

Ministry of Finance begins to fix CIT regulations

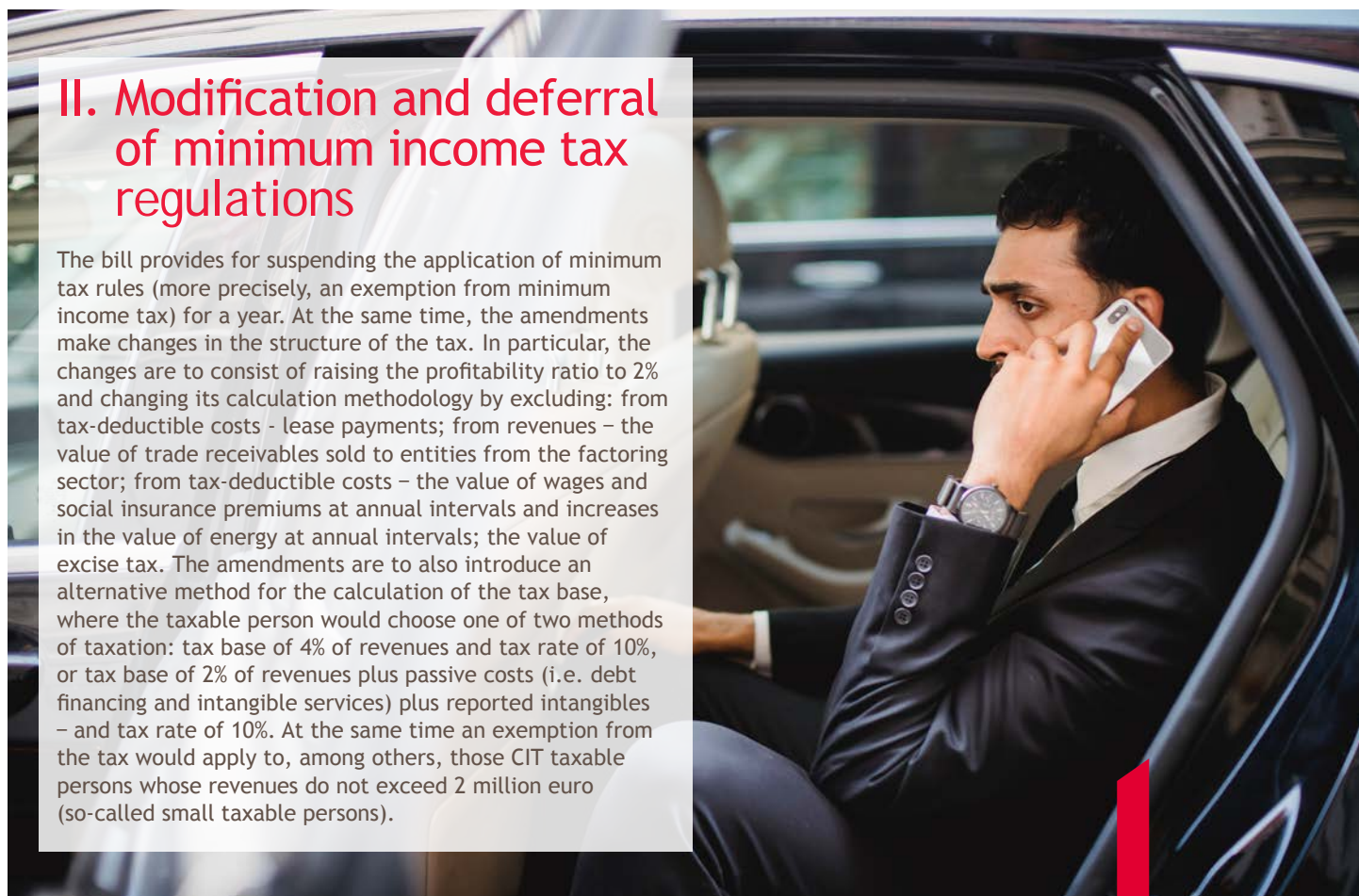
I. Ministry of Finance has prepared a draft of numerous CIT and PIT amendments

A draft bill amending the Corporate Income Tax Act and certain other acts was published at the end of June (paper UD404). It provides for more than 20 changes in the CIT Act, the PIT Act, as well as the Tax Ordinance and the Health Benefits Act. According to the reasons for the amendments: “The objective of the draft bill is to improve the provisions on corporate income taxation (and, analogically, certain personal income tax and withholding tax regulations) in a way that will make them simpler, more transparent, while at the same time ensuring their increased effectiveness from the standpoint of their application and the purpose they are to serve.”

The Ministry of Finance has prepared extensive amendments to income tax regulations, including in particular the CIT Act. Among others, they are to suspend for a year the application of the provisions on minimum CIT, as well as change the provisions on withholding tax or tax haven transactions. These are, however, only examples of changes, which are to affect more than 20 areas in total.

