} There are other tax advantages, such as the treatment on the death of the general partner, and other non-tax advantages, such as the inapplicability of the works council legislation.

\textsuperscript{153} Aufsichtsrat (advisory board), but often translated as supervisory board, although a different concept from the German supervisory board of a corporation as it does not supervise or control the business. The state law adopting them is now based on the Uniform Limited Liability Partnerships Amendments of 1996 to the Revised Uniform Partnership Act.
only of his own negligence or wilful misconduct. This gives even greater protection than a civil law informal partnership for a professional person. In Ontario, a partnership can be formed as a limited liability partnership, with the result that the partners practising a profession, other than the partner at fault, have their liability for malpractice limited to their partnership capital, but have normal joint, or joint and several, liability in all other cases. Limited liability partnerships do not exist in Australia, but legal practices can now incorporate.

In spite of its name, a UK limited liability partnership is a corporation with full legal personality and unlimited legal capacity. Its internal affairs are governed by agreement between the members, which are subject to default provisions similar to those of a partnership. It is normally taxed in the United Kingdom as a partnership. All the members have limited liability as members, and a member’s only liability is similar to that of a director of a corporation. The members are agents of the “partnership” and have power to bind it. Presumably, the reason for creating this new type of corporate body is that its limited liability is more likely to be accepted in other countries, although this carries with it the corresponding disadvantage that, if other countries base their tax treatment on its non-tax law characteristics, they are likely to classify it as a corporation.

3. CATEGORIZATION OF FOREIGN PARTNERSHIPS FOR TAX PURPOSES: COMPARISON OF THE RESULTS OF APPLYING INTERNAL LAW

So far we have looked at the non-tax characteristics of partnerships. We now turn to taxation and consider how foreign bodies are categorized for tax purposes. The methods of doing this vary between (a) determining that all foreign bodies are taxable as corporations (Italy, Switzerland when taxing a permanent establishment or real estate in Switzerland), (b) categorizing a foreign body according to whether it is a legal entity (Belgium, to some extent Canada), (c) allowing the taxpayer to choose the categorization (United States), and (d) trying to fit the body into the closest category of bodies known in internal law (most of the other countries represented). The reason for this last approach is obviously that a foreign body corresponding to a local body should be taxed in the same way, particularly when the tax is on a source basis. This approach raises the difficulty of how to determine whether a foreign body is similar to one’s own partnerships when, as we saw in the previous part, there are wide differences between different types of partnerships, even though virtually none of the differences is as significant as it appears.

3.1. Italy

Italy treats all foreign bodies as opaque, both for taxing their income derived from Italy and for taxing the Italian partners. Surprisingly, few treaties specifically preserve Italy’s right to tax foreign partnerships as opaque: the effect of the treaty’s non-discrimination article might otherwise prevent it. When applying a treaty, the result is different, where the treaty contains an exchange of information provision, the interest and bonds issued by Italian resident banks and Italian quoted companies is exempt from withholding tax when paid to a resident of the treaty country, and the exemption applies with respect to the partners (resident in the treaty country) of foreign partnerships (transparent for tax purposes in the treaty country), rather than with respect to the partnership. As a further exception, the effect of the recent CFC legislation is to treat the share of income attributed to the Italian members of a foreign body carrying on an enterprise (as understood by Italy, but not defined) as business income, rather than as a dividend, which was the previous treatment. This approach, while giving certainty, makes no attempt to determine the nature of the body in the other country.

3.2. Switzerland

Switzerland is similar to Italy in treating all foreign partnerships as opaque for tax purposes, but Switzerland does so only when taxing a permanent establishment or real

153. Delaware RUPA § 15-306
154. See e.g. Legal Profession Amendment (Incorporated Legal Practices) Act 2000 (NSW). As this legislation is not uniform throughout Australia and large law firms operate Australia wide, in practice it is still difficult for lawyers to obtain limited liability.
155. Limited Liability Partnerships Act 2000, Sec 1; Limited Liability Partnerships Regulations 2001, which contain about 50 pages of modifications to the Companies Act 1985, and other legislation as applied to LLPs. The Act came into force on 6 April 2001
156. Limited Liability Partnerships Regulations 2001, Reg 7
157. But only so long as it carries on a trade or profession with a view to profit; if it ceases to do so, it is taxed as a corporation (TA 1988, Sec. 118ZA and TCGA 1992, Sec. 79A). Because it is a body corporate, unlike a partnership, it can be the top company of a VAT group (Business Brief 3/2001)
158. Which may not be particularly great, see Williams v Natural Life Health Foods Ltd (1998) 1 WLR 850 But see Merrett v Burl (2001) 3 WLR 1, where an employed surveyor of a sole practitioner surveyor was held to be liable to a third party for a negligent valuation made by the employee. The distinction may be that the employed surveyor was exercising professional skill in signing the valuation report addressed to the lenders with his name and qualifications and was assuming responsibility to the borrower in a way not contemplated by the director in Williams. If this is the right distinction, a professional member of an LLC may still have significant liability for his own actions.
159. Except where the member had no authority and the person with whom he was dealing knew that he had no authority or did not believe him to be a member, which is the same rule as for partnerships. UK Partnership Act 1890, Sec. 5 and similar provisions in the equivalent legislation in New South Wales (Sec. 5) and Ontario (Sec 6)
160. New South Wales and three other Australian states have rules for recognizing the limited liability of foreign limited partnerships which list the jurisdiction in which they are recognized (Partnership Act 1890, Sec 64 and Partnership Regulation 1997). The list includes 47 of the US states and Quebec (only) in Canada, but no other limited partnerships from the countries represented by the authors, apparently because reciprocity of treatment is required
162. Italy–Greece (1965), Italy–Ireland (1971), former Italy–Israel (1968) and former Italy–United Kingdom (1960) The Italy–Ireland treaty reads: “The provisions of this [non-discrimination] article shall not be construed as affecting the imposition in Italy of the tax on companies (imposta sulle società) charged according to the Italian Law.”
property in Switzerland of the partnership. In other cases, it follows the characterization of the foreign general law, which is the method used in most other countries (see 3.5.). Even in the former case, some comparison with domestic bodies is necessary as the taxation of the entity follows the domestic legal entity it most closely resembles — either (i) a corporation or (ii) an association, foundation or other legal entity,\(^{164}\) the rate of tax on which is lower than that on a corporation.\(^{165}\)

3.3. Belgium

The approach of Belgium is to tax a foreign body as a corporation if it is a legal person in its own country.\(^{166}\) An as exception, where the issue is the taxation of the Belgian-source income of a foreign body, as opposed to the taxation of a Belgian partner in a foreign body, the body is taxed as a corporation not only if it has legal personality but also if it has a legal form comparable to a Belgian corporation with legal personality.\(^{167}\) Where the exception applies, the approach is similar to the method used in most of the other countries represented (see 3.5.).

3.4. United States

The United States lists a limited number of foreign bodies which are always treated as corporations\(^{168}\) and enables the taxpayer to decide how other bodies are categorized by the “check-the-box” regulations. In default of an election by the taxpayer, a foreign entity is (a) treated as a partnership if it has two or more members, at least one of whom does not have limited liability, (b) treated an association if all the members have limited liability, or (c) disregarded if it has a single owner who does not have limited liability. The check-the-box regulations give certainty but, because the categorization results from the taxpayer’s choice rather than any differences between the bodies, this method is not likely to be accepted by other countries.\(^{169}\)

Before the check-the-box regulations were adopted in 1996, the determination of whether a business enterprise was taxable as a corporation was based on whether the enterprise’s corporate characteristics were such that the enterprise more nearly resembled a corporation than a partnership, which is the position in most of the other countries discussed in 3.5. The characteristics that were deemed to separate partnerships from corporations were (1) centralization of management, whether in some members or non-members, (2) continuity of life upon the death, insanity, bankruptcy, retirement, resignation or expulsion of a member, (3) limited liability, and (4) free transferability of interests without the consent of the members so as to substitute the transferee as a member of the organization.\(^{170}\) The absence of two of these characteristics resulted in the classification of the organization as a transparent partnership. These tests were applied to both domestic and foreign organizations. With the increased use of Treasury resources to classify organizations, the Treasury decided to replace the increasingly formalistic rules with the simpler approach of “check the box”, except in the limited number of specifically-listed organizations in each country.

3.5. Other states: Introduction

Most of the other countries represented, including Australia, Canada, France,\(^{171}\) Germany, Japan, the Netherlands, Sweden, Switzerland (when taxing the partners) and the United Kingdom,\(^{172}\) compare the attributes of a foreign body with domestic bodies and tax the foreign body in the same way as the equivalent domestic one. In some cases, countries do this by listing the attributes of a domestic partnership in a way similar to the former US approach. The tax authorities in the United Kingdom, the Netherlands and Germany have published the criteria they use for categorizing foreign entities as transparent or opaque for tax purposes, and Sweden has a definition of foreign legal entity in its tax law. This approach has its limitations in

