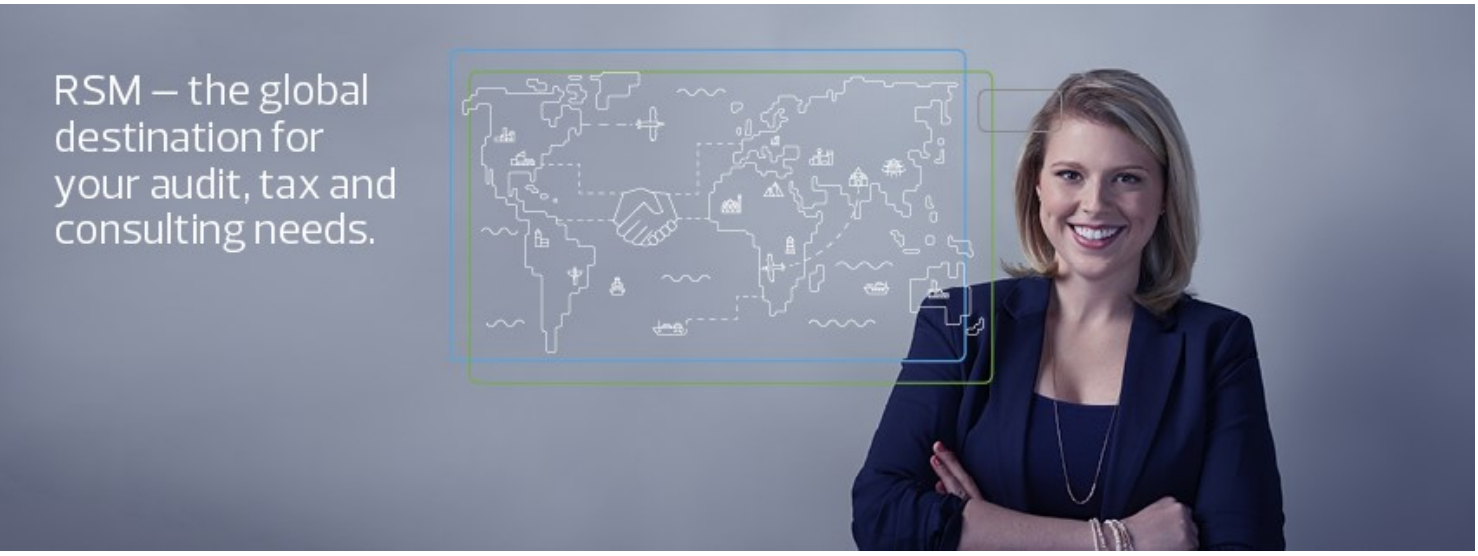

DRAFT AMENDMENTS TO THE CORPORATE INCOME TAX ACT

Tax Alert

Dear Sirs,

A draft bill was published on 22 February 2016 to amend the Personal Income Tax Act and the Corporate Income Tax Act. This Tax Alert discusses the proposed changes to the Corporate Income Tax Act ("CIT Act"). As pointed out in the motivation to the draft, the changes are to clarify the currently existing solutions and remove any interpretative doubts.

The proposed changes in the CIT Act aim to, among others, lower tax rates for selected groups of taxpayers, specify cases when the income of a non-resident is considered to be obtained within the territory of the Republic of Poland, clarify the rules on receiving licence fees, specify the rules defining revenue for the acquisition of company shares in exchange for contribution in kind, clarify the condition relating to substantiated economic reasons for preferential taxation in case of company mergers and divisions as well as to widen the scope of its application with the so-called share swap transaction.

TAX RATE REDUCED TO 15% FOR SMALL TAXPAYERS

The draft, in the amended Article 19(1) of the CIT Act, provides for reduction of income tax from 19% to 15% for small taxpayers (i.e. taxpayers whose value of sales revenue – including the amount of VAT due – did not exceed in the previous fiscal year, the amount corresponding to the equivalent of EUR 1.2 million, expressed in PLN) and for those starting a business.

The reduced tax rate to 15% will only apply to corporate income taxpayers. In addition, a start-up company, founded as a result of restructuring operations (listed in paragraph 1a added to Article 19 of the CIT Act) or transformation of the entrepreneur being a natural person, may pay a reduced tax only for income earned in the third fiscal year after the transformation.

The Ministry of Finance estimates that the relief will benefit about 393 thousand entrepreneurs, and tax revenues on this account will decrease by about PLN 270 million. On average, one small CIT taxpayer will, therefore, save around PLN 687 per year (PLN 57 per month). According to the explanatory memorandum to the draft, the amendment is to create "conditions for development and improved competitiveness inside and outside the company".