II. Modification and deferral of minimum income tax regulations

The bill provides for suspending the application of minimum tax rules (more precisely, an exemption from minimum income tax) for a year. At the same time, the amendments make changes in the structure of the tax. In particular, the changes are to consist of raising the profitability ratio to 2% and changing its calculation methodology by excluding: from tax-deductible costs - lease payments; from revenues - the value of trade receivables sold to entities from the factoring sector; from tax-deductible costs - the value of wages and social insurance premiums at annual intervals and increases in the value of energy at annual intervals; the value of excise tax. The amendments are to also introduce an alternative method for the calculation of the tax base, where the taxable person would choose one of two methods of taxation: tax base of 4% of revenues and tax rate of 10%, or tax base of 2% of revenues plus passive costs (i.e. debt financing and intangible services) plus reported intangibles - and tax rate of 10%. At the same time an exemption from the tax would apply to, among others, those CIT taxable persons whose revenues do not exceed 2 million euro (so-called small taxable persons).



III. Change in deadline to update individual taxable person data

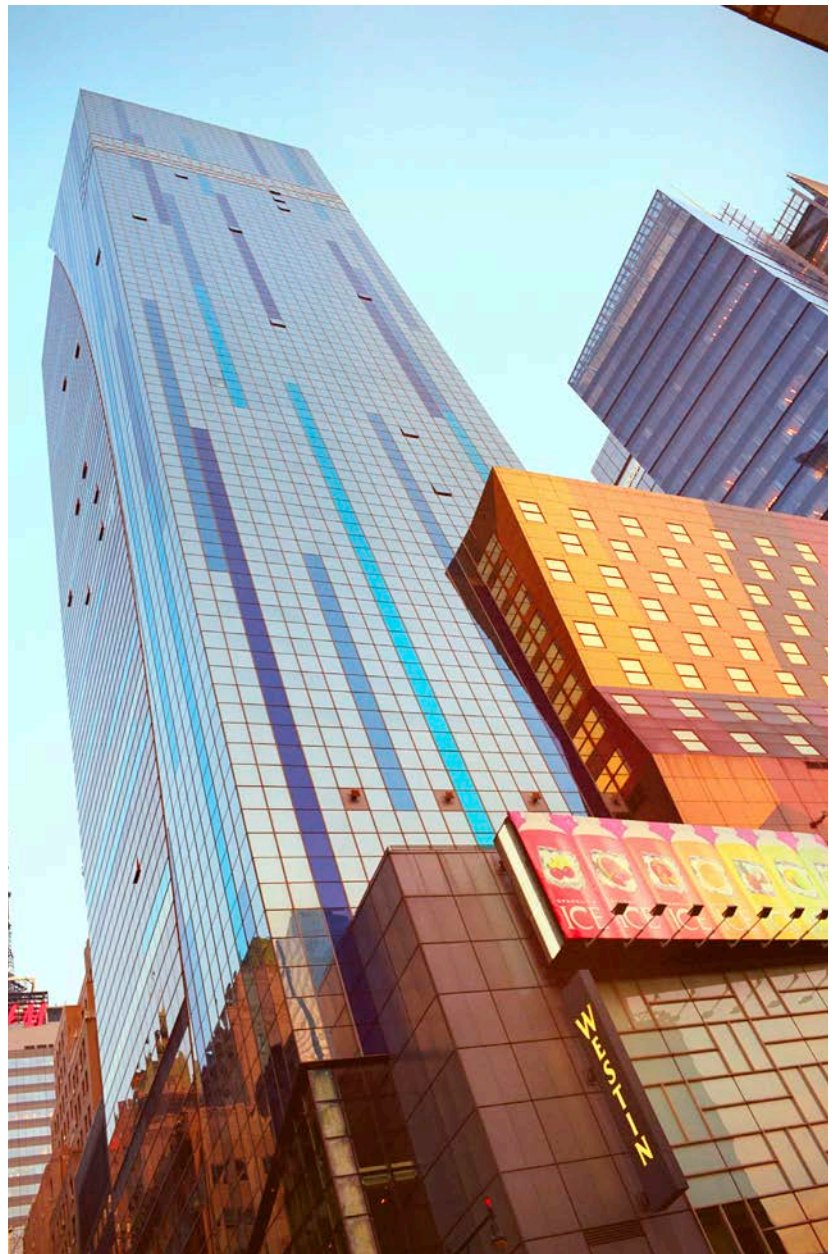
The amendments will also make changes to Article 27b par. 8 of the CIT Act, i.e. the provisions on updating individual taxable person data. Such data arise out of tax returns filed in the previous year and are published by 30 September. They are also updated quarterly as at the first day of the month in which the given calendar quarter ends. Now the ministry wants to introduce a provision allowing for a less frequent, i.e. yearly update of such data. Publication of individual taxable person data applies to: tax groups, irrespective of revenues earned; taxable persons other than tax groups whose tax year revenues exceed the equivalent of 50 million euro translated into PLN at the average exchange rate announced by the National Bank of Poland on the last working day of the calendar year preceding the year of publication of individual taxable person data; real estate companies, including real estate companies that belong to a tax group.