164. Federal Law on Direct Federal Tax, Arts. 11 and 49(3)
165. Torrione, Henri, Chapter on Switzerland, in The International Guide to Partnerships (Amsterdam: IBFD Publications, 1996). See also Donati, Davide G S, Bestimmung ausländischer Personengesellschaften in der Schweiz (Bazel, 2001), at 3 et seq
166. Court of Appeal of Brussels, 4 June 1974, I D F , 1975, at 82, concerning a French societé civile immobilière, and Official Commentary on the Income Tax Code, No. 179/8 and 9. See Court of Appeal of Brussels, 30 April 1998, discussed by M. van Keitsch in 38 European Taxation 8 (1998), at 249: where it was unclear whether the body had legal personality, the Court looked at whether the foreign body possessed the general characteristics associated under Belgian company law with having a separate legal personality, such as a joint capital account versus separate capital accounts for the partners; resolution to distribute profits versus direct attribution of income/profits and expenses/losses to each partner; continuity of life; possibility of withdrawal before dissolution; and liability of the partners. The Court was wrong to look at the partners’ liability as this is not a feature of legal personality under Belgian company law. The Court also ignored relevant features, such as name, transfer of partnership interest and the ability to sue and be sued.
167. Income Tax Code, Art 227, 2nd
168. Normally, only one type of body is treated as a corporation in a particular country, for example, Australia: public limited company; Canada: corporation and company; France: SA and SAS; Germany: AG; Italy: società per azioni; Japan: kabushiki-kaiisha; Netherlands: NV; Sweden: publika aktiebolag, Switzerland: AG; United Kingdom: plc. This list does not always reflect substantial differences between the bodies that are included or excluded. For example, in Sweden, the only difference between a public company, which is included, and a private company, which is excluded, is the amount of capital; and a UK limited company is virtually identical to a plc in its corporate characteristics.
169. In a question-and-answer session by Joseph Guttentag published in Tax Notes International, 14 January 2002, he suggests that the rules would be suitable for use in the European Union if a way could be found to prevent loss of revenue, as was originally intended in the United States. There are now proposed regulations which apply where a CFC elects to treat a subsidiary as transparent prior to a sale of the shares in order to avoid Subpart F income. See Prop. Regs § 301.7701-3(b)
170. Since these tests are no longer used, we shall not show the effect of applying them to civil law bodies. It is worth pointing out, however, that centralization of management in only some of the partners is frequently found in civil law partnerships; a German formal partnership that is not a legal person has continuity of life; limited liability is not a distinguishing feature of a corporation even in common law systems since unlimited companies exist in Australia and the UK, and many common law countries have L.P.;s; and free transferability is considered in relation to the Dutch tests.
171. France has rules applicable to US partnerships in the 1994 United States-France treaty only, which have regard to whether the partnership is disclosed, the transferability of partnership interests and, in particular, the liability of the partners (a partnership requiring joint and several liability of the partners, and a corporation requiring limited liability of all the members). These rules apply only where France is the source state with regard to the taxation of the US partners. The same rules are applied in the absence of a treaty.
172. And Belgium which was included above, but only to determine whether, in the case of a body deriving Belgian-source income, the body has a legal form comparable to a Belgian corporation having legal personality; see text at note 167, supra.
light of the difficulty of understanding the background and terminology of the other systems of law described in 2. Ideally, a country asking a question needs to know the answer to the question as understood in its system of law, not the other country’s system. But some questions can be answered only from the point of view of the other system, which may understand the concepts in the question differently. We have illustrated this in our discussion of whether a partnership is a legal person. If a country categorizes a body by asking whether it is a legal person (Belgium and usually Canada), the country asks the question with its own understanding of legal person in mind (for example, Canada equates legal person with capacity), but it is the other country which answers the question whether its partners are legal persons, using the meaning of legal person in its law. Interpretation Bulletin IT-343R, issued by the Canada Customs and Revenue Agency, deals with what is a corporation and defines a corporation by saying that it is:

an entity created by law having a legal personality and existence separate and distinct from the personality and existence of those who caused its creation or those who own it. A corporation possesses its own capacity to acquire rights and to assume liabilities, and any rights acquired or liabilities assumed by it are not the rights or liabilities of those who control or own it. As long as an entity has such separate identity and existence, the Department will consider such entity to be a corporation even though under some circumstances and for some purposes the law may ignore some facet of its separate existence or identity.

This approach is difficult to apply to a partnership formed in a country that does not equate legal personality with legal capacity, such as Germany, Italy and the Netherlands, where a formal partnership has legal capacity but is not a legal person; Canada has classified a German formal partnership (oHG) as a partnership. This approach is also difficult to apply to bodies which have both legal personality and the capacity to own assets: a French formal partnership (SNC) and a Delaware RUPA partnership have been classified as partnerships, while a Kazakhstan limited liability partnership has been classified as a corporation, although these bodies appear to be identical in their legal personality. The fact that a French SNC and a Delaware RUPA partnership, both of which are legal persons, are regarded as partnerships means that the test applied in Canada cannot simply be whether the body is classified as a legal person by the other country’s law. Similarly, a decision of the French Conseil d’État treated a Dutch limited partnership (CV), which is not a legal person, as transparent. Swedish law (see 3.9) overcomes this difficulty by defining foreign legal entity in a way that does not depend on the other country’s view of what a legal entity is. Elsewhere, where the other country does not have the same understanding of the question of what constitutes a legal person, it is unlikely that the answers will be meaningful.

Table 3 gives a broad summary of the questions asked by the German, Dutch and UK tax authorities and by Swedish law to determine whether a foreign body corresponds to a domestic one. The actual questions are set out below.

173. This may no longer be the sole test in Canada in view of the ruling on a French formal partnership (see note 178, infra) and the revised ruling on a Delaware RUPA partnership (see note 179, infra). It has been suggested that a possible distinction is whether the legal personality is given by statute or, as in the case of the Delaware RUPA partnership, by agreement, but a French SNC derives its legal personality pursuant to the Civil Code as a result of registration and not by agreement.

174. In Australia, the question of classification of foreign entities has not arisen often. In Clyne v. Comm. of Taxation (1983) 14 ATC 509, the nature of an Anstalt was raised, but was not necessary to deal with the matter as the transactions involving the Anstalt were found to be a sham. More recently, the treatment under Australia’s CFC legislation of the residence of limited partnerships and limited liability partnerships formed in the UK and the US was raised in a draft ruling (TD 2001/D14), but it is clear that they are companies for tax purposes from Australia’s point of view (see note 16, supra). A company is defined for tax purposes to include “all bodies or associations corporate or unincorporated, but does not include partnerships”, and partnership is defined (in part) as covering partnerships under partnership law. On the basis of this legislative construct, it is possible to argue that a body corporate (i.e. legal person) may still be a partnership, but decisions on domestic entities have suggested that a legal entity cannot be a partnership for tax purposes (i.e. legal person – and the things that go with it in the common law tradition, such as a common seal and the capacity to hold property and sue in its own right – is a critical factor in this decision). In this connection, the UK proposal to make English partnerships legal persons (see text at note 82, supra) may be important. If the entity is not a legal person, the decisions look to factors such as management and transferability of interests. See Case 85 (1943) 11 CTR 173 and Case 1173 (1957) 8 TBRD 337.

175. IT-343R lists 23 bodies which are regarded as corporations. It does not include any of the bodies described as partnerships in this article. There is also an Interpretation Bulletin, IT-90, concerning partnerships, but this deals only with domestic partnerships.

176. The courts take a similar approach. In the only case on the topic, Mathewson v. MNR, 63 D.T.C. 490, the Tax Appeal Board (the predecessor of the Tax Court of Canada) dealt with a claim by a US citizen resident in Canada who was a shareholder of a US "Subchapter S corporation" that he should be entitled to deduct his share of the corporation’s loss in computing his income for Canadian tax purposes. In dismissing the taxpayer’s claim, the Tax Appeal Board pointed out that Canada’s income tax law has no provision for a company to elect to be treated as a partnership; nor, where such a company incurs a loss, is there a provision for the shareholder to deduct the loss proportionately from his other income. The Board also pointed out that the Canada–United States tax treaty had no provision covering such a situation. The Board said that "for the purposes of the Canadian income tax law, [the] company is a separate and distinct entity from either the taxpayer or his co-shareholder and therefore cannot be treated as a partnership, irrespective of any election by the company’s shareholders to have it so treated under the provisions of the Internal Revenue Code of the United States”.

177. An interpretation letter classifies a German oHG as a partnership (No. 9419255 of 25 October 1994).


179. Initially, it was classified as a corporation in an interpretation letter of 25 July 2000, which was withdrawn, and it was subsequently classified as a partnership.


181. Diebold Courtoise, 13 October 1999, and commentary by J-P Le Gall in Droit fiscal, No. 15, 12 April 2000. Contrary to his view, it has been suggested that the court might have come to a different decision if the partnership had been a legal person See Vogel, Klaus, “Tax Treaty News”, 54 Bulletin for International Fiscal Documentation 10 (2000), at 502 (Characterization of income of foreign partnerships in France), agreeing with a comment by Haimut Hahm in Internationale Steuerrecht 2000, at 202.

Table 3: Summary of categorization questions in different countries

<table>
<thead>
<tr>
<th></th>
<th>Netherlands</th>
<th>UK</th>
<th>Germany</th>
<th>Sweden</th>
</tr>
</thead>
<tbody>
<tr>
<td>Resolution to distribute profits</td>
<td></td>
<td>x</td>
<td></td>
<td>x*</td>
</tr>
<tr>
<td>Limited liability</td>
<td></td>
<td>x</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Ownership of assets</td>
<td></td>
<td></td>
<td></td>
<td>x</td>
</tr>
<tr>
<td>Interest in the body freely transferable</td>
<td></td>
<td>x</td>
<td></td>
<td>x</td>
</tr>
<tr>
<td>Capital is divided into shares</td>
<td></td>
<td>x</td>
<td></td>
<td>x</td>
</tr>
<tr>
<td>The body is subject to foreign taxation</td>
<td></td>
<td>x</td>
<td></td>
<td>x</td>
</tr>
<tr>
<td>The body has separate legal existence</td>
<td></td>
<td>x</td>
<td></td>
<td>x</td>
</tr>
<tr>
<td>The business is carried on by the body</td>
<td></td>
<td>x*</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Responsibility for liabilities of the body</td>
<td></td>
<td></td>
<td></td>
<td>x</td>
</tr>
<tr>
<td>The body can be party to court proceedings</td>
<td></td>
<td>x</td>
<td></td>
<td>x</td>
</tr>
<tr>
<td>The owners can dispose of the body's assets</td>
<td></td>
<td></td>
<td></td>
<td>x</td>
</tr>
<tr>
<td>Management by the members</td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Preservation of capital</td>
<td></td>
<td>x</td>
<td></td>
<td></td>
</tr>
</tbody>
</table>

* Test is regarded as important

Not surprisingly, there is little similarity between the tests because they are each trying to describe the features of a domestic partnership, which are bound to be different in each country; there is, for example, no test that is common to all four countries. The four countries' tests make an interesting comparison because the countries comprise (a) a civil law jurisdiction where formal partnerships are legal entities having entity characteristics which are at the top end of the spectrum (Sweden), (b) a country with fewer entity characteristics (Germany), (c) a common law country containing jurisdictions where partnerships are, and are not, legal persons (Scotland and England), and (d) a civil law jurisdiction (the Netherlands) that is out of line with the other civil law jurisdictions and closer to the common law, which categorizes not only foreign, but also domestic, partnerships for tax purposes according to their characteristics, rather than treating all partnerships in the same way.

