Tax&Legal Highlights

Poland

Mandatory reporting of tax-planning schemes

The amendment to Polish tax provisions adopted by Polish Parliament on 26 October 2018 introduces into the Polish Tax Ordinance Act mandatory reporting of so-called tax-planning schemes (Mandatory Disclosure Rules – MDR). The amendment imposes new obligations not only on advisors (attorneys-at-law, legal counsels, tax advisors), but also on their clients.

The amended provisions are to enter into force on 1 January 2019, but tax-planning schemes will have to be disclosed retroactively if the first activity related to implementation of the given scheme was performed after 25 June 2018 (cross-border schemes) or after 1 November 2018 (domestic schemes)

What is subject to mandatory disclosure?

Mandatory disclosure concerns tax-planning schemes which have or may have an impact on tax liability and which at the same time meet criteria indicated in the amended provisions - different for cross-border schemes (of which mandatory disclose results from the EU DAC6 Directive) and for domestic schemes (not covered by the Directive).

Subject to reporting will be a wide scope of information concerning the scheme, i.a. its detailed description, applied tax law provisions as well as the expected value of tax benefit. Disclosed schemes will be assigned a so-called NSP - number of the tax-planning scheme.

In which cases will domestic schemes be subject to mandatory disclosure?

Domestic schemes will be subject to mandatory disclosure if the beneficiary of the scheme will be a qualified entity (revenues, costs or assets of the beneficiary or of its related party exceed EUR 10m, or the scheme concerns items or rights of market value exceeding EUR 2.5m), and at the same time:

1) the main or one of the main benefits that the beneficiary expects to derive from the scheme is a tax advantage (understood very broadly - generally as any reduction in tax liability or postponement in its creation), and additionally the scheme fulfills criteria of at least one of the so-called "generic hallmarks" (broad and imprecise set of features, including i.a. situations when documentation and/or structure of the activities does not need to be substantially customized for implementation depending on the beneficiary, there is an undertaking to comply with a condition of confidentiality as concerns the way in which the scheme can secure a tax advantage, schemes where the intermediary is entitled to receive a success fee, etc.), or

2) regardless of what is the main benefit of the scheme (tax or non-tax-related) - if it meets at least one of numerous other criteria - for example:

(i) has an impact on deferred part of income tax or on deferred tax assets or provisions which is materially relevant to the entity from accounting perspective and this impact exceeds PLN 5m per year,

(ii) concerns non-withholding of tax in the amount exceeding PLN 5m per year, which withholding tax would have been levied if double taxation treaty or tax exemption would not be applied.

When will cross-border schemes be subject to mandatory disclosure?

Cross-border schemes will be subject to mandatory disclosure, regardless of whether the beneficiary is a qualified entity, in a situation when:

1) the main or one of the main benefits that the beneficiary expects to derive from the scheme is a tax advantage (understood analogously as in case of domestic schemes) and additionally the scheme fulfills criteria of at least one of the so called "generic hallmarks" (the set of these conditions is to some extent narrower than with respect to domestic schemes), or

2) regardless of what is the main benefit of the scheme - if it meets at least one of numerous different criteria listed in the amendment, for example:

a) the scheme involves tax-deductible cross-border payments to related entities located in tax havens,

b) the same income or property benefits from method of elimination of double taxation in more than one state,

c) there is a non-transparent structure of legal ownership or it is difficult to determine the beneficial owner,

d) the scheme involves a transfer of "hard-to-value intangibles".

Who will be obliged to report?

Mandatory disclosure obligation will as a rule burden the intermediary (understood as each person which develops, offers, makes available, implements or manages the implementation of the arrangement – in particular a tax advisor, legal counsel or attorney-at-law), and in specific situations the beneficiary (the person to whom the scheme is made available, who is prepared for its implementation or performed an activity related to implementation of the scheme). In addition to the above, in a situation when the scheme will not be reported neither by the intermediary nor by the beneficiary, the mandatory disclosure may additionally burden a so-called supporting entity (a broad definition including i.a. each person who has undertaken to provide assistance, support or advice regarding development or implementation of the scheme - for example a notary public).