IV. Lifting of regulations on so-called hidden dividends

The ministry's bill also provides for lifting the provisions of the Act of 29 October 2021 on so-called hidden dividends (they were to go into effect as of 1 January 2023). The regulations provided that where it was determined that a payment had the nature of a hidden dividend, the taxable person could not include it in tax-deductible costs. At the same time there were three categories of costs considered to constitute hidden dividends. Firstly, when the amount of such costs or the date of their incurrence were in any way conditioned on the generation of profit by the taxable person, or on the amount of such profit. Secondly, when a reasonably acting taxable person would not incur such costs or could incur lower costs if an unrelated party performed a comparable service. And thirdly, when the costs included consideration for the right to use assets owned or jointly owned by a shareholder or shareholder's related party prior to the formation of the taxable person.

V. Change in provisions on controlled foreign companies (CFC)

The ministry is also proposing to change the regulations on controlled foreign companies (CFC). The changes are to consist of, firstly, introducing regulations to eliminate double taxation of CFC when dividends are paid between controlled foreign entities within the same holding structure. Secondly, clarifying one of the premises that constitute a CFC (i.e. the premise relating to CFC's high profitability in relation to its assets – it is to amount to 25%) in the event of a potential disposal of assets in the course of a year. And thirdly, clarifying the definition of subsidiary. As indicated in the draft, elimination of double taxation could occur on the following conditions: revenue (income) from the CFC is also included in the tax base of the parent CFC, where the burden of proof that that revenue (income) has been included would rest with the taxable person, and the said revenue (income) from the subsidiary CFC comes from dividends. Additional limitations have also been proposed.



VI. Change in regulations on shifted profits

With regard to companies that have their place of establishment or management in the territory of the Republic of Poland and are subject to the shifted profits tax, the amendments clarify that, among other things: the scope of shifted profits tax includes tax-deductible costs (generally it is only in such cases that erosion of a Polish taxable person's tax base can occur); such companies are not subject to the shifted profits tax if the total passive costs incurred by the company in a tax year for the benefit of a related party (those related parties) constitute less than 3% of the total tax-deductible costs declared for tax purposes by that company in the tax year, in any form. In that respect, under the new wording of the regulations, the proportion counter only includes the said passive costs incurred for the benefit of related parties that meet the conditions relating to the shifted profits tax, and not – as is the case now – the said passive costs incurred for the benefit of all, including unrelated entities. The conditions that each related party must meet have also been made more precise. In addition, the amendments simplify the condition for preferential taxation in the state of the related party's place of establishment, management, registration or location.

VII. Change in regulations on withholding tax (WHT)

The overall objective of the proposed changes in withholding tax regulations is to relax and realign the new mechanism for the collection of the tax (pay & refund) in effect since 1 January 2019. In this case, the changes lift the obligations of broadly defined withholding agents (i.e. issuers as remitters *sensu stricto*, as well as entities that are so-called technical remitters) when it comes to the taxation of interest and discount on treasury securities (i.e. treasury bills and bonds), as well as make more flexible the structure of the remitter's declaration exempting from the requirement to apply pay & refund. To this end the ministry proposes broadening the scope of the exemption from income tax for non-resident taxable persons and to extend it onto treasury bills and bonds offered on the domestic market, along with a corresponding change in withholding agent obligations. In addition, the ministry is proposing flexibility in the effective dates of the remitter's declaration by extending its validity until the end of the tax year (instead of the current two months). This means that filing the declaration would allow the remitter to not apply the pay & refund mechanism until the end of his tax year.



VIII. Changes in accounting for debt financing costs

Under currently binding regulations, the costs of debt financing obtained from a related party, insofar as it has been used, directly or indirectly for capital transactions, in particular an acquisition of shares, acquisition of the total rights and obligations of an unincorporated entity, capital contributions, raising of share capital or buyback of own shares for the purpose of their redemption, are not considered tax-deductible. Now, as part of the amendments, the ministry is proposing limiting the application of this regulation and excluding debt financing granted by banks or cooperative savings and loan associations with their place of establishment in a European Union member state or another European Economic Area state, as well as eliminating its application to debt financing granted for the acquisition of shares or total rights and obligations of entities unrelated to the taxable person. In accordance with a transitional provision the changes would go into effect retroactively as of 1 January 2022.



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IX. Change in regulations on initial public offering relief

The changes the ministry plans to make to IPO relief regulations consist of taking away the ability to deduct from the tax base the expenses incurred for an initial public offering by taxable persons who earn income from qualified intellectual property rights taxed at the preferential rate of 5%. This change has to do with the nature of the expenses, which may be recognized when determining income from qualified intellectual property rights. Expenses incurred for an initial public offering cannot be recognized as costs incurred to generate, secure or preserve a source of income from qualified intellectual property rights. According to the ministry, leaving the regulations as they are could breach the OECD guidelines in the Action 5 Report as part of the Base Erosion and Profit Shifting Project entitled “Countering Harmful Tax Practices More Effectively, Taking into Account Transparency and Substance”.

NOTE: Owing to the fact that the amendments relate to various regulations we have chosen to discuss them in two consecutive alerts.

The present alert contains part 1.

You will receive part 2 next week.

The information presented herein does not constitute comprehensive information or opinion. Consult your adviser before making any decisions.

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