We shall test the merits of these methods of asking questions in order to determine whether a foreign country's bodies are similar to one's own partnerships by applying the Swedish and German tests to a common law partnership, the United Kingdom's tests to a civil law partnership, and the Dutch tests to both civil law and common law partnerships because of the differences between Dutch law and both systems.

3.6. Dutch tests

3.6.1. The six tests

The tests below, which are laid down in a Decree of the tax administration, are applied only where the Netherlands is the residence country of the partners, although the tests are not universally accepted as being in accordance with case law. If all the tests are satisfied, the foreign entity is considered opaque. The tests are applied to the particular partnership agreement and not to the partnership law in the other country generally. The result of applying the tests to other countries' partnerships is indicated below.

(1) Is a resolution required to distribute profits? If the test were applied to either type of Dutch partnership, the answer would be no, although frequently limits are placed on a partner's drawings, which do not affect the transparency of the partnership. The answers for the other states are that a resolution is required in Belgium for a formal partnership, a resolution may be required in Germany and France for a formal partnership and in Germany also for an informal partnership, but otherwise a resolution is not required. Such a resolution is not required in the common law countries as a matter of law because, once the profits are ascertained and divided among the partners, they belong to the partners in com-
mon, which is the same as saying that they belong to the partnership; agreement of the partners is, however, required for an individual partner to draw his share of profits. It would be formal for a common law partnership agreement to regulate drawings of profits because the existence of a profit does not mean that there is cash that can be drawn. It is interesting that the Netherlands regards this as one of the most important tests, and Dutch law on this is different from many other civil law countries.

(2) Is liability limited to the capital contribution? The meaning of this is clear, and the answer is universally no in both common law and civil law partnerships, except for a limited partnership where some partners have limited liability and others do not. A limit may also be found in silent partnerships.\(^{191}\)

(3) Is the entity the owner of the assets used for conducting the business operations? If the test were applied to either type of Dutch partnership, the answer would be no. Implied in this question is that, although in the Netherlands legal capacity and legal person are not equivalent, a partnership that is not a legal entity cannot be the owner of assets. The answer in common law is that the partners, and not the partnership, are the owners of the assets, although there is a concept of partnership property, except that Scots and Delaware RUPA partnerships as legal persons are the owners of the assets. In civil law, a formal partnership is generally regarded as the owner of its assets, even when it does not have legal personality; an informal partnership does not own the partnership assets.

(4) Are interests in the entity freely transferable? This means transferable without the consent of all the other partners.\(^{192}\) If this test were applied to either type of Dutch partnership, the answer would be that the interests are not freely transferable, but the partnership agreement may provide that they are. In both common law\(^{185}\) and civil law partnerships, a partner’s share in a partnership is not transferable without the consent of the other partners. This is normally also the case for limited partners’ interests, although partnership agreements sometimes provide that limited partnership shares are freely transferable.\(^{194}\) In the United States\(^{195}\) and Canada, interests in limited partnerships are sometimes issued to the public, are freely transferable and may be listed on stock exchanges.

(5) Is the capital divided into shares? For this purpose, the term “shares” means an equal or proportionate interest that can be transferred without the consent of all the partners. As stated above, a Dutch partnership does not have shares\(^{196}\) that are freely transferable unless the partnership agreement so provides. Other countries do not usually regard their partnerships’ capital as being divisible into shares, except for French\(^{197}\) and Belgian formal partnerships and, in any case, in those countries such shares cannot be transferred without consent. Although a UK limited liability partnership is a corporation, the provisions of company law on shares are not applicable.\(^{198}\)

(6) Is the entity subject to foreign taxation? If the test were applied to either type of Dutch partnership and to domestic (as opposed to foreign) tax, the partnership could be liable to corporate income tax but only if, for tax purposes, it is regarded as having shares that are transferable without the consent of all the other partners. A limited partner’s interest is taxed if the limited partner’s share is freely transferable. In other common law and civil law countries, a partnership (except a Japanese or Belgian formal partnership) is not normally liable to tax,\(^{199}\) although it could elect to be taxable in France, the United States (under the check-the-box rules) and, from 1 January 2002, Italy.\(^{200}\) Limited partnerships are taxable in Australia, Belgium, France (as to the limited partners) and Japan.\(^{201}\) This test is interesting as it applies to the taxation of a partner in a foreign partnership, whereas most of the tests are aimed at taxing foreign partnerships on a source basis in a way similar to domestic partnerships. The test is also interesting in that it considers the other country’s tax treatment.

3.6.2. Partnerships that do not satisfy all six tests

In many cases, a partnership satisfies only some of these tests, in which case it is not prima facie opaque. The Dutch

\(^{191}\) See text at note 31, supra.

\(^{192}\) The shares in an Australian, Ontario or UK private company where (normally) the directors’ consent is needed to transfer shares would, therefore, be regarded as freely transferable.

\(^{193}\) See note 100, supra, for the transfer of partnership shares in common law countries.

\(^{194}\) No consent is required for the transfer of a share in a Quebec limited partnership (Civil Code, Art. 2243) The consent of the other partners to the transfer of a partner’s share is required in Belgium (Code on Companies, Art. 209, France (Commercial Code, Art. 221-13), Germany (Civil Code, Art. 719), Italy (Civil Code, Art. 2252) and Sweden (Partnerships Act 1980, Chap. 2, Sec. 2); the consent of the unlimited partners is required in Japan (Commercial Code, Art. 154). In Ontario, a limited partner’s interest in the partnership is assignable, but a distinction is made between an assignment without consent, which carries a right to profits, and assignment to a “substituted limited partner”, which requires the consent of all the partners (or a provision in the partnership agreement) and carries with it all the rights of the assignor as a limited partner (Ontario Limited Partnership Act 1990, Sec. 18). In New South Wales and the UK, unless the agreement provides otherwise, the consent of the general partner is required (Partnership Act 1892 (NSW), Sec. 69; Limited Partnership Act 1907, Sec. 6(5)(b)). Under the Delaware Revised Uniform Limited Partnership Act § 17-702, a partner’s share is transferable, but the transferee is not entitled to exercise any of the rights or powers of a partner. In Sweden, limited partnership interests are transferable only to the extent that the partnership agreement provides. Where the law requires consent but the partnership agreement provides that no consent is required to a particular transfer, this may be construed in the Netherlands as an advance consent, with the result that consent is still required.

\(^{195}\) As a result of loss of tax through the elimination of corporate tax, the US Internal Revenue Code (IRC) was amended to provide that a limited partnership whose interests are readily tradeable is taxed as a corporation (IRC § 7704(a)). Since the partners are subject to tax on the income whether or not distributed, it is common to find in most partnership agreements a requirement that at least 40% to 45% of the profit be distributed annually in order for the partners to have sufficient cash to satisfy their income tax liability.

\(^{196}\) In Hoge Raad of 24 December 1976, BNR 1978/13, the Netherlands Supreme Court held that the capital of the civil law (informal) partnership in the case was not divided into shares and that shares meant interests divided into equal or proportionate parts which could be transferred without consent. The Netherlands Commercial Code (Art. 19(3)) provides that limited partners do not have share capital.

\(^{197}\) This is accepted by the Dutch tax authorities as the Decree treats a French SNC as a company whose capital is divided into shares and, accordingly, a Dutch company qualifies for the participation exemption even though the SNC as such is not taxed in France; tax is instead levied on the partners.

\(^{198}\) Limited Liability Partnerships Regulations 2001, Sch. 2.

\(^{199}\) See note 15, supra, for the taxation of limited partnerships. A German formal partnership is liable to municipal trade tax, but an informal partnership, with rare exceptions, is not.

\(^{200}\) Law of 23 December 2000, No. 388.

\(^{201}\) See note 15, supra.
tax authorities then proceed to determine whether a body is transparent or opaque by applying a further test. For this purpose, a distinction is made between limited partnerships and other entities. An entity is considered to be a limited partnership for this purpose if: (a) the limited partners have a limited liability for the partnership’s debts, (b) the assets used to operate the partnership business are owned by the general partner, and (c) the limited partnership does not have rights and liabilities of its own. This is a somewhat restricted definition of a limited partnership, particularly (b) and (c), which seem to be peculiar to the Netherlands. It would not, for example, include limited partnerships that are legal entities, as in Belgium, France, Japan or Sweden; Scots and Delaware RUPA partnerships; limited partnerships that are not legal entities but are considered to own their assets and have rights of their own as formal partnerships, as in Germany, Italy and Switzerland; or common law limited partnerships where the assets are not owned by the general partner but by all the partners in common.

In respect of foreign entities other than limited partnerships, if the foreign entity is the owner of the assets, it is opaque unless the business is effectively carried on for the risk and account of the partners (which is assumed if no resolution is required for the distribution of partnership profits). The result of applying this test to partnerships in countries represented by the authors is that, while a formal partnership is usually regarded as the owner of its assets even in countries where the partnership is not a legal entity, normally no resolution is required as a matter of law to distribute profits, except that a resolution is required in Belgium for a formal partnership and may be required in Germany and France for a formal partnership and in Germany also for an informal partnership. Commonly, a resolution will be required in the partnership agreement for drawings as a matter of prudence. In countries where such a resolution is required and the partnership owns its assets, which is the case for a formal partnership, the partnership is treated as opaque; in all other cases, it is transparent. In common law countries, presumably the situation is similar to that in the Netherlands — that it is more correct to say that the partners own the assets even though there is a concept of partnership property. Where a common law partnership is considered to own its assets, as is the case with Scots and Delaware RUPA partnerships, although no resolution is required by law to distribute profits, it is likely to be a requirement found in the partnership agreement, so that the partnership would be treated as opaque.

For a limited partnership within the above definition, the only criterion that determines whether a foreign limited partnership is to be treated as opaque is whether a partnership interest can be transferred without the consent of all the partners. Whether a limited partner’s share is transferable, and hence whether the partnership is treated as transparent, may depend on the terms of the partnership agreement.205 Although this means that categorization of foreign bodies for Dutch tax purposes depends on the terms of the partnership agreement, the same is true of domestic partnerships.

In summary, these tests are more successful when applied to a common law partnership because of the greater similarity between Dutch and common law partnerships. Many civil law general partnerships are regarded as the owner of their assets and require a resolution to distribute profits, in which case they are treated as opaque, while still being similar to a Dutch partnership. The test applied to limited partnerships depends on the definition of a limited partnership. The Netherlands differs in its definition from all the other countries represented by the authors.