Mandatory disclosure rules are different for the so-called standardized schemes (repetitive, possible to be implemented or made available to more than one beneficiary without the need to change essential assumptions of the scheme) and for non-standardized schemes.

What obligations will be imposed on beneficiaries?

The beneficiary will be obliged to report the scheme when:

1) the given scheme is subject to disclosure, and the beneficiary has not been informed by the intermediary that the scheme has already been reported (as described in justification to the discussed amendment – e.g. in cases when the beneficiary has developed and implements the arrangement on his own and does not cooperate with any intermediary);

2) with respect to non-standardized schemes, if the beneficiary will be informed that the intermediary will not disclose this scheme (as it would violate the professional secrecy obligation binding the intermediary, from which the beneficiary did not release it) - in such case, the intermediary shall provide the beneficiary with specific data that is subject to mandatory disclosure.

In the above situations, the beneficiary will report within 30 days from the day following the day in which the scheme will be made available, from the day following the day of preparation for implementation of the scheme or from the day of performing the first activity related to implementation of the scheme - depending on which of these events occurs first. Making available of the scheme is understood very broadly and includes i.a. providing the beneficiary with information about the arrangement in any form, including by e-mail, phone or in person.

Regardless of the obligation to report (which will usually burden the intermediary), in each situation when the beneficiary will apply a scheme, it will be obliged to provide the Chief of National Fiscal Administration with so-called information on application of the tax-planning scheme, within the deadline for filing the tax return concerning the settlement period in which the beneficiary performed any activities that are part of the scheme or obtained a tax benefit resulting therefrom. The disclosed information will include i.a. the NSP of the scheme and the amount of the tax benefit resulting from the scheme, obtained in the given settlement period. Therefore, each application of a tax-planning scheme will be compulsorily disclosed by the beneficiary to the fiscal administration.

The abovementioned information will be submitted under penalty sanction for perjury for making a false statement and will be signed by a taxpayer being a natural person, and in the case of taxpayers being legal persons - by all members of the taxpayer's managing body.

What are the sanctions for non-reporting?

The amendment foresees fines for failing to fulfill obligations related to reporting of the tax-planning schemes. The court may also order, in such cases, a penal measure of prohibition to perform specific business activity.

In the case of intermediaries, entities that employ intermediaries or that actually remunerate intermediaries, the revenues or costs of which exceeded in the previous financial year PLN 8m, the provisions impose an obligation to implement a so-called internal procedure determining the rules of conduct in the field of reporting. The amendment also introduces fines up to PLN 2m (in specific situations – up to PLN 10m) in case of non-implementation of internal procedure by obliged entities.

It should be noted that taking into account the broad definition included in the amendment, entities obliged to implement internal procedure will include not only tax advisors, legal counsels or attorneys-at-law, but in specific cases also other entities (i.a. banks or financial institutions, but also companies having internal tax departments).

When will the reporting obligation come into force?

The relevant provisions are to enter into force on 1 January 2019, whereas the reporting obligation will be partly retroactive – obligation to report will also cover schemes with regards to which the first activity related to their implementation was performed:

1) in the case of domestic schemes – after 1 November 2018,

2) in the case of cross-border schemes – after 25 June 2018.

Information about retroactively disclosed schemes will have to be reported by the end of June 2019 (if the disclosing entity will be the intermediary) or by the end of September 2019 (if the disclosing entity will be the beneficiary).

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New changes in income taxes and the Tax Ordinance on the way

The draft of significant changes in tax regulations planned from January 1, 2019.

