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## Transfer pricing: grouping transactions in the light of new regulations

### Tax Alert

Dear Readers,

Although the new transfer pricing regulations have been in force for only a few months, there have already appeared strikingly contradictory positions regarding grouping transactions in order to determine whether the statutory limit obliging a taxpayer to prepare transfer pricing report has been exceeded. In the opinion of the Provincial Administrative Court in Kraków (judgement of 23 February 2017, ref. No. I SA/Kr 1290/16), the linguistic interpretation of the newly added Art. 9a(1d) of the Corporate Income Tax Act (hereinafter: "CITA") leads to the conclusion that the term "of one type" does not refer to "transactions" but only to "other events". Thus, during the verification of the transaction threshold, it is necessary to sum up all the transactions carried out with related entities. However, the Head of the Tax Chamber in Poznań takes a different view (individual interpretation of 3 February 2017, No. 3063-ILPB2.4510.207.2016.1.ŁM). He believes that the aforementioned limit should be applied separately to each transaction concluded with a related entity.

#### PROVINCIAL ADMINISTRATIVE COURT IN KRAKÓW TO THE DISADVANTAGE OF TAXPAYERS

The case concerned a company which assumed that in 2017 it would purchase such services from related entities as, for instance, trademark licences, IT services, accounting services and market research services, and it would purchase fixed assets and office equipment (computer hardware). In addition, the company was to provide to related entities such services as, among others, tax consultancy services, real estate lease services, and it planned to grant loans to the related entities.

The subject of the inquiry was to decide whether, according to the interpretation of the regulations applicable since 1 January 2017, the company would be obliged to sum up all the transactions with related entities or only the transactions considered as transactions of the same type. The company was of the opinion that the provision and purchase of such different services as, inter alia, granting a licence and a loan agreement results in the absence of the obligation to sum up their values. According to the company, the term "of one type" included in Art. 9a(1d) of the CITA applies also to transactions, and while grouping the transactions, such elements as for instance performed functions, assets engaged by the parties, risks and costs incurred should be taken into account.

Nevertheless, in the individual interpretation dated 15 July 2016, the Minister of Finance disagreed with the company's position. He pointed out that by using the "or" alternative, the legislator has determined that the term "of one type" applies only to "other events". To confirm his position, he quoted the content of Art. 9a(1)(1) of the CITA indicating that by placing transactions and other events within separate editorial units of the aforementioned provision (letter a and letter b), the legislator demonstrated the need to treat them separately.

While examining the company's complaint, the Provincial Administrative Court agreed with the position presented in the challenged individual interpretation (as at the date of the publication hereof, the judgement passed is not final). By referring to the substance of the dispute, the court decided that the wording of the provision indicates that it was the will of the legislator to assign the term "of one type" only to "other events". By confirming the interpretation of the Minister of Finance, the Provincial Administrative Court emphasised that both the literal wording of the provision, due to the use of the "or" alternative, and placing the terms "transactions" and "other events" in separate sections of Art. 9a(1)(1) of the CITA lead to the conclusion that it was the will of the legislator to refer the discussed term only to "other events". According to the Provincial Administrative Court: *In the light of the above, it was legitimate to assume that the transactions with related entities do not need to be of the same type to be subject to the obligation to prepare transfer pricing report in relation to their total value; after all, the legislator does not refer such an attribute to them.*

#### **HEAD OF THE TAX CHAMBER IN POZNAŃ OF A DIFFERENT OPINION**

The Head of the Tax Chamber in Poznań drew different conclusions in the individual interpretation of 3 February 2017, No. 3063-ILPB2.4510.207.2016.1.ŁM. The case concerned a taxpayer who carried out different types of transactions with related entities, i.e. starting from the services of water supply network construction, through water testing services to premises rental services; some of them constituted the taxpayer's core business and others were only side transactions and accounted for a negligible share in general revenues/costs.

The taxpayer asked the tax authority if in the wording applicable since 1 January 2017 on the limit of the transactions that have significant impact on the amount of the taxpayer's income (loss) should be applied separately to each transaction concluded with a given related entity. Referring to the report on public consultations prepared during works on the amendment of the Act (published on the website of the Government Legislative Centre on 17 June 2015), according to which, in the opinion of the Minister of Finance, the materiality criterion applies to *individual transactions or other events taking place between related entities*, the tax authority decided that both the thresholds, and the materiality criterion should be applied to individual (types of) transactions and other events. Therefore, in the opinion of the Head of the Tax Chamber in Poznań, the limit stipulated in Art. 9a(1d) of the CITA, in the wording applicable since 1 January 2017, should be applied separately to each transaction concluded with a given related entity.

To confirm the presented position, the Head of the Tax Chamber referred to the conclusions resulting from the works of the OECD. In the opinion of the authority, according to the guidelines of the Organisation for Economic Cooperation and Development, *the obligation to prepare transfer pricing report should focus on material transactions and, thus, present the analysis of the most important issues related to such transactions. Moreover, the OECD Guidelines indicated also that tax authorities, by imposing on a taxpayer the obligation to prepare the transfer pricing report, should take into account the expected costs and the administrative burden related to the preparation of such report.(...) Therefore, according to the OECD Guidelines, the purpose of changes in documenting the transactions with related entities should focus on in-depth analysis of significant intra-group transactions, and not side transactions of minor importance.*

#### **SUMMARY**

At present, it is impossible to say which of the above positions will be leading. In the decision of the Provincial Administrative Court, a linguistic interpretation is presented but the question is if such an interpretation is sufficient to determine the legal norm included in the provision. Was it the intention of the legislator to impose on entities additional documentation burden concerning all transactions? In our opinion – no. In order to determine the legal norm, the Provincial Administrative Court should refer not only to the editorial technique but also to the purpose of the regulation. It is true that in Art. 9a(1)(1) of the CITA the legislator included "transactions" and "other events" in separate editorial units, but, in our opinion, only this should not prove the fact that the legislator refers the attribute of homogeneity only to "other events".

Undoubtedly, the purpose of the legislator is to provide tax authorities with access to information concerning transactions between related entities which may result in the reduction of the amount of tax to be paid. The question is whether the purchase, for instance, of 20 pens of the value of PLN 10 has equally large impact on the interest of the Treasury as the purchase of marketing services worth a million zlotys? According to the interpretation presented by the Provincial Administrative Court, an entity should sum up the value of those transactions and prepare the transfer pricing report for both these events (which does not make any sense in business terms).

Despite the aforementioned doubt, for the safety of taxpayers, it is advisable to follow the interpretation presented by the Provincial Administrative Court and wait for further decisions in this respect or to request an individual interpretation.



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

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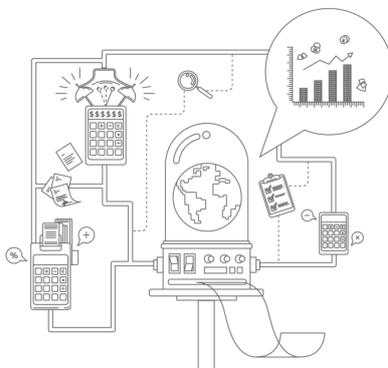
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