3.7. United Kingdom tests

The Inland Revenue has published an entirely different set of tests which it uses, and they are set out below.206 An overall conclusion is reached from looking at all the factors together, but particular attention is paid to the factors in (3) and (4). The conclusion reached is then applied to the relevant piece of UK tax law, which may not result in the same answer in all cases, as the relevant UK tax law may work in different ways. The result of applying these tests to a civil law partnership is indicated below.

(1) "Does the foreign entity have a legal existence separate from that of the persons who have an interest in it?"

As mentioned earlier, there are no degrees of legal capacity in the United Kingdom: either there is a legal person with full capacity or there is not,207 although the Scots partnership is an exception. But even an English partnership must in some sense have an existence separate from the partners, for example, because the contractual obligations are incurred jointly and there is the concept of partnership property. Since, in the United Kingdom, legal existence is determined by the capacity of the body, there is an overlap between this and some of the other questions

202 This seems to be unique to Dutch limited partnerships, and the result is that a sole general partner’s personal and partnership credits rank equally (see note 145, supra). It seems to reflect the absence of a Dutch silent partnership (see note 33, supra).
203 If no resolution is required to distribute an SNC’s profits, the SNC is accepted by the Decree as transparent and, accordingly, the profits attributable to a French permanent establishment are exempt. If a resolution is required to distribute profits, the SNC is accepted as a company with capital divided into shares, with the result that the participation exemption applies to the Dutch corporate partners even though the SNC as such is not taxed in France (since the partners are taxed). The individual partners are taxed on the distribution with a credit for the French tax on the distribution.
204 This is the view of the Ministry of Finance. In its decision of 13 April 2000, No 0000101 (Vakstude-Nieuws) 2000/40.5, however, the Lower Court of Arnhem ruled that a limited partnership is transparent if any of the partners must consent.
205 See note 194, supra.
206 Tax Bulletin, February 1999, at 627. Examples of the result of applying this UK approach are given in Tax Bulletin, December 2000, at 809. This treats as transparent the bodies that we have included as partnerships in Canada and the United States (under the Uniform Partnership Act and Uniform Limited Partnership Act, but the Delaware RUPA partnership is not dealt with); formal partnerships in Belgium (SNC only), France (SNC, SCS and société en participation, but not société civile immobilière or société civile agricole), Germany (HG, KG and Gbr), Japan (gomi-kaisha and goshi-kaisha), the Netherlands (VOF and both open and closed CVs); and informal partnerships in France (SF), the Netherlands (maatschap) and Switzerland (société simple). The German stille Gesellschaft is treated as opaque, as in Memec v IRC [1998] STC 754 (see note 34, supra). An attempt to challenge the Revenue’s opinion that a Jersey limited liability partnership would be taxed as a corporation failed on procedural grounds, and the court did not give any indication on the substantive issue. R v IRC ex p Bishop [1999] STC 531. The issue does not arise in relation to a UK LLP because of specific tax legislation.
207 See text at note 73, supra.
discussed below because a test of whether a body has a legal existence includes its capacity in (3) to carry on business, in (4) to own the profits, and in (6) to own its assets. Conversely, for countries where legal capacity and legal person are not equivalent, these questions are difficult to answer.

This test is hard to apply in civil law countries, which generally accept the existence of degrees of capacity. Civil law partnerships clearly have a separate legal existence in countries which regard them as legal persons. Where a formal partnership is not a legal person in civil law, it will have sufficient capacity to indicate that it has a separate legal existence, and an informal partnership will generally not have a separate legal existence (see 2.3).

(2) "Does the entity issue share capital or something else that serves the same function as share capital?" Share capital is the interest of the owners of a corporation which is easily transferable and, on transfer, the transferee stands in the shoes of the transferor as owner of that proportion of the ownership interest in the corporation. There is no implication that a share must be transferable without consent. Normally, with private companies, which form the majority of companies, the consent of the directors, though not the other members, is required for a transfer of shares. In the United Kingdom, a share in a partnership is an asset that can be assigned, although the effect is different from the transfer of the share capital of a corporation since the assignee will not thereby become a partner. The assignee is entitled to the assignor's share of profits, but must accept the account of profits agreed by the partners. The assignee is not entitled to interfere with the management or administration of the partnership business, to require any accounts of the partnership transactions, or even to inspect the partnership books. This result is the same as for a shareholder in a company, but the difference is that the transferor shareholder did not have these rights, whereas a transferor partner did. Therefore, a UK general partnership does not have anything that serves the same function as share capital. However, in the case of a limited partnership where a limited partner assigns his share without needing the consent of the general partners, the assignee becomes a limited partner, which is similar to the case where there is share capital.

Belgian and French formal partnerships could be said to have shares. In other civil law countries, a partnership does not have shares.

(3) "Is the business carried on by the entity itself or jointly by the persons who have an interest in it?" This and the following test are regarded as the most important. Inherent in this question is the equating of legal capacity with being a legal person. If there is a legal person, it has the capacity to carry on business; if there is no legal person, as in the case of an English partnership, the partners must be carrying on the business jointly. Scots and Delaware RUPA partnerships are in the strange position that, although they are legal persons and would have the capacity to carry on business, it is nevertheless the partners that carry on the business because the definition of partnership requires this. Therefore, in the United Kingdom, this is a factor that clearly differentiates partnerships from corporations, which is presumably why it is regarded as one of the two most important tests.

There is a problem with the question referring to the business carried on by the entity because, in many civil law countries, a partnership need not carry on a business (enterprise) at all. Leaving that aside, a formal partnership in civil law countries does, because it possesses greater entity characteristics than a common law partnership, carry on the business either because a legal person naturally carries on its own business or, if it is not a legal person, because it has the capacity to do so in those countries where legal capacity does not determine what a legal person is (see 2.4). The partners carry on the activity of an informal partnership. Because of the UK definition of partnership, one can understand why this is regarded as an important test in the United Kingdom, but the answer for all formal civil law partnerships will be different from the answer for a UK partnership. It is not clear that the difference should be material.

(4) "Are the persons who have an interest in the entity entitled to share in its profits as they arise; or does the amount of profits to which they are entitled depend on a decision of the entity or its members, after the period in which the profits have arisen, to make a distribution of its profits?" This and the previous test are regarded as the most important. Implied in this question is the distinction between a corporation, which requires a resolution to distribute profits to the members (in the absence of which the profits remain that of the corporation), and a partnership, where all the profits belong to the partners as they arise, the only question being when a partner can draw them. The United Kingdom Partnership Act is silent on the distribution of profits, and a resolution to distribute profits is thus not necessary even in Scotland, where the partnership is a legal person. It is, however, normal for the partnership agreement to regulate drawings since the existence of profit does not mean that there is cash available for drawings. It is thought that this question is aimed more at entitlement to profit than to drawings.

In many civil law countries, owing to the greater entity characteristics of formal partnerships, the same clear distinction between a corporation and a partnership as is possible in the United Kingdom cannot be made. A resolution is often required for the distribution of profits, as we saw in relation to (1) of the Dutch tests. This is the other test regarded as important by the United Kingdom; it is unfortunate that, in many cases, the answer is likely to depend on the terms of the partnership agreement so that the result may be similar to giving the taxpayer the choice of how to characterize the body in a way similar to the US check-the-box regulations.

(5) "Who is responsible for debts incurred as a result of the carrying on of the business: the entity or the persons who have an interest in it?" As before, this question impliedly equates legal capacity with legal personality. If

208 Partnership Act 1890, Sec 31. The position is the same for LLPs; on the assignment of a member's whole share, neither the former member nor the assignee can interfere in the management or administration of the business of the LLP, Limited Partnership Act 2000, Sec 7.

209 Limited Partnership Act 1907, Sec 6(5)(b)
the body is a legal person, it has the capacity to incur debts for which only it is responsible; if it is not, the members must be responsible. In many countries, however, because of the capacity of a partnership that is not a legal person to incur debts, the distinction is not so clear. There is also the difference within the United Kingdom that, in England, the liability of the partners is the only liability and, in Scotland, the partnership is liable first and the partners are secondarily liable in a way similar to a guarantee of the partnership’s liability.

For a civil law partnership with unlimited liability, both the partnership and the partners are liable for the partnership debts (see 2.6.). One could generally say that, for a formal partnership, the entity is liable first but, in Belgium, Germany and Sweden, the partners can be sued at the same time as the entity. For an informal partnership without legal personality, the partners are liable for their proportionate share.210

(6) “Do the assets used for carrying on the business belong beneficially to the entity or to the persons who have an interest in it?” Also implied in this question is that legal capacity is equated with being a legal person. In the United Kingdom, if the body is a legal person, as in the case of a Scots partnership, it has the capacity to own its assets; if it is not, only the members can own them.

As with the previous question, in most civil law countries, the answer is that both alternatives apply to a formal partnership: the partnership owns the partnership assets but the partners have residual ownership (see 2.3.). For an informal partnership, the partners own the assets.

In summary, the United Kingdom tests are not particularly successful when applied to civil law partnerships, particularly those where legal capacity is not equated with legal personality. For the most important tests, (3) and (4), a different answer may be given for a civil law partnership which is not very different from a UK partnership because civil law regards a partnership as more of an entity while still not being similar to a corporation. In (5) and (6), both alternatives commonly apply.

3.8. German tests

Case law in Germany, as interpreted by a letter from the Ministry of Finance,222 has developed four guidelines for characterizing foreign entities. These guidelines and the effect of applying them to a common law partnership are indicated below.

(1) Whether the members have personal liability. Members do have personal liability in a German partnership. The partners in a common law partnership have personal liability, but so do the members ultimately of a UK unlimited company.

(2) Whether there is an entity legally separate from the members. A German partnership is not classified as a separate legal entity. A common law partnership (except a Scots or a Delaware RUPA partnership) is not a separate legal entity, but the common law meaning of legal entity is clearly different from that in Germany. It is likely that common law countries would classify a German formal partnership as a legal entity if they had an equivalent body since it can acquire rights and obligations and own property, although Germany does not classify it as a legal entity.

(3) Whether management is centralized and may include non-members. For a common law partnership, as in a German partnership, management is in the hands of the partners and is not centralized or in the hands of non-members.

(4) Whether there is a requirement to preserve capital. There is no such requirement for a German general partnership, although there is a requirement for a limited partnership. There is also no such requirement for a common law partnership, but nor is there for an Australian or UK unlimited company.