In the autumn of 2017, we signaled that as a result of legislative initiative of the Ministry of Finance, tax regulations will undergo fundamental transformations from January 1, 2018 when the largest amendment to the Corporate Income Tax was to come into force. Recent weeks show that January 1, 2018 was not the end of fundamental changes of tax regulations. Subsequent bills, designed to significantly change tax regulations from January 1, 2019 were published by the Ministry of Finance at the end of the summer holidays. These projects concerned not only the income tax from legal persons, but also transfer pricing and the Tax Ordinance. After further modifications, on September 25, 2018 these projects were addressed to legislative work in the Parliament (hereinafter: "Amendment”).

1. Changing the principles of collecting withholding tax (so-called Withholding Tax)

2. Taxation of unrealized capital gains - so-called Exit Tax

3. Obligation to inform about „tax schemes”

4. Significant changes to the tax anti-avoidance clause

5. Preferential taxation rules of the so-called IP Box

6. Changes in transfer pricing

7. Other changes

Below, we present some of the planned changes in tax regulations that the Amendment is to introduce – and which changes, in your opinion, may potentially turn out to be crucial for the activities of most entities:

1. Changing the principles of collection of withholding tax (so-called Withholding Tax)

The draft amendment introduces into the Polish tax law significant changes to the previously applied principles of collection of withholding tax – i.e. the principle of direct application of preferences / exemptions in the field of withholding tax while meeting the documentary requirements provided for in the Corporate Income Tax Act (so-called *withholding tax relief at source*).

In the light of the Amendment, from January 1, 2019, the basic mechanism for charging withholding tax **for payments exceeding PLN 2 million (in relation to the one recipient in a given tax year) will be the principle of obligatory collection of withholding tax at basic rates** provided for in the Act on corporate income tax (i.e. 20% / 10% in relation to payments indicated in Article 21 of this Act and 19% in relation to payments indicated in Article 22 of this Act), with the possibility of a subsequent request for reimbursement of the above-mentioned tax by the tax office - so-called "withholding tax refund on demand". It should be noted that **the waiting time for the withholding tax refund will be 6 months**, but it will be possible to extend it - which may result in a significant cash-flow deterioration.

The Amendment assumes the possibility to apply the existing principles of settling
the withholding tax (i.e. the possibility for the payer to apply withholding tax preferences / exemptions) in the situation of:

• **submission by the payer to the tax authority of appropriate declarations** regarding the fulfillment of formal requirements and diligence **in verifying** fundamental conditions for applying tax preference in the withholding tax, or

• **obtaining the so-called opinion on the application of the withholding tax exemption**, which allows - in relation to a certain category of payments (subject to Article 21 of Act No 3 and Article 22 of Act No 4 of the CIT Act) - to settle on the current basis, i.e. the taxpayer's use of withholding tax preferences at the time of payment.

In addition to the above changes in the principles of collection of withholding tax
the Amendment also introduces:

• **clarifying the definition of the actual owner** – by introducing a *"warrant to take into account the broader context accompanying payments to foreign entities in assessing their status as recipients of receivables"* to confirm whether these foreign entities: (i) carry out a real economic activity in the country of residence, (ii) incur economic risks related the loss or loss of value of a given receivable; and (iii) they are able to decide independently on the intended use of a receivable.

• additionally, in the case of the Act on Corporate Income Tax, the Amendment provides for **a change of the special clause against the abuse of tax exemptions resulting from the regulations implementing EU directives (Article 22c of the CIT Act).**

2. Taxation of unrealized capital gains - so-called Exit Tax

The draft amendment introduces into the Polish tax law a mechanism known colloquially as **"exit tax".**

Exit tax pertains to situations that **cause Poland to lose its right to tax the values specified in the CIT Act**, generated before the transfer of assets / change of residence. The loss of Poland's right to tax may result, in particular, from the stipulations of agreements to avoid double taxation.

Events that give rise to tax obligations in reference to the planned regulations are:

• **transfer of an asset outside Polish territory**, as a result of which Poland loses

(*in whole or in part*) the right to tax income from the sale of that asset, **or**

• **change of tax residence** by a taxpayer subject to unlimited tax liability, which means that Poland loses the right (*in whole or in part*) to tax the income from the possible disposal of the taxpayer's property.

