

Liquidation of sole proprietorship does not take away eligibility for flat-rate PIT

I. Closing a business and eligibility for flat-rate PIT

In its ruling of 4 February 2022 (case file II FSK 1372/19) the Supreme Administrative Court found that a natural person who in the course of one tax year discontinued the operation of a sole proprietorship and the following year earned income as a shareholder from holding an interest in an unincorporated company, may continue to benefit from his earlier choice made based on Article 9a par. 2 of the Personal Income Tax Act to have his income from non-agricultural business operations taxed as specified in Article 30c of that act (flat-rate tax). In accordance with Article 9a par. 5 of the PIT Act, where a taxable person: 1) is a sole proprietor and is a shareholder of an unincorporated company, 2) is a shareholder of an unincorporated company – his choice of the form of taxation applies to all of the forms of operations that are subject to the provisions of the act. The Court pointed out that the form of taxation referred to in Article 9a par. 2 of the PIT Act relates to the methods specified in Article 30c of that act, i.e. proportional (so called flat-rate) tax.

A natural person who in one tax year discontinued the operation of a sole proprietorship and in the following year earned, as a shareholder, income from having an interest in an unincorporated company, can continue to benefit from his earlier choice to be taxed with flat-rate tax – the Supreme Administrative Court has ruled.

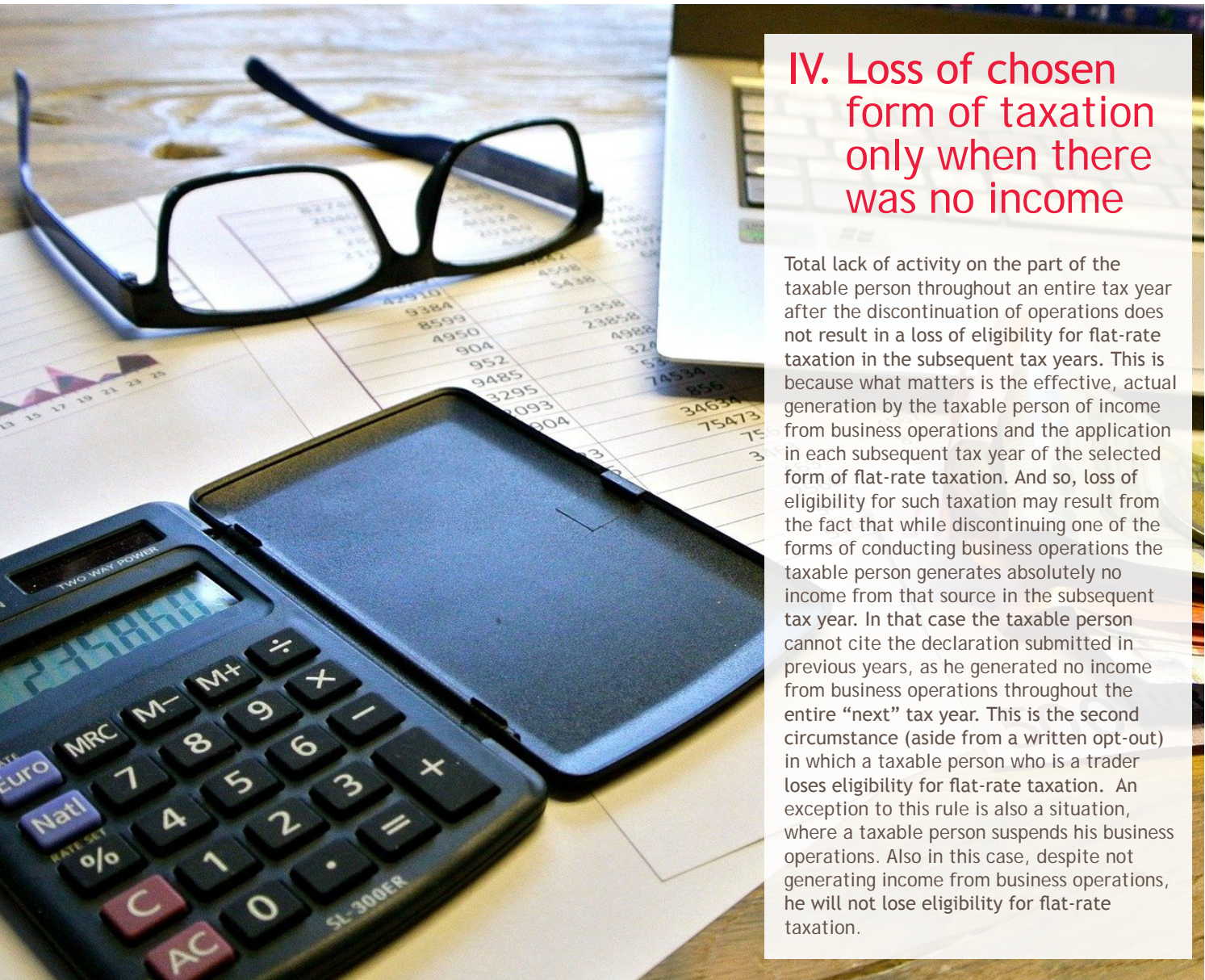


II. Chosen form of taxation applies to all forms of operations

The Court found that the regulation of Article 9a par. 4 of the PIT Act (provision on choosing the form of taxation) covers all of the possible instances of earning income from a source classified as business activity now and in the future, rather than only at the time of making the declaration. It therefore covers income from a sole proprietorship, as well as income from having an interest in an unincorporated company. The Court pointed out that the form of taxation chosen in the declaration also applies to subsequent years, unless the taxable person, by 20 January of the tax year, submits a written notice to the head of the relevant tax office of opting out of this form, or a written declaration or request to apply forms of taxation specified in regulations on lump-sum income tax. The opt-out notice may be submitted based on freedom of business activity regulations.

III. Chosen form of taxation in effect until changed

According to the Supreme Administrative Court, the lawmakers have provided for automatic continuation of a once made choice of proportional taxation of income from business operations, irrespective of the form in which they are conducted. To lose the chosen form of taxation the taxable person must perform a specific action, i.e. submit, and do so in writing, a notice of opting out from the previously chosen form of taxation, and must do so by a strictly set deadline, i.e. by 20 January of the tax year (under the legal status in effect until 2021), or submit, by the same deadline, a written declaration or request to apply forms of taxation specified in the PIT Act. The lawmakers have not provided for other circumstances under which the eligibility for the flat-rate taxation of income from non-agricultural business operations may be lost. In particular, "liquidation", i.e. discontinuation of the operation of a sole proprietorship, is not such a circumstance.