There is no statement dealing with entities that satisfy some, but not all, of the tests; the tests are intended as guidelines only. While a common law partnership is classified as a partnership, it seems that two of the four tests could be satisfied by some common law companies as well.

3.9. Swedish tests

Sweden’s definition of foreign legal entity does not depend on whether the other state classifies the body as a legal entity.213 To qualify as a foreign legal entity, the body must pass all of the three tests indicated below according to the law of its domicile.214 Unlike the Netherlands tests,
the Swedish tests are applied to the general law of the other state and not to the terms of the particular partnership agreement. A body that does not qualify as a foreign legal entity under these tests is normally transparent for Swedish tax purposes.\(^{215}\) If it is a foreign legal entity, either: (a) it is treated by Sweden as a company if it pays sufficient tax in the other state\(^{216}\) or, with certain exceptions,\(^{217}\) is a resident of a state with which Sweden has a tax treaty that applies to the body, or (b) if it does not satisfy either of the tests in (a), it is subject to the CFC rules if Swedish residents have sufficient interests in it for those rules to apply.\(^{218}\) In addition, if a foreign legal entity is not treated as a company because it fails the tests in (a) but the partners are taxed by the other country, they are liable to tax in Sweden with a credit for the other country’s tax. This avoids the timing problem of taxation in the other country when the profits are earned and, in Sweden, when they are distributed. The tests below are the three foreign legal entity tests and the result of applying them to a common law partnership.

(1) “The entity\(^{219}\) can acquire rights and incur obligations according to the law of the state in which it is domiciled” (höra hemma). At first sight, this is similar to questions (1) and (6) of the United Kingdom tests, but here the implication is quite different because, in Sweden, a formal partnership is a legal person that has its own rights and obligations. A common law partnership does not have rights and obligations in this sense, but the partners incur rights and obligations which are different from their personal rights and obligations.

(2) “The entity can be party to court proceedings and to proceedings before authorities.” If this test was applied to a Swedish partnership, a formal partnership could, and an informal partnership could not, be party to court proceedings. We considered this question above (see 2.4.) and concluded that common law partnerships can generally be party to legal proceedings, but the point is of little significance in common law countries as it is merely a question of whether the partnership name can be used or whether the names of the partners have to be listed.

(3) “The assets of the entity cannot be freely disposed of by the members.” This criterion probably means that the partners (in the case of a partnership) cannot dispose of the assets (not a partner’s interest in the assets) without the consent of the other partners according to law rather than the terms of the partnership agreement. If this test was applied to a Swedish partnership, the assets could not be disposed of by a partner in either a formal or informal partnership. A partner in a common law partnership can do so in relation to the disposal of assets in the ordinary course of business, but not other assets, so that the answer for a common law partnership is that it cannot. This factor has also been criticized by Nils Mattsson as being pointless since in no legal entity can the members dispose of the assets without the consent of the other members, but it seems to us that the criticism assumes what one is trying to determine. There are certainly bodies that are legal entities under their own law where one partner can dispose of, at least some of, the partnership assets without the consent of the other partners, for example a Scots or a Delaware RUPA partnership, so long as the disposal is in the ordinary course of business.

A common law partnership will fail at least one of these tests. Even if it passed all three, however, it would not matter since most such partnerships will not be taxed by the home country and, accordingly, the Swedish CFC rules will treat them as transparent entities; thus, for Swedish tax purposes, the partners in them will still be taxed on their share of the profits. In other words, the level of tax in the other country will determine the characterization.

In summary, applying these tests to a common law partnership does not give clear answers, particularly the test in (1) because of the different nature of a common law partnership. The ultimate categorization of a partnership, however, normally depends on whether the other country taxes, which is a solution we propose below (see 4.1.).

3.10. Conclusion on the tests used to categorize bodies

We have already seen in 2. that the descriptions of the features of partnerships have to be understood in light of the general legal background, particularly the law of agency or representation, and apparently different answers may not represent differences of substance. It is therefore difficult to apply the tests that are relevant to domestic partnerships to other countries’ bodies and obtain meaningful answers.

A good example of the difficulties of this approach can be seen by comparing an English case\(^{220}\) with a Dutch case\(^{221}\) in which the court had to categorize a French formal part-

of a foreign legal entity when it is considered as transparent (and the Swedish partners are therefore taxed) is outside the scope of this article. Sweden, however, applies the general Swedish rules for business taxation in determining a foreign legal entity’s income; for case law on the determination of income, see RA 1992 ref. 94 and Supreme Administrative Court decision of 19 January 2000. There is one major difference: If the foreign legal entity has incurred a loss, the partner may not deduct his portion of the partnership loss, which would be the case for a company partner. Instead, the foreign partnership may carry forward the loss; Income Tax Act, Chap. 14, Sec. 11. 215. In Supreme Administrative Court RA 1997 ref. 35 (Fb), a German GbR was not regarded as a foreign legal entity as it was not able to acquire rights or incur obligations. Although the main issue was whether the Swedish individual was to be considered as carrying on an enterprise, and therefore came under Art 7 of the 1992 Germany–Sweden tax treaty, it was necessary first to determine the status of the foreign participation.


217. This enables Sweden to take countries off the “white list” if legislation is introduced after the treaty is concluded. This is the case with e.g. Australia, Malaysia and Thailand — all three of which have introduced offshore banking companies after the conclusion of the treaty with Sweden. Malta was removed from the white list, but was reinserted on 1 January 1997 after a treaty change which excluded offshore companies from the application of the treaty.

218. If the owners do not have sufficient interests for the CFC rules to apply and if the other country taxes the body but not sufficiently enough to satisfy (a), it is still treated as a company.

219. We have translated the Swedish word “association” with “entry.” The Swedish word excludes e.g. “stiftelse” that approximate to trusts, which are entities but not associations. The Advance Rulings Board decided in RA 1999 not 20 that an Isle of Man trust was outside the scope of the definition of foreign legal person. Although the Supreme Administrative Court denied an advance ruling on procedural grounds, the Board’s decision is illustrative.

220. Dreyfus v. IRC, 14 TC 560.

nership (SNC) in order to determine how to tax a partner resident in the country concerned. In the English case, the court relied particularly on the following features of an SNC: that its existence as a legal person resulted from its registration; that, as a legal person, it owned its assets and incurred its liabilities; that only the gérants (managers), who were not agents of one another, could bind it; and that profits could not be distributed until there was a resolution to do so. None of these was a feature of an English partnership, and all were features of a UK corporation. It is hardly surprising that the court treated the SNC as opaque, reversing the Commissioners’ decision that it was a partnership, even though the result of treating it as non-transparent seems inappropriate particularly because similar formal partnerships in other countries are treated as transparent. The Revenue do not follow the case in practice.

In the Dutch case, the court came to the opposite conclusion, relying on the following factors: that the profits were taxed in the hands of the partners; that they were jointly and severally liable for the liabilities; that transfer of the partners’ interests was restricted; and that (unlike the particular SNC in the English case) no decision was required to distribute profits. In light of these factors, the court concluded that the SNC was transparent. As in the English case, the tax authorities did not like the decision, but it was not appealed on factual grounds and the Decree on the characterization of foreign entities followed. It is interesting that, of the factors considered in the two cases, only one, the need for a decision to distribute profits, was common to the two cases and, in respect of that factor, the particular partnerships in the two cases were different. Presumably the other, different, factors were ones that the respective courts regarded as important seen from the perspective on partnerships in the country concerned, which demonstrates the difficulty of this approach. In addition, there is the problem with an approach based on a list of questions of what to do when the answers to a number of questions do not all point in the same direction, as is likely to be the case for bodies from a different legal system.

It is frequently the case that, when taxing business profits and real estate income on a source basis, for reasons of neutrality countries want to tax foreign bodies that are similar in their legal form to domestic ones in the same way as domestic ones. Even where countries apply a method of categorizing foreign bodies which is different from comparing them with domestic bodies, this is often subject to taxing on a source basis foreign entities that are similar to domestic ones in the same way as domestic ones. This can be seen in Belgium, the Netherlands and Switzerland. If similarity is determined by asking a series of questions, it is clear that the approach does not work because describing the features of domestic partnerships in one’s own system of law does not help in determining whether a body formed in another system of law is actually different or just appears to be so.

A major difference relates to the nature of a legal person; countries that equate legal capacity with legal person should recognize that other countries do not do so. This is fundamental and affects the answers to questions about who owns the assets and carries on the business. The difference between the common law and civil law of agency is also the cause of many apparent differences. The Swedish definition of foreign legal entity is an advance on many countries’ approach of asking whether something is a legal entity under the other country’s law without realizing that the meaning of legal entity varies from country to country. Being a test that determines whether other countries’ bodies are companies, however, it is less successful when applied to partnerships that are different in nature from companies. Similar comments can be made on other questions, such as who owns the assets, who can be sued, who carries on the activity, and who is liable for the liabilities. As we saw in 2., apparent differences tend to disappear when they are examined. While it may be possible to design questions that determine whether a foreign body is similar to one’s own, these need to be written with respect to other systems of law where the questions have to be answered rather than with respect to one’s own system of law. It is doubtful whether the approach of any of the countries described in this part is successful in achieving this. It may also be doubted whether similarity in legal form is a sufficient reason for taxing a foreign body in the same way as a domestic body.

4. PROPOSALS FOR REDUCING CATEGORIZATION PROBLEMS

It is clear that there are serious difficulties in categorizing foreign bodies by comparing them to domestic ones. We shall examine three ways of reducing the problem of categorizing foreign bodies. The first is to apply a different rule for characterizing foreign entities when taxing resident partners of a foreign body based on the tax treatment in the partnership’s state if the partnership is taxed as a resident, or the source state if it is not. The second is to use tax treaties to determine the categorization of the other state’s bodies. The third is to accept the source state’s characterization, but to interpret the treaty or include specific treaty provisions that require the source state to follow the categorization of the partner’s residence state.