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INCOME (REVENUE) OBTAINED BY NON-RESIDENTS WITHIN THE TERRITORY OF THE REPUBLIC OF POLAND

The draft law, by adding paragraph 3 to Article 3 of the CIT Act, indicates a sample non-exclusive list of income (revenue) types generated within the territory of the Republic of Poland by so-called non-residents. Such income (revenue) will cover, among others, adjustable receivables, including those made available, paid and deducted by individuals, legal persons or organizational units without legal personality who have their domiciles, normal places of residence or head offices within the territory of the Republic of Poland, irrespective of the place of conclusion of the contract and performance of services as well as income (revenue) from securities and derivative financial instruments which are not securities admitted to public trading within the territory of the Republic of Poland for the regulated exchange market, including those generated from the sale of these securities or instruments and the execution of the resulting rights.

Moreover, paragraph 4 was added to Article 3 of the CIT Act, in which licence fees referred to in Article 21(1) of the CIT Act and dividends referred to in Article 22(1) of the CIT Act obtained by non-residents are defined as income (revenue).

The change, although it clarifies the issue of income earned by non-residents, does not provide the definition of income (revenue) they generate. In addition, it should be noted that the amended provision should always be interpreted with reference to the relevant agreements on the avoidance of double taxation.

SUBSTANTIATED ECONOMIC REASONS AS A CONDITION FOR APPLYING TAX PREFERENCES

The draft law changes the current wording of Article 10(4) of the CIT Act which governs the exclusion of tax preferences for the transactions of company mergers or divisions. The planned exclusion is governed by the amended Article 10(4) of the CIT Act and paragraph 4a added to the said Article. According to the draft, the exclusion also covers share swap transactions.

According to the amended Article 10(4) of the CIT Act, exemption from taxation (tax deferral) for transactions such as company merger, company division or share swap does not apply if their only or main objective is to avoid or evade taxation. In accordance with paragraph 4a of the Article, it should be presumed that the only or main objective of the said transactions is to avoid or evade tax if this operation is not carried out for substantiated economic reasons.

The new provisions assume that each transaction of company merger, company division or share swap aims to avoid or evade taxation. The burden of proving economic purpose (economic sense) of these transactions lies with the taxpayer. This solution is intended to effectively discourage taxpayers to carry out the transactions.

RULES DEFINING REVENUE FOR THE ACQUISITION OF COMPANY SHARES

The draft also changed Article 12(1)(7) of the CIT Act defining revenue as the value of shares in a company taken in exchange for a contribution in kind. According to the amended provision, revenue is the value of the contribution defined in the company statute, articles of association or other document, in case of contribution in kind provided to the company or cooperative in a form other than the company or its organized part. If the value deviates from the market value of the contribution, revenue is determined at the market value of the contribution on the day transfer of ownership of the contribution in kind is made. The provision will increase the tax base of in-kind contribution other than the company or its organized part.

COMPANY OR FOREIGN ESTABLISHMENT RECEIVING INTEREST AND LICENCE FEES AS THEIR BENEFICIAL OWNERS

Another novelty introduced by the draft law is the changed wording of Article 21(3)(4) of the CIT Act clarifying one of the conditions for tax exemption on interest and license fees by stating that the recipient of the above receivables must be their beneficial owner. Analogously, Article 26(1f) of the CIT Act was expanded with the provision that the written statement referred to therein should specify the company or its foreign establishment as its beneficial owner with respect to the payment of licence fees and dividends.

The table below presents the changes described:

Provision introduced or changed	The nature of the change
Article 3(3-5) of the CIT Act (added)	Non-exhaustive list of income (revenue) types obtained by non-residents within the territory of the Republic of Poland.
Article 10(4) (amended) and paragraph 4a (added) of the CIT Act	Exclusion of tax preferences for the transactions of company merger, company division and share swap. Passing on to the taxpayer the burden of proving that the transaction of company merger, company division or share swap was carried out for a substantiated economic reason.
Article 12(1)(7) of the CIT Act (amended)	In case of contribution in kind provided to the company or cooperative in a form other than the company or its organized part, the market value of the contribution always constitutes revenue.
Article 19(1) (amended) and paragraph 1a (added) of the CIT Act	Lowering the income tax rate from 19% to 15% for small taxpayers and for those starting a business.
Article 21(3)(4) of the CIT Act (amended) and Article 26(1f) CIT Act (amended)	Exemption from withholding tax relating to payments of interest and licence fees applies, provided that the receiving company (foreign establishment of the company) is located in another Member State (and taxed there) is their beneficial owner. Consequently, the obligation to have a written statement of the company (foreign establishment of the company) indicating that, in relation to the payment of licence fees, it is their beneficial owner.

The changes proposed in the draft law are to clarify the currently existing solutions and remove any interpretative doubts. The purpose of the changes is to tighten the tax system. The amendments would come into force on 1 January 2017, the draft law is currently being reviewed.

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

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