IV. Loss of chosen form of taxation only when there was no income

Total lack of activity on the part of the taxable person throughout an entire tax year after the discontinuation of operations does not result in a loss of eligibility for flat-rate taxation in the subsequent tax years. This is because what matters is the effective, actual generation by the taxable person of income from business operations and the application in each subsequent tax year of the selected form of flat-rate taxation. And so, loss of eligibility for such taxation may result from the fact that while discontinuing one of the forms of conducting business operations the taxable person generates absolutely no income from that source in the subsequent tax year. In that case the taxable person cannot cite the declaration submitted in previous years, as he generated no income from business operations throughout the entire "next" tax year. This is the second circumstance (aside from a written opt-out) in which a taxable person who is a trader loses eligibility for flat-rate taxation. An exception to this rule is also a situation, where a taxable person suspends his business operations. Also in this case, despite not generating income from business operations, he will not lose eligibility for flat-rate taxation.

V. Generation of income from business operations not conditioned on taxable person's formal status

In the reasons for its ruling the Court stressed that business operations or their synonym used in the PIT Act - non-agricultural business activity – is autonomously defined in that act. The said provisions do not refer to any definition of legal business operations in tax or any other laws that deal strictly with its performance, such as the Business Operators Act of 6 March 2018, or the Freedom of Business Activity before that. It is also not necessary for the taxable person to have any formal confirmation of his status as a trader in order to generate income from this source. Importantly, the legal definition does not at any point make a reference to the registration of traders who are natural persons based on the Act on the Central Register and Information on Business Operations and Information Point for Business Operators. Business operations have an objective nature that is not created by notifying the relevant authorities, as it is an event, namely a sequence of specific factual events related to this particular form of making a living, as well as generating revenues and income therefrom.



RAFAŁ KOWALSKI
Head of Tax Department
tel.: +48 22 543 16 00
Rafal.Kowalski@bdo.pl



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BDO spółka z ograniczoną odpowiedzialnością sp.k., ul. Postępu 12, 02-676 Warszawa;
tel.: +48 22 543 1600, fax: +48 22 543 1601, e-mail: office@bdo.pl