4.1. The partner’s residence state to follow the partnership state’s tax categorization

We have seen that it is likely that states will want to tax foreign bodies that are similar to domestic bodies in the same way when taxing them on a source basis. It is less clear, however, that the approach of comparing the non-tax characteristics of the foreign body to a domestic one is appropriate when taxing resident partners in foreign bodies. Here one is not concerned with taxing similar bodies in the same way. It is desirable when taxing the partner on

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222. Both partners were in fact also gérants.
223. The second feature is true of a Scots partnership. The partners are agents of each other as well as of the partnership.
224. *International Tax Handbook*, ITTI1673; Tax Bulletin, December 2000. A French SC, however, is treated as opaque: Tax Bulletin, December 2000. A Dutch court has held a French SCI (société civile immobilière) to be transparent even though, for French dividend tax purposes, it was considered to be a separate entity, although income tax was levied in the name of the partners; Hof Amsterdam, 11 November 1998, No. 9600250, Vakstudie-Nieuws 1999/15.6.
225. Because this approach is limited to treaty cases, it is dealt with in 4.3
a residence basis to avoid differences between states on the identity of the taxpayer, the time when the income is taxed, whether a treaty applies, and whether relief is given for the other state’s taxes. These complications are reduced if the residence state follows the partnership state’s tax treatment where the partnership is taxed as a resident, regardless of whether the foreign body is similar to a domestic one. Where three states are involved, this approach could require both the partner’s residence state and any state that taxed the partnership as an entity to follow the source state’s approach. Further provisions would be required to deal with giving relief where tax was paid by a person different from the person taxed by the residence state.

In the majority of cases, partnerships are transparent for tax purposes in their own state and, following this approach, the same treatment will also apply in the partner’s residence state. Partnerships are transparent in 32 out of 37 types of general (i.e. not limited) partnership in those OECD countries that provided such information for the OECD Partnership Report, 226 although it is less true for limited partnerships, the equivalent figures being that only 10 out of 32 limited partnerships in OECD countries are completely transparent and a further seven are transparent for the general partners but opaque for the limited partners. 227 It is unclear why the tax treatment in the other state is not generally accepted as a proper test for categorizing the other state’s bodies, at least when the taxation of resident partners is concerned. 228 It needs to be recognized that the other state’s tax categorization may depend on the taxpayer’s choice, as in the United States, France and, from 2002, Italy, but it is the logical conclusion of this approach to take account of the other state’s tax treatment regardless of whether this arises from the taxpayer’s choice. 229 There might, however, need to be restrictions on the rule applying where the taxpayer has a choice if a state does not charge significant corporate tax where the taxpayer chooses to pay tax as a corporation. In many cases, any advantage that might be obtained will be prevented by CFC rules, which exist in all the countries represented by the authors, except Belgium and Switzerland, although only to a limited extent in the Netherlands.

Only the Netherlands has a separate test for characterizing foreign entities which includes the tax treatment in the other state, but that will not normally be the decisive test. We have also referred to the Swedish internal law provision that, if the partnership’s state taxes the Swedish resident partners because it considers the partnership to be transparent, Sweden (which does not consider the partnership to be transparent) will also tax the partners in order to enable them to obtain a credit for the tax paid in the other state. 230 There would seem to be considerable advantages in the partner’s residence state following the entity state’s tax treatment rather than using the same method of characterizing the foreign entity as is used when a state is the source state.

4.2. Determining categorization in tax treaties

The second proposal, which does not seem to be used frequently, is that categorization is determined in the tax treaty, which would enable each state to categorize the other state’s bodies. This approach would be particularly advantageous for limited partnerships which are more often taxed as opaque bodies than as transparent entities. A problem with this approach is that the OECD Model does not make a distinction between companies and partnerships based on how the body is taxed; thus, as it stands, it would be difficult to fit categorization into the OECD Model. The Commentary assumes that companies are legal entities and that, in most countries, partnerships are not, which may be true generally, but is now subject to numerous exceptions. 231 “Company” is defined in the OECD Model (Art. 3(1)(b)): “the term ‘company’ means any body corporate or any entity that is treated as a body corporate for tax purposes.” This definition applies unless the context otherwise requires.

Thus, “company” means, first, any body corporate, which we equate with legal person and, second, any entity (necessarily not a body corporate) that is treated as a body corporate for income tax purposes. A body corporate is treated as a company whether or not it is taxed as such, and the expression may therefore include some transparent partnerships because they are bodies corporate. 232 The OECD Model makes a distinction between companies and partnerships in relation to the reduced 5% withholding tax on dividends. The 5% rate applies “if the beneficial owner is a company (other than a partnership) which holds directly at least 25 per cent of the capital of the company paying the dividends” (Art. 10(2)(a), emphasis added). The Commentary explains that, if the partnership is treated as a body corporate for tax purposes, i.e. falls within the

226 Taken from Annex III of the OECD Partnership Report (see note 1, supra).
227 The total number is affected by the fact that only 24 OECD countries are included—of the countries represented by the authors, not including Italy (whose inclusion would increase both figures by two) — and that some countries have more than one type of partnership. The cases in which ordinary partnerships are taxed as opaque are: Belgium; SNC, Japan; gomeki-konsha, Mexico; A or P and Spain: sociedad colectiva. These figures do not include silent partnerships which, if included, would add six to the number of transparent (in the sense of not being taxed as a corporation) partnerships and to the total.
228 In the countries represented by the authors, limited partnerships are opaque in Australia, Belgium, France (as to the limited partners), Germany (as to the limited partners), Japan, and the Netherlands (but only if the limited partners’ shares are freely transferable and then only as to the limited partners). We have included US limited partnerships as transparent because that was their original treatment, although they could be opaque under the check-the-box regulations. Including Italy, which is not included in the OECD Annex, would increase the number of transparent limited partnerships by one.
229 The reason in Belgium is that, in determining a Belgian resident’s tax liability, the Belgian courts should, based on territoriality rules, apply only Belgian tax laws and not the laws of other jurisdictions (Court of Appeals of Brussels, 4 June 1974, J.D.F., 1975, at 82). Under its rules of private international law, however, Belgium applies the other country’s commercial or corporate law to determine whether a foreign body is a legal person, which affects Belgian taxation; see 3.3.
230 There are seemingly inconsistent Technical Interpretations in Canada which treat a French SNC that elects to be taxed as a corporation as not being a treaty resident (Tech Intep 2000-0048855) and a US limited liability company that elects to be taxed as a corporation under the check-the-box rules as a resident for treaty purposes (Tech Intep 9728445).
231 See text (following note 216, supra).
232 Para. 1 of the Commentary on Art. 10 of the OECD Model.
233 See notes 226 and 227, supra. The term “company” also includes corporations that are taxed as transparent bodies, for example, the Subchapter S corporation in the US and the UK LLP.
second limb of the definition of company, this provision may be modified by deleting this reference to a partnership in order to give it the benefit of the reduced rate of withholding tax. A partnership will be included in the first limb of the definition of company if it is a body corporate. But if, although it is taxed, the amount of tax is the same as if it were a transparent entity and not a body corporate, as in France and Sweden, it should not receive the benefit of the 5% rate of withholding tax and so the words in parentheses are included in order to prevent this result. If, however, a partnership is included in the second limb of the definition of company by being taxed as a body corporate without being one, it is reasonable that the partnership should receive the benefit of the reduced rate of withholding tax, as proposed by the Commentary.

The other reference to partnerships in the OECD Model is in the definition of "national" in Art. 3(1)(g): "the term ‘national’ means: (i) any individual possessing the nationality of a Contracting State; (ii) any legal person, partnership, or association deriving its status as such from the laws in force in a Contracting State” (emphasis added). This definition applies unless the context otherwise requires.

The Commentary explains that the reference to partnerships in this definition is necessary to deal with those countries in which a partnership is a person but not a legal person. In many countries where a partnership is not a legal person, it is regarded as a person. It would be clearer if item (ii) in the English version of the OECD Model referred to "body corporate", the term used in the definition of "company" quoted above, rather than "legal person"; the French version uses the same expression, "personne morale", in both places. Since the definition of national is required primarily in connection with the non-discrimination article, where the national must be taxed for the article to be applicable, it is not clear why item (ii) of the definition does not just refer to "a person other than an individual", since individuals are dealt with in item (i), instead of "legal person, partnership or association". An entity treated as a body corporate for tax purposes, within the second limb of the definition of company and therefore within the definition of person, would then be expressly included without the need to consider whether it was a partnership or association.

For this approach to work, it would be necessary to amend the OECD Model to make a clear distinction between companies and partnerships. The definition of "company" would need to be changed to delete the reference to body corporate, which is not relevant to how it is taxed, so that it would read: "the term ‘company’ means any entity that is treated as a body corporate for tax purposes." This change would enable deletion of the two references to partnerships considered above. If this were done, treaties would then be suitable for dealing with problems of categorizing the other state’s bodies by listing them and stating whether or not they are companies within the treaty definition. This still leaves problems caused where three countries are concerned. Another problem with this approach is that new bodies can be created or the tax law changed for existing bodies so that a treaty categorization needs to be flexible. It does not seem particularly contro-

versial to give the competent authorities power to make changes to the categorization of listed bodies in the way proposed where they result from new bodies or changes in tax law, but if it were thought to be going too far, states could express their willingness to deal with such a question in a protocol.

4.3. Mitigating by treaty the effects of the source state’s internal law categorization

The third suggestion is to start from the position that states will want to compare foreign bodies with similar domestic ones when taxing the foreign body on business profits or income from real property on a source basis. The differences caused by this approach can be mitigated either by treaty interpretation or by specific treaty provisions. These enable the treaty to apply even though one of the states treats the body as transparent and the other as opaque. The solution in the OECD Partnership Report is that, regardless of the source state’s internal law categorization, the source state should interpret the treaty so that the treaty with the partners’ residence state applies if that state treats the partnership as transparent. In this way, the treaty is made to apply between the source state and whichever state taxes the income in the hands of a resident. The United States recently amended its withholding tax regulations to provide that the test of whether the income is “derived by” a resident of the treaty partner, entitling it to a reduced rate of withholding tax, depends on whether the entity is fiscally transparent under the tax law of the treaty partner. For this purpose, an entity is fiscally transparent only if the holders of interests in the entity are required to include the income as their income, regardless of distributions, and the character and source of the item are determined by the original item of income. Where, on this basis, the entity is fiscally transparent, regardless of whether it is transparent in another state, the holders of interests in the entity can claim the treaty rate of withholding tax applicable to their state of residence in its treaty with the United States as the source state of the income paid to the entity.

