

RSM – the global destination for your audit, tax and consulting needs.



ADJUSTING COSTS WHEN AWARDED A GRANT

Tax Alert

Dear Sirs,

The recent justification for the Resolution of 7 judges of the Supreme Administrative Court (hereinafter referred to as the "SAC") of 14 December 2015, ref. no. II FPS 4/15, states that the one-off classification of expenses financed by a grant as tax deductible costs may be adjusted on a current basis - after obtaining refinancing. In this Tax Alert, we would like to present Sac's interpretation which is very favourable for taxpayers financed with grants.

In its decision of 22 June 2015, ref. no. II FSK 1499/13, the Supreme Administrative Court addressed the following judicial question to the court in extended composition: **in case of prior classification of incurred expenses (costs) then directly financed from tax-exempt income (revenues), including the exemption pursuant to Art. 17 Sec. 1 items 47 and 52 of the Corporate Income Tax Act (hereinafter: the CIT Act) as tax deductible costs, will the taxpayer, after receiving a grant, be required pursuant to Art. 16 Sec. 1 item 58 of the CIT Act to adjust (reduce) tax deductible costs as at the date on which such expenses were recognised for tax purposes as tax deductible costs, or should they be adjusted on a current basis at the time of receiving the grant?**

The case concerned a company conducting service activities in the field of information technology, which had concluded a grant agreement in respect of a programme associated with the creation of new jobs, financed in part by the state budget and the European Union. The company received grant payments based on applications showing eligible expenditure, submitted to the Minister of Economy. The company requested the tax authority to issue an individual interpretation of when it should exclude the expenses covered by the grants from tax deductible costs. The company presented the view that the exclusion of the expenses should be made in the year in which the grant was received, also if the expenses covered by the grant were recognised as costs for tax purposes in previous fiscal years. The tax authority considered the standpoint of the company as incorrect, and therefore the case was sent to the Voivodship Administrative Court (the WSA) in Wrocław, which dismissed the appeal of the company.

In the justification of the ruling, the court upheld the tax authority's arguments according to which the adjustment of the costs should be made for the period of erroneous recognition of individual expenses, so the adjustment should apply to the year in which the costs were recognised for tax purposes. According to the court, as far as the right moment of adjustment is concerned, it does not matter whether a certain expense incurred as part of the programme covered by the grant was incurred before or after the grant payment. According to the court, Art. 16 Sec. 1 item 58 of the CIT Act will apply here, pursuant to which tax deductible costs do not include expenses and costs directly financed by some tax-exempt income (revenues), including the exemption pursuant to Art. 17 Sec. 1 items 47 and 52 of the CIT Act. Consequently, it means that all

expenses and costs incurred by the company that were covered by the grant programme, either from the state budget or from the European Union, will be exempt from the category of tax costs despite the assumption that they were incurred to achieve revenue. In the case of prior classification of the refundable eligible expenditures as tax deductible costs, the taxpayer, after receiving a grant, is required to adjust (reduce) tax deductible costs, and thus adjust (increase) income tax (advance payments for taxable periods), in which they showed inflated costs. It does not matter when the taxpayer receives the income referred to in Art. 17 Sec. 1 item 25 of the CIT Act, but it does matter that ultimately the expense will have no impact on the depletion of their assets, which means that taxpayer's assets will not be the source of its financing. The case went to the Supreme Administrative Court, which decided to stay proceedings and formulated a request for adopting a resolution.

The SAC in extended composition took the view that in the case of a one-off classification of the expenses (costs) incurred to generate revenues, or to maintain or secure the sources of income, which were subsequently reimbursed from funds representing tax-exempt income (revenues) pursuant to Art. 17 Sec. 1 items 47 and 52 of the CIT Act, the taxpayer, pursuant to Art. 16 Sec. 1 item 58 of the CIT Act, **is obliged to reduce the reimbursed tax deductible costs in the month of receiving the grant.**

The SAC emphasised that it may be concluded from the content of Art. 17 Sec. 1 items 47 and 52 of the CIT Act that the final and total economic burden of the refinanced expenditure resulting from grants awarded to the beneficiary shall be borne by the EU and the State Treasury. The State may not impose on taxpayers any additional public-law burdens in connection with the awarded aid, and taking into account the WSA's standpoint would involve the adjustment of the previous tax return with all tax consequences in the form of tax arrears and the obligation to pay interest. Considering the above, for grants refinancing the expenses already incurred by the taxpayer, charging interest on late payments due to the retrospective tax deductible costs adjustment would in fact be imposing an additional tax obligation on the monetary benefit, which is not provided for by EU law.

Until now, administrative courts were of the opinion that only the cost of purchase or manufacture of fixed assets may be adjusted on a current basis after receiving reimbursement (SAC's ruling of 25 March 2015, ref. no. Act II FSK 955/14, SAC's ruling of 30 September 2014, ref. no. II FSK 2024/14), and one-off deducted expenses should be reduced in the year in which the taxpayer received the grant to cover the expenses eligible for refunds, which resulted in the formation of tax arrears (ruling of the WSA in Wrocław of 21 November 2012, ref. no. I SA/Wr 1068/12, I SA/Wr 1069/12).

In conclusion, the Resolution is good news for taxpayers awarded grants from domestic and EU sources, as from that moment on they will not be forced to make unfavourable retrospective adjustments resulting in returning part of the granted aid to the State Treasury in the form of interest on tax arrears.

RSM Poland is a member of RSM, the world's 6th largest network of independent advisory and auditing companies, with over 760 offices in more than 120 countries, employing over 38,300 professionals worldwide.

RSM Poland has been operating on the Polish market since 1991. Throughout this time we have gained vast knowledge and experience. We take pride in the unique team of professionals, counting among the best, that we were able to form.

Our company is shaped by our clients, whose requirements always take priority. That is why we offer comprehensive services tailored to meet individual needs. It is our clients who decide about the range of available services, while we give them opportunity for development and growth at every stage of their business.

Years of experience show that our approach is the key to mutual success.



Should you wish to discuss the above mentioned amendments in detail, feel free to contact us:

Piotr LISS
Tax Partner
Tax advisor (10240)

RSM Poland
Droga Dębińska 3b
61-555 Poznań, Poland
www.rsmpland.pl
office@rsmpland.pl

RSM Poland BLOG

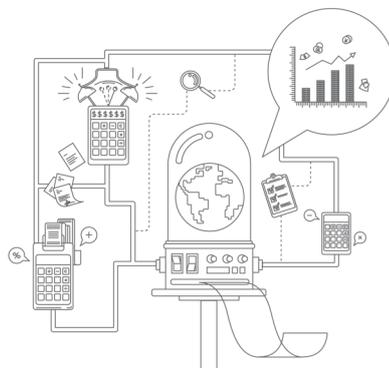


Practical guide to taxes and business.
We invite you to read our publication!



Please note that the presented text should not be understood as legal advice, as each individual case requires a separate, thorough analysis. Henceforth, RSM Poland Spółka Doradztwa Podatkowego S.A. and RSM Poland Audyt S.A. assume no liability in connection with use of information, advice and suggestions included in this publication.

© RSM Poland, 2016



THE POWER OF BEING UNDERSTOOD
AUDIT | TAX | CONSULTING

RSM Poland is a member of the RSM network and trades as RSM. RSM is the trading name used by the members of the RSM network. Each member of the RSM network is an independent accounting and consulting firm which practices in its own right. The RSM network is not itself a separate legal entity in any jurisdiction.

