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Support to working capital in connection with COVID-19 without revenue and without costs

Expenses covered with financial aid from EU funds for the purchase of goods necessary to manufacture products, as well as for current operations, are not tax-deductible — indicates an interpretation issued by the tax authorities. In addition, such financing does not constitute revenue.

I. An interpretation has been issued on the effects of working capital financing

A tax interpretation issued on 10 February 2021 (0115-KDIT3.4011.613.2020.2.MJ) explains the tax consequences for taxable persons of financial support received based on a financing agreement as part of an action to support working capital in connection with temporary suspension or reduction of production and sales caused by the COVID-19 outbreak (action co-financed with EU funds). The taxable person (general partnership) used the funds received as part of working capital financing to purchase materials, semi-finished products essential in production, as well as to cover the costs associated with ongoing maintenance, such as gas, energy, cleaning services, etc. The financing was used to cover the net purchase price, whilst VAT was paid out of the taxable person's own current funds. The interpretation clarifies two issues: whether the received financing constitutes revenue for the general partnership's partners and whether the expenses covered from the financing are tax-deductible.

II. Grants, subsidies and co-financing constitute taxable revenue

As reminded by the tax authorities, considered to be revenue from operating actitivites are amounts receivable, even if not actually received, excluding the value of goods returned and rebates and discounts granted. For a taxable persons who sell goods and services subject to taxation with VAT, considered to be revenue from such sales is the revenue less the resulting output VAT. Also considered to be revenue from operating activities (with some exceptions) are grants, subsidies, co-financing and other free benefits received to cover costs or as reimbursement of expenses, except when they are associated with the receipt, purchase or own production of depreciable tangible or intangible assets.

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III. Co-financing from EU funds makes it possible to avoid tax

In accordance with currently binding regulations, free from income tax are funds received by project participants as assistance granted as part of a program financed with the participation of EU funds. The exemption referred to in the provision includes funds received by project participants as assistance granted as part of a program financed with the participation of EU funds. In the case of this provision, the exemption applies to all of the paid out funds. To apply the exemption the funds must have been received by a project participant as assistance granted as part of the program. Whereas considered to be project participants are those persons for whom the assistance granted as part of the project is actually designated. In addition, the term "with the participation of EU funds" used in the provision should be understood to mean co-financing from such funds. The subjective exemption covers only financial, i.e. cash benefits.

IV. Working capital co-financing may be exempt from tax

The interpretation states that co-financing as part of an action to support working capital in connection with temporary suspension or reduction of production and sales caused by the COVID-19 outbreak constitutes revenue under the Personal Income Tax Act, which needs to be classified as revenue from operating activities resulting from grants, subsidies, co-financing and other free benefits received to cover costs or as reimbursement of expenses. At the same time, however, the value of the funds granted in the form of a bonus payment - defined in the co-financing agreement, for operations relating to working capital support – as assistance granted under a program financed with the participation of EU funds, may be exempt from taxation based on Article 21 par. 1 point 137 of the PIT Act. Therefore, in this specific case, the taxable person (general partnership partners) does not have to add the received assistance to their revenue.

V. Purchases made with exempt revenue are not tax-deductible

The tax authorities have also reiterated that tax-deductible are costs incurred in order to generate revenue or to maintain or secure a source of revenue, with the exception of expenses clearly indicated in the regulations as not tax-deductible. In order, therefore, for an expense to be considered tax-deductible, it should, under the cited provision, meet all of the following conditions: it must remain in a cause and effect relationship with revenue or a source of revenue and must be incurred in order to generate revenue or to maintain or secure a source of revenue; must be correctly documented; must not be on a list of costs not recognized as tax-deductible. In the context of the last condition, the tax authorities reminded that under currently binding regulations, not considered tax-deductible are the expenses and costs financed directly out of the income (revenue) referred to in, among others, Article 21 par. 1 point 137. In consequence, expenses covered from financial support, for the purchase of goods necessary to manufacture products and for current operating costs, are not tax-deductible.

VI. Majority of aid under crisis shields also tax-exempt

While describing the above interpretation it should be remembered that the situation is somewhat different in the case of aid received under the crisis shields financed from Polish funds (without EU participation). In this case, not all forms of aid are exempt from taxation. For example, stand-down benefits and renewed stand-down benefits are not included in revenue. Also exempt from taxation are micro loans and non-returnable subsidies paid out under the shields. In addition, in an interpretation issued on 30 December 2020 (0111-KDIB1-3.4010.503.2020.1.MBD.) the tax authorities found that "aid received in the form of a subsidy to employee wages and ZUS premiums from the Guaranteed Employee Benefits Fund is not tax neutral".

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VII. A forgiven PFR loan constitutes revenue, but the costs remain

Funds received as part of PFR support are treated differently than the other forms of assistance. According to the Ministry of Finance, at the time of receipt, paid out subsidies are treated as loans. Thus the receiving business is not required to pay tax on such a loan when it is granted, and the expenses paid for with the loan are tax-deductible. The situation changes when the subsidy is forgiven. Forgiveness of a PFR loan constitutes a gain for the business, which leads to the formation of a tax liability on the resulting revenue (see MF's answer to inquiry No. 14065). Regulations allow for forgiveness of up to 75% of a loan received from PFR. Whereas the costs financed with a loan received under the Financial Shield are classified as tax-deductible in accordance with generally binding regulations. All of the expenses that have been covered from funds provided by PFR are tax-deductible if they meet the general conditions arising out of tax regulations for such classification. Classification of expenses as tax-deductible costs does not change even if the loan is forgiven.

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