233. Para. 11 of the Commentary on Art. 10
234. Para. 10.1 of the Commentary on Art. 3, added in the 2000 update of the OECD Model and Commentary
235. Or subjected to requirements related thereto, although the article is not restricted to income taxes and extends to all taxes. It is possible that partnership and association are referred to specifically as any connected requirements would be imposed on the partnership or association rather than on its members
236. An example is found in an exchange of notes to the new United Kingdom–Jordan treaty (2001): “it is understood that in the event that either Contracting State introduces legislation whereby a partnership is to be regarded as a taxable entity it will notify the other State of this fact, and the two States will without delay enter into the negotiations of any amendment of the Convention necessitated by this change.”
237. Para. 8.4 of the Commentary on Art. 4
238. It can be both states; see Example 9 in the OECD Partnership Report, supra note 1
239. Treas. Reg. § 1.894-1(d)
240. Treas. Reg. § 1.894-10(c)(5), Example 2. This is in accordance with the OECD Partnership Report, supra note 1, Para. 73-75. For a treaty provision with similar effect, see the new (2001) United States–United Kingdom treaty, Art. 1(8)
In the Netherlands, a Decree issued by the Under-Secretary\(^241\) deals with a foreign body\(^242\) holding a “substantial interest shareholding” in a Dutch company in circumstances where the Netherlands as the source country regards the foreign entity as opaque, but the other country regards it as transparent. In principle, and subject to a number of reservations, the Ministry is prepared to apply the treaty as if the participants in the foreign entity owned a proportionate share in the Dutch company directly, as suggested in the OECD Partnership Report.\(^243\) For this to apply, the foreign body must have legal personality or have a form similar to a Dutch open CV, a limited partnership in which the limited partners’ interests are transferable without consent. This concession applies both to income tax (non-resident shareholders in certain circumstances are regarded as non-resident taxpayers in respect of dividends, interest and capital gains) and to dividend tax. The concession is extended to participants resident in third countries if that country has a treaty with the Netherlands.

Where this result cannot be reached by interpreting the treaty, the Commentary goes on to say that a specific treaty provision could be included having this effect. An example of such a treaty provision is found in the 2001 United States–United Kingdom treaty, Art. 1(8),\(^244\) which provides:

An item of income, profit or gain derived through a person that is fiscally transparent under the laws of either Contracting State shall be considered to be derived by a resident of a Contracting State to the extent that the item is treated for the purposes of the taxation laws of such Contracting State as the income, profit or gain of a resident.

Another example is found in the protocol to the new (2001) Belgium–Netherlands treaty:\(^245\)

4(b) Where a company\(^246\) is not subject to tax as such in a Contracting State and is subject to tax as such in the other Contracting State, the other Contracting State shall apply, at the request of the company, the provisions of Chapters III, IV and V of this Convention insofar as these provisions would have applied if the persons entitled to the company’s capital had directly received the income or owned the capital, each according to its share in the company. The application of the preceding sentence shall not alter the base on which the tax is imposed on the company according to internal law of the other Contracting State and shall reduce this base only insofar as such reduction results directly from the preceding sentence.

Both provisions apply where there is a conflict between the two states. We shall start with cases where the partner’s residence state treats the partnership as transparent because otherwise the partner will not have been taxed on the income as it arises but only on distributed income.\(^247\) The first situation covered is where the source state regards the partnership as opaque and no state regards the partnership as a resident (Case 1).\(^248\) Where the partnership is opaque, it can be resident in the source state, which must accordingly also regard it as opaque (Case 2). Alternatively, the opaque partnership can be resident in a third state, with the source state continuing to regard it as opaque (Case 3). It cannot be resident in the partner’s residence state since that state must treat it as transparent. The fourth possibility is that the source state regards the partner’s residence resident in the other state as transparent and the partner is resident in the source state (Case 4). These two treaty provisions are similar in requiring (or under the Belgium–Netherlands treaty provision, giving the option to require) the state that treats the partnership as opaque (the source state in Cases 1 and 3, which is also the partnership’s residence state in Case 2) to treat it as transparent. The United States–United Kingdom treaty provision does the opposite in Case 4 by requiring the source state, which would otherwise regard the payment as made to the partner in the same state, to treat the payment as made to the partnership which is resident in the other state.\(^249\) We shall

241. Decree No. IFZ/27/204, 17 March 1997. See the parliamentary discussion on the 1992 United States–Netherlands tax treaty, where questions were raised as to the application of the treaty to US limited partnerships and Subchapter S corporations, both of which are transparent for US tax purposes and opaque for Dutch tax purposes. The then Under-Secretary stated (Kamerstukken, 1993/94, 23220, No. 84a at 9 and No. 84c at 11) that it was the policy of his Ministry to reduce the tax on dividends paid by Dutch resident companies to such entities if the participants in the entity were entitled to treaty benefits, as if they had received the dividends directly. In 1996, when the threshold for “substantial interest shareholdings” was lowered from 35% to 5%, the issue was raised in the Committee of Ministers (Kamerstukken, 1996/97, 24339, No. 620 at 17) and the Dutch claim that this would have on shareholdings held through foreign hybrid entities. The answer was open-ended: no serious problem had been identified and, if double taxation arose, it would be considered on a case-by-case basis.

242. The term “lichaam” is not defined in general law, but in tax law, it is defined in Art. 2(1)(a) of the General Tax Act as “associations and other legal persons, civil law partnerships and companies, business enterprises of public law persons and doelvermogens.” (emphasis added). This last term is an undefined term used in several taxing acts; the literal translation is “assets grouped for a special purpose.” No definition has ever been given. The Hoge Raad has ruled that a discretionary irrevocable trust is a “doelvermogen.”

243. The Netherlands’ reservations on the OECD Partnership Report, supra note 1, and its observation on the OECD Commentaries resulting from the reservations relate to giving relief when taxing the Dutch partner (see Para. 80 of the Commentary on Art. 23), not to the case where the Netherlands is the source country (there is no observation on Para. 84 of the Commentary on Art. 4).

244. See below for the corresponding double taxation relief provision. This provision is contained in the 1996 United States Model. An earlier version, which was contained in the 1981 United States Model and in some US treaties, provided: “in the case of income derived or paid by a partnership, estate, or trust, this term [resident] applies only to the extent that the income derived by such partnership, estate, or trust is treated as income subject to tax in that State as the income of a resident, either in its hands or in the hands of its partners or beneficiaries.” A similar provision is found in the Swedish Model and some Swedish treaties.

245. A further point dealt with by this treaty relates to limited partnerships. Art. 10(7) provides (in a literal translation of the Dutch text) that “income derived by a silent [limited] [in French: associé communaire, not referring to ‘silent’] partner from participations in the profit [in French: actions ou parts beneficialités] of an enterprise of one of the Contracting States may be taxed in that State in accordance with the laws of that State.” The effect of this provision is obscure.

246. The “term ‘company’ means any body corporate or any entity which is treated as a body corporate for tax purposes in the Contracting State of which it is a resident.”

247. This point is clear in the US–UK treaty. It is not clear in the Belgium– Netherlands treaty, giving rise to Cases 5, 6 and 7, below, if the provision applies where the partner’s residence state treats the partnership as opaque.

248. The opposite case, where the source state regards the partnership as transparent and the other state taxes it as a resident, must under the US–UK treaty be a case where the partner’s residence state and the source state are the same (Case 4); otherwise, the income is not “derived through” the entity by a resident of one of the states. The Belgium–Netherlands treaty may deal with the opposite case in Cases 5 and 6.

249. The US–UK treaty provision applies more widely than in differences in entity characterization. From the UK point of view, a body is treated as fiscally transparent if the capital gains of a non-UK resident close company are taxed on the participator (which appears to mean only not that the treaty can prevent the US from taxing a gain that is to be taxed only in the source state of the alienator made by a third-state entity, but also that, if the gain is made by a US non-transparent entity, the gain is treated as made by a UK alienator and so both
compare the results of applying each of these treaty provisions in these four cases.

(1) Source state, opaque; partner's residence state, transparent; partnership not taxed as a resident by any state. The source state must change its view when applying the treaty and regard the payment as made to the partners. This is the situation dealt with in Example 4 of the OECD Partnership Report. No relief problems then arise. The Dutch official commentary to the Netherlands–Belgium treaty gives, as an example of this provision applying, a Dutch individual and a Dutch company that are partners in a Dutch VOF (formal partnership) which holds shares in a Belgian BVBA (a company). Although Belgium regards the dividends paid by the BVBA as paid to the VOF, which Belgium regards as opaque, but not a resident of the Netherlands because the VOF is not taxable there, the Netherlands regards the dividends as paid to the partners in the VOF, which is transparent. The provision of the protocol quoted above means that the VOF can require Belgium to apply the rates of withholding tax on the dividends as if they had been paid to the partners. The problem with such an interpretation is that “company” is a defined expression that cannot apply to the VOF, which is neither a body corporate nor taxable as a body corporate in the Netherlands. A company that is not a body corporate can therefore exist only if it is taxed as a resident in the state that regards it as opaque. The only way for the protocol to apply in this case is to say that the context requires that the definition of company not be applied. We shall assume in the further examples that the definition of “company” should not be applied here.

(2) Source state and partnership's residence state (the same state), opaque; partner's residence state, transparent. Again, the source state (and partnership's residence state) must apply the treaty as if the payment is made to the partners, even though it considers that the payment is internal to its state. This could apply to a Dutch resident individual who is a partner in a Belgian VOF deriving Belgian-source income, which the Netherlands regards as transparent and Belgium taxes as a company. The Netherlands will exempt the income under the treaty. In other cases, and in the United States–United Kingdom treaty provision, since the partnership state still taxes the income, the partner’s residence state must give relief for that tax in accordance with the further provisions discussed below. Those provisions also prevent Belgium from imposing withholding tax on the dividends paid. The OECD Partnership Report does not provide a solution to this case.

(3) Source state, opaque; partnership's residence state (a third state), opaque; partner's residence state, transparent. The treaty applies and the source state must change its view and apply the treaty as if the partnership were transparent from the source state's point of view. The third state may tax the partnership, in which case the relief provisions mentioned below may be required. This is the situation dealt with in Example 9 of the OECD Partnership Report.