It should be noted that taxation will be independent of whether the asset is actually disposed of or not by the taxpayer. This means that **the tax may occur even if the taxpayer does not achieve any real benefits** from the asset.

Income subject to CIT / PIT taxation in Poland in accordance with the new regulations will constitute an excess of the market value of the transferred asset over its "tax value". The deadline for submitting the declaration and payment of tax is the 7th day of the month following the month in which the event causing taxation occurred.

The proposed tax rates for PIT taxpayers are to be **3%** or **19%**. In the case of PIT taxpayers, the provisions on tax on unrealized profits, as a rule, do not apply when the market value of the asset or the sum of their market values **does not exceed PLN 4 million**. In the case of CIT taxpayers, a single rate of 19% will apply, regardless of the value of transferred assets.

3. Obligation to inform about "tax schemes"

The amendment also introduces extensive regulation and assumes the need to **report to the Head of the National Treasury Administration (KAS) the so-called "Tax schemes"**. The assumption is that the regulations constitute an implementation of the Council Directive (EU) 2018/822 as of 25 May 2018 - nevertheless, in practice, the obligations imposed by the Amendment will be **much more far reaching than those resulting from EU regulations**. The Directive applies only to cross-border schemes, while the amendment also introduces the obligation to report national schemes.

The **"tax scheme" definition contained in the Amendment is extremely wide** - the scheme will be the so-called "Arrangement" (i.e*. "an activity or a set of related activities, including a planned activity or a set of planned activities of which at least one party is a taxpayer or who have or may have an influence on the occurrence or lack of occurrence of tax obligation"*) having "recognition features" specified in the provisions of law. This may mean the necessity to provide the Head of KAS with information on a lot of transactions made by taxpayers.

The obligation of reporting may be imposed on a "**promoter**", i.e. on an entity that "*formulates, offers, makes available, implements or manages the implementation of the arrangement*". Aside from promoters, reporting obligations may lay on "beneficiary", that is, entities to whom the arrangement is made available or implemented, or which are prepared to implement the arrangement or have made any act to implement such an arrangement. The amendment also imposes **a number of duties on "supporting"**, i.e. persons involved in the implementation of the arrangements, for example, **financial directors, accountants, employees**

of financial departments, notaries or employees of banks servicing a given entity.

Failure to comply with reporting obligations will entail substantial fines (liability under the provisions of the Fiscal Penal Code).

4. Significant changes to the anti-avoidance clause

The planned changes presented in the Amendment also encompass the modification of the wording of the provisions of the anti-avoidance clause ("GAAR") resulting in **a change in the logic pertaining to the application of the provisions of the clause**.

In the current legal state, GAAR refers generally to activities that are not sufficiently motivated by economic / business considerations. At the same time, there is generally no restriction on the co-existence of tax advantages in such situations.

The proposed amendment means that the clause may be applied already in a situation where, **despite the existence of significant business reasons, the activity will also result in a significant tax advantage**. Then the given activity will be considered as being done mainly to achieve a tax advantage, irrespective of its economic justification. Such a modification may significantly change the way of applying discussed regulations, minimizing the significance of economic goals, which may be even very important in planning the given activity, but they will not protect the taxpayer against application of GAAR. In practice, this means that it is necessary to analyze each significant amount of transactions from the perspective of a clause against tax avoidance - if the taxpayer has the opportunity to choose several ways to achieve the expected economic effects, and the chosen method will be more favorable than others in terms of tax, then this situation may potentially lead to the application of the clause against tax avoidance by tax authorities.

In addition, the legislator in the content of the Amendment has decided to introduce into the text of the Ordinance **an additional tax liability** (in the amount of 10 to 40%), which will be imposed by a decision by the tax authorities, in the event of a decision, inter alia, on the provisions of the anti-avoidance clause.

5. Preferential taxation rules of the so-called IP Box

The amendment also introduces **preferential taxation** at the rate of 5% CIT (analogically PIT) of income generated by intellectual property rights (so-called IP BOX, Innovation Box).

The bill provides for in the Act of Corporate Income Tax the introduction of a **favorable tax solution for entrepreneurs who earn income from the commercialization of intellectual property rights created or developed by them,**

the so-called. Innovation Box. The project also provides for the possibility of commissioning the performance of research and development works to other entities, both unrelated and related.

The prerequisite for using the proposed preference is **the requirement for the taxpayer to conduct research and development activities directly related to the creation, commercialization, development or improvement of qualified intellectual property rights**. A taxpayer who wants to take advantage of the proposed preferences will be obliged to keep **detailed accounting records** in a way allowing calculation of the tax base, including the relation of the incurred costs of research and development with the reached income from IP rights resulting from the work carried out.

With proper structuring of the business conducted, where intellectual property is a significant carrier of value, the use of IP Box preferences may therefore bring **measurable tax advantages by reducing the effective income tax rate**.

6. Changes in transfer pricing

We would like to point out that a separate document will introduce changes in transfer prices, rebuilding current regulations.

The most important include the following areas:

- New definition of related entities, including the introduction of the term of 'exerting significant impact' (also applies to persons who do not formally perform any functions in companies - the need to analyze the reporting line on the formation of links)
- Change in transaction thresholds determining the obligation to prepare documentation and comparative analyzes
- Direct introduction of the obligation to apply the market price principle and extending the catalogue of available methods of transfer pricing calculation - the need to adjust the applied cooperation principles to available tax methods
- Introduction of detailed rules of restructuring assessment - the need to comprehensively analyze the issue of 'exit fee' / the possibility of structured risk management estimation / challenge of 'exit fee'
- Extension of the scope of the required economic analysis to indicate and justify a particular level of the market price - the need to create a model of transfer pricing calculation, which does not create the risk of the lack of possibility of defense
- Omission or re-characterization of transactions - the need to closely link an intra-group transaction to business needs / economic realities
- New, extended reporting duties
- Available simplifications - the opportunity to focus on the most important business and value issues.

7. Other changes

Planned changes presented in the Amendment also include:

- Introducing an incentive to leave capital for development in companies by increasing the tax attractiveness of own financing by introducing the possibility of increasing the costs of obtaining revenues by the equivalent of debt financing costs - despite the fact that these costs were not actually incurred by the taxpayer (so-called **notional interest deduction**).

- Introduction of changes with respect to the rules of taxation **of expenses related to the use (operation) in the company of passenger cars** - also leased.
- Introducing the possibility of using **copies of tax residence certificates** by taxpayers, in the case of payments not exceeding PLN 10,000 per calendar year (for a single entity).
- Introduction of **an alternative method of taxing eurobonds**. The Amendment provides for the tax exemption of interest and discount obtained by non-residents (both PIT and CIT taxpayers) from bonds issued and admitted to trading on a regulated market or introduced into an alternative trading system within the meaning of the Act of 29 July 2005 on Trading of Financial Instruments with maturity not shorter than one year.
- Introduction of regulations on **the taxation of virtual currencies** (the so-called cryptocurrencies). What is important, the above regulations assume, inter alia, that revenues from trading in virtual currencies will be qualified in accordance with revenues from cash capital (Article 17 of the PIT Act) or capital gains (Article 7b of the Act on Corporate Income Tax) - but for these revenues specific tax rules will be determined and these revenues will not be combined with other revenue from cash capital / capital gains (a separate "basket").
- Introduction of **changes in tax loss settlement rules** by adding the possibility of a single reduction of income obtained from a given source in one of the following five tax years, for the amount of tax loss from this source, not exceeding PLN 5 million.
- Introduction of **a reduced (9%) CIT rate** for small taxpayers whose tax revenues do not exceed EUR 1.200,000 and for start-up taxpayers..

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