(4) Source state and partner’s residence state (the same state), transparent; partnership’s residence state (the other state), opaque. The United States–United Kingdom treaty provision means that the source state must still apply the treaty even though, from its point of view, the payment appears to be internal to that state. The partner’s residence state (which is also the source state) will still tax the income as that of the partner, but must give relief for the tax paid by the partnership in the other state by the further treaty provisions discussed below. Under the Belgium–Netherlands treaty provision, the other state cannot tax the partnership if it makes the election. The other state may, however, tax the partners resident in the source state under the reasonable assumption that they are deemed to have a permanent establishment in the other state to which the income concerned is attributable.

Under the Saint-Gobain rule of Art. 26(3) of the treaty (similar to Art. 24(3) of the OECD Model), the other state would have to give the partner concerned relief from double taxation as if it were a resident. The OECD Partnership Report does not provide a solution to this case.

Turning to the cases where the partner’s residence state regards the partnership as opaque, the Belgium–Netherlands treaty provision (but not the United States–United Kingdom treaty provision) may apply. The problem with such an interpretation is that, according to internal law, the partner’s residence state will tax only distributions from the partnership. If the partnership elects to be transparent, the partner’s residence state needs to tax the partnership’s income, which it may not be able to do under internal law if the treaty cannot create a tax charge unless states can tax). An interest in possession trust is also treated as fiscally transparent, which is the case anyway under English law and is deemed to be the case under Scots law, where that is not the case under the law of the trust, for example, New York law (see Garland v. Archer-Shee, 15 TC 695), and New Jersey law (see Kelly v. Rogers, 19 TC 692), although the correctness of these decisions is doubted in the US. The provision also applies where, under the rules relating to settled-interest trusts or to taxing the transfer of assets transferred to an entity abroad in which he has power to enjoy the income (TA 1988, Sec. 739), a different person is taxed.

250. See note 1, supra.
251. Kamersstukken, II 2001-2002, 28259, No. 3, under “Gezamenlijke artikels-gewijze toelichting” and further under “Algemene begrippenbepalingen”. It is understood that this document will be approved by the Belgian parliament, in which case it will have the status of “context” in Art. 5(2) of the Vienna Convention on the Law of Treaties, or possibly, depending on the constitutional position, the status of a treaty.
252. The Dutch official commentary, supra note 251, concludes in this example that Belgium should withhold 10% tax on the dividends: each of the two partners in the entity holds a 50% interest, which means that 15% is withheld on 50% and 5% on the other 50%. Although the mathematics are fruitless, it does seem a strange interpretation of “transparency”.
253. See note 246, supra.
254. US–UK treaty, Exchange of Notes, second paragraph under Art. 1(8).
255. If the entity were a CV, Art. 10(7) would apply; see note 245, supra. The interaction with this provision is obscure.
256. In this case, no problem with the definition of “company” in the Belgium–Netherlands treaty arises, although the effect of the election to ignore the partnership’s is that the partnership is no longer a “company”.
257. It is not clear whether the election affects the partnership in its entirety or only to the extent of the partners that are resident in the state that regards the entity as opaque. A “partial” election would avoid the additional problems of applying the treaty where the partners are resident in different states, but, of course, could lead to great practical difficulties.
258. See the next paragraph for the question whether such taxation in the other state is constitutionally possible. See Cases 5 to 8 for the constitutional problems involved.
259. Compagnie de Saint-Gobain, Zweigniederlassung Deutschland v. Finanzamt Aachen-Innenstadt, Case C-307/97 (European Court of Justice).
260. Because the income is not “derived through” the entity by a resident of one of the states.
internal law is changed to impose the charge. This potentially gives rise to four further cases, as follows.

(5) Source state; transparent; partnership’s residence state and partner’s residence state (the same state), opaque. This case demonstrates the constitutional problem at its most acute since the partnership’s residence state (and partner’s residence state) has to give up taxing the partnership on the income with a source in the other state without necessarily being able to tax the partner. In taxing the partner, the partner’s residence state should allow a credit or exemption in respect of the income from the source state.  

(6) Source state, transparent; partnership’s residence state (a third state) opaque; partner’s residence state, opaque. In addition to the constitutional point affecting these four cases, there is the additional possibility that the treaty between the partner’s residence state and the third state might prevent the former from taxing the income. This is the same argument that CFC legislation may be overridden by treaties. There is the added problem that the relief provision discussed below does not apply to give relief for the third-state tax because the relief is restricted to third-state tax withheld at source.

(7) Source state, transparent; partnership not taxed as a resident by any state; partner’s residence state, opaque. In addition to the constitutional point affecting these three cases, the same problem of obtaining relief as in Case 6 can arise if the third state in which the partnership operates tax it as having a permanent establishment there; relief for the third-state tax is restricted to tax withheld at source.

(8) Source state and partner’s residence state (the same state), opaque; partnership not taxed as a resident of the other state. This is the same as Case 4, with the positions of the states reversed.

Naturally, such provisions give rise to difficulties in giving double taxation relief in the partner’s residence state, which in turn requires further treaty provisions. The new United States—United Kingdom treaty, in an exchange of notes, deals with giving relief where each state taxes a different person:

It is understood that, under paragraph 4 [the saving provision permitting a state to tax its residents or citizens as if the treaty had not come into effect] or 8 [quoted above 263] of Article 1 (General Scope), the provisions of the Convention may permit the Contracting State of which a person is a resident (or, in the case of the United States, a citizen), to tax an item of income, profit or gain derived through another person (the entity) which is fiscally transparent under the laws of either Contracting State, and may permit the other Contracting State to tax (a) the same person; (b) the entity; or (c) a third person with respect to that item. Under such circumstances, the tax paid or accrued by the entity shall be treated as if it were paid or accrued by the first-mentioned person for the purposes of determining the relief from double taxation to be allowed by the State of which the first-mentioned person is a resident (or, in the case of the United States, a citizen) ...  

The protocol to the new Belgium—Netherlands treaty, in addition to the relief provisions in the part quoted above, contains a provision having similar effect:

2. Where a company 265 is subject to taxation as such in a Contracting State but the income or capital of the company is, in the other Contracting State, taxed as income or capital of the participants in the company, the provisions of this Convention shall not result in double taxation or total or partial exemption of such income or capital. In order to avoid such effect, the tax, income and capital of the company shall be deemed to be the tax, income and capital of the participants in the company in proportion to their entitlement to the company’s income or capital. To the extent necessary, the participants in the company shall be entitled, each for their part, to credit the tax levied on the company in respect of this income or capital (including any tax withheld at source in a third State 266) against the tax for which they are liable in respect of the same income or capital, and the State of residence of the company waives any taxation of the participants in the company who are residents of the other Contracting State in respect of the profits distributed by the company to such participants.

Art. 2 provides the manner in which relief for double taxation is to be given in the case of hybrid entities. It is not clear how this article, which is mandatory, interacts with Art. 4(b) of the protocol, which is at the election of the hybrid entity. If the election is not made under Art. 4(b), the “opaque state” would continue to tax the entity, but under Art. 2, the tax, income and capital of the company shall be deemed to be the tax, income and capital of the participants. This would mean that the election under Art. 4(b) is meaningless. Art. 2 reaches further in that it also attributes the tax paid by the entity to the participants. This is inherently contradictory: if the income is deemed to be the income of the participants, the entity should not be taxed on it and therefore there can be no tax to be attributed to the participants.

Art. 2 prescribes a credit “to the extent necessary” and does not mention “exemption”. This is strange if the income of the entity is income which would normally qualify for exemption relief (real estate income, business profits). Perhaps the meaning of Art. 2 is that, if no election is made under Art. 4(b), the participants give up their claim for an exemption, and receive only a credit. If the election under Art. 4(b) is made, both states regard the income as that of the partner, in which case no problem of relief will arise.

These two provisions enable the partners who are taxed on the partnership’s income in their residence state to take a credit for the tax paid by the partnership in the other state, thus preventing either double taxation or, in an exemption state, double relief. The provisions deal with the partner’s residence state taxing the partnership as an entity and the partners’ residence state treating it as transparent and taxing the partners by enabling the partners to claim relief in their residence state for the tax imposed by the

261. For partners resident in a third state, this should be done applying Art. 24(3) of the OECD Model or the Saint-Gobain rule.
262. See text at note 266, infra.
263. See text at note 244, supra.
264. There is an exception for income or gains from real property, where the country in which it is situated taxes first and the other country gives a credit.
265. See note 246, supra, for the applicable definition.
266. This is an unusual example, particularly for the Netherlands which normally gives credit only by treaty, of a treaty provision requiring credit for third-state tax.
source state or the partnership’s residence state on the partnership. The Belgium–Netherlands provision deals with double relief occurring, for example, where the partnership’s residence state does not in fact tax the income and the partner’s residence state exempts the income from tax on the basis that the partnership’s residence state has the right to tax the income. That provision also prevents distributions from the partnership from being taxed, on distribution, by the state that regards the partnership as a non-transparent resident, while the United States–United Kingdom treaty provision requires relief for tax on distribution. The United States–United Kingdom treaty provision is wider in dealing with bodies taxed as a resident in a third state (Case 3), with which the Belgium–Netherlands treaty provision does not deal as it deals only with third-state source tax, not third-state residence tax (Case 6).

4.4. Conclusion on the proposals for reducing categorization problems

It is premature to draw conclusions on the relative merits of the three suggestions put forward. The treaty solutions in 4.3. are just beginning to be used, and the Belgium–Netherlands treaty provision suffers from conceptual and definitional problems. It can, however, be said that the relief provisions in the United States–United Kingdom and Belgium–Netherlands treaties are an important step forward in dealing with the main problem of differences in categorizing entities. The suggested amendment to the OECD Model in 4.2. would remove the assumption that all companies are opaque and all partnerships are transparent, which would assist future treaty developments dealing with this problem.

Essentially, the solutions in 4.1. and 4.3. are similar in requiring one state to defer to the other state’s categorization: 4.1. requiring the partner’s residence state to follow the other state’s categorization, and 4.3. requiring the state that regards the partnership as opaque to follow the other state’s categorization as transparent. The approach in 4.3. seems more flexible as it starts with the taxation of the partner and enables relief provisions to deal with any remaining problems of double taxation or, as demonstrated by the Belgium–Netherlands treaty provision, double exemption. It would also be possible to develop these relief provisions so that each state could continue to tax in accordance with its law. We believe that the way forward is to develop treaty solutions to these problems.

267. This may not be true for limited partnerships in view of the provision in note 245, supra.
268. Except in Case 4 under the US–UK treaty